SAVCA
SOUTHERN AFRICAN VENTURE CAPITAL AND PRIVATE EQUITY ASSOCIATION

17 August 2018

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Attention: Ms Teboho Sepanya **/** Mr Allen Wicomb

Dear Ms Sepanya / Mr Wicomb

RE: SAVCA RESPONSE TO THE DRAFT TAXATION LAWS AMENDMENT BILL

Introduction

1 We refer to the Draft Taxation Laws Amendment Bill (the "**Draft Bill**") published by the Department of National Treasury on 16 July 2018.

2 The Southern African Venture Capital and Private Equity Association ("**SAVCA**") wishes to submit comments and proposals for consideration, relating to proposed amendments to Section 12J of the Income Tax Act 58 of 1962 ("**Section 12J**") as set out in the Draft Bill ("**the Proposed Amendments**").

3 SAVCA is the industry association and public policy advocate for venture capital and private equity ("**VCPE**") in Southern Africa, with circa 120 venture capital and private equity fund managers registered as SAVCA members, managing approximately R168bn in assets under management.

4 SAVCA respectfully requests that it be **granted an opportunity to make oral representations at the Public Hearings on 21 August 2018**. We note that through SAVCA's 2017 Annexure C submission, we requested National Treasury to consider tightening the legislation to ensure the capital raised through this incentive flows to the

intended recipients and is not abused. SAVCA highlighted the potential for abuse as part of its civic duty and because it determined that growing abuse of the legislation would pose a risk to the sustainability and longevity of the Section 12J incentive. In SAVCA's view, the incentive has proven itself highly effective and beneficial (as outlined below) and we are concerned to see the loss of momentum and risk to the incentive created by the Proposed Amendments. It was SAVCA's preference to achieve targeted legislation to curb abuse. Unfortunately, the Proposed Amendments are extremely far reaching and do not address only the perceived abuse, but threatens the existence of probably all approved Venture Capital Companies ("**VCC**"). On this basis, SAVCA would like to make representations to Parliament.

5 SAVCA does not view Section 12J as an asset class in itself, but rather a section of the Income Tax Act, which is utilised by a number of participants in the market, of which private equity and venture capital fund managers form only a part. The investment incentive as set out in Section 12J thus impacts a specific sub-set of our members that have opted to utilise a Section 12J VCC for a whole or part of their capital raising, investment strategy and/or business model. The SAVCA Section 12J membership is represented in the table below:

	S12J Market (Information provided by SARS)	S12J SAVCA Membership		S12J Market (Information provided by SARS)	SAVCA S12J Membership	
	28-Feb-18	28-Feb-18	Percentage of total	28-Feb-17	28-Feb-17	Percentage of total
Total Number of Approved VCCs	103 (However, 2 VCCs have been withdrawn)	19	18%	49	13	13%
Total Number of Investors into VCCs	2 221	1775	80%	892	776	87%
Total Number of Qualifying Companies	155	57	37%	56	30	54%
Total Amount invested into the VCCs (R)	3 641 338 187	1 927 669 104	53%	1 832 128 574	887 043 746	48%
Total Amount invested into Qualifying Companies (R)	932 133 212	632 629 749	68%	410 349 135	298 993 138	73%

6 We particularly note that there was a slow take-up of Section 12J, with the number of VCCs and capital raised accelerating only in the past 18 months. As of 28 February 2015, 13 VCCs were approved (with negligible capital under management), rising to 31 in 2016, 49 in 2017 (with a jump in capital raised) and 101 in 2018[1]. Accordingly, measurement of the impact of Section 12J has been delayed. Nevertheless, SAVCA's VCC members have provided initial insight into its impact to date (see paragraph 16) and have committed to funding and participating in research to measure and monitor the

[1] 103 approved as at 28 February 2018 but 2 have been withdrawn.

impact of Section 12J by its members and the broader VCC industry during the course of 2018.

7 SAVCA's Section 12J fund manager members share certain similarities, in that they focus on investments in privately-held companies, principally drawing on the value-adding approach of private equity and venture capital to not only direct capital to these companies, but also introduce skills, governance, advice, best practice and financial management practices for the benefit of the companies and their various stakeholders. Notwithstanding these similarities, each fund manager deploys its own distinct business, investment and capital raising model and SAVCA does not regulate this in any way.

8 SAVCA's mandate is to represent the VCPE fund managers and is submitting this response to the Draft Bill in relation to broadly representative and traditional VCPE business practices. SAVCA is not privy to specific member structures or deals and has suggested that where appropriate, members should complete their own submissions to National Treasury and include specific structures, to allow National Treasury to better understand the investments made by VCCs and the impact of these investments.

9 The vast majority of SAVCA Section 12J members operate using a pooled model of investment (the "**Pooled Fund Model**"), whereby a number of third party investors invest into a fund managed by a fund manager, which invests into a portfolio of underlying privately-held companies.

10 In addition to the traditional Pooled Fund Model, SAVCA understands that there are alternative models in the market that provide capital to Small, Micro and Medium-Enterprises ("**SMMEs**") in a non-pooled manner (the "**Non-Pooled Fund Model**"). As far as SAVCA understands, these Non-Pooled Fund Models using Section 12J were established in reliance on SARS Binding Private Rulings specifically addressing the "ring-fenced" or non-pooled nature of these funds. SAVCA's members are predominately operating Pooled Fund Models. For this reason, the SAVCA submission focuses **only on Pooled Funds** and does not engage on the manner in which Non-Pooled Fund Models operate nor the impact thereon of the Proposed Amendments. That being said, SAVCA understands that there are numerous benefits and positive applications for Non-Pooled Fund Models, such as Enterprise and Supplier Development ("**ESD**"), corporate venturing, deal-by-deal investments and accelerators. Flexibility to accommodate such models, with specific policy guidance from National Treasury as to acceptable practices, will allow a meaningful allocation of capital to intended recipients in support of National Treasury's policy objectives that would not otherwise occur, and which should be encouraged, especially where traditional VCPE

practices via a Pooled Fund Model may not be able to fully achieve South Africa's ambitious growth and job targets.

11 We recommend that National Treasury engage further with VCCs deploying the Non-Pooled Fund Model in order to provide clarity on acceptable practices that enable the SMME ecosystem benefits to continue whilst curbing any potential abusive practices.

12 SAVCA believes that the Section 12J incentive has positively contributed to South Africa in directing much-needed capital and skills to growth businesses and SMMEs to stimulate economic growth, job creation/retention and innovation. Whilst it is still early days to be able to demonstrate the benefits of these investments, given that capital has only been raised and deployed meaningfully in the last 18 months due to the slow uptake noted above, the early signs and statistics are extremely encouraging (see paragraph 16 below) and the Section 12J regime should not be allowed to lose momentum. It is our hope that tighter, but targeted legislation and policy certainty, will continue to bolster investment in this space without disruption to VCCs operating in support of the intended purpose and tenets of the legislation.

Economic growth, job creation/retention and Section 12J

13 SAVCA firmly believes that investment into growth businesses and SMMEs in South Africa is key to fostering economic growth and innovation and is imperative to tackle challenges of poverty, inequality, unemployment and vulnerability of small companies. This is supported by global and local research such as the "Finfind Inaugural South African SMME Access to Finance Report[2]". In this regard, SAVCA welcomed the bold initiative by National Treasury when it introduced Section 12J in 2008, and subsequently improved Section 12J in 2011 and 2014 in order to address the slow uptake of the incentive. The various Binding Private Rulings issued by SARS since 2015 further assisted to boost investments in VCCs.

14 Entrepreneurs and small businesses in South Africa nevertheless suffer from a severe lack of access to capital and professional investors, as very few institutional investors are willing to consider investment into SMMEs, rather favouring less risky investments in larger companies. According to the Global Entrepreneurship Monitor ("GEM") 2016/2017 report[3], 50% more South African entrepreneurs discontinue their businesses because of lack of access to finance, as compared to the average for Africa. The

[2] SA-SMME-Access-to-Finance-Report-2017-FINAL-VERSION-FOR-RELEASE-on-10-July-2018.pdf
[3] gem-south-africa-2016-2017-report-1494860333.pdf

incentive under Section 12J was therefore crucial in unlocking investment into SMMEs as it meaningfully de-risked the otherwise risky investments.

15 SAVCA is of the view that Section 12J has proven effective in 1) raising capital from sources that would not otherwise have invested in the SMME space, and might otherwise have invested those same funds offshore or in local "risk averse" investments that do not have the same potential for unlocking growth as SMME investing does 2) enabling more private equity and venture capital fund managers to operate in the SMME space, bringing capital and skills to fill a much needed gap in the market, 3) creating new and sustainable jobs, and 4) stimulating economic growth and innovation. A number of SAVCA's fund managers have utilised Section 12J as the basis of their funds, raising capital to invest in early-stage and high growth SMME companies or priority sectors such as hospitality and manufacturing. The Section 12J incentive has been instrumental in attracting private sector investment capital to this market, which has been historically very under-supported in South Africa.

16 SAVCA acknowledges the urgent need for VCCs to demonstrate social return on investment in support of national objectives and the furtherment of South Africa's growth, equality and prosperity, and has already indicated to National Treasury that it will be undertaking a survey of all VCCs to gather information on the economic impact of the investment incentive to date. In the interim SAVCA requested high-level impact numbers from its members as part of this submission, and in aggregate QC's show over 180% increase in direct jobs since investment by the VCC, with indirect jobs showing an even more impressive increase. SAVCA has appointed a research partner, and we will be commencing the detailed survey as soon as possible and publishing a Section 12J Impact Study report. This report will be shared with National Treasury as soon as it is available.

It is, nevertheless, important to understand that:

16.1 despite the attractiveness of the incentive[4], it took some time before the market accepted and took up investment in Section 12J investment vehicles in a significant manner. This was due to regulatory uncertainties within Section 12J that have been largely cleared up over the past few years (with a number still outstanding which could

[4] Section 12J was improved with effect from 1 January 2015 to make the deduction permanent (previously there was a recoupment on disposal) and to increase the asset limits for qualifying QCs. The real uptake in VCC registrations was only from 2015 onwards.

further improve the legislation – see prior SAVCA submissions[5]), and a process of educating the market and dealing with investor concerns.

16.2 the impact of VCPE investing tends to follow a J-Curve, with an initial period of time and investment in positioning a business for growth and ensuring its stability, followed by a more rapid expansion – both in terms of revenue and employment. It is important to understand the nature of investment and medium-term time-scale for properly and sustainably growing businesses. The SAVCA VCC members have committed themselves, nevertheless, to driving such social returns as employment, economic growth and innovation in the near term as an urgent priority and reporting on this to National Treasury.

17 The recent uptake in Section 12J provided an opportunity to begin to demonstrate the benefits of the Section 12J incentive arising from c.R3 billion raised and c.R1 billion invested in underlying investments as of 28 February 2018. However, following the release of the Draft Bill, virtually all Section 12J vehicles have experienced a significant disruption in terms of capital raising and deployment as a result of lack of certainty and the risks of non-compliance under the Proposed Amendments. SAVCA is extremely concerned that all momentum, progress and validation of the Section 12J incentive could now be compromised as a result of the policy uncertainty triggered by the Proposed Amendments.

SAVCA remains committed to promoting the success and sustainability of Section 12J as a mechanism for growth, employment and innovation in South Africa.

Market sentiment and policy certainty

18 It is not clear from the Draft Bill, nor from the accompanying explanatory memorandum, the specifics of all the types of transactions National Treasury consider "abusive" and sought to remedy through the Draft Bill. SAVCA cannot speculate on this, but notes that the Proposed Amendments have exceptionally far reaching effects and appear to jeopardise the entire Section 12J industry. In other words, the Proposed Amendments do not address only the perceived abuse, but threatens the existence of probably all approved VCCs. As National Treasury has not expressed a desire to close down the Section 12J VCC regime, we assume the consequences are unintended.

[5] Prior submissions by SAVCA recommended additional improvements to ensure uptake, deployment and effective management of VCC regime investments. Kindly see prior submissions from SAVCA addressed to the Taxation Policy Unit dated 8 May 2018, as well as SAVCA's Annexure C submission dated 24 November 2017.

19 As a consequence of both the far-reaching nature of the Proposed Amendments and the retrospective impact, the market is in a state of paralysis with potentially no capital being raised by VCCs or invested into qualifying company's (**"QCs"**) due to the risk of non-compliance, which would affect both VCC investors and QCs alike. VCC investors, who are primarily individuals and retail in nature having in good faith invested savings and personal investment capital, have been shaken by the Proposed Amendments. It is exceptionally difficult for SMMEs to raise capital in the current economic conditions, and where the capital that was available from VCCs is no longer available, these companies may be at risk. The costs to unwind structures will be substantial and the loss of investor confidence (and likely investor capital) may result in this incentive failing to achieve its desired outcome or worse, failing altogether, rendering any future policy/ incentives ineffective.

20 The Proposed Amendments also do not seem to provide VCCs with the option to unwind their structures and fails to consider potential negative tax and commercial consequences of such an early unwind, for the VCC, its investors and QCs alike.

20.1 Under the Proposed Amendments, should a VCC established in good faith and operating in accordance with the legislation prior to the draft Bill, not be able to comply with the Proposed Amendments following a SARS notice to comply, it will have 125% of the expenditure incurred by any VCC shareholders for the issue of VCC shares, included in the income of the VCC, a significant penalty making the VCC unviable.

20.2 The Proposed Amendments do not provide for any kind of roll-over relief to the extent that tax may be triggered as a result of a VCC or QC amending its structure in order to comply with the requirements as provided by the Proposed Amendments. Should National Treasury require VCCs and/or QCs to convert their structures to comply with the requirements in this regard, such conversion should not trigger tax for any of the parties.

20.3 Similarly, consideration should be given to the 36-month time period for assessment of various terms of Section 12J that continues to run even though the market has been sterilised during this current period of uncertainty.

21 The Proposed Amendments have caused grievous concern amongst VCC investors and QCs, and a lack of confidence and certainty across the market. Whilst the Proposed Amendments have been crippling for SAVCA's Section 12J members (and Section 12J vehicles more broadly) we are of the view that a far better outcome could emerge from this process. SAVCA supports tighter legislation with narrow interventions that stamps

out abuse, provides extreme clarity in terms of what is acceptable, providing improved certainty for investors and further capital investment into this important area of the market. We also hope that the dialogue will enhance trust between business and legislators, thus resulting in further improvements to the legislation driving uptake in investments for sustained economic benefit.

22 ***A failure to achieve this outcome in a very short period of time would jeopardise the good that has been done and the significant investments to date by National Treasury*** to use policy to drive key national priorities and would undermine public trust in policy setting, rendering future policy and incentives ineffective. Therefore, SAVCA respectfully requests that in considering the Proposed Amendments, National Treasury:

22.1 provides policy certainty and clear guidance in relation to the intention of this section, the acceptable practices, and what needs to be achieved through Section 12J initiatives in order to meet National Treasury objectives. The guidance provided in the Explanatory Memoranda from 2008 to 2018, have not provided the market with sufficient clarity in terms of acceptable practices in relation to this incentive. We believe that tightening of the legislation in a targeted manner will result in more capital flowing to the intended recipients of this section and thereby ensuring the sustainability of the investment incentive in the future.

22.2 acts promptly and provide responses to the issues raised by SAVCA and the rest of the market in this regard as a matter of extreme urgency. Press coverage on the Proposed Amendments and the general message in the market is creating widespread negative sentiment towards Section 12J as a whole. Should the current uncertainty persist, irreversible damage could be done to the Section 12J market as well as to any other future initiatives of National Treasury in this space. The retrospective application of the proposed amendments is causing uncertainty which spreads far wider than just the VCC space. Investor confidence amongst both local and foreign investors have been damaged by the proposal to retrospectively amend legislation, and by the fact that the retrospective amendments would apply even in those instances where the parties were relying on Binding Private Rulings to confirm the SARS position.

22.3 confirms as compliant with no risk of attack, all capital raised by VCCs and capital invested into QCs, prior to the issuance of the Draft Bill, that were within the letter and understood intention of the section. In order to restore confidence, SAVCA suggests that existing structures and funds be “grandfathered” and any changes to the final TLAB should have only a prospective impact. We respectfully request that

existing structures which are clearly abusive, be challenged under the General Anti-Avoidance Rule ("**GAAR**") or specific provisions in the Income Tax Act that have been used.

Review of Proposed Legislation on VCCs

23 The following paragraphs address the impact of the following specific Proposed Amendments:

- QC – restricted to one class of share (Section 1)
- VCC – restricted to one class of share (Section 2)
- Limitation of QC income derived from VCC shareholders (Section 3)

24 SAVCA's view is that local and internationally accepted best practice is the most convincing way in which to illustrate that various share classes and the structuring thereof is commercial and essential in circumstances where there is no use of a tax incentive – and therefore an imperative for the sustainability of VCPE using the Section 12J incentive. SAVCA has included this background information below to provide market context when considering the review of the legislation and the alternative proposals noted below.

Section 1: Impact of QC share class restriction

<u>Description of the Problem</u>

25 According to the Proposed Amendments, the QC cannot have more than one class of shares in issue on the date of the acquisition of any shares in that company by a VCC and at any time during any year of assessment after that date.

26 This Proposed Amendment is problematic for the following reasons:

26.1 Start-up, early stage and growth businesses require numerous capital injections as they progress through various growth stages. Global practices use, amongst other approaches, various classes of shares in the capitalisation of a business so as to attract necessary flow of capital on a risk-adjusted basis, align interests and enable important governance / voting rights distinctions. Extensive research and evidence (for example see attached research by globally renowned experts, Kaplan, Martell and Stromberg, 2003) can be provided to National Treasury to confirm the commercial rationale and the fundamental necessity of such structures for funding

start-ups and scale-ups. Without the ability to use various share classes in QCs, the venture capital industry will be unable to deploy its investment model using Section 12J, and recent progress in South Africa will be set back substantially, leaving venture capital an under-supported industry and many innovations and growth potential thwarted.

26.2 The ability for a QC to issue various classes of shares is thus instrumental in attracting capital and allowing it to achieve its growth potential. This is commercial practice in funding private companies and not tax driven, and as stated above, is a commonly used feature in venture capital investing around the world.

26.3 Furthermore, multiple share classes may already be in existence in a QC before receiving VCC funding, and a QC may elect to issue multiple share classes after a VCC has invested. The VCC has no control over either of these events and would render the QC un-investable, or the VCC non-compliant.

26.4 By legislative design, the VCC cannot have outright control of the QC. Accordingly, where the VCC has already invested into a QC with multiple classes of shares, it is not possible for the VCC to compel the QC to change its share classes.

26.5 In addition, where the VCC has already invested as such, it is quite possible (in fact probable) that there will be other non-Section 12J investors in the QC that require the share class distinctions. The restriction imposed by the Draft Bill will make it untenable for VCCs to invest alongside non-Section 12J investors into QCs. It will also make existing structures impossible to manage.

26.6 In addition, for SMME's raising capital, they are now denied access to a useful and valuable capital source as VCCs will not be able to co-exist with other investors investing in the SMME's drawing on best practice commercial structures.

<u>Our recommendation:</u>

27 Withdraw this amendment and replace it with amendments that are focused on the specific abuse. SAVCA has provided proposals for consideration below.

Section 2: Impact of VCC share class restriction

<u>Description of the Problem</u>

28 According to the Proposed Amendments, the VCC cannot have more than one class of shares in issue in respect of a year of assessment during which that company commences trade and at any time during any year of assessment after that date.

29 This Proposed Amendment is problematic for the following reasons:

29.1 Virtually all fund managers managing Section 12J funds are impacted by the restriction on share classes at the VCC level as most employ different classes of shares in order to manage the economic split for the fund manager (the performance-related incentive arising from successfully managing these funds), and/or voting and governance rights. Global VCPE practice is that there is typically a fee for funds under management (which serves as working capital for the fund manager who deploys time and skill to source, execute and oversee/manage investments) as well as a performance-related incentive once a hurdle rate (minimum rate of return) has been achieved (which serves to align the interests of the fund manager and the fund investor to maximise value in the underlying companies).

29.2 In a VCC structure, the above structure is achieved by issuing investors and fund managers different classes of shares in the VCC. E.g. ordinary shares for investors in the fund who contribute capital (some of which is typically contributed by the fund manager to ensure 'skin in the game' and alignment) and which in the case of a VCC earns a tax deduction, and "A Ordinary Shares" (or similar) which entitle the fund manager to distributions (performance-related incentive) only after the full invested capital has been returned to the investors and/or governance and decision-making rights. The different share classes afford capital protection to investors and performance incentive to the fund manager for which they operate the business. These structures are therefore imperative to aligning the interests of the investors with the fund managers. The restrictions on share classes in the VCC render these structures non-compliant in their current form.

29.3 Furthermore, a traditional VCPE fund manager will raise multiple rounds of capital to invest over time. Often this is done through several limited life tax transparent vehicles (e.g. partnerships) with restricted time periods for capital to be raised in the market and returned. The VCC structure however is a company, therefore perpetual in nature, which lends itself to multiple capital raises within a single "fund" structure in different market conditions over the life of the company. There are practical and commercial difficulties around raising of multiple rounds of capital into a VCC for example revaluing the VCC shares and dilution of existing investors. To simplify capital raising, the VCC can issue new share classes for each tranche of capital (but

still in a pooled manner). The alternative, a new VCC for each fund raise, is expensive with onerous compliance and reporting requirements. These and other commercial uses of structuring securities facilitate business and if limited, would constrain, complicate and cost VCCs and QCs in a manner that is out of line with general investment market practice in the SMME sector.

29.4 Some VCCs have also used different classes of shares to provide different investment strategies and risk profiles to investors (or class of investor) within a single VCC, but still in a pooled manner (i.e. a number of passive investors who will invest in a portfolio of underlying QCs).

Our recommendation

30 Withdraw this amendment and replace it with amendments that are focused on the specific abuse. SAVCA has provided proposals for consideration below.

Section 3: Impact of limit on QC income derived from VCC shareholders

Description of the Problem

31 According to the Proposed Amendments the QCs may not earn any meaningful trading income directly or indirectly from the VCC's shareholders, or any parties connected to a VCC shareholder.

32 This Proposed Amendment is problematic for the following reasons:

32.1 One of the benefits that VCPE brings to its portfolio of investee companies (the QCs) is networks and business development. One of the valuable ways to achieve this is to profile the investee companies to the investors in the VCC with the objective of generating further business from the VCC investors and their networks or own enterprises on an arm's length basis. This would not be allowed under this clause and prove detrimental to the QCs that the VCC is working to support.

32.2 Additionally, QCs may coincidentally and unbeknownst to the VCC earn trading income from a party related to a VCC investor. This is therefore constraining and practically problematic.

32.3 The limitation on trade will adversely affect ESD initiatives by corporates, whereby if that corporate (or connected persons to that corporate) is also an investor into the VCC, even if that trade is carried out on an arm's length basis. This proposed amendment does not align with National Treasury's objectives in providing equity

finance to SMME's and the Department of Trade and Industry's Codes of Good Practice on Broad-Based Black Economic Empowerment to assist and accelerate the growth and sustainability of black enterprises.

32.4 Any restriction on the types of businesses that a SMME trades with on an **arm's length basis** would jeopardise the SMME's ability to grow and be profitable, and render investment by a VCC a risk to any SMME.

Our recommendation

33 Withdraw this amendment as the alternative proposal noted below removes the potential for non arm's length trading relationships between VCC investors and QCs.

Alternative Proposals as it relates to VCCs deploying a Pooled Fund Model

34 The abovementioned issues can be resolved through the following proposed alternatives as they relate to pooled fund investments:

34.1 **PROPOSAL 1: Proposal to confirm as compliant with no risk of attack, all capital raised by VCCs and capital invested into QCs, prior to the issuance of the Draft Bill, that were within the letter and understood intention of the section.**

34.1.1 In order to restore market confidence, SAVCA requests that National Treasury consider "Grandfathering" of structures compliant under the current legislation and that any policy changes have only a prospective effect.

34.1.2 Although the changes are proposed to come into effect only in 2019, they will have retrospective effect if they apply to existing structures and investments.

34.2 **PROPOSAL 2: Proposal to narrow the scope for abusive structures: Limiting ownership in a particular class of VCC shares AND distinguishing between VCC shares and non-VCC shares**

34.2.1 The proposal is that no one investor can hold 20% or more of the VCC shares in a particular class of share, together with any connected persons. i.e. the connected person test is performed on a per-class basis. This is tested at the VCC level; **and**

34.2.2 Each class of shares has a single asset limit in relation to their linked underlying QCs of 20% (i.e. test the single asset limit per share class); **and**

34.2.3 Further, the VCC should be allowed to issue both VCC shares (which are tax deductible, and for which the connected person test applies per share class) and non-VCC shares (for which no tax deduction is permitted but also for which no connected person test be required). At a minimum the fund manager shares would need to be non-VCC shares for the majority of the market to be compliant, as it also relates to fund manager participation and governance (as set out above). The same should apply to "angel" and/or non-resident investors who do not wish to claim a tax deduction, but whose investment may result in them being connected persons to the VCC.

34.2.4 In effect, the above proposal results in the different classes of shares within the VCC being treated as separate companies for purposes of the connected person requirement in Section 12J(3A) and the investment requirement in Section 12J(6A)(c), the defining features of the Pooled Fund Model.

34.3 **PROPOSAL 3: Proposal to establish safe harbour structures for Pooled Fund Models.**

34.3.1 SAVCA requests that, in order to settle uncertainty in the market and not slow the progress of structures that National Treasury intends for the legislation to support, that National Treasury provides clear guidance on which applications of multiple share structures are fully compliant and pose no risk, such as (we propose) use of multiple share classes at the VCC level for the purpose of governance, voting rights and economic splits for the fund manager, and use of multiple share classes at the QC level in compliance with international VCPE best practice. VCCs could then continue to raise and deploy capital within these bounds without fear of non-compliance (retrospectively or prospectively).

We propose that this guidance be provided on an accelerated basis as delays until November will seriously compromise the Section 12J capital raising and investment programme in the interim period, with potentially lasting effects.

SAVCA notes that the alternative proposals listed above, are only in relation to a **Pooled Fund Model**. We recommend that National Treasury engage further with VCCs deploying the Non-Pooled Fund Model in order to provide clarity on acceptable practices that enable the SMME ecosystem benefits to continue whilst curbing any potential abusive practices.

Conclusion

Thank you for considering SAVCA's submission. We are fully supportive of the steps taken by National Treasury to date to encourage investment into this section of the market. We strongly believe that with tighter legislation and increased policy certainty, this investment incentive will provide significant economic and job creation benefits that will showcase the positive results that can be achieved when government and the private sector work together with a common purpose.

Yours sincerely

S Lotz

Head of Regulatory Affairs: Southern African Venture Capital and Private Equity Association

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