Australian Innovation Research Group

INNOVATION INSIGHTS
JULY 2018

BY PETER WILLIAMSON, CEO OF AUSTRALIAN INNOVATION RESEARCH GROUP

AS A FOLLOW ON TO HIS LAST INNOVATION INSIGHT RELATED TO THE AUSTRALIAN GOVERNMENT'S 2018-19 BUDGET, PETER WILLIAMSON OFFERS SOME OF HIS PERSONAL VIEWS ON THE GOVERNMENT'S RECENT RESPONSE TO INNOVATION AND SCIENCE AUSTRALIA'S RECOMMENDATIONS IN THE 2030 PLAN IN THE CONTEXT OF THE BUDGET AND RECENT MELBOURNE ROUND TABLE DISCUSSIONS RELATED TO THE DIRECTION OF GOVERNMENT POLICY AND ITS EFFECTS ON THE LEVEL AND CHARACTER OF AUSTRALIAN R&D.

Changes to the R&D Tax Incentive Legislation

As I discussed in earlier AIRG articles, some significant changes to the R&D Tax Incentive were telegraphed in the Government's response to the 2030 Plan and confirmed in principle in the recent Budget.

The changes will likely affect all Members of the Australian Innovation Research Group.

The Government has recently repeated its view that the 2016 Review of the R&D Tax Incentive and the 2018 Innovation and Science Australia 2030 Strategic Plan found the R&DTI did not fully meet its policy objectives, particularly in inducing business research and development expenditure beyond business as usual activities.

The Government is now seeking stakeholder feedback on changes to the R&D Tax Incentive Legislation

On the 29th June 2018, Treasurer Scott Morrison and Senator Michaelia Cash, Minister for Jobs and Innovation, released a joint media statement regarding potential changes to the Research and Development Tax Incentive (R&DTI) and released draft legislation for public comment.

There is an opportunity for the Australian Innovation Research Group and/or individual AIRG Members to provide a response on the implementation of the proposed amendments. Interested stakeholders are encouraged by the Government to provide their views by Thursday 26 July 2018.

The exposure draft legislation, explanatory materials and consultation document are available on the Treasury website or can be downloaded from the following links:

Consultation Paper
PDF 694KB

Draft Explanatory Materials
PDF 958KB

Draft Legislation
PDF 458KB

The changes are intended to reduce the amount paid out by the programme of more than $2 billion and refocus support for larger companies undertaking high-intensity R&D

For larger companies with aggregated annual turnover of $20 million or more, under the new legislation, there will be an R&D premium that ties the rates of the non-refundable R&D tax offset to the incremental intensity of R&D expenditure as a proportion of total expenditure for the year. Incremental R&D intensity will be calculated as eligible R&D expenditure as a percentage of total expenditure, such that:

$$\text{R\&D intensity} = \frac{(\text{eligible R\&D expenditure (R\&D notional deductions)})}{(\text{total expenditure (expenditure)})}$$

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My concern with this approach is that it may give rise to unintended distortions where a company operates as a broader collection of subsidiaries where R&D activity happens in separate subsidiary to those that experience other development and commercial expenditures within a broader economic group.

Under the draft legislation, the marginal R&D premium will be the claimant's company tax rate plus:

- 4 percentage points for R&D expenditure between 0 per cent to 2 per cent R&D intensity;
- 6.5 percentage points for R&D expenditure above 2 per cent to 5 per cent R&D intensity;
- 9 percentage points for R&D expenditure above 5 per cent to 10 per cent R&D intensity; and
- 12.5 percentage points for R&D expenditure above 10 per cent R&D intensity.

The draft legislation also incorporates an increase in the R&D expenditure threshold from $100 million to $150 million.

For smaller companies with aggregated annual turnover below $20 million, the R&D tax offset rate will be equal to their corporate tax rate plus a 13.5 percent premium. This represents a change to the current situation where smaller companies are entitled to an R&D tax offset rate of 43.5 percent.

In addition, a $4 million cap on annual cash refunds has been introduced, although amounts that are in excess of the cap can become a non-refundable tax offset that can be carried forward into future income years.

As a shield for **biomedical companies,** clinical trials will not count towards the cap and remain refundable.

The changes incorporate increased disclosure

Other changes, according to the draft legislation, include increasing transparency by enabling the Australian Taxation Office to publicly disclose details of how much a company has claimed and details of their R&D expenditure under the scheme.

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Closing date for submissions: 26 July 2018

If you wish to make a response, you can contact the relevant Government department via the details below. Alternatively, contact me at **peter.williamson@airg.org.au** and I can assist.

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