

21 September 2012

Business Tax Working Group Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600
email: BTWG@treasury.gov.au

Dear Sir/Madam

RE: Business Tax Working Group Discussion Paper, 13 August 2012

The Association of Australian Medical Research Institutes (AAMRI) welcomes the opportunity to comment on the Business Tax Working Group Discussion Paper of 13 August 2012.

AAMRI is the peak body representing Australia's pre-eminent independent medical research institutes (MRIs). Our 41 members, all not-for-profit research organisations, are international leaders in health and medical research and collectively account for 8,000 research staff and students and an annual research and development (R&D) expenditure of over \$700 million.

AAMRI is genuinely concerned about the consideration by the Business Tax Working Group of limiting or denying the R&D Tax Incentive to larger firms. The R&D Tax Incentive is the primary government program that incentivises Australian business expenditure on R&D (BERD). Watering this recently-improved scheme down would run the risk of reducing the viability of Australia's medicines industry – the nation's biggest producer of high technology exports, worth \$4 billion in exports annually – underpinned by over \$1 billion per annum in business R&D investments.¹

Such a cut would also have negative repercussions on Australia's health and medical research sector, including MRIs, universities and hospitals. Through spin-off companies, licensing agreements, contracts and collaborations, the research sector has strong links with Australia's biotech and pharmaceutical industry, including large firms such as CSL, with an annual revenue of more than \$4 billion and an annual investment in Australian R&D of over \$150 million.² Given Australia's relatively small market place, there is an increased importance of research-industry collaborations and licensing with existing large companies to bring Australian discoveries to market. These collaborations leverage substantial investment in Australia's ongoing knowledge base, and mean that the value this R&D generates through local manufacturing and intellectual property ownership stays onshore. A strong biotech and pharmaceutical industry also employs and grows a highly qualified pool of commercially experienced Australian scientists who will fuel knowledge-intensive industries of the future.

¹ Australian Bureau of Statistics (2012) *International Trade in Goods and Services, Australia, July 2012*, Catalogue No 5368.0, ABS, Canberra; Australian Bureau of Statistics (2012) *Research and Experimental Development, Businesses, Australia, 2010-11*, Catalogue No 8104.0, ABS, Canberra.

² For example, several collaborations between the Walter and Eliza Hall Institute and CSL:
www.wehi.edu.au/site/latest_news/2.2_million_agreement_to_find_next-gen_treatments_for_inflammatory_disease,
www.wehi.edu.au/site/latest_news/wehi_spin-out_murigen_restructures_g-csf_antagonist_program_with_csl.

1. Business investment in R&D is essential for the future prosperity of Australia's economy

A primary objective of the Business Tax Working Group is to increase productivity, including by attracting new investment, while delivering relief to struggling businesses to ensure Australia's future competitiveness and prosperity in the Asian Century.

It is well documented that BERD is tightly linked to long-term economic growth through improvements in multi-factor productivity. BERD also (by definition) underpins high and medium-high technology industries, which will play a crucial role in Australia's ability to compete on the international stage in the Asian Century.

In an economy with a poor record in BERD (1.3% of GDP versus 1.6% of GDP for the OECD),³ high and medium-high technology exports (ranked 2nd last in the OECD as a proportion of total exports),⁴ and multi-factor productivity growth (with productivity declining since 2004), it would be counter-productive to reduce the primary government subsidy that stimulates these very factors underpinning our future prosperity. Because of the long-term nature of R&D and the lag in financial returns, anything that jeopardises Australia's strong decade of BERD growth has the potential to cause long-term harm to Australia's knowledge-intensive industries, including the biotech and pharmaceutical industry.

2. Cutting R&D tax concessions will negatively impact BERD and the economy

AAMRI strongly agrees with the Business Tax Working Group's rationale that, to the extent that incentives are not effective in influencing BERD, government revenue forgone should be better expended. The Working Group's consideration of cuts to the R&D Tax Incentive program for large firms is based on the observation in the OECD's *Tax Reform Options: Incentives for Innovation*, that tax incentives have different impacts on the R&D performed by small relative to large firms. However, there are serious caveats to this reasoning.

Evidence indicates that while the influence of R&D tax incentives on large firms is lower than that for small and medium enterprises (SMEs), R&D tax incentives do still generate additional R&D investments in large firms beyond what would have been invested in the absence of an incentive.⁵ Further, R&D tax incentives have outcomes beyond increases in R&D investment, many of which are very poorly assessed in the evaluation of R&D tax incentive programs around the world.⁶ This very lack of comprehensive information on the full benefits of R&D tax incentives means that the proposed cuts to the R&D Tax Incentive are premature and insufficiently founded on evidence.

We are in a century where multinational companies are increasingly moving R&D activities offshore to take advantage of preferential tax environments. This is highlighted in Deloitte's *2012 Global Survey of R&D Tax Incentives*:

*...many countries are promoting re-location of R&D operations as part of their innovation-led economic development strategies. R&D tax incentives are an important component of these strategies. Countries offering R&D tax incentives are often regarded as an optimal location for internationally-mobile R&D.*⁷

³ Main Science and Technology Indicators (MSTI), OECD.stat, accessed 20 September 2012.

⁴ Structural Analysis (STAN) Indicators, OECD.stat, accessed 20 September 2012; Australia ranks 31 out of the 32 OECD countries for which data is available.

⁵ OECD (2010) *R&D tax incentives: rationale, design, evaluation*, OECD Innovation Policy Platform, November 2010, OECD, Paris; Lokshin, B and P Mohnen (2009) *How Effective Are Level-based R&D Tax Credits? Evidence from the Netherlands*. Updated UNU-MERIT Working paper No.29, University of Maastricht.

⁶ Ibid.

⁷ Deloitte (2012) *2012 Global Survey of R&D Tax Incentives*, Deloitte Global Services Ltd, UK.

The discussion paper fails to consider the implications of cutting Australia's R&D Tax Incentive scheme on decisions by Australia's large multinational firms to move their operations and/or R&D activities offshore, or on Australia's ability to attract new international knowledge-intensive businesses.

Australia's R&D Tax Incentive scheme must compete with similar schemes in 25 other OECD countries. Australia's scheme is by no means the most generous amongst R&D tax incentive programs of OECD countries, and the global trend is for an increase in the breadth and generosity of R&D tax incentives.⁸ While the Business Tax Working Group is considering winding back incentives for large firms, the UK, for example, plans to expand its R&D tax incentive scheme in 2013 to include large firms.⁹

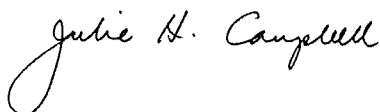
Should a large multinational company move its R&D operations offshore, this would have significant implications on Australia's economy and government revenue, possibly exceeding the savings to government of some of the scenarios under consideration. This makes the decision to reduce the R&D Tax Incentive scheme for large firms a highly risky one.

3. There is a strong case to continue R&D tax incentives for health and medical research

Finally, there is specifically a strong case for maintaining the R&D Tax Incentive at current levels for business investment in health and medical research because of the social benefit such R&D provides to Australians. Australia is facing fierce international competition for R&D investment in areas such as clinical trials. Clinical trials give early access of novel medicines and medical devices to patients, and result in better patient outcomes. Hospitals active in R&D also attract the best clinicians and health professionals and provide better health services. There are also health problems specific to Australians, or in which Australia has a higher than average prevalence, where business investment in Australian R&D is essential. Australia should be encouraging private sector investment that helps find major health solutions that we are struggling to meet, not jeopardise this investment through the removal of the R&D Tax Incentive for large firms.

AAMRI strongly believes, and the evidence shows, that support for business investment in R&D is crucial to Australia's future prosperity. Reducing the company tax will undoubtedly attract investment to the country. However, if this requires the watering down of the current R&D Tax Incentive scheme, it will be at the risk of losing investments in knowledge-intensive industries, such as biotech and pharmaceuticals, crucial to Australia's future economic prosperity.

Yours sincerely



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President, Association of Australian Medical Research Institutes

⁸ OECD (2012) *OECD Science, Technology and Industry Outlook 2012*, OECD, Paris.

⁹ <http://www.bis.gov.uk/policies/innovation/business-support/rd-tax-credits/about>.