

FAO Chris Lyons
General Manager
Business Tax Division, Treasury

By Email

31 August 2012

Dear Sir / Madam

Re: Submission re consultation on quarterly R&D credits

We appreciate the opportunity to respond to your request for submissions on the issues that will arise in respect of the proposed quarterly credits provisions that will interact with the refundable R&D tax offset rules under Division 355 of the *Income Tax Assessment Act 1997*.

The enclosed annexure sets out what we believe are the main practical, technical and compliance issues in the order in which the questions were set out in the document inviting submissions.

We hope that this proves useful in the drafting of the proposed legislation on this issue.

Should you wish to discuss our submission in greater detail, please do not hesitate to contact either me on (03) 9671 7805 or alternatively Roisin Arkwright on (02) 9322 7412.

Yours sincerely



Jason Crawford
Director
Deloitte Tax Services Pty Ltd

Annexure 1

1. *Are the proposed arrangements for quarterly credits workable? What features are most useful? Are there any features that are problematic? How might the arrangements be improved while appropriately managing risks to companies and the Commonwealth?*

The arrangements set out in the consultation paper appear to be sensible from a theoretical and tax policy perspective, and are appropriately built upon commonly known rules within the PAYG instalment provisions contained within Schedule 1 of the *Taxation Administration Act 1953* (TAA 1953).

That said, we do have initial but substantial concerns that the proposed quarterly payment system is not streamlined and simple enough for any taxpayer to be encouraged to actually use it. Essentially, the benefit of the quarterly system is to obtain a cash-flow advantage that can effectively be valued by the interest saving obtained by having the money earlier. However, to actually obtain this cash-flow related benefit, which could be minor if the company has access to alternative funding, it appears that taxpayers will actually need to:

- Provide AusIndustry with an outline of projected activities to be included in the future registration, i.e. almost a separate registration type form based on projected activities
- Wait for acceptance and a quarterly notification number from AusIndustry. These steps could themselves be perceived as likely to trigger a review or an early finding in respect of eligibility
- Separately approach the ATO and wait again for advice on the amount of the quarterly credit to be received
- Notify the ATO that it remains eligible each quarter

It is also possible at any time that a quarterly refund amount will be offset against any tax liabilities that the company has, rather than necessarily being paid out in cash.

Given these requirements, risks and perceived high compliance costs compared to the value of the cash-flow timing benefit gained, we understand anecdotally that it may be too complex for many smaller entities to bother with, unless the refund will be for quite a material amount.

We would therefore strongly suggest that given the timing nature of the refunds involved and the low level of risks concerned, it would be substantially more effective to:

- 1) Allow companies to self-assess the eligibility of their ongoing R&D activities and eliminate this compliance step completely. In practice, unless an Advance Finding is requested, AusIndustry often accept a registration application subject to being selected for a subsequent review. It would appear to us on an analysis of the costs and risk involved that the compliances need for notification outweighs the long term risks involved.
- 2) Require the subsequent step of dealing with the ATO as one of two alternatives being:
 - Retaining the safe-harbour ATO notification approach as suggested; or
 - In place of the proposed variation rules, merely allow a company to self-assess their quarterly credit or refund. This achieves exactly the same effect of varying the safe harbour amount and the proposed variation penalty rules drafted could be drafted to apply where there is a substantial margin between the self-assessment amount and what would have been a lower safe-harbour amount (which can be easily calculated by the taxpayer when self-assessing). This would also allow taxpayers to self-assess on their most recent financial information.

These types of options are familiar to taxpayers in the Division 40 effective life provisions.

Were both of these self-assessment options available such that a quarterly form merely needed to be filled out to claim a quarterly refund, and end of year reconciliations undertaken, it would go a significant way to encouraging small business to take advantage of the proposed opt-in provisions (a key objective of the refundable tax incentive).

We believe that such a system would also align with the current self-assessment nature of registering R&D activities with AusIndustry and claiming the expenditure on the company income tax return. It also remains a low risk approach given the potential application of the GIC and a suitable variation penalty when required. As such, its advantages are strongly recommended.

It would be also extremely beneficial if, at the outset, the ability for the Commissioner to apply his discretion were embedded into the following provisions:

- The variation penalty provision where unforeseen events etc had occurred; and
- The provisions which will allow taxpayers access to the quarterly refund system only if it a complying taxpayer (for example, allowing taxpayers access by discretion if one tax return was outstanding for accepted good reasons).

2. *What type of guidance material or services would be most useful to assist companies to access quarterly credits and meet any associated obligations?*

An ATO factsheet and worked examples would be expected, and information sessions for small R&D advisers and accountants. The AusIndustry hotline would also need to be prepared to address all of these issues.

A completely integrated guide to all aspects of the refundable R&D tax offset would also assist in place of various ad hoc guidance materials that can be located between AusIndustry and the ATO. That said, this would also be beneficial for the non-refundable R&D offset!

3. *Do the proposed arrangements for quarterly credits create any problematic interactions with other taxation or regulatory arrangements? If so, what are these interactions and how should they be addressed?*

We believe that generally it will be important to implement appropriate reciprocal references between the proposed new provisions and each of the following:

- The R&D rules themselves in Division 355 ITAA 1997, particularly s.355-100;
- Section 67-30 and ss.205-15(4) of ITAA 1997 which deal with the refundable tax offset itself and the deferred franking debit impact on the franking account;
- The newly introduced provisions in TAA 1953 that give the ATO the power to withhold refunds in certain circumstances;
- The running balance account rules in TAA 1953 (which presumably would be in point where it is intended to apply the refund against other tax liabilities).

4. *Are there any other comments on the proposed arrangements for quarterly credits outlined in this consultation paper?*

From a practical perspective, on a review of the arrangement of the TAA 1953, an appropriate positioning of the new rules could be a new Part IIC of the Act itself with appropriate interaction, links or references to the PAYG instalment rules contained in Part 2-10 of Schedule 1.

If the legislation does go ahead as drafted, generally the time limits in question may be unrealistic given the application requirements of applying to both AusIndustry and the ATO.

The payment is made by reference to four quarterly payments being made with no provision for any catch up for missed payments. It is suggested that if there is a delay in the approval process this should be taken into account in assessing the payments. It is noted that it is still open to a taxpayer to vary its remaining quarterly payments to take into account any missed payments but it would not have the safe harbour provisions and penalty interest would be charged if it was incorrect.

There is a requirement for a taxpayer to be a complying taxpayer in respect of the relevant income year. It must not have any outstanding tax liabilities and be up to date with respect to all lodgement requirements. It would need to be clarified whether this was in respect of only income tax issues or cover BAS's, FBT etc.