

October 26, 2009

The General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam

Re: Response to Consultation Paper: The New Research and Development Tax Incentive

This submission is based on the following principles which are either implied or expressed in the R&D consultation paper (RDCP):

1. That the countries identified as benchmark (US / UK /) in the RDCP are inappropriate, particularly given their economic performance over the past 12 – 18 months. For Australia to be internationally competitive R&D activities must be superior to other OECD countries, not merely comparable;
2. The premise that changes to R&D must be revenue neutral. The risks to the federal budget associated with the R&D provisions are minimal in comparison to the size of the budget. Moreover, for Australia to become an international centre for R&D, we must be prepared to invest and improve our R&D efforts. The notion that Government R&D expenditures must be revenue neutral is counter intuitive to both the need to be internationally competitive and also from pronouncements made by Ministers and the recommendations of the Cutler Innovation Review;
3. Software development and use (and therefore broader spillover benefits) is equally dependant on the development of interface mechanisms as it is other forms of software R&D. The rapid changes being experienced in both delivery mechanisms for example, mobile phones and distribution mechanisms, for example wireless make the development of user interface fundamental to the successful leverage of underlying technologies.

When considered in the context of an increasing consumer active economic environment, the exclusion of software interface activities is at best, short-sighted and at worst will result in the loss of substantial activities in this area;

4. Whilst recognizing the importance of supporting R&D expenditure, expenditures incurred in carrying out direct R&D expenditures should be treated preferentially to those incurred in supporting activities; and
5. Production related activities is an integral part of the R&D process particularly in the high technology manufacturing sector – the technology must be able to be delivered (built) and produced at competitive prices, both of these aspects are function of production related activities. A failure to recognize this link does not recognize the importance and role of production related activities in the R&D process.

Our submission applies these concerns to the relevant paragraphs contained within the RDCP.


Paragraph	Comment
39	<ul style="list-style-type: none"> Treat R&D expenditures that do not qualify for preferential treatment as normal expenditure for the purposes of the claim. This would preclude these monies from receiving a credit and also eliminate the need for cash refunds.
48 - 49	<ul style="list-style-type: none"> Whilst agreeing with the general principle of spill over benefits, perhaps a test could be introduced to the existing definition of research and development innovative or technical risk that requires the claimant to demonstrate that the R&D project would not proceed in the existing year without the benefit of the provision.
52	<ul style="list-style-type: none"> Disagree with the logic that you need innovation and high levels of technical risk to produce benefits. The RDCP does not provide any evidence for this assertion and the proposition that expenditures of either an innovative or those involving a high degree of technical risk both produce benefits can be equally strongly argued. The existing difficulties surrounding demonstrating innovation compared to technical risk will be extenuated and will present both additional risks and costs in claiming the R&D provision.

55	<ul style="list-style-type: none"> Comparisons with the US and UK at the moment are particularly irrelevant given their economic performance. Australia should be benchmarking against countries of similar size, development, and where possible, economic structure. If recent pronouncements by Ministers and the results of the Cutler Innovation review are to be considered to provide context to the R&D framework, any benchmarking should be undertaken against countries where R&D is broadly defined or have been successful in generating high ratios of R&D expenditure to GDP.
61 - 63	<ul style="list-style-type: none"> Not practical. Many SME organisations 'mesh' R&D and supporting activities with other non R&D activities. Whilst the actual conducting of the supporting activities is of itself undertaken to purely support the direct R&D, the actual manner in which this conducted is often integrated into other organizational activities (e.g. production). Being able to utilize employees for 10% – 15% of their time in supporting R&F activities is often critical to the success of the project and employment and skill development of the employees and the organizational more broadly.
64 - 65	<ul style="list-style-type: none"> This is just not correct in an SME environment when employee roles are less clearly defined. For the employee to be sufficiently productive to allow them to complete R&D activities they may need to be engaged in some form of production (non R&D) output.
70	<ul style="list-style-type: none"> Is the preferred approach to this issue. The underlying systems are already in place, reducing the costs and confusion of changing to alternatives. This approach also recognizes the importance of supporting activities in the development of R&D. The Australian economy has a high manufacturing base which requires high degree of supporting activities and a failure to adequately reflect this within the R&D framework is at best discriminatory towards manufacturing related R&D activities (making a determination to favour a particular sort of R&D over any other is not the role of Government).
76	<ul style="list-style-type: none"> Major change that fails to recognize the nature of the software industry and the forces driving development in the industry. The proposed change does not take into account the significant of: user interface and allowing access to the complex underlying software through interfaces; and websites as key drivers / enablers of underlying software development activities

77	<ul style="list-style-type: none"> Without many of the developments being undertaken in [76] the benefits of [77] will not be realized. [76] activities represent the application of often complex underlying software engineering and R&D to the broader market. Making such software usable and accessible does not mean this is any less important in terms of spillover benefits, or requires less innovation and technical risk. It could be argued that without [76] activities, [77] activities would not produce the broader societal and spillover benefits as the underlying software would be as accessible. The proposition discriminates against one type of R&D over another. To illustrate our point, without the interface technologies used by google or facebook, the underlying software technology would not be available to broader society. [76] and [77] software technologies are symbiotic, and to discriminate in favour of one over another risks both, not just [76] type R&D.
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We trust this submission will be positively received and the comments employed in the development of this critical legislation.

Yours sincerely



MAL VALLANCE
CHAIR