

# Roger Gray and Associates Pty Ltd

ABN 34 132 592 495

20<sup>th</sup> October, 2009

The General Manager,  
Business Tax Division,  
The Treasury,  
Langton Crescent  
Parkes ACT 2600

Dear Sir,

**Re: The new research and development tax incentive – Consultation Paper**

Thank you for the opportunity to provide feedback and comments on the consultation paper, which raises a number of important issues relating to future R&D tax incentives. Comments on particular aspects of the paper are provided below.

## **Introduction**

Paragraph 1 refers to a “more streamlined R&D incentive from 1 July, 2010”. A critical issue is the need for simplicity, noting that the complexity of the present scheme invariably requires business to seek expert professional advice, the cost of which is substantial, especially to smaller early stage companies having little or no income stream. A general perception, on reading the paper, is that complexity might increase with the new incentives, thereby adding further to administrative costs at the expense of the R&D expenditure at which the incentive is targeted.

Greater simplicity will lead directly to a more cost effective scheme for both industry and government.

## **Principle 1**

Paragraph 22 notes that the Refundable R&D tax credit will be open to companies with up to 50% ownership by exempt entities (from 1 July 2010). This is welcomed. However, Section 4.2 of the present guide states that, where exempt companies own *or have the right to acquire* at least 25% of the voting power or rights to distributions from the company, the eligibility requirement will not be met.

Thus it would seem that a company putting in place arrangements that would grant an exempt company the right to acquire 25% or more (but less than 50%) of the voting rights in 2010/11 or later would be ineligible if those arrangements were made before 30 June 2010.

Transition arrangements are needed to enable business and universities to plan ahead without risking their eligibility for the current tax offset. This could be achieved by removing the condition in the present scheme relating to an exempt company's right to acquire 25% or more.

Paragraph 28 states that location of IP ownership is not relevant. However, overseas ownership of IP may lead to Australia's exclusion from any ongoing commercial benefits and from further research opportunities that may arise from successful completion of the relevant R&D.

Adoption of this concession will add to government expenditure without necessarily providing additional benefits to the Australian taxpayer.

## **Principle 5**

This states that the R&D tax incentive should target R&D that is in addition to what otherwise would have occurred and which provides spillovers. Paragraph 49 goes on to note that the

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principle of additionality (of R&D expenditure) and spillovers will underpin the design of rules for eligible activities.

Narrow interpretation of this principle may lead to exclusion of otherwise eligible R&D for the sole reason that the R&D would have been undertaken anyway, without the benefit of tax incentives and ignoring issues that directly impact on the potential success of the R&D, such as:

- timeliness of the R&D to achieve technological competitiveness,
- scale - back of essential complementary work to enable a company to fund its R&D without the benefit of incentives, potentially reducing the commercial success of the R&D, and
- extended duration of the R&D project, so as to contain the rate of expenditure within the rate at which funding becomes available without the benefit of concessions. Delays can lead directly to lost opportunities.

It is acknowledged that eligibility constraints are needed to ensure that the incentive is properly targeted and managed within government budget allocations. However, increased government expenditure arising from relaxation of principle 5 could be offset through a reconsideration of the proposals in paragraph 22 to extend availability of the concession to include cases where IP is owned outside Australia and in paragraph 37 to increase the turnover cap to \$20 million.

Otherwise smaller companies, not yet able to generate sufficient revenues of their own, will be disadvantaged.

### **Principle 7**

Care is needed to avoid unnecessary complexity in the definition and interpretation of Core and Supporting R&D. Otherwise compliance and administration costs and effort could be excessive for only marginal benefits to the taxpayer.

Also, section 61, suggesting a sole purpose test, overlooks a possibly a better option, namely:

“other activities that are carried on for the purpose of supporting the carrying on of [core activities]”

I trust that these comments will be taken into consideration as the new scheme is being developed.

Yours faithfully,

Roger Gray  
Director