



the coal industry's research program

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**Submission – The New Research And Development Tax Incentive Exposure Draft Legislation
and Associated Explanatory Material**

Dear Sir/Madam

I would like to provide a submission regarding "The new research and development tax incentive Consultation paper" for your consideration.

Australian Coal Research Limited (ACRL) is a Registered Research Agency and manages the Australian Coal Association Research Program (ACARP) on behalf of the Australian black coal industry. ACRL is a 'not for profit' tax exempt entity operating under an MOU between the Commonwealth and the Australian Coal Association. It is not a coal producer but purely a research organisation established to enhance the productivity, safety, sustainability and environmental performance of the black coal industry.

ACRL does not conduct research in its own right but contracts the required research out to many of Australia's most prestigious research organisations such as CSIRO, universities, CRCs etc. Its average annual research expenditure is in the range of \$12 - \$15 million.

ACRL has received two Class Rulings (CR2005/9 and CR 2009/45), both of which allow contributions paid to the ACARP program to claim a deduction under subsection 73B(13) for levies/contributions paid to ACRL and applied in return for the performance of research and development activities (as defined in subsection 73B(1)) on their behalf by ACRL. They recognise ACARP as an industry research program and allow participants to claim levy payments in the year they are made.

ACARP is funded through a voluntary five cents per tonne levy on all saleable coal. Producers participate on the basis that all levy contributions are eligible for the 125% R&D Tax Concession. Our ATO Class Rulings also state that all levy-funded expenditure must qualify for the 125% R&D Tax Concession (and logically, its successors).

Under the proposed new arrangements, ACRL will have to apply for a new Class Ruling under the R&D Tax Credit system to ensure this requirement is met. This is an eight month exercise on the last

experience. I believe this creates an unnecessary uncertainty, an additional compliance burden and cost that could otherwise be used for additional research.

I believe that the Class Rulings would be unnecessary if the new arrangement recognises industry research programs like ACARP (apparently there are only around 5 or 6 of these) that meet defined criteria such as:

1. Operate under a Commonwealth or State MOU or similar arrangements that have legislative backing;
2. Have the written support of the relevant industry peak body;
3. Be not for profit and operate for the clear benefit of an industry sector;
4. Have a track record over time of compliance with subsection 73B(13); and
5. Have Research Service Provider status.

ACRL and black coal producers have been participants in the R&D Tax Concession arrangement since its beginning, and I would like to think, are seen as stakeholders in any changes being considered with the introduction of the R&D Tax Credit system.

I would like to provide the details of my submission in the same order in which they appear in the Exposure Draft Explanatory Materials:

General

The ACARP program is made up of a number of research themes, some of which stretch back a number of years. An example of this is the Automated Underground Mining Research Theme, which began as a scoping study in 2000 and has since led to the development of an automated longwall shearer control system that is now a commercial reality and available to producers in this country. It improves productivity, reduces downtime, and removes personnel from this dangerous mining environment. It has been a great success.

Because of this long term integrated research strategy, what may appear to others as a series of unrelated projects funded year by year are really milestones in a long running theme, mostly core research, with some supporting activities (such as dissemination of learnings such as best practice guidelines for uptake by producers). Each technical area has its own five year strategic research plan that feeds into ACARP's integrated five year research plan.

The themes are managed as individual projects to maintain close control over outcomes and are treated as decision gates. The Commonwealth should take care to craft the guidelines in such a way so as to recognise long term research programs and the linkages this can create over time between core and supporting activities.

Point by point

1.12 R&D activities are defined as either 'core' or 'supporting' R&D activities.

- Core R&D activities are experimental activities that are systematic and investigative and:
 - involve considerable novelty and high levels of technical risk; and
 - are conducted for the purpose of acquiring new knowledge or information, including knowledge or information concerning the creation of new or improved materials, products, devices, processes or services.
- Supporting R&D activities are activities undertaken for the dominant purpose of supporting core R&D activities.

I believe dash point 2 (highlighted above in bold) should be amended to read “new, safer or improved”. Safety research makes up over 30% of ACARP’s research program because no-one should have to risk their life or health simply to make a living.

Accidents have a huge impact on the nation’s productivity, especially in mining, and any safety-related research or development that can effectively reduce this huge cost should be automatically accepted as Core R&D, and lower hurdles for “considerable novelty and high levels of technical risk” applied. I will leave it to the Treasury to consider the optics of rejecting safety-related R&D that could save lives and injuries.

- 2.21 Novelty means the development of technology or a new use of existing technology, by comparison with knowledge of the technology that is publicly available on a reasonably accessible worldwide basis.

I believe this clause overlooks the fact that State-based regulatory barriers often preclude accessibility. For example, a technology that may be available for applied research/use in NSW coal mines is NOT automatically available for use in other States. The technology must be authorised for use separately in each State jurisdiction by the relevant Mines Safety Authority before research can be undertaken on site and subsequently accepted for use on site. I believe this arises in part from Australia’s Constitution and the powers it grants States versus the Commonwealth. This regulatory regime dramatically limits accessibility, and needs to be taken into consideration when determining whether a technology is “reasonably accessible”.

In the case of ACARP it often means that the research must be conducted in several State jurisdictions either concurrently or sequentially, possibly technically reducing its novelty under the proposed definition. I therefore believe the phrase “in the environment to which it is to be applied” should be added to the definition of novelty to recognise the barriers of jurisdiction.

- 2.25 Technical risk exists when knowledge of whether something is scientifically possible or technologically feasible, or how to achieve it in practice, is not readily available or deducible by a competent professional working in the field.

I believe the phrase “or provable to be safe in the environment to which it is to be applied” should be added to the definition of technical risk. I submit that technical risk also arises where something may be scientifically possible or technologically feasible, but has yet to be proven to be safe in the proposed working environment. As in my statement for clause 2.21, there may be no technical risk in implementing a new technology in a domestic dwelling or a factory, but due to the danger of a methane explosion, technical risk remains until it can be proven to be safe in an underground coal mine.

- 2.40 In discerning the purpose for undertaking an activity, regard must be had to the overall circumstances within which the activity is conducted. Similar sets of activities that might qualify as supporting activities in one context might not in another. A critical factor will be the extent to which the activities in question will also achieve outcomes (such as production or other commercial goals) over and above assisting the conduct of the core activities, and the importance of those outcomes in the context.

ACARP conducts research on behalf of the entire Australian black coal industry and makes the research available to all producers. Its only purpose is to conduct and disseminate the outcomes of research. One of the many benefits of the arrangement is that it eliminates the replication of similar

R&D by multiple producers, i.e., “reinventing the wheel”. Clearly this reduces costs for producers AND the Commonwealth in respect of R&D Tax Credit claims.

ACARP literally does it once and for all, and then makes it available to all producers via downloadable reports, seminars, websites etc. It is pointless to conduct research and then not to publish it in the most digestible form to benefit the industry. The best technology diffusion mechanism is chosen for each research outcome to encourage the highest levels of uptake. The research tools themselves are then often made available to producers for implementation on site as part of the dissemination process. Once again, this reduces costs for the industry as a whole AND the Commonwealth in respect of R&D Tax Credit claims.

I believe these benefits should be considered as “spillover” and be considered as a critical factor when determining eligibility as Supporting R&D Activities. In all cases the dominant purpose is to conduct research to enhance the productivity, safety, sustainability and environmental performance of the industry. I submit that ACARP’s dissemination of research outcomes to producers in all its forms be allowable as a supporting R&D activity regardless of the delivery mechanism employed. Eligible Supporting R&D Activities should therefore include the development of websites that are dissemination platforms as an allowable non commercial technology diffusion mechanism in the case of Research Service Providers.

- 2.44 The existing exclusion for ‘in-house’ software is strengthened and incorporated into the exclusions list (rather than being in a separate provision) [Schedule 1, item 1, paragraph 355-35(2)(o)]. The exclusion continues to be couched in terms of a ‘multisale’ requirement that, if satisfied, carves an activity out of the exclusion.
- 2.45 However, the multisale test can only be satisfied where the purpose of the supply is to make a commercial return directly from the supply. This has the effect that the test is not satisfied where software is licensed for zero or a nominal charge — such as where principally made available to enable customers to access other products (for example, software supplied to customers so that they can conduct their online shopping or banking with the supplier of the software).

The software exclusion 355-35 (2) (o) appears to include the development of any non-commercial software for research purposes and excludes them as either Core or Supporting Activities. ACARP (and many other research organisations) appear to be captured by the clause because ACARP is a not-for-profit organisation that conducts research on behalf of the whole industry and does not benefit itself. As Intellectual Property always remains with the contracted researcher (and therefore any potential commercial returns down the track), ACARP does not appear to satisfy the requirements of 355-35 (2) (o). It appears to be precluded from conducting vital research by this exclusion because our ATO Class Ruling (CR2009/45) states that all levy expenditure must qualify for the R&D Tax Concession (and logically its successor - the R&D Tax Credit).

ACARP often conducts computer intensive research to assess whether a technology is potentially feasible before proceeding with scale models and on site research. This reduces risk and cost of developing a technology that may not work in practice. Examples include Finite Element Analysis and Discrete Particle Analysis modelling of explosions to discover new ways of suppressing underground explosions. It would be impossible to simulate an explosion in an underground mine without employing computers, which inevitably requires some input of data and programming to be successful. It is unclear if programming of existing software as part of the data input phase of research, or development of a specific non-commercial software research tool is captured by the exclusion.

Clearly, it would be unconscionable to exclude research of this type that can save lives, and so I believe is an unintended oversight that will be rectified.

The dominant purpose is to develop safer and improved processes and technologies, not commercial software.

Similarly, when trying to develop improved coal beneficiation processes, physical components such as cyclones are modelled on computer via Discrete Particle Analysis and similar methodologies to determine dynamic flows and wear patterns under various conditions because it is simply impossible to safely achieve this in the real life situation – it is simply a research tool. Once again, this inevitably requires input of data and some programming to be successful. The dominant purpose is to develop improved processes and technologies and reduce downtime, not production of commercial software.

These examples demonstrate the reasonableness of software/programming developed as part of the research process for research purposes being allowable as a supporting activity. These should be allowable as a supporting activity for organisations like ACARP.

Occasionally software is incidentally developed as part of a research project that leads to a commercial product developed by third parties down the line. A potential commercial return could arise for end users who develop or use the software, or for coal producers who implement the improved technology proven up by the software or simulations. However, all of these are separate entities to ACRL and so ACRL itself remains excluded by 355-35 (2) (o) (ii). These should be allowable as a supporting activity for organisations like ACARP as part of the research process for research purposes being allowable as a supporting activity (a “spillover” outcome”).

Another example is where an interactive non-commercial software tool is developed as a technology diffusion strategy for use by producers to improve processes and procedures on site. An example of this could be an interactive database to help identify improved tyre-changing procedures for application on the mine site based on accident reports gathered from around the globe. This type of research dissemination tool is far more effective than a paper-based report and should be allowable as a supporting activity. The database is simply a dissemination tool leading to improved “spillover” outcomes.

I recognise that it could be intended that this situation is covered by 355-35 (2) (o) (ii), but this is ambiguous and could not be relied upon unless specifically clarified. To prevent this I submit that clause 355-35 (2)(o) of the draft Bill be amended to include the following point:

- (iii) for the purpose of conducting or disseminating research by a Research Service Provider to defined end users.

Alternatively, in the case of organisations such as ACARP a flow through could be allowed to them as a distinct declared class of Research Service Provider, recognising that any potential commercial returns would be to their defined “end users”, i.e, in ACRL’s case, the coal producers.

Conclusion

It is not by accident Australia is among the safest, cleanest and most productive coal producers in the world. The industry’s foresight in establishing ACARP in 1993 has been a significant factor in the performance of the Australian coal industry.

I believe these suggestions have the ability to improve the new tax system in a way that will positively impact the industry's potential to continue to enhance its productivity, its safety record, its environmental performance and its long term sustainability and allow it to continue to be a significant contributor to employment and GDP in this country.

ACRL and Australian black coal producers are keen to support any move to increasing the incentive for the funding and overall amount of R&D undertaken in Australia provided it reduces the complexity of definition and does not result in differing levels of tax support within any legitimate R&D program such as ACARP.

ACRL has a keen interest in the new tax incentive system and would like to ensure by its active participation that:

1. The transition go as smoothly as possible;
2. If possible, the new arrangement be simpler to administer, and lastly,
3. ACARP and coal producers not be disadvantaged by changes to the current arrangement.

Yours faithfully

A handwritten signature in blue ink, appearing to read 'Mark Bennetts', with a stylized flourish at the end.

Mark Bennetts
Executive Director