

Re-Think: Tax discussion paper

AIIA response

1 June 2015

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1. About AIIA

The Australian Information Industry Association (AIIA) is the peak national body representing Australia's information and communications technology (ICT) industry. Since establishing 35 years ago, the AIIA has pursued activities aimed to stimulate and grow the ICT industry, to create a favourable business environment for our members and to contribute to the economic imperatives of our nation. *Our goal is to "create a world class information, communications and technology industry delivering productivity, innovation and leadership for Australia".*

We represent over 400 member organisations nationally including hardware, software, telecommunications, ICT service and professional services companies. Our membership includes global brands such as Apple, EMC, Google, HP, IBM, Intel, Microsoft, PWC, Deloitte, EY and Oracle; international companies including Telstra, Optus; national companies including Data#3, SMS Management and Technology, TechnologyOne and Oakton Limited; and a large number of ICT SME's.

2. Executive Summary

The AllA appreciates the opportunity to provide this submission to the Government's Re-Think: tax discussion paper.

This submission outlines that:

1. AllA supports the current R&D tax incentive scheme and considers government support for R&D should be seen as a net benefit for the economy not a cost.
2. If anything, the scheme should be expanded for a number of reasons:
 - If Australia's R&D tax incentive is not attractive companies will relocate their R&D activities to locations that better incentivise R&D activity
 - Current business spending in R&D is low and reducing the R&D tax incentive will exacerbate this.
3. Any R&D reform needs to be considered in the context of broader reforms to the innovation system. This is critical to ensuring the right policy, regulatory and financial levers are in place to foster and support effective innovation.
4. The key characteristics of an expanded R&D scheme include:
 - Stability and certainty in government policy;
 - Adopting best practice in R&D tax incentive schemes; and
 - A more informed and systematic approach to building innovation in Australia.

We also note concerns with the Government's proposal around online GST and multinational tax avoidance.

3. R&D tax incentives

This section addresses questions 39 and 40 of the tax discussion paper:

- Qt 39: Does the R&D tax incentive encourage companies to conduct R&D activities that would otherwise not be conducted in the absence of government support? Would alternative approaches better achieve this objective and, if so, how?
- QT40: What other taxation incentives, including changes to existing measures, are appropriate to encourage investment in innovation and entrepreneurship?

3.1 AIIA supports the current R&D tax scheme

Policy objective

As noted in the discussion paper, the R&D tax incentive aims to:

- encourage R&D activity that would not otherwise occur;
- improve the incentives for smaller companies to engage in R&D by providing a source of funding to grow their business and take risks that they otherwise would not; and
- attract new investment in R&D activities, including from foreign investors.

Government support for R&D should be seen as a net benefit for the economy not a cost

The policy rationale for public funding of R&D is well-understood:

- R&D is a costly and risky activity that creates significant positive externalities for society as the knowledge that R&D creates inevitably diffuses across the economy and creates benefits that cannot be fully captured by the individual researchers and companies conducting the R&D.
 - Although no review of the economic benefits of Australia's R&D incentives has been conducted in Australia, a review of R&D incentives in the EU indicates a multiplier effect of \$1 for every dollar of R&D Tax incentive support.¹
- Crucially, for a small open economy like Australia, R&D leverages and builds STEM skills in the workforce, and increases the capacity of companies to take up innovations at a faster rate.

Given the significant structural change that is currently occurring in Australia's economy, innovation will be crucial to maintaining Australia's competitiveness internationally. Accordingly, the R&D tax incentive should not be seen as a cost to cut, but rather valued in terms of its overall benefit to the economy through spillovers and competitiveness.

3.2 If anything, the scheme should be expanded

If Australia's R&D tax incentive is not attractive companies will relocate their R&D activities to locations that better incentivise and reward R&D activities

Whether or not the R&D tax incentive encourages companies to conduct any more R&D than they otherwise would, it certainly encourages them to undertake more R&D activities in Australia. ICT businesses and their employees are internationally mobile, which means they can and will relocate to countries with more attractive support for R&D.

The R&D tax incentive is the primary source of public support for private sector R&D activities in Australia. The R&D tax incentive currently provides:

¹John Clark and Erik Arnold Technopolis, The Evaluation of Fiscal R&D Incentives, 2005, http://ec.europa.eu/invest-in-research/pdf/download_en/final_version_technopolis_report.pdf

- a 45% refundable tax offset for eligible entities with an annual aggregated turnover of less than \$20 million, and which are not controlled by income-tax exempt entities, for expenditure on eligible R&D activities in Australia; and
- a 40% non-refundable tax offset for all other eligible entities for eligible R&D expenditure.

As at 30 June 2014, 11,936 companies had registered to claim the tax incentive for the 2012-13 income period, of which 2,700 were first time claimants. The total R&D expenditure registered was \$19.69 billion. As at 29 August 2014, the tax incentive had a reported cost to the Budget of around \$2.5 billion for the 2012-13 income period.²

Many of Australia's major competitors offer more generous support for R&D and innovation. For example, in the UK, available incentives include R&D tax relief, an R&D tax credit, and an R&D allowance for capital expenditure. Qualifying income from patents can also be taxed at a lower corporate tax rate.³ In 2013, the latest available data, the UK government spent £28.9 billion on R&D support.⁴

Current business spending in R&D is low and reducing the R&D tax incentive will make it worse

Alla notes that in the 2014-15 Budget, the Government announced that the refundable and non-refundable tax offset rates would be reduced by 1.5 percentage points, from 45% to 43.5% and from 40% to 38.5%, respectively. The proposed changes would take effect for income years commencing on or after 1 July 2014.

On 12 February 2015, the Parliament enacted the Tax Laws Amendment (Research and Development) Act 2015, which introduces a limit of \$100 million on the amount of R&D expenditure that companies can claim at the standard offset rate. For amounts above \$100 million, companies will be able to claim a tax offset at the company tax rate. The changes take effect for income years beginning on or after 1 July 2014.

These measures are counterproductive given business spending on R&D in Australia is already low, and business investment generally is weak.

According to ABS latest data, Australia's business spending on R&D (BERD) occurred mainly in Mining and the Financial and Insurance Service industries, which lifted their combined share in total BERD from 26% in 2006 to 37% in 2012. Consequently, the contribution of Manufacturing, the sector typically associated with higher end technological products, declined from 36% to 24% over this period.⁵

Investment in intangibles is another broad proxy measure for investment in innovation-related activities. Intangible capital includes assets such as data, software, designs, new organisational processes, management quality, R&D, patented technology, reputation (brand equity) and firm-specific skills. In many developed countries, annual business investment in intangible capital rivals or exceeds investment in physical capital. This is not the case in Australia. The ratio of intangible capital investment to physical capital investment was 42% in Australia in 2010. This compares poorly with the US at 200% and the OECD average of 82% in the same year.⁶

² Department of Industry 2014, 2014-15 Science, Research and Innovation Budget Tables, Australian Government, Canberra, www.industry.gov.au/innovation/reportsandstudies/Pages/SRIBudget

³ EY, Worldwide R&D Reference Guide, 2013-2014; [http://www.ey.com/Publication/vwLUAssets/EY-Worldwide_R_and_D_incentives_reference_guide/\\$FILE/EY-Worldwide-R&D-incentives-reference-guide.pdf](http://www.ey.com/Publication/vwLUAssets/EY-Worldwide_R_and_D_incentives_reference_guide/$FILE/EY-Worldwide-R&D-incentives-reference-guide.pdf)

⁴ UK Government, Office of National Statistics, Gross Domestic Expenditure on Research and Development, 2013, <http://www.ons.gov.uk/ons/rel/rdit1/gross-domestic-expenditure-on-research-and-development/2013/index.html>

⁵ Australian Government, ABS, 8104.0 - Research and Experimental Development, Businesses, Australia, 2011-12, <http://www.abs.gov.au/ausstats/abs@.nsf/lookup/8104.0Media%20Release12011-12>

⁶ Australian Government, Office of the Chief Economist, Australian Innovation System Report, 2014, <http://www.industry.gov.au/innovation/reportsandstudies/Documents/Australian-Innovation-System-Report-2014.pdf>

3.3 Any R&D reform should be done in the context of an innovation system reform

R&D is part of the innovation ecosystem that is critical to Australia's future global competitiveness.

Innovation is a key factor for competitiveness and growth in a developed economy.⁷ 1950s economist, Robert Solow, found that labour and capital accumulation only explains about 30% of economic growth. The rest is explained by innovation. Solow's growth accounting model⁸ is a widely supported economic theory,⁹ indicating the crucial role of innovation in explaining long-term economic growth.

R&D plays a key role in innovation. Generally, R&D turns money into knowledge and innovation is the process of creating business out of this knowledge. The benefits of innovation to an advanced economy are well documented. It should be concerning for the Government that Australia performs relatively weakly on this measure.

Australia's innovative outputs are low despite having the right fundamentals for innovation

The Australian Innovation System Report series annual reports show that Australia does not do well in producing original goods, with very little high-tech products making their way to global markets.¹⁰

International comparisons of Australia's performance support this finding. The 2014 Global Innovation Index (GII)¹¹ ranked Australia 17 out of 143 economies across 81 indicators. Our 17th position overall was based on a relatively strong performance in its innovation inputs (i.e. public research funding), ranked 10, while its innovation outputs ranked 22 demonstrating the low efficiency of Australia's innovation system, which overall achieved a score of 0.70, below the average of 0.74 of all 143 countries.

This essentially means we have the right fundamentals for innovation, such as public research spending, but we do not use these advantages for outcomes that are on par with the most competitive countries. In fact, we are outclassed by countries such as Malta and Estonia.

The 2014-15 Global Competitiveness Index (GCI),¹² also indicates that Australia is losing ground in terms of our international competitiveness. We achieved our best result in 2009 at number 15 and has since slipped to number 22 out of 144 countries assessed.

Lack of innovation culture

Innovators and entrepreneurs are a nation's job creators. With increasingly rapid advances in technology, they are also the 'creators' of the jobs and careers of the future - a point borne out by Michael Mandel's recent analysis, Jobs in the Australian App Economy¹³.

Notwithstanding that repeat entrepreneurs who have failed once before have been shown to have a higher chance of success than those trying for the first time¹⁴, Australia's tolerance for business risk and failure is low. The low acceptance of business failures means potential innovators are often reluctant to launch new ventures for fear of harming their reputation. It is also reflected in the

⁷ OECD (2013) Science, technology and industry scoreboard, OECD Publishing, <http://www.oecd.org/sti/scoreboard.htm>

⁸ Solow RM (1957) Technical change and the aggregate production function, Review of Economics and Statistics 39(3):312-320

⁹ See Deirdre McCloskey's keynote speech at the 14th Joseph Schumpeter Conference, Brisbane, July 2012; Rosenberg N et al. 1992, Technology and the wealth of nations, Stanford University Press; and Verspagen B 2005, Innovation and economic growth, in: Fagerberg J, Mowery DC & Nelson RR (eds), The Oxford handbook of innovation, Oxford University Press.

¹⁰ Ibid 6

¹¹ The Global Innovation Index 2014, <https://www.globalinnovationindex.org/content.aspx?page=GII-Home>

¹² The Global Competitiveness Report 2014-2015, <http://reports.weforum.org/global-competitiveness-report-2014-2015/>

¹³ Mandel, M. 2014. Jobs in the Australian App Economy. Progressive Policy Institute.

¹⁴ P A Gompers et al., "Performance Persistence in Entrepreneurship and Venture Capital", Journal of Financial Economics. Vol 96. No.1 2010

reluctance of talented people to transfer from the tertiary education sector to private sector organisations - the perception that it is a failure to go from research in university to business.¹⁵

The Innovation Systems Report 2012¹⁶ includes an analysis suggesting that around 70% of businesses have some degree of innovation culture, but 44% have an ad hoc approach and 6% do not practice it despite having a strategy in place. Only 18%, mostly large businesses, are strategic innovators. Additionally, the University of Melbourne and the Australian Institute of Management conducted a survey of 2,400 business professionals from all sections of industry and government that found that poor leadership is the main reason organisations fail to innovate.¹⁷

A characteristic of countries with a mature innovation ecosystem is that they typically have a more established history and culture of entrepreneurship.¹⁸ This must be an explicit goal of Australia's innovation ecosystem.

Further dilution of the existing R&D tax incentive undermines the development of an effective national innovation culture, particularly amongst small businesses, which typically have limited cash flow. The R&D tax incentive provides a much needed financial incentive to encourage R&D risk taking.

3.4 Key Characteristics of an expanded R&D scheme

Businesses that invest in R&D require stability and certainty to plan their R&D investment

AIIA recommends the Government commit to an internationally competitive R&D scheme. The next section explores what this scheme might look like.

Best practice for R&D tax incentives

AIIA understands that global best practice is not always applicable to the Australian context. However, international schemes provide examples that Australia can draw from.

The 2014 EU Report on R&D tax incentives¹⁹, which explores whether or not R&D tax incentives work, puts forward 20 principles of best practice for R&D tax incentives. These principles are grouped into three categories; scope, target and practice. Some key principles for an effective R&D tax scheme are outlined below. These are provided for information only.

- Volume-based R&D tax credits are preferred over incremental ones. Incremental R&D tax incentives may trigger firms to change the timing of their R&D investment plans. For example, incremental schemes make it more attractive for firms to gradually increase their R&D investment than to do a single large investment now if profits from these investments will materialize later in time. This might result in a slower pace of innovative outcomes than would otherwise be the case. Also, incremental schemes result in higher administrative and compliance costs. As incremental schemes probably are not more effective than volume-based schemes, the higher costs of incremental schemes make volume-based schemes a better practice. The vast majority of instruments are volume-based.
- Tax incentives should only be aimed at R&D activities that are likely to contribute to the world-wide stock of knowledge, rather than support activities limited to advancement in

¹⁵ Ibid.

¹⁶ Australian Government, Department of Industry, Innovation, Science Research and Tertiary Education, Australian Innovation System Report, 2012,
<http://www.industry.gov.au/science/policy/AustralianInnovationSystemReport/AISR2012/index.html>

¹⁷ The report Innovation: The New Imperative, 2013, identified three main barriers to innovation that were all leadership related. It found that: organisations are too risk adverse; employees do not get rewarded for innovating; and it takes an exceptionally long lead time to develop ideas.

¹⁸ The Power of Three. Together, governments, entrepreneurs and corporations can spur growth across the G20. EY. 2013

¹⁹ EU, Taxation Papers, working paper n 52 2014, A study on R&D tax incentives, final report,
http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_papers/taxation_per_52.pdf

a firm's own expertise. The impact of a tax incentive on innovation will depend strongly on the strictness of its novelty requirement. Without any novelty requirement, a tax incentive could stimulate imitation, rather than innovation. Especially for countries close to the technology frontier, such a scheme could reduce innovation instead of promote it. A number of R&D tax incentive schemes have strict novelty requirements, including in Canada and the United Kingdom.

- Tax incentives should ideally apply to those types of expenditures that bring about strong knowledge spill overs. Tax incentives based on the wage bill paid to researchers can be considered best practice in this context, for example because they are likely to generate higher knowledge spill overs than other types of R&D expenditure: researchers move from one employer to another and take their former's employers knowledge with them. A practical advantage of tax incentives for R&D wages is that they have lower administration and compliance costs.
- Young companies, rather than SMEs in general, are more likely to bring the innovations that challenge large incumbent firms. A favourable environment for entrepreneurs might not only contribute to a country's innovativeness but also to the flexibility of its economy. Targeting young companies/start-ups is key to an effective R&D system. A scheme which has been identified as a good practice and explicitly targets young firms is the French tax credit for young innovative enterprises (Jeunes Entreprises Innovantes).
- As R&D expenditure may precede revenue generated by innovation by several years, it is good practice to provide a carry-over facility and an option to receive the benefit even where a company is not profitable (cash refunds). Such features offer firms more flexibility and certainty for investment decisions. This is especially relevant for young companies that typically are not profitable in the first years of operations. While most of the R&D tax incentives analysed offer a carry forward facility, cash refunds are available only in nine countries.
- With respect to the organization of a tax incentive it is good practice to have a one-stop, online application procedure. This is already in place in majority of countries. In addition, the time it takes for tax authorities to make a decision on eligible expenses should be as short as possible, and ideally not exceed one year. Several countries have already introduced an option to receive an immediate refund for smaller companies, as these firms are typically more liquidity constrained.
- Systematic evaluations are also recommended. High-quality firm-level data is indispensable for a rigorous quantitative evaluation and should be collected according to international standards. For seventeen countries no evaluation study has been found. Currently, only few countries have frequent evaluations, for example The Netherlands and France. The quality of evaluation studies is mixed and in many cases does not meet the standards of peer-reviewed academic journals.

More informed and systematic approach to building innovation is necessary

Of course, innovation is not an end in itself; it is the means to achieve the growth, productivity and competitiveness that underpins national prosperity. It is because innovation is so critical to achieving these outcomes that a more informed and systematic approach to building innovation is necessary.

The World Economic Forum report on *Entrepreneurial Ecosystems around the Globe and Early-Stage Company Growth Dynamics* found that the conditions necessary to foster a robust start-up ecosystem are below par in Australia.²⁰ Key impediments that were identified include: the lack of effective links between start-ups and larger companies to connect start-ups with global value and

²⁰ World Economic Forum, *Entrepreneurial Ecosystems Around the Globe and Early-Stage Company Growth Dynamics*, 2014, <http://reports.weforum.org/entrepreneurial-ecosystems-around-the-globe-and-early-stage-company-growth-dynamics/wp-content/blogs.dir/34/mp/files/pages/files/nme-entrepreneurship-report-jan-8-2014.pdf>

supply chains, limited access to capital, unsupportive tax arrangements, overly burdensome government regulations and poor cultural support for early stage companies. The need for a more systematic, joined-up approach to the innovation system is crucial.

As outlined in AIIA's response to the 2014 Senate Parliamentary inquiry into [Australia's National Innovation System](#) any reform in this area should encompass:

- Infrastructure and Knowledge
- Collaboration
- Education and Skills
- Funding
- Regulation and Policy
- Culture

Critically these do not stand alone. The success of the innovation depends on their interconnection.

In our response to the review of Australia's innovation system, AIIA argues that the future of innovation in Australia critically depends on an effective and cohesive ecosystem which incorporates all of the elements above. The R&D tax incentive is a key component of that ecosystem not simply because it provides financial incentive and relief for R&D and innovation risk taking but because it ensures R&D activity is fostered and remains in Australia. It is AIIA's contention that retaining the integrity of Australia's innovation system is undermined by individual, piecemeal policy changes. Abolishing, reducing or changing the R&D tax incentive in isolation further compromises the effectiveness of Australia's innovation investment.

Further details regarding AIIA's contention regarding a holistic innovation ecosystem is contained, for information only, in the Attachment.

4. Other issues

4.1 Online GST

AIIA supports the principle of taxing goods and services consistently. However, it is not clear that this can be achieved in practice. While the Government may be able to require large companies with international reputations to comply with Australian law, despite having no physical presence, it is not clear that the Government will be able to enforce these provisions for smaller overseas suppliers.

Consumers may be able to use technology to circumvent any regime that companies put in place including using virtual private networks to disguise the location of the purchaser or using third party services in the event that credit card details are used to identify country of origin.

As such it is unclear whether the proposed measures in the 2015 budget will serve to level the playing field or just produce a different set of distortions.

It is also not clear how this legislation will effect companies that have existing sale tax obligations under their domestic law.

4.2 Multinational tax avoidance

Company income tax is based on the concept that tax should be levied at the source of where the income is produced. Information technology companies generate most of their income through IP and infrastructure that is not located in Australia.

As such under the existing concept of company income tax it is appropriate for those companies to attribute that income to overseas sources. The reality is that international capital is more mobile and it is relatively easy for technology based companies to relocate, that is why it is important for Australia to have a more competitive tax system.

Information technology is responsible for a substantial proportion in the increase of productivity and wealth that is experienced worldwide. If the Australian government wants a bigger share of this income to be generated in Australia (and therefore taxable by the Australian government) it also needs to put in place a range of other measures to support the domestic ICT industry, practically in relation to STEM education and skills and incentives such as the R&D tax incentive.

Importantly, this is not a technology industry specific issue. It is about global companies that operate across a broad range of industries and reflects cross boarder taxation issues impacting many countries. The OECD is already well advanced in its consideration of the fair taxation treatment of multinational companies in a global digital economy.

AIIA supports a multi-lateral approach and is concerned that unilateral action by Australia or any country will undermine OECD efforts to develop international tax principles for dealing with multinational tax issues.

5. Recommendations

Alla strongly supports retention of the R&D tax incentive to support and sustain an effective innovation system and Australia's competitiveness as a global innovator. We note concerns regarding recent changes to the R&D tax scheme which will result in further limitations to current arrangements.

A vibrant innovation system is necessary to underscore Australia's growth and global competitiveness and the R&D tax incentive is a key component of that system.

6. Attachment

The following summaries AIIA's discussion in our response to the Review into Australia's Innovation System. It provides actionable recommendations to the critical components of a holistic innovation ecosystem.

While AIIA considers all the recommendations we have made a priority, we have identified as **Priority 1** those which we believe must be executed as a matter of urgency.

Infrastructure and Knowledge

To ensure Australia's innovation system is supported by the infrastructure and knowledge required to drive effective innovation outcomes, AIIA recommends:

Priority 1:

- The differentiated role of publically funded research to Australia's innovation system is recognised and better leveraged through a new model of engagement between universities and industry. AIIA recommends consideration of the UK Catapult program, which provides a physical hub to connect business, researchers and academics to stimulate innovation and support the innovation lifecycle. AIIA strongly encourages the Government to build on the now mature capability of NICTA to support and guide such a model.
- Availability of and access to high-end technology developments and ubiquitous high speed broadband. Technology is a crucial enabler and platform for innovation across all industry sectors. Government needs to foster technology as a platform for innovation by supporting the open, free, decentralised and dynamic nature of the Internet

Priority 2:

- Public investment in basic research with a focus on national priorities that leverage Australia's competitive advantage.

Collaboration

Recognising the critical role of collaboration (at all levels) to drive high performance innovation outcomes, AIIA recommends:

Priority 1:

- Establish cross disciplinary and cross sector collaborative models such as the UK Catapult program to facilitate increased collaboration between researchers and business.
- Universities are incentivised to collaborate with industry to develop the commercial potential of their research.
 - This requires reassessment of performance based block funding arrangements under the Excellence in Research in Australia (ERA) program to rebalance the current focus on producing published research papers as opposed to applied outcomes.

Priority 2:

- Establish a national register of intellectual property (IP) for Australian Government funded research institutions to speed up the commercialisation process. IP could be charged (or not) at different charge rates.
 - Where IP from university based research is not used within a specified timeframe that IP is made commercially available.
- Develop a mechanism that supports small and medium sized businesses contract with universities to provide stronger research capacity to their projects.

- Leverage smart digital technology to drive the creation, diffusion and application of knowledge.

Education and Skills

To ensure Australia develops the skills and capability to underpin sustained innovation development AIIA recommends:

Priority 1:

- Development of STEM skills is identified as a priority education focus for all students in years K-12.
- Implement and actively support the Digital Technologies Curriculum. A priority focus must be appropriate training and support for teachers delivering the curriculum.
- Continue to support the current Digital Careers program aimed specifically at increasing the take-up of ICT and specifically computer science courses at the tertiary level.
- To attract entrepreneurs from other countries introduce work visas for entrepreneur. This will help accelerate the growth and maturity of Australia's start up and innovation ecosystem and facilitate relevant skills transfer.

Priority 2:

- Develop a national program of education to support entrepreneurship. Schools and universities have an important role to play in equipping aspiring and potential entrepreneurs with the right skills and attitudes.
 - Such a program needs to be 'hands on' - not constrained by traditional teaching and academic models. A key focus should be giving students' experience of real world business challenges, including how these are managed.
 - Provide student mentoring and coaching programs aimed to provide practical support to young people interested in exploring innovative ideas and entrepreneurship. The support of existing entrepreneurs, philanthropists and innovative businesses - experienced advocates of innovation and entrepreneurship is critical.
- Develop a more integrated approach to driving innovation and entrepreneurship at the university level. This includes a multidisciplinary learning approach that brings together the science and technology students with the business students that could help commercialise their ideas - for example the Centre for Innovation & Entrepreneurship (CIE) at the University of NSW. The Diploma in Innovation Management is a unique multi-disciplinary program, which encourages students to explore an entrepreneurial mind-set and develops the knowledge and skills necessary for commercial innovation.
- Develop a national network of student start-up incubators as proposed in the April 2014 Crossroads Report.²¹

Funding

To assist innovators and entrepreneurs access the capital they need to fund innovation and to appropriately recognise and support investors AIIA recommends:

Priority 1:

- Develop innovative funding platforms such as crowdfunding and microfinance as a means to encourage increased private investment.
- Tax relief for investors in innovative start-ups and high growth companies. This includes relief in the form of tax credits or a reduced rate of tax in the first instances and/or

relief in the form of capital gains tax reductions or exemptions for qualifying venture investments.

- A government innovation fund to source new products, services and solutions from small business to support the development of solutions for government. The U.S. Small Business Innovation Research (SBIR) program is an example of such a model.²²

Priority 2:

- Increasing R&D tax incentive credits in areas of R&D priority aligned with national growth objectives.

Culture

Australia's business culture is inherently risk averse. Innovation and entrepreneurialism is fundamentally about risk taking. To develop a more risk tolerant business culture and one that supports innovation AIIA recommends:

Priority 1:

- Government taking a leadership role in delivering innovative approaches to government service delivery.
- Actions that remove the stigma of 'failure', particularly in relation to business start-ups.
 - This could include amending bankruptcy laws to strike the right balance between protecting the interests of creditors and giving entrepreneurs another chance and providing additional tax relief for investors engaged with companies that go bankrupt.

Priority 2:

- Develop an entrepreneur scholarship program targeted at young people. In addition to providing financial support for young entrepreneurs to access relevant support programs and/or provide them some financial support while they focus on their idea, the program legitimises a career focus on entrepreneurship.
- Showcasing success. This includes businesses showcasing success and emphasizing the benefits of entrepreneurship including job creation and broader social and economic impacts.

Regulation and Policy

Policy and regulatory frameworks that facilitate and support innovation are essential. A number of existing impediments need to be addressed and more flexible policy design that supports innovation and entrepreneurial ventures. AIIA recommends:

Priority 1:

- Develop a whole of government approach to innovation policy with a focus on mechanisms that coordinate policies and activities across agencies.
- Reform current Employee Share Option arrangements to ensure tax on options is not applied until after the value has been realised.
- Introduce innovative funding platforms such as crowdfunding and microfinance. This includes a review of existing legislative arrangements including current prospectus requirements, ability to advertise fund/investment raising activities and support for p2p debt crowd funding from non-sophisticated investors.
- Reform government procurement processes to facilitate increased take-up of innovative solutions offered by small and medium sized business. Government can play a key role in

driving innovation and developing innovative skills by using its purchasing power to engage with and 'invest in' companies with innovative solutions and capabilities. This also facilitates the maturity and growth of businesses and strengthens innovative supply chains.

Priority 2:

- Reduce the administrative burden of tax, regulation and compliance.
 - Simplifying tax codes, creating convenient, accessible online tools that help entrepreneurs and innovators navigate regulatory requirements and simplified rules to help companies understand and raise equity and debt capital smooth the innovation to commercialisation pathway. This includes streamlining ways for business to deal with all levels of government.