ATSE

SUBMISSION TO THE

Research & Development Tax Incentive Amendments

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AUSTRALIAN ACADEMY OF
TECHNOLOGY AND ENGINEERING

ATSE SUBMISSION TO THE DRAFT R&D TAX INCENTIVE AMENDMENTS

The Australian Academy of Technology and Engineering (ATSE)[1] welcomes the opportunity to provide input to the Treasury's Draft Research and Development (R&D) Tax Incentive Amendments.

Key points and recommendations

- The R&D Tax Incentive is an effective measure when used in the spirit that the program is intended and is pleased that the Government is taking action to improve the program.
- The Academy supports the Government's decision to appoint the Board of the ISA along with the Australian Tax Office (ATO) to jointly administer the Incentive.
- ATSE views the Government's non-acceptance of Recommendation 2 of the Review of the R&D Tax Incentive (the Review) as a missed opportunity. To drive greater collaboration, ATSE recommends that the R&D Tax Incentive should provide a premium rate to companies for expenditure on R&D undertaken with Australian publicly funded research organisations.
- The Academy welcomes the proposed clinical trials exemption, which will support the growth of the Australian clinical trials industry.
- The outcomes of the R&D Tax Incentive Changes should be monitored to ensure the impacts on companies is minimised, with resourcing of the ABS to monitor these outcomes improved.
- The Incentive remains a critical part of the nation's innovation ecosystem and it is important that confidence in the program is maintained to provide certainty to businesses and support growth in Australian R&D.

The Academy would be pleased to provide further advice to the Treasury. Please contact ATSE Policy Analyst, Dominic Banfield, on (03) 9864 0903 or dominic.banfield@atse.org.au, if you have any further questions.

[1] ATSE is an independent think tank that comprises the leaders in the fields of technology and engineering, who gain Fellowship to the Academy in a highly competitive process. ATSE is one of Australia's four national Learned Academies but uniquely its 800-strong Fellowship come from industry, government and research organisations, as well as academia. Our Fellowship develops trusted, informed and visionary views to persuade decision-makers to implement the most progressive policies on the development of technology for the betterment of Australia and its people. www.atse.org.au

Administration of the R&D Tax Incentive

The Academy supports the Government's decision to appoint the Board of Innovation and Science Australia along with the Australian Tax Office (ATO) to jointly administer the Incentive. The Academy also agrees with the decision to allow the Board of the ISA to be given a broader scope of delegation powers, make binding determinations, approve grant extensions and determine whether eligible R&D expenditures satisfy the definition of a clinical trial.

Incentivising collaboration to improve knowledge transfer

Innovation and Science Australia's 2016 *Performance Review of the Australian Innovation, Science and Research System* [2] recognised the importance of knowledge creation, knowledge transfer and knowledge application. It found that while there is a focus on supporting the transfer of knowledge between research institutions and businesses, collaboration between researchers and businesses is still limited.

The Review addressed these limitations by recommending (Recommendation 2) the application of a premium rate to the Incentive for businesses that collaborate with publicly funded research organisations, including universities and research agencies. The Review's recommendations were based on the finding that the current Incentive does not encourage collaborative R&D. It cites evidence that collaboration more than triples the likelihood of business productivity growth.

Introducing a premium rate for collaboration will complement other measures in the National Innovation and Science Agenda (NISA) aimed at boosting engagement between industry and research, such as the Australian Research Council's Engagement and Impact Assessment exercise (which is based on the Research Engagement for Australia metric previously developed and piloted by the Academy). Adoption by the Government of Recommendation 2 of the Review would have ensured that this enhanced focus on engagement in the research sector is mirrored by increased collaborative activity on the part of the private sector.

Significantly, the Review recommended that this premium rate be available to businesses that employ recent PhD graduates, echoing a finding from the Australian Council of Learned Academies (ACOLA) review of research training that the value of higher degree graduates be made more evident to Australian industry. Consistent with the ACOLA review, the Government should consider extending this provision to recent research master's degree graduates.

It is worth noting that one of the objectives of the original R&D tax concession, when introduced in 1985, was to improve linkages between business and public sector research organisations. Given that the Incentive represents such a significant amount of public money being directed to private businesses, it is important to ensure that this tax expenditure derives an additional benefit to the nation through improved collaboration.

Research-industry collaborations are underpinned by a commercial transaction, and as such the actual expenditure claimed is readily auditable. Whereas self-assessed internal research expenditure can carry risks of inflated estimates, being based on assumptions on eligibility and cost allocation. Also, the cost to revenue of allowing a higher incentive for shifting to externally performed research

[2] Innovation and Science Australia (2016) *Performance Review of the Australian Innovation, Science and Research System 2016*. Commonwealth of Australia. Canberra.

will be offset to some extent. A premium rate can also help to overcome industry concerns about the learning curve for new collaborations with researchers.

Nevertheless, it should be noted that a successful collaboration may be more dependent on the absorptive capacity of the industry partner than on any premium incentive to pursue it. If industry does not have the receptors in place to absorb or manage collaborative input from a research organisation, a premium tax incentive may be wasted. Therefore, while collaborative research is important for spillover benefits, the value of in-house R&D is also acknowledged. A premium incentive for research-industry collaborations, while enhancing Australia's innovation dividend for research funding, does not penalise businesses undertaking R&D internally or elsewhere.

As such, the Academy emphasises that the program would benefit greatly if the changes described in Recommendation 2 were to be implemented.

Evaluating an appropriate cap

Recommendation 3 of the Review proposed the introduction of a $2 million cap on the annual cash refund payable under the R&D Tax Incentive, with remaining offsets to be treated as a non-refundable tax offset carried forward for use against future taxable income. For companies with an annual turnover below $20 million, the 2018 Federal Budget introduced a refundable R&D offset based on the claimant's company tax rate, and a $4 million per annum cap on cash refunds from the refundable R&D tax offset.

The Academy noted concern about the potential introduction of a blanket cap on the cash refund in the ATSE Submission to Innovation and Science Australia's 2030 Strategic Plan Issues Paper[3]. ATSE supports the proposed increase of the value of the cap to $4 million but maintains its position that a blanket cap for the R&D Tax Incentive could potentially result in significant negative impacts to certain sectors, through a reduced ability to employ staff and graduates, a reduced capacity to attract investment and loss of global competitiveness. On this basis, ATSE strongly encourages the Government to monitor the data and evaluate case studies across sectors to identify any unintended negative impacts of the application of the cap.

The clinical trials exemption is a valuable amendment, which will support the Australian clinical trials service industry. The definition of trials could also mention specifically medical devices, a growing and important industry in Australia with several notable successes, such as Resmed and Cochlear.

Monitoring impacts

The proposed changes including the new intensity calculation have the potential to negatively impact Australia's pre-profit and high research intensity businesses, including biotechnology, medical device and small innovative engineering companies. The Australian Bureau of Statistics must be appropriately resourced to adequately monitor and report on the impacts of the changes to business R&D activity through its surveys, as well as Australia's overall Business Expenditure on R&D.

[3] ATSE (2017), *Submission to the Innovation and Science Australia's 2030 Strategic Plan Issues Paper* https://www atse.org.au/Documents/submissions/isa-2030-strategic-plan-issues-paper.pdf

Maintaining certainty

Stability through long-term consistency will be the key to the success of the Incentive. This can be achieved with an effective and coherent set of policies with long-term bipartisan support along with a range of other measures. Most leading practice countries have well-resourced and coordinated innovation strategies, which provide a reference point to guide the selection of policy and program options"[4]. The Australia 2030 roadmap developed by ISA[5] provides this for Australia.

[4] ACOLA (2015) *Translating research for economic and social benefit: country comparisons*

[5] Innovation and Science Australia (2017) *Australia 2030: prosperity through innovation*, Australian Government, Canberra.