

The New ■ ■ ■ Research & Development Tax Incentive

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What we will cover



- Summary of key changes
- Level of support
- Eligibility criteria
- R&D expenditure
- Adjustments
- Application process
- Planning and key dates

New legislation



- New legislation introduced on the 24th August to apply to new and existing R&D activities from 1 July 2011
- Transitional rules for expenditure incurred prior to start date

Summary of key changes



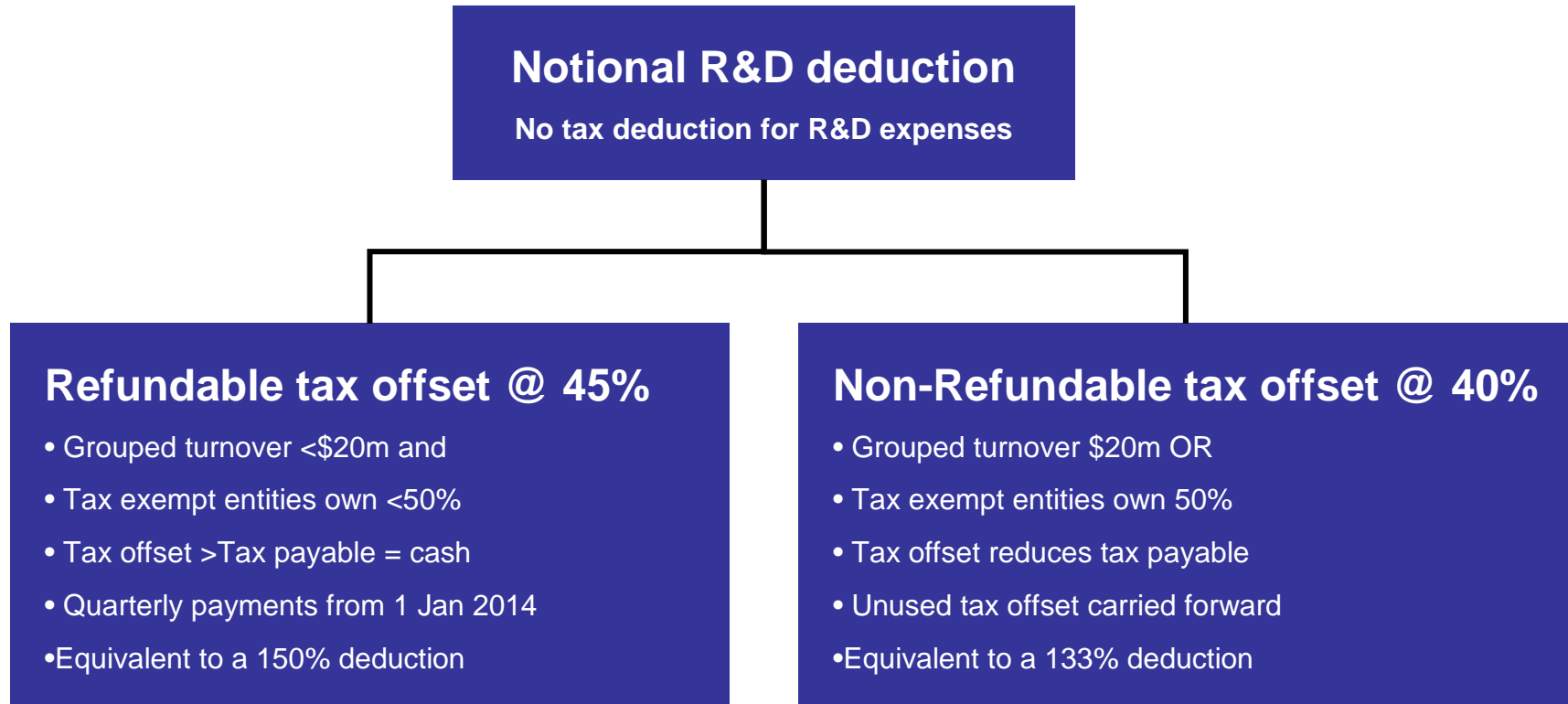
- Different tax treatment for R&D expenditure
 - Notional deductions & tax offset
- Increased level of support
 - Greater incentives
 - Quarterly cash payments
 - Overseas activities
- Changes to who can apply
 - Foreign companies

Summary of key changes



- New definition of eligible R&D activities
 - Core & supporting
- New findings process to confirm eligibility of R&D activities
- Changes to what is included in R&D expenditure
 - Payments to associates
 - Core technology
- Changes to application process and record keeping requirements

Level of support



Level of support – comparison



	Old rules R&D tax concession	New rules R&D tax incentive
	Cash Rebate	Refundable Offset
- Amount	37.5% of R&D expenditure (30% x 125%)	45% of R&D expenditure
- Eligibility	Grouped expenditure < \$2m Grouped turnover < \$5m Tax exempt entities own < 25%	No limit Grouped turnover < \$20m Tax exempt entities own < 50%
	Company in tax loss	Tax offset > tax payable

Level of support – example



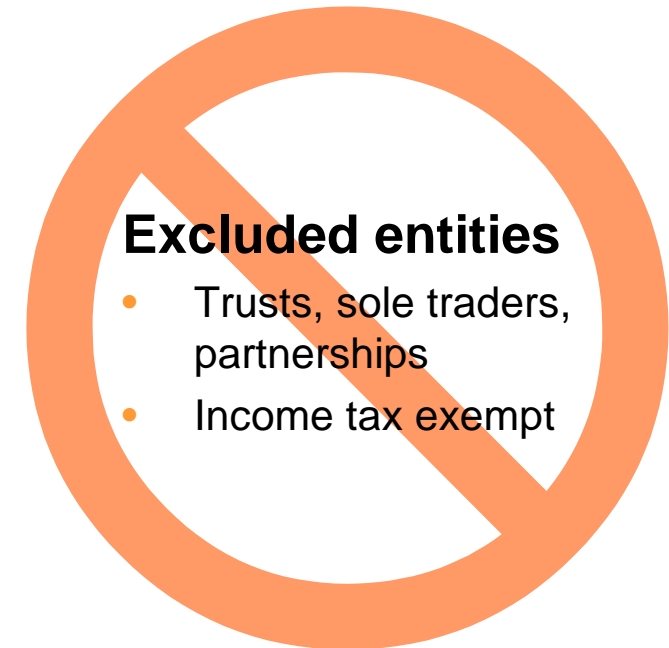
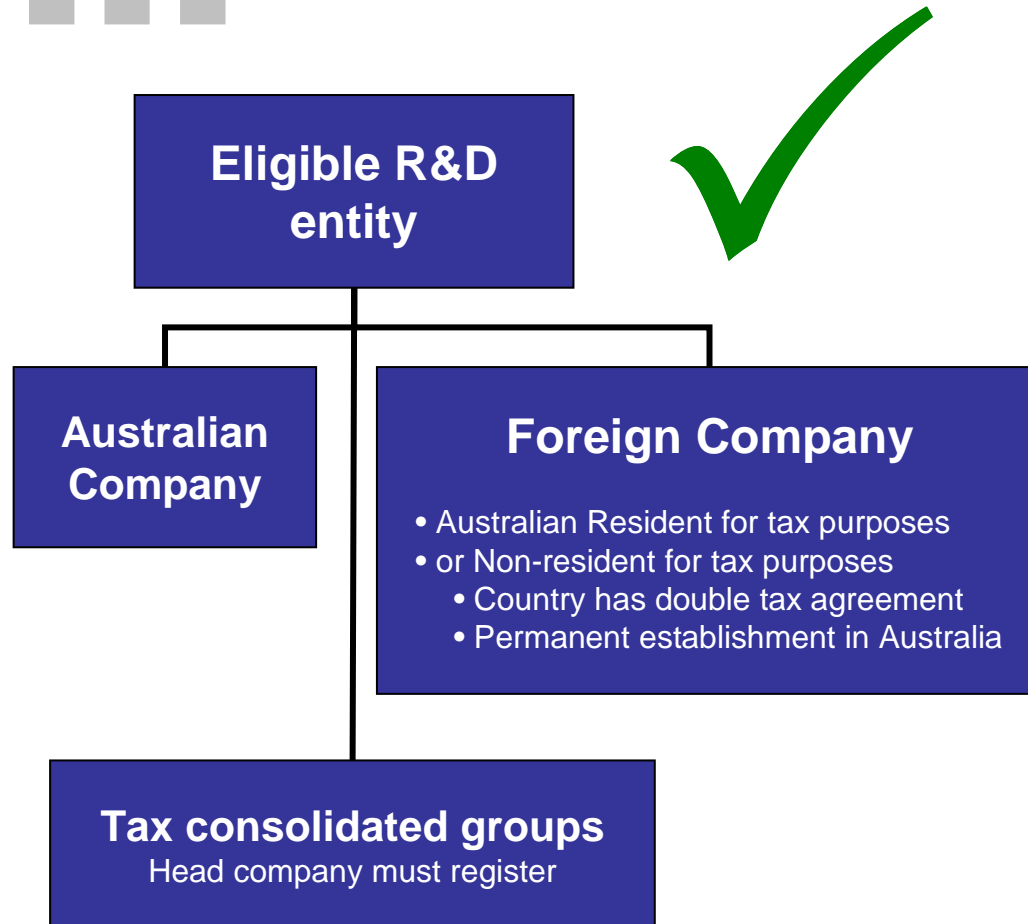
	Old rules R&D tax concession	New rules R&D tax incentive
R&D expenditure	\$1,500,000	\$1,500,000
Tax savings		
- Company tax saving	\$112,500 (7.5%)	\$225,000 (15%) / \$150,000 (10%)
- Effective deduction	\$1,875,000 (125%)	\$2,250,000 (150%) / \$2,000,000 (133%)
Cash received		
- Amount	\$562,500 (37.5%)	\$675,000 (45%)

Eligibility criteria

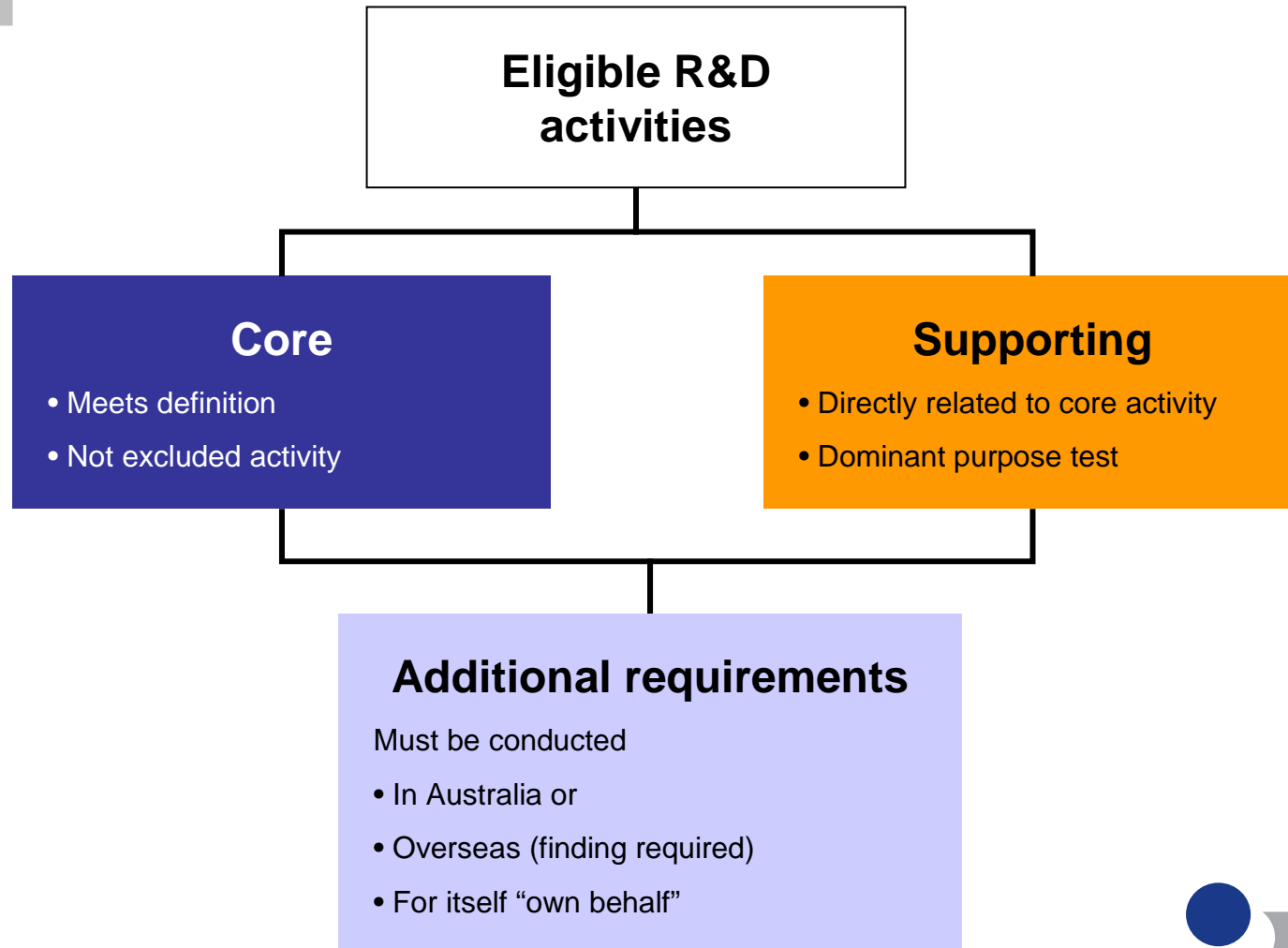


- Eligible R&D entity
- Carry on eligible R&D activities for own behalf
- Minimum level of R&D expenditure = \$20,000

Eligible R&D entities



Eligible R&D activities



Core activities



- Core Activities = Experimental Activities
- Must meet the following tests
 - Outcome could not be known in advance (knowledge gap)
 - Carried out using the scientific basis and method
 - Hypothesis>Experiment>Observation>Evaluation>Conclusion
 - Purpose to generate new knowledge
 - Improved materials
 - Products
 - Devices
 - Processes
 - Services

Excluded core activities



- ✘ The following activities are specifically excluded:
 - ✘ Market research, market testing etc
 - ✘ Prospecting, exploring or drilling for minerals or petroleum
 - ✘ Management studies or efficiency surveys
 - ✘ Research in social sciences, arts or humanities
 - ✘ Patenting, licensing etc
 - ✘ Complying with statutory requirements or standards
 - ✘ Reproduction of a commercial product or process
 - ✘ Software for the dominant purpose of use by the entity or related entities for their internal administration

Supporting activities



- Must be directly related to core R&D activity
- Subject to the dominant purpose test where:
 - Specifically excluded core activity; or
 - Produces or is directly related to producing goods or services

Eligible activities - example



- Examples in Explanatory Memorandum to new legislation
 - <http://law.ato.gov.au/atolaw/view.htm?DocID=NEM%2FEM201018%2FNAT%2FATO%2F00004>
- Core activities
 - Experimental activities actually undertaken during testing process
- Supporting activities
 - Attending a conference for preliminary research
 - Researching methods to conduct experiments
 - Manufacturing and preparing test batches
 - Setting up a production line to conduct experiments
 - Constructing apparatus to capture and record results
 - Developing a computer model to interpret results

Eligible activities cont.



- ATO to provide industry specific examples on eligible activities
- AusIndustry findings will confirm or deny
 - Voluntary
 - Overseas
 - Audit activity

Overseas activities



- Must lodge application for finding within first income year R&D activities are conducted
- Key tests:
 - Eligible as core or supporting
 - Significant link to one or more core activities in Australia
 - Activities could not be conducted in Australia
 - Facilities, expertise or equipment
 - Contravene quarantine law
 - Population (of living things)
 - Geographical or geological feature
 - Total spend on eligible overseas activities < total spend on eligible Australian activities in all income years

“Own behalf” rule



- R&D activities must be conducted for the entities own behalf
- Key tests:
 - Who owns
 - Who controls
 - Who bears the financial risk
- Exceptions:
 - R&D activities conducted in Australia under a written agreement
 - For related foreign tax resident (DTA), or
 - By foreign company through permanent establishment

Eligible R&D expenditure



- ✓ Relates to eligible, registered R&D activities
 - salary and wages, contractors, travel, overheads etc
 - Depreciation and balancing adjustments
 - Apportionment applies
- ✓ R&D partnership share
- ✓ Cash contributions to Co-operative Research Centre (CRC)

Eligible R&D expenditure - special rules



- Expenditure incurred and paid to associates
 - Only claimable when paid
 - Can elect to claim under normal tax rules
- Claim for Overseas expenditure limited to claim for Australian expenditure

Excluded R&D expenditure



- × The following types of expenditure are specifically excluded:
 - × Incurred to acquire or renovate a building
 - × Cost of depreciable plant and equipment
 - × Depreciation can be claimed
 - × Interest expense
 - × Incurred on acquiring core technology
 - × transitional rules
 - × Expenditure not at risk ie “own behalf rule”
 - × Exceptions re IP owned offshore

R&D adjustments



- Tax adjustments are required for the following types of R&D expenditure:
 - Clawback for grants received for R&D activities
 - Feedstock adjustments

R&D adjustments



- Clawback rules for grants received
 - Extra income tax @ 10% of the grant relating to eligible R&D expenditure
 - Implications
 - 45% refundable tax offset
 - Cash benefit reduces from 45% to 35% (if in tax losses)
 - Tax saving reduces from 15% to 5% (if profitable)
 - 40% standard tax offset
 - Tax saving reduces from 10% to 0%

R&D adjustments



- Feedstock rules for goods, materials or energy transformed or processed during R& D activities
 - Feedstock adjustment required to be included in assessable income
 - Calculated as 1/3 of the lesser of:
 - The feedstock expenditure, or
 - The feedstock revenue

Application process



Key dates



	Now	Apr 2012	May 2012	Jun 2012	July 2012	Aug 2012	Sept 2012	Oct 2012	Nov 2012	Dec 2012	Jan 2013	Feb 2013	Mar 2013	Apr 2013
Register for 2011 R&D tax concession	30.4.2012													
Apply for overseas finding	30.6.2012													
Register for 2012 R&D tax incentive					30.4.2013									

Record keeping



- Companies must keep records that sufficiently demonstrate to both AusIndustry and the ATO that:
 - They carried out eligible R&D activities;
 - They incurred eligible expenditure in relation to those activities; and
 - Their R&D activities and expenditure met all legislative requirements for eligibility under the program
- R&D plan not formally required
- ATO to provide guidance

Planning – actions items



- Determine if you are an eligible R&D entity
- Assess whether R&D activities are eligible:
 - Define your R&D projects and activities being undertaken within each project
 - Ensure activities undertaken are experimental
 - Split project activities into core vs supporting
 - Ensure activities are not specifically excluded from being core activities
 - Determine if dominant purpose test applies to supporting activities

Planning – actions items



- Request an advance finding from AusIndustry on R&D activities if unsure, forms to be released October 2011
- Request a finding on overseas activities from AusIndustry by 30 June 2012 i.e. end of current claim year. Forms to be released October 2011

Planning – actions items



- Review “Own behalf rule” for eligible activities:
 - Determine entity effectively owns and controls project
 - Document IP ownership
 - If work done for foreign associate confirm country has double tax agreement
 - Ensure written agreements are in place for activities conducted in Australia

Planning – actions items



- Review forecast grouped turnover and tax exempt entity ownership to confirm refundable tax offset can be claimed
- Analyse payments to associated entities
 - Will this create funding problems
- Ensure you maintain adequate records and evidence of conducting eligible R&D activities to substantiate your claim



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