RISK RESEARCH
INTERNATIONAL

Submission to Senate on Tax Laws Amendment (R&D) Bill 2010 and Income Tax Rates Amendment (R&D) Bill 2010
by
Risk Research International Pty Ltd , 23 May 2010

Key Issue Ignored

Debate to date has missed a major point. Nobody has remarked on the reduction of the refundable tax credit from 125% as it stands now, down to 45%[1]. This drastic cut in refundable credit will make research impossible for small research companies who are in the pre-income generating phase.

Why is this so critical? Because there are no other sources of funding for research. Neither venture capital nor banks will contemplate funding research, and inspired angels are few and far between. Individuals' personal resources go only so far, as we outline below (see Our Experience).

Does the Government Understand its Policy?

The Minister seems to have been poorly informed of the practical effect of this change:
"Small innovative firms are big winners from the new R&D Tax Credit, with greater access to cash refunds for their R&D expenditure and more generous rates of assistance." (Press release Senator the Hon Kim Carr, 13 May 2010).

The reality is quite the opposite.

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[1] See the existing policy at third para of the Fact Sheet ***("Expenditure which is eligible under the concession can be deducted at 125%, and in some cases at 175%")*** at : http://www.ausindustry.gov.au/InnovationandRandD/RandDTaxConcession/Pages/RDTaxConcession-TaxOffset-FactSheet.aspx

Not only does this change close off the only funding possibilities for "small innovative firms" dedicated to research, but it favours the larger ones which see innovation as an adjunct activity, and are less in need of support anyway. What the Minister should say is that only companies with substantial turnover up to $20m, who can afford it, will benefit henceforth.

The Dynamic Behind this Obfuscation

Why has a change so fundamental been ignored in the debate? One reason is that commentators rely on accounting firms and other financial protagonists who have little interest in innovation per se. Their main purpose is to protect the financial interests of clients. Presumably their custom lies at the big end of the eligible companies spectrum. Productive innovation is less the issue than optimising budgetary outcomes for fee-paying clients.

Roots of Innovation

Evidence from the US, consistently, is that productive innovation derives from confluence of expert individuals– motivated and expert individuals cross-fertilising is the key. Structures should therefore provide scope for these basic ingredients to come together. No facts have been provided for this new policy on where expected innovative value lies across the spectrum of companies looked at in this policy. Indeed it is probably not useful even to think in terms of company size.

At the same time we are aware, anecdotally, of exploitation of the 125% refundable tax offset in Australia by financiers with little interest in the research. But the answer to that is stronger provisions on the eligibility of the research, not scrapping the opportunity for genuine researchers. In this sense we have sympathy for the tightening of eligibility criteria in this new policy.

Our Experience

Risk Research International was set up in 2001 to research long term strategic investing and superannuation. This was a neglected and fertile area then and remains so to date, despite Australia's massive interest in it. Both my colleague, Dr Stuart Craig and and I are PhDs in the physical sciences with long experience in making productive gains at the national level through cross discipline thinking and research[2]. We are the only researchers inquiring into the business end of superannuation.

Our work has been financed by our personal cash injections. We have had no assistance whatsoever from government programs or elsewhere. We already let a patent lapse in the US because of cost (which would be minor to most). We now have a rich list of research material which can be opened up only if the existing tax credits apply.

This Policy Can Be Improved

What Australia is left with in this legislation defies logic. Is the government really aware of the upshot of what is being proposed here? The Prime Minister chairs an innovation council, yet this change will mean genuine innovator companies with little or no income, but lots of expertise and ideas, have no future in Australia. If that is what the government wants then it should say so, and give its reasons. The current portrayal is a gross misrepresentation.

We are not asking for handouts, nor for rorts to be preserved. There are parallels in government partnering with worthwhile national endeavours. Most obviously, government supporting people in higher education requires that it is repaid once income begins to flow.

More topically, the Henry treatment of mining provides for support in the early risky days of the venture, and then demands a contribution once the profits roll in. It’s surprising that the Henry Review is silent on innovation[3].

If these suggestions are too innovative we suggest simply that the refundable tax credit be on a sliding scale, starting at the current level of 125% for genuine, tightly - defined research for companies in the pre-income phase and reducing with increasing turnover of a company to around 40%.

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[2] We have previously helped the Parliament on innovation at the national level: http://www.aph.gov.au/HANSARD/joint/commttee/j2026389.pdf

[3] The pedigree of this new policy is hard to trace- statements come randomly from either the Treasury or the Industry sides of government. It appears to have had a life of its own outside of the Henry Review.