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L A W Y E R S

21 August 2001

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Our reference

DAM/MILE3010-6387208

Mr Peter Hallahan
Secretary
Senate Economics Legislation Committee
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Parliament House
CANBERRA ACT 2600

BY EMAIL

Email: economics.sen@aph.gov.au

Dear Sir

**TAXATION LAWS AMENDMENT (RESEARCH AND DEVELOPMENT)
BILL 2001**

I refer to your letter of 14 August 2001 regarding the Senate Economics Legislation Committee's inquiry into the above mentioned legislation, which invited me to make a submission to the inquiry.

I was Chair of the Innovation Summit Implementation Group (ISIG) which was established to prioritise recommendations developed by the highly successful February 2000 National Innovation Summit. The ISIG report *Innovation – Unlocking the Future* was forwarded to Government in August 2001

The recommendations of *Innovation – Unlocking the Future* were broad-ranging, covering such areas as awareness raising and skills development; stimulation of innovation and development of research capability; and turning ideas into action to enhance Australia's competitiveness.

Innovation - Unlocking the Future noted that there had been both an absolute decline in the amount of business investment in research and development (“R&D”) in Australia since the mid-1990s and a relative decline expressed as a share of GDP. It noted that Australian business expenditure on R&D (BERD) as a share of GDP was markedly lower than the OECD average (ranking seventh out of 24 OECD nations), and was falling while the average for OECD countries continued to rise.

The report expressed concern that without strong public and private sector funding for research and development, Australia was at risk that it would not be able to compete in a modern, knowledge-based economy. ISIG considered that a

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significant increase in the amount of business investment in R&D would be achieved by rewarding those who undertook additional R&D through an improved concession.

I was pleased by the way in which the Government's Innovation Statement *Backing Australia's Ability* responded to ISIG's proposed changes to the R&D Tax Concession for incremental R&D and its recommendation of a rebate for small and medium sized enterprises.

The new incentives provided for by the *Taxation Laws Amendment (Research and Development) Bill 2001* are, I believe, a direct response to the recommendations of *Innovation – Unlocking the Future* and will encourage an increase in the level of business expenditure on research and development.

175% Premium R&D Tax Concession

Innovation – Unlocking the Future proposed that the Government should raise the rate of the R&D tax concession to between 170% and 200% for the increment of research and development, over and above a threshold base. To qualify, it was recommended that companies would need to increase their level of research and development by an average of 10% (a threshold) over the identified base rate determined by, for example, their previous claim history.

I welcome the Government's decision to accept ISIG's recommendation to introduce an incremental tax concession. The 175% Premium Tax Concession proposed by the Government provides an excellent incentive to business to undertake additional investment in R&D. I note that it does not include a threshold of 10% as recommended by ISIG, and see this as a determined effort by the Government to drive business investment in R&D.

I also welcome the Government's decision to simplify the calculation required for the 175% Premium since the initial announcement in January. Replacing the research intensity model to one based on increased R&D expenditure will reduce compliance costs for companies, increase certainty for companies in planning their R&D and improve access to the Premium across the board.

In recommending the higher rate for the tax concession, ISIG recognised that companies should qualify by demonstrating an increase in their level of R&D over a base rate, possibly determined by their claim history. I consider that the Government's proposed use of a three year claim history provides a sound basis for ensuring that the premium goes to reward those companies that have increased

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their R&D. It is appropriate that firms should show a long term commitment to R&D to gain the Premium rate.

R&D Tax Rebate

Innovation – Unlocking the Future proposed that small to medium sized enterprises with a turnover of less than \$1 million and investment in R&D of less than \$1 million be able to ‘cash out’ the concession and receive a payment equivalent to the concession. I note that the Government has endorsed this recommendation and expanded access by using a turnover of \$5 million.

Through this tax rebate, the Government is providing for small companies, particularly those in tax-loss, to have access to a rebate equivalent to the value of the R&D Tax Concession. This initiative will foster the growth of innovative, small companies by providing them with timely support and will increase the cashflow of such companies when they most need it – during their initial growth phase. I particularly welcome the decision to allow companies to obtain the 175% Premium R&D Tax Concession as a rebate where eligible - giving encouragement to small firms to continue to increase their R&D effort.

I note also that the rebate, while directed towards the private sector, will in certain circumstances support increased commercialisation by firms derived from public sector research organisations. Although these organisations are not eligible to access the R&D Tax Concession, companies in which they have up to 25% shareholding (ie, spin-off companies) will be eligible for the Tax Rebate. This will encourage increasing commercialisation of public sector R&D.

Summary

Innovation - Unlocking the Future prioritised action to stimulate business investment in research and development. The proposed legislation, in particular the 175% Premium R&D Tax Concession and the R&D Tax Rebate, are significant steps in addressing the issues raised at the Innovation Summit and in the report *Innovation – Unlocking the Future*. I see the legislation as an appropriate and timely response to the concerns of business as articulated at the National Innovation Summit.

Enactment of the legislation as soon as possible will enable businesses to plan with certainty their R&D activities in the light of the proposed Premium Concession and rebate.

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Thank you for the opportunity to contribute to the inquiry.

Yours sincerely

David Miles

Partner

and former Chair

Innovation Summit Implementation Group