

Chapter 7

Administrative and transitional measures

7.1 As is presently the case, the R&D tax incentive will be jointly administered by the Commissioner of Taxation and the Department of Innovation, Industry, Science and Research (through the Innovation Australia Board).

7.2 At present, Innovation Australia (IA) is responsible for registering R&D activities of eligible R&D entities; the Commissioner is responsible for determining the concession available through the assessment process following lodgement of the company's return. These agencies will retain these responsibilities under the new arrangements.

Administration

Current arrangements

7.3 As explained in Chapter 5, accessing the existing R&D tax concession requires that an entity register with Innovation Australia. Although annual registration does not mean that an entity's R&D activities are eligible, it allows IA to monitor the activities of registered entities, on a risk assessment basis. Entities are required to self assess their eligibility although may later be subject to 'audit' by IA.¹

7.4 Innovation Australia (the Board) is an independent statutory board that assists with the current administration and oversight of Government innovation programmes delivered through the Department of Innovation, Industry, Science and Research.²

Innovation Australia also has functions relating to promoting the development and improving the efficiency and international competitiveness of Australian industry by encouraging research and development activities, innovation activities and venture capital activities.³

7.5 The Tax Concession Committee within Innovation Australia provides advice to the Board about the operations of the R&D tax concession. It is the Tax Concession Committee that is responsible for assessing the eligibility of R&D.⁴

1 AusIndustry, Guide to the R&D Tax Concession Part B – Research and Development Activities Version 4.2, July 2008, para B2–1, p. 6.

2 Mr Peter Thomas, Chair Tax Concession Committee, Innovation Australia, *Proof Committee Hansard*, 21 May 2010, p. 49.

3 Mr Peter Thomas, Chair Tax Concession Committee, Innovation Australia, *Proof Committee Hansard*, 21 May 2010, p. 49.

4 Mr Peter Thomas, Chair Tax Concession Committee, Innovation Australia, *Proof Committee Hansard*, 21 May 2010, p. 49.

Proposed arrangements

7.6 Under the new administrative framework, which will be introduced in Division III of the IR&D Act 1986, entities will continue to self-assess whether or not their activities are eligible for the offset under Division 355.⁵ A number of new requirements will however be introduced.

Registration

7.7 Under these new provisions, R&D entities will be required to seek registration of their activities with IA. Although this is an existing requirement, under the new provisions, there will be a requirement that those entities, when applying, separately identify core and supporting R&D.⁶ The Board will then be required to confirm or reject all requests for registration of an entity's activities as either 'core' or 'supporting' activities.

7.8 This aspect of the proposed registration process attracted considerable criticism from submitters who are of the view that the requirement to separately identify core and supporting activities in their application will add compliance cost and is directly opposed to the self assessment regime in which the broader tax system currently operates.

Disappointingly, claimants will still be required to document and cost core and supporting R&D activities separately on registration of their activities. This will be a heavy burden on all claimants and in particular many of the SMEs that are the focus of this new bill.⁷

...it is a major concern that the Bill allows for registrations to be rejected purely on the content of the submitted form. The registration process has been made more complicated...This is not a self assessment environment.⁸

It is not clear why the administration regime for the new R&D tax credit needs to be more strict than the normal income tax self-assessment system...This power is unlike that of the Commissioner of Taxation who accepts a company's statements in its income tax return at the time of lodgement...Innovation Australia, appear to be stepping away from a self-assessment system...the Bill appears to give greater powers to IA to unilaterally reclassify activities and reject registrations...IA is not required to make any of its decisions or findings within particular timeframes...The registration process should align with the income tax self assessment process...Under a self-assessment regime, a company should also be

5 Explanatory Memorandum, para 5.2, p. 117.

6 Explanatory Memorandum, Tax Laws Amendment (Research and Development) Bill 2010, para 5.5, p. 118.

7 Deloitte Touche Tohmatsu Ltd, *Submission 22*, p. 9.

8 Confidential Submitter, *Submission 15*, p. 4.

deemed to be registered in respect of R&D activities upon lodgement of its Application for Registration.⁹

It is reasonable to expect that the proposed changes will add complexity and require companies to invest greater internal resources to the claim process. In particular, the requirement for claimants to distinguish between these activities has the potential to discourage companies from lodging an R&D tax credit claim.¹⁰

7.9 In addition to the concerns that the new registration process moves away from the self-assessment regime was a concern that the Department does not have the industry expertise to make these judgments. When questioned as to the suitability of their staff for this role however, the Department commented that:

Our role is to apply the law to the projects that we see. The decisions we take are supported by private sector experts. That is why Innovation Australia, the statutory body, are the group that have control of the program in an administrative sense; they are private sector experts. Where we are unsure, we do two things. We use industry experts to help us. We commission them to look at the projects and give us a report and then we utilise that information in making our decisions. We also use the experts on our tax committee and on Innovation Australia to vet our decisions, because at the end of the day they make decisions under the current program.¹¹

Committee view

7.10 Having considered the evidence presented throughout the course of the inquiry, the Committee takes the view that the Department, through IA, will have the expertise, requisite knowledge and skills to make decisions regarding the registration of applicants.

7.11 The Committee notes the Department's undertaking to provide two levels of information — general guidance material (fact sheets, guidelines, etc) and public findings¹² and takes the view that the provision of such guidance material should mitigate the compliance impacts that were raised by some submitters.

Findings

7.12 In addition to the changes to registration, other amendments that will affect administration of the R&D tax incentive are being introduced. They include:

9 KPMG, *Submission 9*, pp 4 and 20.

10 NOAH Consulting, *Submission 8*, pp 3-4.

11 Dr Russell Edwards, General Manager, Department of Innovation, Industry, Science and Research, *Proof Committee Hansard*, 20 May 2010, p. 53.

12 Dr Russell Edwards, General Manager, Department of Innovation, Industry, Science and Research, *Proof Committee Hansard*, 20 May 2010, p. 50.

- (a) the Board may choose to consider an application in more detail and make a formal finding in relation to all or some of the activities mentioned in the application; an applicant's registration will be automatically varied to be consistent with a finding of the Board;
- (b) an entity may request an advance finding;
- (c) an entity wishing to claim a tax offset for activities conducted outside of Australia must apply for a finding — this is required to be an advance finding; and
- (d) the Commissioner of Taxation can ask the Board to make a finding that particular technology is or is not core technology.¹³

7.13 The subject of findings did not attract attention throughout the inquiry.

Transitional measures

7.14 The amendments set out in Schedule 2 of the bill that will introduce the new Part III of the IR&D Act 1986 will commence from 1 July 2010. The provisions they are replacing will be repealed but, as the Board will still require powers in relation to what will be the 'legacy' R&D tax concession, some provisions of Part IIIA will be preserved through transitional arrangements.¹⁴

Drafting comments

7.15 Throughout the inquiry it was contended that the explanatory memorandum and bill contained minor drafting errors. A list of the 'errors' identified is attached in Appendix 3.

Recommendation 6

7.16 The Committee notes the claim of drafting errors. The Committee notes that minor drafting errors are common when framing new legislation. The Committee does not believe that these minor errors are of sufficient magnitude to delay passage of the bill but considers it preferable that they be dealt with before the bill is enacted.

13 Explanatory Memorandum, pp 121–122.

14 Explanatory Memorandum, para 5.181, p. 155.