

TAX BULLETIN

An update publication for our clients

September 2011

Research and Development claims post 1 July 2011

Introduction

After repeated delays, the new Research and Development (“R&D”) Tax Incentive finally received Royal Assent in September 2011. The new R&D program applies from 1 July 2011 and represents the Government’s principal means of encouraging industry investment in R&D.

The new R&D Tax Incentive consists of two core components:

- A 45% refundable tax offset (equivalent to a 150% tax deduction) to eligible entities with an aggregated turnover of less than \$20 million per year; or
- A 40% non-refundable tax offset (equivalent to a 133% tax deduction) to all other eligible entities. Unused offsets may be able to be carried forward for use in future income years.

Whilst this new R&D Tax Incentive affords more generous tax benefits than the previous base 125% R&D Tax Deduction, we note that the 175% R&D Incremental Deduction previously available has also been removed.

As noted in our previous alerts, the definition of R&D activities has also been amended to provide a more targeted (ie. restricted) definition under the new R&D Tax Incentive. R&D activities are separated into two categories, being core R&D activities and supporting R&D activities.

Core R&D Activities

Core R&D activities are experimental activities:

- (a) whose outcome cannot be known in advance on the basis of current knowledge, information or experience but can only be determined by applying a systematic progression of work that:
 - i. is based on principles of established science; and
 - ii. proceeds from hypothesis to experiment, observation and evaluation, and leads to logical conclusions; and
- (b) that are conducted for the purpose of generating new knowledge (including about the creation of new or improved materials, products, devices, processes or services).

In determining whether activities are core R&D activities, claimants need to determine:

- Was an experiment (or set of related experiments) carried out?
- Could the outcome of the experiment have been known or determined in advance?
- Did the experimental activities employ the scientific method?
- Was the experiment’s purpose to generate new knowledge?



Supporting R&D Activities

Supporting activities are activities directly related to core R&D activities. A new requirement is that certain supporting activities can only qualify as R&D activities if they are undertaken for the dominant purpose of supporting core R&D activities.

No Cap

There is no upper limit on the expenditure that may be incurred by companies in order to claim the tax offset, provided the expenditure and activities meet the eligibility requirements.

Who can Claim?

The R&D Tax Incentive maintains the long-standing position that trusts are generally not eligible for tax benefits under the R&D provisions. However, the Incentive expands eligibility of entities to include not only Australian companies, but also foreign corporations which are permanent Australian taxpayers.

Documentation

Whilst R&D plans are no longer formally required under the new R&D Tax Incentive, a company's business records must be sufficient to verify the nature of the business activities, the amount of expenditure incurred on R&D activities and the relationship between the expenditure and the R&D activities.

Like the previous R&D Tax Concession, companies will be required to register annually with Innovation Australia before being able to claim the tax offset. Companies will need to register within 10 months after the end of their income year in which the R&D activity was undertaken.

AusIndustry Fact Sheets, Guides and Forms

We note that AusIndustry have already issued a number of fact sheets regarding the R&D Tax Incentive, but have not yet released the Registration Form relevant to claiming the R&D Tax Incentive. We further understand that AusIndustry is currently preparing a comprehensive Guide to the R&D Tax Incentive which will be released in draft form later this year. Should any significant detail emerge from this Guide or Registration Form, we will provide further alerts accordingly.

Until the further detailed guidance material and registration information is published by AusIndustry, we recommend that you continue to maintain your current approach to identifying, documenting and costing R&D activities.

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Further Information

The recent changes provide an opportunity for you to consider any R&D activities that you may be undertaking and to review your R&D expenditures to ensure that you not only qualify for the R&D Tax Incentives claims but that you also maximise your entitlement. We would be pleased to assist you in any part of this process.

Please ask either your regular Pitcher Partners tax contact or any of the contacts in the Pitcher Partners firms below for further details on the issues raised in this Tax Bulletin:

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