

An introduction to the R&D Tax Incentive

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What is the R&DTI?

The Research and Development Tax Incentive (R&D Tax Incentive or R&DTI) encourages research and development (R&D) activities that generate new knowledge. It is a way for the Australian Government to encourage business to invest in research and development that will benefit companies and the broader Australian economy.

Planned R&D is more likely to generate knowledge that is of benefit to the wider Australian economy, and your business is also more likely to benefit from such R&D. Yet, such research may be a risk for you and may not return a commercial benefit. The R&D Tax Incentive offers a tax offset to encourage you to conduct eligible R&D that you might not otherwise undertake.

The Department of Industry, Innovation, Science, Research and Tertiary Education (the department), on behalf of Industry Innovation and Science Australia (IISA), administers the R&D Tax Incentive with the Australian Taxation Office (ATO). AusIndustry is the Australian Government's specialist business program delivery division in the department. The R&DTI is a targeted tax offset program. It offers a refundable tax offset for R&D entities with an annual turnover under \$20 million. A non-refundable tax offset is available to R&D entities with an annual turnover of more than \$20 million. You need to have eligible R&D expenditure of \$20,000 or more to register and claim the tax offset unless you use a registered Research Service Provider (RSP) to conduct your R&D. Your activities must meet all of the requirements of the law for you to be eligible for the program.

Who is eligible apply for the R&DTI?

You need to:

- be incorporated under Australian or a foreign law
- conduct or plan to conduct one or more eligible core research and development activities
- have eligible R&D expenditure greater than \$20,000
- if your expenditure is less than \$20,000 you can still claim the tax offset by using a registered RSP to conduct your R&D.

Not available to Trusts.

What is the difference between eligible core R&D and supporting R&D activities?

There are key terms that you need to understand under the R&DTI.

Core R&D activities experimental activities are activities:

- (a) whose outcome cannot be known or determined 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 new knowledge in the form of new or improved materials, products, devices, processes or services).

Supporting R&D activities

A supporting activity is one that is directly related to core R&D activities or, for certain activities, has been undertaken for the dominant purpose of supporting core R&D activities.

Activities that must satisfy the dominant purpose requirement are those that produce - or are directly related to producing - goods or services; or are excluded from being core R&D activities.

Supporting (evidentiary) Documentation

Compliance activity by both AusIndustry and ATO is high. Therefore, complete and well-organised documentation which evidences the core and supporting activities being undertaken and which demonstrates the nexus between the activities and the expenditures being claimed is essential.

If requested, AusIndustry will require documentation which demonstrates use of the Scientific Method – the process of forming a hypothesis, and proceeding to experiment, observation, evaluation and conclusion (think high school science experiment!). It will also require evidence to demonstrate what the current state of knowledge was when the R&D activities commenced, the purpose of doing the R&D, what the new knowledge sought was and why the outcomes of the activities could not be known in advance by a competent professional.

Contemporary documents, generated at the time that the activities took place, such as R&D templates, web searches, expert opinion, experimental method/plan (DoE), data gathered, reports, spreadsheets, photos, emails, meeting minutes, contracts, drawings, simulations/modelling, plus any other documents that are generated during the R&D activities, which are archived systematically and chronologically, are therefore essential to demonstrate this.

The ATO requires documentation which demonstrates that the R&D is being undertaken by the claimant company, or on its behalf, and that expenditures incurred have a clear nexus with the R&D activities being claimed.

Where staff or contractors are being claimed, it expects to see evidence of how any time spent working on the R&D activities is recorded and what those activities were.

Documents may include written contracts and agreements, invoices which clearly reference the R&D activities, time sheets, job cards, diary entries, and any apportionment methods used (where expenditures may be jointly on R&D and non-R&D activities). Expenditures now need to be recorded at an activity, rather than project level.

What R&DTI tax offset benefits are available?

For R&D undertaken before 30 June 2021

43.5%

REFUNDABLE TAX OFFSET

for companies with annual turnover less than \$20 million

OR

38.5%

REFUNDABLE TAX OFFSET

for companies with annual turnover of \$20 million or more

For R&D activities conducted prior to 1 July 2021, if your eligible expenditure exceeds \$100 million for an income year, the tax offset is calculated using your company tax rate

New incentive benefits apply for R&D conducted from 1 July 2021. You can receive a premium on top of your corporate tax rate.

Companies with an aggregated turnover of **less than \$20 million** may receive a refundable R&D offset rate equal to your corporate tax rate plus an 18.5% premium.

OR

Companies with an aggregated turnover of **\$20 million or more** may receive a non-refundable R&D tax offset rate equal to your corporate tax rate plus an incremental premium. Premium increments are based on the intensity of your R&D expenditure as a proportion of total expenditure for the year. There are two premium increments:

- * R&D intensity up to 2% receives a tax offset equal to your company tax rate plus 8.5% premium.
- * Additional R&D intensity above 2% receives a tax offset equal to your company tax rate plus 16.5% premium.

From 1 July 2021, if your eligible expenditure exceeds \$150 million for an income year, the tax offset is calculated using your company tax rate.

What Expenditures can I claim?

Eligible R&D Expenditures can include those incurred on:

- Salaries and Wages (including Super, Payroll Tax, workers compensation)
- Contractors
- Sub-contracted work
- Payments to Research Service Providers
- Consumables used during the R&D activities
- Portion of the Depreciation of assets used during the R&D activities
- CRC Contributions
- Portion of general business overheads (internet, electricity, rent, etc.)

The R&DTI is a self-assessment program

Before you register to apply, you must decide whether your R&D activities are eligible according to the legislation.

You are responsible for ensuring your R&D activities meet legal requirements.

- Refer to the law when assessing whether your activities are eligible
- Keep records to support your claim
- AusIndustry may review your registration to educate you on eligibility and to comply with the law

What is the process and timing?

Identify R&D activities (ideally throughout the year as and when they commence).
Collect contemporary evidentiary documentation

Prepare and lodge R&D claim with AusIndustry through the myGov portal within 10 months of year end (30 April for 30 June year end)

Identify eligible R&D expenditures for each core and supporting activity

Receive R&D Registration Number from AusIndustry

Incorporate eligible R&D expenditures into income tax return – within amendment timings

ATO processes claim and any refundable monies are paid

Find out more at business.gov.au/rdti

About Jonathan Turner

Jonathan is a qualified engineer, registered tax agent and independent R&D tax advisor. Prior to forming his company in 2017, he was a tax partner at KPMG, heading up its Brisbane R&D practice. Before that he worked as an engineer in the defence, transportation and automotive industries in the UK, joining KPMG's UK R&D team in 2005. Jonathan works collaboratively with his clients to assist with the preparation and lodgement of their R&D claims and calculation of allowable expenditures, as well as helping to put in place frameworks and processes for the contemporary recording of R&D activities and assimilation of evidentiary documentation. He has experience of working across a broad range of industries, including agriculture, horticulture, software, engineering and manufacturing.

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