

Maximising your R & D Concession

Presented by Steven Jones and
Robyn Tyler

Agenda

- Introduction
- Administration;
- Eligibility;
- Eligible Expenditure;
- Special Areas;
- A few real world examples;
- Tips and Traps

Introduction

- Steve and Robyn and our quest
- Getting start ups off the ground
- 3 keys to successfully commercialising technology
- What is R & D and are there other options...a good example
- What isn't R & D and why

What are the tax savings?

- Entitlement basis;
- Utilised by Australian companies;
- The concessional rates on expenditure are:
 - 125% base rate
 - 175% premium rate
- Cash rebate for certain small companies.

Example

Tax Deduction Received

R&D Cost \$100,000 = \$125,000 Tax Deduction

Tax Saving = \$7,500

R&D Offset Received

R&D Cost \$100,000 = no tax deduction

Credit Received = up to \$37,500

Eligibility Criteria

A business must satisfy the following conditions:

- Company (or public trading trust);
- R&D Plan;
- > \$20,000 spent (except RRA);
- Must bear technical and financial risk;
- Control project and effectively own results;
- Substantiation of projects and financials;
- Exploit R&D on commercial terms to benefit the Australian economy; and

Eligibility Criteria cont.

- R&D Activities that have been undertaken must involve the following:
 - A technical problem that can not be resolved on the basis of publicly available information;
 - An original idea to solve the problem; and
 - Systematic experimentation in the form of testing or trials to resolve the technical uncertainty.

R&D Activities

- The definition of R&D is based around R&D Activities.
- Monitoring and assessment by IR&D is on the nature of activities.
- The Board considers that there are two categories of R&D activities:
 - Systematic, investigative and experimental (SIE) activities; and
 - Directly related activities.
- Eligible projects must contain at least one SIE activity.

Types of Activities

SIE Activities

- Activities overall must have the character of *systematic, investigative* and *experimental* activities;
- Key criteria that must be satisfied;
- It's important to establish that experimental activities have been undertaken with the project;

Directly Related Activities

- Directly related activities are other tasks carried on for a purpose directly relating to the core activities.

SIE Exclusions

- Legislation excludes a number of activities from being SIE, but they can be directly related activities. These include:
 - Market research, market testing and development, or sales promotion;
 - Quality control;
 - Making cosmetic modifications or stylistic changes;
 - Management studies or efficiency surveys; and
 - Conducting pre-production trials.

SIE Activities

- SIE Activities involve either innovation *or* high levels of technical risk, conducted for a purpose of:
 - Acquiring new knowledge; or
 - Creating new or improved materials, products, devices, processes or services.

Novelty or High Technical Risk

- Activities are defined by IR&D to involve innovation where:
 - An appreciable element of novelty;
 - Must be meaningful in the context of the activities undertaken and there must be some development of the technology or new use of existing technology;
 - Original thought with a wider application.

Novelty or High Technical Risk cont.

- The alternative is activities that had a high level of technical risk.
- Need to identify the technical uncertainty undertaken, the activities to resolve, and explain how it relates to knowledge and experience in the public arena.
- Company would need to show that activities undertaken followed a scientific method.

Computer Software, Multiple Sale Criteria

Software development is not considered to be an SIE activity unless it is undertaken for the purposes of multiple sale (in contrast to development solely for in-house use).

- If only experimental activities within a project are development and testing of the software, the project is considered a software development project to which the multiple sale criteria applies;
- Multiple sale is taken to include sale, rent, licence, hire or lease to two or more non-associates of the company;

R&D Plans

- Plan in place at the start of the project;
- In approved format;
- Activities considered ineligible if there is no project plan in place prior to commencement of major activities;
- Plan may refer to existing documents;
- Approval required by Board of Directors or authorised officer; and
- Update and amend as project progresses.

On own behalf

- A company can not claim a deduction for carrying on R&D on behalf of another person or entity. This restricts the R&D claim to the company that:
 - Bears the financial risk of the R&D project;
 - Has control over the R&D project; and
 - Effectively owns the R&D results.
- This does not stop a company from contracting out some or all of the company's R&D.

Overseas Expenditure

- Can be an issue.
- Limitation of overseas R&D to 10% of total project costs;
- IR&D Board certification is required in advance;
- Requires third party support for position; and
- Exception for incidental or de minimis activities.

Eligible R&D Expenditure

- Seven main categories of expenditure:
 - Salary;
 - Contracted;
 - Other R&D Expenditure;
 - Plant;
 - Feedstock;
 - Core Technology; and
 - Interest.

Salary Expenditure

- Covers expenditure incurred directly on eligible activities by way of salary, in relation to employees who are engaged directly in carrying out an eligible R&D activity, including:
 - Researchers undertaking conception and/or creation of new knowledge and products;
 - Employees undertaking technical tasks to support R&D;
 - Supervisors of researchers and technical staff.

Other R&D Expenditure

- Two classes of expenses:
 - Those that can be reasonably expected to be identified as directly related to the project.
 - Claim the cost associated with the project
 - Those that can not be clearly identified as R&D because it relates to a cost of business operations.
 - Is calculated on an apportionment basis of wages usually.
- = eligible expenses x $\frac{\text{eligible R\&D wages}}{\text{total company wages}}$

Plant & Interest

- Rates depend on acquisition date;
- Special rules surrounding prototypes;
- Does not cover leased equipment (this is captured under 'other R&D expenses');
- Plant acquired after 29/01/2001 can be apportioned between R&D and normal depreciation; and
- Depreciation on buildings is not claimable.
- Interest is claimable at 100%.

Special Issues

- Grants and Clawback;
- R&D Tax Offset;
- 175% Premium Deduction;
- Substantiation; and
- Grouping Rules.

Grants & Clawback

- Offsets the benefit of R&D Tax Concession for companies that have received a government grant (federal or state) for the same project;
- Clawback is applied on a project basis, not the entire claim;
- Clawback is twice the amount of the Grant; and
- This figure is then claimed at 100% and the balance at 125%.

Clawback Example

Company spends \$100,000 on R&D during the year and receives a \$20,000 grant.

Company Expenditure	100,000
Less clawback amount	(40,000)
Eligible expenditure	\$60,000

R&D Offset

- Forgo the tax deduction and get the cash;
- Great for startup businesses;
- Rate of cash is equal to 30% of the grossed up deduction.
- The eligibility rules include:
 - Turnover of < \$5m;
 - Aggregate R&D spend of <\$1m
 - < 25% ownership by tax exempt entity; and
 - Grouping rules to determine thresholds.

Example

	No Rebate	Rebate	Rebate
Net Profit/(Loss)	(300,000)	(300,000)	(300,000)
R&D Expenditure	250,000	250,000	450,000
R&D Tax deduction	312,500		
Taxable Income	(362,500)	(50,000)	150,000
Tax Payable (30%)	0	0	45,000
R&D Tax Offset		93,750	168,750
Cash Back	0	0	123,750

175% Premium Deduction

- Deduction of 175% for expenditure above a three year rolling average;
- Can not be claimed by company until year four;
- This is affected by grouping rules; and
- Adjustments occur where R&D falls more than 20% between 2 years.

Grouping

- Grouping applies to R&D Offset and 175% premium; and
- Looks at the relationships between related entities (such as trusts, companies, partnerships and individuals).

Substantiation

- Must have contemporaneous records of:
 - Activities; and
 - Expenditure.
- Declaration by authorised officer of contemporaneous records.
 - Eg Payroll records, plants, minutes, diaries.

Proposed Changes to R&D

- To be effective from 1 July 2010
- 45% refundable credit to small companies
- Narrower definition of R&D
- Additional excluded activities
- Qualify activities as core or supporting
- Four year amendment period

Top Ten Tips

1. Use a specialist accountant and advisor
2. Make sure the cost benefit stacks up in making the claim
3. Register early with AusIndustry
4. Keep timesheets for all people involved with project
5. Track holidays and leave for everyone

Top Ten Tips cont.

6. Track specific expenditure for projects
7. Look to maximise wages for owners (being cash effective)
8. Pay superannuation on time
9. Identify specific assets being used for R&D
10. Ensure all business costs are in company financials

Bonus Tip!

What is most important is developing a product the market will buy, bringing it to market on time and on budget, and surviving the cash flow hurdles. R & D is only one small element in this.

srj.ascenta.com.au

