Australian Government
Department of Industry, Science, Energy and Resources

Australian Government
Australian Taxation Office

# R&DTI – Review of the dual-agency administration model

September 2021

**Department of Industry, Science, Energy and Resources and the Australian Taxation Office**

**Joint submission**

# Contents

# Executive summary

The Department of Industry, Science, Energy and Resources (DISER) and the Australian Taxation Office (ATO) welcome the opportunity to provide a joint submission to this review.

The Research and Development Tax Incentive (R&DTI) is one of the Government's most important industry innovation policies. At heart, these policies are premised on extensive national and international research demonstrating that the social benefits from business R&D are greater than the benefits to individual businesses. The benefits of R&D spillover into the broader economy through ideas, skills and knowledge transfer, and play an important role in Australia's technological progress and economic growth.

Policy support for research and development (R&D) was first introduced in Australia in 1985. To focus support on genuine R&D, the policy included a clear definition and enhanced administration, including the involvement of the Industry Department to provide contemporaneous public guidance, and greater certainty through a (then) new system of advanced findings. The dual-agency delivery model was designed to bring together the knowledge, expertise and innovation measures delivered by the Industry Department, with the efficiency, effectiveness and familiarity of the taxation system. This design ensures compliance costs for business are kept relatively low, particularly when compared to direct policy support in the form of grants.

Australian businesses invest in a wide range of innovative activities, and encounter diverse challenges in their R&D and innovation journeys. Through the R&DTI, the Government encourages companies to invest in R&D activities that are less likely to be undertaken without government support and most likely to deliver benefits to the broader Australian economy. DISER also delivers a suite of complementary policy measures to support business at all stages of the business life cycle.

Since its inception in 2011-12, the R&DTI has experienced growth in the number of registered participants, and the subsequent value of tax benefits delivered. The total annual cost of the program to the Government in the form of revenue forgone and refunds exceeds $2.5 billion. The program has delivered benefits to over 11,000 businesses each year.

The focus of both DISER and the ATO is to deliver the R&DTI as efficiently and effectively as possible while maintaining the integrity of the program.

Due to its importance to business, the R&DTI has been extensively studied and reviewed, including this year by the Australian National Audit Office (ANAO). Both agencies have welcomed the opportunity to engage with the ANAO through the audit, and look forward to seeing the findings of its report when it is tabled in Parliament later this year.

The program has been significantly reformed over the past three years, including through the adoption of DISER's new Integrity Framework, refreshed guidance, a new customer portal, and joint DISER-ATO communication protocols on compliance matters. Additional reforms are in the pipeline, including further updates to both DISER and ATO systems and further targeted guidance material.

The joint administration model has been in place for many years now and appears to be working well. Strong governance structures ensure a shared understanding of program objectives, clear assignment of responsibilities, and longstanding commitment to continuous improvement. The stability of the joint administration model provides beneficial outcomes for business and the economy.

DISER and the ATO will continue to assist the Board of Taxation with its review of the dual-agency administration of the R&DTI. Both agencies look forward to seeing the findings of this review, and any insights or suggestions for improvement the Board might wish to convey in its final report.

# 1 R&DTI policy context

**Key points**

* The R&DTI is a broad based, demand driven entitlement program delivered through the tax system. It is accessible by companies of all sizes across all industry sectors, comprising over one third of all support for R&D, and over 95 per cent of all support for business R&D, as the Australian Government's largest innovation support measure.
* The R&DTI has provided over 11,000 businesses with over $2.5 billion in tax offsets each year.
* Enhanced reforms to the R&DTI were introduced for income years commencing on or after 1 July 2021. For these income years, for eligible annual R&D expenditure up to $150 million, the R&DTI provides a refundable offset for SMEs of 18.5 per cent above the company tax rate, and a tiered non-refundable offset 8.5 per cent or 16.5 per cent above the company tax rate for large companies dependent on their R&D intensity.
* The R&DTI is part of a suite of Government programs supporting science, research and innovation.

## 1.1 Why does the Government support business R&D investment?

Innovation is recognised as a key driver of productivity and long-term growth. It is also instrumental in responding to societal and economic challenges, including those posed by the COVID-19 pandemic. Due to various failures in the market for R&D, in the absence of government intervention, businesses are likely to underinvest in R&D relative to the socially optimal level.[1] Many R&D activities may not be profitable for an individual company, but their outcomes may deliver wider benefits to society and the economy. It is in the interests of governments to take steps to encourage businesses to undertake these activities.

Governments in OECD countries predominantly rely on expenditure based R&D tax incentives, which represent around 55 per cent of total OECD government support for business R&D. Compared with more direct forms of support, like grants, expenditure-based tax incentives are generally market-driven and broad-based (rather than selective), and less costly to administer.[2]

Like other expenditure-based R&D tax incentives, the R&DTI increases post-tax returns on expenditure on more marginal R&D activities in which investment would otherwise be sub-optimal. This reduces the cost of undertaking those activities and incentivises additional investment.

## 1.2 How the R&DTI works

The R&DTI is a broad-based, demand-driven entitlement program jointly administered by DISER and the ATO. It is delivered through the tax system and is accessible by companies of all sizes across all industry sectors. Comprising over one third of all support for R&D, and over 95 per cent of all support for business R&D, the R&DTI is the Government's largest innovation support measure.[3] It is focussed on encouraging

[1] OECD, Corporate effective tax rates: the case of expenditure-based R&D tax incentives, July 2021.
[2] OECD, Corporate effective tax rates: the case of expenditure-based R&D tax incentives, July 2021.
[3] SRI Budget Tables: https://www.industry.gov.au/data-and-publications/science-research-and-innovation-sri-budget-tables.

businesses to spend more on R&D to generate spillover benefits for the broader Australian economy by providing over 11,000 businesses with over $2.5 billion in tax offsets on up to $100 million in eligible R&D expenditure each year.[4]

Core R&D activities are experimental activities:

- whose outcome cannot be known or determined in advance (and which can only be determined by following a systematic progression of work, from hypothesis to conclusion consistent with principles of established science), and
- which are undertaken to generate new knowledge.

Supporting R&D activities are those activities directly related or, in particular circumstances, undertaken for the dominant purpose of supporting core R&D activities.

Both core and supporting activities are eligible.

Under the program, eligible companies forgo the normal tax deduction for business expenses at the company tax rate in favour of an R&D tax offset. The offset is refundable for small and medium enterprises (SMEs) with an aggregated turnover of less than $20 million, and non-refundable for large businesses with an aggregated turnover of $20 million or more. This means that, where the tax offset exceeds tax liabilities, an SME can take the difference as a cash refund, whereas a large business must carry forward the difference to the next income year. Typically, SMEs comprise over 80 per cent of registrants under the program, are responsible for around half of registered expenditure, and receive most of the benefits each year through tax offsets.

## 1.3 How the R&DTI fits into the broader suite of industry innovation programs

Australian businesses invest in a wide range of innovative activities and encounter diverse challenges in their R&D and innovation journeys. The Australian Government provides numerous programs that help businesses rise above these challenges, incentivising and enabling them to develop their ideas from early-stage research through commercialisation to technology adoption and knowledge transfer.

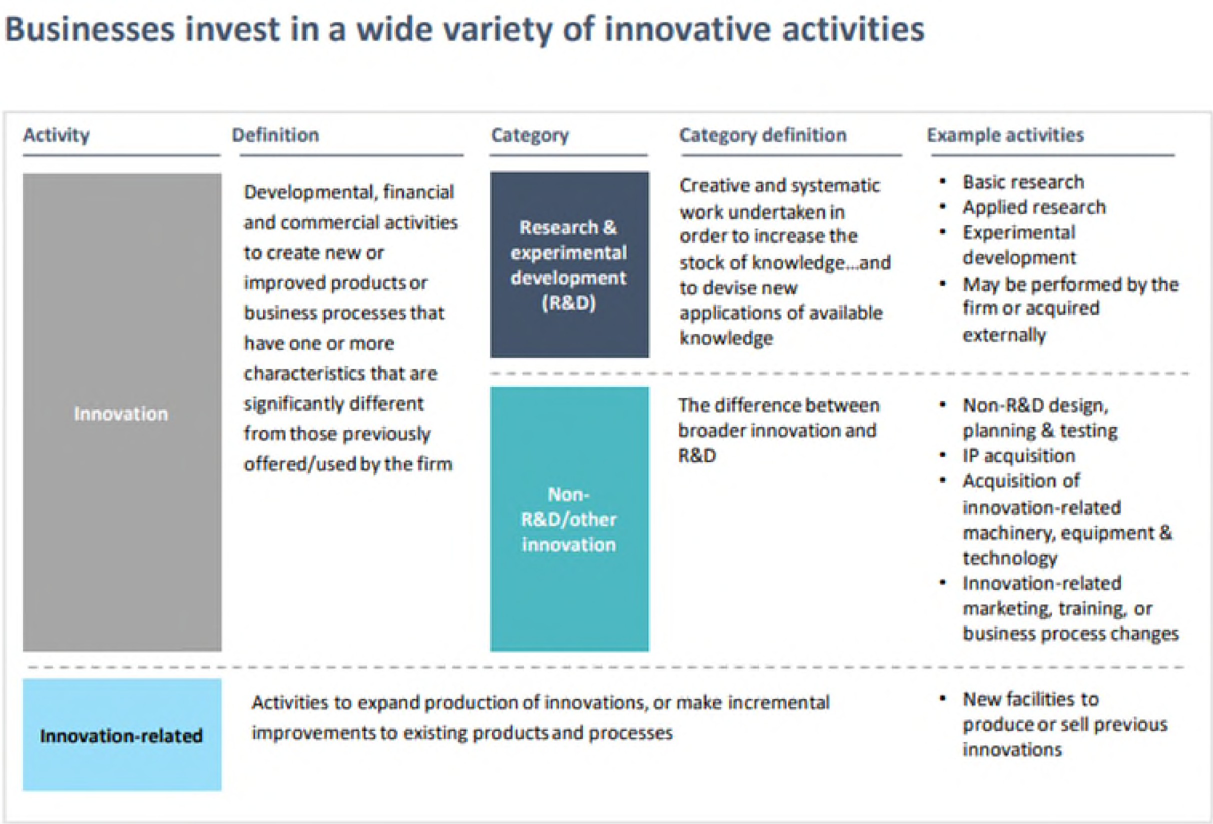
The R&DTI is broad-based and directed at companies that conduct scientific and technological R&D activities with unknown outcomes to benefit society and the broader economy.

Other programs also support the R&D and innovation ecosystem by providing expertise, funds or capital to:

- support basic, applied and experimental R&D (CSIRO Kickstart, Entrepreneurs' Programme – Innovation Connections, Business Research and Innovation Initiative, Cooperative Research Centres)
- progress ideas and initiatives (Early Stage Venture Capital Limited Partnerships, Early Stage Innovation Companies, The Biomedical Translation Fund, CSIRO Access to high tech prototyping and production facilities, Industry Growth Centres)
- develop sectors and platform technology (Medical Research Future Fund or the Modern Manufacturing Initiative)
- support entrepreneurs, businesses and researchers with business advisory and research collaborative services (Entrepreneurs' Programme – Accelerating Commercialisation, Cooperative Research Centres).

[4] SRI Budget Tables: https://www.industry.gov.au/data-and-publications/science-research-and-innovation-sri-budget-tables.

The types of innovative activities in which businesses invest is captured in OECD Diagram 1.1 below. This diagram shows that R&D is critical to the development of the new knowledge that underpins new-to-world rather than incremental, design or marketing innovation.



Businesses invest in a wide variety of innovative activities

| Activity | Definition | Category | Category definition | Example activities |
|---|---|---|---|---|
| Innovation | Developmental, financial and commercial activities to create new or improved products or business processes that have one or more characteristics that are significantly different from those previously offered/used by the firm | Research & experimental development (R&D) | Creative and systematic work undertaken in order to increase the stock of knowledge...and to devise new applications of available knowledge | • Basic research<br>• Applied research<br>• Experimental development<br>• May be performed by the firm or acquired externally |
| | | Non-R&D/other innovation | The difference between broader innovation and R&D | • Non-R&D design, planning & testing<br>• IP acquisition<br>• Acquisition of innovation-related machinery, equipment & technology<br>• Innovation-related marketing, training, or business process changes |
| Innovation-related | Activities to expand production of innovations, or make incremental improvements to existing products and processes | | | • New facilities to produce or sell previous innovations |

**Diagram 1.1 Types of innovative activities businesses invest in**[5]

## 1.4 How R&DTI has changed over time

The R&D Tax Concession was reviewed and modified a number of times before it was replaced by the R&DTI in 2011.

In comparison to the concession, the R&DTI provides more generous benefits for expenditure on a narrower range of R&D activities. It focussed support towards SME's on the grounds that those businesses have been found to be more incentivised by tax measures to invest in additional R&D.[6] The R&DTI is also better focussed on activities considered less likely to be done by companies in the absence of a financial incentive, and more likely to deliver spillover benefits to the economy.

Initially, the tax offset rates under the R&DTI were set at: 40 per cent (large companies), equivalent to a 133 per cent enhanced deduction; and 45 per cent (SMEs) equivalent to a 150 per cent enhanced deduction. A minimum R&D expenditure threshold of $20,000 was set for the refundable element, which can be waived if an SME engages with a Research Service Provider registered under the program.

In 2015 a $100 million annual R&D expenditure threshold was introduced. For R&D expenditure in excess of this threshold, companies receive a tax offset at the prevailing corporate tax rate, rather than the more generous R&DTI rate.

[5] OECD (2015) Frascati Manual. 2. OECD (2018) Oslo Manual.
[6] 2016 Review, OECD MicroBeRD.

In 2016 tax offset rates were reduced by 1.5 percentage points, to 38.5 per cent (large companies) and 43.5 per cent (SMEs). Therefore for income years commencing between 1 July 2016 and 30 June 2021, for eligible R&D expenditure up to $100 million in each income year, the R&DTI provided:

- for eligible companies with an aggregated turnover of less than $20 million per annum – a 43.5 per cent refundable tax offset
- for eligible companies with an aggregated turnover of $20 million or more per annum – a non-refundable 38.5 per cent tax offset.

Enhanced reforms to the R&DTI were introduced for income years commencing on or after 1 July 2021. For these income years, for eligible annual R&D expenditure up to $150 million, the R&DTI will provide:

- for eligible companies with an aggregated turnover of less than $20 million per annum – a refundable tax offset of 18.5 per cent above the 25 per cent tax rate
- for eligible companies with an aggregated turnover of $20 million or more per annum – a two-tiered non-refundable tax offset, depending on a company's R&D intensity[7]
    - a tax offset of 8.5 per cent above a company's prevailing tax rate (25 or 30 per cent) for expenditure up to 2 per cent R&D intensity
    - a tax offset of 16.5 per cent above a company's prevailing tax rate (25 or 30 per cent) for expenditure above 2 per cent.

## 1.5 The cost to government of the R&DTI

The R&DTI cost to the Government is reported annually, typically in September/October, in the Science, Research and Innovation (SRI) Budget Tables.[8] The most recently published SRI Budget Tables (Table 1.2) show the following cost ($ million) of the R&DTI:

**Table 1.2 SRI Budget Tables**

| Financial Year | 11-12 | 12-13 | 13-14 | 14-15 | 15-16 | 16-17 | 17-18 | 18-19 | 19-20 | 20-21 | 21-22 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| R&DTI – Refundable | 1,502 | 1,703 | 1,868 | 1,992 | 2,092 | 2,003 | 1,894 | 1,848 | 2,026 | 1,999 | 2,067 |
| R&DTI – Non-refundable | 1,070 | 1,160 | 970 | 810 | 730 | 630 | 560 | 570 | 570 | 570 | 680 |
| **R&DTI – Total** (CP*) | **2,572** | **2,863** | **2,838** | **2,802** | **2,822** | **2,633** | **2,454** | **2,418** | **2,596** | **2,569** | **2,747** |
| **R&DTI – Total** (IA*) | **2,928** | **3,199** | **3,174** | **3,090** | **3,129** | **2,935** | **2,638** | **2,551** | **2,648** | **2,569** | **2,740** |

*CP is current prices, IA is Inflation Adjusted using the GDP Deflator

The R&DTI figures reported in the SRI Budget Tables vary each year due to policy changes, amended assessments, and economic shifts/disruptions that impact R&D activities and tax receipts. Chart 1.1 depicts changes in actual and forecast R&DTI costs set out in the SRI Budget Tables over multiple years. Notwithstanding major changes in forecasts over the years shown in Chart 1.1, the program's cost to Government has remained relatively steady, particularly since the 2018-19 Budget announcement, ranging between $2.5 billion and $2.8 billion per annum (inflation adjusted), as shown in Table 1.2.

[7] R&D expenditure as a proportion of total expenditure.
[8] While a number of other Government publications, including Budget Paper 1 and the Treasury Tax Benchmarks and Variations Statement, provide information on R&DTI receipts or costs, the SRI Budget Tables provide the most comprehensive source of information on the cost of the program to Government. As they also include the costs to Government of other SRI programs over time, the SRI Budget Tables also facilitate the comparative assessment of Government outlays in support of scientific endeavour, R&D and innovation.

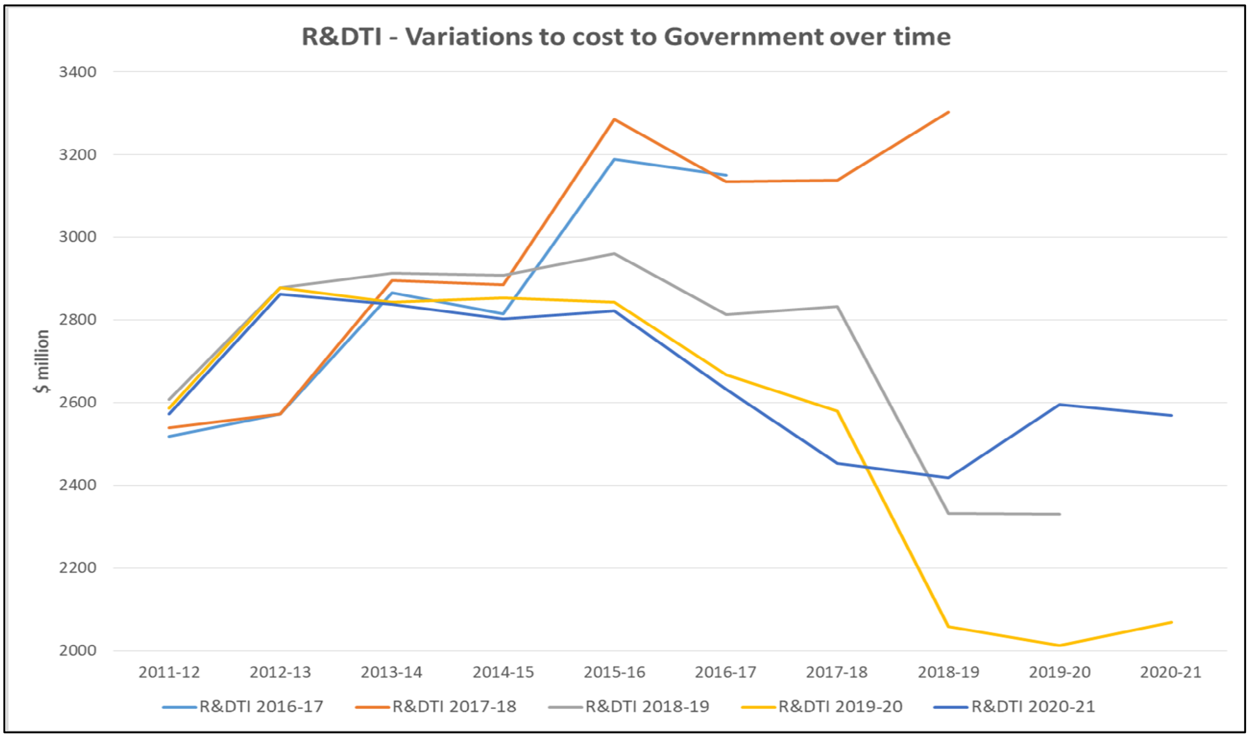



**Chart 1.1 Changes in actual and forecast R&DTI costs**

# 2 Benefits of dual-agency expertise

**Key points**

The dual-agency administration of the program draws on the distinct expertise and authority of both agencies to deliver:

- an industry innovation entitlement program
  - aimed at delivering broader benefits to society and the economy
    - by incentivising Australian companies to perform more R&D
      - through the tax system
        - while protecting national revenue.

## 2.1 Two step process

As the R&DTI leverages the taxation system to deliver an innovation policy, responsibility for policy oversight is shared between DISER and the Department of the Treasury. Similarly, responsibility for program administration is shared between DISER, on behalf of Industry Innovation and Science Australia (IISA), and the ATO.

IISA is a statutory Board established under the (IR&D Act), reporting to the Minister for Industry, Science and Technology. The Minister has established a number of committees to advise the IISA Board, including the R&D Incentives Committee (R&DIC), to which the IISA Board has delegated its R&DTI decision-making responsibilities.[9] DISER supports IISA and the R&DIC in the administration of the program.

The joint administration model allows IISA and DISER, and the ATO to combine the knowledge and expertise of each agency to deliver the R&DTI.

There is two-stage process for companies to access the R&DTI.

1. Firstly, within 10 months of the end of a given income year, a company must self-assess and register their eligible R&D activities conducted within that income year with DISER. Once businesses have registered their activities, a registration number is issued. This registration number is used when applying for the tax offset from the ATO.
2. Secondly, once registered, the company submits an R&D expenditure schedule as part of its company tax return identifying expenditure incurred on R&D activities, and the R&DTI offset is applied by the ATO.

Note: The purpose of registration within 10 months of conducting activities is to ensure that Government support is going to activities that are less likely to have been conducted in the absence of the R&DTI. The underlying rationale is that companies will plan R&D activities, and the availability of the R&DTI for those future activities, will improve the underlying investment case for undertaking them.

[9] https://www.industry.gov.au/sites/default/files/May%202018/document/pdf/research-and-development-tax-incentive-review-report.pdf?acsf_files_redirect, Review of the R&D Tax Incentive, 4 April 2016, page 6.

On behalf of IISA, DISER is responsible for registering R&D activities and Research Service Providers, and managing program integrity through the provision of guidance materials and education, and the conduct of compliance activities. DISER is also responsible for advising or making advance and overseas findings on R&D activities for specific R&D entities and, from 1 January 2021, making public determinations.

DISER has significant expertise in delivering policies and programs to support Australian businesses through an Australia-wide network of program and delivery experts. These experts have a deep understanding of business needs to invest in new technologies to innovate and grow. They match businesses with government support including program information, referrals to business advisors, grants and regional outreach. This expertise is important to successful administration of the R&DTI, which supports over 11,000 businesses each year.

The ATO is the Australian Government's principal revenue collection agency, and administers the tax, excise and superannuation systems that fund services for Australians. Therefore the ATO is best placed to administer claims for R&DTI tax offsets. The ATO is responsible for determining whether the claimant is an R&D entity, and whether expenditure incurred on, or assets used for R&D activities are eligible for the tax offset. The ATO also provides advice (including private binding rulings) and undertakes compliance activities.

DISER and the ATO recognise that a vibrant economy based on innovation is critical to Australia's future and to our global competitiveness, and that business R&D plays a key role in promoting innovation. Both agencies work together closely to ensure these outcomes are achieved, recognising that a balanced approach to administration must be taken to safeguard the integrity of the program.

## 2.2 Governance arrangements

While DISER and the ATO have distinct roles in the administration of the program as set out in legislation, the joint administration model has allowed increasing alignment in approaches and activities to support end-to-end program delivery and integrity assurance.

The joint administration model is underpinned by a robust governance and administration framework documented in a Memorandum of Understanding and Services Schedule (MoU). The MoU supports DISER and the ATO's strategic objectives, which include maintaining and improving program integrity, minimising the compliance burden on participants and supporting an effective joint delivery model between the two agencies. The MoU allows for the sharing of information to:

- provide assistance to the other agency in relation to their respective roles in administering the program
- consult industry and share information, as necessary, to better understand concerns and views of companies
- undertake joint risk assessments and take appropriate measures to address risks related to the program as a whole
- explore opportunities to jointly improve compliance through increased client engagement and relationship management
- bring to the other agency's attention any matters that are likely to have risk management implications to the program's administration.

Since the program's introduction, there has been close collaboration in relation to data sharing, compliance and risk analysis, as well as collaboration on guidance, education and communication products. Three key governance groups have been established for the delivery of the joint administration, summarised in Table 2.1 below.

**Table 2.1 Governance of the R&DTI**

| Group Name | Level | Role |
|---|---|---|
| Joint Operations Group (**JOG**) | Senior Executive | Oversees joint administration and risk setting |
| Joint Administrative Governance Group (**JAGG**) | Senior Managers | Strategic direction and assurance |
| Joint Management Group (**JMG**) | Operational Managers | Implementation of joint strategies and information sharing |

The R&DTI Program Governance Structure diagram (Diagram 2.1) below illustrates the roles of these three key groups within the broader governance framework for the joint delivery of the R&DTI program.

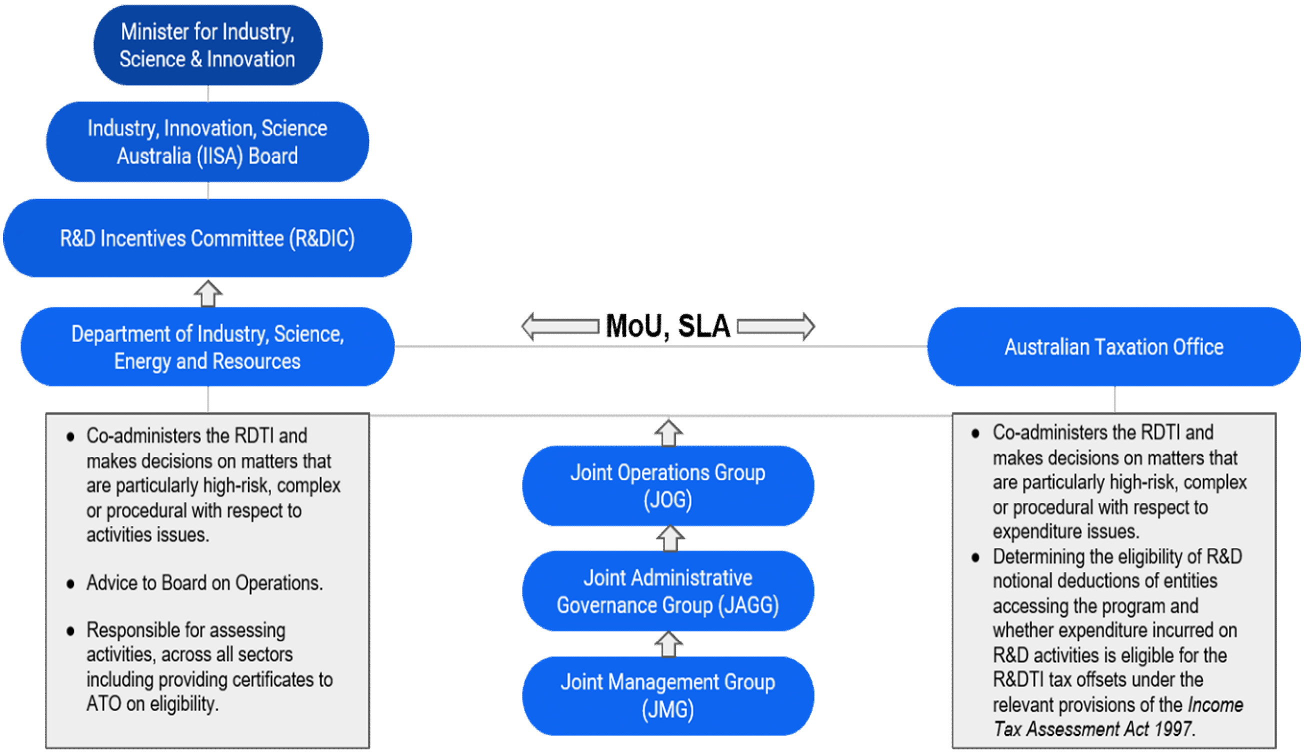



**Diagram 2.1 R&DTI Program Governance Structure**

## 2.3 Combined agency intelligence

Joint administration allows for the identification of broad risk factors under the program. By combining approaches to identifying and addressing risks, the ability to uphold the integrity of the program is a particular strength of this dual-agency model. Key to this are the rich datasets that each agency holds and draws from to enhance risk identification when administering the program.

However, due to the different legal frameworks under which DISER and the ATO operate, there are limitations on data and information that can be shared between the two agencies and this can impact companies. Where possible, the two agencies actively share information to ensure that all legislative requirements are met and appropriate outcomes are delivered to companies accessing the program.

For example, the ATO can profile a business based on all tax dealings the business has had with the ATO. Although specific details cannot be shared with DISER, the ATO can provide an indication of whether or not a business has triggered one or more risk indicators within the ATO that may potentially affect eligibility for the R&DTI. This allows DISER to take the risk into consideration when processing applications for registration and/or undertaking education and compliance activities.

Likewise, DISER holds data on business interactions with other programs that DISER administers, as well as past compliance activities that have occurred. DISER uses this data to assess the relative risk associated with a particular company or activity and, where warranted, share its assessment with the ATO.

This sharing of intelligence derived from large datasets allows both agencies to uphold the integrity of the program, and to effectively deliver appropriate benefits to R&D active businesses and the economy.

## 2.4 Joint administration in practice

The R&DTI program operates under a self-assessment, self-registration system.

A company self-assesses their eligibility, registers the R&D activities with DISER, and claims the R&DTI offset when it lodges its company tax return, which is also self-assessed.

The company then lodges its R&DTI claim together with its tax return with the ATO. Typically, the ATO will process a tax return and R&D schedule automatically without any manual intervention. Manual intervention may occur if an error is identified as part of the processing of the tax return or the tax return is selected for a review.

Diagram 2.2 below demonstrates the lodgement of the company registration with DISER, through to the lodgement of the company tax return and R&D schedule with the ATO.

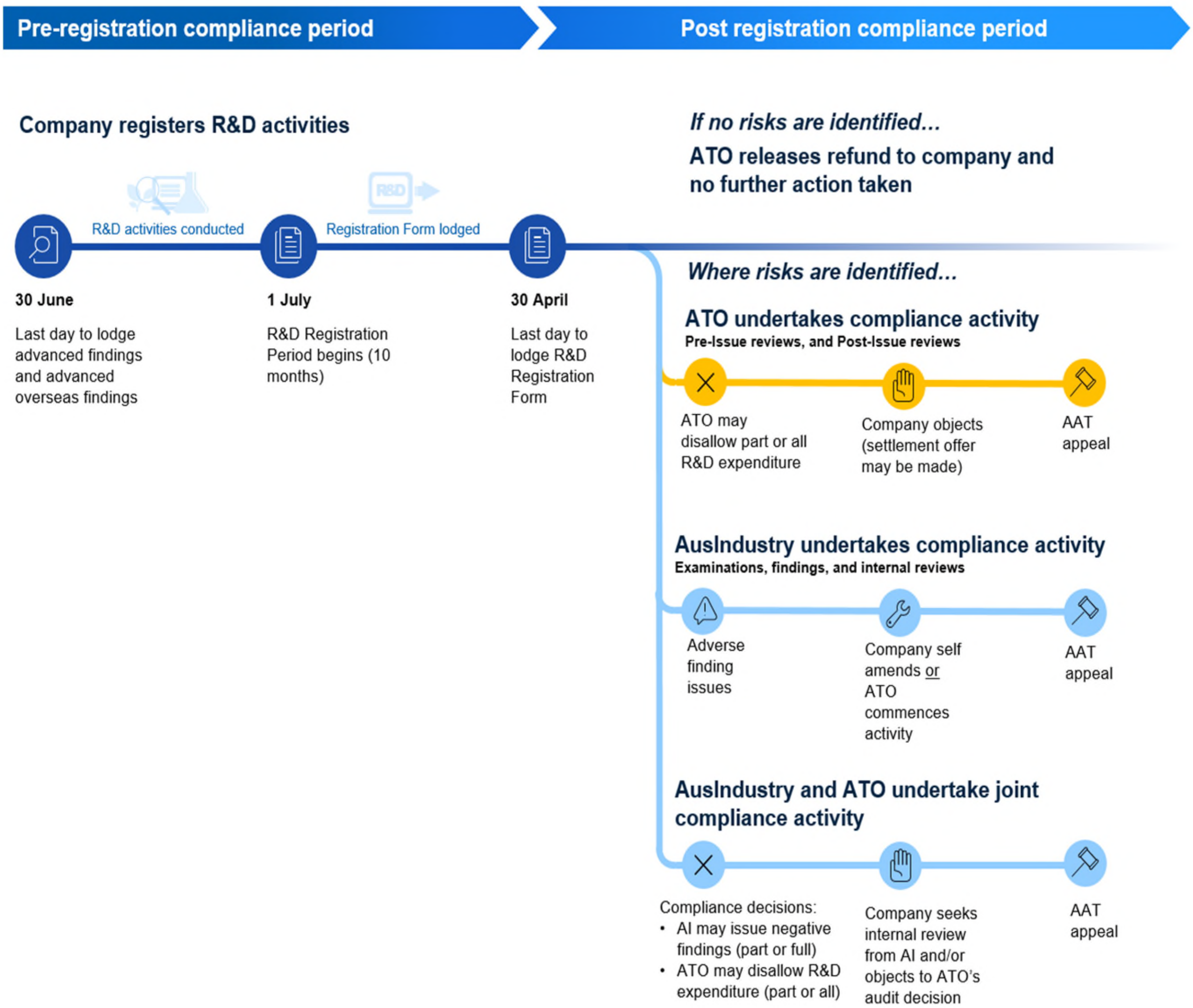



**Diagram 2.2: Compliance process for R&DTI**

## 2.5 Education and stakeholder engagement

To support companies to self-assess correctly, both the ATO and DISER conduct joint consultative forums and presentations to companies, R&D consultants, tax agents and industry groups. Both agencies undertake education activities, including joint visits to companies (pre-COVID), and virtual meetings where possible. This is generally well-received by companies and consultants. Both agencies also produce communication products to promote the R&DTI, support self-assessment and disseminate legal decisions and tax payer alerts relating to the R&DTI.

The ATO and DISER regularly discuss program administration and can act quickly to respond to emerging issues. For example, in 2020, DISER and ATO discussed options for adjusting R&DTI administrative practices to alleviate burdens on companies impacted by the bushfires and the COVID-19 pandemic. Companies were allowed a 5-month extension beyond the usual deadline to register R&D activities undertaken in the 2018-19 income year. Companies that required a further extension were able to apply for an extension in the usual way. Around 25 per cent of applicants for the 2018-2019 income year took up the extension.

DISER and the ATO look for and value opportunities to engage with stakeholders, individually or in broader settings. For example, DISER and the ATO jointly arrange regular forums to engage with program users on specific topics and to share information. Recent stakeholder engagement has occurred in relation to:

- the new R&DTI Customer Portal and registration form
- development of guidance on software-related activities and record keeping
- R&DTI Roundtable and State Reference Group (SRG) meetings
- external speaking engagements and information sessions.

DISER and the ATO also value the feedback received from R&DTI stakeholders through external sources, like Parliamentary Committee inquiries and the recent consultation sessions held nationally as part of the Board of Taxation review process. Insights and feedback from these sources present ongoing opportunity for improving customer service and administrator interactions.

## 2.6 Compliance activities

To meet the expectations of the Government and taxpayers, DISER and the ATO have established effective compliance frameworks and working arrangements to maintain the integrity of the program in delivering its objectives.

Common feedback received by both agencies from program users is that DISER and the ATO could better coordinate compliance activities, potentially to conduct them at the same time. DISER and the ATO acknowledge that compliance activities are not always conducted simultaneously. Compliance activities may be conducted by only one agency where the risk is limited to that agency's area of responsibility. For example, the risk could be limited to concerns that the registered activities are not eligible, with no potentially high risk expenditure present. In cases like this, DISER may conduct compliance activities without needing to involve the ATO.

However, if DISER conducts a compliance assessment and issues a finding to a company advising that all or some of its registered activities are not eligible, and the company does not self-amend its tax return to remove the expenditure associated with the ineligible activities, the ATO is required to undertake compliance action to give effect to the findings.

Whether the action is concurrent or after one agency has completed its actions, both agencies share the information received to the extent possible to minimise duplication and help reduce the cost of compliance to the company.

## 2.7 Dispute management and how issues are resolved

Within DISER:

- An applicant may apply for an internal review within 28 days of receiving a notification on a reviewable decision (on a primary assessment decision that is outlined in section 30A of the IR&D Act) using an approved Internal Review Request Form.
  The reviewable decision can be on:
  - Pre-Registration finding
  - Post-Registration finding, and/or
  - Advance and Overseas findings.
- An application may then be made to the Administrative Appeals Tribunal (AAT) for review of an internal decision made by the IISA Board under section 30E of the IR&D Act. Applicants may also seek leave to appeal AAT decisions to the Federal Court of Australia (FCA).

Diagram 2.3 outlines the R&DTI process from a pre-registration finding to external appeals.

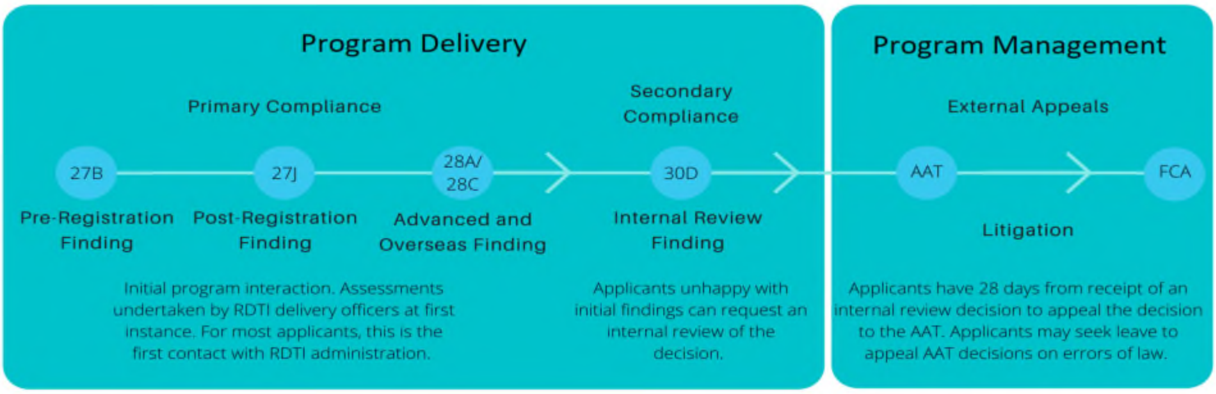



**Diagram 2.3: Applicant interactions as defined by IR&D Act**

Ten years on, the program has reached a level of maturity such that DISER and the ATO have a strong understanding of the program's operation, scale, risks and environment.

Using this as a foundation, DISER and the ATO now look to drive a step-change in their joint administration of the program that will reinforce and uplift a holistic and focussed whole-of-program approach that draws on the strengths of each agency and makes best use of the capabilities, authority and resources of both agencies. This is aligned with respective corporate objectives to build stronger relationships, effectively use data and embrace digital solutions to improve decisions, services and compliance.

# 3 Reviews of the R&DTI

The administration of the R&DTI has been raised in a number of reviews, as set out in this Section. Some of the administrative reforms implemented by DISER and the ATO in recent years (set out in Section 4) were informed by these reviews. Others resulted from stakeholder engagements and/or commitments to continuous improvement. A range of program improvements are still in progress, as set out in Section 5.

**Key points**

* Recommendations for improving the administration of the R&DTI were made by the 2016 Review of the program and the ASBFEO.
* The ANAO is currently auditing the administration of the R&DTI by DISER and the ATO.
* In the context of the Senate Select Committee's inquiry into Australia as a Technology and Financial Centre, tech sector representatives have been working with the joint administrators to better understand how the R&DTI applies to software development.

## 3.1 Administrative aspects of the 2016 Review of the R&DTI and 2018-19 Budget reforms

### 3.1.1 Background

In 2015, the Government commissioned a review of the R&DTI program in conjunction with the announcement of the National Innovation and Science Agenda. The 2016 Review of the R&DTI was undertaken by Mr Bill Ferris AC, Dr Alan Finkel AO and Mr John Fraser, informed by several research and evaluation projects already commissioned by DISER. The Review found that the R&DTI did not fully meet its stated objectives of inducing additional R&D and positive spillovers, and could be enhanced to deliver more fully on its outcomes.

### 3.1.2 2016 Review recommendations

The Review made a number of policy and program recommendations aimed at improving the effectiveness, integrity, sustainability and transparency of the R&DTI.

Recommendation 1 sought clearer guidance on the scope of the program, rather than legislative change to narrow the definition of eligible activities and expenses.

> ***Recommendation 1****: Retain the current definition of eligible activities and expenses under the law, but develop new guidance, including plain English summaries, case studies and public rulings, to give greater clarity to the scope of eligible activities and expenses*

In making Recommendation 1, the panel observed:

> *The panel finds that the definition of eligible R&D broadly aligns with the OECD Frascati Manual, which is regarded internationally as setting the benchmark for identifying R&D activities. The supporting legislation is drafted using a principles-based approach with a broad concept of eligible expenses, allowing flexibility as R&D activities evolve over time.*

Recommendation 6 included a package of measures focussed on administrative aspects of the program, including the joint administration by DISER and the ATO.

> ***Recommendation 6****: That the Government investigate options for improving the administration of the R&D Tax Incentive (e.g. adopting a single application process; developing a single programme database; reviewing the two-agency delivery model; and streamlining compliance review and findings processes) and additional resourcing that may be required to implement such enhancements. To improve transparency, the Government should also publish the names of companies claiming the R&D Tax Incentive and the amounts of R&D expenditure claimed.*

In making Recommendation 6, the panel observed:

> *'The panel notes that despite the level of coordination between AusIndustry and the ATO, the significant growth in the scale of the programme is placing increasing strain on the administrative and compliance model for the programme. The Government should consider options to improve administration. These could include: adopting a single application process rather than the current separation of registration and claims, introducing a single database for the entire programme, reviewing whether both AusIndustry and the ATO should continue to administer the programme jointly and closer collaboration and streamlining around review and findings. Either or both agencies may require additional resourcing to enable such improvements.*
>
> *To place the programme into alignment with modern expectations and to allow public visibility of companies receiving public support for their activities, tax secrecy provisions should be adjusted to allow the publication of the names of companies claiming the Incentive and the amounts of R&D they have claimed.'*
>
> *'The scale of the programme and method of delivery creates challenges for the programme administrators to strike a balance between providing a positive user experience and ensuring programme integrity. User experience is influenced by the ease of access to the programme benefits. In this respect, the level of guidance provided by administrators can influence the cost of compliance and the need to resort to specialist advisers to support registration and claims. The growth in specialist adviser activity could point to the complexity of the process and the need for enhancement of the administration.'*[10]

### 3.1.3 R&DTI administrative and compliance costs

Ahead of the 2016 Review of the R&DTI, the Centre for International Economics (CIE) was commissioned by DISER to review the program. The CIE produced a report[11] which ultimately informed the final report of the 2016 Review by the review panel.

CIE measured the administration and compliance costs of the R&DTI, concluding that:

- Compliance costs to firms incurred to register for and claim the R&DTI were estimated to be around 9 per cent of the benefits they receive in offset or refunded taxes. A significant share of this (around 46 per cent) was paid to consultants
- Administrative costs to the government to administer the program, including compliance activities, were reported to be up to $28 million per year.

The CIE broke down compliance costs to program users and these costs are included in Table 3.1 below.

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[10] https://www.industry.gov.au/sites/default/files/May%202018/document/pdf/research-and-development-tax-incentive-review-report.pdf?acsf_files_redirect, Review of the R&D Tax Incentive, 4 April 2016, pages 4 and 22.
[11] *R&D Tax Incentive Programme Review, CIE, 2016*.

**Table 3.1 Survey responses on compliance costs ($ per firm)**

| Cost item | unit | All firms (weighted average) | Large firms | SMEs |
|---|---|---|---|---|
| Application and registration | $ | 13,784 | 49,599 | 9,503 |
| R&D schedule of tax return | $ | 11,554 | 27,354 | 9,665 |
| Record keeping | $ | 10,120 | 37,171 | 6,887 |
| Other | $ | 1,396 | 3,748 | 1,115 |
| Total compliance costs (95% confidence interval) | $ | 36,854 (25,730 to 47,980) | 117,872 (78,860 to 156,885) | 27,170 (19,380 to 34,962) |
| **Total compliance cost as a share of benefits** | % | **9** | **8** | **23** |
| Paid to a consultant | $ | 16,797 | 63,334 | 11,233 |
| Share paid to a consultant | % | 46 | 54 | 41 |

*Source:* R&D TI survey 2015.

The CIE also broke down government costs associated with the R&DTI and these are included in Table 3.2:

**Table 3.2 Government administrative costs, typical year ($'000)**

| Cost item | Funding | Data source |
|---|---|---|
| Administered funding: AusIndustry | 2,823 | Portfolio Budget Statements 2014–15, Budget Related Paper no. 1.12, Industry Portfolio |
| Departmental funding: ATO | 5,800–8,700 | ATO, pers. comm. |
| Departmental funding: DIIS | 13,432 | DIIS, pers. comm. |
| **Total administrative costs** | **22,055–24,955** | – |

ATO = Australian Taxation Office; DIIS = Department of Industry, Innovation and Science.

*Note:* Estimates of forgone revenue and refunds are included in the next section. These costs are based on costs for 2014–15, as they are thought to be the most reliable estimates of costs to run the program in a typical year.

### 3.1.4 Australia 2030: prosperity through innovation

Then Innovation & Science Australia (ISA), the predecessor of IISA, chaired by Mr Bill Ferris, released its *Australia 2030: Prosperity through Innovation* plan (2030 Plan) in January 2018. While the 2030 Plan included a slightly modified set of recommendations, ISA did not propose any changes to Recommendation 1 or 6 of the 2016 Review, or any further changes to the administration of the R&DTI.

### 3.1.5 Government's response to the 2016 Review

In response to the 2016 Review, in the 2018-19 Budget, the Government agreed to a package of measures to help improve the effectiveness and fiscal sustainability of the program. Administrative reforms in response to Recommendations 1 and 6 of the 2016 Review were included in this package:

> *'The integrity and affordability of the R&DTI will also be improved through increased resourcing for administrators, helping ensure that ineligible R&D claims are denied.*
>
> *Greater transparency around who is claiming the R&DTI will promote public accountability for those benefitting from taxpayer support.*
>
> *Businesses claiming the R&DTI will benefit from improved guidance material to help them correctly claim for eligible R&D activities.'*[12]

The administrative reforms announced as part of the 2018-19 Budget package remained largely unchanged in the enhanced reforms announced as part of the 2020-21 Budget package.

[12] 2018-19 Budget Overview, page 29.

## 3.2 2019 Australian Small Business and Family Enterprise Ombudsman (ASBFEO) Review

In 2019 the ASBFEO, Kate Carnell AO, conducted a review of the administration of the R&DTI. The review investigated the experiences of SMEs that have claimed offsets under the program. During the review, both DISER and the ATO met with the ASBFEO to discuss its interactions with businesses and respond to the ASBFEO's queries. Neither agency was provided with a copy of the report before it was released on 12 December 2019.

The report put forward a suite of recommendations for the co-administrators to consider, both individually and jointly. The report's 24 detailed recommendations were aimed at improving the experience of SMEs accessing the R&DTI, and covered the following key themes:

- Where compliance examinations or audits are necessary, they should take place as close as possible to the first year of registration of a project
- Guidance material needs to be comprehensive, clearer and up-to-date and developed in consultation with small business
- Agency record keeping requirements need to be simplified and take into account commercial practicalities for a small business
- Small business must be assisted to help identify and retain professional and responsible R&D consultants.[13]

## 3.3 ANAO R&DTI 2021 audit

The ANAO has commenced an audit of the DISER and the ATO co-administration of the R&DTI Program, with a focus on effectiveness.

Both agencies welcome the opportunity to be involved in the ANAO audit and look forward to the final report when it is tabled in Parliament in November 2021.

Two key criteria of interest in the ANAO's audit concentrate on whether DISER and the ATO have effective:

- registration, eligibility review and compliance arrangements in place
- performance measurement and monitoring arrangements.

## 3.4 Other reviews

Submissions were received by the Senate Select Committee's inquiry into Australia as a Technology and Financial Centre.[14] Some of the submissions supported the expansion of the R&DTI to cover broader software development activities, or a separate tax in incentive to cover a broader range of innovative software development activities. The Committee is due to release its final report on 30 October 2021.

In the context of this inquiry, a number of technology companies wrote to the Commissioner of Taxation seeking a collaborative workshop with administrators to resolve uncertainty around the application of the R&DTI to software development. Section 5.2.1 outlines ongoing engagement with the tech sector in response to this request.

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[13] https://www.asbfeo.gov.au/news/news-articles/ombudsman-recommends-sweeping-changes-rd-tax-incentive-administration.

[14] Originally the Senate Select Inquiry into Financial Technology and Regulatory Technology.

# 4 The reform journey

DISER and the ATO have implemented a broad range of administrative improvements. These improvements include the reforms announced by Government in the 2018-19 Budget in response to the 2016 Review, as well as changes resulting from feedback from the ASBFEO and other stakeholders (see Section 3). Other improvements are in progress, as set out in Section 5.

**Key Points**

Improvements to the program include:

* a behaviourally-based Integrity Framework that acknowledges that most participants in the program are trying to do the right thing
* a customer engagement approach that focusses first on education and guidance and only moves into formal statutory examination in clear cases of non-compliance
* an approach that seeks to limit the impact of overly-retrospective compliance action
* a new R&DTI Customer Portal with a new application form that: helps companies register their R&D activities and manage their applications, reduces time and costs to apply; and helps DISER to identify participants that need help to understand program requirements, or who are registering non-compliant activities
* better decision-making through enhanced procedural fairness and transparency processes, as well as partnering with CSIRO's Data61 to provide advice into complex assessments in ICT/software
* a new determinations framework that will allow the IISA Board to publicly state its positions on the application of its functions and/or on the interpretation of relevant legislation that is binding on the Board and its delegates.

## 4.1 Customer-focussed compliance

Additional funding provided in the 2018-19 Budget allowed DISER and ATO to improve their compliance processes in response to Recommendation 6 of the 2016 Review. This raised the awareness of stakeholders on the eligibility of their activities and expenditure and enabled the costs of the program to be brought back within expectations. As shown in Chart 1.1 (page 10), program costs have stabilised in recent years, and did not reach the unsustainable levels forecast at the time of the 2016 Review.

Following feedback from stakeholders, including the ASBFEO, DISER considered further improvements to its processes. DISER has since implemented a guidance-first approach to compliance. This approach places an emphasis on education as a first step in ensuring program integrity. It then moves through to formal statutory examination as a second step, or in clear cases of non-compliance. DISER's approach relies on a behaviourally-based Integrity Framework which acknowledges that most participants in the program are trying to do the right thing.

### 4.1.1 Improved guidance materials

Consistent with Recommendations 1 and 6 of the 2016 Review, additional funding received by DISER through the 2018-19 Budget was also used to bolster existing other education and compliance efforts. This included funding to address a then growing group of litigation cases.

Following the 2016 Review of the R&DTI, DISER and the ATO analysed their existing guidance materials against customer needs. Both agencies then implemented a series of improvements to their collective guidance products. Diagram 4.1 indicates the lessons learned from the analysis undertaken.

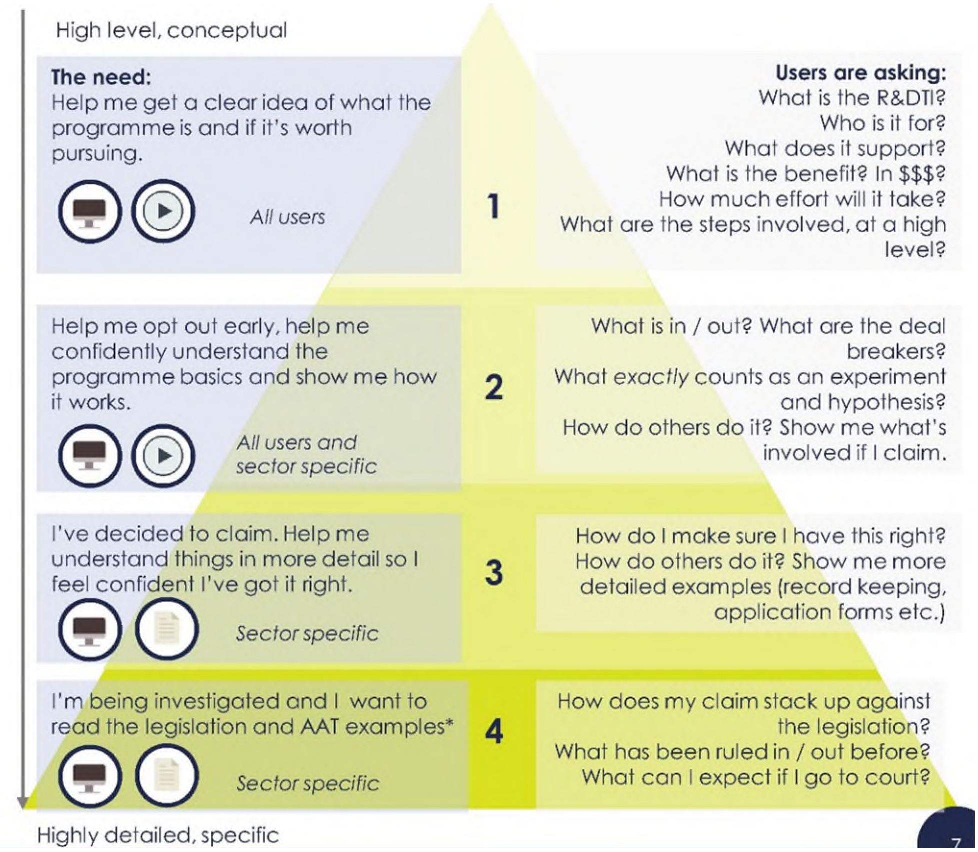


**Diagram 4.1: Improved guidance materials for stakeholder needs**

Stakeholder research indicated that businesses found the language used in (former) guidance products created an impression of legal complexity. Businesses wanted clear direction on what they need to do, and practical examples that do not need translation or interpretation. As a result of this research, changes were made to all information products. The existing guidance material on software related activities was reviewed and updated, with a user-focussed approach that provided easy to understand information for businesses and examples of how other businesses engaged with the R&DTI.

DISER has also provided additional support and guidance to businesses since the publishing of the ASBFEO Review. In 2020, the *Guide to Interpretation* was revised and made clearer for businesses to help them better understand the eligibility criteria for the program.

DISER has also worked to improve its website. Over the past year, DISER revised the layout of its business.gov.au webpages. DISER and the ATO also jointly developed new guidance products, such as the R&DTI Insights podcast, to support businesses to better understand eligibility under the program. DISER and the ATO issued a number of joint Taxpayer Alerts to raise concerns with companies and their advisors of certain R&D claims. A diverse catalogue of case studies and customer stories was prepared to assist program users and potential users understand what success looks like under the program. More recently, guidance on registrations and findings has been embedded in DISER registration application forms.

The ATO company tax return and R&D Schedule also includes detailed instructions for completion by companies or their advisors.

DISER and the ATO continue to listen to stakeholders and respond to the demand for clearer guidance, whether it be on certain issues or in respect of specific industry sectors. For example, both agencies are committed to developing a start-up guide to the R&DTI program and improving other guidance products to assist small companies that are in the program, or considering the program for the first time.

### 4.1.2 Improved DISER decision-making

DISER is improving its transparency when making decisions. A number of changes have been made to DISER processes to facilitate this objective. They include providing copies of Examination of Evidence Reports with Findings Certificates to provide greater clarity for stakeholders.

DISER provides final draft Internal Review Examination of Evidence Reports where the recommended decision is to confirm or amend the original decision to allow companies to respond to any claimed factual or legal issues prior to the final decision and any potential subsequent litigation action. This approach is aligned with the Service Commitment to be 'supportive', communicative' and 'transparent'.

DISER also aims to improve stakeholder confidence in its decision making by partnering with CSIRO's Data61 to provide advice on complex technical assessments in the ICT/software domain. In addition, as part of the internal and external review process, DISER responsively considers new information provided by companies; and where appropriate, adjusts previous decisions.

### 4.1.3 Improved compliance checks

Companies need to accurately self-assess their activities and register them correctly to meet program objectives. DISER and the ATO are responsible for ensuring the integrity of the program by checking the eligibility of activities and expenditure.

Both DISER and ATO provide companies with the tools and guidance to self-assess the eligibility of their activities and expenditure. Companies desiring certainty for specific activities can apply to DISER for a finding on those activities. Companies interested in certainty in regards to expenditure can apply to the ATO for a private ruling. Companies and their advisors also contact DISER and the ATO for general advice in regards to their R&DTI registrations and claims.

DISER and the ATO updated their approaches to R&DTI post-compliance activities following the Government's response to the 2016 Review. However during ASBFEO consultations, administrators heard of circumstances and saw evidence where companies' interactions with DISER and the ATO did not demonstrate the attributes associated with good program governance. For example, some of the cases spanned many years, with a number still being considered either by the ATO or DISER at the time of the review. These are discussed in the ASBFEO's key findings.[15]

In 2020 and 2021, DISER reviewed its approach to compliance to make it clear that most companies believe their activities are eligible for the program, and are either correct in this assessment or trying to get it right. Diagram 4.2 below contains DISER's new Integrity Framework. It shows how the levels of company compliance risk (from 'getting it right' through 'trying to get it right' to 'does not comply') are managed. More assistance is provided to companies who need help to understand self-assessment processes. The highest level of compliance check is provided to companies that do not follow guidance or do not comply with legislation.

Diagram 4.3 'User Journey' captures the education-led compliance approach experienced by the majority of companies and a greater level of compliance action for companies that do not follow DISER guidance.

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[15] https://www.asbfeo.gov.au/sites/default/files/documents/ASBFEO-RDTI-report.pdf, Review of the R&D Tax Incentive December 2019, Australian Small Business and Family Enterprise Ombudsman, page10.


| Company compliance risk | Company behaviour | Our response |
|---|---|---|
| Does not comply | Company considers the legislation and guidance but does not apply it as intended. Their R&D activities do not meet program requirements. | We deter high-risk approaches with targeted compliance activity. |
| Trying to get it right | Company tries to follow the legislation and guidance. They may not understand it or apply it as intended. Some R&D activities may be eligible and some may not. | We provide tailored guidance to help companies self-assess. Ineligible activities may be varied or withdrawn. |
| Getting it right | Company understands the legislation and program requirements. Their registration indicates accurate self-assessment. | We keep the company informed about their registration and monitor future applications. |
| Learning about the program | Company is new to the program. Some companies need assistance to understand the self-assessment process. | We provide guidance and support to help the company access the R&D Tax Incentive. |

**Diagram 4.2 DISER's new Integrity Framework**

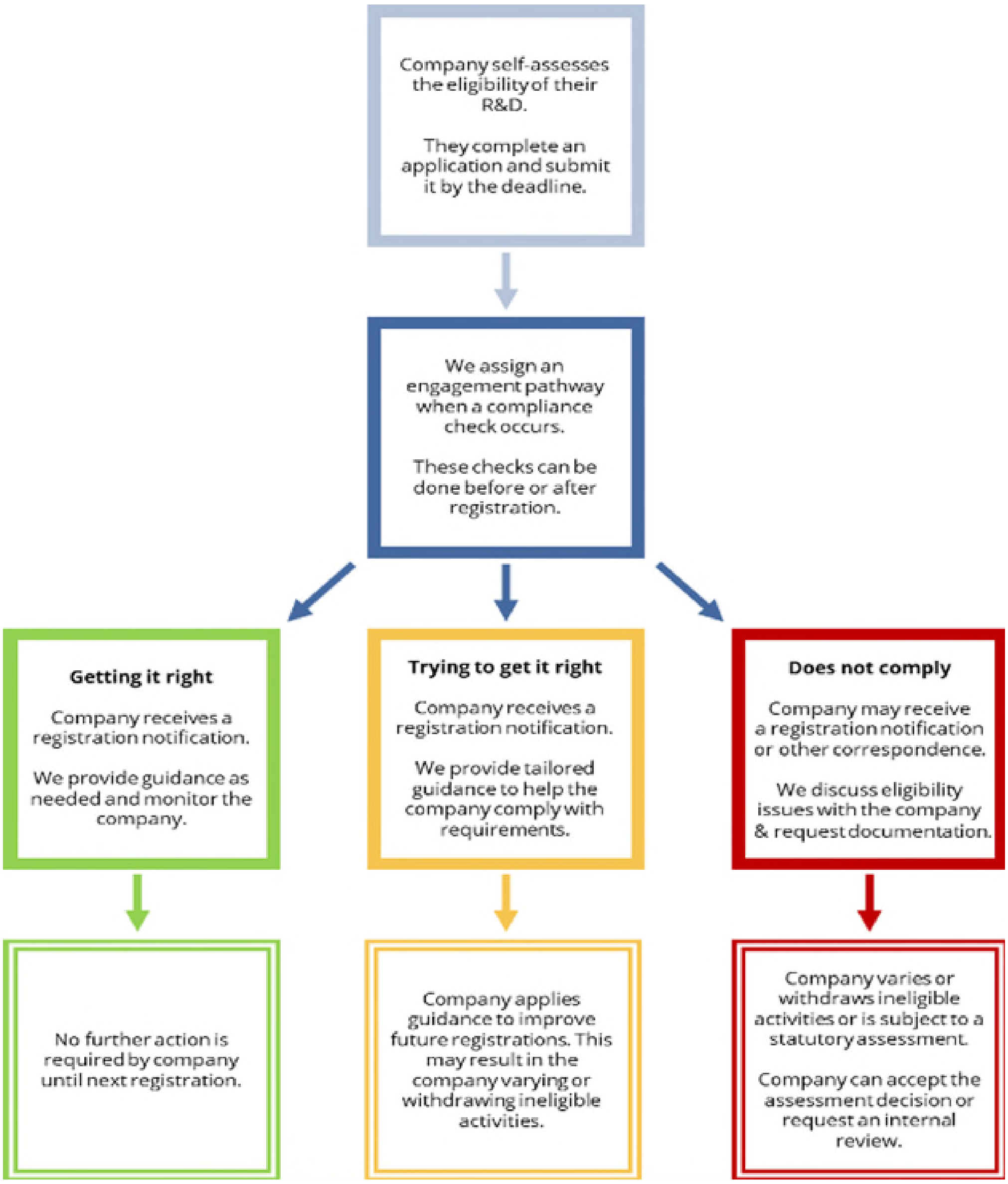



**Diagram 4.3 User Journey**

In response to feedback from stakeholders, including the ASBFEO, DISER has also adopted an approach that seeks to limit the impact of overly-retrospective compliance action where possible. Should the ATO need DISER to assess earlier years, DISER will do so in the interests of good joint administration. When selecting companies for DISER initiated risk reviews and examinations, however, it seeks to operate in the pre-registration space wherever possible, before an offset has been received. If this is not possible, DISER seeks to limit scrutiny to the most recent registration year.

Initiatives delivered or now underway to support DISER's revised compliance strategy include:

- Identifying Change – understanding the impact of increased guidance
- Large R&D claimants – building confidence in large R&D investment and influencing compliance behaviour
- Providing Draft Reports for Internal Reviews – aligning with the Service commitment to be Supportive', 'Communicative' and 'Transparent'
- Random Sample Project – assessing the level of compliance of a random selection of R&DTI registrations
- Behavioural Insights – translating behavioural consideration to improve business' engagement and program outcomes.

### 4.1.4 DISER Customer story

In 2019 DISER's R&DTI Early Engagement Team was being piloted as ASBFEO developed its December 2019 report. Creation of the team addresses key themes of the report by scaling up the program's capacity to engage with companies early in their program experience, provide education about program requirements and guidance to 'get it right' in future registrations.

Rob's company intelliHR first met with the new Early Engagement Team in October 2019 to discuss the company's 2017-18 registration and how future registrations might be improved. The team followed through with further guidance on the 2018-19 and 2019-20 registrations. Rob engaged constructively with the team and the guidance; the improved quality of registrations shows intelliHR is clearly on the path to 'getting it right'.

**Customer Story: intelliHR benefited from the education-led approach**

My name is Rob Bromage. I am the founder and managing director of intelliHR. We are a fast growing global technology business that grew out of Brisbane, Australia and now operates in 20 countries across the world and accelerating, I suppose, in terms of the number of businesses that are coming on to our platform. We are a next generation people management and data analytics software-as-a-service application that our customers use to look after their people. Certainly in these times of the global pandemic, the focus on people has been more than ever, which has seen our platform rolled out globally and really help businesses look after their people, which is incredibly rewarding.

The R&D Tax Incentive program has been incredibly instrumental to the growth of our organisation on a number of fronts. We compete in the creative industry so it is all about innovation and forward thinking and, with the support of the R&D Tax Incentive program, we have been able to continue to invest in R&D, which has really helped our product set itself apart in a global market place, competing with very large global businesses.

The R&D work we do is associated with our analytics capabilities. We do some exciting work around artificial intelligence, using machine learning techniques for natural language processing and natural language generation. We serve insights to our customers in real-time and leverage the data that flows across their organisations in real-time to help generate those insights.

The R&D program has helped us improve our focus on R&D. Really understanding the approach to take and the structure of the program really helped introduce a lot of rigour and focus to experiment better and test better and improve the quality of what we were actually doing.

I think the program has been quite key to us building our competitive advantage and put us in a place where we're able to provide a global leading product that sees us compete not only in the global marketplace but with multi-billion dollar funded organisations. This is a real testament to the quality of engineering and talent we actually have here in Australia.

A massive thank you. I certainly would recommend to anybody to reach out to AusIndustry* and learn more about the R&D Tax Incentive. It certainly benefitted our business. It has seen us grow from an engineering team of 4 or 5 people to now employing 80 people and a business that is now operating globally and competing on the back of the success of its innovation and the efforts of R&D that are actually improving the product that we actually provide and the workplaces of all our customers.

* Division of DISER

## 4.2 IISA Determinations – legislation and principles

The legislation to implement the original R&DTI reforms announced in the 2018-19 Budget included the introduction of provisions enabling the IISA Board to make general determinations that were binding on IISA and its delegates.

While the original legislation did not pass, these provisions were included in subsequent legislation, including that introduced and passed in October 2020 to implement the enhanced reforms to the R&DTI announced in the 2020-21 Budget. The determination provisions commenced on 1 January 2021.

Determinations are intended to supplement program guidance by binding the IISA Board and its delegates to publicly-stated positions on the application of the IISA's functions and/or on the interpretation of relevant legislation. The public availability of determinations will provide clarity and certainty to business, as well as the ATO as joint administrator, on the way IISA and its delegates will apply legislation and perform their functions.

DISER has worked with the ATO and other agencies to develop a determinations framework based on the legislation and a number of principles to ensure they are used effectively. Under those principles, a determination could be made in a situation where:

- there is uncertainty or misunderstanding in law
- there is an opportunity to provide clarity and certainty on a program position through an engagement process
- it will not prevent the program acting in the manner in which it should.

In situations that do not lend themselves to determinations, more general non-binding guidance will continue to be provided through other channels. The clarity and certainty delivered by determinations is expected to enable companies to plan their R&D with confidence and encourage more eligible R&D to be conducted in Australia. It is important to note that a determination cannot limit the IISA Board's decision-making powers. See Section 5 for information on the development of the first determination.

## 4.3 ICT reforms

In implementing the Government's decision on the 2016 Review, DISER and ATO received funding to improve their systems.

To this end, DISER released its new R&DTI program ICT systems on 5 July 2021, including the R&DTI Customer Portal. The portal allows R&D entities and their agents to register for the incentive, apply for an advance or overseas finding request, an extension of time, variation or withdrawal and see the status of their applications. DISER's new ICT systems include the R&D Incentive Assessment System for processing registrations, conduct examinations and undertake other administrative activities.

DISER's new ICT systems provide a more modern experience for our customers. Benefits of DISER's new systems include:

- improved security for customers
- a revised registration form that is closely aligned to legislation and written in plain English
- improved real-time information for customers on the status of their applications and indicators of upcoming deadlines
- standardised and automated workflows improve consistency of approaches
- clearer service level agreement information for DISER staff to ensure that processes are timely
- automated program data and reporting.

## 4.4 Reduced compliance costs for R&DTI applicants

Through significant and sustained improvements to program administration, DISER and the ATO are continuing to reduce compliance costs for R&DTI applicants. Improved systems, early engagement and better education and guidance is improving self-assessment. This is reducing resources spent on time-consuming and costly post-registration activities, such as internal reviews and external reviews (including the AAT or FCA).

For cash-poor SMEs, this reduces inadvertent over-claiming and the need to pay back cash refunds. It also provides them with the opportunity to secure alternative support for activities that are not eligible under the R&DTI.

Improved self-assessment by applicants also allows DISER and ATO to focus post-compliance resources on genuine non-compliance, leading to more effective administration of the R&DTI.

### 4.4.1 Lodging registrations

Prior to July 2021, DISER relied on survey-based data to track the time it takes R&DTI applicants to complete registration forms. This metric provides an indication of the compliance costs applicant companies incur as part of participating in the R&DTI. Survey data collected in September 2020 indicated that that 64 per cent of applicants spend **over 25 hours** completing their registration form (see breakdown in Table 4.1 below of survey responses to the question: ‘How long does it take you to complete your registration form?’, which received 77 responses).

**Table 4.1: Responses to the question “How long does it take you to complete your registration form”**

| Option | Total | Percent |
|---|---|---|
| 0-10 working hours | 4 | 4.76% |
| 10-15 working hours | 4 | 4.76% |
| 15-20 working hours | 9 | 10.71% |
| 20-25 working hours | 6 | 7.14% |
| 25-30 working hours | 4 | 4.76% |
| 30-35 working hours | 3 | 3.57% |
| 35-40 working hours | 10 | 11.90% |
| 40+ working hours | 37 | 44.05% |
| We have not completed this type of application | 0 | 0.00% |
| Not Answered | 7 | 8.33% |

The R&DTI Customer Portal went live on 5 July 2021. Since that time, over 1,000 registration applications have been submitted through the portal. Early results indicate that the new registration form is faster for applicants to complete with the longest portal form taking **under 23 hours** to complete. Based on data collected up to 20 August 2021, of the 1,222 registration applications that have been submitted in the portal, the three longest times captured to complete a registration are:

- 22 hours 44 minutes
- 15 hours 37 minutes
- 12 hours 5 minutes.

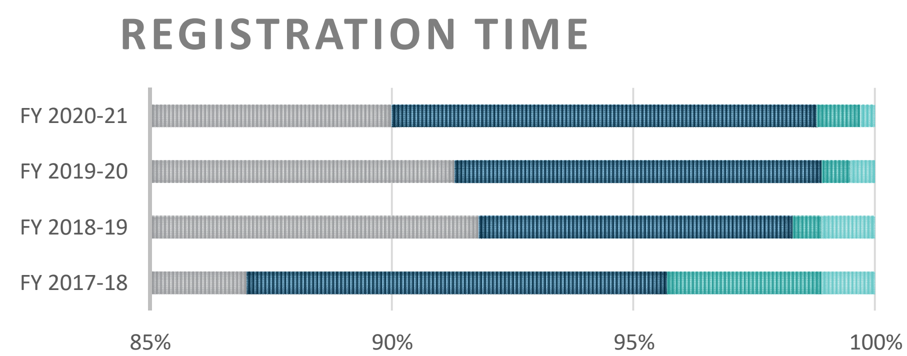
Longest times are used as a comparison to the 2020 survey data as it is possible to work outside of the portal and copy and paste into the portal forms as the last step.

The highest compliance costs for applicants are now likely to be incurred through the increased focus on early engagement under DISER’s Integrity Framework as part of the pre-registration and registration process. This includes increased high-quality education that addresses the concerns of companies who are attempting to ‘get it right’.

## 4.4.2 Processing applications

The increased focus on education and engaging with companies at the front-end of the R&DTI program will lead to better submissions as part of the pre-registration and registration processes, a more efficient early engagement process with better outcomes for companies through faster registration, shorter time to undertake advance and overseas findings and internal reviews, and a reduction in the complexity of cases arising from mistakes made by the applicants.

This faster registration process is reflected in Chart 4.2 below. In 2017-18, 87 per cent of applications were registered in 10 days or less, and has remained above 90 per cent in the 2018-19, 2019-20 and 2020-21 financial years. The time taken to register complex cases that took between 21 and 30 days reduced from 3.2 per cent in 2017-18 to less than one per cent in the 2018-19, 2019-20 and 2020-21 financial years. Cases that took more than 30 days to register reduced from 1.1 per cent in 2017-18 to less than one per cent in the 2018-19, 2019-20 and 2020-21 financial years.




| | FY 2017-18 | FY 2018-19 | FY 2019-20 | FY 2020-21 |
|---|---|---|---|---|
| 10 days or less | 87.00% | 91.80% | 91.30% | 90.00% |
| Between 11 and 20 days | 8.70% | 6.50% | 7.60% | 8.80% |
| Between 21 and 30 days | 3.20% | 0.60% | 0.60% | 0.90% |
| Greater than 30 days | 1.10% | 1.10% | 0.50% | 0.30% |

**Chart 4.2 Time taken to register applications 2017-18 to 2020-21 financial years**

NB: To demonstrate changes over time the X-axis starts at 85 per cent and Chart 4.2 shows incomplete data for the 2020-21 financial year

## 4.4.3 Internal and external review

Currently the number of appeals to the AAT or FCA emanating from DISER R&DTI program delegates decisions is very low relative to the size of the program; noting that the AAT mostly uphold these decisions. As shown in Chart 4.3, over the lifetime of the R&DTI program, more than 70 per cent of DISER's decisions were upheld by the AAT or the FCA.

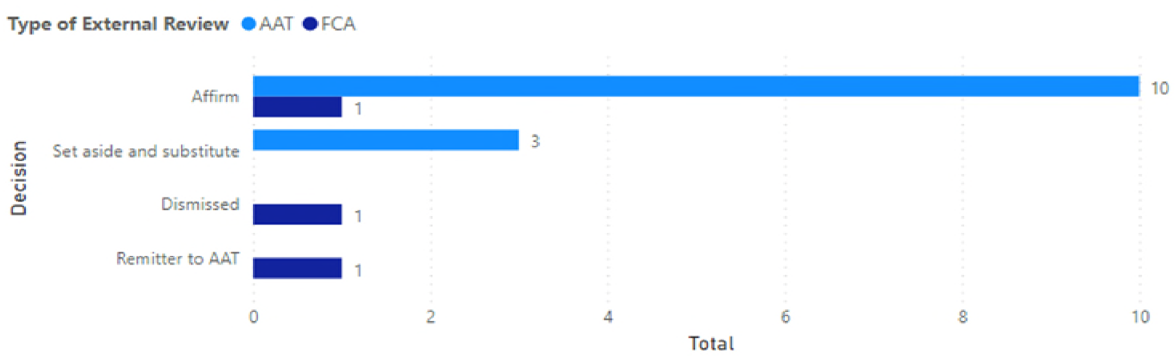



**Chart 4.3: Summary of External Decisions (2011-2021)**

DISER resolves matters through alternative dispute resolution processes where possible to reduce litigation costs to the Commonwealth and the applicant.

Chart 4.4 provides data on legal settlements since the start of the R&DTI Program. DISER has resolved over 25 per cent of litigated matters through in-principal settlements. The majority of these resulted from new information being brought forward by the applicants which demonstrated that the claimed R&D activities were eligible.

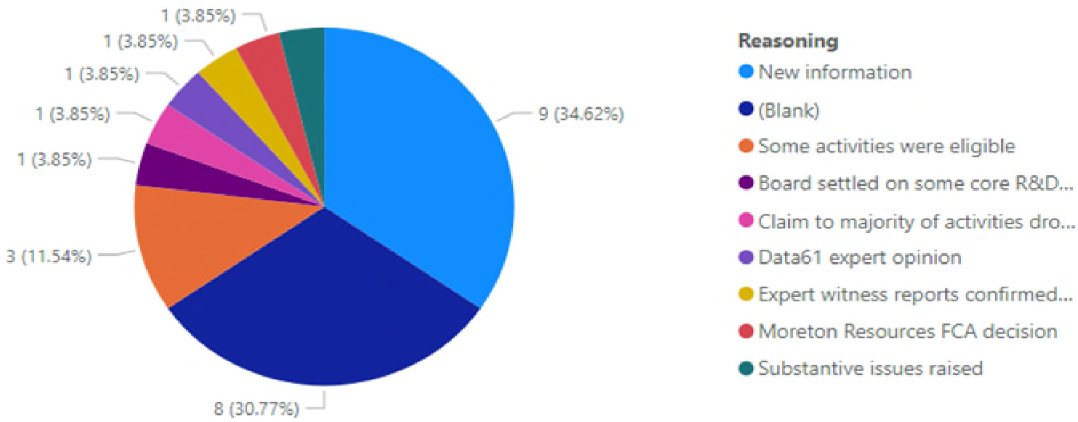



**Chart 4.4 Reason for Settlement (2011-2021)**

# 5 Planned future improvements to the R&DTI program administration

Ten years on, the program has reached a level of maturity where DISER and the ATO have a strong understanding of the program's operation, scale, risks and environment. Using this as a foundation, DISER and the ATO now look to drive a step-change in their joint administration of the program. This will reinforce and uplift a holistic and focussed whole-of-program approach that draws on the strengths of both agencies and makes best use of their respective capabilities, authority and resources. Adopting this approach supports both agencies' corporate objectives to build stronger relationships, effectively use data and embrace digital solutions to improve decisions, services and compliance.

**Key Points**

Upcoming improvements to the program:

* further releases of the DISER Customer Portal
* updates to ATO IT systems and website, Tax Return and R&D schedule instructions
* preparation for publication of information about R&D entities
* streamlined and automated data sharing between administrators
* improved guidance materials from both administrators – including software guidance
* development of the first determination under the R&DTI determinations framework
* review of legislative instruments due to sunset on 1 April 2022 unless re-made.

## 5.1 Enhanced digital delivery

### 5.1.1 DISER

DISER has two more planned releases to introduce improvements to the new customer portal, with the possibility of further releases if required. These releases will focus on implementing improvements that have been suggested by customers and DISER staff to help improve the customer experience and to ensure ICT systems help DISER staff administer the program efficiently.

The next release will be on the first weekend in November 2021. This release will include additional features – such as an enhanced set of special characters, improved guidance, help text and alerts to assist customers navigate the registration process, and enhanced features for sorting projects, core activities and supporting activities.

### 5.1.2 ATO

The ATO systems are on schedule to be updated for the legislative changes announced in the 2020 Budget that apply for the 2021-22 income year. Some of the changes include the rates for the refundable and non-refundable offsets and the R&D Calculator, which companies use to assist in the assessment of their entitlements and to complete R&D schedules.

### 5.1.3 Automated data-sharing between DISER and ATO

DISER and the ATO are in the process of finalising a joint system build that will allow more streamlined and automated data sharing between the agencies. The purpose of the joint system build is to speed-up validation of self-reported data and enhance risk profiling using combined data from DISER and ATO. This build commenced with funding in the 2018 Budget.

## 5.2 Enhanced guidance materials

### 5.2.1 Refreshed software guidance materials

Following representations from key stakeholders in the tech sector in the context of the Senate Select Committee inquiry into Australia as a Technology and Financial Centre, collaborative workshops involving the software industry, DISER and ATO were held on 28 April and 11 August 2021. The workshops explored how greater certainty could be provided on how the R&DTI applies to software development. The outcomes of these workshops have been positive, and further engagements are planned.

In particular, these workshops are helping with the drafting of refreshed software guidance material. For example, the April workshop informed the first draft of DISER's refreshed software specific guidance, which was released for public consultation in May 2021. DISER expects the final version to be released later in 2021.

The ATO is also working on a new software expenditure guide, and both agencies are collaborating to produce a guide for start-ups.

**Stakeholder engagement: co-design of software guidance**

DISER and the ATO consult extensively with program users in the development of application forms, and guidance and education products.

In March 2021 representatives from 12 tech companies and organisations wrote to the Commissioner of Taxation proposing a collaborative workshop to focus on how software-related activities are treated under the R&DTI. In its media release of 9 March 2021, SmartCompany noted that the ''signatories say the RDTI scheme is a 'critical support mechanism' for fostering innovation in Australia''.


Speaking about the proposal, InnovationAus reported that StartupAus Chief Executive, Mr Alex McCauley, had said the 'RDTI has been a critical part of the huge success of Australia's tech sector over the last five to ten years. That's why we're so committed to working constructively with the government to make sure we continue to support the growth of this high-value industry'.

Responding to stakeholders, a co-design workshop involving participants from the software industry and government was held on 28 April 2021. The purpose of the consultation was to improve the understanding between government agencies and the software industry on the application of the R&DTI.

Outcomes from the workshop were used to refresh the guide on software-related activities that was made available for comment on DISER's consultation hub from 17 May to 18 June 2021. Feedback from around 30 submissions on the refreshed guidance indicated that: it was generally easy to read and understand, businesses are likely to refer to the guidance to help them self-assess their activities, and that case studies and examples are welcome, however more are requested.

A second workshop, which was delayed due to the pandemic, was held on 11 August 2021. This workshop focused on record keeping to help applicants correctly self-assess activities and substantiate expenditure incurred on software-related R&D activities. Outcomes from this workshop, including suggestions for a record-keeping template, are currently being worked through as part of further improvements to software specific guidance.

Work continues on this valuable collaboration between industry and administrators to facilitate access to and improve delivery of the R&DTI.

### 5.2.2 Additional ATO guidance materials

The 2020-21 Budget announced enhanced R&DTI reforms applying from 1 July 2021. In response, the ATO has been taking an iterative approach to updating its web guidance to ensure there is no confusion for taxpayers lodging returns for the 2020-21 income tax year under the old legislation.

The ATO will publish additional guidance before the new legislation applies in the 2021-22 year. In addition to updated web guidance, the ATO will also be making changes to the Company Tax Return and R&D schedule instructions. The ATO will work with software companies to align their accounting software packages with the updated ATO systems to come online for 1 July 2022.

The ATO is currently working through the administrative design procedures for the requirement for the Commissioner of Taxation to publish selected R&D information about entities claiming the R&D tax offset. The first publication is required two years after the end of the 2021-22 financial year and will be published as soon as practical after 30 June 2024.

In addition, the ATO is currently working to refresh the R&D website content on ato.gov.au by late 2021. The structure of the website will be more user-friendly with a modular approach. The content will provide greater guidance to companies and advisors by including more detailed case studies and enhanced details on eligible expenditure including topics such as:

- apportionment
- nexus between the registered R&D activities and the R&D expenditure
- record keeping
- payments to associates.

### 5.2.3 First determination – drafting and consultation

DISER expects that the first determination to be made under the new R&DTI determinations framework (see Section 4.7) will relate to clinical trials. Work has commenced on the draft determination. To select this topic, DISER identified medical products as a national priority area, and will leverage data in existing positive advance findings to analyse the factors that have contributed to positive and negative findings.

Subsequent determinations may respond to issues identified by program participants and other program stakeholders. DISER will prepare determinations in consultation with industry and the ATO before finalised determinations are published on business.gov.au.

## 5.3 Upcoming legislative reviews

Two legislative instruments, *Industry Research and Development Regulations 2011* (Regulations) and *Industry Research and Development Decision-Making Principles 2011* (Decision-making Principles), are scheduled to sunset on 1 April 2022. These legislative instruments support the administration of the R&DTI. The review is aimed at ensuring the Regulations and Decision-making Principles are fit-for-purpose. Public consultation on a proposal to remake the instruments with minor amendments was undertaken by DISER and closed on 9 September 2021. The proposed minor amendments were primarily aimed at providing further clarity and certainty for stakeholders and administrators on operation of the R&DTI. Feedback from the consultations was under consideration at the time of this submission.

# 6 International comparisons

**Key Points**

* While R&D tax incentives are the most common form of support for business R&D in the OECD, other countries have a more balanced mix of direct and indirect measures than Australia.
* While single administration models run by tax authorities are the most common models, many still require a step to certify projects either ahead or after activities are undertaken.
* Some jurisdictions have mechanisms to provide companies certainty about future activities.
* Dual-agency administration models are able to leverage the expertise of each agency for different aspects of administration.
* Single-agency administration models can benefit from efficient decision-making, operations and resource allocation, but can also be ineffective where program and agency objectives are misaligned.
* DISER and the ATO engage with administrators from other jurisdictions to share information and learn from their experiences.

## 6.1 International business R&D support models

In a 2020 report[16], the OECD identified 37 OECD countries with expenditure-based R&D tax incentives. The benefits are of different types and are often broad-based with many, such as France, Canada, Korea and Singapore, offering a premium to SMEs. Australia's support for business R&D is broadly in line with that provided by other countries.

Some countries, like Australia, Japan, and Portugal, opt for a broad-based tax incentive as the main means of encouraging business investment in R&D across the economy. Other countries, such as Finland, Sweden, Poland, and Brazil, rely predominately on direct measures to support business R&D. Most countries (25 out of 30) blend indirect measures (tax incentives) with direct measures (grants) to target certain types of research, sectors of the economy, and behaviours such as collaboration between industry and researchers.

In addition to tax relief redeemable against corporate income tax, some jurisdictions also provide tax relief redeemable against payroll withholding tax or social security contributions. In Vietnam qualifying companies can access tax holidays, and in a few countries personal income tax benefits are also available to employees working in certain fields.

## 6.2 International R&D tax incentive administration models

The administration of R&D tax incentives varies from country to country and is particular to the type of incentive suited to the economic conditions and profiles in each jurisdiction. Eight countries, including Australia, use similar multiple agency administration models (the other seven are Austria, Chile, France, Hungary, Lithuania, Luxembourg, NZ, and Norway). In these countries, departments focussed on science, research and technology administer the eligibility of activities; and the tax authority typically holds responsibility for offset calculation, payment and audit.

[16] OECD 2020, *Measuring Tax Support for R&D and Innovation.* OECD. www.oecd.org.

In Australia, dual-agency administration of the R&DTI is formalised in legislation. The rationale for a dual-agency model centres on leveraging the expertise and focus of the respective agencies to best serve both industry and the program's economic objectives. This has been clear from introduction of the Income Tax Assessment Amendment (Research and Development) Bill in 1986.

The single-agency model is more common. While a number of large OECD countries with a single-agency model do not require a registration process, in many single-agency models there are still two steps before a tax offset can be disbursed. In Germany, companies apply first to a certifying body to confirm projects as 'qualifying R&D' ahead of their conduct, before the claim for confirmed R&D activities is then submitted to the tax office after the end of the income year in which those qualifying expenses were incurred. Certifying bodies play a role in administering R&D tax incentives in several jurisdictions. Some are government entities, others are accredited private consultancies.

In some jurisdictions there are mechanisms to provide companies with certainty about their intended future R&D activities. For example, in Norway, a company's proposed R&D activities are assessed by the Research Council against the definition of R&D in tax law before the claim is submitted. Approvals are usually given for 2 to 3 years. In Australia's Overseas and Advanced Findings process, eligible activities may be approved for up to 3 years (or longer in the case of Overseas Findings).

Table 6.1 contains details of R&D activity administration models in Australia, NZ, Canada, the United Kingdom (UK) and Ireland. Australia and NZ both have a dual or multi-agency model, whilst Canada, the UK and Ireland have a single-agency model.

**Table 6.1 R&D activity administration models in selected jurisdictions**

| | Australia | New Zealand | Canada | United Kingdom | Ireland |
|---|---|---|---|---|---|
| **Administration** | Joint agencies administration | Joint agencies administration | Single agency administration | Single agency administration | Single agency administration |
| **Self-Assessed** | Yes | No (From 2020-21 onwards) | Yes | Yes | Yes |
| **Eligibility** | • Must meet legislated eligibility criteria.<br>• Must be a company incorporated in Australian law, or incorporated under a foreign law but an Australian resident for income tax purposes, or Incorporated under a foreign law but are a resident of a country with which Australia has a double tax agreement and is carrying on business in Australia through a 'permanent establishment'<br>• Minimum R&D expenditure of $20,000 unless undertaking the research with a Research Service Provider (RSP) | • Must meet legislated eligibility criteria.<br>• Must have a fixed establishment in NZ and carry out activities in NZ.<br>• A minimum R&D expenditure threshold of $50,000 per year, unless the expenditure is related to R&D contracted out to an Approved Research Provider | • Must meet legislated eligibility criteria.<br>• R&D must be conducted by a Canadian company, through a Canadian subsidy of a foreign parent, or through a Canadian-controlled private corporation (CCPC) | • Must meet legislated eligibility criteria.<br>• Eligible companies must be liable to pay Corporation Tax in the UK. | • Must meet legislated eligibility criteria.<br>• Must be within the charge of Corporation Tax in Ireland<br>• Must carry out qualifying R&D activities in Ireland or the European Economic Area (EEA) or the UK |
| **Offset Amount** | • 43.5 per cent (aggregated turnover of less than $20 million per annum)<br>• Non-refundable 38.5 per cent (aggregated turnover of $20 million or more per annum | • 15 per cent | • A refundable Investment Tax Credit (ITC) of 35 per cent for Canadian controlled private corporations, up to $3 million.<br>  ○ Non-refundable ITC at 15 per cent on over $3 million<br>• 15 per cent ITC for Sole proprietorships, trusts, branch operations, and partnerships operating businesses in Canada | SME R&D Relief<br>• 230 per cent deduction of qualifying costs. 14.5 per cent payable credit.<br>R&D Expenditure Credit<br>• 13 per cent of qualifying expenditure | • 25 per cent tax credits for expenditure on qualifying R&D activities<br>• Companies can receive an additional to the 12.5% corporate tax deduction (even if the expenditure does not qualify as R&D expenditure) for these expenses.<br>  ○ Therefore, the effective tax relief is 37.5%. |

As at February 2021

## 6.3 Lessons from other jurisdictions

As noted in Section 2, a strength of the dual-agency model is the expertise each agency contributes to the effectiveness of a program's outcome. Joint governance structures are required to ensure this model works smoothly and efficiently, with joint and complementary guidance material and a mutual understanding of the risks associated with each agency's area of expertise.

For example, DISER is well-versed in eligibility requirements for R&D activities, but also needs to understand the key risks associated R&D expenditure. Similarly, the ATO is well-versed in taxation law, but needs to understand where the key risks lie in terms of eligible R&D activities.

The single-agency model can have strengths in streamlined decision-making, operational efficiency, resource allocation and coordination. Where an agency's mission and a program objectives are not aligned, however, single-agency models can adversely impact on the ability to achieve either the agency's mission or the program's objective – or both.

**Early implementation review of New Zealand's Research and Development Tax Incentive: – lessons learned**

Some countries with a joint administration model use three or more agencies in different modalities to manage the process, accredit eligible activities, and to undertake compliance activities. New Zealand launched its Research and Development Tax Incentive (RDTI) in 2019. The RDTI was based on the Australian example. It is administered by three agencies under a tripartite Memorandum of Understanding between: New Zealand's Ministry of Business, Innovation and Employment (MBIE), Callaghan Innovation, and the Inland Revenue Department (IRD).

In 2020 MBIE commissioned an independent review of the early implementation of the RDTI. One of the findings of the review was that even with the expertise of Callaghan Innovation, and the industry and innovation impetus of MBIE:

*"…administration of the RDTI is placing more weight on protecting the tax base than it is on increasing the level of R&D expenditure."* [17]

This demonstrates that even with a multi-agency administration model, care must be taken to ensure there is a common understanding of the objective of the program, and the respective roles and responsibilities of each agency. To deliver the program, agencies need to work together to harness the full range skills, expertise and resources available, and to continuously review their performance to get the balance right.

DISER and the ATO continue to engage bi-laterally and in multinational forums to share knowledge and discuss different aspects of R&D tax incentives and direct benefit programs around the world.

In the 2019-20 financial year, DISER met representatives from the Canadian Revenue Agency, and New Zealand's Callaghan Innovation and Inland Revenue Department to discuss the administration of each country's R&D support programs. The purpose of these meetings was to understand how each country administers its R&D programs and to learn about the challenges each country faces. By applying this shared knowledge, each administrator can improve the administration of their respective incentive.

Furthermore, DISER participates in formal and informal OECD discussions on R&D tax incentives and related topics and both DISER and the ATO enjoy an ongoing dialogue with Her Majesty's Revenue and Customs and Treasury in the UK.

[17] https://www.mbie.govt.nz/assets/rdti-review-of-implementation.pdf p.4.