



How Should Companies Group R&D Activities?

Specific Issue Guidance

What do companies and their advisors need to consider when deciding whether to group R&D activities for registration?

Introduction

Applying to register research and development activities with AusIndustry requires a company to think through its R&D activities and assess which of them are:

- eligible core R&D activities,
- eligible supporting R&D activities, and
- not eligible for support from the R&D Tax Incentive and will not be registered.¹

The most important point for a company to address in its registration is to specify what constitutes the activities, in a way that an independent person can understand what the activities consist of. The completeness of the description is critical to claiming because companies can only claim expenditure they have incurred on registered activities. The more significant a component of an activity is in terms of eligibility or expenditure, the more important it is for the company to describe it clearly.

When applying to register, companies may elect to 'group' a number of R&D activities together into a single R&D activity where each of the component activities could otherwise be described as individual R&D activities; for example, grouping multiple related tests as part of the same core R&D activity. This document provides guidance about what to consider in deciding whether to group activities together to register as a 'grouped' activity.

Guidance – grouping of activities

If grouping similar core R&D activities will maintain the clarity of the description of the activities then a company may wish to group them.

For example, a series of related experiments that are all trying to resolve a single technical challenge may be grouped as a single core R&D activity. Companies should be able to explain why they have chosen to group the R&D work, describe the experimentation and capture records to demonstrate that these experiments were conducted.

However it may not always be preferable to group activities. Companies should be careful not to make the description confusing or unclear, or obscure the eligibility of activities by grouping too much work into too few activities.

Companies should be careful not to group a diverse mixture of different activities into one activity description. Grouping dissimilar activities or too many activities together often means companies do not provide sufficient detail to clearly describe the activities. Companies should consider whether the activity grouping is helping them to describe the activities that they wish to register.

¹ See the *R&D Tax Incentive* 'Registration' web page at <http://www.business.gov.au/grants-and-assistance/innovation-rd/RD-TaxIncentive/Registration/Pages/default.aspx> and the *R&D Tax Incentive: A Guide to Interpretation* which is available from <http://www.business.gov.au/grants-and-assistance/innovation-rd/RD-TaxIncentive/ProgramInformation/Guide-to-Interpretation/Pages/default.aspx> for more information on registration requirements and how to self-assess whether you have undertaken core R&D activities and supporting R&D activities.

In general, activities that are not being undertaken in order to address the same hypothesis or related hypotheses should be registered as separate activities.

Keeping core R&D activities separate may allow companies to step through the logical progression of experimental activity more clearly in their registration application and their documentary records. It also makes it easier to understand the eligibility of supporting R&D activities by demonstrating a direct, close and relatively immediate relationship to the relevant core R&D activity.

When a company chooses to group its R&D activities it is important to ensure that the individual parts of each activity are described in the registration. It is important that eligibility can be explained and demonstrated for each part of these activities. It may also assist companies to maintain records about how activities that have been grouped are related.

Examples where activities could be grouped

The following brief examples illustrate how the experimental activities which have been grouped together correspond to one or more related hypotheses. A hypothesis relates to a specific experiment or set of related experiments, and not the project as a whole.²

- Testing a prototype medical device on a number of different sets of patients for its ability to diagnose multiple disease stages.
- A number of similar tests aimed at assessing the effectiveness of a new chemical mixture to extract different contaminants from soil.
- Multiple iterations of the same type of test required to obtain a reasonable level of certainty or statistical significance.

Grouping supporting R&D activities

Supporting R&D activities must be separated from core R&D activities in the registration application.

However, it is acceptable to group supporting R&D activities where they have a similar relationship to the same core R&D activity. It is also acceptable for a supporting R&D activity to support more than one core R&D activity. In this situation, the company must be careful to describe how each part of the supporting R&D activity is directly related to the core R&D activities.

If a company wants to group supporting R&D activities together it will need to ensure it can explain and demonstrate the direct relationship of each of the grouped supporting R&D activities to the relevant core R&D activity. If that relationship is not clear then the supporting R&D activity grouping may be too broad and/or require further explanation.

Eligibility assessment – AusIndustry can ungroup activities

Companies should be mindful that AusIndustry will apply the legislative requirements when conducting compliance reviews. This means, where necessary, AusIndustry on behalf of Innovation Australia may:

- a. ask for more detail of what the activities constitute; and/or,
- b. make separate decisions about different parts of grouped activities.

Below are some tips and considerations that may help companies to effectively register their activities and be prepared to respond to an AusIndustry compliance review if selected for one.³

² See the *R&D Tax Incentive: A Guide to Interpretation*.

³ For information on effective compliance and record keeping, and on AusIndustry's risk reviews see the online 'Compliance Readiness' guides at <http://www.business.gov.au/grants-and-assistance/innovation-rd/RD-TaxIncentive/ComplianceAssurance/Pages/default.aspx>.

Some useful tips:

1. Ask yourself whether an independent third party could understand what has been done from reading the description

A registration application should describe the activities so that an independent reader with no knowledge of the activities could understand what has been done. If a description does not clearly communicate to an independent reader how all of the elements of a core R&D activity fit together, the company should consider not grouping them in its registration.

2. Do not use vague or generic descriptions

Activity titles such as 'Feedback R&D' or descriptions that simply describe the generic development cycle of a product in a particular industry with the intention that many activities are included in that description often fail to describe what the activities actually are.

It is not sufficient to just describe the company's or the industry's general approach to product development. Nor is it sufficient to describe only the features of the product or service being developed without providing sufficient details of the experimental activities and other activities that were undertaken to develop the product or service.

Providing quantities such as the duration of activities, the number of test iterations, the volume of components produced, or the number of samples taken or tested, can help to register a clear description of an activity, especially grouped activities.

3. Align your registration application with your Advance or Overseas Finding

The titles and descriptions of the activities being registered should be aligned to those in any Advance or Overseas Finding Certificates. Where the company has an Overseas Finding⁴, companies should separate the overseas R&D activities from the Australian R&D activities. This will enable AusIndustry and the Australian Taxation Office to reconcile the activities more easily, potentially heading off unnecessary compliance reviews.

4. Separate supporting activities that are subject to the dominant purpose test

For any supporting R&D activity that is excluded from being a core R&D activity⁵, produces goods or is related to producing goods or services, it is best to keep this activity separate from all other activities.

This is because a company needs to be able to show that these activities are undertaken for the dominant purpose of supporting a core R&D activity as well as being directly related to that core R&D activity.

⁴ An Overseas Finding Certificate is required before companies can claim expenditure incurred on R&D activities undertaken outside Australia and its external territories (unless that expenditure is insignificant in the context of the Australian R&D activities). For questions relating to expenditure and when an Overseas Finding is required please contact the Australian Taxation Office.

⁵ Subsection 355-25(2) of the *Income Tax Assessment Act 1997* lists certain activities which cannot be core R&D activities. These are referred to as excluded activities. For more details refer to *The R&D Tax Incentive: A Guide to Interpretation*, page 27.

For further information on the R&DTI, visit www.business.gov.au/RDTI or contact us at: RDTI.Engagement@industry.gov.au