



Australian Government
Department of Industry and Science

Business



The R&D Tax Incentive

Overview

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Introduction

The R&D Tax Incentive is a broad-based, market driven program accessible to all industry sectors. It provides a targeted tax offset to encourage more companies to engage in research and development (R&D).

The *R&D Tax Incentive* aims to boost competitiveness and improve productivity across the Australian economy by:

- encouraging industry to conduct R&D that may not otherwise have been conducted;
- providing business with more predictable, less complex support; and
- improving the incentive for smaller firms to engage in R&D.

The *R&D Tax Incentive* replaces the *R&D Tax Concession* for R&D in income years commencing on or after 1 July 2011. The *R&D Tax Concession* continues to be administered for R&D in income years commencing prior to 1 July 2011.

What benefit does the R&D Tax Incentive provide?

The *R&D Tax Incentive* has two core components:

- a 45 per cent refundable tax offset (equivalent to a 150 per cent deduction) for eligible entities with a turnover of less than \$20 million per annum, provided they are not controlled by income tax exempt entities.
- a non-refundable 40 per cent tax offset (equivalent to 133 per cent deduction) for all other eligible entities¹. Unused non-refundable offset amounts may be able to be carried forward to future income years.

¹ The Australian Government has announced its intention to change the rates of assistance to 43.5 and 38.5 per cent respectively.

The Government has also committed to target access to the *R&D Tax Incentive* to entities with aggregated assessable income of less than \$20 billion. Both changes require legislation. More information is available from AusIndustry.

Part A · *Program administration*

Who administers the *R&D Tax Incentive*?

The *R&D Tax Incentive* is administered jointly by:

- AusIndustry (on behalf of Innovation Australia); and
- the Australian Taxation Office (the ATO).

Who is Innovation Australia?

Innovation Australia is a board established under the *Industry Research and Development Act 1986* (the IR&D Act) to administer a range of Australian Government innovation and venture capital programs.

Membership of Innovation Australia is drawn primarily from the private sector. Members' qualifications and experience cover a wide range of commercial and technical areas in various industries.

Innovation Australia manages the process for registering R&D activities, registering research service providers, and ensuring program integrity. Innovation Australia also makes decisions (in the form of 'findings') about R&D activities and registration.

Who is AusIndustry?

AusIndustry is a specialist program delivery division within the Department of Industry and Science. It delivers many programs designed to support the Australian business community through its customer service managers who are located in offices across Australia.

AusIndustry assists Innovation Australia by administering many aspects of the *R&D Tax Incentive*. Innovation Australia has delegated certain functions and decision-making powers to AusIndustry to enable it to perform this function.

Under these delegations AusIndustry administers the process for registering R&D activities, registering research service providers, and managing program integrity through education and compliance activities.

AusIndustry informs the business community about the *R&D Tax Incentive's* benefits and eligibility requirements through guidance material and its customer service manager network in offices across Australia. AusIndustry guidance material is available from business.gov.au.

Who is the ATO?

The ATO is the Australian Government's principal revenue collection agency. The ATO manages and shapes tax, excise and superannuation systems that fund services for Australians.

The ATO determines whether expenditure relating to, or assets used for, eligible R&D activities are eligible for the *R&D Tax Incentive*. The ATO also provides advice (including private binding rulings) and undertakes compliance activities as part of its administration of the *R&D Tax Incentive*.

Further information on claiming the *R&D Tax Incentive* as part of a company's income tax return is available on the ATO website ato.gov.au/randdtaxincentive.

Part B · *Applicant eligibility*

Who can apply?

The types of entities eligible for the *R&D Tax Incentive* are corporations (called 'R&D entities') that are:

- incorporated under an Australian law; or
- incorporated under foreign law but are Australian residents for income tax purposes; or
- incorporated under foreign law, and
 - are residents of a country with which Australia has a double tax agreement, including a definition of 'permanent establishment'; and
 - carry on business in Australia through a permanent establishment as defined in the double tax agreement.

Generally trusts are not R&D entities. The definition of R&D entities extends to body corporates in the capacity of trustees of public trading trusts, but not to trustees of any other sort of trusts.

What entities are not eligible?

The following entities are not eligible for the *R&D Tax Incentive*:

- non-incorporated entities (such as sole traders, partnerships and most trusts);
- those whose entire income is exempt from income tax; and
- corporate limited partnerships.

Companies who are uncertain about whether they are an eligible entity should contact the ATO.

How are consolidated or multiple-entry consolidated (MEC) groups treated?

If a company is part of a consolidated group (for income tax purposes) or a multiple-entry consolidated group, only the head company should register the R&D activities performed by members of their group. Subsidiary members cannot register their R&D activities in their own name, for the period they belong to a consolidated or multiple-entry consolidated group.

Head companies of consolidated groups also claim R&D tax offsets on behalf of the entire group.

Part C · Eligibility of R&D activities

R&D activities must meet certain criteria to be eligible for the *R&D Tax Incentive*. Eligible activities are categorised as either core R&D activities or supporting R&D activities.

What are core R&D activities?

Core R&D activities are experimental activities:

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

Further information on core R&D activities is available in the *R&D Tax Incentive – Eligibility of activities (core and supporting R&D activities) Information Sheet*.

Activities excluded from being core R&D activities

The following activities are excluded from being core R&D activities and they may only be claimed as 'supporting R&D activities' if they are undertaken for the dominant purpose of supporting core R&D activities:

- market research, market testing or market development, or sales promotion (including consumer surveys);
- prospecting, exploring or drilling for minerals or petroleum for the purposes of one or more of the following:
 - discovering deposits;
 - determining more precisely the location of deposits;
 - determining the size or quality of deposits;
- management studies or efficiency surveys;
- research in social sciences, arts or humanities;
- commercial, legal and administrative aspects of patenting, licensing or other activities;
- activities associated with complying with statutory requirements or standards, including one or more of the following:
 - maintaining national standards;
 - calibrating secondary standards;
 - routine testing and analysis of materials, components, products, processes, soils, atmospheres and other things;

- any activity related to the reproduction of a commercial product or process:
 - by a physical examination of an existing system; or
 - from plans, blueprints, detailed specifications or publicly available information;
- developing, modifying or customising computer software for the dominant purpose of use by any of the following entities for their internal administration:
 - the entity for which the software is developed, modified or customised;
 - an entity connected with the developer;
 - an affiliate of the developer, or an entity of which the developer is an affiliate.

What are supporting R&D activities?

An activity is eligible as a supporting R&D activity where:

- it is directly related to a core R&D activity; and
- in some scenarios, it has been undertaken for the dominant purpose of supporting core R&D activities.

What is directly related?

For an activity to be 'directly related', the activity needs to have a direct, close and relatively immediate relationship with the core R&D activities. Supporting R&D activities are usually required in order for the core R&D activities to take place. They can occur at a different location or time to the core R&D activities so long as they maintain the required relationship.

What activities are subject to the dominant purpose requirement?

Activities that must satisfy the dominant purpose requirement in order to be a supporting R&D activity are those that:

- are excluded from being core R&D activities (listed earlier); or
- produce, or are directly related to producing, goods or services (production activities).

Production activities can range from a once-off activity to mass production.

What is the dominant purpose requirement and how is it determined?

‘Dominant purpose’ means the prevailing or most influential purpose of an activity. In determining the dominant purpose, consideration is given to the overall circumstances within which the activities are conducted. It is possible that similar activities may be eligible in one context, but not in another. Companies need to consider:

- the extent to which the supporting R&D activities also achieve commercial or production outcomes in addition to assisting the conduct of the core R&D activities; and
- the importance of those non-R&D outcomes.

How are software activities treated?

Software is subject to the same eligibility tests as other forms of R&D, with the exception of certain software activities which are excluded from being a core R&D activity. This exclusion covers activities related to the development, modification or customisation of software where the software is for the dominant purpose of internal administration by the entity (or connected entities or affiliates) for which it was developed, modified or customised.

Software for ‘internal administration’ includes management information systems and enterprise resource planning software that is for use in the day-to-day administration of a business.

The software exclusion does not apply to software developed in-house that is of an applied nature, forming an integral part of an electrical or mechanical device (such as home appliances or industrial equipment).

Where can the R&D activities be conducted?

Generally only R&D activities conducted in Australia or the external Territories² qualify for the *R&D Tax Incentive*. However in certain circumstances, R&D activities conducted overseas may also qualify.

A company intending to claim a tax offset for R&D activities conducted overseas must apply to Innovation Australia for a decision (called a ‘finding’) about the eligibility of these overseas activities. Innovation Australia can issue a finding that overseas activities are eligible for the *R&D Tax Incentive* where it is satisfied that:

1. the activities are eligible as core or supporting R&D activities. Innovation Australia will be satisfied of this if the company has obtained an advance finding stating that the activities are eligible. Advance findings are discussed under Part D.
2. the activities to be conducted overseas have a significant scientific link to core R&D activities conducted in Australia that are registered or reasonably likely to be conducted and registered;
3. the activities cannot be conducted in Australia due to one of the following reasons:
 - conducting it requires access to a facility, expertise, or equipment not available in Australia;
 - conducting it in Australia would contravene a law relating to quarantine;
 - conducting it requires access to a population (of living things) not available in Australia; or
 - conducting it requires access to a geographical or geological feature not available in Australia.
4. the total expenditure on the activities conducted or to be conducted overseas in all income years is less than the total expenditure on certain R&D activities conducted or to be conducted in Australia in all income years.

The application should be made in the first income year that the overseas activities are conducted as it comes into force at the start of that income year. The application can also be made in advance of the company conducting the activity outside Australia. The application cannot relate to activities conducted in previous income years. The application form for findings about overseas activities is available on the business.gov.au website.

Further information on applying for overseas findings is available in the *R&D Tax Incentive – Overseas R&D Information Sheet* and *R&D Tax Incentive – Guide to Findings* on the business.gov.au website.

² Within this section, a reference to activities conducted in Australia should also be taken to be a reference to activities conducted in the external Territories.

For whom are the R&D activities conducted?

A company is only entitled to a tax offset for R&D activities conducted 'for' itself. There are some exceptions to this, where the activities are conducted for associated foreign corporations.

Who is entitled to claim the expenditure?

Generally, expenditure on R&D activities conducted to a significant extent for another entity will not be eligible for a notional deduction. A notional deduction is an amount that a company can take into account in calculating their tax offset. Notional deductions are discussed under Part E.

The requirement that a company's eligible expenditure be on R&D activities conducted for it, and not to a significant extent for some other entity, is intended to limit claims to cases where the company is the major benefactor from its expenditure on those activities. In some cases it will also prevent duplication of claims by different entities where essentially the same activities are involved.

Determining who is the major benefactor

The major benefactor of expenditure on R&D activities is determined by examining the extent to which R&D activities are conducted for the R&D entity compared to the extent to which they are conducted for any other entity.

This is tested by weighing up three key criteria concerning who:

- 'effectively owns' the know-how, intellectual property, or other results arising from the R&D entity's expenditure on the R&D activities;
- has appropriate control over the conduct of the R&D activities; and
- bears the financial burden of carrying out the R&D activities.

Exceptions to the rule

There are some exceptions where an entity may be able to claim a tax offset for activities conducted on behalf of other entities. For example, an offset can be claimed where R&D activities are conducted:

- on behalf of one or more foreign residents provided that the foreign resident is from a country with which Australia has a comprehensive double taxation agreement; or
- for the body corporate carrying on business through a permanent establishment for the body corporate (rather than for that permanent establishment)

and the activities are conducted under a written agreement between the entities.

There are strict conditions regarding when these exceptions may apply. If this applies to you, further information is available on the ATO website, including in the ATO *Research and development tax incentive – for whom are the R&D activities conducted?* fact sheet.

Part D · *The application process*

How do I access the R&D Tax Incentive?

Companies access the *R&D Tax Incentive* by a two-stage process that involves:

1. **Registering:** Register R&D activities with AusIndustry (on behalf of Innovation Australia); and
2. **Claiming:** Claim the tax offset in your company's annual income tax return. The tax return must be accompanied by the ATO's *R&D Tax Incentive* Schedule detailing the R&D expenditure incurred.

Note: A company is not eligible to claim the *R&D Tax Incentive* unless its R&D activities have been registered for the relevant income year. Companies must register for the *R&D Tax Incentive* prior to submitting its annual tax return.

When do I register?

Annual registration of a company's R&D activities is a prerequisite for claiming the *R&D Tax Incentive*.

Companies have ten months from the end of their income year to lodge their application for registration of R&D activities conducted in the previous year. Innovation Australia may allow a further period to submit a company's registration application in exceptional circumstances.

What is the registration process?

Applications for registration may be lodged online or through any AusIndustry office.

Registration applications are processed by AusIndustry. Registration applications submitted online are processed and reviewed more quickly than hardcopy applications. AusIndustry's Customer Service Charter standard is 10 days to register an online application compared to 30 days for a paper application.

A unique registration number is given to the company for each income year in which it registers its R&D activities. When a company claims a R&D tax offset in their income tax return, they must quote their registration number on the accompanying *R&D Tax Incentive* Schedule.

Innovation Australia, or AusIndustry through its delegated powers, may refuse registration if the activities described in the application are not eligible R&D activities, or if the application is received after the deadline.

What if a third party assists with my registration or claim?

AusIndustry neither encourages nor discourages the use of an agent to assist with completing a company's application for registration. Companies should however ensure that service providers they deal with are registered Tax Agents if they provide tax agent services (such as preparing a registration form) for a fee, or engage in other conduct connected with providing such services.

Information on tax agents is available from the Tax Practitioners Board website tpb.gov.au.

What is an 'advance finding'?

Innovation Australia can make a number of decisions (in the form of findings) that affect a company's ability to register and claim tax offsets for expenditure on eligible R&D activities. One such decision is an advance finding about the eligibility of R&D activities before registration. Other types of findings can also be made at the time of registration or once activities have been registered³.

An advance finding is intended to increase certainty for a company in relation to whether Innovation Australia considers their planned R&D activities are eligible under the program. An advance finding by Innovation Australia binds the ATO for the year the application was made, and the next two income years.

In an advance finding, Innovation Australia may find that an activity is eligible, ineligible, or may refuse to make a finding.

Should I apply for an advance finding?

A company requesting an advance finding should weigh up the benefits of receiving certainty about the eligibility of the activities against the time, effort, and cost of seeking that certainty.

A company will still need to register their R&D activities annually to claim the *R&D Tax Incentive* even if they have an advance finding covering those activities. An advance finding is not the same as registration and is not a substitute for registration.

If the company, having received an advance finding, conducts an activity which differs materially from that described in the advance finding, the advance finding will not apply to that activity.

³ Findings are discussed in Part F 'Assessment of R&D activities and expenditure'.

Companies may wish to consider applying for an advance finding where:

- it is unsure about the eligibility of particular activities; and/or
- it wants to rely on the advance finding for securing support (financial or otherwise) for the conduct of the commercial project.

Companies should only apply if they will be able to provide the information required to support an advance finding application.

When is it possible to apply for an advance finding?

A company may apply to AusIndustry (on behalf of Innovation Australia) for an advance finding in relation to activities conducted or completed in the current income year, and proposed activities that are reasonably expected to be conducted in the current or next two income years.

An application should be made in the income year that the relevant activity was or will be conducted. The application can also be made up to two income years before the activity is conducted.

On receipt of an application for an advance finding, AusIndustry staff will conduct a formal assessment of whether the described activities meet the eligibility requirements and provide a recommendation to Innovation Australia so that it can make a decision (the finding).

More information on advance findings is available in the *R&D Tax Incentive – Guide to Findings* on the business.gov.au website.

How do I claim the R&D Tax Incentive?

The *R&D Tax Incentive* is claimed through the company's income tax return at the end of the company's income year. To claim, the company must complete and lodge the *R&D Tax Incentive* Schedule along with its income tax return. The *R&D Tax Incentive* Schedule must include the company's registration number for the relevant income year. Company income tax returns and *R&D Tax Incentive* Schedules are available on the ATO website ato.gov.au from 1 July each year.

What type of R&D tax offsets can I claim?

The type of R&D tax offset a R&D entity can claim depends on whether their aggregated turnover is less than the threshold of \$20 million and the extent to which they are controlled by exempt entities.

'Aggregated turnover' is defined in the small business entity provisions of income tax law. It is the sum of the annual turnovers of:

- the R&D entity;
- any entity connected with the R&D entity; and
- any entity affiliated with the R&D entity, excluding any dealings between those entities.

For more information about the concepts 'affiliate' and 'connected with' refer to the ATO website.

The *R&D Tax Incentive* provides eligible entities (called 'R&D entities' – see Part B) with a tax offset for expenditure on, or the decline in value of depreciating assets used in, eligible R&D activities. It has two core components:

- a 45 per cent refundable tax offset (equivalent to a 150 per cent deduction) for eligible entities with an aggregated turnover of less than \$20 million per annum (unless they are controlled by tax exempt entities); and
- a non-refundable 40 per cent tax offset (equivalent to 133 per cent deduction) for all other eligible entities.⁴

Eligible entities accessing the non refundable tax offset can carry forward any unused offset amounts subject to the tax offset rules.

For more information about 'control by a tax exempt entity' refer to the ATO website.

How does a refundable tax offset affect my tax liabilities?

If the R&D tax offset is a refundable tax offset, the normal income tax rules for refundable tax offsets apply. These include the priority rules about how a taxpayer's tax offsets must be applied against their basic income tax liability. A refundable tax offset is applied after all other tax offsets, except the tax offset that arises from the payment of franking deficit tax.

If there is an excess of tax offset, the taxpayer is entitled to a refund, subject to the rules on how the ATO must apply credits, including refunds, to a running balance account or against a particular tax debt.

How does the R&D non-refundable tax offset affect tax liabilities?

If the R&D tax offset is a non-refundable tax offset, it is applied against basic tax liability before refundable tax offsets and the tax offset that arises from the payment of franking deficit tax, but after all other tax offsets (such as a foreign income tax offset). A R&D entity may carry forward any unused non-refundable tax offset to be used in a later year, provided that it satisfies the tax offset carry-forward rules.

⁴ The Australian Government has announced its intention to change the rates of assistance to 43.5 and 38.5 per cent respectively.

The Government has also committed to target access to the *R&D Tax Incentive* to entities with aggregated assessable income of less than \$20 billion. Both changes require legislation. More information is available from AusIndustry.

Part E · *Eligibility of expenditure*

What notional deductions can a R&D entity take into account?

Eligible R&D amounts that a R&D entity can take in account in calculating their offsets are referred to as 'notional deductions'. Notional deductions are subject to the eligibility criteria referred to previously (including those in relation to 'for whom' the R&D activities are conducted, and the location of the R&D activities), and may include the following amounts:

1. expenditure incurred, to the extent it is incurred on eligible, registered R&D activities;
2. the decline in value of depreciating assets used for R&D activities;
3. balancing adjustments for depreciating assets used only for R&D activities;
4. expenditure incurred to an associate in an earlier income year, but paid in the current year (subject to restrictions);
5. a partner's proportion of expenditure incurred by a R&D partnership on eligible, registered R&D activities, and the decline in value of, and balancing adjustments for, R&D partnership assets; and
6. monetary contributions made under the Cooperative Research Centre (CRC) program.

R&D expenditure

Assuming program eligibility requirements are met, expenditure incurred on R&D activities and other activities needs to be apportioned to ensure that amounts are only included as notional deductions to the extent they are incurred on eligible R&D activities.

For example, expenditure on salary and superannation contributions for an employee who works partly on R&D activities should be apportioned to determine the eligible R&D portion.

Exclusions include expenditure in relation to buildings, interest, expenditure on core technology and expenditure incurred to associates not paid in the year the expenditure was incurred. See the later section on 'What expenditure cannot be claimed' for further details.

Notional deductions in relation to depreciating assets

A R&D entity is entitled to a notional deduction for the decline in value of depreciating assets if it:

- uses the asset for the purpose of conducting registered R&D activities; and
- would be entitled to deduct an amount under the depreciating asset provisions of Division 40 of the *Income Tax Amendment Act 1997* (ITAA 1997) if those provisions applied with certain changes as outlined in section 355-310 of the ITAA 1997.

If the asset is used for a purpose other than the R&D activities, the amount claimed must be reduced to the extent that the asset is used for that non-R&D purpose. However, the R&D entity may be entitled to a tax deduction for that other use separate to the *R&D Tax Incentive*. For example, if the asset is used in carrying on a business for the purpose of producing assessable income.

Balancing adjustments for depreciating assets used solely for R&D activities may be taken into account as a notional R&D deduction.

Expenditure incurred to an associate

If a R&D entity incurs and pays an amount of expenditure to an associate in the same income year, that amount is claimable in the income year that the expenditure was incurred and paid (assuming other eligibility conditions are satisfied).

Expenditure incurred to an associate in an earlier income year, but paid in the current year (subject to restrictions) may only be claimed as a notional deduction in the income year in which it is paid.

However, if the R&D entity does not pay the amount incurred until a later income year, the entity has a choice:

- it can deduct the amount in the income year the expenditure was incurred under the normal income tax provisions; or
- it can claim the amount paid to the associate under the R&D provisions in the year of payment.

The entity must make this choice by the time it lodges its income tax return for the most recent income year before the income year in which it paid the amount.

If the R&D entity has claimed a deduction for this expenditure in an earlier income year, it forgoes any entitlement to claiming under the R&D provisions in the year of payment. This cannot be reversed, for example, by later requesting an amendment of the assessment to disallow the deduction claimed.

R&D Partnerships

Under the *R&D Tax Incentive*, a tax offset is available to a R&D entity that is a partner in a R&D partnership. A R&D partnership is a partnership in which each of the partners is a R&D entity.

The partner can claim notional deductions for their proportion of expenditure incurred by a R&D partnership on R&D activities, and the decline in value of, and balancing adjustments for, R&D partnership assets.

The central consideration is the partner's proportion of various amounts, including expenditure, attributable to the R&D partnership. The proportion is the partner's interest in the net income or loss of the R&D partnership, unless the partners have agreed that the partners should bear or be entitled to a different proportion.

Under this rule, a R&D entity that is a partner in a R&D partnership will be able to claim a tax offset for that portion of the R&D partnership's R&D expenditure, if the eligibility conditions are met.

CRC contributions

Monetary contributions that a R&D entity incurs out of its own funds (and not out of government funding) under the CRC program may be able to be claimed as a notional deduction.

The R&D entity can only claim the monetary contribution it incurs under the CRC program once it is actually registered for the activities on which the contribution is spent. In some cases, this contribution is incurred in the income year prior to when the entity is registered. In these cases the notional deduction still applies to the year in which the expenditure is incurred, but the entitlement to that notional deduction does not arise for that year until the entity is registered for those activities.

Special rules operate to prevent double benefits being claimed in respect to the same transactions.

More information on these notional deductions is available on the ATO website.

What adjustments may apply to my R&D amounts?

What if I'm entitled to a R&D grant or recoupment?

A clawback adjustment may apply where a R&D entity receives, or becomes entitled to receive, a recoupment (including a grant) from an Australian government agency or State/Territory body that relates to R&D activities, unless the recoupment is received or receivable under the CRC program.

Where this occurs, the company will have to pay extra income tax at 10 per cent of the recoupment (subject to a cap equal to the R&D part of the grant). The extra income tax is payable for the year in which the recoupment is received or receivable, regardless of whether the related R&D tax offset benefit was used in the same, earlier or later income years. Therefore, the clawback adjustment may result in retrospective amendment of past income tax assessments.

More information is available on the ATO website.

What if my R&D activities produce tangible products? (commonly known as feedstock adjustments)

The feedstock provisions adjust the *R&D Tax Incentive* that is available in relation to certain inputs to R&D activities, to reflect the value of related outputs obtained from those activities. The feedstock adjustment includes an amount in a R&D entity's assessable income. It applies in relation to expenditures on goods or materials (feedstock inputs) that are transformed or processed during R&D activities that produce one or more tangible products which are subsequently sold or applied for the company's own use, and expenditures on energy directly input into that transformation or processing, to the extent that this expenditure is a notional deduction.

The feedstock adjustment involves a comparison of the amounts claimed for feedstock inputs, including energy expenditure, with the feedstock revenue associated with related feedstock outputs. The adjustment is done by including an amount in assessable income for the income year in which the adjustment is triggered (i.e. the year the feedstock output is sold or applied to internal use). The amount included in the assessable income is one third of the lesser of the relevant notional deduction and feedstock revenue. The intention is to 'claw back' the benefit from the *R&D Tax incentive* that is enjoyed on the recouped notional deduction.

More information on feedstock adjustments, including how they are calculated, is available on the ATO website.

How does the Goods and Services Tax (GST) affect my notional deductions?

If a company is registered for GST it can claim a GST input tax in relation to its R&D expenditure. The amount of this input tax credit is excluded from its calculation of its notional deductions. If a company is not registered for GST, and hence not entitled to claim input tax credits, this exclusion does not apply.

What expenditure cannot be claimed?

The following types of expenditure are expressly excluded from being claimed under the *R&D Tax Incentive*.

1. Expenditure incurred to acquire or construct a building (or part of a building or an extension, alternation or improvement to a building).

There is an exception for expenditure on a building, or part of a building, that is plant. That expenditure is specifically excluded from Division 43 of the ITAA 1997 and so a building (or part thereof) that is plant is subject to the depreciating asset rules in Division 40 of the ITAA 1997. Consequently, a R&D entity may be able to obtain a notional R&D deduction for the decline in value of a building, or more commonly part of a building, that is plant.

2. Expenditure included in the cost of a tangible depreciating asset for the purposes of working out the notional decline in the value of the asset under the *R&D Tax Incentive*. This simply reflects that the R&D depreciating asset rules have priority over the expenditure rules.
3. Expenditure incurred for interest payable to an entity.
4. Expenditure on acquiring core technology cannot be claimed.

Core technology includes technology acquired for the purpose of R&D activities directed towards obtaining new knowledge based on that technology, or creating new or improved things (for example, materials, products, devices or processes) based on that technology.

The exclusion does not extend to expenditure that the entity incurs in developing the technology itself. A R&D entity or the ATO may apply to AusIndustry (on behalf of Innovation Australia) for a finding about whether particular technology is core technology.

Further information is available in the *R&D Tax Incentive – Core Technology Information Sheet*.

5. Expenditure that is not at risk (for example, if there is guaranteed return under a financing arrangement or an indemnity).

This does not apply to:

- R&D activities conducted by the R&D entity for one or more foreign corporations that are related to the R&D entity; or
- where activities are conducted by a foreign corporation through a permanent establishment in Australia for other parts of the corporation.

6. Expenditure incurred to an associate in a year, but not paid in that year (refer to 'Expenditure incurred to an associate' discussed previously).

These excluded expenditures need to be considered under the normal deduction provisions of the income tax law.

What are the minimum notional deductions for claiming a R&D tax offset?

A company must have notional deductions for an income year of at least \$20 000 in order to claim a R&D Tax offset.

However, this threshold does not apply in cases where:

1. expenditure is incurred to a Research Service Provider (that is not an associate of the R&D entity) registered with AusIndustry (on behalf of Innovation Australia); and/or
2. expenditure is incurred as a monetary contribution made under the CRC program.

Effect on calculation of taxable income.

If an amount is used to calculate an entity's entitlement to the R&D tax offset, it cannot also be used as a deduction against the company's taxable income. The reason an entity cannot deduct this amount is because they would result in getting a double benefit – both a deduction and a tax offset – for the same amount of expenditure or decline in value.

Who are Research Service Providers?

A Research Service Provider (RSP) is an organisation approved by Innovation Australia that has appropriate scientific or technical expertise and resources to perform R&D on behalf of eligible companies or groups of companies.

RSPs help small to medium-sized companies identify and gain access to expert R&D resources in particular fields. Collaborating with RSPs enables companies to conduct R&D activities without having to invest in the specialist staff or infrastructure needed to support such activities. Companies can contract R&D activities to RSPs with confidence since all RSPs must meet a set of criterion to qualify for registration.

An advantage of contracting R&D activities to a RSP is that the *R&D Tax Incentive* expenditure threshold of \$20,000 does not apply to notional deductions for R&D activities contracted to a RSP.

Further information relating to RSPs is available on the business.gov.au website.

Who are Cooperative Research Centres?

The CRC program is a program administered by the Australian Government that links researchers with industry to focus R&D efforts on addressing major challenges, and progress R&D products towards utilisation and commercialisation. A CRC is an incorporated or unincorporated organisation, formed through medium to long-term collaborative partnerships between publicly-funded researchers and end users. CRCs must comprise at least one Australian end-user (either from the private, public or community sector) and at least one Australian higher education institution (or research institute affiliated with a university).

Special rules apply to claiming CRC contributions for the *R&D Tax Incentive* (refer to 'CRC contributions' discussed previously). Further information can be found on the ATO website.

What if I contract to others?

A company can contract to an organisation or person other than a RSP for the performance of its R&D activities. In these circumstances, however the company can only claim the *R&D Tax Incentive* if it has incurred notional deductions for an income year of at least \$20,000 (i.e. the company is subject to the \$20,000 annual threshold).

In these circumstances, the company contracting the R&D (or the relevant foreign company in the case of foreign owned R&D) should comply with the eligibility requirements regarding 'for whom' the R&D activities must be conducted, as discussed earlier.

Part F · *Assessment of R&D activities and expenditure*

How is eligibility of R&D activities assessed?

When applying for registration, a R&D entity self-assesses whether the activities it conducted in an income year are eligible core R&D activities or supporting R&D activities.

As the *R&D Tax Incentive* is a self-assessment program, the majority of applications to Innovation Australia will be registered by AusIndustry without formal examination of the eligibility of the described activities. Registration of activities does not indicate that Innovation Australia has accepted that the activities are eligible R&D activities.

The AusIndustry compliance model

AusIndustry's compliance model aims to assure the ongoing integrity of the *R&D Tax Incentive*. The model's framework includes the monitoring of registration trends and behaviours to ensure taxpayers receive benefits to which they are entitled with minimal compliance burden.

AusIndustry provides education and guidance material to help companies better understand how to meet their obligations under the program. After registration of activities, AusIndustry regularly selects companies for compliance reviews based on perceived levels of the risk of non-compliance.

Minimising the compliance burden invariably depends on the quality and integrity of business systems that companies implement to meet their compliance requirements under the program. Companies can work with AusIndustry by ensuring that their records and business processes are 'compliance ready'.

Companies should make sure that they understand their obligations under the *R&D Tax Incentive* by referring to education and guidance materials, or seeking advice from AusIndustry. Detailed information on AusIndustry's compliance model is available from the business.gov.au website.

The finding process

As referred to in Part D, Innovation Australia may make an advance finding about the eligibility of activities before registration. In addition, other findings may be made at the time a company seeks to register activities or once activities have been registered. Findings may arise in three ways:

1. **Innovation Australia initiated:** Innovation Australia may initiate a finding about an application for registration, or activities that have been registered.
2. **ATO request:** The ATO may request findings on activities that have been registered.
3. **Company request:** A company may request findings as to whether their registered activities are eligible R&D activities.

Applicants will be advised in writing of Innovation Australia's decisions relating to findings. The notice will include one or more certificates in relation to the decisions made. These findings are binding on the ATO.

More information on findings is available in the *R&D Tax Incentive – Guide to Findings* on the business.gov.au website.

The ATO compliance program

The ATO takes a risk-management approach to compliance and are increasing efforts to differentiate engagement with taxpayers based on the relative likelihood of non-compliance and the consequences of this behaviour. The ATO will verify compliance via risk reviews and audits where it believes the likelihood of non-compliance is higher and will also seek assurance that compliance is occurring where the consequences are relatively high.

For further information on the ATO compliance program visit ato.gov.au.

What time periods apply to amendments and objections to assessments of eligibility of R&D expenditure?

There is a limited time in which the ATO can amend an assessment for claiming the *R&D Tax Incentive*. Generally the ATO has four years from the time of giving notice of an assessment to amend an assessment. This period is reduced to two years for some smaller taxpayers. There are however, special amendment periods allowing the ATO to amend an assessment outside of these normal periods.

Where a certificate setting out a finding is given to the ATO, the ATO has an additional two years after the certificate is given to amend an assessment if giving effect to the certificate increases the R&D entity's tax liability. The ATO may amend the assessment at any time where giving effect to the certificate results in reducing the company's liability.

Reviews

Can I seek an internal review of Innovation Australia decisions?

Companies whose interests are affected by certain decisions made by Innovation Australia may apply for an internal review of that decision. These decisions are referred to as reviewable decisions under the legislation.

Applications for internal review must be in the approved form and made within 28 days of notification of the decision (or a further period as Innovation Australia allows). The ATO can also apply for internal review of a reviewable decision at any time. Examples of reviewable decisions include decisions to register or refuse to register activities, and those relating to 'findings'.

If Innovation Australia does not complete its review within 90 days, it is deemed to have confirmed the original decision. However, if Innovation Australia subsequently makes a decision, the 'deemed decision' will be taken not to have been made (unless a company has already applied to the Administrative Appeals Tribunal for a review of the deemed decision).

What happens if I am still unhappy with the outcome of an internal review of an Innovation Australia decision?

Companies that disagree with an internal review decision, including deemed decisions, can apply to the Administrative Appeals Tribunal (the AAT) for a further review of that decision.

An application for review by the AAT must be made within 28 days of receiving notification of the internal review decision or, in the case of a deemed decision, within 28 days from the time the internal review decision was deemed to have been made. Application forms and advice about applying for an AAT review are available at the AAT's website www.aat.gov.au.

Can I seek an internal review of ATO decisions?

If a company is dissatisfied with the amount of a tax offset allowed by the ATO, they may object within the normal timeframes and subject to the usual rules which apply to income tax objections. An objection is considered internally, by an ATO officer independent of those involved in the original decision.

Special rules apply for objections to 'nil' assessments. Where a R&D entity has a nil assessment, having applied the refundable R&D tax offset, it can object to the amount of the refundable R&D tax offset. However where the non-refundable R&D tax offset has been applied in a nil assessment, the R&D entity will have to wait until they have an assessment for the year in which any part of their non-refundable R&D tax offset carried forward is first applied, to object to the amount of that offset.

A company can ask for an objection decision of the ATO to be reviewed by applying to either the AAT or the Federal Court. Applications of this type need to be lodged within 60 days of service of the objection decision.

Part G · *Company requirements and obligations*

Good record keeping is required

Companies intending to access the *R&D Tax Incentive* must keep records that sufficiently demonstrate to both AusIndustry and the ATO that:

- they carried out eligible R&D activities;
- they incurred eligible expenditure in relation to those activities; and
- their R&D activities and expenditure met all legislative requirements for eligibility under the program.

In deciding what records are required in order to demonstrate eligibility under the *R&D Tax Incentive* a company should consider each aspect of the eligibility requirements for the program. A company should then consider which records are appropriate to demonstrate compliance in the context of their particular business.

Good record management helps a company self-assess its eligibility, meet its compliance obligations, and potentially identify new areas where it can access the benefits of the *R&D Tax Incentive* program. It also assists the company to conduct its work and re-visit ideas, processes and solutions in future. If the company seeks to commercialise its work, potential investors will expect to have access to a wide variety of records.

Maintaining these documents is advantageous to companies as it will minimise the costs that may be associated with a compliance review.

Further information regarding record keeping is available on the business.gov.au and ATO websites.

Part H · Assistance for companies

How do I know if I am eligible?

Applicants need to self assess their eligibility for the *R&D Tax Incentive*. If you require certainty in relation to your eligibility, you may wish to seek an advance finding about your activities from Innovation Australia or a private binding ruling from the ATO about your eligibility to claim a notional deduction.

Some of the issues you need to consider in self-assessing your entitlement include the following:

- Are you an eligible entity?
- Are the activities being undertaken experimental activities? Experiments can take place in a range of settings, from a separate laboratory to an otherwise normal production line.
- Can the outcome of the experiments be known or determined in advance on the basis of publicly available knowledge, information or experience? You will need to indicate how you established this knowledge gap.
- Where are the activities being undertaken? If they are being undertaken overseas, you will need to obtain an overseas finding.
- For whom are you conducting the activities? A company is only entitled to a tax offset for R&D activities conducted 'for' itself. There are some exceptions to this, where the activities are conducted for associated foreign corporations.
- Do you have notional deductions of \$20,000 or more? If not, have you contracted the activities to a registered Research Service Provider (RSP), or made a monetary contribution under the CRC program?
- Do you have appropriate records and evidence of conducting eligible R&D activities to substantiate your claim?

Where can I find further information?

Further information on the *R&D Tax Incentive* is available on both the business.gov.au and ATO websites and in a series of information and fact sheets on:

- Registration
- Eligibility of activities (core and supporting R&D activities)
- Overseas R&D
- Advance Finding
- Core Technology
- Record-Keeping and R&D Planning
- How do I register as a RSP?
- How do I access a RSP?
- Refundable and non-refundable tax offsets
- Expenditure incurred to an associate
- Grouping for aggregated turnover purposes
- For whom are the R&D activities conducted?
- Feedstock adjustments
- Clawback adjustment

AusIndustry and the ATO can also attend to phone queries and provide guidance or refer you to where you can find more information.

Contact information for AusIndustry and the ATO is available under the heading 'Where do I go for more information?'

Two final points to remember

- You may not claim the *R&D Tax Incentive* in your company tax return unless your R&D activities have been registered for the relevant income year.
- Applications for registration must be lodged within 10 months after the end of the year of income in which the R&D activities were conducted.

Disclaimer

The material in this document aims to provide general guidance only. The intention of the guidance material is to provide useful information that will assist taxpayers seeking to claim the tax offsets available under the *R&D Tax Incentive*. However, it is by no means exhaustive or in the nature of definitive legal or financial advice. The guidance material cannot and does not purport to extend or supplement the operation of the legislation. Any examples provided in the guidance material are for illustrative purposes only and are not an exhaustive statement of the application of the legislation to any particular fact situation.

It is up to you and your advisers to manage your financial and tax affairs, and to ensure the accuracy of any information that you provide concerning your claims. You are also responsible for keeping yourself informed of any changes to the law that may affect your rights and responsibilities in claiming the *R&D Tax Incentive* for R&D activities.

Where do I go for more information?

For information on registration, eligibility of R&D activities and findings, contact AusIndustry

Visit the 'Contact Us' page on the business.gov.au website for full details on how to contact us via phone (**13 28 46**), email or web chat.

For information on eligible entities and amounts you can claim contact the ATO

- Visit the website | ato.gov.au/randdtaxincentive
- Call the ATO | **13 28 66** between 8.00am and 6.00pm Monday to Friday
- Email the ATO | innovation@ato.gov.au

If you are a tax agent, call **13 72 86** and select the relevant fast key code.

If you do not speak English well and want to talk to a tax officer, phone the Translating and Interpreting Service on **13 14 50** for help with your call.

If you have a hearing or speech impediment and have access to appropriate TTY or modem equipment, phone **13 36 77**.

If you do not have access to TTY or modem equipment, phone the Speech to Speech Relay Service on **1300 555 727**.

