CHAMBER OF COMMERCE AND INDUSTRY QUEENSLAND SUBMISSION

R&D Tax Incentive Review Panel Report

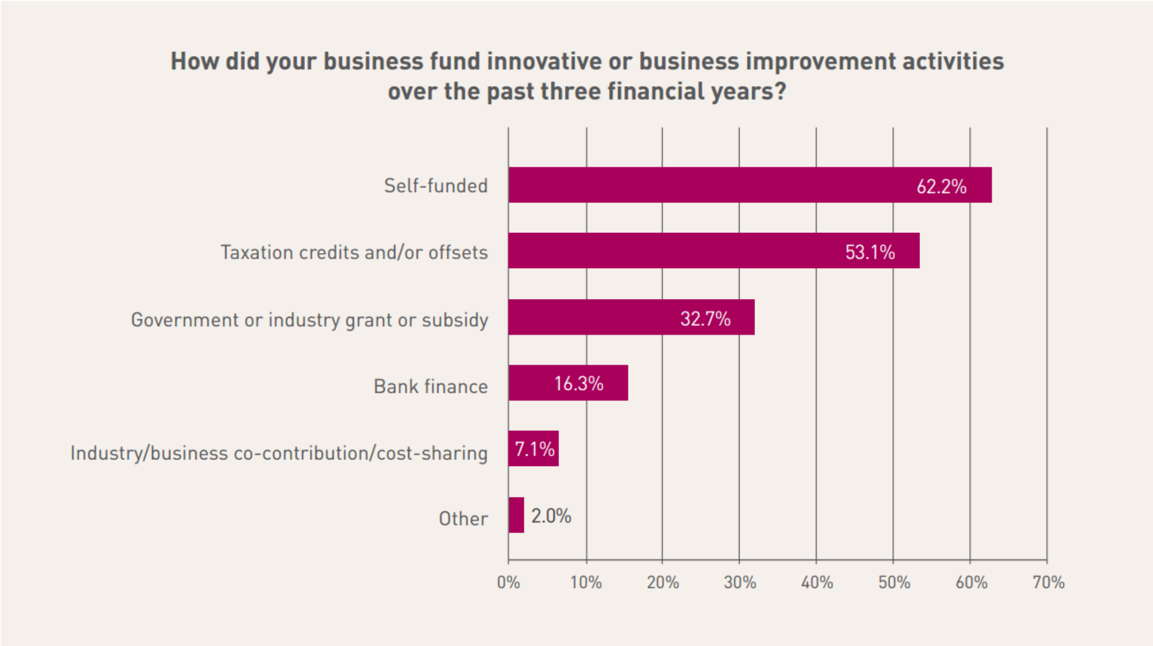
Department of Industry, Innovation and Science

OCTOBER 2016

Powering business potential

Introduction

1. The Chamber of Commerce and Industry Queensland welcomes the opportunity to provide feedback to the Department of Industry, Innovation and Science on the *R&D Tax Incentive Review Panel Report*.
2. The importance of continued support for research and development is critical for Australia's innovation ecosystem as well as for the growth of our over 2 million small businesses.
3. Government backing for research will mean Australia can maintain our position in the top 15 countries for research and development (Global Innovation Index, 2016), as well as work closer to translating local research and innovations into commercial opportunities.
4. It has been rightly identified that there are further opportunities to improve the effectiveness and integrity of the R&D Tax Incentive, which is fundamental to shaping Australia's future 'knowledge' economy.
5. The panel made six recommendations to improve the R&D tax incentive:
    1) A premium rate of up to 20 per cent for collaborative R&D projects with publicly-funded research organisations (such as universities), and for the costs of employing new STEM PhD graduates for the first three years of their employment;
    2) Retaining the current definition of eligible activities and expenses, but developing new guidance to clarify the scope of the program;
    3) A cap of $2 million on the annual cash refund payable under the R&D Tax Incentive for companies with a turnover under $20 million;
    4) An intensity threshold of 1 to 2 per cent for larger companies, such that only R&D expenditure in excess of the threshold attracts a benefit;
    5) Increase the expenditure threshold to $200 million should the intensity threshold be introduced; and
    6) Investigating options to improve the administration of the R&D Tax Incentive.
6. It is evident many businesses have considered the current R&D tax incentive scheme when it comes to making long-term investments. For small businesses and early-stage start-ups, the incentive scheme plays a crucial part in product development.
7. In a CCIQ survey conducted in 2013, it was found that having adequate financial resources is a prerequisite to increasing levels of innovation activity. When asked how small businesses funded innovative or business improvement activities between 2010-2013, more than 1 in 2 businesses relied on taxation credits and/or offsets.



Source: CCIQ Innovation Survey 2013

8. Furthermore, throughout the wider reform, the Government will need to be mindful of sustaining Australia's international tax competitiveness and the importance of collaboration between business and publicly-funded research bodies going forward.

Focus lacking on small business and start-ups

9. CCIQ's main concern is in relation to the recommended cap of $2 million on the annual cash refund payable under the R&D Tax Incentive scheme for businesses with a turnover of less than $20 million.
10. First, the $20 million turnover limit in the incentive was solely introduced to limit the availability of the cash refund option for loss making companies, rather than as a definition for an SME. According to the ATO, the definition of an SME is a business with a turnover of $250 million or less. As such, many SMEs who wish to access the R&D tax incentive may be excluded from doing so.
11. Furthermore, the cap will mean yet another cut which has occurred every year for the past decade. The incentive scheme undoubtedly needs a greater level of stability if it is to deliver sustained higher investment in innovation.
12. It could be said that the "considerable growth" on the cash refund payable to start-ups and SMEs could in fact be viewed as a success of the program and an effective incentive strategy for R&D, rather than as threat to the program.
13. It is understood that the program needs to remain financially sustainable through appropriate risk management and reducing the ability for the program to be rorted. This "tightening" however has seen to be targeted too heavily towards the start-up and SME cohort.

14. At the same time a cap has been placed on incentives for SMEs, a recommendation has been put forward to *increase* the expenditure threshold to $200 million for large corporations who could equally take advantage of the available tax incentives.
15. Small businesses could be justified in saying that the R&D tax incentive will continue to be largely about subsidising big corporations to produce their own commercial products (R&D which would have occurred in any case), instead of targeted at the small end where every dollar spent is a dollar of R&D that wouldn't be happening otherwise.
16. Every dollar spent on small businesses and start-ups would translate directly into jobs and additional R&D being conducted. Furthermore, R&D at the small business and start-up end is considered to be about more innovative research, development and most importantly commercialisation.
17. However, it is not to be suggested that there be no increase in the proposed R&D the expenditure threshold to $200 million for large corporations. Globally, Australia is still behind in terms of government financing for R&D and therefore additional support is always welcomed.

Proposed funding arrangement

18. A 12-month wait for the cash refund is considered far too lengthy and significantly diminishes the ability of small and new businesses to compete. Often, these businesses need to grow quickly and a year without sustainable funding can make a huge difference.
19. It is recommended that the R&D refunds should be paid quarterly as start-ups and small businesses need the cash injection more regularly than their larger company counterparts. This is disseminated into creating more jobs and directly into more R&D.
20. Recent research has found about 60 per cent of SME loan applications through banks are rejected every year, mostly because they don't fit with a bank's risk bias or were poorly presented by the borrower or broker.
21. Many small businesses avoid this path altogether as it could result in a bad credit rating simply because their lending history shows that they failed to secure a bank loan in the past.
22. As a result of irregular cash injections and a reluctance from banks to assist in this space, many businesses are seeking loans from new fintech companies, who while assisting tremendously, often charge high interest rates to account for taking on the greater risks.
23. There exists here an apparent market failure to which government can assist, simply with a number of minor changes to the funding arrangements and the cap on annual cash refunds for small business under the R&D Tax Incentive scheme.

Conclusion

24. Critically important for Australia is the need to boost our R&D capacity for all businesses, regardless of size. More can be done to accelerate the transfer and commercialisation of R&D outputs which includes providing easier access to publicly funded research data.
25. The traditional closed systems do not allow the type of innovation of realisation of its benefits that are required in today's global marketplace. However, encouraging open innovation must coincide with improvements in the management of intellectual property and other legal risks.
26. We thank the Department for the opportunity to provide comment and welcome any feedback. Please contact Catherine Pham, Policy Advisor, at cpham@cciq.com.au for matters relating to this submission.