RSM Australia Submission to:

Senate Standing Committees on Economics,

Treasury Laws Amendment (Research and Development Incentive) Bill 2018 and Explanatory Materials

5 November 2018

[redacted]

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

RSM appreciates the opportunity to make a submission to the ***Senate Inquiry into Treasury Laws Amendment (Making Sure Multinationals Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2018*** and specifically the contained cuts to the R&D Tax Incentive.

RSM Australia (RSM) is one of the largest nationally owned accounting firms and forms part of RSM International, which is the sixth largest international accounting and consulting organisation worldwide. In Australia, RSM is one of the fastest growing mid-tier firms with over 115 Directors and Principals and over 1,200 employees operating from 30 locations throughout Australia. Our staff operate across a range of industries, public, private, Government and not-for-profit-sectors.

RSM provides audit, tax, and a wide variety of corporate financial and advisory accounting services. This includes R&D Tax services for a broad array of industries and technologies, and assist entities ranging from start-ups to SMEs through to multinationals.

RSM has previously made submissions to the many Reviews, Reports and Papers that have formed the underlying context from which this Bill has been prepared:

- Response to Treasury Laws Amendment (Research and Development Incentive) Bill 2018;
- The Tax Expenditures Statement – Consultation Paper (TES Paper);
- Treasury's "Re:Think" Tax Discussion Paper (Re:Think Paper);
- The Chief Scientists STEM report (STEM Report);
- The FFF Review of the R&D Tax Incentive prior to the report being completed;
- The FFF Review of the R&D Tax Incentive subsequent to the report being released (3F Response Paper); and
- Senate Economics Legislation Committee regarding the Budget Savings (Omnibus) Bill 2016 (Omnibus Bill).

We would like to bring to your notice that many of the issues that we (and others) have addressed in the above appear to have not been taken into account in the new R&D Tax legislative cuts.

The Consultation Paper for the Bill states:

> *"The 2016 Review of the R&D Tax Incentive and the 2018 Innovation and Science Australia 2030 Strategic Plan found the R&DTI did not fully meet its policy objectives, particularly in inducing business research and development expenditure beyond business as usual activities. The Government's response acknowledges these reports' findings with a package of reforms to enhance the additionality, integrity and fiscal affordability of the R&DTI.*
>
> *…*
>
> *the Government will amend the R&DTI to better target the program and improve its integrity and fiscal affordability in response to the recommendations of the 2016 Review of the R&D Tax Incentive."*

We disagree with the conclusions reached by the Government that there are currently integrity, fiscal affordability, and additionality challenges regarding the current R&D Tax Incentive, and that there is a need for significant change. The FFF review selectively presented information, including the overstated Government budget data to build a case for making substantial changes to the R&D Tax Incentive. Please refer to previous submissions for the details, in summary:

- The actual cost to the economy and budget of the current R&D Tax Incentive has not been modelled to a complete extent, which if correctly modelled would demonstrate that the program has the nature of a loan made through the tax system from Government to companies claiming R&D tax. This loan is repaid by companies over time through forgone tax losses, and shareholders through reduced availability of franking credits. There is no fiscal affordability issue with the current program, which is a point that has been made repeatedly by all major accounting firms involved in the R&D tax incentive. Specific issues that should be taken into account in the modelling include:
  - net tax benefit (R&D offset rate less corporate tax rate) should be modelled for both refundable and non-refundable R&D tax offsets, versus the current practice of using close to the full R&D rate cost (43.5%) for budget cost of the refundable offset;
  - franking impact due to R&D Tax claims resulting in shareholders paying higher amounts of tax. This is as a result of reduce availability of franking credits;
  - revenue benefits to the budget and economy from companies conducting R&D in Australia versus overseas (considering that a company can cost effectively conduct R&D anywhere in the world); and
  - the long term revenue loss to the economy and budget that will result from a national reduction in BERD and loss of productivity gains that would have been produced by the R&D tax incentive has not been modelled.
- While it has been found that there have been a small number of incorrect R&D Tax claims, and the ATO and AusIndustry are dealing with these, there has been no evidence or data presented to suggest that broad integrity issues exist, on the contrary the authors of the FFF review have agreed in published statements on multiple occasions that there is no evidence of significant rorting;
- The concept of encouraging additional R&D expenditure fails to take into consideration that in the current global economy significant support is required to just maintain the status quo level of R&D in Australia due to international competition. Companies should be encouraged and supported to do any R&D in Australia as it enhances productivity. For large companies, some of what the Government terms "business as usual" R&D may happen anyway, but in the absence of a reasonable level of support through the R&D tax incentive will likely happen overseas;

- "Business as usual R&D" needs to be removed as a concept in Government R&D tax policy. The term is an unhelpful Government construct that does not reflect the reality of how companies select or progress projects. Any R&D activity undertaken although ultimately for commercial gain is high risk with potential knowledge spillover benefits that deserves Government support; and
- There is a lack of transparency in modelling of any proposed changes on various Australian industry segments as well as any detailed analysis of international innovation competition from other Governments in either tax or grant form that Australian Policy should consider, when making changes to Australia's most practical and utilised innovation support program.

Our response to the R&D Tax cuts has previously provided detailed recommendations on how to better implement the proposed cuts. I would like to suggest that it would be more effective to throw out the legislation and return to our concerns raised above.

Until an effective economic model of Australia's R&D Tax system takes place, that includes true global competitive comparison, and more importantly understands the fundamental challenges of innovation and the difference between research, translation, startups, SMEs and large corporations there will be a disconnect between policy and results.

Regards

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