



Australian Government

The Board of Taxation

REVIEW OF R&D TAX INCENTIVE DUAL AGENCY ADMINISTRATION MODEL

the **board** of **taxation**
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FOREWORD

The Board of Taxation (the Board) is pleased to submit this report to the Assistant Treasurer following its evaluation of the dual agency administration model for the Research and Development Tax Incentive (R&DTI).

The Board's review involved assessing the current administration of the R&DTI program by the Industry Innovation and Science Australia (IISA), the Department of Industry, Science, Energy and Resources (DISER) and the Australian Taxation Office (ATO) against the Terms of Reference (TOR) set out on the following page.

The Board appointed a Working Group that included Board members Mr Neville Mitchell and Mr Chris Vanderkley. The review was led by Mr Neville Mitchell.

Over 40 participants attended the Board's virtual roundtable consultations. In addition, the Board received numerous written submissions and collected further feedback from targeted consultation sessions with stakeholders. The Board would like to thank officials from DISER, the ATO and the Department of Treasury, and all those who participated in the consultation sessions and responded to the consultation paper, for their valuable assistance and contributions during the course of this review.

The ex-officio members of the Board — the Secretary to the Treasury, Dr Steven Kennedy PSM, the Commissioner of Taxation, Mr Chris Jordan AO, and the First Parliamentary Counsel, Ms Meredith Leigh — have reserved their final views on the observations and recommendations made in this report for advice to Government.



Rosheen Garnon

Chair of the Board



Neville Mitchell

Chair of the Working Group

TERMS OF REFERENCE

The R&DTI program is a self-assessment program that provides tax offsets for eligible company research & development (R&D) expenditure. The stated objective of the program is to encourage industry to conduct R&D activities that may otherwise not be conducted, particularly where the new knowledge gained is likely to benefit the wider Australian economy.

The R&DTI is jointly administered by IISA, DISER and the ATO, with DISER (on behalf of IISA) being responsible for registering companies' R&D activities; and the ATO being responsible for the administration and processing of R&D tax offset claims in the Company Tax Return.

The purpose of the review was to evaluate the R&DTI dual agency administration model, with a view to identifying opportunities to reduce duplication between the two administrators, simplify administrative processes, or otherwise reduce the compliance costs for applicants. In conducting the review, the Board has:

- analysed R&D administration models in other comparative jurisdictions and considered how the international experience may inform improvements to Australia's R&DTI dual agency delivery model
- consulted with companies to obtain an insight into their experience during the registration and claiming process, including their understanding of the different roles and responsibilities of the ATO, DISER and IISA in administering the program
- considered any new and streamlined processes undertaken by the two agencies in response to previous reviews of the scheme's administration, such as the 2016 Review of the R&DTI and the recent Australian Small Business and Family Enterprise Ombudsman Review
- identified the advantages and disadvantages of its recommendations, any potential financial impacts, and any trade-offs between simplification and/or reductions in compliance costs and the scheme's integrity.

The Board notes that changes to the R&DTI's broader policy settings, such as eligibility requirements or rates of support, are outside of the scope of this review.

EXECUTIVE SUMMARY

The R&DTI program is one of the Australian Government's key measures to support innovation and to stimulate R&D activity in Australia. The program provides more than \$2 billion in tax offsets each year making it the largest of the Government's innovation programs.

With the Australian R&DTI program being a dual agency administration model, it is relatively unique as there are only a small number of comparative jurisdictions that use a dual agency administration model. Rather, the majority of comparative jurisdictions use a single agency administration model administered by their Taxation/Revenue Authority.

The Board has reviewed the dual agency administration model taking in account:

- stakeholder experiences with registering and making a claim under the R&DTI program improvements made to the R&DTI program following the recent program reviews undertaken by Government
- comparative jurisdiction R&D models with consideration of how international experience could be leveraged to improve Australia's R&DTI program.

In undertaking the review, the Board conducted extensive consultation on the effectiveness of dual agency administration of the R&DTI program. The Board received overwhelming and consistent feedback from consultees in relation to the administration of the program. This feedback has formed the basis for the Board's observations and recommendations set out in this report.

Following the extensive consultation process, the Board has concluded that the dual administration model should be maintained. The key reasons supporting the Board's recommendation to maintain the existing dual agency administration model are as follows:

- There would be significant complexities and costs involved in unwinding the existing dual agency model and moving to a single agency model
- Given the significant reforms to the R&DTI program over the last few years, there was a strong desire and preference from a number of stakeholders to see a period of relative stability with the program in order to avoid increased uncertainty, confusion and increased administrative burdens involved with changing existing processes
- Both DISER and the ATO now have the required technical expertise and skills sets to administer the program and as such both should be retained in administering the program.

The Board notes that significant improvements have been made to the existing R&DTI program following a number of policy and administration reviews undertaken by the Government between 2016 - 2019. The improvements implemented following those reviews highlighted that the dual administrators are moving towards a customer engagement approach that focusses on

education and guidance and increasing their engagement with companies throughout the R&DTI program. The improvements were viewed by stakeholders and consultees as positive steps undertaken by both DISER and the ATO to improve the administration of the R&DTI program.

Notwithstanding the improvements made to the R&DTI program, following feedback received from consultees, the Board identified a number of additional improvements that can be made to address existing issues in the dual agency model. These will continue to improve the R&DTI program to ensure it is administered effectively and efficiently as well as ensure a more streamlined and cost-effective process for companies. The Board's recommendations focussed on:

- Defining the roles and responsibilities of DISER and the ATO in administering the R&DTI program
- Increased information sharing between DISER and the ATO (which is currently restricted due to legislative provisions) to reduce duplication between the two administrators
- Creating greater certainty for claimants by issuing clear and relevant guidance material in a timely manner
- Publishing clear and transparent timeframes for reviews undertaken by both DISER and the ATO
- An Alternative Dispute Resolution (ADR) process (that involves both administrators) to resolve reviews undertaken by DISER and the ATO in an efficient, cost effective and timely manner.

In assessing the dual agency administration model, the Board received feedback from consultees in relation to the treatment of software under the R&DTI program with select consultees raising with the Board consideration of a separate R&D program for software. During the Board's review, it became apparent that the treatment of software is a contentious issue under the R&DTI program, with the stakeholders concerned about the definition of what constitutes R&D, and how it applies to software, and the treatment of the R&D registrations and claims relating to software.

Following the review, the Board does not recommend a separate program for software related R&D activities. The Board is of the view that the recommended improvements set out above to the R&DTI program, along with actions and activities already in train, would address the uncertainty and challenges faced by stakeholders in relation to making R&D claims in respect of software.

LIST OF RECOMMENDATIONS AND OBSERVATIONS

RECOMMENDATION 1

The dual administration model of the R&DTI program should be maintained, noting that improvements in the model would be achieved by implementing the other recommendations in the Board's report.

RECOMMENDATION 2

A separate software R&D regime is not required. Improvements to the administrative handling of software R&DTI claims should continue with regular dialogue between the industry and the co-administrators encouraged, including through the release of refreshed guidance to support the software sector.

RECOMMENDATION 3

Information and data sharing between the co-administrators should be improved by amending relevant legislation. DISER would be subject to the same offence provisions as ATO staff.

RECOMMENDATION 4

Transparent and clear timeframes for DISER findings and ATO audits should be implemented, with timeframes on expectations of completion of findings and audits publicly available and reviewed periodically.

RECOMMENDATION 5

Clear and concise guidance with examples should be released jointly between the two administrators including an overarching guidance document or manual. Changes to guidance and application dates should be notified in the document or manual. The ATO should finalise and release outstanding guidance products on overheads and draft determinations. Also, the administrators should give consideration to a joint webpage where guidance could be published.

RECOMMENDATION 6

The Justified Trust Regime should be more effectively extended to the R&DTI for larger companies and for smaller companies processes such as Assurance Letters be considered to provide certainty for those companies.

RECOMMENDATION 7

DISER (from the powers of IISA) and the ATO should issue their binding determinations in a timely and efficient manner, to assist companies in understanding their obligations of the program.

RECOMMENDATION 8

The ATO and DISER should provide clarity of their roles in the R&DTI, including their responsibilities and limitations. A Program Charter could be the mechanism to establish the clarity of the roles. Refer to Recommendation 9 for additional information on the Charter.

RECOMMENDATION 9

ATO and DISER should develop and implement a publicly available Program Charter that clearly sets out the expectations and roles of all parties that participate in the R&DTI program. The Program Charter should include expectations on timeframes for engaging with all aspects of the program, how the co-administrators will work together and how they will engage with the companies which have registered for the program.

RECOMMENDATION 10

Market updates of activities undertaken by both the administrators should be published which includes information on compliance/integrity activities.

RECOMMENDATION 11

Alternative Dispute Resolution mechanisms should be implemented for use before escalation to the Administrative Appeals Tribunal. These should involve dispute resolutions amongst all parties: the company, DISER and the ATO. Where appropriate, both DISER and the ATO should be present where discussions on settlements are occurring.

Observations

OBSERVATION 1

There is a significant timeframe between the activities being conducted, the registration deadline with DISER and the lodgement of the Company Tax Return with the ATO. Future consideration could be given by the administrators to bring these dates into closer alignment, where the registration date aligns closer with the lodgement date of the Company Tax Return (that is, ultimately the registration deadline is brought forward).

OBSERVATION 2

Issues have been identified by R&DTI program stakeholders about the new registration portal implemented by DISER in July 2021. DISER have been responsive to the issues and planned upgrades of the Portal are due to occur. The Board encourages DISER to continue to respond to user feedback to ensure the Portal is as user friendly and efficient as possible.

OBSERVATION 3

The Board encourages continued training and engagement of technically capable assessors; however, the Board also notes that the engagement of experts such as those from Data61 to assist in complex cases has been a positive step. The Board encourages the continuation of this type of engagement and potentially expanded to other program areas.

OBSERVATION 4

The use of contingency fees in the R&DTI program is not as widespread feature and information provided to the Board indicates that the use of these types of fees by the accounting, legal and consulting professions has reduced. However, if this changes (that is, contingency fees start to become a regular feature), the Government should consider whether this fee structure should continue and its bearing on the integrity of the program. In doing so the Government should take into account how other jurisdictions have dealt with this market practice.

GLOSSARY

The following abbreviations and acronyms are used throughout this report.

Abbreviation	Definition
AAT	Administrative Appeals Tribunal
ADR	Alternative Dispute Resolution
ANAO	Australian National Audit Office
ATO	Australian Taxation Office
Administrators / Co-Administrators	Department of Industry, Science, Energy and Resources and the Australian Taxation Office
Board	Board of Taxation
CAN	Canada
DE	Germany
DISER	Department of Industry, Science, Energy and Resources
FATA	<i>Foreign Acquisition and Takeovers Act 1975 (Cth)</i>
FCA	Federal Court of Australia
FFC	Full Federal Court
HMRC	HM Revenue & Customs
ITAA 36	<i>Income Tax Assessment Act 1936 (Cth)</i>
ITAA 97	<i>Income Tax Assessment Act 1997 (Cth)</i>
IISA	Industry Innovation and Science Australia
IRDA	<i>Industry Research and Development Act 1986 (Cth)</i>
NZ	New Zealand
Guide	Regulator Performance Guide
R&DTI	Research and Development Tax Incentive
R&D	Research and Development
TAA	<i>Taxation Administration Act 1953 (Cth)</i>
UK	United Kingdom
US	United States
US IRS	United States Internal Revenue Service

CHAPTER 1: INTRODUCTION

1.1 On 11 May 2021, the Assistant Treasurer requested that the Board undertake a review to evaluate the dual agency administration model for the R&DTI program (the review).

The Review Team

1.2 The Board appointed a Working Group led by Board member Mr Neville Mitchell (Chair of the Working Group), with assistance from Board member, Mr Chris Vanderkley. In addition, the Working Group comprised private sector experts Paul Suppree, Corporate Tax Association and Kris Gale, Michael Johnson Associates as well as officials from the Department of the Treasury, the ATO and DISER.

Consultation Process

1.3 The Board's consultation process involved:

- The publication of a Consultation Guide (in June 2020) describing the scope of the review, and presenting a series of questions to help identify the key difficulties being encountered and possible reform options
- Virtual consultation sessions with over 40 attendees who joined and participated in the sessions
- Virtual meetings with international regulators/administrators from New Zealand (NZ), United Kingdom (UK), Canada (CAN) and the United States (US) about the issues and developments in their R&DTI programs
- Virtual meetings with the UK and US offices of an international professional services firm to obtain the advisor's perspective on the operation of the program in their respective countries and a large commercial company in New Zealand which is involved in the NZ's R&D Tax Incentive scheme
- Desktop reviews of other international R&D incentive models
- Virtual meetings with selected and consenting companies about their views on the current administration of the Australian R&DTI program
- The conduct of a survey via a questionnaire on compliance costs with a select number of consenting companies.

Submissions

- 1.4 The Board received 17 written submissions, with one additional confidential submission, from a range of stakeholders in response to the Consultation Guide.
- 1.5 The Board recognises the significant contributions made by stakeholders in making their submissions. The Board carefully considered all submissions and other contributions made during the review. Further details of the consultation process and submissions are available at Appendix A.

The Board's Report

- 1.6 In formulating this report, the Board considered the key themes and issues raised by consultees in submissions and at the virtual consultation meetings, and the views of the members of the Working Group. The key themes and issues raised by the consultees and members of the Working Group were consistent. This feedback has formed the basis for the Board's observations and recommendations set out in this report.
- 1.7 The Board's recommendations were developed specifically in response to the TOR and the following two relevant tax design principles:
- good practices in the administration of R&DTI programs
 - the Australian Government's principles of regulator best practice.

Good practices in the administration of R&DTI programs

- 1.8 Since the R&DTI is a tax expenditure¹ and therefore a particular form of taxation, the Board has considered the R&DTI dual agency administration model against relevant criteria such as simplicity, efficiency and equity, which are the dominant tests of merit for individual taxes and for the tax system as a whole.
- 1.9 Similarly, the European Commission in its 2017 report² on how to make R&DTI programs most effective concluded that:

Good practices in the administration of R&D tax incentives include among others one-stop, online application procedures and guidelines for businesses, short times for

1 Tax expenditures arise when the 'normal' tax liability is reduced in order to encourage a particular behaviour or to assist a particular group. Tax exemptions, tax deductions, tax offsets, concessional tax rates and deferrals of tax liability are examples: Dr Anne Holmes, 'Tax Expenditures' Parliamentary Library Briefing Book, <https://www.aph.gov.au/About_Parliament/Parliamentary_Departments/Parliamentary_Library/pubs/BriefingBook45p/TaxExpenditures>

2 D. Ognyanova, 'R&D tax incentives. How to make them most effective?.' European Commission. Policy Development and Coordination (2017).

decisions on eligibility, assessors of R&D tax incentives claims with expertise in the field, use of risk-based control mechanisms.

Principles of regulator best practice

1.10 As part of the Australian Government's support for Commonwealth agencies in increasing accountability and demonstrating best practice, it published the *Regulator Performance Guide* (the Guide)³ that sets out the Government's expectations for regulator performance and reporting via three principles of best practice including:

- Continuous improvement and building trust
- Risk based and data driven
- Collaboration and engagement.

1.11 The third principle is most relevant to the Board in carrying out this review of the R&DTI dual agency administration model. The Guide states that '*in practical terms, demonstrating collaboration and engagement means regulators*':⁴

- engage genuinely and regularly with stakeholders, including regulated entities, other regulators and the community, including on the development of and reporting against meaningful performance measures
- seek out real time stakeholder feedback to inform regulatory decisions, and loop back in a timely way on outcomes
- offer a range of consultation mechanisms to ensure small businesses, sole traders and the wider community can easily engage and provide feedback
- establish processes that enable meaningful and timely stakeholder engagement by providing early notification of operational changes
- provide guidance and information that is relevant, clear, concise and easily accessible to help regulated entities understand their obligations and responsibilities to encourage voluntary compliance
- are transparent in their decision-making and, where possible, provide reasons for regulatory decisions or share anonymised compliance or enforcement 'case summaries'

3 Australian Government, *Regulator Performance Guide*, Canberra 2021.

4 *Ibid*, p9.

- implement innovative approaches in considering regulatory or policy issues such as 'regulatory sandboxes'.

1.12 The abovementioned features, demonstrating what 'collaboration and engagement' means for regulators have guided the Board during the review of the R&DTI dual agency administration model. It formed the foundation in assisting the Board with:

- Identifying the key themes and issues associated with the current dual administration model
- Making observations
- Developing recommendations.

CHAPTER 2: AN OVERVIEW OF THE CURRENT ADMINISTRATION OF THE R&DTI

KEY POINTS

- The R&DTI dual administration model should be maintained. DISER and the ATO each broadly have the required technical expertise to administer the program and the significant complexity and disruption in unwinding the model is not warranted.
- The current R&DTI program is sector agnostic and is flexible to support all industry sectors including software. Further improvements to the administration of the R&DTI program and guidance to assist in identifying eligible R&D activities and fulfill record keeping requirements will address the uncertainty and challenges faced by stakeholders in relation to software R&D activities.

2.1 The purpose of this chapter is to provide a high-level overview of the operation of the existing dual agency administration model of the R&DTI program.

Overview of the R&DTI program

2.2 The R&DTI program reduces the costs to companies of undertaking eligible R&D activities as the program offers beneficial tax offsets for eligible R&D expenditure up to \$150 million (from 1 July 2021) each income year. The two main components of the R&DTI currently are:⁵

- For R&D entities with aggregated turnover of less than \$20 million, the refundable R&D tax offset is an 18.5 per cent premium over the entity's relevant company tax rate
- For R&D entities with aggregated turnover of \$20 million or more, the non-refundable R&D tax offset is an incremental premium over the entity's relevant company tax rate. The premium increments are based on levels of R&D Intensity. The R&D Intensity is a

5 Claiming eligible R&D conducted up to 30 June 2021, the previous tax offset rates apply; and depending on a company's annual turnover, the R&DTI provides either a refundable or non-refundable tax offset: a 43.5 per cent refundable tax offset is available to companies with an annual turnover of less than \$20 million; and a 38.5 per cent non-refundable tax offset is available to companies with an annual turnover is more than \$20 million.

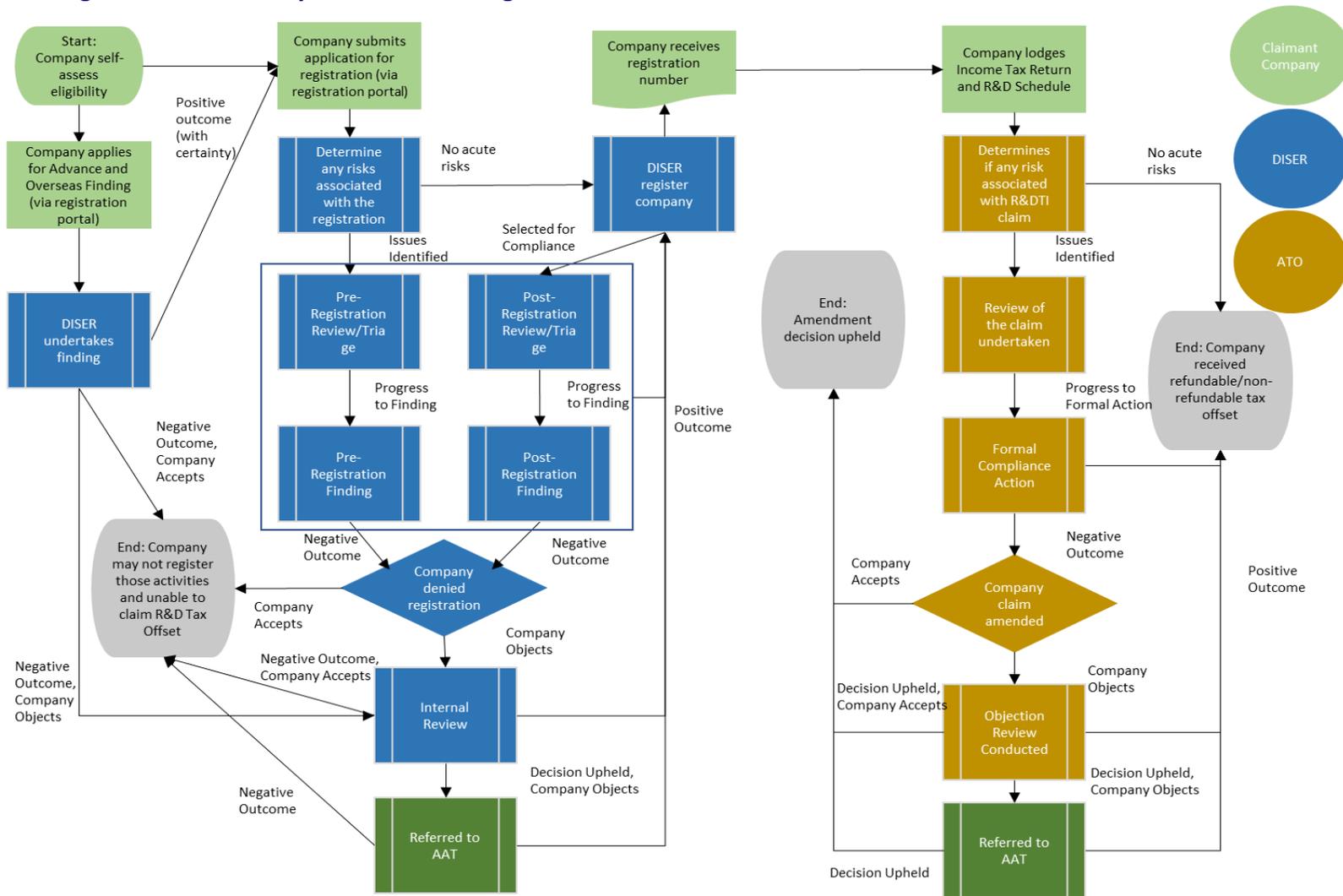
percentage of an entity's eligible R&D expenditure as a proportion of that entity's total expenditure. The premium increment is calculated as follows:

- All eligible R&D expenditure up to 2 per cent R&D Intensity will receive a non-refundable R&D tax offset equal to the entity's relevant company tax rate plus an 8.5 per cent premium.
- Additional eligible R&D expenditure above 2 per cent R&D Intensity will receive a non-refundable R&D tax offset equal to the entity's relevant corporate tax rate plus a 16.5 per cent premium.

R&DTI Registration and Claiming Process

- 2.3 IISA is a statutory Board established under the *Industry Research and Development Act 1986* (Cth) (IRDA), reporting to the Minister for Industry, Science and Technology. DISER administers the R&DTI program on behalf of IISA.
- 2.4 DISER (on behalf of IISA) is responsible for registering companies R&D activities and assessing the eligibility of R&D activities. DISER also has responsibility for registering Research Service Providers.
- 2.5 The ATO is responsible for determining if the R&D expenditure claimed in respect of registered R&D activities in the Company Tax Return is eligible for R&D tax offsets under the relevant provisions of *the Income Tax Assessment Act 1997* (Cth) (ITAA 97).
- 2.6 The registration and claiming process is illustrated in Figure 1 below, alongside the high - level processes involved in compliance activities in the program.

Figure 1: User Journey in the R&DTI Program



2.7 To access the R&DTI program, companies follow a two-stage process:

- Companies first apply to register their R&D activities with DISER up to 10 months after the end of their financial year
- Once registered, companies use their registration information to lodge an R&D expenditure schedule as part of their Company Tax Return with the ATO to claim the tax offset.

OBSERVATION 1

There is a significant timeframe between the activities being conducted, the registration deadline with DISER and the lodgement of the Company Tax Return with the ATO. Future consideration could be given by the administrators to bring these dates into closer alignment, where the registration date aligns closer with the lodgement date of the Company Tax Return (that is, ultimately the registration deadline is brought forward).

Dual Agency Administration Model

- 2.8 The current administration model of the R&DTI program is a dual agency model with each administrator having a defined role. Through the consultation process, the Board has explored and undertaken analysis on the effectiveness of the operation of the existing dual agency administration model.
- 2.9 In reviewing the dual agency model, the Board considered and analysed the R&DTI administration models in comparative jurisdictions. These findings are detailed in Chapter 6 of this report.
- 2.10 Following discussions with the regulators in comparative jurisdictions, the Board considers the Australian R&DTI program, being a dual agency administration model, to be relatively unique. There are only a small number of comparative jurisdictions that use this type of model. Rather, the majority use a single agency administration model administered by their local Taxation Authority.

The Board's Analysis

- 2.11 During the consultation process the Board received overwhelming feedback from consultees in relation to the R&DTI dual agency administration model. The following feedback was obtained from consultees:
- Maintain the current dual administration model going forward (without caveat)
 - Maintain the current dual administration model (but with changes/improvements to program administration), given the process of changing to a single model would add

complexity and additional costs for participants in the program and would take considerable time and resources to implement

- Move to a single administrator to create efficiencies, but with the caveat of expected improvements to program administration.

2.12 Most stakeholders agreed that a dual agency model should be maintained and that the transition and adoption of a single agency model has more disadvantages than maintaining and improving the dual agency model. Examples of feedback from the consultees in relation to the dual agency model are included in the following paragraphs:

2.13 BDO noted that:⁶

BDO is fully supportive of both the administering bodies' roles in maintaining the integrity and compliance of the R&DTI programme. In our view it makes sense for both agencies to be involved in administering the R&DTI.

2.14 The Tech Council of Australia (TCA) in their submission noted:⁷

The TCA understands the need for dual administration of the R&DTI and is supportive of it continuing, subject to some changes to optimise the model.

2.15 Chartered Accountants Australia and New Zealand noted:⁸

Given AusIndustry's long history with the R&DTI, the unique science, innovation and industry focus of AusIndustry and the critical importance of certainty and stability for the program, CA ANZ considers that on balance, the dual administration model has merit and should be retained. But...there are areas where administration must be improved.

2.16 PwC noted:⁹

Moving to one administration model would prima facie create efficiencies, reduce administration costs and create more certainty but only if the regulator's approach to reviews was to significantly change from current practices.

2.17 Based on the feedback from the consultations and discussions with international regulators in comparative jurisdictions, the Board is of the view that the current dual agency administration model should be maintained, and therefore a single agency model should not be pursued, for the following reasons:

6 Submission 5, p.3.
7 Submission 15, p.3.
8 Submission 9, p.2.
9 Submission 14, p.1.

- *Strong feedback supporting the continuation of a dual agency administration model*

The feedback received by the Board indicated that the majority of the consultees were strongly supportive of the dual agency administration model continuing with both DISER and the ATO administering the R&DTI program.

- *The experience, knowledge and capabilities that both agencies bring to the current dual administration model*

DISER has technical expertise in assessing R&D activities but also has a wealth of experience with grants and other programs where support can be provided beyond the R&DTI program. The ATO is best placed and has the resources available to administer the tax offset for the R&DTI program and review matters related to expenditure on eligible activities. The differentiation between the roles of DISER and ATO have a significant advantage in the program as both administrators broadly have the relevant specialist skills to administer their respective roles in the program.

- *Complexity and costs involved in unwinding the dual agency program*

There would be significant complexity in moving from the current dual administration model to a single administration model, including an increase in the level and nature of resourcing required by the separated administrators, the logistical shift of technical expertise and the resultant reduced efficiencies in each agency during and after the transition of resources into the single agency model.

Any shift of the administration model from two administrators to one administrator would result in additional costs and complexity for companies participating in the program while the model transitions. There would not only be a significant resource impact in moving to a single agency, but considerable time and resources would be spent on scope and planning activities. These activities are likely to use existing program resources, which would take away from day-to-day program managements activities and further impact companies who participate.

- *Consultees need stability in a program that has undergone significant reform over several years*

Many consultees expressed the view that the program has already gone through a significant period of reform, with several reviews recently undertaken and recent policy changes to the program. Given the changes to date, many consultees indicated to the Board that they would like to see a period of stability in the program to provide increased certainty for companies currently participating in the program and for future participants.

- *Resourcing constraints for a single agency*

The Board is of the view that if the existing dual agency model moved to a single agency model, the ATO would be the only administrator that has the size and scope of agency to conduct both functions of the program, the ATO does not, however, currently have the technical expertise to undertake DISER's role of assessing the registrations in the program. There would need to be consideration of moving resources from DISER to the ATO, which would result in additional costs to the ATO in ensuring the technical skills are maintained. The skillset of the resources that would need to transfer to the ATO would not provide broader benefits to the ATO as that skillset and technical expertise does not form part of the ATO's core workforce requirements. This could result in a doubling up of resources across two agencies given that DISER also requires these skills to support other programs such as the administration of grants.

- 2.18 In light of the above, the Board makes the following recommendation which is in line with the three principles of best practice (continuous improvement and building trust, risk based and data driven, and collaboration and engagement) set out in the Guide.

RECOMMENDATION 1

The dual administration model of the R&DTI program should be maintained, noting that improvements in the model would be achieved by implementing the other recommendations in the Board's report.

Software and the R&D Tax Incentive

- 2.19 In assessing the dual agency administration model, the Board received feedback from consultees in relation to the treatment of software under the R&DTI program with select consultees proposing a separate R&D program for software.
- 2.20 During the Board's review, it became apparent that the treatment of software under the R&DTI program is a contentious issue. Consultees were concerned about the definition of what constitutes R&D, how it applies to software, and the treatment of the R&D registrations and claims in that space. In particular, consultees advised the Board of the following issues relating to software:
- There are challenges in defining the eligibility of software R&D activity under the current definition of R&D activity in the ITAA 1997 as the current definition lends itself to more traditional scientific based R&D and does not as clearly align with innovative software activities.
 - There is constant innovation in the software sector including:
 - the creation of new computer languages

- new processes and platforms that enable the storage and analysis of large complex databases
 - the use of algorithmic decision making and robotic machine operations occur.
- There is a risk that the pace at which the software industry is advancing and innovating may result in activities that previously would have qualified for R&D no longer qualifying in the existing definition in the ITAA 1997.
 - Documentation developed and used as evidence to support R&D activities in the software industry can differ from what is generated in other industries. This has caused challenges for both the claimant and the administrators in identifying the appropriate documentation required to support an R&D activity. Notwithstanding this uncertainty, consultees advised the Board that work is currently being undertaken by the ATO and DISER with the industry to provide further clarity and certainty on these documentation requirements.
- 2.21 As part of the review, the Board undertook independent research and analysis of R&D programs in comparative jurisdictions. Based on discussions with international administrators of comparable R&D programs in NZ, UK, CAN and the US, it is clear that all administrators (with both single and joint administration models) are facing similar challenges in determining the eligibility of software activities given the constant advances being made.
- 2.22 Even though the administrators in comparable jurisdiction face similar challenges, their programs did not have a separate system for processing claims for software development.
- 2.23 In light of the challenges faced by companies in the software industry, consultees have advised the Board that the R&DTI co-administrators have taken positive steps to engage with the software sector on establishing common principles and guidelines regarding what constitutes R&D activities and the appropriate documentation required to be maintained for software projects.
- 2.24 The Board was advised that this has involved:
- *Collaborative workshops held between the software sector, DISER, the ATO and the Treasury* - An initial workshop was held in April 2021 and additional workshops held in August and November 2021 progressed the shared understanding and planning of collaborative guidance. Further workshops and discussions are also planned between the Industry and the co-administrators. At the workshops, discussions focused on what

constitutes eligible software activities versus more routine activities that do not meet the definitional requirements.¹⁰

- *Development of user-focussed guidance products* - Recent collaboration of different stakeholders in respect of software R&D is focused on the development of collaborative guidance products including record keeping and documentation requirements. This has resulted in the co-administrators obtaining a deeper understanding of the types of records generated through software activities and how they may be used in the program.

The Board's Analysis

- 2.25 As noted above, during the consultation process, some consultees in the software industry requested the Board consider a separate R&D program for software activities given the challenges faced in relation to the current definition and administration of the R&DTI program.
- 2.26 The Board acknowledges the challenges faced by those companies and agrees that with the fast pace advances to software development, it is important that improvements are made to the R&DTI administration model to ensure that there is a path to participation for companies in the software industry. It is also important that the program is achieving the Government's policy objective of stimulating the economy by encouraging companies to develop innovative ideas and activities.
- 2.27 The Board is of the view that the R&DTI program in its current sector agnostic format is appropriate to support all industries and therefore the Board does not support a separate R&DTI program for the software industry. The Board's recommendation is based on the following feedback obtained during the consultation process:
- *Creating a separate R&DTI program specifically for software would be complex* - The Board understands that there would be significant effort, complexity and cost involved in either carving out software from the current R&DTI program and/or developing an entirely new program relating to software only.
 - *Equity in participation for all program participants* - Integrity, standards for the tax benefit and government funding are important considerations and need to be at an equivalent level for all program participants. This may be difficult to achieve across two separate programs.

10 To register eligible R&D activities, the company needs to conduct or plan to conduct at least one core R&D activity; and any supporting R&D activities must directly relate to those your core R&D activities. The statutory definitions of core and supporting R&D activities are contained in sections of 355-25 and 355-30 of the *Income Tax Assessment Act 1997*.

- *Improvements to the program are being made to address uncertainties relating to software* – The engagement between the co-administrators and the software sector has significantly improved with the recent collaborative workshops. All parties have agreed to identify issues unique to the software industry and to explore how greater certainty could be provided in respect of software development claims.
- *Refreshed guidance on software to provide certainty to companies* – The co-administrators have refreshed existing guidance material and are developing new guidance material on software related activities to ensure that guidance assists companies in the software industry with understanding the program requirements.

2.28 For the abovementioned reasons, the Board makes the following recommendation which is in line with the three principles of best practice (continuous improvement and building trust, risk based and data driven, and collaboration and engagement) set out in the Guide.

RECOMMENDATION 2

A separate software R&D regime is not required. Improvements to the administrative handling of software R&D claims should continue with regular dialogue between the industry and the co-administrators encouraged, including through the release of refreshed guidance to support the software sector.

CHAPTER 3: NEW PROCESSES AND CHANGES IN THE R&DTI PROGRAM FOLLOWING PRIOR REVIEWS

KEY POINTS

- Feedback provided to the Board indicated there has been notable change and improvement in the program administration since 2019.
- Notwithstanding the improvements made to the R&DTI program, additional enhancements can be made to the dual agency model so that the R&DTI program can be administered more effectively and efficiently. This will encourage additional companies to participate in the program and ensure a more streamlined and cost-effective process for companies.
- The co-administrators are inhibited from fully realising the benefits of the dual administration model as a result of legislated secrecy provisions, which affects the information sharing between the agencies. Legislative change is needed to enable further improvements in the effective administration of the R&DTI program.

Prior Reviews of the R&D Tax Incentive

3.1 The R&DTI program has been the subject of several policy and administration related reviews since 2016. Table 1 below outlines the reviews undertaken into the R&DTI program, dates released and purpose of the reviews.

Table 1: Recent reviews of the R&DTI program

Review Undertaken	Date Released	Purpose of the review
Review of the R&D Tax Incentive	April 2016	Examine whether the R&D Tax Incentive program was meeting its stated policy objectives.
Ferris, Finkel and Fraser Review (3F Review)		

Review Undertaken	Date Released	Purpose of the review
Australia 2030: Prosperity through Innovation Innovation & Science Australia	November 2017	A plan for Australia to thrive in the global innovation race (which built on the 3F Review – with no significant changes to earlier recommendations).
Australian Small Business and Family Enterprise Ombudsman (ASBFEO)	December 2019	Examine the impact of the administration of the R&D Tax Incentive program on small businesses.
Australian National Audit Office	November 2021	Examine the effectiveness of IISA's, DISER's and the ATO's administration of the R&DTI program.

3.2 The Board considered the changes and improvements implemented by the co-administrators in response to the previous reviews commissioned by the Government. The purpose of this chapter is to analyse and detail the changes that have been made to the administration of the program since the abovementioned reviews were completed.

3.3 Evidence provided to the Board in consultation sessions and written submissions indicates that there have been substantive and noticeable improvements and a change of approach in program administration since 2019 for many taxpayers.

3.4 The Board notes that the improvements made to the R&DTI program are in line with the Government's objectives of stimulating the Australian economy through R&D activities and innovation as Australia moves towards a post COVID environment.

ANAO Audit

3.5 The Australian National Audit Office (ANAO) has carried out an audit to examine the effectiveness of IISA, DISER and the ATO in administering the R&DTI program. It is understood that the ANAO is due to release its report (or has released its report) in November 2021.

- 3.6 The Board understands that the scope of the ANAO review is to examine the effectiveness of IISA, DISER and the ATO administration of the R&DTI program and in particular is focused on whether DISER and the ATO have:
- effective registration, eligibility review and compliance arrangements
 - effective performance measurement and monitoring arrangements.
- 3.7 The Board met with ANAO senior officers to determine whether there was any degree of overlap or conflict in the Board’s review and the ANAO’s audit processes. The scope of work for the ANAO audit has some similarities to the Board’s scope as the scope of the audit includes the effectiveness of the two administrators.
- 3.8 Whilst there may be some overlap with the ANAO review, the Board’s Terms of Reference have a broader scope including the examination of the dual agency model itself and international comparisons.
- 3.9 The Board notes that the ANAO released their Performance Audit Report on the administration of the R&DTI program on 25 November 2021.¹¹ The ANAO made three recommendations which were agreed to by IISA, DISER and the ATO. Two recommendations were made to IISA and DISER, aimed at improving processes around advance findings and examinations, and one recommendation was made to the ATO relating to establishing monitoring and reporting arrangements for its compliance activities. The Board considers that these recommendations complement the recommendations in this report.

Compliance Processes

- 3.10 Since 2019 the co-administrators, particularly DISER, have made significant improvements in their approach toward compliance activities.
- 3.11 During the consultation process, the Board heard that prior to 2019, compliance activities undertaken by DISER would begin with a ‘statutory finding’ process, rather than an education led approach in the first instance.¹²
- 3.12 An example was provided to the Board where a company had incomplete documentation, DISER worked collaboratively with the company and the tax agent to assist in outlining the documentation requirements and how the requirements could be satisfied by the

11 The Auditor-General, *Auditor-General Report No.10 2021–22 Performance Audit - Administration of the Research and Development Tax Incentive* <Administration of the Research and Development Tax Incentive (anao.gov.au)>

12 Findings are the formal mechanism in which the eligibility of R&D activities are determined by DISER

company. The tax agent noted, prior to 2019, that incomplete documentation would have usually resulted in commencement of a statutory finding.

- 3.13 Several consultees also acknowledged that since 2019, that administrators have taken a more educative and collaborative approach. This was acknowledged by the co-administrators in their own submission as follows:¹³

Improvements to the program include:

A customer engagement approach that focuses on education and guidance and only moves into statutory examination in clear cases of non-compliance.

- 3.14 The improved approach to compliance aligns with the implementation of DISER's new *Integrity Framework* which provides guidance on how DISER engages with companies that meet program requirements and the levels of compliance risk for companies (that is, from 'getting it right' through 'trying to get it right' to 'does not comply').¹⁴ The Integrity Framework implemented by DISER considers eligibility risks and company behaviour to categorise compliance risks.

- 3.15 The implementation of the *Integrity Framework* was viewed by many consultees as a positive step in the right direction in relation to the administration of the R&DTI program.

- 3.16 RSM Australia noted:¹⁵

AusIndustry's most recent compliance regime ('New Integrity Framework – User Journey') with their 'traffic light' approach has been a good step forward. It has resulted in better engagement with industry and a less adversarial approach from AusIndustry.

- 3.17 Deloitte noted:¹⁶

We acknowledge our general impression that recent dealings with IISA have improved as the new 'customer journey' and education processes have started to evolve.

- 3.18 Some consultees advised the Board of an enhanced use of experts in certain cases since 2019 which had improved the compliance processes. This observation is supported by the partnering with CSIRO's Data61 to provide expert advice for complex assessments in computing and software cases. The use of experts is further explored in Chapter 4.

- 3.19 In addition to the changes in compliance approach and engagement of experts, the Board notes that draft internal review reports are now provided to companies for review and

13 Submission 16, p.21.

14 Business.gov.au, 'How we monitor R&D Tax Incentive applications', viewed 23 November 2021, <<https://business.gov.au/grants-and-programs/research-and-development-tax-incentive/how-we-monitor-rd-tax-incentive-applications>>

15 Submission 17, p.5.

16 Submission 7, p.6.

feedback prior to finalisation. This was also viewed as a positive step by several consultees. As an example, Grant Thornton noted:¹⁷

The pilot program started by AusIndustry during 2020 to provide companies a draft report before findings are issued be implemented as a matter of course. This provides a reviewed company with more transparency, and is an opportunity to identify any errors of fact which can impact the outcome before the findings are finalised.

- 3.20 Evidence provided to the Board indicated that the abovementioned improvements were an important step forward however the program could be further improved and enhanced.

Guidance

- 3.21 A number of consultees advised that positive steps had been taken by both the ATO and DISER to improve the program guidance. This included the development and release of the refreshed 'Guide to Interpretation', DISER's flagship guidance product to guide eligibility for the program.
- 3.22 As noted previously, steps were also taken by the co-administrators to work together and collaborate with companies in the software sector in relation guidance specific to their industry. However, consultees indicated that there is still a strong need for guidance to be finalised quickly and for that guidance to incorporate practical case studies and examples of issues such as documentation in the software industry.
- 3.23 The Board acknowledges that improvements have been made to guidance materials, however overwhelming feedback was received from consultees that there is generally a lack of clear and relevant guidance materials available. The improvements to guidance material are further explored in Chapter 4.

Registration Portal

- 3.24 In July 2021, DISER launched its new registration portal. The portal is a new way for companies and tax agents to submit their program registrations and further interact with the program, including submitting advance and overseas findings and managing the functions associated with registrations. The new registration process is intended to reduce time to apply for the program and help DISER identify participants that need assistance

17 Submission 6, p.2.

with understanding the program requirements, or who are registering non-compliant activities.¹⁸

- 3.25 Evidence provided to the Board through consultation sessions and written submissions indicate that the portal is an improvement compared to the previous registration process. Further improvements could be made to ensure a more positive and seamless user experience. These improvements include more appropriate character limits, adjustments to messaging displayed in the portal and clearer instructions within the portal on how guidance products should be viewed. This is supported by the Australian Investment Council who noted in their submission proposed updates to the portal:¹⁹

Refine the new registration portal to ensure it provides a clear path for applicants to register their projects and does not lead to additional compliance costs. Implement these changes when the next release of the customer portal is implemented in November 2021.

- 3.26 The Board understands that DISER is in the process of updating the registration portal by December 2021.

OBSERVATION 2

Issues have been identified by R&DTI program stakeholders about the new registration portal implemented by DISER in July 2021. DISER have been responsive to the issues and planned upgrades of the Portal are due to occur. The Board encourages DISER to continue to respond to user feedback to ensure the Portal is as user friendly and efficient as possible.

Limitation on Information Sharing

- 3.27 Notwithstanding that the Board received positive feedback during the consultation process in relation to improvements made to the administration of the R&DTI program, many consultees indicated that limited information sharing between DISER and the ATO is a key area of concern that is causing frustration for companies who are making claims under the R&DTI program.
- 3.28 Statutory secrecy provisions²⁰ currently constrain the ATO and DISER from sharing information relating to the R&DTI program.
- 3.29 Consultees suggested that the inability for the co-administrators to share information causes frequent delays to review processes and results in inefficiencies, duplication of work/information requests and increased costs for companies. The feedback was

18 Submission 16, p.21.

19 Submission 3, p.6.

20 Sections 355-50 and 355-65 of the *Taxation Assessment Act 1953* outlines who within Government the ATO can share information with and for what purpose.

evidenced in a number of written submissions indicating there are problems caused as a result of the prevention of the sharing of information between DISER and the ATO. Examples of the feedback provided are set out below.

- 3.30 Grant Thornton noted this issue in relation to information sharing and the impacts on ‘double handling’:²¹

The administrative burden on ‘double handling’ – if a company is reviewed by the ATO and AusIndustry at separate times, our experience is that the two authorities do not share information already obtained such that the company is effectively required to provide the same or similar information twice on the same incentive claim. Companies should legitimately expect that such information already provided to one authority and its conclusions should already be available to the other before it proceeds with a subsequent review.

- 3.31 The Tax Institute noted the following regarding information sharing:²²

We recommend that the government considers codifying an ability for the ATO and IISA to share information and confer with each other in appropriate situations. Among other things, this would foreseeably contemplate situations where one agency has commenced proceedings or investigations in respect of a particular applicant. In such cases, consideration should be given to whether one administrator could be required to consider its position with respect to how the legislation it administers applies to a particular applicant at the same time as the other agency commences an investigation, audit, or other inquiry. This would mean that issues could be dealt with around the same time and ideally be resolved simultaneously. Overall, this would have the added benefit of providing transparency to taxpayers as to the information that is shared between the two agencies and minimising the duplication of work by both taxpayers and the administrators.

- 3.32 EY noted that improved information sharing and communication was a priority:²³

It is our recommendation that improvements be made to the administrative process to provide claimants with a consistent approach and increased certainty regarding the eligibility of their R&D activities and expenditure [this includes] ... Improved communication and collaboration between both the ATO & DISER, including joint visits, sharing of information and a reduction in the duplication of questions and reviews.

- 3.33 BDO noted issues with interagency communication and information sharing:²⁴

21 Submission 6, p. 2.
22 Submission 2, p. 10.
23 Submission 13, p. 2.
24 Submission 5, p. 7.

Limited interagency communication. One common example is where a company has a substituted accounting period (SAP). AusIndustry's registration team's practice is to contact the claimant's nominated contact requesting a copy of the original letter from the ATO approving the SAP, which may be some years old. It is unclear why this sort of information can't be requested directly by AusIndustry from the ATO.

3.34 The Ai Group noted:²⁵

All steps should be taken to avoid duplication of effort and data between agencies.

3.35 Consultees also advised that as a result of the co-administrators not being able to share information, problems arose with having joint meetings with DISER and the ATO as there were sensitivities around the information discussed while both administrators were present.

3.36 The impact of the two administrators not being able to share information is illustrated in the case study below which is based on the experience of a large multi-national company.

CASE STUDY 1 – INFORMATION SHARING

A large multinational company has been participating in the R&DTI program as they believed the benefits outweighed the costs and the program provided encouragement to innovate.

In 2020, the company was notified by the ATO of the commencement of a R&D review and in addition they would encourage DISER to also undertake a review to look at the R&D activities. The company thought it logical that DISER would review the activities first and then the ATO review on expenditure and that this process would be coordinated between the two administrators.

The company noted the review situation quickly deteriorated through a lack of communication between the administrators. The company asked for a meeting with both of the administrators to request better coordination, however the conversation was limited citing privacy reasons in what the administrators could share with each other.

These reviews were undertaken over 2020 and 2021 calendar years (and were still continuing at the time of the consultations). The company has advised that it will not lodge a 2020 claim until the reviews are completed. The company had not been given a potential end date for the reviews, making their claim situation uncertain.

The company noted to the Board that this process had made the company question if it '*was worthwhile going through this (the program) again*'. There had been significant disruption to key personnel and many hundreds of pages of documents provided.

The company noted the program was '*ripe for improvement*', with improvements in engagement and the administrators working together as critical.

25 Submission 1, p.1.

The Board's Analysis

- 3.37 Following feedback received during the consultation process, the Board agrees that the statutory secrecy provisions preventing DISER and the ATO from sharing information are creating significant inefficiencies in the administration of the R&DTI program with companies making claims under the R&DTI program ultimately bearing the burden of this inefficiency.
- 3.38 DISER and the ATO can share information in relation to the Venture Capital program (which is administered by both the ATO and DISER). As such, there is currently legislative precedent in place allowing information to be shared between DISER and the ATO under the co-administered Venture Capital program.
- 3.39 The Board agrees that amendments should be made to legislation to permit broader information sharing between DISER and the ATO in relation to the R&DTI program to improve the experience for companies participating in the program and ultimately creating a more efficient process. This is particularly important where companies are subject to review by both DISER and ATO as it will reduce the risk of duplicating work and additional resources needed by companies to respond to multiple reviews.
- 3.40 The Board makes the following recommendation which supports the desired feature to provide guidance and information that is relevant, clear, concise and easily accessible to ensure companies understand their obligations and responsibilities and encourage voluntary compliance.

RECOMMENDATION 3

Information and data sharing between the co-administrators should be improved by amending relevant legislation. DISER would be subject to the same offence provisions as ATO staff.

CHAPTER 4: OPERATIONAL ISSUES FROM COMPANY PARTICIPATION IN AND EXPERIENCES WITH THE R&DTI PROGRAM

KEY POINTS

- The Board has identified a number of operational improvements to the dual administration model to make it more effective.
- Transparent and clear timeframes for DISER findings and ATO audits should be implemented.
- Clear and concise guidance with examples should be released jointly by the two administrators including an overarching guidance document or manual.
- Throughout the consultation process, consultees repeatedly emphasised to the Board the need for clear guidance and sustained certainty of operational processes and procedures by the administrators.
- The Justified Trust Regime should be more effectively extended to the R&DTI for larger companies and for smaller companies processes such as Assurance Letters should be considered. Similarly, DISER and the ATO should issue their binding determinations in a timely and efficient manner.

4.1 The purpose of this chapter is to highlight operational issues that have been brought to the Board's attention and to provide recommendations for addressing these issues.

4.2 These key operational issues relate to:

- Timeframes to complete reviews and audits
- Technical capabilities of the co-administrators
- Program guidance and education
- Program certainty and assurance
- Issuing of binding determinations
- Contingency fees.

Timeframes to complete reviews and audits

- 4.3 Both DISER and the ATO have specific roles & responsibilities in the program associated with program integrity.
- 4.4 DISER has responsibility for assessing and determining the eligibility of R&D activities against the definition of core and supporting activities in sections 355-25 and 355-30 of the ITAA 1997.
- 4.5 The ATO's role is to determine any entity's eligibility to participate in the program and whether the R&D expenditure incurred by the entity is eligible for the program through having a nexus to the R&D activities undertaken.
- 4.6 Each administrator has a different process to determine the eligibility of the activities or expenditure. DISER has a suite of different types of findings to determine the eligibility of the activities. Findings are the formal mechanism through which the eligibility of R&D activities are determined. The ATO undertakes assurance and compliance reviews and audits on the expenditure aspect of the programs, often in conjunction with other tax matters.

The Board's Analysis

- 4.7 Through the Board's consultations it became apparent that there are frequently long timeframes to complete audits and findings by DISER and the ATO, respectively.
- 4.8 Consultees advised the Board that the long timeframes to complete reviews leads to confusion and frustration for companies awaiting outcomes on the eligibility of their activities and/or expenditure. In many instances, working capital critical for company continuity is delayed as a result of the time taken to complete reviews and ultimately provide refunds.
- 4.9 In respect of the eligibility of R&D activities, there are different types of findings that can be undertaken by DISER. These are broadly split into those initiated by DISER or initiated by the company. Findings initiated by DISER are undertaken where they are concerns over the eligibility of the R&D activities. Findings by the company fall into Advance or Overseas Findings:
 - A company can apply for an Advance Finding for DISER to assess the R&D activities before they are undertaken. If deemed eligible, the company then has certainty that the R&D activities are eligible, and this decision is binding on the Commissioner of Taxation.
 - A company can apply for an Overseas Finding where R&D activities cannot be conducted in Australia (for a specific reason). A company must have an approved

Overseas Finding in place to register those overseas R&D activities as part of its R&DTI claim.

4.10 The Board received feedback from a number of consultees indicating the lengthy timeframes taken by DISER to complete findings and in particular, the Advance and Overseas Finding process. The feedback was evidenced in a number of written submissions.

4.11 Cochlear expressed the view that:²⁶

Slow timeframes from both regulators and hold ups are moving companies overseas. Advanced Finding does not reduce the taxpayer's administrative burden.

4.12 EY recommended that:²⁷

The outcomes of reviews by both the ATO and DISER be provided to taxpayers within 30 days, in line with the requirements placed on the taxpayer to provide information in response to said review.

4.13 During the consultation process, the following case study was provided by a small company operating in the Biotech industry. The case study highlights the need for improvements in administrator review timeframes given the significant impacts for companies claiming benefits under the R&DTI program.

26 Submission 10, p.2.

27 Submission 13, p.7.

CASE STUDY 2 – IMPACT OF REVIEW TIMEFRAMES

A Biotech company has been making applications in the R&DTI program for over 20 years and has applied for combinations of Advance and Overseas Findings in that period. The company does not use the service of a tax agent, applying for the program themselves.

The company highlighted to the Board an experience they had in applying for an Advance and Overseas Finding in 2019. The company noted this was a *'drawn out'* process which was very repetitive as there were several Requests for Information (RFI) submitted to the company in that period.

From the date of submission of the Advance Finding to the final approval date was 367 days. Due to length of time to resolve the finding, there was a significant delay in applying for the R&DTI incentive and a consequential effect of receiving a refund well after the expenditure was incurred. The company noted this left them with a shortfall in working capital while this process was resolved.

There was significant investment in time and resources for the company. As a small company preparing their own application, the completion of the application for the Advance and Overseas Finding and the responses to RFIs were a *'major distraction to day-to-day work and building the company'*.

The company noted how important the R&DTI program was to the operations and while they continue to participate, they would like to see improvements in working with the co-administrators and timeframes to complete the findings.

- 4.14 Consultees also raised with the Board issues in relation to the time taken by the ATO to complete audits. On occasion, these delays were caused by the separate reviews undertaken by the co-administrators not being aligned. This is explored further in Chapter 5 in the Program Charter.
- 4.15 In light of the feedback received from consultees, the Board considered whether the R&DTI program should require the co-administrators to comply with statutory timeframes to engender a timely response to requests from companies seeking to register and make claims under the R&DTI program or whether publishing agreed timeframes publicly would achieve the same result.
- 4.16 The Board notes that under certain Australian Government programs, there is a use of statutory timeframes. For example, statutory time frames are imposed on the Treasurer in relation to prohibiting a proposal that would be contrary to the national interest

under the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (FATA) which gives legislative support for the Government's foreign investment policy.²⁸

- 4.17 The Board notes that the bodies such as the Foreign Investment Review Board (FIRB) publishes timeframes to complete applications, usually within 30 days to complete the process as outlined in the FATA. FIRB advises applicants on its website about increases in processing times which may be extended beyond the 30 days.²⁹
- 4.18 Notwithstanding the above precedent the Board is of the view that statutory timeframes are not required. Rather the Board recommends that the co-administrators agree to implement and publish transparent timeframes. This approach will balance the need to ensure accountability and transparency by the co-administrators and allow flexibility in timeframes to complete reviews and audits. The flexibility will allow the timeframes to be reviewed periodically and reset as appropriate in relation to the matters being reviewed. This will ensure that compliance reviews progress efficiently.
- 4.19 The Board's recommendation satisfies the regulator performance practice to engage genuinely and regularly with stakeholders, including on the development of and reporting against meaningful performance measures, as set out in the Guide.

RECOMMENDATION 4

Transparent and clear timeframes for DISER findings and ATO audits should be implemented, with timeframes on expectations of completion of findings and audits publicly available and reviewed periodically.

Technical capabilities of the co-administrators

- 4.20 During the consultation process, consultees informed the Board of the improvements made in connection with the technical understanding and training of both DISER and ATO assessors of R&DTI registrations and claims. However, consultees did highlight areas where further improvements could be made:
- There are, at times in complex cases, challenges in the DISER and ATO assessors understanding of the nature of the R&D activity which can have a negative impact on a registration and claim at the outset of the engagement.

28 If the Treasurer is given a notice that a significant action is proposed to be taken, the Treasurer must make a decision within a certain period (generally, within 30 days of receiving the notice, or within an additional period of up to 90 days from the registration of an interim order).

29 Foreign Investment Review Board, *Website*, viewed 23 November 2021 <Increase in processi...~https://firb.gov.au/about-firb/news/increase-processing-times>

- DISER and the ATO can at times rely on information found on websites (which may be high-level and have limited detail) and without effectively considering the views of the experts provided by the companies.
- There were instances where DISER and ATO assessors did not adhere to good governance principles in being fair, consistent and transparent in conducting reviews.

4.21 Further evidence was provided to the Board in relation to the technical capability of the co-administrators in the following written submissions:

Chartered Accountants Australia and New Zealand noted:³⁰

The feedback from CA member R&D practitioners is that there is a perceived technical deficiency with AusIndustry at the level of the officers conducting reviews. This means that technical understanding of R&D projects and activities is not seen as being up to the standard expected by applicants and other stakeholders.

The Australian Small Business and Family Enterprise Ombudsman noted:³¹

AusIndustry should ensure when reviewing the eligibility of small businesses' registrations, that sufficient expert industry advice is utilised.

4.22 The Board agrees that there are areas for improvement in the engagement with the co-administrators. As an example, the Board recommends the development of an R&DTI Program Charter which outlines what a company can specifically expect when engaging with the co-administrators and the R&DTI program. The R&DTI Program Charter should implement a consistent and professional experience that every company can expect when participating in the R&DTI program. The development of an R&DTI Program Charter will ultimately assist in improving the overall compliance experience. The R&DTI Program Charter is discussed further in Chapter 5.

4.23 The Board acknowledged the work of DISER in bringing in external experts, on certain occasions, to provide advice on complex cases. An example of this is the use of Data61, CSIRO's data and digital specialist data sciences arm, to assist DISER in determining the eligibility of R&D activities in complex software cases.

4.24 The co-Administrator's submission highlights the recent changes they have made to procedural fairness and engaging experts:³²

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

30 Submission 9, p.13.

31 Submission 4, p.2.

32 Submission 16, p.23.

of Examination of Evidence Reports with Findings Certificates to provide greater clarity for stakeholders.

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.

- 4.25 The feedback provided to the Board suggests that engagement with experts like Data61 has been well received by stakeholders and that bringing in subject matter experts has enhanced the decision-making process. DISER should continue to utilise these experts and consider using experts in other sectors where they can be brought in to assist with complex cases to supplement the skills DISER has in determining eligible R&D activities.

OBSERVATION 3

The Board encourages continued training and engagement of technically capable assessors and notes that the engagement of experts such as those from Data61 to assist in complex cases has been a positive step. The Board encourages the continuation of this type of engagement and potentially expanded to other program areas.

Program Guidance and Education

- 4.26 DISER undertakes education activities and both agencies provide guidance and support to companies accessing the R&DTI. This includes the opportunity to apply for an Advance Finding to receive a binding decision on R&D eligibility.
- 4.27 To improve registration of eligible activities and the claiming of associated eligible expenses, the ATO and DISER have released targeted guidance (including in the form of 'getting it right' guides) for certain industry sectors.
- 4.28 The ATO and DISER have also issued several joint Taxpayer Alerts to raise concerns with companies and their advisors of certain R&D claims and in particular, concerns in three major industry sectors: software development, agriculture and building and construction.
- 4.29 DISER and the ATO noted in their joint submission that:³³

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

33 Submission 16, p.22.

recently, guidance on registrations and findings has been embedded in DISER registration application forms.

4.30 The European Commission (EC) noted in its report, *Mutual Learning Exercise: Administration and Monitoring of R&D tax incentives*, published in 2017 that the:

'administration rules and practices of R&D tax incentive schemes must be understandable and user friendly if they are to induce businesses to undertake more R&D. The outreach efforts made by the administrators in the different countries vary considerably both in intensity and methods used. Some meet companies face to face, some give special assistance to first time applicants, and some have websites with considerable guidance material. Many agencies arrange workshops, conferences and webinars to assist both potential claimants as well as intermediaries'.³⁴

4.31 The EC further noted in its report that:

'over time most countries have, in response to an increasing need by companies, progressively expanded their outreach activities. Significantly, it also observed that the use of unregistered or unregulated consultants is widespread and perceived as a problem for some countries. It considered that greater provision of guidance would help address this issue. In addition, it noted that administrations could offer guidance on the sensible use of consultants, and the type of contracts that should be avoided'.³⁵

The Board's Analysis

4.32 During the review, a common theme raised by consultees was the inadequate program guidance and education of the R&DTI program by the administrators. In particular, consultees raised concerns about the scope and currency of such guidance and education delivered by both administrators. Many companies felt that the R&DTI program is very complex and that they required an external consultant to assist them in participating in the program. This included sophisticated and well-established large companies.

4.33 Consultees raised the following issues with the Board regarding program guidance and the impact on program participants:

- There is almost no guidance which is positively framed, rather guidance currently reflects what cannot be claimed. There is the opportunity for the co-administrators to develop guidance on the benefits of the R&DTI program and who the program is designed for, in order to set the foundations and tone for participation

34 *Mutual Learning Exercise: Administration and Monitoring of R&D tax incentives*, European Commission, Horizon 2020 Policy Support Facility, 16 February 2017, pp 11 & 26.

35 *Mutual Learning Exercise: Administration and Monitoring of R&D tax incentives*, European Commission, Horizon 2020 Policy Support Facility, 16 February 2017, p. 29.

- Guidance (from both administrators) could be more expansive by including information on selecting a tax agent (including a suggested checklist)
- The changing/updating of guidance and which version of the guidance can be relied upon when preparing advice to companies
- The ATO should provide simplified guidance on the claiming of overhead allocations³⁶
- Both agencies should collaborate to create clear joint guidance so there is a shared view from the co-administrators
- The need for binding guidance to provide certainty on particular program issues.³⁷

4.34 The abovementioned issues were raised in a number of the written submissions. As an example, in relation to the guidance content itself, PwC stated that:³⁸

Given the R&DTI is self-assessed, the best outcomes are achieved when certainty can be expected by claimants (that is,, no surprises). This requires clear and relevant guidance materials. We note that the ATO has not issued a final public ruling on R&D since the new law was implemented but has issued five Taxpayer Alerts. AusIndustry does not issue rulings or an equivalent of an ATO Interpretative Decision (ATOID), which would be beneficial for education, transparency and ultimately certainty.

4.35 EY commented on the changes to guidance and its application at the time of an administrator review or audit when it stated that:³⁹

Frequent changes to guidance material, as well as the application of guidance material that was not available at the time creates a lack of certainty surrounding the application and review process which can act as a disincentive for some claimants. As an example, claimants are required to use available guidance and materials at the time of lodgement, however when reviewed recent guidance is used by the administrators to counter any arguments made by the claimant. In our opinion it is unreasonable to expect claimants to adhere to guidance that was not released at the time of lodgement. This has also led to more guidance being published via the relevant administrator websites rather than as official documentation, making it difficult to detect any changes, as well as archive historical guidance.

4.36 EY similarly commented on the need to update guidance material and websites:⁴⁰

That guidance material be updated appropriately including websites and documentation to outline the segregation of duties more clearly between the two administrators; and

36 The Board notes that such guidance was withdrawn by the ATO in 2010 but has not yet been replaced.

37 Submission 12, p.4, para 7.

38 Submission 14, p.4.

39 Submission 13, p.10.

40 Submission 13, p.4.

that better delineation and clarity be provided in regard to which administrator is responsible for which components of the R&D Taxpayer Alerts as they cover both expenditure and eligibility concerns.

4.37 In relation to the use of websites for providing guidance, the CTA pointed out that:⁴¹

Website information on the incentive has improved, but some of it is not user friendly, needs updating or better co-ordination between ATO and AusIndustry. For example, the ATO R&D website guidance still refers to the EM of the old law and has not been updated for the law effective from 1 July 2021.

4.38 In assessing the feedback received by consultees in relation to guidance, the Board has also considered international experiences regarding better practices in providing guidance. The case study below highlights an international approach which could be applied to improve guidance issued under the Australian R&DTI program.

CASE STUDY 3 – INTERNATIONAL GUIDANCE APPROACH

Through viewing international models of R&D programs, the Board has identified different ways in which regulators in other countries approach guidance.

One example is the Internal Revenue Service (IRS) approach to providing guidelines for claiming software development activities in the Research Credits Program. The webpage ‘Audit Guidelines on the Application of the Process of Experimentation for all Software’ are examiner guidelines to aid in risk analysis of software development activities.

Crucially, these guidelines rank software development activities at high, medium and low levels of risk of constituting an eligible software activity. Low risk is those activities that rarely fail to constitute qualified research through to high-risk activities that often fail to constitute qualified research under the relevant legislation. The guidelines provide examples of the types of activities that fall under each category. The guidelines were last refreshed in March 2021.

The Board is of the view that this approach of providing not only examples of activities that may not qualify for the program but activities that do or should qualify for the program would be a positive step forward in the administrator’s guidance practices.

4.39 In light of the above feedback received and observations from regulators in comparative jurisdictions, the Board makes the following recommendation which satisfies the regulator performance practice to provide guidance and information that is relevant, clear, concise and easily accessible to help entities understand their obligations and responsibilities to encourage voluntary compliance.

41 Submission 12, p.4.

RECOMMENDATION 5

Clear and concise guidance with examples should be released jointly between the two administrators including an overarching guidance document or manual. Changes to guidance and application dates should be notified in the document or manual. The ATO should finalise and release outstanding guidance products on overheads and draft determinations. Also, the administrators should give consideration to a joint webpage where guidance could be published.

Program Assurance

- 4.40 The need for assurance and certainty for companies participating in the R&DTI program was a frequent issue raised with the Board in its consultation sessions.
- 4.41 The Board considered assurance products for equivalent R&D programs in comparative jurisdictions. As an example, the UK R&D program provides certainty and assurance for qualifying SME companies when making their first R&D claim by providing Advance Assurance. If Advance Assurance is granted, any R&D claims in the first three accounting periods will be accepted provided they are in line with what was initially agreed.
- 4.42 Another feature of the UK R&D program is the use of Customer Relationship Managers (CRMs) to manage HMRC's relationships with the 2000 largest and most complex companies. The CRM framework helps to improve the handling of complex issues and allows for risk assessment, including R&D tax relief claim risks, to take place against a published framework. Other jurisdictions such as NZ and CAN provide similar programs for its claimant companies.
- 4.43 Further detail in relation to assurance products in comparative jurisdictions is set out in Chapter 6 of this report.
- 4.44 Since 2016, the ATO has applied the concept of 'Justified Trust' through a program of assurance reviews of the top 100 taxpayers to ensure large public businesses, multinationals and superannuation funds are paying the right amount of tax and have the appropriate tax governance processes in place. The program has been increased to the next 1,000 public groups, plus a top 500 and top 5,000 program in the privately owned and wealthy groups sector.
- 4.45 Where a top 100 taxpayer attains an overall high level of assurance under the justified trust program, it means the ATO have high confidence that the taxpayer has complied with Australian income tax laws. Consequently, the ATO will proceed with a future engagement approach to focus on maintaining the taxpayer's high level of assurance via its 'Monitoring and Maintenance' approach. This approach applies to taxpayers for the two income years following an overall high assurance outcome.

- 4.46 Feedback provided to the Board indicated that Justified Trust was an important part of a taxpayer's tax compliance strategy and governance framework. Consultees indicated that whilst large taxpayers would get clearance on all other of their tax matters, they would encounter difficulty in getting certainty in relation to their R&DTI portion of a Justified Trust review. Justified Trust overall is an important marker for Company Board's in providing certainty on tax matters, including the R&DTI program.

The Board's Analysis

- 4.47 The Board notes that certainty and assurance in respect of the R&DTI program was another consistent theme raised by consultees during the consultation process. The feedback from consultees included the following:

- The ATO should consider a company's R&D tax position through the lens of Justified Trust
- The ATO and DISER's timeframe for periods of review should be reduced to improve consistency and certainty for companies
- As noted above, through the Justified Trust program, the ATO provides a level of assurance for a number of tax matters but in evidence provided to the Board, it does not always extend to assurance of the R&DTI portion of a taxpayer's claim.

- 4.48 The written submissions provided to the Board highlighted that this issue impacted program participants in a number of different ways. Examples are set out below.

- 4.49 PwC provided that:⁴²

Although Ausindustry visits to client sites were common during the early stages of the program, during more recent years, Ausindustry reverted to a less collaborative approach and at one stage refused to undertake site visits that could better inform decisions of eligibility.

- 4.50 EY similarly commented on broad statements of ineligibility & imprecise language which exacerbates uncertainty:⁴³

It is our recommendation that if the regulators request an examination of all or part of an R&D entities [sic] claim, that they undertake reasonable due diligence in understanding the activities by consulting with appropriate scientific representatives including those of the applicant and independent third parties. This would reduce the occurrence of large in-depth reviews.

42 Submission 14, p.4.

43 Submission 13, p.5.

4.51 In relation to the ATO's Justified Trust program, CAANZ stated that:⁴⁴

Justified Trust and R&D – 'The ATO refuses to give any assurance on R&D, so it is excluded from the scope of Justified Trust because of AusIndustry's involvement. Therefore, a company can only get an "amber light" in the Justified Trust report simply because they have an R&D claim as part of their tax affairs.'

4.52 The Board is of the view that there is scope to expand the Justified Trust program by more readily including the R&DTI program in its outcome reports. Feedback from consultees indicate that while Justified Trust can include R&D claims, there were many of examples where R&D was not included in the review and ultimately is impacting the overall Justified Trust rating.

4.53 The Board considered other options of applying certainty and assurance, particularly to smaller taxpayers. The Board believes a mechanism such as Assurance Letters could provide certainty to smaller companies where the co-administrators could write to small / low risk companies to offer them a form of assurance on their R&D registrations / claims.

4.54 The Board acknowledges the potential additional resource requirements on both co-administrators of implementing this recommendation of providing further certainty and assurance. However, the Board considers that these additional resources and costs will be outweighed by the resulting positive impact that the recommendation will have on companies that participate in the R&DTI program.

4.55 The Board makes the following recommendation which satisfies the regulator performance practice to implement innovative approaches in considering regulatory or policy issues such as 'regulatory sandboxes', as set out in the Guide.

RECOMMENDATION 6

The Justified Trust program should be more effectively extended to the R&DTI program for larger companies and for smaller companies processes such as Assurance Letters be considered to provide certainty for those companies.

Issuing of Binding Determinations

4.56 The lack of binding determinations by DISER and the need for joint determinations by both agencies (where applicable) was a theme raised during the consultation process and is directly related to the provision of program certainty and assurance to the companies.

44 Submission 9, p.11.

- 4.57 The Board notes that under the *Industry Research and Development Act 1986* the Board of IISA may make determinations regarding the circumstances and ways in which it will exercise its powers or perform its functions or duties in relation to the R&D Incentive. These determinations are binding on the Board of IISA. The Board understands DISER has developed a R&DTI Determinations Framework to guide the process of making a determination.
- 4.58 The ATO has the power to make binding determinations in respect of its role under the R&DTI Program.

The Board's Analysis

- 4.59 During the review, the Board received feedback that companies faced increased uncertainty as there was a lack of binding determinations. The examples of feedback received from consultees is set out below.
- 4.60 PwC stated that:⁴⁵

Part of the reason for claimants' lack of certainty and confidence in the consistency of the regulator's interpretations during reviews stems from the apparent hesitancy of AusIndustry to clearly acknowledge the findings of the FFC and the AAT and to quickly adopt the views in public guidance and reviews in progress.

This requires clear and relevant guidance materials. We note that the ATO has not issued a final public ruling on R&D since the new law was implemented but has issued five Taxpayer Alerts.

- 4.61 In relation to the use of websites, the CTA pointed out that:⁴⁶

Whilst current guidance has improved, there is currently no binding AusIndustry guidance (other than an IISA Board Finding). The IISA Board should consider using its powers to make determinations under the amendments contained in Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Act 2020 possibly by making current non-binding guidance (such as software guidance) into formal determinations. AusIndustry could also consider creating a list of potential issues for public consultation.

- 4.62 The Board understands that DISER expects the first determination to be made under the new R&DTI Determinations Framework will relate to clinical trials and that work on the draft determination has commenced.⁴⁷

45 Submission 14, p.3.

46 Submission 12, p.5.

47 Submission 16, p.33.

- 4.63 An example of an overseas administrator providing certainty to an applicant is the US Internal Revenue Service (IRS) which has issued guidance to Large Business & International examiners in determining whether a taxpayer in the pharmaceutical, biotechnology and agriculture industries has appropriately computed the credit for increasing research activities under the US Internal Revenue Code⁴⁸. This guidance provides that the development of pharmaceutical drugs and therapeutic biologics (medicine) may be broken down into four stages: Discovery and Preclinical Stage, Clinical Trial Stage, Regulatory Review Stage and the Post Approval Stage.
- 4.64 After the US Food and Drug Administration (FDA) approves the Investigational New Drug Application (INDA) in stage two, IRS examiners should not challenge the amount or the eligibility of qualified research expenses (QREs) paid or incurred by the company undertaking the development of the medicine during the taxable year and the company provides a Certification Statement about the QREs.
- 4.65 In the context of issuing binding determinations, the Board suggests that the administrators should consider replicating this accelerated FDA approval and automatic acceptance of a company's QREs process in industry sectors such as pharmaceutical and biotechnology.
- 4.66 The Board makes the following recommendation which satisfies the regulator performance practice to provide guidance and information that is relevant, clear, concise and easily accessible to help regulated entities understand their obligations and responsibilities to encourage voluntary compliance, as set out in the Guide.

RECOMMENDATION 7

DISER (from the powers of IISA) and the ATO should issue their binding determinations in a timely and efficient manner, to assist companies in understanding their obligations of the program.

Contingency Fees

- 4.67 A contingency fee agreement is an arrangement where the fee of the R&DTI consultant or tax agent is conditional on the company's R&DTI claim being successful and calculated by reference to the quantum of that claim. The contingency fee may be set as a fixed

48 United States IRS 2012, Guidance for Computing and Substantiating the Credit for Increasing Research Activities under Section 41 of the Internal Revenue Code for Activities Involved in Developing New Pharmaceutical Drugs and Therapeutic Biologics, Washington, viewed on 3 November 2021 <GuidanceforComputing...~https://www.irs.gov/businesses/guidanceforcomputingsubstantiatingpharmaceuticaldrugtherapeuticbiologics>

amount or a fixed percentage of the R&DTI offset the company receives after its Company Tax Return is processed by the ATO.

4.68 The use of contingency fees was raised in a number of the consultation sessions and included the following:

- the quantum of the fee may not represent the amount of work undertaken by the consultant / tax agent and remuneration was directly linked to a successful claim which may impact approaches to making claims
- refunds of fees may be required if upon audit the amount of the claim is reduced.

4.69 In the Board's discussion with international regulators about the operation of their R&D programs, there was some peripheral discussion about the use and prevalence of contingency fees. In some jurisdictions (such as the UK) the imposition of such fees (for example; 20 per cent or 25 per cent the benefit received from HMRC) is part of market practice. In other jurisdictions such as NZ, the agreement to impose the contingency fee between the consultant/agent and the company may render the consultant/agent to be liable for a penalty if the arrangement involving R&D tax credits results in a shortfall penalty for an abusive tax position being imposed on the company.⁴⁹

4.70 The extent of the use of contingency fee agreements in the UK market is exemplified by a UK commentator calling for contingent fees to be fully embraced by clients seeking the best possible outcome for their R&D and innovation tax credits strategy stated that:⁵⁰

Contingent fees mean the R&D consultant is outcome focused, whereas under a fixed fee arrangement consultants will charge larger companies for research and review work, creating an incentive to pad out the time taken to build a claim, but no incentive to maximise the value of the claim. It means fixed fees become a very expensive way to charge for an uncertain outcome and lack integrity as a result.

4.71 Following the consultation process, it became clear to the Board that the use of contingency fees is no longer as widespread in the Australian R&DTI advice area of the accounting, legal and consulting professions, as it had been in previous years.

49 Sections 141EB and 141EC, *Tax Administration Act 1994* (NZ) which provides that a promoter of an arrangement where you either provide services on a contingency fee basis in relation to R&D tax credit claims. If you are a promoter of an arrangement involving R&D tax credits, you may be liable for a promoter penalty. if the arrangement results in a shortfall penalty for an abusive tax position being imposed on a party to the arrangement. An arrangement includes any agreement, contract or understanding, whether it is enforceable or not.

50 Steve Phillips 2019, *GovGrant urges separation of audit and consultancy in order to embrace contingent fees for consultancy services*, London, viewed 3 November 2021, < <https://www.govgrant.co.uk/latest-thinking-news-and-views/govgrant-urges-separation-of-audit-and-consultancy-in-order-to-embrace-contingent-fees-for-consultancy-services/>>

- 4.72 The Board did not consider the use of contingency fee agreements in the Australian R&DTI program on the basis that they do not have an impact on companies understanding their obligations under the R&DTI program.
- 4.73 For completeness, the Board notes that the issue regarding the use of contingency fees was not only problematic for the Australian R&DTI program in the past (noting that the use of contingency fees has reduced), but remains so for other industries in Australia. For example, the acceptance or prohibition on contingency fees in the Australian legal profession has been the subject of reviews and reports over the last decade.⁵¹

OBSERVATION 4

The use of contingency fees in the R&DTI program is not as widespread feature and information provided to the Board indicates that the use of these types of fees by the accounting, legal and consulting professions has reduced. However, if this changes (that is, contingency fees start to become a regular feature), the Government should consider whether this fee structure should continue and its bearing on the integrity of the program. In doing so the Government should take into account how other jurisdictions have dealt with this market practice.

Compliance Costs

- 4.74 As part of the review, the Board sought to gain an informed understanding of the impact and level of compliance costs incurred by companies accessing the R&DTI program.
- 4.75 The costs of compliance in relation to the R&DTI program was a common issue raised by a number of consultees.

Compliance cost survey

- 4.76 In addition to the submissions from the CTA⁵² and the co-administrators,⁵³ the Board conducted its own research by carrying out a compliance cost survey.⁵⁴ The methodology used was a targeted survey that was undertaken by a select number of companies that

51 Productivity Commission, Access to Justice Arrangements (Inquiry Report No 72, 5 September 2014); Integrity, Fairness and Efficiency – An Inquiry into Class Action Proceedings and Third Party Litigation Funding, Australian Law Reform Commission Report 134, December 2018

52 Submission 12, p.9 & 10.

53 Submission 16, p.18 & 19.

54 The Board sought answers to 15 questions in a questionnaire which was sent to select consenting companies from both the R&DTI claimant entity with an annual turnover less than \$20 million (Small Entity) category and the R&DTI claimant entity with an annual turnover greater than \$20 million (Large Entity) categories.

volunteered to provide feedback on the compliance costs and issues involved in participating in the R&DTI program.

- 4.77 The methodology used and the survey features about this small-scale survey are set out in **Appendix B**, along with relevant extracts from the CTA and co-administrators submissions.
- 4.78 For the purpose of the Board's research, compliance costs include the time and resources required to complete:
- the registration process with DISER
 - a programme tax schedule as part of the Company Tax Return with the ATO
 - maintaining proper records to justify the activities; responding to reviews and audits
 - the costs of tax agents/R&D consultants.⁵⁵

Summary of Survey Results

- 4.79 The main drivers for compliance costs in the R&DTI program as identified in the responses to the survey questionnaire are set out as follows:
- Costs of external advisers/consultants engaged by the company.
 - Registration process (such as gathering evidence or obtaining independent advice on eligibility of activities, for example, reports and tests) including documenting all registered claims in a manner that is supported by DISER.
 - Lodgement of the R&D Schedule with the Company Tax Return (maintaining records and expenditure items for labour and non-labour inputs).
 - Preparing the project descriptions for DISER in a clear manner that confirms eligibility.
 - Preparatory work undertaken on potentially eligible projects to assess whether the activities meet the eligibility criteria. Compliance costs are incurred on the assessment of these types of projects even though they may not proceed to the claim process.
 - Cost for separate lodgements per year to participate in the program and additional cost for submitting an Advance and/or Overseas Finding.
 - Audit/compliance process (preparing and responding to audits and compliance queries by DISER and the ATO).

55 A more detailed explanation of the Board's definition of 'compliance costs' is contained in Appendix B.

- 4.80 The most prominent driver of compliance cost identified through the survey is the costs of external advisers/consultants engaged by the company. This is followed by the registration process such as gathering evidence or obtaining independent advice on eligibility of activities, for example, reports and tests; and then lodgement of the R&D Schedule with the Company Tax Return (which includes maintaining records and expenditure items for labour and non-labour inputs).
- 4.81 In response to the survey questionnaire, various suggestions to reduce the regulatory burden, and therefore reduce compliance costs, were made and are listed below:
- Simplification of the process of lodgement including simplification of the documentation required. Other areas of the tax system have implemented simplification rules, and the R&DTI program could benefit from implementing a similar approach.
 - Greater collaboration and information sharing between DISER and the ATO so that costs paid to R&DTI consultants can be reduced.
 - Task or functional alignment between DISER and the ATO would reduce compliance costs paid to R&DTI consultants on the basis that the costs spent on DISER queries currently are in addition to the costs incurred in relation to responding to ATO queries.
 - Complete transparency by DISER and the ATO in relation to changes to rules and interpretation concerning the R&DTI process on their respective websites (including the date of change) would reduce the re-work in defending a company's claim.
 - DISER and the ATO consider implementing an audit/review service charter whereby their review and turnaround times are defined and agreed upon. The survey indicated that long drawn-out reviews are costly and create a great deal of uncertainty for the claimant company.
- 4.82 It is worth highlighting that the suggestions to reduce the regulatory burden drawn from the responses in the small-scale survey are similar, in many instances, to the Board's recommendations in this report. Additionally, the drivers of compliance cost broadly align with the issues that were raised by consultees and stakeholders to the Board during the consultation process.
- 4.83 The abovementioned similarities confirm the operational and governance issues identified during the review and is indicative of broader business support for recommendations raised in this report.

CTA and co-Administrator Submissions

- 4.84 The CTA submission reported that the cost of compliance for their members is \$214,000 on an average incentive claim of around \$2.3 million (the permanent difference of 8.5 per cent of the eligible R&D expenditure) and that the cost of compliance is on average

about 9 per cent of the cost of claiming the incentive for large corporates before taking into account any cost associated with subsequent ATO or DISER review activity.

- 4.85 The co-Administrators in their joint submission referenced the Centre for International Economics (CIE) report, which was commissioned by DISER to review the program. In particular, the CIE measured the administration and compliance costs of the R&DTI program, 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 and that a significant share of this (around 46 per cent) was paid to consultants.
- 4.86 The submissions made by the CTA and co-Administrators in relation to the cost of compliance in the R&DTI program provided useful context to the Board in understanding the compliance costs involving in registering and making a claim under the R&DTI program.

Conclusion

- 4.87 The Board's compliance cost survey identifies main drivers for compliance costs in the R&DTI program which broadly aligns with the issues raised by consultees during the consultation process. The Board's recommendations set out in this report will assist with addressing these issues and creating an efficient and effective program which should ultimately result in a reduction to the compliance costs for companies participating in the R&DTI program.
- 4.88 The Board notes that any reduction in compliance costs in participating in the R&DTI program is an important objective as any cost savings can be used by companies to pursue their R&D activities.

CHAPTER 5: GOVERNANCE ISSUES FROM COMPANY PARTICIPATION IN AND EXPERIENCES WITH THE R&DTI PROGRAM

KEY POINTS

- The Board has identified a number of governance improvements to the dual administration model to make it more efficient and effective. The development and release of a R&DTI Program Charter alongside improved program reporting, will enhance transparency and the company experience.
- Feedback to the Board has indicated that at times there can be confusion in the roles of the two administrators, with clarity needed to re-establish clear roles.
- DISER and the ATO are unable to undertake a joint Alternative Dispute Resolution process which results in a number of cases heading to costly AAT hearings. The Board recommends that an option is provided for an Alternative Dispute Resolution mechanism that involves all parties.

5.1 The purpose of this chapter is to examine issues brought to the Board through stakeholder consultations and written submissions, related more broadly to the potential improvements in the governance of the R&DTI program.

Roles of the co-administrators

5.2 As outlined in Chapter 2 of this report (Current Administration Model), DISER and the ATO are co-administrators of the R&DTI program. Through the consultation process, the Board sought to understand from consultees whether the roles of the co-administrators were well understood and, if not, how this could be enhanced.

5.3 The feedback provided to the Board indicated, that at a high level, the roles of the two administrators are broadly understood but more so by tax agents, and less so by the companies themselves.

The Board's Analysis

5.4 Consultees advised the Board that there has been a 'blurring of lines' or confusion over the roles of the administrators.

- 5.5 In particular, PwC noted issues with the roles of the co-administrators:⁵⁶

Claimants are less certain than ever about both the eligibility of activities and the expenditure that can be claimed in relation to those activities...A second aspect is that it has been observed that the ATO often makes decisions about the eligibility of activities when clearly this is not their mandate. The basis and reasoning for the ATO doing this is tenuous but allows for questioning and denial of expenditure claims often with a degree of ambiguity.

- 5.6 The Board acknowledges that the ATO has the power to make determinations over the nexus between the R&D activities and expenditure, and that at times this may cause confusion over the roles of the administrators. However, numerous examples were provided to the Board of the ATO seemingly moving into the analysis of R&D activities without involving DISER in the case/discussion. Based on the feedback received, it appears that the nexus of expenditure audits can be a source of confusion which results in blurring of roles in determining the eligibility of R&D activities.

- 5.7 A number of written submissions received by the Board, highlighted *obiter dicta*⁵⁷ in a 2021 Full Federal Court decision *Commissioner of Taxation v Auctus Resources Pty Ltd* (Auctus Resources case).⁵⁸ It reads:⁵⁹

Registration by an R&D entity of particular activities as being 'core R&D activities' or 'supporting R&D activities' under s 27A of the IRD Act, whilst a necessary requirement to be eligible for the tax offset refund, is not conclusive of such activities having the character of being 'R&D activities'. Either the Commissioner or the Board might conclude that they are not. The Board might do so by making findings under ss 27B or 27J. If the Board has not made findings (which is often the case), the Commissioner might form his own views about whether a taxpayer's activities are R&D activities. As the legislation currently stands (tax offset refunds being part of the process of assessment), if the Commissioner took the view that particular activities were not R&D activities and there was no binding finding about that, then the Commissioner would have to act on his view in performing his assessment obligation under s 166 of the ITAA 1936. In fulfilling his duty, the Commissioner is bound by a finding made by the Board if one happens to exist (s 355-705), but is otherwise responsible for administering the tax laws according to their terms. The Commissioner is not bound by the taxpayer's self-assessed view that their activities are 'R&D activities'. If it were otherwise, the taxpayer's opinion about their activities constituting R&D activities would, in the absence of a finding by the Board, be determinative of this aspect of the taxpayer's eligibility to the tax offset refund.

56 Submission 14, p.3.

57 A judge's expression of opinion uttered in court or in a written judgement, but not essential to the decision and therefore not legally binding as a precedent.

58 Commissioner of Taxation v Auctus Resources Pty Ltd [2021] FCAFC 39

59 Ibid, para 32.

- 5.8 The Board is not in a position to comment on that obiter dicta. The submissions highlighted concerns over the clarity of the roles of the administrators and that the commentary in the judgement, in the view of some consultees, further exacerbates this uncertainty.
- 5.9 Other evidence provided to the Board through the written submissions further highlights this issue with potential blurring of the lines of responsibility and confusion over the two administrators' roles.
- 5.10 The Australian Small Business and Family Enterprise Ombudsman identified a lack of clarity as an issue:⁶⁰

The ATO and AusIndustry should provide clarity of their roles in the R&DTI, including their responsibilities and limitations. A significant concern of the dual administration model is the lack of clarity around the roles and limitations of the ATO and AusIndustry. Small businesses and their advisers tend to have varying experiences with the ATO and AusIndustry, usually with one agency causing significant burdens to small businesses' registrations and claims.

- 5.11 As part of the CTA Submission, members were asked to comment on what they see as the key issues for the Board's review with accountabilities a clear issue:⁶¹

Clearer administrative accountabilities are needed between AusIndustry, the Industry Innovation and Science Australia Board (IISA Board) and the ATO, especially after the Auctus decision clarified the respective roles can overlap as a matter of law...The CTA survey confirms the uncertainty in the market as to the roles of the ATO, AusIndustry and the IISA Board. Only 3 per cent of the survey respondents indicated the accountabilities of both administrators are clear.

- 5.12 Based on the consistent feedback provided through this review, the Board agrees that there is a need to improve the clarity and definition of the roles of the co-administrators in the R&DTI program.
- 5.13 The feedback received by the Board from consultees on how to address this issue has been varied (that is, whether any improvement is made via legislation or via other avenues). The Board is of the view that it may not be necessary to enact legislative change to clarify the roles of each agency.
- 5.14 In conjunction with Recommendation 9 (Development and Implementation of an R&DTI Program Charter), the Board recommends that ATO and DISER should provide clarity of their roles in the R&DTI program, including their responsibilities and limitations.

60 Submission 4, p.1.

61 Submission 12, p.3.

RECOMMENDATION 8

The ATO and DISER should provide clarity of their roles in the R&DTI, including their responsibilities and limitations. A Program Charter could be the mechanism to establish the clarity of the roles. Refer to Recommendation 9 for additional information on the Program Charter.

R&DTI Program Charter

5.15 A key aspect to the governance of any Government program is the expectations a company has of engaging with the program and its administrators. Evidence provided to the Board has identified several areas, in the ATO's audit processes or DISER's Finding processes, where there have been issues with those processes.

5.16 The feedback provided to the Board identified the following issues:

- There are often delayed timeframes within the review processes, with companies asked to provide evidentiary documentation to support their R&D activities in very tight timeframes. This results in a strain on company's resources required to collate and deliver all the required documents to meet either or both administrator's relevant timeframes. Once the information is provided to the ATO or DISER, consultees noted there is often no acknowledgement of receipt of the information and/or the timelines for a returned response from the administrators. Companies would often not be contacted for months, further increasing the uncertainty experienced in the Finding / audit process.
- Having joint meetings with both administrators has been an issue. Anecdotal evidence provided to the Board indicates that when meetings like this do occur, they are beneficial and result in all parties reaching a mutual understanding about the R&D activities and expenditure. However, consultees also noted that it was often the case that bringing the administrators together was a difficult task.
- Reviews are not streamlined as between the co-administrators. Reviews may start at different times and when that occurs, evidence presented to the Board indicates that there is limited communication and a lack of information sharing between the co-administrators. This frequently leads to duplicative processes for the company.

The Board's Analysis

5.17 The feedback regarding the current processes was provided to the Board through many of the written submissions.

- 5.18 KPMG outlined some of the existing program engagement issues and proposal for improvements, including the following suggestion:⁶²

A R&DTI Customer Charter be developed in consultation with industry to provide taxpayers with confidence that administrators will administer the program in a fair, transparent and accountable manner.

- 5.19 Michael Johnson & Associates also noted the need for a Charter:⁶³

Consideration be given to an RDTI Charter that governs the interaction between stakeholders regarding matters of program design features and guidance. Clarification of timeframes and procedures surrounding risk assessments and audits should be included in the Charter.

- 5.20 EY also noted in their submission the need for a Charter:⁶⁴

It is our recommendation that DISER implement an R&D Tax Charter to assist Taxpayers in understanding their rights and obligations as well as explain what they can expect when being examined. The current DISER Charter is focused on customer service and does not sufficiently explain or outline their attitude or behaviour towards review and compliance activity.

- 5.21 Finally, the Tax Institute noted the need for a Charter type document:⁶⁵

The exact responsibilities and accountabilities of the two administrators should be explicitly stated in a protocol or an inter-departmental document that is made publicly available. This would provide clarity to officers within each agency as to the scope of their responsibilities and the ways in which they can work together more seamlessly. It would also allow taxpayers to refer to a central document to identify the roles played by the ATO and AusIndustry in administering the R&DTI.

- 5.22 Following the feedback received during the consultation, the Board agrees that a proposed solution to the issues raised by consultees is the development and implementation of a publicly available R&DTI Program Charter. The charter should outline what a company can specifically expect when engaging with the co-administrators and the R&DTI program.

- 5.23 The purpose of the R&DTI Program Charter will provide participants in the program with a clear outline of roles and responsibilities, and further encourage an increased collaborative approach between the co-administrators and the company; leveraging the work done to date on the implementation of the Integrity Framework.

62 Submission 11, p.18.

63 Submission 8, p.13.

64 Submission 13, p.14.

65 Submission 2, p.10.

- 5.24 The Board notes an existing Taxpayer Charter is in place to support Taxpayers in understanding their rights and responsibilities in the tax process. The recommended Charter would be specifically for the dual agency R&DTI program and, could reference the current Taxpayer Charter where appropriate.

RECOMMENDATION 9

ATO and DISER should develop and implement a publicly available Program Charter that clearly sets out the expectations and roles of all parties that participate in the R&DTI program. The Program Charter should include expectations on timeframes for engaging with all aspects of the program, how the co-administrators will work together and how they will engage with the companies which have registered for the program.

R&DTI Program Transparency

- 5.25 The R&DTI program, like many Government programs, generates a significant amount of data which provides insights into the trends within the program. Data is generated across a number of metrics such as the number of participants, timelines to complete activities and the amount of expenditure registered and claimed.
- 5.26 The program numbers are published regularly through annual reports and updates to consultation groups including the R&DTI Roundtable. The last public release of the number of program participants and expenditure data was in the IISA Annual Report released in October 2021. At around the same time, claims and offset value numbers were separately published by the ATO.
- 5.27 Other program metrics including for example, numbers on compliance activity are not regularly published by the co-administrators. This type of information has been presented on occasion to the R&DTI Roundtable and/or State Reference Groups.

The Board's Analysis

- 5.28 Feedback provided to the Board indicated there is a high level of interest in data and information related to the program and for this to be circulated in a more transparent manner. This was reflected in several written submissions.
- 5.29 KPMG noted performance could be strengthened by publication of program numbers:⁶⁶

Performance could be strengthened by the publication of AusIndustry metrics or key performance indicators (for example, average time taken to issue registrations, commence and conclude reviews, issue findings, etc.). Care would need to be taken so as

66 Submission 11, p.7.

not to truncate the process and timeframes at the expense of taxpayers or proper administration of the program.

5.30 The CTA noted that there should be more public transparency in the program:⁶⁷

Public transparency on the administration of the scheme including at least yearly updates on...[the] cost of ATO and AusIndustry in administrating [sic] the incentive, numbers of applications and decisions on advance findings and overseas findings that are favourable and unfavourable and number of reviews, adjustments, and outcome of review activity including the quantum of an[y] adjustments made, and what is driving adjustments.

5.31 The Board agrees that the program could enhance its transparency by publishing information, which could be done through a publicly available 'Market Update'. This would be an opportunity to publish aggregated data / high level numbers on registrations, claims, expenditure and compliance.

5.32 The Market Update could also be a mechanism for the co-administrators to raise with the market areas of concern in the program that they will be exploring further. It would be an opportunity to provide a fair warning to participants on areas of concern.

5.33 The Board notes the recent legislative change requiring the Commissioner of Taxation to publish information about the R&D activities of the company claiming the R&D tax offset, two years after the relevant income year.⁶⁸ The information published includes information such as a company's name and the amount of the notional deductions claimed.

5.34 While this measure will improve program transparency overall, the Market Update would publish aggregated numbers to help the market identify trends and assist the co-administrators with identifying areas of concern with compliance. The Market Update would complement the information published under the abovementioned transparency measure and provide the market with increased transparency over the R&DTI program.

RECOMMENDATION 10

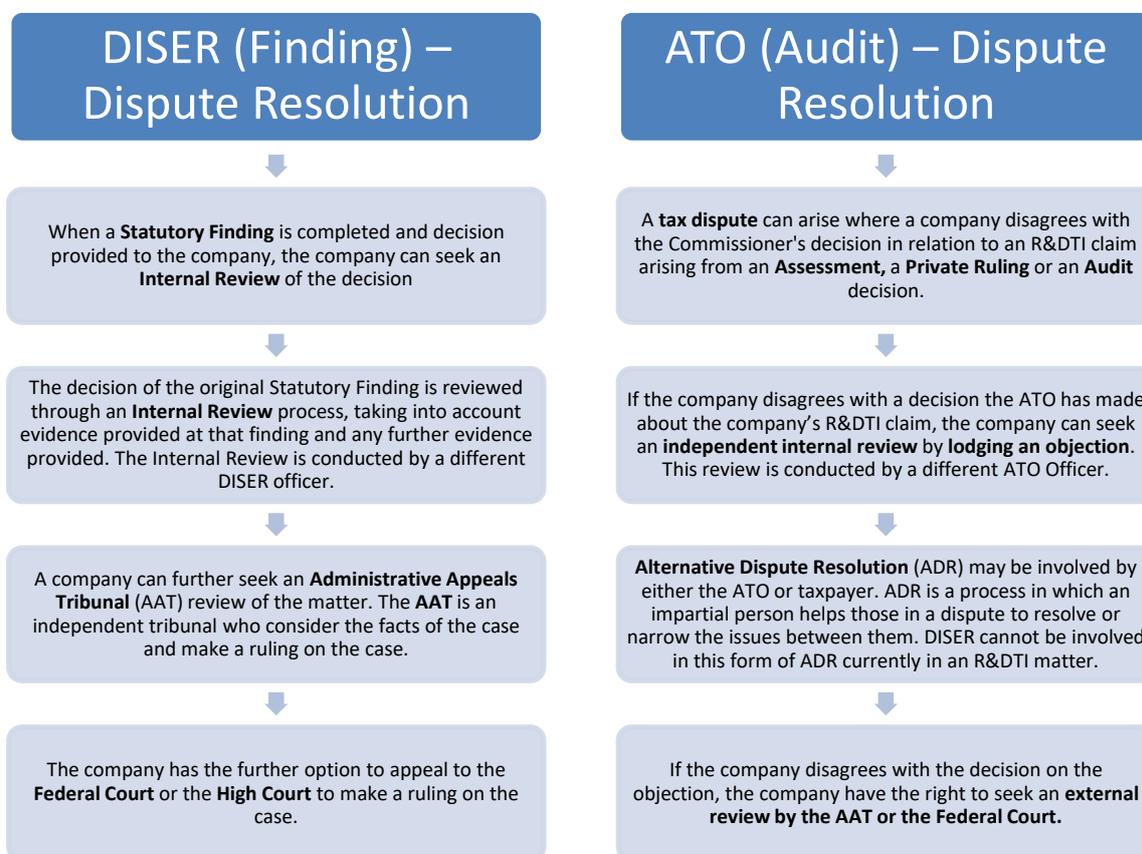
Market Updates of activities undertaken by both the administrators should be published which includes information on compliance/integrity activities.

67 Submission 12, p.6.

68 *Treasury Laws Amendment (A Tax Plan for the COVID-19 Economic Recovery) Act 2020* (Cth), Schedule 6, item 1, which inserts subsections 3H(1) and (2) of the TAA.

Alternative Dispute Resolution

5.35 The diagram below presents the current dispute resolution processes for both DISER and the ATO:



5.36 As noted in the diagram above, the first step in the process for addressing disputes on Findings made by DISER, is that a company can request an Internal Review of the original decision made on a finding. The Internal Review is conducted by an officer within DISER who has not participated in the original case. At that point, further evidence can be presented to support the company's registration application. If the Internal Review reaffirms the original decision that the R&D activities are ineligible, the company can appeal to the Administrative Appeals Tribunal (AAT).

5.37 Reviews of ATO decisions follow a similar process, with the option for a review of the original decision if the company is dissatisfied with the outcome. The company can further appeal to the AAT or the Federal Court of Australia (FCA) for a review of the decision. The ATO also has an alternative pathway for dealing with disputes through a form of Alternative Dispute Resolution (ADR). It is important to note that as a result of the

statutory secrecy provisions (refer Chapter 3), ADR procedures currently cannot involve DISER.

The Board's Analysis

- 5.38 Consultees have indicated that there should be an ADR process for disputes in place where all parties are involved (that is, the company, DISER and the ATO), prior to matters progressing to the AAT. Matters progressing to the AAT can be costly and time consuming for companies and the co-administrators. This is especially relevant for small / start-up companies, typically short of funds to pursue an AAT or court process.
- 5.39 An ADR process such as a mediation between all parties involved in the first instance, may prevent matters progressing to the AAT or a court. This brings the possibility of a negotiated settlement to occur.
- 5.40 This process would also have the added advantage of DISER being involved alongside the ATO in settlement discussions and meetings. Consultees have suggested to the Board that this practice would be an improvement to the current administration of the regime as having DISER involved in the discussions would assist in agreeing which R&D activities are eligible and working with the ATO on the associated expenditure that is claimable.
- 5.41 The Board received the following written submissions advocating for DISER to be actively involved in settlement discussions.
- 5.42 Deloitte noted the need for further mediation:⁶⁹

Provide IISA the capacity and legislative mechanisms to mediate and 'settle' disputes with taxpayers where the need arises.

- 5.43 The Tax Institute noted:⁷⁰

Members have noted difficulties when negotiating settlements with IISA in cases where there are extant issues involving the ATO. This issue is exacerbated by the fact that these proceedings generally cannot be resolved through discussions and negotiations with reference to the value of the tax concessions in question (as is common in tax disputes) since matters of expenditure are outside the scope of IISA's remit.

- 5.44 The Board received the following submissions advocating for ADR. Grant Thornton suggested:⁷¹

Consideration of alternative dispute resolution mechanism (for example, mediation and ADR processes with specialist R&D tax incentive mediators) to R&D tax incentive claim

69 Submission 7, p.9.

70 Submission 2, p.6.

71 Submission 6, p.3.

reviews by AusIndustry if agreed outcomes cannot be reached with the administrators at first instance and before applying to the AAT or a Court for review.

5.45 PwC noted:⁷²

Consideration should be given to setting up a specific cost-effective Tribunal (for example, like the Small Claims Tribunal or the Land and Environment Court) with appropriate technical expertise to deal with disputes between the regulators and claimants in a more cost effective and efficient way. This should reduce the cost of litigation and increase access to review options to small businesses.

5.46 Based on the feedback provided to the Board and the difficulties with the current dispute resolution process, the Board has identified a need for improvements to the ADR mechanisms. This improvement should occur where all parties of ATO, DISER and the company can be involved concurrently in the discussions.

5.47 The Board does not see the need for a specific new ADR process (such as a separate tribunal). Improvements could occur within the existing ADR frameworks that the ATO has but with all parties involved (ATO, DISER and the company).

5.48 The Board notes the Recommendation 3 (Information Sharing) would need to be implemented first to fully realise the benefits of Recommendation 11 (Alternative Dispute Resolution).

RECOMMENDATION 11

Alternative Dispute Resolution processes should be implemented for use before escalation to the AAT. These should involve dispute resolutions amongst all parties: the company, DISER and the ATO. Where appropriate, both DISER and the ATO should be present where discussions on settlements are occurring.

R&DTI Roundtable

5.49 A final governance issue raised with the Board relates to the R&DTI Roundtable. Feedback provided to the Board outlined that the R&DTI Roundtable is a useful mechanism by which both administrators bring key program stakeholders together to provide program updates and discuss both program and marketplace issues. The R&DTI Roundtable is made up of representatives from Government, tax agent firms, tax agent associations, Industry Associations and companies.

5.50 Feedback provided to the Board indicated that there are some issues with how the R&DTI Roundtable is currently operating.

72 Submission 14, p.2.

- 5.51 The Board acknowledges the R&DTI Roundtable as a forum where information can be shared between the co-administrators and key stakeholders in the R&DTI program. The Board encourages the co-administrators to continue to enhance the administration of the R&DTI Roundtable so it is an effective information sharing forum.

CHAPTER 6: ANALYSIS OF INTERNATIONAL R&D ADMINISTRATION MODELS

KEY POINTS

- The Board engaged directly with international R&D administrators in NZ, UK, CAN and the US to directly gain insights on program administration in those countries.
- The Board also engaged with professional service practitioners in the US and the UK to learn more about the practical implications of the programme in those countries.
- Furthermore, the Board reviewed and researched the administration processes in Norway and Germany.

- 6.1 The purpose of this chapter is to analyse R&D administration models in other comparative jurisdictions. It also provides insights into how international experiences have informed and assisted the Board in making its observations and recommendations to improve Australia's R&DTI dual agency delivery model.
- 6.2 During the course of the review, the Board held consultations with the international regulators/administrators of similar R&DTI programs/schemes such as NZ, UK, CAN and the US. The Board also conducted consultations with the UK and US offices of an international accounting firm to obtain the advisor's perspective on the operation of the program in their respective countries and a large company in NZ which participates in that R&D Incentive program.
- 6.3 These international consultations were invaluable and provided the Board with a better insight as to how other jurisdictions deal with similar administration issues such as review and audit timeframes, program guidance, a regulator's technical ability and how to achieve certainty in the program.

Background

- 6.4 Most countries provide R&D support measures through either direct subsidies (such as subsidies or grants) or tax incentives (such as allowances, exemptions, deductions, accelerated depreciation of capital or credits and offsets). 'R&D tax credits are the most

popular type of incentive, followed by enhanced allowances and accelerated depreciation'.⁷³

- 6.5 Whilst generally provided through the corporate taxation system, some countries have also provided (additional) incentives that apply to social contributions and/or wage taxes. Given that there is a significant variation in the extent of R&D support measures, it is difficult to compare across countries. Notwithstanding this, the Organisation for Economic Cooperation and Development (OECD) and the EC have undertaken such comparisons on a regular basis.⁷⁴
- 6.6 The Board understands that Australian companies may consider a number of factors when deciding when and where to undertake their R&D activities such as their business plan, regulatory environment, corporate tax rates, workforce capabilities, technological change, features and administration of the R&DTI program, and also the features and administration of international R&D support measures.

73 C. Jensen, 'A Study on R&D Tax Incentives.' A Study on R&D Tax Incentives: Final report. European Commission, 2014, 5.

74 D. Ognyanova, 'R&D tax incentives. How to make them most effective.' European Commission. Policy Development and Coordination (2017).

Comparative Analysis

6.7 Set out below is the Board's comparative analysis of the administration of the R&DTI programs in specific countries where there are like international R&D systems.

New Zealand

Table 2: Comparative Analysis of International R&DTI Program Administration – New Zealand

Overview	Self-assessment program for 2019/20 FY (1st year of program). The Ministry of Business, Innovation, and Employment (MBIE) has policy responsibility for the Research, Science and Innovation portfolio and is the lead policy agency on the RDTI program.
Regulator (Single or Dual) & Capability	There are dual regulators: Callaghan Innovation (Callaghan) – a New Zealand Government agency - has operational responsibility for assessing R&D eligibility; and Inland Revenue (IR) - New Zealand's revenue authority has operational responsibility to assessing entity and expenditure eligibility. The regulators engage experts (for example, software issues) as required.
Registration	From 2020/21 (onwards), companies must get pre-approval for their R&D activities by applying for General Approval. For significant performers where R&D expenditure is more than \$2 million, companies can apply for Criteria and Methodology (CAM) agreement/approval, which is pre-approval for their programs and processes as a whole rather than on an activity-by-activity basis.
Eligibility (Expenditure)	A company can manage both their registration and claim information through one system.
Compliance (Review & Audit)	If a company's tax return is selected for audit or review, it is essential that the company has retained sufficient documentation to support the expenditure claimed as eligible for the tax credit.
Certainty (Assurance)	Companies must submit their R&D core and supporting activities as per the registration process; and then each companies' activities are assessed against the statutory criteria before filing a tax return. Companies have certainty then that their activities are eligible when they file their tax returns. This avoids the activation of a review of those activities at the request of IR. This provides each company that applies for the program with legislated certainty that their activities are eligible.
Guidance & Education	Following an independent review during 2020 into the early implementation of the R&DTI scheme, the RDTI guidance was reviewed and updated to ensure it is fit for purpose, focusing specifically on eligible R&D activities.
Data/Information Sharing	There is a single-entry point into the program, so the program user is only dealing with one interface. Information between IR and Callaghan is transferred through a back-end system, so even though the user effectively deals with two separate departments, the experience involves dealing with one processing/data system.

Observation points

6.8 From discussions with MBIE, Callaghan and IR about the NZ R&DTI program, the Board notes that in relation to the NZ experience:

- There have been recent improvements in bringing the two agencies (Callaghan and IR) together with more joint processes
- It had taken some time for the two agencies to work through their different personas, with the aim of having one customer facing persona for the R&DTI program
- It was important to improve the operational environment to work as one entity

- Some timeframes can be controlled, and some cannot; but further improvements could be made in relation to processes and timeframes
- The focus for both administrators (Callaghan and IR) was improving the approval process and resolving uncertainty
- Callaghan from time to time will engage external experts
- Both agencies are working with the software sector on guidance materials; and there is a challenge in dealing with digital vs software sectors.

United Kingdom

Table 3: Comparative Analysis of International R&DTI Program Administration – United Kingdom

Overview	The United Kingdom provides R&D tax relief through a volume-based R&D tax allowance with a potential payable credit for loss-makers for Small and Medium Enterprises (SME); and in the case of large companies, a taxable Research and Development Expenditure Credit (RDEC). Claiming the R&D tax relief is a self-assessment process, and the R&D claim is made on the Company Tax Return .
Regulator (Single or Dual) & Capability	There is a single Regulator: HMRC decides (does not extend to modifying, only interpreting) what is R&D in the meaning of the tax law, and what the eligible costs are. The definition of R&D is set out by BEIS (Dept for Business, Energy and Industrial Strategy) and definition of eligible costs is in primary legislation. As part of the conduct of an audit/investigation, assessors can consult the specialist teams, and refer the most complex cases to tax and legal specialists.
Registration	No prior approvals from regulatory agencies are required. For SMEs (see https://www.gov.uk/guidance/corporation-tax-research-and-development-tax-relief-for-small-and-medium-sized-enterprises). If a company claims tax relief on one to three projects, details of all three projects are required. If a company claims four or more projects, details of three to a maximum of ten projects, which cover 50 per cent or more of the total qualifying R&D costs are included.
Eligibility (Expenditure)	A company can claim the relief in its Company Tax Return. Under the UK's electronic filing system, all SME claims for R&D relief are automatically referred to an Incentive and Reliefs (I&R) Unit. However, the details of this are slightly different in the two schemes.
Compliance (Review & Audit)	HMRC risk assesses all claims. Where risks are identified, claims are referred to investigation teams to review and where appropriate, investigate. HMRC Investigation teams are tax trained assessors, with experience and training in the R&D tax relief schemes.
Certainty (Assurance)	Smaller SME companies making their first R&D claim can qualify for Advance Assurance. If Advance Assurance is granted, any R&D claims in the first three accounting periods will be accepted if they're in line with what was agreed. A similar pilot is underway for large businesses. Customer Relationship Managers (CRMs) manage HMRC's relationships with the 2000 largest and most complex businesses. The CRM framework helps to improve the handling of complex issues, and allows for risk assessment, including determination of R&D tax relief claim risks, to take place against a published framework.
Guidance & Education	HMRC publishes a list of common risk areas and errors made, both for the guidance of HMRC staff, and claimants and their agents. The list of risks and errors includes features such as the incorrect claiming of project activities outside the scope of R&D, expenditure outside the qualifying categories, staffing costs in respect of people who are not employees of the company or externally provided workers, etc.
Data/Information Sharing	At this stage, we do not have any information about the provision of data about the operation of the UK Program.

Observation points

6.9 From discussions with HMRC and UK Treasury about the UK R&DTI program, the Board notes that in relation to the UK experience:

- HMRC has specialists who undertake reviews on complex software claims, and these trained officers look at the claims and speak directly with the companies. HMRC used to have specific industry sector officers, but it has more of a general model now; and the expectation is on the company to explain the R&D in terms that HMRC can understand/progress
- There is some sector specific guidance on software and pharmaceuticals. Otherwise, the HMRC approach is to attempt to explain the R&D definition in guidance rather than providing very specific items/examples
- HMRC have an aspiration to respond to 95 per cent of claims with 28 days. There are challenges with this as risk work is either done very quickly or after the event, to meet the timeframe. Over the past several years, HMRC have sought to be more engaging and have re-organised the way they are structured
- There is very little information provided initially by the company on their R&D portion of the claim. HMRC have advised that there will be a detailed announcement on 30 November 2021 setting out some changes.
- The R&D claimant companies have requested the HMRC to shorten the processing times for claims and expedite payments of the R&D tax relief allowances and credits.

United States

Table 4: Comparative Analysis of International R&DTI Program Administration – United States

Overview	Under the Research & Experimentation (R&E) Credit program, the R&E credit is incremental; that is, the credit amount equals the applicable credit rate times the amount of qualified research expenses (QRE) above a base amount.
Regulator (Single or Dual) & Capability	There is a single regulator: the Internal Revenue Service (IRS) which decides what is R&D in the meaning of the tax law, and what the eligible costs are.
Registration	There is no separate registration process, the benefit is claimed in the company tax return.
Eligibility (Expenditure)	Accessing the program is done through a specific form in the tax return process (Form 6765 – Credit for Increasing Research Activities). The form does not request any details in relation to the R&D activities that were undertaken, questions are related purely to expenditure.
Compliance (Review & Audit)	It is possible that the IRS will examine an R&E Credit position. Original tax returns that include R&E Credit positions are no more likely to be examined than those that do not include R&D Credit positions. Amended tax returns claiming R&E Credits that are used in the years under examination have been more likely to be examined. If examined, R&E Credits may be allowed or disallowed, in whole or in part. Companies which claim the R&E Credit are required to retain sufficient records that substantiate the expenditures claimed. There is no requirement to provide that information at the time of claiming the credit.
Certainty (Assurance)	The Compliance Assurance Process (CAP) was developed by the Large Business and International (LB&I) Division to improve the federal tax compliance of large corporate taxpayers by employing real-time issue resolution tools and techniques. It is important to note that taxpayers must apply to be in the CAP program, and not every taxpayer is eligible for or accepted into the program. In CAP, the IRS and taxpayer work together to achieve tax compliance by resolving issues prior to the filing of the tax return. The Pre-Filing Agreement Program (PFA) encourages taxpayers to request consideration of an issue before the tax return is filed and thus, resolve potential disputes and controversy earlier in the examination process.
Guidance & Education	The IRS publishes 'Audit Technique Guides', which covers the high-level approach that the IRS should adopt when auditing claims and more detailed guides for specific sectors. These are the manuals that the IRS uses to assess claims and they are published so companies have some signposts on how a claim will be audited. The specific sectors for which audit guidelines are published are software, pharmaceutical and aerospace.
Data/Information Sharing	The IRS does not publish data about the operation of the R&E Credit program. However, it does have a complex planning & analysis division which undertakes reviews of various tax programs (for example, Large Business & International Division).

Observation points

6.10 From discussions with the US Treasury and the IRS about the R&E Credit program, the Board notes the following:

- The US does not have a separate system for processing claims for software development under R&E Credit program
- The IRS has issued Audit Guidelines on the Application of the Process of Experimentation for all Software which provides guidelines on applying the process of experimentation test to software development activities
- The IRS consult with the MITRE corporation, which is an independent company, in relation to software issues

- During the CAP, the IRS actively liaise with the taxpayer and provide education material (Audit Technique Guides and Manuals) in the event that the taxpayer may fail part or all of an audit. This material is provided with the intent of assisting the taxpayer with filing a compliant tax return which does not need to be audited. Sometimes issues cannot be resolved prior to the return filing due date, however, so it is possible we are required to complete a post-filing review to ensure compliance.

Canada

Table 5: Comparative Analysis of International R&DTI Program Administration – Canada

Overview	The Scientific Research and Experimental Development (SR&ED) Program is a federal tax incentive program designed to encourage Canadian businesses of all sizes and in all sectors to conduct R&D in Canada. It consists of two types of incentives: first, it allows businesses to deduct qualifying expenditure from income for tax purposes; and secondly, businesses can receive an SR&ED Investment Tax Credit (ITC) on qualified expenditures in the form of a reduction of tax payable, a cash refund, or both.
Regulator (Single or Dual) & Capability	The Canadian Revenue Agency (CRA) assesses the claim against legislation set out by the Department of Finance in the Income Tax Act and will deliver the investment tax credits if the claim meets the legislative requirements. In other words, the CRA administers the program, the Department of Finance makes the laws.
Registration	No prior approval from a regulatory agency is required: the claim is made on the tax return. Claimants file an income tax return together with a prescribed form in which technical project details and associated expenditures are completed.
Eligibility (Expenditure)	Claimants must maintain supporting evidence to substantiate that SR&ED work was performed and allowable SR&ED expenditures were incurred. The CRA may subsequently review claims made. Companies are required to file the specific SR&ED claims along with income tax forms electronically. Claims which have been accepted as filed without a review will be processed within 60 days of the date that CRA receives a complete claim.
Compliance (Review & Audit)	The maximum time limit within which the claims should be processed is set out in 'Service standards'; claims receiving refundable tax credits that are selected for a review will be completed within 180 days of the date that CRA receives the complete claim. An automated risk-assessment tool is used for the initial screening of claims, to detect those that are at highest risk of non-compliance. For those claims that are selected for review, the compliance activities of the CRA includes using scientists and technical experts to assess a company's technical eligibility for the incentives, as well as tax auditors to ensure compliance with the tax legislation in regards to expenditures. Technical reviews are conducted by research and technology advisors (RTAs). They report to research and technology managers (RTMs), who may become involved in a technical review. In some cases, an RTA may get help from a national technology sector specialist in the SR&ED Directorate.
Certainty (Assurance)	Different forms of application assistance are available: First-time claimant advisory service (FTCAS), SR&ED Self-assessment and Learning Tool (SALT), Pre-Claim Consultation (PCC), and Pre-Claim Review (PCR). Also, if claimants do not agree with the results of a review, assistance is also available to resolve their concerns. The FTCAS is a free in-person service that provides first-time claimants with an opportunity to meet with CRA staff at their own place of business, and to gain a better understanding of the SR&ED Program. The FTCAS is provided after the claim is lodged, but it is not a review or an audit. The focus of the FTCAS is to educate claimants in terms of eligibility and documentation requirements, and to increase predictability in subsequent claims. The Pre-Claim Consultation is a free on-demand service that enables potential claimants to find out with certainty whether their R&D work qualifies for the incentive, prior to submitting a claim. CRA also has a Pre-Claim Review service where businesses allow the CRA to conduct a review in real-time, while the work is taking place, which helps to provide some certainty that a claim will be accepted as lodged with the CRA.

Guidance & Education	The CRA has developed a client-centred service involving a number of tools for potential claimants, and comprehensive support for first-time applicants. Furthermore, it is possible to subscribe to the SR&ED mailing list that informs about the different policy changes and upcoming information seminars/webinars. CRA has an interactive learning tool that companies can use to self-assess their work before they lodge their applications.
Data/Information Sharing	Every year, the CRA assesses 60,000 R&D projects, processes close to 20,000 claims and provides approximately \$3 billion in tax incentives to over 20,000 claimants, of which 75 per cent are small businesses (<500k in revenues).

Observation points

6.11 From discussions with the CRA about the CAN R&DTI program, the Board notes that in relation to the CAN experience:

- The CRA's approach towards integrity and compliance within the Scientific Research and Experimental Development (SR&ED) Program involves intervention based on needs and risk; strengthen collaboration with tax preparers through professional associations such as the Chartered Professional Accountants (CPA) and the Association de planification fiscal et financière (APFF); focus on timeliness, transparency and technical competency
- CRA provides both SR&ED guidance on the interpretation of the law as well as sector-specific guidance. In August 2021, the CRA released updated Guidelines on the Eligibility of Work for SR&ED Tax Incentives
- CRA's approach to the treatment of software SR&ED claims is that there are no provisions in the Income Tax Act that are specific to software; and the CRA recognises that software is pervasive across all industries
- The CRA has been shifting the focus towards more education and outreach.

Norway

Table 6: Comparative Analysis of International R&DTI Program Administration – Norway

Overview	Norway has the 'SkatteFUNN' R&D tax credit, which is a two-tier system with a higher 20 per cent credit for SMEs and an 18 per cent credit for large enterprises. The credit is fully refundable. There is a maximum ceiling to the R&D expenditure that can be claimed (again two-tier, depending on size of the company).
Regulator (Single or Dual) & Capability	There are Multiple Regulators. The SkatteFUNN R&D tax deduction system lies administratively under the Ministry of Trade.
Registration	Innovasjon Norge (Innovation Norway) makes a first assessment of whether the project qualifies for support or not. Forskningsrådet (The Research Council of Norway) approves or disapproves the application. Skatteetaten (Skattedirektoratet, Directorate of taxes) is decides the amount of the tax deduction. The content of the project must be approved in advance by the Research Council of Norway. The electronic application system is a one-stop system.
Eligibility (Expenditure)	There is also a requirement that the costs included in the calculations for the R&D tax credit application have to be verified by an auditor. The Tax Authorities control the reported costs and calculates the size of the tax deduction. If the tax deduction is higher than the taxes which must be paid, the difference will be paid out to the company as a subsidy. A subsidy is also provided to companies that do not have any taxable income.
Compliance (Review & Audit)	The tax authority is bound by the decision of the Research Council concerning what is regarded as an R&D project and R&D activities; and is responsible for deciding the costs that are eligible and that they are sufficiently documented. The payment of a negative tax or a grant is made when the tax authorities have completed their tax assessment; and takes place the year after the actual R&D expenses have occurred. Companies are required to present a project plan and budget, sub-divided into sub-projects and milestones. These must be approved ex-ante. Companies must report on the progress of their project to the Research Council. The Directorate of Taxes will often compare the tax credit claim with the project plans/budget.
Certainty (Assurance)	The tax credit scheme favours small and medium-sized enterprises, as they are offered a higher rate of tax credit. Furthermore, a maximum ceiling of eligible expenditure applies, which may especially impact large firms with typically larger R&D budgets.
Guidance & Education	The Research Council of Norway spends considerable time and effort to increase awareness of the tax incentive scheme. It hosts seminars and conducts one-on-one meetings. It also educates auditors and accountants on the scheme.
Data/Information Sharing	A database has been created which contains time-series data on companies. It includes data from The Research Council of Norway (SkatteFUNN), the Directorate of taxes, and Statistics Norway (R&D statistics, structural statistics and the accounts statistics). There are more than 18 000 firms in the database, and it comprises firms that have applied for SkatteFUNN-money or are included in the R&D statistics of Statistics Norway.

Germany

Table 7: Comparative Analysis of International R&DTI Program Administration – Germany

Overview	The R&D Tax Allowance Act became effective from 1 January 2020 which provides that companies in Germany are entitled to a 25 per cent R&D tax allowance on their internal or subcontracted R&D activities, provided certain criteria are met. The incentive is available to all companies, regardless of their size or income level. Generally, eligible costs are limited to EUR 2 million per year, resulting in a maximum subsidy amount of EUR 500,000 per group of companies. Due to the COVID-19 pandemic, the eligible cost basis has been increased to EUR 4 million per year, raising the maximum annual incentive that can be received to EUR 1 million per group of companies. The increased limit applies to eligible costs incurred from 1 July 2020 up to 30 June 2026. Any person with unlimited or limited tax liability within the scope of the Income Tax Act and the Corporation Tax Act is eligible to benefit from the incentive scheme.
Regulator (Single or Dual) & Capability	There is a single regulator: the German Tax Office which decides what is R&D in the meaning of the tax law, and what the eligible costs are.
Registration	Applications for the R&D tax incentive follow a two-stage process. First, potential projects must qualify as R&D according to the definition given by a 'certifying body'. Second, after the end of the fiscal year in which qualifying expenses are incurred, claims for confirmed R&D activities (projects) may be submitted electronically to the relevant tax office. Funding is open for three types of R&D projects: (1) a company's own R&D projects, (2) cooperative projects, for example, with universities, and (3) contract research.
Eligibility (Expenditure)	The eligibility will be assessed at a central office which is under the aegis of the Federal Ministry of Education and Research. The processing time for the assessment of eligibility is predicted to be approximately three months. In order to apply for an assessment of eligibility, it is not necessary that the R&D projects have already been started. A positive assessment is binding for the local fiscal authorities. Companies will need to apply for a certificate from a certifying body (outside the finance administration) confirming that the conducted activities qualify as R&D based on the EU definition.
Compliance (Review & Audit)	The R&D tax credit will be assessed in an annual tax assessment from the local fiscal authorities. This assessment will be based on the prior assessment of eligibility of the projects as well as on their annual costs. The assessed annual tax credit amount will then be set within the next corporate / personal income tax assessment against any tax payable or added to any tax refund.
Certainty (Assurance)	Unable to verify whether there is any assurance program, noting it commenced in January 2020.
Guidance & Education	Unable to verify whether there is any guidance or education program, noting it commenced in January 2020.
Data/Information Sharing	Unable to verify whether there is any data published about the operation of the program, noting it commenced in January 2020.

APPENDIX A: CONSULTATION PROCESS AND PARTICIPANTS

In June 2021, the Board released a Consultation Guide describing the scope of the review and a series of consultation questions to identify key issues and difficulties encountered with the dual administration model of the R&DTI. The Board received 17 written submissions from the following organisations during the consultation period:

- 01 – Australian Industry Group (Ai Group)
- 02 – The Tax Institute
- 03 – Australian Investment Council
- 04 – Australian Small Business and Family Enterprise Ombudsman (ASBFEO)
- 05 – BDO
- 06 – Grant Thornton
- 07 – Deloitte
- 08 – Michael Johnson & Associates
- 09 – Chartered Accountants Australia and New Zealand (CAANZ)
- 10 – Cochlear
- 11 – KPMG
- 12 – Corporate Tax Association (CTA)
- 13 – EY
- 14 – PwC
- 15 – Tech Council of Australia
- 16 – DISER and the ATO (joint submission)
- 17 – RSM Australia

From July to September 2021, the Board held a series of virtual consultations with over 40 participants. Organisations represented at the roundtables included:

- ABA Legal Group
- AB&H
- Australian National University (ANU)
- Australian Small Business and Family Enterprise Ombudsman (ASBFEO)
- BDO
- Chartered Accountants Australia and New Zealand
- Cochlear
- Council of Small Business Organisations Australia (COSBOA)
- Corporate Tax Association
- Deakin University
- Deloitte
- EY
- Findex/Crowe Australasia
- Grant Thornton
- Holding Redlich
- Insight Compliance
- Institute of Public Accountants
- KPMG
- Law Institute of Victoria
- Medicines Australia
- Michael Johnson & Associates
- PwC
- RSM Australia
- Small Business Association
- Swanson Reed

- Tech Council of Australia
- The Tax Institute
- University of Melbourne

From July to October 2021, the Board also engaged with Government's agencies and tax agents from several international jurisdictions including UK, NZ, US and CAN.

From July to September 2021, the Board had confidential consultation sessions with ten individual companies who provided their views on the R&DTI program.

APPENDIX B: COMPLIANCE COST IN THE R&DTI PROGRAM

Methodology

The Board conducted a small scale and targeted survey that was undertaken by a small and select number of companies which had volunteered to provide feedback on the compliance costs and issues involved in dealing with the R&DTI program. Details below are taken from the responses to the survey questionnaires completed by companies which have been involved with R&DTI program and claimed the tax offset.

Survey Features

Set out below is a description of the features about the conduct of the compliance costs survey.

What were the characteristics of the companies which participated in the survey?

Most of the selected companies completed a structured questionnaire containing 15 questions. The Board used the results of the survey to gain an understanding of the impact and level of compliance costs incurred by claimant companies accessing the R&DTI program. The person who completed the survey was a representative or employee of the company.

In 60 per cent of the cases this person was a member of the tax team of a company, and the other 40 per cent it was the Public Officer or Director of the company. 80 per cent of the companies indicated they were large entities (>\$20million) for R&D purposes and the balance of the companies indicated as a small entity (<\$20 million) for R&D purposes. All companies had recent involvement with the R&D requirements.

What industries were they involved in?

The selected companies which completed the questionnaire operated in the following industries:

- Mining,
- Wholesale Trade,
- Professional, scientific, and technical services,
- Manufacturing, and
- Multiple industries.

How much time did the businesses spend on complying with the requirements of the R&D regime?

The companies were asked to estimate how much direct and indirect time they spent complying with the R&DTI program requirements (these details are shown in Table 7 below).

However, combining the direct and indirect times, the overall combined times spent complying with the requirements are:

- Company 1 (large company) – 180 hours
- Company 2 (large company) – 150 hours
- Company 3 (small company) – 74 hours
- Company 4 (large company) – 5,100 hours
- Company 5 (large company) – can't be separately identified.

These times vary considerably. Estimating compliance costs is a difficult activity as it is often overlaps with other business activities.

What are the main compliance activities that a business must do to meet the R&D requirements?

All companies were asked to distribute the time taken across ten (10) compliance activities. The compliance activities that emerged with the overall highest times are:

- Compiling work papers, record keeping and data validation on R&D activities.
- Preparing and responding to compliance requests (audits and reviews) from DISER and the ATO.
- Working with tax agents and R&D consultants.
- Undertaking record keeping for the purpose of quantifying or substantiating an expenditure claim.

Do the businesses use advisors to assist with meeting the requirements and how much does this cost?

All companies used an advisor to assist with complying with the requirements. These advisors were accountants, tax agents or R&D consultants. Not all the companies provided an estimate of the fees paid – only three did. However, all companies engaged an advisor separately and independently of the usual business advisors they used and so fees paid were in addition to any annual fee for professional advisor services.

Of the three companies which provided an estimate, the fees paid were about \$25,000 to \$35,000; \$75,000 and over \$100,000.

What administrative or compliance issues cause problems with complying with the R&D requirements?

The companies were presented with eight (8) administrative or compliance issues and asked to what extent they agreed or disagreed with the statements. Most statements attracted levels of agreement that indicated unsatisfactory or negative views.

The issues that attracted the most dissatisfaction were:

- Dual agency administration
- Dual agency guidance and information products
- Overlaps blurring the roles between the agencies when they seek information or making decisions.
- The length of time between making the claim and the audit and review of that claim.
- Evidence needed must be specifically generated.

CTA Submission

The CTA reported⁷⁵ that the average cost of compliance is \$214,000 on an average incentive claim of around \$2.3 million (the permanent difference of 8.5 per cent of the eligible R&D expenditure); and that the cost of compliance is on average about 9 per cent of the cost of claiming the incentive for large corporates before taking into account any cost associated with subsequent ATO or DISER review activity.⁷⁶ See the below Table 8 about these averages.

Table 8: Compliance Costs Averages

	All data (\$000)	Excluding outlier (\$000)
Average external fees	119	111
Average internal cost	95	101
Total cost	214	211
Average internal hours	834	883
Average R&D permanent benefit (@8.5%)	2320	1920
Total cost to claim ratio	9%	11%

75 Submission 12, p.9 & 10.

76 Assuming a 8.5 per cent tax benefit, for those respondents that provided data the average incentive claim was \$2.3 million (median \$1.8m). Information on the cost of compliance was also provided by the above companies which indicated the average cost of external fees was \$119,000 and the average internal organisational hours spent on R&D compliance was 834. We have used \$114 per hour as an average hourly rate.⁷⁶ All respondents utilised external advisors in the preparation of R&D incentive claims, and on average these costs accounted for around 50 per cent of total compliance costs.

The CTA indicated⁷⁷ that removing a large outlier from the data reduces the average claim to around \$1.9 million (median \$1.6m), average external fees to \$111,000, but internal hours increase to 883. The average total cost remains similar at around 11 per cent of the incentive, before taking into account subsequent ATO and DISER review activity.

In their survey, the CTA asked respondents to rank (from one to four) the drivers of compliance costs, with 63 per cent indicating ‘technical team documentation requirements’ was the main driver of cost followed by external fees (23 per cent) and the time involved in calculating the eligible expenditure ranked third (9 per cent). 6 per cent ranked the largest driver of cost being the cost of subsequent ATO and DISER reviews.

DISER/ATO Joint Submission

DISER/ATO in their joint submission⁷⁸ referenced the CIE report, which was commissioned by DISER to review the program. The 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 11 below.

Table 9: 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

77 Submission 12, p.9 & 10.

78 Submission 16, p.18 & 19.

Definition of Compliance Costs

For the purposes of the survey, the Board developed a definition of 'compliance costs' closely modelled on the Australian Government's regulatory burden measurement framework.⁷⁹ This framework is the principal tool used by the Australian Government and its agencies in quantifying regulatory burden costs and savings.

Consistent with the regulatory burden measurement framework, the Board's definition of compliance costs is built around a core definition and a number of specific exclusions.

The Board's core definition of compliance costs consists of:

- a. *Administrative costs* – costs incurred by R&DTI claimant entities registering for the R&DTI and lodging a tax claim for expenditure incurred on R&D activities; for example, the costs of keeping plans and keeping records.
- b. *Substantive compliance costs* - costs incurred by R&DTI claimant entities in registering for the R&DTI and lodging a tax claim for expenditure incurred on R&D activities; for example, the cost of tax advice on eligibility and claiming expenditure on R&D activities.

In the context of the Board's review, compliance costs include but are not limited to costs incurred to carry out the activities in the following table.

Table 10: Definition of Compliance Costs

Logistical activities	Activities related to decision-making
Record keeping	Learning about the registration and tax lodgement process for R&DTI
Compiling project papers	Training staff, working with external advisors
Data validation	Performing relevant calculations
Lodging registration forms and R&DTI Schedule in tax return	Compiling work papers

79 Department of the Prime Minister and Cabinet, Office of Best Practice Regulation, 2016, *Guidance Note: Regulatory Burden Measurement Framework*, www.pmc.gov.au