Getting your potential cash refund

R&D IN AUSTRALIA

What is R&D relief?

Tax offset

Only companies

Minimum $20,000 spend

Research and development (R&D) relief is provided in Australia through a tax based incentive program whereby the Australian Government provides companies with a tax offset (as opposed to a tax deduction) if they conduct eligible R&D activities (and spend at least $20,000 on such R&D activities). This offset is available annually on an ongoing basis to companies of all sizes and within all industry sectors. However, the size and nature of the offset differs depending on the turnover of the company as well as, from 1 July 2014, on the amount of R&D expenditure incurred.

Clients conducting R&D activities through non-corporate structures may therefore want to consider incorporating their business structures if they are conducting R&D activities, since the incentive is NOT available to businesses conducting R&D activities through trusts, partnerships or as individuals.

The incentive is generally only available for R&D activities conducted in Australia, but in certain circumstances it can also be available for R&D activities conducted outside Australia (broadly if the overseas activities have a significant scientific link to core R&D activities conducted in Australia and are not able to be conducted in Australia).

How does the R&D offset work?

Do you spend more than $100 million on R&D?

45% refundable offset if turnover < $20 million

40% non-refundable offset if turnover ≥ $20 million

A company can claim a tax offset for notional deductions such as expenditure incurred on eligible R&D activities and for the decline in value (and balancing adjustments) of depreciating assets used in R&D activities (provided the $20,000 spend requirement is met).

The size and the nature of the offset depend upon the turnover as well as the amount of R&D expenditure incurred by the company:

- A company with a group turnover of less than $20 million can qualify for a 45% refundable offset (i.e. such smaller companies can get a cash refund equal to 45% of the amount spent on eligible R&D activities, regardless of whether they are in a loss position or not); and
- A company with a group turnover of $20 million or more can qualify for a 40% non-refundable offset (i.e. such bigger companies who are in a loss position will only be able to carry forward their 40% offset to be used in later years when they are profitable again).

However, from 1 July 2014, these rates of 45% or 40% will only apply to R&D expenditure up to $100 million – R&D expenditure in excess of $100 million will be subject to a tax offset at the company rate (currently 30%) .

The 45% refundable offset available to smaller companies can therefore provide a cash injection to help start-ups that are often cash-strapped - for example, a startup company that is in a loss position for tax purposes who spends $1 million on R&D will receive a $450,000 cash refund under this incentive.

What are eligible R&D activities?

Core & supporting R&D activities

Broadly, eligible R&D activities will create new or improved materials, products, devices, processes or services and can consist of either:

- **Core R&D activities** (systematic experimental activities conducted to create new knowledge); or
- **Supporting R&D activities** (activities that relate to the core R&D activities).

Companies should meticulously document how they are conducting their R&D activities as well as keep records of their observations, evaluations and conclusions resulting from these activities.

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Some examples of activities that are **NOT** core R&D activities (but may be supporting R&D activities) include:

- Reverse engineering or computer software for internal administration;
- Market research, management studies or research in humanities, social sciences or arts; or
- Mineral exploration or activities to comply with statutory requirements or standards.

What are the formalities to claim the R&D offset?

Lodge registration by 30 April 2015

A company wanting to claim the R&D offset for an income tax year must lodge its registration with certain government departments (i.e. Innovation Australia through AusIndustry) by 30 April the next calendar year (i.e. assuming a company wants to claim the R&D offset in respect of the 2014 income tax year, it must lodge its registration by 30 April 2015).

To register, the company must provide details of all their R&D projects and core and supporting activities undertaken in the income tax year. It is therefore very important that the company keeps good records describing each activity, its planned objective, and the actual outcome as this will help a company to prove its eligibility in the event of a review or audit.

Once the company is registered, it can claim the R&D tax incentive when it lodges its tax return (that contains a R&D schedule). This schedule will contain details of all expenditure related to each R&D activity (e.g. even the wages of laboratory assistants, overheads relating to the R&D activity and consumables used in the process). It is therefore very important that the company keep good records (e.g. time sheets for staff costs) of all its R&D expenditure.

Future changes to Australia's R&D regime?

We do not expect further fundamental changes to Australia's R&D regime in the near future.

The most recent change to R&D was on 5 March 2015 where legislation became law whereby, from 1 July 2014, the current 45% or 40% tax offset will only be available to R&D expenditure up to $100 million – R&D expenditure in excess of $100 million will be subject to a tax offset equal to the company tax rate (currently 30%).

How can Edwards Marshall assist you?

Edwards Marshall has the necessary skills and experience to assist you with all your R&D claims and record-keeping requirements to ensure you have the best chance of qualifying for the incentive.

We can assess the eligibility of a company's business and projects (e.g. determine whether their activities are core or supporting R&D activities) and register the R&D activities with AusIndustry by 30 April so that when the company lodges its company tax return and R&D schedule, it can claim the offset/refund from the ATO.

It may therefore be worth your while discussing with us whether any of your activities may qualify as R&D, and therefore qualify for the offset.

Please contact Edwards Marshall if you are interested to learn more about the R&D incentive and what this can mean for your business.

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