

1 November 2016

Go8 response to the Report of the R&D Tax Incentive Review

Introduction

The Group of Eight (Go8) welcomes the opportunity to comment on the Report of the R&D Tax Incentive Review.

The Go8 institutions may make individual and more detailed responses to the report and therefore the Go8 response is deliberately high-level.

The Go8 represents Australia's leading research-intensive universities, accounting for over two-thirds of Australian university research activity, spending around \$6 billion per year on research with the Go8 investing \$3 billion annually in applied research and experimental development.

The R&D Tax Incentive is the Government's largest single program in R&D estimated to be \$3.19 billion or nearly one-third of the Government's total R&D investment of \$10.12 billion in 2015-16.

As such, the Go8 highlights the need for the R&D Tax Incentive to facilitate collaboration between industry and universities and for spending – and importantly results - under the Incentive to be transparent, effective and necessarily targeted to ensure the best returns for the Australian economy.

In this context the Go8 is pleased to note the Review's commitments to an evidence based reform of the R&D Tax Incentive, to increase the additionalities and spillovers from the program and to drive collaboration and integration with other elements of Government's R&D investment, in particular Higher Education.

Go8 Key Points

1. The Go8 supports Recommendation 2 of the report, including:

- the introduction of a collaboration premium of up to 20 per cent for the non-refundable tax offset to provide additional support for collaborative R&D undertaken with publicly funded research organisations (PFROs)
- that the premium also apply to the cost of employing STEM PhD graduates in their first three years of employment.

Further, the Go8 would strongly recommend that Recommendation 2 eventually be extended such that the cost of employing PhD graduates from all disciplines is covered by the collaboration premium.

2. The Go8 supports the sustainability of the R&D Tax Incentive and in this light suggests that the Government must consider carefully the report recommendations to introduce an intensity threshold; to increase the limit of how much R&D expenditure the R&D Incentive is applied to from \$100 million to \$200 million.

It is important that any savings that are made through improving the sustainability of the R&D Tax Incentive are reinvested to support Australian R&D through other aligned mechanisms.

3. The Go8 encourages the Government to adopt a whole of system approach to R&D – particularly as applies to collaboration as suggested by the Review Panel – and align support for the R&D Tax Incentive with other elements of the Government’s R&D investment, particularly related to publicly funded research, such as the Biomedical Translation Fund and similar future investments.
4. The Go8 supports the R&D Incentive as one measure within the Government’s already charted Innovation “eco-system”, and is keen to have Government recognise that changes to the program must be made within this ‘eco-system’ context – they cannot be made in isolation. For example, the Go8 supports the Minister’s view as it relates to the introduction of a National Innovation Fund, and the Go8 submission is made with the expectation details of this Fund will be further defined within the change process related to the current R&D Tax Incentive.

The Go8 notes that there will be a need for further consultation and development of these key points to ensure that the details policy settings achieve the desired outcomes.

Discussion

Collaboration premium

A 20 per cent collaboration premium to foster collaboration with PFROs is strongly welcomed by the Go8. The application of the premium to the cost of employing STEM PhD or equivalent graduates will build increased capacity in industry to both undertake R&D within industry and collaborate effectively with Australia’s world class university and PFRO research system.

The Go8 emphasises the importance of PhD graduates from all disciplines in driving innovative R&D in industry, whether directly through R&D or through increasing the “absorptive capacity” of industry in terms of adopting new research findings and innovative practices.

The Go8 is definitive in its position that the collaboration premium is a critical element of fostering a long-term culture of PhDs as embedded commercial assets – as is currently the case in the UK, Europe, the US and Canada. While there is much talk of the value of collaboration to the nation’s productivity, it cannot be fully realised without the cultural change that better values PhDs and which Government can assist drive by its policy actions such as the collaboration premium.

The Go8 is particularly supportive of policy frameworks that recognise the value of PhDs driving innovative practices within SMEs.

The Go8 believes that the collaboration premium should apply to companies falling below the intensity threshold (if introduced as recommended), as collaboration between industry and PFROs should be fostered and encouraged at any level.

Further clarity is needed as to whether the proposed collaboration premium would apply to any company regardless of size. The report alludes to the additional financial incentive the premium would provide for large R&D-conducting companies; however, elsewhere does not specify targeted parties.

Comments on Recommendations 3, 4 and 5 from the report

The Go8 recommends that the Government undertakes further modelling to demonstrate that the proposed thresholds under Recommendations 3, 4 and 5 are both financially sustainable and well-targeted.

Recommendation 3

The \$2 million cap on annual cash refund payable must be targeted to avoid inadvertent effects that may reverse existing interest by SMEs to collaborate with universities. SMEs that already find it difficult to raise capital in the early stages of R&D may be further challenged by such a cap. Further investigation is recommended to more fully understand the likely impacts of such a cap before a decision is taken to implement it. Alternative options may be: to not apply such a cap; to apply the cap at a higher level; or to establish differential, well-evidenced, caps for different sectors.

The recommended cap has insufficient regard to the variety in levels and breadth of innovative activity from sector to sector. For example, a number of health science start-ups and companies that rely on collaboration with universities are often smaller enterprises that historically have claimed in excess of the \$2 million. Companies that take the development path of key Australian successes such as Vaxxas (receiving \$25m in Series B venture financing in 2015), Fibrotech (sold for \$81m in 2014) and Spinifex (sold for \$261m in 2015) would be unduly disadvantaged in the event of such a cap.

The report insufficiently substantiates its claim that refundability is likely to provide fewer tangible benefits for SMEs with larger R&D expenditures and that these SMEs would be able to find alternative sources of finance.

Nor does the report adequately support its claims for opposing a quarterly payment system to improve cash flow as can be critically needed by SMEs and in any start-up's early stage trajectory toward commercialisation.

Recommendation 4

The introduction of an intensity threshold of between 1-2% of business expenses dedicated to R&D to access the incentive would have positive effects in terms of requiring a minimum level of R&D activity – which in itself would likely promote the desired greater levels of collaboration. Implementation of such a threshold should be guided by a better understanding of what level of intensity can be realistically sought that represents an effective balance to an increased claimable expenditure threshold. Clarity that the intensity threshold would apply to larger companies, better defined, is also needed.

Recommendation 5

An increase of the limit of how much R&D expenditure the R&D Incentive is applied to from \$100 million to \$200 million should foster and assist further university and research collaborations with large innovative companies. However, it may be counterproductive to sustaining the sustainability of the R&D Tax Incentive measure and may work against encouraging incentives for innovation-active SMEs and businesses of all sizes and age to access Go8 research and IP, thereby reducing commercialisation or translation opportunities.

Alignment of the R&D Tax Incentive with other Government investment in R&D

The Go8 notes that the review panel suggests, but does not formally recommend, that the Government review, consolidate and refocus existing programs to prioritise collaboration, referencing the Research Block Grants, the CSIRO Innovation Fund, the Cooperative Research Centres, the Growth Centres, Innovation Connections, Rural Research and Development Corporations, Australian Research Council (ARC) linkage scheme and impact and engagement measures. Significant work is already occurring under the National Innovation and Science Agenda and via response to previous reviews that should constitute the bulk of the response by the Government to this suggestion.

There is validity in holistically considering measures to promote collaboration, and in considering the impact and effort of programs that do not directly or principally promote collaboration between industry and researchers but nevertheless promote conditions necessary to such collaboration (such as research infrastructure investments).

Any response by the Government to this suggestion would need to naturally take account of recent measures to review or assess such programs, and that activities undertaken during the R&D Tax Incentive Review would already in some measure have refocused existing initiatives to promote collaboration. This includes the development of new Research Block Grant Guidelines released on 11 October 2016 and the guidelines for the newly revamped and expanded Innovation Connections.

In particular, the Go8 strongly suggests that the Government work to align the R&D Tax Incentive with current and possible future National Innovation and Science Agenda initiatives, such as:

- The Biomedical Translation Fund and the Government's already stated direction of establishing a companion National Innovation Fund for the translation of non-medical sciences research at Australian universities. Any such new fund would need to be carefully designed and targeted to fit in with existing early commercialisation support programs such as the fund being established in a collaboration between the Go8 and the UK IP Group.
- Government research infrastructure investment - such as through NCRIS – and maximising the value from the university and PFRO precincts that most productively house this research infrastructure.

In closing:

The Go8 would like to add the comment that through every recent review and discussion with Government, the higher education sector's need for policy and funding certainty has been stated as of paramount concern. Programs that have been highly successful internationally that assist drive an innovation agenda and



therefore productivity and jobs, have one thing in common – they have been allowed time to succeed quarantined from political vagaries and changes of Government. Long-term and sustainable must also apply to any changes to the R&D Tax Incentive.