New Zealanders for
HEALTH RESEARCH

A Research and Development Tax Incentive for New Zealand

Discussion Paper

April 2018

Submission by

New Zealanders for Health Research (NZHR)

Recommendations

The 10 year R&D expenditure aspiration be set at 3.3% of GDP

The tax incentive be set at 35% of eligible expenditure

Non-tax paying entities which conduct R&D be as equally incentivised as businesses

Small start-up companies be eligible for the incentive from the scheme's commencement

The R&D tax credit be targeted to government priority areas

Eligibility include a requirement that R&D activity be founded on robust research methodology

s 9(2)(a)
[redacted]
www.nz4healthresearch.org.nz

Overview of NZHR's submission

New Zealanders for Health Research (NZHR) was formally established in November 2015 to lift investment in health research from all sources including industry, government and philanthropy. Our members include University of Otago, Massey University, Victoria University, the Malaghan Institute, Merck Sharp and Dohme, Roche, AbbVie, CureKids, Auckland Medical Research Foundation, the Cawthron Institute and the New Zealand Association of Clinical Researchers (NZACRes).

NZHR's ultimate aim is to achieve improved prosperity and health for all New Zealanders, and we believe that well-resourced, appropriately directed high quality health research is a key contributor to these outcomes.

We therefore support in principle the introduction of a New Zealand R&D tax incentive. We believe that with appropriate targets and policy settings it will create an environment which will foster increased and much needed investment in health research, which in turn will lead to improved health outcomes and a strengthened economy.

NZHR welcomes the opportunity to comment on the R&D Tax Incentive discussion paper.

In summary our submission is that:

- The government's commitment to increasing R&D expenditure to two percent GDP over 10 years is not ambitious enough and needs to be bolder
- The proposed 12.5% tax credit on eligible expenditure is too low an incentive to be effective in counteracting prevailing disincentives to business investment in research, including health research
- SOE's, Crown Research Institutes, District Health Boards, Tertiary Education Institutions, and their subsidiaries should be equally incentivised to invest in R&D
- The incentive should be available to small start up companies
- The R&D tax credit should be targeted to government priority areas to ensure that it not only contributes to business development and growth, but also maximises positive societal and community impact
- Eligibility for the tax credit should be based on demonstrating that the R&D activity is based on research which uses robust methodologies

R&D Expenditure as a percentage of GDP

The discussion paper notes that New Zealand's gross expenditure on R&D as a percentage of GDP is 1.3%. This compares unfavourably to all of the comparison countries identified on page 7 of the paper, and to the OECD average of 2.38%. Furthermore New Zealand's business expenditure on R&D is 0.64% of GDP compared to an OECD average of 1.65%.

New Zealand's gross R&D expenditure is therefore 55% of the OECD average and business expenditure 39%. Given that the focus of the discussion paper is on incentivising growth in business R&D it would have been helpful if the discussion

paper had also included comparative figures for business R&D, or at least a reference to source documents. This notwithstanding according to Statistics NZ 2014 figures, New Zealand business R&D as a percentage of GDP has been significantly lower than both other comparable small advanced economies and our major trading partners, as follows[1]:

Table 1
Research and development expenditure as a proportion of GDP
Small advanced economies
2013 or 2014

Small advanced economy	Business	Government (excluding higher education)	Higher education	Total
	Percentage of GDP			
New Zealand	0.54	0.27	0.36	1.17
Denmark(1)	1.95	0.07	1.01	3.05
Finland(1)	2.15	0.27	0.73	3.17
Ireland	1.11	0.07	0.31	1.49
Israel(1)	3.47	0.08	0.52	4.11
Singapore	1.34	0.25	0.60	2.20

1. Totals include private non-profit sector performing research and development which is excluded from the sector breakdowns.
Note: Due to Footnote 1 and rounding some figures may not add to stated totals.
Source: OECD data and Statistics New Zealand

Table 2
Research and development expenditure as a proportion of GDP
Major trading partners
2013 or 2014

Major trading partner	Business	Government (excluding higher education)	Higher education	Total
	Percentage of GDP			
Australia(1)	1.19	0.24	0.63	2.11
China	1.58	0.32	0.14	2.05
Japan(1)	2.79	0.30	0.45	3.59
United Kingdom(1)	1.09	0.13	0.44	1.70
United States(1)	1.94	0.31	0.39	2.74
				2.38

1. Totals include private non-profit sector performing research and development which is excluded from the sector breakdowns.
Note: Due to Footnote 1 and rounding some figures may not add to stated totals.
Source: OECD data and Statistics New Zealand

[1] http://archive.stats.govt.nz/browse_for_stats/businesses/research_and_development/research-development-nz-2014/international-r-and-d-activity.aspx

The Ministers' forward to the discussion paper makes the point that "for businesses R&D is recognised as a key indicator of innovation, which enhances their ability to be successful in changing markets". NZHR's analysis of how New Zealand's business R&D as a percentage of GDP compares with other countries on average and other specific comparable economies, as above, suggests that the OECD average of 1.65% represents a broadly appropriate aspirational ten year target. Given that business R&D currently comprises about half of New Zealand's total R&D, and assuming that this continues to be appropriate, NZHR believes that New Zealand should be aspiring to increase R&D expenditure to 3.3% GDP over 10 years.

Failing to be relatively bold and ambitious risks achieving little except for maintaining the status quo.

Proposed tax credit rate too low

NZHR believes that the monetary value of the tax incentive should be sufficient to both contribute to achieving an appropriate R&D % of GDP target, and to encourage businesses to actually take advantage of it.

Apart from acknowledging that it is not the only variable, the discussion paper does not provide any information about the cause and effect relationship between the proposed R&D tax incentive and R&D expenditure as a percentage of GDP.

NZHR was not able to independently identify any evidence that there is in fact any correlation between R&D tax incentives and R&D as expenditure as a percentage of GDP, and we understand that of the countries referred to in Table 1 above neither Denmark or Finland have them. We also understand that Switzerland and Germany, with business R&D at 2.4% and 2.0% respectively, do not have them either.

Furthermore, it has been noted that while tax incentives can induce firms to invest more in R&D, it appears that the innovativeness of an economy is unlikely to depend on their presence. Simply introducing an R&D tax incentive or making an existing scheme more generous in countries where framework conditions for innovation are lacking might be a waste of government resources. Policymakers should first focus on policies that enhance the overall entrepreneurial environment, in which R&D tax incentives can be a nice addition.[2]

Other commentators note that while tax incentives are better than grants[3], there are several reasons why R&D policy interventions might not be effective, including that: R&D might directly substitute for private funding of R&D projects that would have been undertaken anyway; it might crowd out private R&D indirectly by increasing the demand for R&D inputs including labour supply; and desired rates of social return might not be achieved.[4]

Furthermore, Australian innovation expert Anna Lavelle, who served on the Australian R&D tax advisory committee, is quoted as saying that the small tax

[2] https://voxeu.org/article/rd-tax-incentives-new-evidence-trends-and-effectiveness
[3] https://acta.mendelu.cz/media/pdf/actaun_2017065020737.pdf
[4] http://bruegel.org/wp-content/uploads/2016/02/WP-2016_01-1.pdf

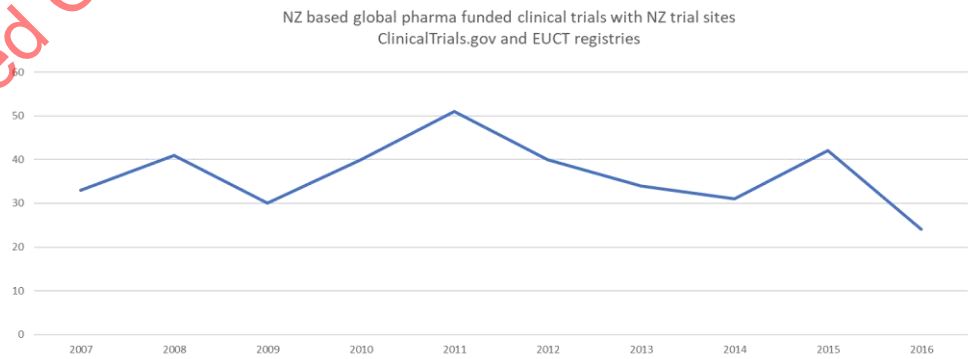
percentage rebate being proposed for New Zealand would not be enough to "move the dial"[5]. NZHR believes that this inertia will to an extent be exacerbated by the fact that for some companies the benefit of the tax incentive will be at least partially offset by no longer having access to the Callaghan Innovation Growth Grant

In order to overcome systemic factors which will militate against the effectiveness of the tax incentive, and assuming that there will be a process to ensure that the proposed incentive will translate into both greater innovation and increased R&D expenditure, NZHR proposes that it be set at 35% of eligible expenditure, for the following reasons.

We note that the 2018/19 budget is forecasting that GDP will be $354.6b by 2022/23. In order for R&D expenditure to be on track to achieve the 2.0% of GDP ten year target, it will need to amount to $5.85b in 2022/23, or an additional $1.25b over and above what it would be if expenditure were to continue at the current 1.3% rate. Given that the 2018/19 budget forecasts that the Research and Development Tax Credit Implementation will require provision of $350m in 2022/23, this appears to represent a good investment (even acknowledging that it is not intended that it will not be the only contributor).

However, as argued in the previous section NZHR believes that the aim should be to achieve an overall 3.3% target over ten years. This suggests that by 2022/23 the country should be aspiring to achieve a 2.3% R&D investment target, or $8.16b which is $3.5b above what it would be if expenditure were to continue at the current 1.3% rate. Assuming that there is a correlation between the size of the tax incentive and its impact on total R&D expenditure NZHR believes that the 12.5% rate will be too low, and that it should be increased to 35%.

In respect of NZHR's mandate to advocate for increased industry investment in health research we note that the quantum of pharmaceutical R&D investment internationally has grown more than any other sector[6]. However, the number of international clinical trials being undertaken in New Zealand by multinational pharmaceutical companies with business operations in New Zealand has been falling since 2011, as illustrated in the following chart.



[5] https://www.nbr.co.nz/article/businesses-asked-comment-125-rd-tax-credit-be-p-214855
[6] https://biblio.ugent.be/publication/8507277/file/8507279.pdf p24

NZHR pharmaceutical company members advise that this is occurring in large part because of the disincentives to investing in R&D in New Zealand associated with Pharmac's medicines purchasing and rationing practices. NZHR believes that an appropriate way to address this problem is to introduce countervailing R&D incentives such as what is proposed in the discussion paper. However a 12.5% setting is unlikely to make any significant difference, whereas a 35% setting is more likely to make a positive impact.

SOE's, Crown Research Institutes, District Health Boards and Tertiary Education Institutions

NZHR maintains that SOE's, Crown Research Institutes, District Health Boards, Tertiary Education Institutions, and their subsidiaries, should, if they pay tax, benefit from the tax incentive in the same way as is intended for business.

If they do not pay tax we maintain that they should be incentivised to engage in R&D activities in other ways. This could be by way of a subsidy on discretionary eligible R&D expenditure which would be equivalent to the financial benefit they would accrue if they were tax paying entities, or the incentive could be applied to those entities' R&D staff PAYE returns.

NZHR advocates for increased government expenditure on health research, and we note that the 2018/19 budget's increased investment specifically in health research is limited to the short term. Our best case estimate is that government health research specific expenditure will peak at 0.81% of health care expenditure in 2019/20 and progressively fall to 0.69% by 2025/26. This is well short of NZHR's recommended level of 2.4%. However, the ability of DHBs in particular to claim a contribution to their discretionary eligible R&D expenditure would assist in ameliorating this situation.

Small start-up companies

In the health research space, a lot of BERD will be contained within start-up biotech ventures. These companies are going to be pre-profit and, in many cases, will not carry an expectation of generating revenue prior to exit so tax credits carried forward are not useful. The scheme as currently proposed does little to support or incentivise these companies, and rather than wait for an unspecified mechanism to be in place by April 2020 NZHR recommends that be included in the scheme from its commencement. Although the context is different we broadly support recent comments offered by Nat Torkington[7]

[7] https://thespinoff.co.nz/business/31-05-2018/why-half-baked-rd-changes-are-a-finger-in-the-eye-to-startups-and-software/

R&D tax credit targeting

NZHR maintains that the R&D tax credit should be targeted to government priority areas to ensure that it not only contributes to business development and growth, but also maximises positive societal and community impact.

Improved health outcomes, for example, have long been a government priority, yet there has not yet been a concerted, evidence based approach to identifying and translating effective interventions into policy and practice.

NZHR believes that a significant proportion of the R&D tax incentive budget should be specifically allocated to health research and development, with the actual proportion based on health expenditure's share of total government spending on all priority areas.

Good research

In order to ensure that the R&D tax incentive has the best chance of maximising positive societal and community impact one of the eligibility criteria should be that the R&D activity is founded upon methodologically rigorous research as determined by a relevant expert third party agency.

Mechanisms for achieving this depend on the nature of the research and the scale of the organisation, but should include the following considerations:

- If research is undertaken through a contracted arrangement to an accredited third party research organisation (Approved Research Organisation) then this can be used as a simple accountability measure.
- In these cases, and in research undertaken within a company or other eligible organisation, R&D tax credit returns should provide information that feeds directly into the National Research Information System (NRIS) that is under development (and which received $10.1million for implementation in Budget 2018). This can be used for audit and accountability purposes, but also to enable the NRIS to fully track R&D activities in New Zealand through a trusted integrated data infrastructure. Business confidentiality and information privacy will need to be built into the NRIS for capturing such information and only reporting aggregated statistics.
- For small enterprises that do not meet the $100,000 per annum annual R&D expenditure threshold (p 22) the proposed mechanism for allowing activities outsources to an Approved Research Provider is good to see, but for many of these organisations (particularly those on a strong growth trajectory) direct support through research growth grants will still be important—such a grant-funding mechanism to augment R&D tax credits can also provide assurance of the quality, nature and outcomes from the research.
- Tracking outcomes from research funded through R&D tax credits will also be important, and requirements for NRIS data to be provided by companies claiming R&D tax credits will greatly benefit this, and will allow the medium- and long-term effectiveness of the scheme to be accurately evaluated and monitored.

Additional comments from NZHR members

- The definition of R&D should include phase 3 trials and should not be limited to phase 1 and 2 trials only (Question 2)
- Relevant activities such as submissions to the SCOTT committee should not be excluded (Question 7)
- The decision to hire clinical research staff is based on two main factors: The volume of work and the full costings of the staff. When a company decides to employ clinical research personnel it will include in its decision process the full costs which include not only salary but the associated costs to complete the role such as travel costs, IT costs, stationary etc. When planning for R&D staff businesses will typically take full costs into account in the decision to proceed or not. It is therefore recommended that full costing be included to drive the effectiveness of the incentive (Question 10)

To: RDincentive@MBIE.govt.nz

Submission on: Fuelling innovation to transform our economy – A discussion paper on a research and development tax incentive for New Zealand

Date: 1 June 2018

Submitter:

s 9(2)(a)

Agcarm – representing NZ's animal medicine and crop protection industries
111 The Terrace
Wellington

s 9(2)(a)

Submission on: Fuelling innovation to transform our economy

1. Introduction

1.1 Agcarm welcomes the opportunity to comment on the Research and Development tax incentive for New Zealand discussion document.

1.2 As an industry association representing members who are focussed on development of new products, we have a strong priority on encouraging policy and regulation that accelerates innovation. Hence, we are very supportive of the government's goal of increasing R&D expenditure to 2 per cent of GDP over ten years.

1.3 Agcarm is supportive of the key points and recommendations raised by Business NZ, and we support their submission.

1.4 We note that the current regulation (e.g. HSNO Act) around development and research of innovative products within the crop protection and animal medicines sectors is very restrictive. We request that in addition to encouraging tax credits, a focus is placed by MBIE on reviewing relative regulation, specifically in providing more encouragement for biotech (e.g. GMO, gene editing) to be researched and products registered for use within New Zealand.

2. General Comments

2.1 Agcarm represents a range of businesses, from small New Zealand enterprises through to global corporates (refer to Appendix 1 for our current membership list). Based on our broad representation we submit that tax credits should be made available to all businesses regardless of their legal structure.

2.2 The new definition (as below) outlined for R&D, appears to be weighted towards research, rather than development. Therefore, there is a risk that if the current definition is introduced, the ability for many businesses to apply for and succeed in obtaining the R&D tax credit scheme will be greatly affected. Especially, in relation to small businesses.

As a first step we recommend that the word 'development' is included within the definition. This will enable businesses to both develop ideas, and then research them to develop new beneficial products.

(a) Core activities: those conducted using scientific methods that are performed for the purposes of acquiring new knowledge or creating new or improved materials, products, devices, processes, or services; and that are intended to advance science or technology through the resolution of scientific or technological uncertainty.

OR

(b) Support activities: those that are wholly or mainly for the purpose of, required for, and integral to, the performing of the activities referred to in paragraph (a).

2.3 Agcarm supports the principle that up to 10 percent of the eligible expenditure on an R&D project can be for overseas costs. Due to a lack of particular species of crops or animals, or regulatory restrictions within New Zealand, it may not be possible for all the development and research to be carried out locally by our members. Hence, the idea of expenditure overseas being eligible for tax credits is supported. There is some thought that this cost could be increased to 20 percent, given the increasing emphasis on global research for innovative solutions within New Zealand.

2.4 When it comes to transparency around the allocation of substantial government funds, the disclosure of relative information that falls within the requirements of the Privacy Act could be released. A similar approach could be adopted as per the Primary Growth Partnership programme, where details on funding are released via an annual report.

2.5 On the evaluation side, Agcarm recommends that a comprehensive review and cost-benefit analysis is undertaken within four years of the introduction of tax credits to ascertain their success or otherwise in promoting innovation and investment to increase New Zealand's productivity.

3. Conclusion

3.1 Agcarm is supportive of any government initiative aimed at increasing innovation, along with R&D. We acknowledge that R&D tax credits are just one means of encouraging innovation, and recommend that MBIE look at additional means such as removing regulatory barriers.

3.2 The key risk of the R&D tax credit scheme is ensuring the correct balance between the correct targeting of tax payer money towards genuine R&D expenditure, while ensuring that any R&D tax credit thresholds are not so constrained as to deter worthwhile businesses from applying for a credit, so that the scheme remains underutilised.

4. About Agcarm

Agcarm is the industry association for manufacturers and suppliers of crop protection and animal health products. For further information and a full list of members, see www.agcarm.co.nz.

Agcarm member products protect public health, improve animal welfare and help environmental management. They:

- Play a pivotal role in growing high yield, sustainable food and fibre products;
- Help supply healthy, nutritional and affordable food;
- Keep New Zealand's agriculture, horticulture and forestry sectors internationally competitive.

Our members are committed to safety, innovation and product stewardship.

Appendix 1: <u>Agcarm Membership</u>

COMVITA® Share Nature. Share Life

1 June 2018

'R&D Tax Incentive team'
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140
New Zealand

By Email: RDincentive@MBIE.govt.nz

To whom it may concern,

As a science-led business, Comvita supports the Governments' vision to help businesses like ourselves invest more in Research and Development (R&D) to contribute to a diverse, sustainable and productive economy. We welcome the opportunity to provide feedback on the proposed new R&D Tax Incentive for New Zealand.

About Comvita

Comvita Ltd. (www.comvita.co.nz) is a natural health products company headquartered in Paengaroa, Bay of Plenty. Comvita was founded in 1974 by New Zealand beekeepers Claude Stratford and Alan Bougen, who set out to connect people to nature for the benefits of good health.

Since then, Comvita has grown rapidly to become a globally-recognised, NZX-listed company (NZX:CVT) with revenue of $156 million per annum (as at 30 June 2017) and more than 450 staff across New Zealand, Australia, Hong Kong, China, Japan, South Korea, North America and the UK. Kiwi Bee Medical Ltd., a wholly owned subsidiary of Comvita, is one of New Zealand's largest apiary operations, with more than 40,000 hives and six locally-operated branches throughout the North Island.

As a science-led organisation we value investment in quality research and our research capabilities and infrastructure. We partner with world class researchers and research organisations, both here in New Zealand and overseas. Our current research programmes include a large Manuka cultivar breeding and plantation programme and laboratory and clinical trial programmes examining the human health benefits of our natural ingredient platforms including Manuka honey, Propolis and Olive Leaf Extract.

Comvita is currently a recipient of a Callaghan Growth Grant and a Ministry of Primary Industries Primary Growth Partnership programme. We have also been a recipient of the prior 2008 tax credit scheme and have supported multiple PhD and MSc students through Callaghan's Student Grants Schemes.

Executive Summary

Having reviewed the proposal and carefully considered the potential impact on our business, and similar NZ businesses, we consider that the R&D Tax Incentive as proposed:

1) Lacks clarity on the scope of eligible R&D and the types of expenditure that can, and cannot, be included.
2) Does not sufficiently encourage business investment in quality R&D.

We have specific concerns regarding the proposed criteria, the amount of funding on offer to individual businesses and the use of the tax system to manage the process. The following section outlines our concerns in more detail and our recommendations to address these concerns.

Concerns and Recommendations

1) The proposal lacks clarity on the scope of eligible R&D and the types of expenditure that can, and cannot, be included

- The definition of R&D under the proposed tax incentive appears, at face value, to be narrower, and the terms used less clear, than the definition under the current Callaghan Growth Grant Scheme. The discussion documents details that the incentive is intended to support:

  > *"R&D that addresses a material problem and anticipates a material advance in science or technology. This is reflected in the requirement that activities are intended to "advance science or technology through the resolution of scientific or technological uncertainty", which ensures that the credit is only available for solving problems that have not already been solved, and which will expand the existing knowledge base."*

  The scientific and technological merit of R&D, and whether a problem has been 'solved' through science, is a somewhat subjective judgement and open to different interpretation. Different thresholds of certainty of scientific resolution apply in different settings. In the health sector multiple similar research studies are required to address residual scientific uncertainty, albeit in some cases small levels of uncertainty. Some may view these type of repeat studies as "me-too, non-novel" research that are outside the scope of the incentive scheme. However, repetition of research is a valid, and valuable, scientific method and is in fact a requirement of many health regulatory authorities whereby key research findings (for example clinical research results) must be repeated in order to demonstrate the scientific validity of the research findings. It is not clear if this type of research is indeed intended to be excluded, or not. If it were to be excluded this would have a negative effect on our business through increasing the net cost of such R&D activity which is currently permitted under the Callaghan Growth Grant Scheme. We believe the impact will be similar on other NZ businesses, particularly in the health sector.

  - ***Recommendation:*** *The criteria should provide specific examples of R&D activities that are intended to be included and excluded as the wording as it currently stands is too subjective and open to interpretation (both by participating businesses and future tax advisors and auditors). The coverage of repeat clinical trials required for resolving residual regulatory authority uncertainty in the health sector should be specifically addressed.*

- The proposal specifically excludes "pre-production" activities, such as demonstration of commercial viability, tooling-up and trial runs. These activities are a critical part of the development stage of "Research and Development". Innovation is an iterative process; whereby prototype products and services are refined following consumer feedback. Pre-production activities and trial runs form an integral part of the R&D feedback loop; excluding these activities would have a negative effect on our business, increasing the net cost of such R&D activity. During discussions, Ministry of Business, Innovation and Employment (MBIE) officials noted verbally that the list of excluded activities, including pre-production activities and market research, "*may be*

included if they were undertaken as part of an R&D project". Clarity on this interpretation is needed.

- *Recommendation: The criteria should provide more clarity on the inclusion, or not, of activities that may cross the R&D and business as usual spectrum, for example manufacturing. Examples should be given to support this clarification. Prototyping and further development of products and services following consumer feedback or to meet market requirements should be included, whereas costs associated with business as usual activities should not.*

- The proposed criteria for eligible expenditure are not clear. Three options are proposed, one includes labour costs only, whilst the other two include overheads as a fixed percentage or apportioned. Currently labour costs, overheads, and other costs of research including third party providers and consumables can be included in Growth Grant Scheme claims. Limiting claimable expenditure to labour costs only would have a negative effect on our business since labour is rarely the primary cost associated with a research project. Research project costs in the health sector are dominated by costs associated with third party research providers laboratory and clinical tests and consumables.

  - *Recommendation: All expenditure associated with R&D should be included as eligible expenditure. This would include direct labour and overhead costs, as well as consumables and all costs associated with conducting research through third party providers.*

2) The Proposal does not sufficiently encourage business investment in quality R&D

- We understand from our discussions with MBIE officials that a large number of businesses in New Zealand conducting R&D are not accessing the currently available Callaghan Growth Grants. We can speculate that barriers to businesses participating is the requirement to provide audit information up front and have their R&D plan audited, reviewed and approved by Callaghan annually.

  The use of the tax system to distribute funding through credits certainly enables more businesses to participate, since all business already participate in the tax system. However, a tax system does not provide any assessment, or reassurance, of the quality of R&D that is being subsidised by the government as this is rightly not IRD's skill set. Our concern is that whilst more businesses may participate in a tax-based scheme, and more money overall may be spent on R&D funding by the government, there is no certainty that such R&D is of sufficient quality to deliver the desired economic or knowledge gains for New Zealand.

  - *Recommendation: Callaghan Innovation continue to play a role in the assessment of the R&D eligible for tax credits, either on a pre-approval basis or in an advisory/auditing capacity.*

- We consider the IRD is not properly equipped to assess the validity of claims for R&D and represents an audit and compliance risk to business which could disproportionally impact small and medium sized enterprises (SMEs). The risk of future penalties may lead some businesses to be very conservative in their tax returns thus missing out on potential tax credits. Different auditors

and tax advisors may give different advice to businesses given the lack of clarity around the criteria as discussed above. In addition, being a yearly tax credit rather than a rebate received quarterly, there would also be a negative effect on cash flow for businesses following the transition.

  - ***Recommendation:*** *The Callaghan Growth Grants scheme should continue alongside the new tax incentive scheme; that way businesses can choose which scheme best suits their needs.*

- The amount of the proposed R&D Tax Incentive, as a percentage of R&D spend, is lower than the existing arrangement under the Growth Grant scheme, administered by Callaghan Innovation. This will have a negative effect on our business, increasing the net cost of our R&D programme and thus providing a disincentive to invest more in R&D. We believe the impact will be similar on other New Zealand businesses, in particular those currently accessing a Callaghan Growth Grant.

  - ***Recommendation:*** *The* R&D Tax Incentive *should, at minimum, match the net (after tax) amount claimable under the Callaghan Growth Grant (14.4% of R&D spend) such that businesses currently accessing this scheme are not disadvantaged by the transition. Arguably there is rationale to increase the rate beyond 14.4% to encourage incremental investment in R&D and account for the potential increase in compliance costs to businesses. A rate of 15-20% would actively encourage more investment in R&D.*

- Whilst the maximum claimable amount per year is theoretically higher under the proposal compared with the Growth Grant scheme ($15 million vs $5 million), the amount of R&D investment required to access more than $5 million is considerable (>$40 million per annum). This is highly unlikely to be attained by the vast majority of New Zealand businesses conducting R&D, therefore, rendering the higher available funding largely moot.

  - ***Recommendation:*** *Given the very small number of New Zealand companies likely to benefit from the proposed higher claimable amount we recommend this be lowered from $15 million to $7.5 million per annum to reduce the overall exposure to the government from the scheme. The small amount of businesses planning to invest more than $60 million per annum in R&D (the amount needed to claim $7.5 million) could be dealt with on a case-by-case basis.*

- We welcome the inclusion of overseas research costs in the proposal; however, in our opinion, the amount being proposed for overseas research (10%) and the criteria being applied render this offering largely meaningless.

  Science is a global business and as such we partner with research groups with the most expertise, and those most likely to deliver on our research questions. Whilst we partner with New Zealand researchers wherever possible, the reality is that the research community here is small and does not always have the expertise, or scale, needed for some of our research needs. This is especially true in the context of clinical trials and health research where research is often outsourced to overseas Clinical Research Organisations or academic research institutes. The tax incentive, as proposed, is at a level that is unlikely to overcome other driving economic and market factors which may lead to businesses deciding to undertake their research activities overseas. For example, these include cost and time benefits, the population being studied, key opinion leader location and market access.

Share Nature.
Share Life

Some countries' regulatory authorities require that research is undertaken in a 'comparable' population to their own, which may not be representative of the NZ population. China specifically requires that research undertaken to support Health Claims is carried out in China. It is our view that benefits of research, in terms of knowledge (creation of research networks, sharing of information with local research teams) and economic benefits (IP ownership, business growth and more skilled jobs), will ultimately flow back to New Zealand regardless of where the research was undertaken, therefore, international R&D should be treated the same as New Zealand R&D.

- ***Recommendation:*** *Eligible R&D expenditure should include research conducted overseas where the costs are incurred by a New Zealand tax resident company. The rate of the incentive for overseas research should be at the same rate as New Zealand-based research without further limiting criteria.*

Thank you once again for the opportunity to provide feedback on the proposed new R&D Tax Incentive. We share the government's vision of NZ businesses, like ourselves, investing more in R&D. However, we are very concerned that the Tax Incentive, as proposed, will not achieve this vision.

We would be happy to meet with officials to discuss our concerns and recommendations in more detail and look forward to working with the Government to deliver a scheme that will fulfil its stated intent.

Yours sincerely

s 9(2)(a)

COMVITA NEW ZEALAND LTD
Comvita New Zealand Limited, 23 Wilson Road South, Private Bag 1, Te Puke 3189, New Zealand. PH: +64 7 533 1426, FX: +64 7 533 1118

From: David Hirst
To: RD Incentive
Subject: RE: Save New Zealand"s knowledge economy [UNCLASSIFIED]
Date: Friday, 1 June 2018 10:32:46 a.m.

Dear Team,

The $100k threshold for R&D spending fails to target most of the smaller companies performing R&D and only provides benefits for the “winning horses”.

I have spent the last 20 years working for a variety of companies, building optical and electrical hardware the fibreoptic, power distribution and industrial safety markets. For most start-ups, intial R&D is bootstrapped on one or two initial sales – there might be some pre-sale R&D but this is (by necessity) performed gratis – with R&D happening while the sales are growing. There is often no ‘full-time R&D’ happening, just product development to support initial sales. To get to $100k of R&D spend typically means that sales will be in the order of $200k - $300k, so the initial hurdle has been overcome and (although doubtless welcome), the R&D tax credit is no longer critical to the company’s development.

The situation is worse for low-volume, high-margin products where the component cost may well be on a par with an employee’s wages, so the initial R&D hurdle is even harder to overcome – the company is even more reliant on fewer sporadic sales and really needs a good angel investor to get them through the first few years.

An alternative to the hard $100k threshold is a sliding scale, starting at (say) $50k. It must also be applied in addition to clear and transparent government funding schemes; if the government pitches itself as a supporter of new enterprise, as an ‘angel investor’, then it must be prepared to lose money on some startups, knowing that it will win on others. That’s the way investment works.

Regards,
Dr David Hirst
P.S. This email address replaces the s 9(2)(a) address used previously. I am responding on my own behalf, not as an employee of Ellis Terry Ltd.

From: RD Incentive [mailto:RDIncentive@mbie.govt.nz]
Sent: Friday, 1 June 2018 10:03 a.m.
To: RD Incentive <RDIncentive@mbie.govt.nz>
Subject: RE: Save New Zealand's knowledge economy [UNCLASSIFIED]

Kia ora, and thank you for your recent email to the Hon Megan Woods regarding the R&D tax incentive.

We really value hearing from people in the startup sector, as we want to ensure we get the policy right to support as many businesses as possible to lift their R&D.

We would appreciate your feedback in more detail on our proposals for the R&D tax incentive. It is really important to this process that we have a strong understanding of your concerns, and how different design options could affect your business.

Official submissions close 5pm today (1 June) on MBIE’s website, so we encourage you to get in and make a submission to the questions relevant to you. Or you can respond to this

email directly.

If you haven't already, have a read of the Minister's response where she addresses Toby Littin's concerns about startups and loss-making firms.

While the submission period is drawing to a close we're still keen to hear from you throughout process of designing the tax incentive, so feel free to keep in touch with us at this address.

Kind regards,
The R&D Tax Incentive Project Team

www.govt.nz - your guide to finding and using New Zealand government services

31 May 2018

R&D Tax Incentive Team
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140

Dear Sir/Madam,

R&D Tax Incentive Submission

We appreciate the opportunity to provide feedback in response to the Ministry's working paper "Fuelling Innovation to Transform Our Economy."

We are pleased to see that Government is working to support increased R&D activity at a national level. We strongly agree that this is in the national interest and essential to maintaining future competitive advantage, both for individual companies and our country as a while.

However, we are concerned that some of the proposed changes do not adequately address the needs of longer lead time, R&D-intensive business like our own in the fields such as process technologies, drug development, and medical devices.

Avertana's submission focuses particularly on:

- proposed R&D Tax Incentive being non-refundable,
- proposed end to Callaghan Innovation's Growth Grant Scheme.
- Supporting activities and R&D related capital expenditure.
- Exclusions and eligible expenditure.
- Cap on R&D tax credit.

We agree both with Government's view that New Zealand's private sector must develop a greater focus on R&D for long-term economic benefit, and with the creation of clear market signals via the tax system that incentivise greater R&D investment.

Our concern is that the policies promulgated by Government need to support all R&D intensive sectors equally. By our reading, the policy as it is currently presented is likely to be more favourable for the majority of "tech" R&D that has a shorter lead time to market (e.g. ICT, food and beverage, agritech) but may not be as favourable as current grant arrangements for technology sectors with a longer lead time (e.g. process technology, drug development, medical devices).

Background

Avertana is a process technology company based in Auckland, that is commercialising proprietary technology to refine waste slag from the steel industry into raw materials used to manufacture everyday goods such as paints, fertilisers, paper, and construction materials.

The company has had a close and positive working relationships with various Government agencies including Callaghan Innovation, NZTE, Ministry for the Environment and MBIE since its establishment in 2014.

From inception and to date, our business has been solely focused on researching, developing, and demonstrating its globally novel intellectual property. Avertana does not generate any significant commercial revenue and is unlikely to do so until the technology has been deployed at scale by a large, industrial partner. This remains some years away at present. Typically, in the process technology field, successful technologies are developed for seven to twelve years prior to first commercial deployment. In the case of our peer company, LanzaTech, this journey took fourteen years, with its first commercial plant now in commissioning in China.

As a result, Avertana is reliant on grants and investor capital to support ongoing operations. Effectively, 100% of the company's revenue is achieved on technology success and completion.

This means that cash is critical and the sole financial consideration of the business. The company's tax position is in a loss long term and therefore any taxation support like the R&D tax incentive proposed is of no value to Avertana or to the many loss making company's similar to us.

Specific Response to Questions

Set out below are Avertana's comments in response to questions where the company foresees a potential issue with the proposed policy.

Question 6 – How well does this definition apply to business R&D carried out in New Zealand?

Supporting activities are crucial as part of the overall R&D effort. Our entire company's sole purpose is technology R&D, but not everyone can be directly involved in scientific and engineering investigation. Complementary commercial activities such as market research, industry analysis, business development, finance and technical pre-sales (sales engineering) are essential to ensuring the technologies we develop meet customer individual needs and deliver to specific market requirements.

Significant capital expenditure is also required to develop industrial process technology, particularly pilot and demonstration plants, but also costly analytical equipment and laboratory fit-out. For example, Avertana has invested over $3 million to date in its demonstration plant, which is required to show potential licensors and investors that our technology is scalable and to deliver meaningful product samples to specification.

Q7 - Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Avertana's view is that exclusions should not apply to market research, information gathering and pilot or demonstration plant operations.

The technology developed may be of no commercial value if it does not address real and clearly defined market needs, or if it cannot be demonstrated at industrially relevant scale, so that customers and investors can satisfy themselves the process is de-risked.

This is equally true of technologies in other longer lead time sectors such as drug development or medical devices, where pilot scale or prototype manufacture and costly clinical trials are necessary.

Q10 - What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour cost?

We feel that overseas expenditure should be deductible, where it demonstrably contributes to core R&D efforts. Companies that are pushing the boundaries of science and engineering practice very often need call upon specialist international expertise that is not available locally. Offshore expertise is also required to obtain detailed information on opaque, technical markets to develop fit-for-purpose technology successfully.

Costs included should be more than direct R&D labour costs, as the efforts of the entire team are required to ultimately deliver a commercial technology to market.

Q16 - How important is a cap or a mechanism to go beyond the cap? Please provide further details.

From Avertana's perspective, the cap is unlikely to be relevant for many years.

In principle, however, we would argue against imposing a cap, as this may disincentivise New Zealand's largest companies from continuing to grow and promote R&D. We are of the view that R&D is important and of national benefit across the spectrum of company scales, from early-stage start-ups to major corporates. To build a long-term national R&D focus, it is important that a clear and consistent signal is given to the entire market.

Summary

Our company currently has no taxable income to make use of tax credits, nor is this foreseen until a commercial plant is delivered and operating which will take many years. This means tax credits will be of no tangible value to us for in the near to medium term. We are solely focused on R&D of new technology that has a long lead time.

We strongly support the consideration, by April 2019, being proposed to the grant scheme that support business's with tax losses and enable meaningful cash support that can be accessed when these businesses are still at a loss-making pre-revenue stage.

Yours Faithfully,

s 9(2)(a)

Submission by

BusinessNZ

GROWING PROSPERITY AND POTENTIAL

to the

Ministry for Business, Innovation & Employment (MBIE)

on the

Fuelling Innovation to Transform our Economy – A Discussion Paper on a Research and Development Tax Incentive for New Zealand

1 June 2018

s 9(2)(a)
PO Box 1925
Wellington
s 9(2)(a)

FUELLING INNOVATION TO TRANSFORM OUR ECONOMY – A DISCUSSION PAPER ON A RESEARCH AND DEVELOPMENT TAX INCENTIVE FOR NEW ZEALAND
SUBMISSION BY BUSINESSNZ[1]

1.0 INTRODUCTION

1.0 BusinessNZ welcomes the opportunity to make a submission to the Ministry of Business, Innovation and Employment (MBIE) on the Discussion Document *'Fuelling Innovation to Transform our Economy'*, referred to as the 'Discussion Document'.

1.1 On several occasions, including on the introduction of R&D tax credits in 2008, BusinessNZ has submitted to the Government on the use of tax incentives and our fundamental viewpoint has not changed over time. In BusinessNZ's view, there are better mechanisms for assisting the business community to foster greater innovation and investment and improve productivity than introducing R&D tax credits. But assuming such assistance is to be provided, the submission provides comment on the best way to do this while ensuring as little distortion as possible.

2.0 SUMMARY OF RECOMMENDATIONS

2.0 BusinessNZ's **primary recommendation is** for:

(a) ***The Government to lower the company tax rate and/or to reduce the top personal tax rate as the first steps to improving New Zealand's level of research, science and innovation (p.3);***

2.1 Notwithstanding its primary recommendation, if the Government decides to introduce R&D tax credits, BusinessNZ recommends:

(b) ***The transition from growth grants to R&D tax credits involve (a) a rolling over of the growth grants during transition, and (b) an extension of the growth grants out to 31 March 2021 (p.5);***

(c) ***State Owned Enterprises are included in the R&D tax credit regime (p.6);***

(d) ***The R&D tax credits' definition places a greater emphasis on development, with an option for the definition to specifically include the word 'development' (p.7);***

(e) ***The definition of R&D is amended to read '… creating new or improved materials, products, production equipment, devices, processes or services …' (p.7);***

(f) ***Determining eligible expenditure on R&D is based on a broader range of direct and indirect costs (including options for determining appropriate overhead expenditure) (p.8);***

(g) ***The overseas concession for up to 10% of the total cost of the project is increased, if an increase is supported by a majority of other submitters (p.9);***

(h) ***R&D software activities are adequately addressed and recognised in the further work officials are currently undertaking (p.9);***

(i) ***The minimum threshold for research and development spending is aimed towards a figure above $50,000 but below $100,000 (p.10);***

[1] Background information on BusinessNZ is attached as Appendix One.

(j) *The R&D tax credit scheme has a tax credit rate higher than currently, combined with a lower cap (p.11);*

(k) *The option of pre-registration for large R&D spending claims beyond the cap is implemented (p.11);*

(l) *Options relating to transparency proceed if generally supported by the majority of current growth grant recipients (p.11);*

(m) *A comprehensive review and cost-benefit analysis is undertaken within four years of the introduction of R&D tax credits to ascertain their success or otherwise in relation to innovation, investment and productivity in New Zealand (p.12); and*

(n) *The aim of any tax incentive scheme is recognised as being to minimise business compliance and administrative costs (p.13).*

OVERALL IMPRESSIONS AND OBSERVATIONS OF TAX CREDITS

2.2 BusinessNZ's long-held and primary recommendation for any broad review of New Zealand's tax system affecting the business community is for a reduction in tax rates both at a company and personal level. Overall, a tax reduction is the most efficient and broad-based way of enabling all businesses to engage in, and/or experience, increased innovation, investment and productivity.

2.3 According to the Discussion Document, the R&D tax credit scheme will not stand alone. The 2018 Budget announced funding of $1b over four years for the scheme. We assume this will be on top of wider government support for New Zealand research, science and innovation, particularly given some existing R&D grants will continue for the foreseeable future.

2.4 As stated in our previous submissions, our overall view of tax incentives is that, as international evidence clearly shows, they create winners and losers, since certain sectors and businesses are more able than others to make use of such initiatives. BusinessNZ has always taken the view that New Zealand's tax system should remain broad-based and as least distortionary as possible, especially when other options such as cuts in tax rates are also available. Tax incentives can lead to the very 'lolly scramble' approach the Government states in the Discussion Document it does not want to occur.

2.5 Tax incentives of this kind can see business practices changing significantly merely to obtain the tax credit, not from any real desire to undertake the activity to which the tax credit is directed. While we appreciate the Discussion Document is trying to establish boundaries for use, there is still a significant opportunity for the inefficient allocation of resources.

2.6 At the same time, we also recognise any loosening of the definition and eligibility criteria would involve a trade-off between ensuring the eligibility of those who should receive an R&D tax credit and the total fiscal cost to the taxpayer. Despite best intentions, the fiscal cost can be an unknown element and a surprise on the upside if the scheme is at a level where there are few barriers to entry. In addition, there is the opportunity cost for government if the money involved could be used for other purposes.

2.7 The key question is: 'what is the optimal way forward for R&D in New Zealand?' Also, what options would the Government look to introduce instead, given the critical importance R&D can play in boosting economic growth for the country? As discussed below, the R&D tax credit scheme will eventually replace an R&D growth grants scheme which, while obviously not perfect, is generally viewed in a positive light by the business community. Will moving from one scheme to another enhance or inhibit R&D in this country?

2.8 Our primary view is still that government should examine other initiatives through the tax system to broadly assist the business community with investing in research, science and innovation.

Primary Recommendation: That the Government view a drop in the company tax rate and/or a reduction in the top personal tax rate as the immediate first step to improving New Zealand's level of research, science and innovation.

2.9 Notwithstanding our primary view that a tax incentive approach should not be adopted, we wish to provide comment on certain issues we feel would at least minimise any negative consequences of what is proposed.

R&D Grants

2.10 As outlined in the Discussion Document, the R&D tax credit will not stand alone. After stopping the R&D tax credit scheme in 2008, the previous Government introduced the R&D grant system, which in its current form is summarised below in table 1.

Table 1: Existing R&D Grants

Type of R&D Grant	Eligible	Restrictions
Getting Started Grants	• Only receive funding for R&D done in New Zealand • Receive a one-off payment on completion of the project.	• Receive 40% of eligible R&D project costs, up to $5,000 (based on a quotation).
Project Grants	• Typically receive 40% of eligible R&D project costs; reducing for large projects, or when the business has had multiple grants, or when the business has had a Growth Grant. • Only receive funding for R&D done in New Zealand (unless pre-approved) • Receive payment in arrears (monthly or quarterly).	• 40% funding for the first $800,000 of eligible R&D, then 20% for the remainder, or • If previous Growth Grant then flat 20% funding, or • If business has had more than $800,000 of R&D Project funding then flat 20% funding applies.
Growth Grants	• Have spent at least $300,000 per annum and 1.5% of revenue on eligible R&D in each of the last two years; OR plan to exceed these levels over the next year (transitional application) • Receive a two year extension after three years, subject to having met annual review requirements.	• Receive 20% of eligible R&D expenditure, up to $5m per annum.
R&D Experience Gants	• Have an active R&D programme i.e. a R&D budget and R&D staff.	• Receive funding of $7,200 (plus GST) for 400 hours of full-time work upon proof of your payment to the student.
R&D Career Grants	• Receive the first six months of the student's annual salary costs up to: o $30,000 (plus GST) for a masters graduate (based on annual salary of $60,000) o $35,000 (plus GST) for a PhD graduate (based on an annual salary of $70,000)	
R&D Fellowship Grants	• Business and the university supervisor will jointly supervise the student's research project, and the research is undertaken at both sites. • Depending on the length of time for the student to complete their qualification, qualifying businesses will receive: o PhD – maximum payments (36 months duration) ▪ Stipend $75,000 (GST exempt) ▪ Travel allowance $2,666 (excluding GST) ▪ University host fee $13,333 (excluding GST) o Masters – maximum payments (12 months duration) ▪ Stipend $20,000 (GST exempt) ▪ Travel allowance $888 (excluding GST) ▪ University host fee $4,444 (excluding GST) • R&D Fellowship Grant students receive a stipend and travel allowance and a fee is paid to the university to support their role in the scheme	

2.11 Although not perfect, the general view of businesses that have gone through the process and received a growth grant is that the scheme has worked well. It has been fairly simple to use both for applying and complying, while supporting cash flow and facilitating innovation, particularly in the early stages. There has also been a greater level of certainty, particularly as once pre-approval has been given, the focus then can be both on research and development. Last, the grant schemes - particularly the growth grant – have led businesses to undertake projects they would not otherwise have undertaken. Therefore, a number of members have asked *'if it's not broken, why fix it?'* .

Transitioning from Growth Grants to the R&D Tax Incentive

2.12 As well as the R&D Discussion Document, we note the Government has also released a Discussion Document entitled *'Managing the Transition from Growth Grants to the R&D Tax Incentive'*. While BusinessNZ does not intend to submit on that Document, we note that those who currently receive growth grants will be able to do so until 31 March 2020. Current growth grant recipients have the option of transitioning to the R&D tax credit scheme from 1 April 2019, with 31 March 2019 the closing date for any new growth grant applications and extensions to existing growth grant contracts. The rationale behind this phasing out, is that the Government will be funding similar types of activity through the R&D tax credit, which they view as having a similar purpose. To the best of our knowledge, we have not seen any indication from the Government that any other types of R&D grants will be phased out, although this is obviously possible given the shifting nature of policy development.

2.13 While R&D growth grant recipients will eventually transition to the R&D tax credit scheme, our members have noted two critical concerns:

- Overall, companies currently receiving the growth grant will most likely receive less money, making them less likely to innovate, and
- The transition period from the growth grant to the tax credit will create business uncertainty.

2.14 A broadening of the scope for what is classified as R&D expenditure would assist with the first concern (discussed in more detail below) while rolling over the growth grants during transition and extending the growth grants out to 31 March 2021 would assist with reducing uncertainty.

Recommendation: That the transition from growth grants to R&D tax credits involve (a) a rolling over of the growth grants during transition, and (b) an extension of the growth grants out to 31 March 2021.

Rate of the R&D Tax Credit Scheme

2.15 The Discussion Document states the R&D tax credit will be set at 12.5%. This is below the 15% rate previously introduced under the 2008 tax credit scheme and lower than the 20% growth grant (14.4% after tax) over the last four years. A relatively low 12.5% does not seem consistent with the aspirational goals outlined in the Discussion Document.

2.16 While we understand the risk of total fiscal cost has seen the Government err on the side of caution by way of setting a lower tax credit rate than previously, obviously existing growth grant users will receive a lesser amount. Also, the lower the rate the lower the probability of a business applying for a tax credit given both actual costs and opportunity costs need to be taken into account. Much like the corporate tax rate, the rate for the R&D tax credit scheme sends an upfront signal to the global market about how seriously investment into innovation and technology is regarded, especially if a primary aim is to drive multi-nationals to shift R&D activities to New Zealand.

2.17 As we will discuss in response to question 16 below, there is an inverse relationship between the rate of the R&D tax credit and a cap on the amount a business can claim each year.

3.0 SPECIFIC DISCUSSION DOCUMENT QUESTIONS

3.0 The Discussion Document has asked a series of questions relating to the introduction of an R&D tax credit. We would like to take the opportunity to comment on some of these questions.

Question 1: If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the tax incentive, what will the likely impact be on business R&D in New Zealand?

3.1 BusinessNZ agrees that Crown Research Institutes, District Health Boards, Tertiary Institutions and their subsidiaries should be excluded from the R&D tax incentive which should, however, be available to all businesses regardless of their legal structure. Any attempt to restrict particular entities would lead to restructuring if an R&D tax incentive were to be claimed and would place further unnecessary compliance and administrative costs on the business in question.

3.2 But BusinessNZ questions the exclusion of State Owned Enterprises (SOEs) from the tax incentive scheme. SOEs have the principal objective of operating as successful businesses. All SOEs are registered as public companies and are bound by the provisions of the Companies Act. Most SOEs operate in deregulated markets and are on equal terms with the private sector. Given the current list includes a variety of industries, including telecommunications, postal services, banking, railways, electricity and broadcasting, exclusion would effectively result in an uneven playing field compared with fully private sector competitors. At the same time, we would expect the Government to monitor the use of R&D tax credits by SOEs to ensure the pool of funds is not all but drained away from private sector businesses.

3.3 Overall, since the objective of R&D tax credits is to achieve an ambitious R&D target that will see a step change in New Zealand's approach to innovation, BusinessNZ believes there is good reason to make the R&D tax credit available to SOEs.

Recommendation: That State Owned Enterprises are included for the R&D tax credit regime.

Question 2: How well does this definition apply to business R&D carried out in New Zealand?
Question 3: Does this definition exclude R&D that you think should be eligible, please illustrate with examples.
Question 4: Does the scientific method requirement exclude valid R&D in some sectors? Please illustrate with examples.
Question 5: What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?
Question 6: How well does this definition apply to business R&D carried out in New Zealand?

3.4 The key to any definition, particularly in relation to R&D, is that it is easily understood by those applying for the credit, has few loopholes and yet is broad enough to capture those at whom the scheme is aimed. In short, a balancing act is required to satisfy both administrators and recipients.

3.5 We are pleased to see the Government has taken the opportunity to investigate definitions for tax incentive provisions based on international best practice. There are countries that are similar to New Zealand in various respects and have success stories (including software) around which to draw on for any R&D incentive approach introduced to New Zealand.

3.6 The Discussion Document states the current definition of R&D used in the R&D grant system and for income tax deductibility, based on the New Zealand equivalent to International Accounting Standard 38 (NZIAS 38), is not considered suitable. This means any new definition on top of the one used for R&D grants is likely to create significant compliance and administration costs, especially as the existing definition is simpler to use for taxpayers already familiar with it for accounting purposes.

3.7 Regarding the definition now proposed for R&D tax credits, we note that the 2007 Act defined R&D as:

1. *Systematic, investigative and experimental activities (SIE) that are performed for the purposes of acquiring new knowledge or creating new or improved materials, products, devices, processes or services and that:*

    - *are intended to advance science or technology through the resolution of scientific or technological uncertainty;*

      or

- *involve an appreciable element of novelty.*

2. *Other activities that are wholly or mainly for the purpose of, required for, and integral to, the carrying on of the activities in paragraph (a).*

3.8 The new definition of R&D (below) is in many ways very similar to the definition used in 2007:

(a) Core activities: those conducted using scientific methods that are performed for the purposes of acquiring new knowledge or creating new or improved materials, products, devices, processes, or services; and that are intended to advance science or technology through the resolution of scientific or technological uncertainty.

OR

(b) Support activities: those that are wholly or mainly for the purpose of, required for, and integral to, the performing of the activities referred to in paragraph (a).

3.9 Despite the similarities between the 2007 and the new definitions, BusinessNZ members who receive the current R&D grants and/or would look to apply for the R&D tax credit scheme generally agree the tax credit eligibility criteria are too greatly weighted toward 'R', rather than 'D'. Some even see the scheme as an 'R' only scheme. The problem with the imbalance between the scheme's two key aspects is that businesses predominantly spend money on 'D' than 'R'. As one member has pointed out:

'Businesses create economic value by developing innovative solutions to solve customer problems. There is inherent risk in the development and commercialisation and the R&D growth grants has helped business to increase their risk appetite. The R&D tax credit scheme will lead to business taking less risk'.

Therefore, we are concerned that if the current definition is introduced, the ability for many businesses to apply for and succeed in getting the R&D tax credit will be greatly affected.

3.10 Also, this limitation will be even more evident when smaller businesses are considered. While larger businesses will have some capacity to undertake research, in reality this is far less likely for SMEs. The financial costs that represent a larger proportion of their total capital mean SMEs, typically, do not focus on research.

3.11 As a first step to address this imbalance, we believe the definition requires a greater emphasis on 'development'. While we have no strong views as to the exact wording that would largely rectify this problem, a positive start would be to include the word 'development' in the definition.

Recommendation: That the definition for R&D tax credits places a greater emphasis on development, with the definition specifically including the word 'development'.

3.12 One other aspect of the definition we believe needs addressing relates to production equipment. During the Bill stage in 2007, BusinessNZ requested (1) to read '... *creating new or improved materials, products,* ***production equipment****, devices, processes or services* ...'. This was because the creation of production equipment is fundamental for some in terms of creating new product, and including that term would help clarify the definition for those applying for an R&D credit.

3.13 Therefore, BusinessNZ again recommends that sentence (a) of the definition read '... creating new or improved materials, products, **production equipment**, devices, processes, or services ...'.

Recommendation: That the definition of R&D read '(a) ... creating new or improved materials, products, production equipment, devices, processes or services ... '.

Question 7: Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

3.14 In addition to discussing the specific issue of dual purpose activities in question 9 below, the only other point we wish to raise is that it needs to be made clearer to the business community that the excluded activities obviously do not reach the threshold for the R&D tax credit scheme (are not core

activities). However, as support activities (part (b) of the definition) there is a higher likelihood they would be included. But many businesses will simply see the excluded list and automatically assume it applies to the entire definition.

Question 8: Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

3.15 On balance, in most instances we believe research on social sciences, arts or humanities should not be included as part of R&D incentives. While we support research into these areas, we believe this will not bring about the level of innovation, investment and productivity the Government is seeking. Research in these fields is often more a by-product of an economy that has already developed a sound infrastructure, and shows strong economic growth.

3.16 However, an exception to this could be where social science research activities are aimed at informing other R&D initiatives, such as a better understanding of the social implications for new products that improve peoples lives.

Question 9: What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive?

3.17 While BusinessNZ appreciates the stance taken regarding dual purpose activities – namely an R&D tax credit would be better targeted if it applies to an activity conducted solely for an R&D purpose – we strongly urge caution. In almost all situations, a business will undertake R&D for the purpose of making income as businesses are generally not narrowly defined by research activity. They have, continuously, to be sufficiently nimble to look for opportunities in the market where R&D is undertaken with the end purpose of commercialising the work. Therefore, to apply the tax incentive solely to R&D purposes without recognising the associated purpose of commercialisation would inhibit almost all businesses from applying. For instance, it is common practice in certain industries to de-risk the commercialization aspect of R&D by pre-selling where possible to recoup part of the cost soon after completion.

Question 10: What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour cost?

3.18 Of the two approaches that are outlined for determining eligible expenditure, BusinessNZ strongly prefers the second approach whereby it is based on a broader range of direct and indirect costs (including options for determining appropriate overhead expenditure). While the labour cost method may be simpler, it would not maximise the potential of the regime to raise R&D expenditure and therefore reaching the goal towards 2% of GDP.

Recommendation: That determining eligible expenditure on R&D is based on a broader range of direct and indirect costs (including options for determining appropriate overhead expenditure).

3.19 In principle, BusinessNZ agrees R&D costs incurred overseas should be eligible for the concession up to a certain percentage of the total cost of the project if the overseas work is part of an R&D project based in New Zealand and at least half the R&D project expenditure is for activities carried out in New Zealand. We view this as a pragmatic outcome and in 2007 we supported a similar stance particularly as it would be idealistic to think New Zealand can do everything as there will always be areas where New Zealand lacks the skills and/or capability. As the paper notes, New Zealand might not have complete capability to do the work locally, so foreign R&D jurisdiction requirements might have to be observed and the customisation of a product for a particular market take place in that market.

3.20 However, a key question is whether the 10% percentage value outlined in the Discussion Document is realistic enough in today's global environment? While we do not want a situation where almost all R&D is done offshore, at the same time we do not want to see missed opportunities because of the restrictive nature of the 10% limit creating some form of silo mentality when it comes to R&D activity in New Zealand. In addition, the Government needs to be mindful of situations where none of the Crown Research Institutes or New Zealand tertiary institutions have sufficient expertise in specific R&D areas, which would mean offshore options become a key focus.

3.21 Therefore, if other submitters provide sufficient practical reasons why the limit should be greater than 10%, we have no significant concerns about an increased percentage.

Recommendation: That the overseas concession for up to 10% of the total cost of the project is accepted, subject to an increase if an increase is supported by a majority of submitters.

3.22 The section on eligible expenditure lists a variety of business expenditure the Government believes should attract the R&D tax credit. While we have no particular comments on the list provided, we want to touch on the broader issue of the administrative and compliance elements involved in ensuring businesses understand exactly what is and is not regarded as eligible expenditure.

3.23 Establishing the boundaries of eligible expenditure for tax incentives has the potential to end up an administrative nightmare for some businesses, taking up a considerable amount of a business's time and resources. If boundaries are not clearly defined, this may well deter many businesses from even considering an application. Businesses already see tax compliance costs as the largest priority for the day-to-day running of their firm. A tax incentive approach causing confusion and administrative headaches will only exacerbate the problem.

3.24 Therefore, the clearer the Government can be about exactly what is or is not considered R&D expenditure, preferably by way of a comprehensive list in any guidance material (discussed in question 21 below), the less time and resource businesses will have to spend on 'grey' expenditure areas.

Question 11: What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? What would the appropriate percentage be?

3.25 Overall, BusinessNZ believes there should not be limits on overhead costs as long as reasonable apportionment is undertaken. However, we would not be adverse to the idea of some form of pre-approved percentage of overhead costs if supported by most other submitters.

3.26 As discussed below, any guidance material around this needs to clearly outline what would be included as overhead costs so as to reduce uncertainty and ensure that the right resources are allocated effectively and efficiently.

Question 12: Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.
Question 13: What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

3.27 BusinessNZ agrees software R&D has become increasingly important in our economy. The fact that it has accounted for approximately 40-50 percent of the value of grants in the last three years is testament to this. Also, we would presume the level and depth of R&D software activities has grown exponentially since New Zealand last had an R&D tax credit ten years ago.

3.28 We are pleased to note the Discussion Document mentions officials currently undertaking additional work to see how the R&D definition should apply to software. However, we are concerned the definition of R&D tax credits is very similar to the one used in 2008 and general feedback from members was that many struggled to meet the 2008 tax credit definition when it came to software. Therefore, unless there is a meaningful discussion on ensuring the barriers to including software are at an appropriate level (such as opening the definition up to the novelty aspect for software), there is a high likelihood that in many instances software activities will be excluded.

Recommendation: That R&D software activities are adequately addressed and recognised in the further work currently being undertaken by officials.

Question 14: Are there reasons why continuity rules should not apply to tax credits? Please describe.

3.29 BusinessNZ has been formally collaborating with a number of interested business groups on the question of whether continuity should be imposed on R&D tax credits carried forward, advocating for

a change to New Zealand's loss continuity rules. We would like to see an amendment to a law that currently disadvantages many fast growing and innovative companies. Specifically, the proposal is to amend the current rule relating to the carry forward of tax losses by enacting a 'same or similar business' test as an alternative to the existing 49% continuity of ownership requirement. This would bring New Zealand's rules into line with those of many comparable jurisdictions, reduce compliance costs, and further the potential for business growth.

3.30 To that end, IRD officials have already undertaken work on both the substantive proposal and on possible implementation costs. A focus on the requirements for the carry-forward of tax credits further recognises the potential unfairness of a continuity of ownership structure.

Question 15: Is the minimum threshold set at the right level? If 'no', please provide further details.

3.31 As a background, BusinessNZ notes the 2008 legislation set the minimum threshold for receiving the R&D tax credit at $20,000. At that time, the then Government indicated the amount was equivalent to a part-time salary and some related overhead costs.

3.32 The new threshold is $100,000, the rationale being to filter out claims unlikely to be for genuine R&D. This is roughly the cost of one full-time employee's salary plus related overhead costs.

3.33 First, as mentioned in 2007, BusinessNZ has no firm view on whether the above figure is appropriate, although we are disappointed the paper lacks any summary showing other countries' minimum thresholds, including the threshold that creates a balance between ensuring the exclusion of questionable R&D and attracting genuine R&D work.

3.34 Second, in New Zealand's case the minimum threshold is not only influenced by a monetary value applying to general costs but also by the thresholds employed by the R&D growth grants. Table 1 (above) shows the closest generic grant above the R&D tax credit value as the growth grant (minimum $300,000 spent on eligible expenditure), while the closest grant below the R&D tax credit value is the getting started grant (40% of eligible R&D project costs, up to $5,000). One could argue that at $100,000, the R&D tax credit sits somewhat in the middle but whether that figure is a bridge too far for many smaller businesses who undertake legitimate R&D work is a key point.

3.35 Given the Discussion Document states the '*proposed R&D Tax Incentive has been designed to provide easily accessible support to a broad range of businesses, and to do so in a fiscally responsible way*', we question whether the increase from $20,000 in 2008 to $100,000 in 2018 meets the accessibility target for smaller businesses. After discussions with members, the most practical monetary threshold is considered to be above $50,000 but certainly below $100,000.

Recommendation: That the minimum threshold of research and development spending is aimed at a figure above $50,000 but below $100,000.

Question 16: How important is a cap or a mechanism to go beyond the cap? Please provide further details.

3.36 As we briefly mentioned in our section on the R&D tax credit rate above, there appears to be an inverse relationship between the R&D tax credit rate and the cap on the amount a business can claim each year.

3.37 According to the Discussion Document, a business will be able to claim a tax credit of up to $120 million of R&D expenditure each year, equating to a tax credit of $15 million each year (based on the 12.5% rate). First, we understand the need for a cap. Given the wider implications for government expenditure, some line in the sand has to be drawn to ensure the total fiscal cost of the R&D tax credit scheme does not balloon out beyond the $1 billion allocated over the next four years. If that happened, there would have to be trade-offs with other areas of government expenditure. This might not only cause problems with the Government's policy programme but could also cast the business community in a less than satisfactory light given the possibility of forsaking expenditure in other areas deemed important by society in general.

3.38 Realistically, BusinessNZ would doubt whether many businesses would get near to $120 million R&D expenditure per year. Therefore, to ensure the three-pronged desirability of minimising exploitation, setting a rate which encourages legitimate R&D expenditure but provides a cap for larger business

claims, a trade-off between a higher rate/lower cap or a lower rate/higher cap is required. Combined with what we outline in question 17 below, BusinessNZ would be more in favour of a higher rate/lower cap so more businesses are able to apply.

Recommendation: That the R&D tax credit scheme looks to have a higher tax credit rate combined with a lower cap.

Question 17: What features of a Ministerial discretion or pre-registration would make them most effective?

3.39 Generally speaking, BusinessNZ is in favour of a cap on how much a business can claim each year, and we agree with the Discussion Document's reasoning that this would protect against the exploitation of loopholes which could create shocks to the cost of the scheme and reduce its sustainability.

3.40 However, we acknowledge a cap can reduce genuine large claims and this should be factored in when considering that New Zealand's largest R&D performers should be encouraged to increase their R&D and large, international R&D intensive firms encouraged to come to New Zealand.

3.41 Beyond the issue of needing to introduce a cap, the Discussion Document outlines two possible ways to incentivise spending on R&D above the level of the cap, either:

1. By having a Ministerial discretion to waive the cap for genuine claims; or
2. Requiring pre-registration for large claims.

3.42 While we accept both options have advantages and disadvantages, we would favour the pre-registration option. Of the two, this option provides greater certainty for business. Also, we see potential pitfalls with the first option as it operates on a case-by-case basis and, in particular, allows the Minister a direct say on when the cap on claims will be waived. At worst, this could lead to political interference.

Recommendation: That the option to require pre-registration of large claims for R&D spending is implemented.

Question 18: What are your views on the proposed mechanisms to promote transparency and enhance evaluation?

Transparency

3.43 While the standard approach to taxpayer-specific information is for secrecy provisions to apply, the Discussion Document proposes that where substantial government funds are allocated through the R&D tax credit, the Government should consider an alternative approach. Transparency would assist in maintaining the integrity of the scheme. This would range from publishing the names of recipients and the amounts of R&D support (expressed in bands with a two-year lag), making taxpayer-specific information relating to R&D tax credit claims available to certain government departments, and integrating the data with Stats NZ's Longitudinal Business Database.

3.44 Overall, BusinessNZ does not have significant concerns with the transparency proposal. However, we note that R&D growth grant recipients are not published, so growth grant recipients moving to the R&D tax credit scheme would obviously see a change in process. We would be concerned if because of the change, many growth grant recipients decided not to move to the R&D tax credit scheme.

3.45 Broadly, we agree that in order to protect commercially sensitive information, a two-year lag before publishing the names of R&D tax credit recipients is a practical step. However, we would not be averse to an extension of the timeframe if realistically, other submitters find the two-year frame too short.

Recommendation: That options relating to transparency proceed if generally supported by the majority of current growth grant recipients.

Evaluation

3.46 BusinessNZ strongly agrees that following the transition from growth grants, the R&D tax credit scheme should be evaluated within four years of commencement. The R&D grant scheme underwent an extensive review, so reviewing the R&D tax credit scheme would be consistent with existing practice.

3.47 The review should seek to ascertain whether there has been any meaningful increase in innovation, investment and productivity on a national basis due to the tax incentives' introduction. The review should involve a comprehensive cost-benefit analysis and recommend whether the incentives should continue.

3.48 How businesses self-select R&D expenditure when completing StatisticsNZ surveys could also be an issue associated with the proposed change in the definition of R&D. With the success or otherwise of the R&D tax credit scheme largely dependent on seeing a genuine increase in gross R&D expenditure as a percentage of GDP, incorrect official survey measurements could hamper further policy development.

Recommendation: That a comprehensive review and cost-benefit analysis is undertaken within four years of the introduction of R&D tax credits to ascertain their success or otherwise in promoting innovation and investment and increasing New Zealand's productivity.

Question 19: Are there any other risks that need to be managed? Please describe.

3.49 As outlined above, the key risk for any R&D tax credit scheme is getting the correct balance between ensuring taxpayer money is correctly targeted towards genuine R&D expenditure, while ensuring any R&D tax credit thresholds are not so constrained as to deter worthwhile businesses from applying for a credit so that the scheme is underutilised.

Question 20: Are there risks with extending penalties to external advisors in this way?

3.50 The Discussion Document states that '*The standard penalties provisions in the Tax Administration Act 1994 would apply to R&D Tax Incentive claims*'. There is also consideration around the idea that '*penalties should be extended where a tax advisor has, or would have, received a direct financial benefit from the claim and the R&D Tax Credit application demonstrates a serious offence*'.

3.51 BusinessNZ does not have a strong view on this matter but would like to point out that if penalties are too heavy handed, this could have an adverse effect on SME applications given the high perceived risk. As mentioned above, the current growth grants require a pre-approval process easing a number of concerns applicants have about possible penalties. Taxpayer funds should be allocated correctly and standard penalties are likely to be needed to ensure consistency across tax policy implementation. However, there is scope for investigating whether concerns over potential penalties could be allayed via some form of auditing process, perhaps undertaken by Callaghan Innovation. This could be part of the investigative work into the second wave of the R&D tax credit scheme post the winding up of growth grants.

3.52 Also, the issue of potential penalties plays out in relation to the accompanying material available to applicants, discussed below.

Question 21: What is the right level of information required to support a claim?
Question 22: What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

3.53 Overall, BusinessNZ supports the initial features of the claims' process under consideration. These range from the use of the MyIR portal, through to the ability of businesses in the future to use third party software to enable records to be kept, ensuring R&D expenditure is correctly characterised.

3.54 One feature of the claim's process BusinessNZ considers especially important relates to the range of guidance and education material (including online tools) to assist claimants. The R&D tax credit guide, on which we commented in 2007/2008, is especially important for the business community.

3.55 First, a guide should be a guide, not a 'locked-in' definitive publication requiring modification or additions over the short to medium term. While the first publicly released guide should be as accurate

as possible, there will most likely be further additions as R&D tax credit issues, perhaps unique to New Zealand, evolve.

3.56 Second, as with the scheme itself, the guide should not be overly prescriptive in its interpretations. IRD generally takes a self-assessment approach to taxation with taxpayers responsible for calculating their own tax obligations, paying the tax to the IRD and filing tax returns. Although the self-assessment regime is buttressed by audit activity, generally the regulatory approach IRD favours facilitates good outcomes compared with prescribing a set way of doing things.

3.57 In 2008, we found the guide's first draft bordered on the prescriptive in its approach requiring considerable planning and record-keeping in order to tell the IRD of actual R&D expenditure incurred. While the guide discussed the role of self-assessment in relation to record-keeping responsibilities, the assessment requirements were high. Obviously, we did not want businesses allocating expenses that were not R&D but the considerable record-keeping provisions created significant compliance costs of which businesses needed to be aware upfront. We did not want businesses to find the prescriptive requirements so high that any decision to apply for a grant was put in doubt. Therefore the full implications of the record keeping and other requirements should be made clear at the front of the guide so businesses were aware of their obligations.

3.58 Third, while the initial guide provided examples throughout that attempted to explain the guidelines' practical outcomes, we also considered there was scope for a 'next level' of examples, going beyond the often simple examples provided in the draft. While all examples had a disclaimer explaining they were simple and applicants should check the guide itself or consult a professional, some more complex examples would help explain the procedure more clearly.

Question 23: What integrity measures do you think Inland Revenue should use?

3.59 BusinessNZ will be taking a keen interest in the success of the R&D tax credits system in improving the country's level of R&D. We hope the scheme will lead to businesses taking a more proactive part, giving strategic consideration to the role played by R&D plays in their further expansion.

3.60 We would also expect IRD to accept rather than reject applications which are on the margin for being classified as R&D expenditure. As mentioned above, BusinessNZ would want to ensure R&D tax credits are provided for legitimate purposes. However, there is a point at which the threshold becomes so difficult to reach, no-one applies and R&D tax credits are underutilised (i.e. there is disuse of the credit from fears of misuse). While IRD might be taking an initially conservative stance to ensure allocated funds are not soaked up by doubtful R&D expenditure, a consistent decline in applications could inhibit businesses' future use of the tax credits. With the time and effort required for the application process, businesses could perceive their chances as low and an application most probably a waste of business resources.

Recommendation: That the process for any tax incentive scheme aims to minimise business compliance and administrative costs.

Appendix One - Background information on BusinessNZ

BusinessNZ is New Zealand's largest business advocacy body, representing:

- Regional business groups EMA, Business Central, Canterbury Employers' Chamber of Commerce, and Employers Otago Southland
- Major Companies Group of New Zealand's largest businesses
- Gold Group of medium sized businesses
- Affiliated Industries Group of national industry associations
- ExportNZ representing New Zealand exporting enterprises
- ManufacturingNZ representing New Zealand manufacturing enterprises
- Sustainable Business Council of enterprises leading sustainable business practice
- BusinessNZ Energy Council of enterprises leading sustainable energy production and use
- Buy NZ Made representing producers, retailers and consumers of New Zealand-made goods

BusinessNZ is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy and services for enterprise, BusinessNZ contributes to Government, tripartite working parties and international bodies including the International Labour Organisation (ILO), the International Organisation of Employers (IOE) and the Business and Industry Advisory Council (BIAC) to the Organisation for Economic Cooperation and Development (OECD).

Joint Feedback and Recommendations from the University of Auckland and Auckland UniServices Limited on the discussion document

'Fuelling Innovation to Transform our Economy'

s 9(2)(a)
[redacted]
www.uniservices.co.nz

s 9(2)(a)
[redacted]
www.auckland.ac.nz

Recommendations for a Research and Development Tax Incentive

1. Executive Summary

The University of Auckland and Auckland UniServices Ltd would like to thank the Ministry for Business, Innovation and Employment (MBIE) for the opportunity to provide feedback on the Research and Development (R&D) Tax Incentive. We congratulate the Government on what we see as a transparent and robust policy to support both large scale and small and medium size enterprises (SMEs) in New Zealand.

In general we support the shift to a tax credit regime, however we feel that further policy work needs to be undertaken to look at mechanisms which will encourage R&D activity by SMEs, acknowledging their significant contribution to the New Zealand economy. It is our view that the system must work effectively for SMEs as they dominate the innovation economy of New Zealand. New Zealand is unusual in that it lacks large businesses of sufficient size undertake research at scale or have the absorptive capacity to effectively work with research providers. When measured by co-publication (a measure of deep partnership in knowledge generation), there are only two New Zealand companies in the top 20 corporates with whom we work.

We support a new R&D tax incentive that accommodates companies in their "burn phase" such as start-ups or spin-outs where R&D expenditure typically peaks as a proportion of turnover, but the company is not in profit.

We would welcome mechanisms to optimise participation of some of the biggest spenders and supporters of research activity including those with a for profit mandate - particularly SOEs and CRIs – and the not-for- profit sector including Universities and District Health Boards (DHBs). A number of these institutions are significant investors in R&D ventures of the type described as core activities in the discussion paper. Including these institutions in the tax incentive scheme will have a positive impact on business R&D in New Zealand, for example, DHBs, who have the 'carrying out of research' in their mandate, might be incentivised to participate more fully.

We would welcome the opportunity to discuss our feedback and ideas further with Government.

We have summarised key recommendations below. Section 3 'Discussion' contains a more detailed response to the questions provided by MBIE in the discussion paper.

Summary of Recommendations

- We recommend that Government reconsider the exclusion of SOEs and Crown Research Institutes (CRIs), which have profit mandate requirements. *(Q1)*
- We recommend that Government investigates mechanisms to enable DHBs, Tertiary Institutions, and their subsidiaries to participate to their fullest capacity in the research ecosystem i.e. that they are not dis-incentivised to work alongside New Zealand business and industry to grow research as a percentage of GDP. *(Q1)*
- We recommend changing the 'and' following 'or services;' to read '**or** that are intended to advance science' in the definition of R&D. *(Q2)*
- We recommend the Government avoids applying a materiality test in respect of the problem, however we believe a materiality test related to the advancement of science and technology is warranted. *(Q5)*

- We recommend that commercial, legal and administrative aspects of patenting that are undertaken in respect of activities that are otherwise eligible under this policy be included in the eligibility criteria as a legitimate R&D expense/cost to business. *(Q7)*
- We support a brightline test as part of the tax rules that make dual purpose activities ineligible under the implementation of any tax credit regime and recommend the Government includes this in tax regulations to maximise investment in truly innovative activity. *(Q9)*
- We recommend that the Government considers both direct and indirect labour costs as part of the implementation of this policy. *(Q10 and 11)*
- We recommend that the Government calculates overhead costs as a set percentage of the direct labour costs for the R&D activity. *(Q10 and 11)*
- We recommend that the shareholder continuity rules do not apply. *(Q14)*
- We recommend that Callaghan Innovation be excluded from the list of Government entities able to access tax-payer specific information. *(Q18)*
- We recommend that the Government, through MBIE or the Inland Revenue Department (IRD), undertake to provide collateral and training to existing research providers to enable them to promote and support New Zealand business to better access the R&D tax credit. *(Q20 &21)*
- We recommend that the 10% eligibility limit on overseas spend is increased to 20 - 25%.

2. Introduction

The University of Auckland (UoA) is the largest university in New Zealand, hosting over 40,000 students on five Auckland campuses. The UoA has a budget of over $1B dollars and had a surplus of $64m in 2017. Most recently, the University launched 'For all our futures', a campaign to provide the funding and support we need to have a lasting impact on the challenges and opportunities faced in a complex and rapidly changing world.

The UoA aspires to be "A research-led, international university, recognised for excellence in teaching, learning, research, creative work, and administration, and for the significance of its contributions to the advancement of knowledge and its commitment to serve its local, national and international communities."

The values of the University reflect a commitment to:

- Conserving, advancing and disseminating knowledge through teaching, learning, research and creative work of the highest standard.
- Creating a diverse, collegial scholarly community in which individuals are valued and respected, academic freedom is exercised with intellectual rigor and high ethical standards; and critical enquiry is encouraged.
- Placing a strong emphasis on serving our student body.
- Working to advance the intellectual, cultural, environmental, economic and social well-being of the peoples of Auckland and New Zealand.
- Recognising a special relationship with Māori under the Treaty of Waitangi.
- Providing equal opportunities to all who have the potential to succeed in a university of high international standing.
- Engaging with national and international scholars, educational and research institutions to enhance intellectual development, educational quality and research productivity.

- The development and commercialisation of enterprise based on its research and creative works.
- Providing high quality management marked by open, transparent, responsive, and accountable academic and administrative policies, practices and services.

Auckland UniServices Ltd (AUL) is dedicated to connecting the UoA capabilities to business, investors, Government and the community and is the largest R&D Company of its kind in Australasia.

AUL is a wholly-owned company of the UoA. In 30 years the company has grown exponentially and has revenues of between $110m and $127 million per annum, far surpassing any similar organisation in New Zealand or Australia. AUL is currently working on 1,200 projects with more than 300 New Zealand firms. In 2016, AUL generated revenues of $114 million, over 50 licenses for intellectual property and created more than 11 businesses to commercialise University research.

AUL is a not for profit company, all surpluses generated are paid to the UoA and applied to expanding and enhancing the University's capabilities in commercial and basic research. AUL and the UoA have been identified by the Massachusetts Institute of Technology - Skoltech Initiative Report as one of the top five 'emerging leaders in entrepreneurship' from around the world expected to become major international entrepreneurial and innovation powerhouses in the decades ahead. The report notes "the University of Auckland offers an exciting blueprint for other universities operating in similar circumstances across the world". MBIE have noted that "Auckland UniServices Limited is very successful at contracting research and transferring intellectual property from the University of Auckland to the public and private sectors, and is an exemplar of how research organisations and businesses partner together to achieve mutual benefit". Working with the UoA, AUL has:

AUL's mission is to bring ideas to life. This is achieved by partnering with the best minds in the University and business to apply intelligent thinking to ideas that have the potential to change the world.

Together with partners, AUL looks to the future, imagines the possibilities, and innovates for public and private good with a strong focus on commercial success.

3. Discussion

Following an in-house workshop and consideration by our Leadership Group we are pleased to provide feedback to MBIE, the Minister of Research Science and Innovation and the Minister of Revenue.

As a company that is intimately involved with R&D at all levels and/or stages of the R&D pipeline we support the Government's commitment to increasing R&D expenditure to two percent of Gross Domestic Product (GDP) by 2027. We note that business needs certainty to invest in R&D; we are of the view that Government is not best placed to 'pick winners'. We believe that R&D tax credits provide a more democratic, transparent and flexible mechanism to support R&D in New Zealand in a way that research grants to industry do not.

To achieve the Government's goals we believe that the mechanisms to support the administration of an R&D tax credit should be simple and easy to complete. Additionally we recommend that the Government work with accredited research providers and industry bodies to provide advice and support to New Zealand business and industry to maximise the benefits of the tax credit system.

We have used the question framework provided in the discussion paper to guide our response. In some cases we do not have specific comments to make. We end our response with several concluding points based on our expertise in the R&D ecosystem.

While we acknowledge the complexity involved in the introduction of a new tax credit system we have endeavoured to limit our responses to each question to enable ease of analysis while communicating key messages.

Q1: If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the tax incentive, what will the likely impact be on business R&D in New Zealand?

Much of the world class research that is currently undertaken in New Zealand is a direct consequence of the contribution of SOEs, Crown Research Institutes, District Health Boards (DHBs), Tertiary Institutions, and their subsidiaries. The vast bulk of the research expertise within the country resides in these institutions. According to MBIE 97% of New Zealand's businesses are small to medium enterprises of 20 employees or less therefore large institutions represent research scale not possible in smaller enterprises. It is our view that Government should reconsider the exclusion of SOEs and Crown Research Institutes (CRIs), which have profit mandate requirements.

By way of example, despite current debates around the level of funding to District Health Boards, the New Zealand Health System is a world class asset. A feature of any system that provides high quality healthcare is the degree to which research informs the delivery of services to their populations. New Zealand has the ability to leverage off this asset through research to support investment in the wider health ecosystem. As such DHBs should not be dis-incentivised from engaging and supporting research activities, rather they should be supported to contribute and partner with the private sector to grow research. A similar argument could also be made for the New Zealand Education system.

The discussion paper does not mention non-tax paying entities such as NGOs, Local Government, Council-Controlled Organisations and for-profit partially taxpayer owned businesses such as Mercury Energy and Air New Zealand which may or may not be classified as SOEs competing in a competitive market. In our opinion the more exclusions or complexity added to the accessibility of the R&D tax credit regime the greater the disincentive for business to access the credit.

When considering R&D tax credits we would also recommend that the Government provides incentives and support for DHBs, Tertiary Institutions, and their subsidiaries to participate to their fullest capacity in the R&D tax credit ecosystem and that they are not dis-incentivised to work alongside New Zealand business and industry to grow research as a percentage of GDP.

Q2: How well does this definition apply to business R&D carried out in New Zealand?

The definition is adequate and reference to the scientific method is a necessary discipline on the system, in part to control the overhead in assessing eligibility. It also protects the credibility of the scheme and helps in terms of the international dimension and scalability. We believe the definition captures both research and development. Our specific feedback on the wording is:

- 'Scientific method' needs a more detailed definition.
- We recommend changing the 'and' following 'or services;' to read 'or that are intended to advance science'.

Q3: Does this definition exclude R&D that you think should be eligible, please illustrate with examples.
Q4: Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

As noted above the definition is broad, however with broadness comes a degree of uncertainty which we believe creates grey areas or ambiguity. Ambiguity potentially creates inherent unfairness in the system, primarily derived from differences in interpretation. For example, there is a potential risk of excluding software development with this definition. While game development (as a product) may not be considered a legitimate activity under the definition of R&D in terms of the intent of the tax credit, gamification of activities (such as tools to improve mental health in a subset of the population) or research into behaviours that support the development of cyber-security applications and their consequent product development and testing are legitimate R&D activities. A specific classification may therefore be required.

Other potential exclusions that may require specific mention include:

- Clinical trials.
- Some market analytics e.g. consumer preferences in New Zealand's export markets (this activity goes beyond basic market research).

Finally, how to take a product or initiative from prototype to full scale production may or may not be excluded under this definition.

Q5: What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

Materiality is defined as a measure of the estimated effect that the presence or absence of an item of information may have on the accuracy or validity of a statement. Materiality is judged in terms of its inherent nature, impact (influence) value, use value, and the circumstances (context) in which it occurs. Given the purpose of R&D is discovery it is unclear what a materiality test would achieve aside from adding complexity and restrictions somewhat akin to applying for business research grants under the current system. Applying a materiality test to 'the problem' removes the benefit of the simplicity of a tax credit regime, adds uncertainty and bureaucracy and creates a 'picking winners' culture which in our view should be avoided.

We recommend that the Government:

- Avoids applying a materiality test to the problem.
- Applies a materiality test related to the advancement of science and technology.

Q6: How well does this definition apply to business R&D carried out in New Zealand?

Q7: Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

The exclusion of these activities is logical in terms of maximising the emphasis on the truly innovative activities of highest benefit. In practice this will be difficult to administer, particularly in areas such as pre-production costs.

Notwithstanding the above statement it is our view that it is in the interest of individuals and companies to protect the intellectual property they create through R&D activities that may otherwise be eligible under this proposal. We therefore recommend that the commercial, legal and administrative aspects of patenting, which are undertaken in respect of activities that are otherwise eligible under this policy, be included in the eligibility criteria as a legitimate R&D expense/cost to business.

Q8: Please provide any examples where social research is has been a core part of business R&D in New Zealand

A social research example from the UoA has been the development of several health apps. Research on understanding the nature of human interaction with the app is critical to the development pathway and ultimate utility.

Q9: What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive?

We support the ineligibility of dual purpose activities for the reasons outlined in several of the comments above. To maximise the benefits of the scheme the investment needs to be targeted at the highest benefits to the innovation system, not simply skewed to the benefit of the company. We therefore support a 'brightline' test as part of the tax rules. Clarity around the 'brightline' would be a requirement of further consultation. As discussed above, we recommend that the Government includes this in tax regulations to maximise investment in truly innovative activity.

Q10: What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour cost?
Q11: What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? What would the appropriate percentage be?

The same issues arise with R&D labour as with "dual purpose activities". The system needs to capture those genuinely engaged in R&D. Also, using direct labour costs alone in a research system that is elsewhere fully costed and fully funded is problematic and thus direct and (reasonable) indirect costs should be included in the calculation. Again, in line with the well tested system used by Universities, overheads as a percentage of R&D labour costs appears a reasonable and practical approach.

We do not support a system where New Zealand businesses are unable to recuperate legitimate overhead or other indirect costs related to the undertaking of R&D. While we support transparency we also note that research is an expensive, and to some extent, risky activity. If Government wish to

incentivise companies to undertake research, and work with experienced research partners, then all costs of undertaking R&D (direct and indirect) should be recoverable.

We recommend that Government considers both direct and indirect labour costs as part of the implementation of this policy.

Included in the discussion paper are two proposals for the treatment of overhead costs. We note that in the current environment for the application of contestable grant funding, most grant funders (MBIE, Health Research Council and Royal Society) calculate overhead cost as a percentage of direct labour costs. As a system it is not without its problems. It incentivises researchers to minimise direct labour costs and thereby reduce the amount of a grant committed to overhead payments to the host institution. In a tax credit scenario it is easy to imagine that businesses may wish to maximise the labour costs to maximise the amount of overhead payable. This is somewhat mitigated against with the effective net 60% co-payment by the business.

We recommend that Government calculates overhead costs as a set percentage of the direct labour costs for the R&D activity.

We note that contestable grant funders currently reimburse institutions between 105% and 120% of direct labour costs. We understand that the rates have been audited by MBIE to ensure they are legitimate. While we do not wish to make a specific recommendation as part of our submission on the rate for overhead reimbursement we consider the range 105% to 120% reasonable.

We recommend that the IRD make the determination on the percentage of direct labour cost to be used as the overhead recoverable by a business and reassess this rate every two years at a minimum.

Q12: Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive?

We support the exclusion of eligibility to claim R&D tax credits to entities who have received commercial consideration except in instances where there is a shared risk and consequently a right to benefits under a commercial research agreement. This risk sharing and the consequent benefit sharing through the provision of in-kind or actual monetary contribution should be considered when tax credits are issued for a particular initiative. Each party should be able to claim up to the total limit of their contribution.

Q13: What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

While the area of software development is increasingly important, the nature of R&D in this area needs to be carefully considered to distinguish research activity from more routine maintenance and updating of software tools. This is another area where activities carried out by entities housed within Universities in particular, are important and would currently not be eligible. For further comment please refer to answers for Q3 and Q4.

Q14: Are there reasons why continuity rules should not apply to tax credits? Please describe.

As an early stage investor in start-ups and spinout companies it is our view that the Government should look at tax credit portability and by doing so turn the tax credit into an asset on the balance sheet that can be realised when the start-up eventually becomes profitable and the rebate can be claimed. This would allow for the benefit of the asset to accrue to the initial investors and support an

entrepreneurial ecosystem. It is our view that this mechanism would support early stage start-ups and encourage investment and increased (but balanced) risk-taking, and therefore a more dynamic economy.

We recommend that continuity rules be excluded from application when applied to tax credits.

Q15: Is the minimum threshold set at the right level? If 'no', please provide further details.

We believe that the exclusion from the threshold for companies that undertake their research activities via an approved research provider allows for a degree of flexibility. We believe the minimum threshold is set at approximately the right level. We note that a junior researcher with the appropriate level of experience could be expected to be paid market rates of between $65k and $80k. With overheads conservatively calculated at 110% the calculation for one full time employee with overheads would be closer to $136k to 168k.

We therefore support the proposed threshold with allowance for approved research providers to provide research services below the threshold. We would expect Universities to be effective contributors to the overall provision of R&D services to the SME sector under the minimum threshold rules.

Question 16: How important is a cap or a mechanism to go beyond the cap?

While we acknowledge the aims of the cap and a mechanism to exceed it we do not consider that this would be a huge issue for New Zealand Business given the $120m R&D expenditure required to reach the cap as broadly discussed above. We therefore have no comment on this issue.

Q17: What features of a Ministerial discretion or pre-registration would make them most effective?

We note that it is not clear which Minister would have discretion to exceed the cap, but this issue aside, adding any type of discretion adds uncertainty to the system as a whole. It is also unclear what the purpose of pre-registration is. We hold the view that pre-registration would add extra work to the process for no real value. Pre-registration is more typical of a grant system and in our view serves as a disincentive to participation. We believe a far more proactive and supportive approach is comprehensive and appropriate advice to support business, provided by a range of actors in the system.

Q18: What are your views on the proposed mechanisms to promote transparency and enhance evaluation?

3.18.1 We support the mechanisms outlined in the discussion document with the exception of making taxpayer-specific information available to Callaghan Innovation. Given that they are both a provider of R&D services as well as a policy provider and advisor we have concerns around a conflict of interest and the provision of commercially sensitive information to a potential competitor.

We recommend that Callaghan Innovation be excluded from the list of Government entities able to access tax-payer specific information.

Q19: Are there any other risks that need to be managed? Please describe.

We remain concerned about the ability of SMEs to undertake or participate in the R&D tax credit programme if they are unable to support the infrastructure to undertake research. As the engine of

the New Zealand economy we would like SMEs to be able to access infrastructure and capability that exists within the New Zealand economy rather than non-participation or duplication of existing resources and infrastructure.

We recommend that the Government, through MBIE or IRD, undertake to provide collateral and training to existing research providers to enable them to promote and support New Zealand Business to better access the R&D tax credit.

Q20: What are the risks with making external advisors liable in this way?
Q21: What is the right level of information required to support a claim?

As noted above we have concerns around conflict of interest and the provision of commercially sensitive information to Callaghan Innovation. We believe that expert advice could be provided by other R&D providers such as New Zealand Universities and CRIs.

We recommend that the Government, through MBIE or IRD, undertake to provide collateral and training to existing research providers (CRIs and Universities) to enable them to provide expert advice in a more competitive environment, which provides for a level playing field. We believe that solely relying on Callaghan Innovation to provide advice to applicants in fields they may not be competent to exercise judgement on, runs the risk of stifling rather than enhancing participation in the scheme.

Q22: What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

We have no comments to make in this area.

Q23: What integrity measures do you think Inland Revenue should use?

We have no comments to make in this area.

4. Additional Comments

The value of overseas contributions and increasing the eligibility limit on overseas spend.
As noted in the discussion paper, eligibility for receipt of tax credits may be considered for certain work and under certain conditions for up to 10% of the value of the R&D spend occurring overseas. We recognise as an exporting nation the value that overseas contributions can make to the capability and capacity of, not only New Zealand companies, but also the wider research ecosystem.

We also note that for many of our 'potential new exports' a range of activities which could be considered legitimate R&D spend by a New Zealand company needs to occur (for regulatory approval or other reasons) in other legislative jurisdictions. We therefore consider the 10% limit should be increased to 20 -25%. At this level we believe the contributions of activities outside of New Zealand will still contribute to the aims and objectives of the Government in terms of capacity and capability building but will also support companies to develop an understanding of divergent markets and jurisdictions in a manner that mitigates risk and is supported prior to extensive investment in market expansion.

More support for SMEs
Business needs certainty to invest and as outlined above, we are of the view that Government is often not best placed to 'pick winners'. We therefore believe that the R&D tax credit proposal provides a more democratic, transparent and flexible mechanism to support research and development in New

Zealand in a way that research grants to industry do not. As discussed, we believe tax credits go some way towards supporting SMEs however we believe that further policy work needs to be undertaken to look at mechanisms which will encourage research activities by this significant part of the New Zealand economy. One example could be the funding of research providers specifically to support industry through a mechanism similar to the 'Return on Science' programme funded by MBIE.

We would like to thank Ministers, MBIE and IRD for the opportunity to respond to the discussion paper on an R&D tax credit incentive.

As New Zealand's largest and highest ranked university and as the largest and most experienced R&D Company of its kind in Australasia we are well placed to see the benefits of introducing a tax incentive. This investment support by government has the potential to provide economic and social benefits for New Zealand. The tax incentive is also likely to lead to an increase in innovative R&D activity in a more diverse range of businesses with greater certainty for those businesses currently engaged or planning to engage in R&D.

As part of the public consultation on the tax incentive proposal we would welcome the opportunity to discuss our ideas further.

R&D Tax Incentives

Section 1: Submission by the Gallagher Group Limited

We strongly support the Government's initiative to further encourage New Zealand businesses to invest in Research and Development and we welcome the opportunity to provide constructive feedback.

Moving from a Grant scheme with a high access threshold to a more equitable and accessible Tax Incentive scheme will encourage more firms to increase their R&D intensity. Although in principle we support the initiative, we have a number of concerns that we want to bring to your attention for consideration.

Gallagher Group R&D Intensity

The Gallagher Group has a very strong commitment to Research, Development and Innovation s 9(2)(b)(ii) This has been one of the critical success factors that has enabled the business to generate substantial export earnings, create jobs and reinvest in innovation. The previous Technology Development Grants and the current R&D Growth Grants have enabled us to further increase our R&D intensity as illustrated in the graph below.

s 9(2)(b)(ii)

s 9(2)(b)(ii) R&D staff numbers have increased from 82 to 120 over the same period. The R&D Grant schemes have been a strong incentive for the Gallagher Group to increase its R&D intensity which in turn has been a major contributor to the growth in revenue.

Proposed R&D Incentives – Our Key Concerns

We are concerned that the proposed R&D Incentive scheme is: 1) going to significantly reduce the R&D support for current Growth Grant recipients, 2) not going to achieve the ministers' ambitious

target of lifting the business expenditure on R&D to 2 per cent of GDP, and
3) not going to offer "greater element of certainty to business"[1] for the following reasons:

1. The proposed definition of R&D is too narrow and does not accurately reflect the R&D activities carried out by the majority of New Zealand's businesses.
    a. The discussion document defines core activities as:
        i. Those conducted using scientific methods;
        ii. Those that are performed for the purpose of acquiring new knowledge or creating new or improved materials, products, devices, processes or services; and
        iii. Those that are intended to advance science or technology through the resolution of scientific or technological uncertainty.

    We understand that the officials' thinking has now moved toward the following definition of core activities:

        iv. Conducted using a systematic approach;
        v. For the purpose of creating new knowledge or creating new or improved materials, products, devices, processes or services; and
        vi. Resolve scientific or technological uncertainty.

    Although this is a step in the right direction, for reasons outlined in the section Broadening Definition of R&D to Include Innovation below, we argue that the modified definition is still too narrow.
2. Reducing the R&D incentive from 20% (~ 14.6% after tax) of eligible R&D expenditure under the R&D Growth Grant scheme to 12.5% tax credit under the proposed R&D Tax Credits scheme will lead to lower business R&D expenditure, particularly given the proposed narrow definition of R&D as mentioned above. In Gallagher's situation based on $18m eligible R&D expenditure under the Growth Grant, the lower rate represents a reduction in R&D funding of $270k for the year.
3. The benefit of the Grant schemes is that entire R&D Programmes (as opposed to individual R&D Projects) of firms were reviewed and pre-approved which provided certainty and predictability for business. The proposed R&D Incentive does currently not have a pre-approval mechanism.
4. The quarterly refunds under the Grant scheme provide businesses with cash flow to support R&D expenditure. The proposed tax credit will have major cash flow implications unless there is a mechanism to include this in the provisional tax returns.
5. The proposed R&D Incentives would come under the jurisdiction of tax law. As tax credits require self-certification, which in the event of disputes, is could lead to severe penalties. In addition to implementing a pre-approval mechanism, we strongly feel that the incentive should be administered separately from the IRD's normal approach to ensure the scheme

[1] Woods, Hon Dr M., Nash, Hon S. (April 2018), Fuelling Innovation to Transform our Economy (p4). Wellington, New Zealand, Ministry of Business, Innovation and Employment.

delivers the desired outcomes (i.e. encouraging an increase in R&D expenditure rather than minimising 'tax leakage'). Alternatively, some leniency would be required with regard to the penalties in instances where our interpretation of the definition and/or exclusions differ from the interpretation of the assessors and where the rules leave room for interpretation.

6. Further to point 1 above, the discussion document states that the NZ equivalent of the International Accounting Standard 38 (NZ IAS 38) is deemed unsuitable. Creating a different definition for eligible R&D could create significant inefficiencies and administrative overhead for business by having to create parallel accounting and reporting mechanisms. The complexity of this would exponentially increase if combined with a project-by-project materiality test as opposed to a pre-approval for an entire R&D programme (as per point 3 above). Also, NZ IAS 38 is generally accepted in business and is widely understood by accountants and auditors. Creating a new and different decision creates uncertainty and makes self-assessment more difficult.

7. Software development to be included. Although software development rarely intrinsically resolves scientific or technological uncertainty, software is in most cases the primary means through which new scientific or technological knowledge is implemented. For example, mathematical models and algorithms are mostly implemented using software therefore software development should be eligible R&D expenditure.

8. Callaghan Innovation should be retained as the administrator/pre-approving authority for the R&D Incentives. Since its establishment in 2013 significant capability and deep connection with industry has been developed. Furthermore, Callaghan Innovation has a key role to play in ensuring that businesses use the R&D Incentives wisely by assisting business with improving R&D capabilities. This is particularly important as more R&D support is made available to businesses with unproven ability to successfully conduct and commercialise R&D. We suggest that Government builds on Callaghan Innovation's capabilities and connections in the implementation of the R&D Incentives.

Broadening Definition of R&D to Include Innovation

Challenging the Underlying Economic Theory

During a workshop on the proposed R&D Incentives with MBIE and IRD officials, one of the officials mentioned that the proposed scheme was underpinned by the economic theory that the creation of new scientific or technological knowledge leads to economic prosperity. We agree that knowledge creation is critical to the creating a diverse, sustainable and productive economy. In our view, new knowledge creation is necessary but insufficient.

The proposed R&D Incentive scheme is focusing the incentive on R&D that addresses a material problem and anticipates a material advance in science or technology. This implies that economic value is created primarily by advances in science or technology. Although this is underpinned by economic theory, significant risks and uncertainty remain around realising the inherent value of these advances. Most commercial opportunities arise from understanding customer/industry problems and opportunities and developing solutions for these problems or opportunities utilising new or existing technology. More often than not it is the *novel application* of the technology that delivers innovation rather than the technology itself. **This is the domain of Business R&D.**

Businesses tend to resolve uncertainty around the application and commercialisation of the scientific and/or technological advances.

Defining Innovation

In the Ministers' Foreword in the discussion document[2], the ministers refer several times to Research, Science and Innovation. While research and science lead to new scientific or technological knowledge, Innovation does not necessarily resolve scientific or technological uncertainty. Instead,

Innovation is the creation of a viable new offering[3].

The authors of this definition further explain this definition:

- **Innovation is not invention** – innovation may involve invention, but it requires many other things as well – including a deep understanding of whether customers need or desire that invention, how you can work with other partners to deliver it, and how it will pay for itself over time.
- **Innovations have to earn their keep** – Simply put: innovations have to return value to you or your enterprise if you want to have the privilege of making another one someday. We like to define viability with two criteria: the innovation must be able to sustain itself *and* return its weighted cost of capital.
- **Very little is truly new in innovation** – Biologist Francesco Redi established the maxim: "Every living thing comes from a living thing." Too often, we fail to appreciate that most innovations are based on previous advances. Innovations don't have to be new to the world – only to a market or industry.
- **Think beyond products** – Innovation should be about more than products. They can encompass new ways of doing business and making money, new systems of products and services, and even new interactions and forms of engagement between your organisation and your customers.

Designing an Holistic Science and Innovation Funding Framework

New Zealand is already investing heavily in science and innovation through a significant number of funds across Investigator-led and Mission-led funds (eg. PBRF, CoREs, Marsden Fund, CRIs, NSC, MBIE Sector-based Research, Health Research Council, etc.) Much of this funding is primarily targeted at creating new scientific or technological knowledge.

[2] Woods, Hon Dr M., Nash, Hon S. (April 2018), Fuelling Innovation to Transform our Economy (p 3-4). Wellington, New Zealand, Ministry of Business, Innovation and Employment.
[3] Keely, L., Pikkel, R., Quinn, B., Walters, H. (2013). Ten Types of Innovation (p5). New Jersey, John Wiley & Sons, Inc.

Funding for Industry-led science and innovation is available through funds such as Primary Growth Partnership, a variety of MBIE Business R&D funds and projects, as well as the more recent Regional Research Institutes.

In order for us to realise the vision of a "better New Zealand for all our people" it is imperative that Government designs a holistic science and innovation framework that has broad political support and continues to provide adequate incentives to realise the inherent value of not only **new** but also **existing** knowledge. **We argue that the definition of eligible R&D should be broadened to include the aforementioned definition of innovation.**

Section 2: Responses to Questions

In this section we provide answers to the specific questions in the discussion document.

Q1: If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the tax incentive, what will the likely impact be on business R&D in New Zealand?

We can't see any immediate impact on business R&D. Research organisations have access to other funding pools for industry-led science and innovation.

There is an opportunity to further encourage collaboration between research organisations, Universities and industry to deliver better outcomes and greater impact for New Zealand.

Q2: How well does this definition apply to business R&D carried out in New Zealand?

As outlined in the previous section, the proposed definition appears to be focused more on 'research' rather than 'development'. We suggest broadening the definition as proposed in the previous section. Additionally, software development should be included as eligible R&D.

Q3: Does this definition exclude R&D that you think should be eligible, please illustrate with examples.

As outlined in the previous section, the definition should include the development of existing knowledge to deliver innovative solutions that solve customer/industry problems.

Q4: Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

We understand that the definition has already been changed from 'using a scientific method' to 'using a methodical approach'. Meaningful R&D should be conducted using a methodical approach and most R&D intensive businesses will have mature R&D methodologies and processes in place.

Q5: What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

The materiality test is relevant if the aim is to address a material problem *and* anticipates a material advance in science or technology. But again, as previously argued, business R&D tends to be focused more on solving customer/market/industry problems though the innovative application of

new and/or existing technology. If the materiality test was applied to business R&D, a significant amount of it would not pass this test.

Q6: How well does this definition apply to business R&D carried out in New Zealand?

This definition does apply in our case. The majority of the supporting activities that do not advance science or technology in themselves, are carried out using a methodical approach and are critically important to effective execution of R&D activities.

Q7: Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

The following activities should not be excluded from core or support activities:

- Market research, market testing, market development or sales promotion (including customer surveys) – Most business that use modern innovation methods and practices, carry out extensive validation with target customers to ensure that the solution solves the customer/industry problem. We argue that market validation that is part of the 'systematic approach' should be eligible.
- Activities involved in complying with statutory requirements or standards – product compliance often requires substantive R&D activities and in many cases leads to new technological solutions and/or innovations. As a result the development cost to comply with these requirements or standards represents a significant portion of the total project development cost. We argue that these activities should be included.
- Pre-production activities, such as demonstration of commercial viability, tooling-up and trial runs – development of new products or services often require the development of new or improved manufacturing processes and capabilities. Furthermore, developing a new product also requires the design and development of tooling to realise the value of the new product. In our view it does not make sense to exclude the costs associated with these activities.

Q8: Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

This is an area that will become increasingly important for R&D in New Zealand. The exponential technologies that are emerging will significantly impact society and will provide significantly change customer experiences. In order to truly understand the impact, mitigate the negative consequences and maximise the benefits, more social science research will be required in both research organisations and business.

Q9: What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive?

The criteria of the R&D Growth Grant already provide a clear delineation between R&D and non-R&D activities. At Gallagher we have systems and processes in place to exclude non-R&D activities. We can't see a significant impact if dual purpose activities were ineligible for the R&D Tax Incentive.

Q10: What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour cost?

The advantage of this would be simplicity which might be useful for organisations that have simple accounting systems and practices. The disadvantage is that the labour-only approach does not reflect the true cost of R&D. We prefer the second option: a broader range of direct and indirect costs (including options for determining appropriate overhead expenditure).

Q11: What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? What would the appropriate percentage be?

Simplicity would be the advantage of a fixed percentage. The disadvantage is that overhead costs could vary significantly between businesses, depending on the nature of their R&D activities. We therefore prefer the first option: include apportioned overhead costs when they are incurred partly for R&D activities.

Q12: Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Costs associated with R&D activities for which commercial consideration is received but where the business still carries a significant amount of risk, should be included. For instance, research and development activities with a significant amount of uncertainty and for which the business only receives a nominal, fixed amount of consideration, should be eligible. We suggest deducting the consideration received from the R&D project cost.

Q13: What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

We strongly argue that software is included in the core activities as increasingly, software is integral to solutions that include new or existing scientific or technological know-how. For more detail, see comments on software development in the previous section of this submission document.

Q14: Are there reasons why continuity rules should not apply to tax credits? Please describe.

The benefit of continuity is that it incentivises investors to take more risk which in turn will ensure that the inherent value of the R&D is eventually released. Most start-ups will go through several rounds of funding before R&D is commercialised. The continuity should be seen as an incentive to keep the R&D moving towards benefit realisation rather than a personal benefit to a potential investor.

Q15: Is the minimum threshold set at the right level? If 'no', please provide further details.

The threshold of $100,000 is still quite high for very early stage companies, particularly in the light of the proposed narrow definition of eligible R&D.

Q16: How important is a cap or a mechanism to go beyond the cap? Please provide further details.

Very few New Zealand businesses spend more than $120m on eligible R&D per annum so this question is irrelevant for the majority of respondents.

Q17: What features of a Ministerial discretion or pre-registration would make them most effective?

Given the limited number of potential cases, Ministerial discretion would be adequate.

Q18: What are your views on the proposed mechanisms to promote transparency and enhance evaluation?

The proposed approach strikes a good balance between creating transparency and preserving commercially sensitive information.

Q19: Are there any other risks that need to be managed? Please describe.

In some cases there may be commercially sensitive information that should be protected for more than two years. There should be a mechanism to enable business to apply for confidentiality beyond the two year time frame.

Q20: What are the risks with making external advisors liable in this way?

As the standard penalties provisions apply, we question whether this is going to deliver the right outcomes. The aim is to increase business R&D expenditure whilst ensuring that the system is not abused. Businesses aim to strike a balance between commercial risk and reward. The tax jurisdiction weights the balance more towards risk due to the potential penalties. This could lead to businesses taking less risk which in turn will lead to lower rewards.

Instead of extending the penalty rules, we suggest appointing an independent authority (i.e. Callaghan Innovation) to assess the R&D Tax Incentive claims.

We do support the suggestion to extend any penalty provisions to tax advisors where advisors receive direct financial benefit based on the quantum of the R&D Tax Incentive. Consideration needs to be given to how the advisors charge for their services.

Q21: What is the right level of information required to support a claim?

Although lacking specific details on the supporting information for the R&D Tax Incentive claims, the proposed return process for the claims appears cumbersome and significantly more complex than the current R&D Growth Grant reporting requirements and process. We are very concerned that this is going to create a significant amount of additional administrative work and additional internal reporting mechanisms.

If the aim is to provide a seamless process, the reporting mechanism and supporting information requirements should reflect that. One of the most significant disadvantages of the 2008 Tax Credit scheme was the onerous reporting requirements for each individual R&D project. With the introduction of the Technology Development Grants and the subsequent R&D Growth Grants, the process and reporting were greatly simplified.

We strongly argue for a similar approach; pre-approval for an entire R&D Programme with quarterly and annual reporting as verified by the auditors.

Q22: What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Please take a look at the Callaghan Innovation web portal. Why recreate something that already exists?

Q23: What integrity measures do you think Inland Revenue should use?

Callaghan Innovation should be appointed as the independent third-party to provide the required integrity measures, provide the customer support, and conduct compliance checks pre- and post-application as well as approve claims.

For and on behalf of the Gallagher Group,

s 9(2)(a)

31 May 2018

R&D Growth Grant Transition

Section 1: Submission by the Gallagher Group Limited

We strongly support the Government's initiative to further encourage New Zealand businesses to invest in Research and Development and we welcome the opportunity to provide constructive feedback.

Moving from a Grant scheme with a high access threshold to a more equitable and accessible Tax Incentive scheme will encourage more firms to increase their R&D intensity. Although in principle we support the initiative, we have a number of concerns that we have outlined in a separate submission on the R&D Tax Incentives discussion document.

In this submission we respond to the proposed transition approach from Growth Grants to the R&D Tax Incentive.

Gallagher Group R&D Growth Grant Contract

Gallagher is a recipient of a R&D Growth Grant. This grant covers the R&D activities of all divisions within the Gallagher Group and therefore includes three separate R&D Programmes; Gallagher Animal Management, Gallagher Security and Gallagher Fuel Systems.

The current Growth Grant contract expires on the 30th of September 2018. Unless Gallagher receive an extension of this contract, Gallagher will not have any R&D support until the new R&D Tax Incentives are implemented.

At present there is no mechanism for us to apply for an extension of our Growth Grant.

During a feedback session with officials from Callaghan Innovation, MBIE and IRD on the 22nd of May, we learned that the proposed transition for Gallagher would be an automatic extension of our current Growth Grant contract until the 31st of March 2020.

Section 2: Responses to Questions

In this section we provide answers to the specific questions in the discussion document.

Q1: What impact will the proposed transition arrangements have on your business? For example, your cash-flow or internal reporting mechanisms? Please describe.

The discussion document does not provide any clarity for our specific scenario. Unless there is an extension of the Growth Grant at the end of our current contract which ends on the 30th of September 2018, Gallagher will not receive any R&D support as the proposed R&D Tax Incentive will not be implemented until the 1st of April 2019. The cash flow implications are quite significant as we stand to lose around $900k of funding per quarter.

The impact of the transition from the Growth Grant to the proposed R&D Tax Incentive could be significant.

The quarterly refunds under the Grant scheme provide businesses with cash flow to support R&D expenditure. The proposed tax credit will have major cash flow implications unless there is a mechanism to include this in the provisional tax returns.

GALLAGHER GROUP LIMITED
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s 9(2)(a)

Although lacking specific details on the supporting information for the R&D Tax Incentive claims, the proposed return process for the claims appears cumbersome and significantly more complex than the current R&D Growth Grant reporting requirements and process. We are very concerned that this is going to create a significant amount of additional administrative work and additional internal reporting mechanisms.

If the aim is to provide a seamless process, the reporting mechanism and supporting information requirements should reflect that. One of the most significant disadvantages of the 2008 Tax Credit scheme was the onerous reporting requirements for each individual R&D project. With the introduction of the Technology Development Grants and the subsequent R&D Growth Grants, the process and reporting were greatly simplified.

We strongly argue for a similar approach; pre-approval for an entire R&D Programme with quarterly and annual reporting.

Q2: What do you believe to be a necessary transitional period? Please explain why this is necessary for your business?

Gallagher is a large, multi-national group of businesses. As a result our internal reporting mechanisms are complex. We believe that a transitional period of one year would be adequate once the details of the R&D Tax Incentive scheme have been implemented.

One year should give us adequate time to design and implement the changes to our internal reporting mechanisms and to get these checked by our auditors.

Q3: What impact will the proposed transition arrangements have on your R&D programme over the next few years?

We elaborated on this in the separate submission document on the R&D Tax Incentive discussion document. In summary, as defined in the discussion document, Gallagher's R&D Programme will have to be reduced based on the anticipated drop in R&D support. Although we have not been able to quantify this as the proposed R&D Tax Incentives still lack detail, we estimate that the R&D Programme will reduce by around 20%. This equates to an approximate reduction in R&D expenditure by around $2.2m and a loss of R&D jobs of around 20 full time equivalents.

Q4: Please provide any other comments about the proposed transition arrangements.

If our existing R&D Growth Grant is automatically extended to the 31st of March 2020 and the details of the R&D Tax Incentives are finalised and implemented by the 1st of April 2019, we believe we have adequate time to manage the transition.

Our concerns as outlined in the submission on the R&D Tax Incentive discussion document remain.

For and on behalf of the Gallagher Group,

s 9(2)(a)

31 May 2018

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1 June 2018

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Dear Sir / Madam

Fuelling Innovation to Transform Our Economy: A Discussion Paper on a Research & Development Tax Incentive for New Zealand

Zespri Group Limited ("Zespri") welcomes the opportunity to submit on the discussion paper "*Fuelling innovation to transform our economy: A discussion paper on a Research and Development Tax Incentive for New Zealand*" ("the Discussion Paper").

We attach our detailed submissions as *Appendix A* for your consideration. The following is a summary of our key recommendations:

- The eligibility criteria for research and development ("R&D") should be "stand alone" and not linked to the tax deductibility of the particular expenditure;
- Dual-purpose activities should be eligible for the R&D tax credit;
- All overseas expenditure should be eligible for the R&D tax credit, not only 10%, if the prescribed criteria are met;
- The definition of "eligible expenditure" should include both direct and indirect costs (including a portion of overhead costs);
- Officials should carefully consider the impact of strengthening the "at risk" rule;
- The R&D tax credit regime should not include any "clawback" mechanisms;
- The shareholder continuity rules, as currently operating, should not apply to the R&D tax credit regime;
- Zespri supports any procedures / processes that will provide certainty for taxpayers, including providing for an optional pre-filing review by Inland Revenue.

Thank you for the opportunity to make submissions. If you have any queries regarding our submissions, please contact s 9(2)(a)

s 9(2)(a)

***Appendix A* – Zespri's Submission**

Introduction

1. Background

1.1. Zespri is a New Zealand based multi-national group that sells high quality premium kiwifruit around the world. Zespri's activities encompass the sale and marketing of kiwifruit. Zespri is a well-known brand in the global fruit industry.

1.2. Zespri employs over 600 people across offices located in Asia, Europe, North and South America, Middle East and New Zealand, with the head office at the centre of New Zealand's major kiwifruit region, the Bay of Plenty.

1.3. Innovation is a critical part of supporting the future growth of the New Zealand kiwifruit industry. Accordingly, Zespri is actively engaged in R&D to keep the industry at the "cutting edge". Some examples of R&D undertaken by Zespri include developing new kiwifruit varieties, developing orchard management and environmental growing methods, and improving post-harvest handling systems.

1.4. Zespri currently receives funding under the Callaghan Innovation Growth Grant ("the Growth Grant"). The current funding applies until 31 March 2020. [redacted] s 9(2)(b)(ii) Zespri claimed R&D tax credits under the previous tax credit regime.

1.5. The following submission points address some of the questions raised in the Discussion Paper as well as other issues not specifically raised by officials.

Detailed submission points

2. Eligible expenditure on R&D

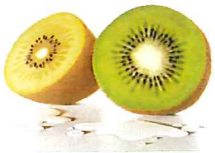
2.1. The Discussion Paper provides that the R&D tax credit will only apply to expenditure that is deductible or amortisable under the Income Tax Act 2007.

2.2. Zespri does not agree with this approach. Rather the eligibility criteria for R&D should be "stand alone" and not linked to the tax deductibility of the particular expenditure.

2.3. The broad purpose of the proposed R&D tax credit is to encourage expenditure on R&D in New Zealand. However, this purpose will not always align with an outcome arising under ordinary tax rules. As such, there is a risk that linking the tax credit regime to income tax deductibility will exclude expenditure on R&D that would have otherwise met the criteria.

2.4. For example, a business may incur expenditure on R&D that is "black hole expenditure" (i.e. non-deductible / non-depreciable) for income tax purposes and therefore would be excluded from the R&D tax credit.

2.5. Further, there will be increased compliance costs, and risk of error, arising if a taxpayer has to consider the income tax treatment as part of claiming the R&D tax credit.



3. Sole purpose vs principal purpose

3.1. The Discussion Paper asks for comment on the impact on business R&D in New Zealand if dual-purpose activities are ineligible for the R&D tax credit. Specifically, the Discussion Paper provides that "if an activity was carried out for a R&D purpose and a non-R&D purpose, the entire activity would not qualify as a R&D activity."

3.2. Zespri considers that activities that have both R&D purposes and non-R&D purposes (i.e. dual-purpose activities) should be eligible for the R&D tax credit.

3.3. The reality is that all businesses in the commercial context ultimately undertake R&D expenditure to increase earning through the commercialisation of the R&D. Therefore applying a "sole purpose" test will effectively exclude all businesses from benefiting from the R&D tax credit, resulting in an absurd outcome.

3.4. The better approach is to apply a "principal purpose" approach where the test is whether the principal purpose (but not necessarily the only purpose) is one of R&D.

4. Overseas expenditure on R&D

4.1. The Discussion Paper notes that up to 10% of eligible expenditure on a R&D project can be for overseas R&D costs provided:

- the overseas work is part of a project based in New Zealand; and
- at least half of the R&D expenditure is for activities carried out in New Zealand.

4.2. Zespri agrees that restrictions are required to ensure that the New Zealand economy benefits from expenditure that attracts the R&D tax credit. However, we do not agree with imposing a 10% limit on R&D expenditure that occurs overseas, despite that overseas expenditure still meeting all of the other R&D criteria.

4.3. The better approach is to apply a two-stage test. The first test being that the expenditure is part of a project based in New Zealand and at least half of the activities are carried out in New Zealand (i.e. the same test outlined above). Secondly, that the intellectual property resulting from the overseas R&D expenditure is owned in New Zealand. Once an organisation meets these eligibility criteria then **all** of that overseas expenditure should be eligible for the R&D tax credit, not only 10%.

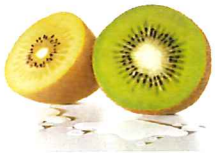
4.4. The suggested approach will prevent the exclusion of R&D expenditure that an organisation conducts overseas for legitimate reasons. E.g. the need for a larger population. In addition, this approach reflects that the resulting intellectual property is often owned in New Zealand and therefore will generate revenue streams that positively affects the New Zealand economy. E.g., license income.

4.5. Officials may choose to include a "cap" that limits the total amount of overseas expenditure that is subject to the R&D tax, as an additional restrictive mechanism.

5. Direct and indirect cost (including overheads)

5.1. The Discussion Paper has asked for the advantages and disadvantages of limiting the eligible expenditure to only R&D labour costs. The alternative approach is to include both direct and indirect costs.

5.2. Zespri's view is that the definition of "eligible expenditure" should include both direct and indirect costs (including a portion of overheads relating to R&D) on the basis this approach more accurately captures the true costs associated with an R&D project.



5.3. Zespri acknowledges the simplicity of a direct labour cost approach. However, the exclusion of non-direct R&D expenditure will outweigh any potential benefits of simplicity. The actual cost of R&D is much broader then only direct labour costs and therefore an approach that captures both direct and indirect costs is more accurate in reflecting the true cost associated with an R&D project.

5.4. It is common for businesses to collaborate with specialist research institutions (e.g. universities / Crown research), with the business paying for R&D and owning the resulting intellectual property. Such arrangements (and collaboration more generally) are critical in creating an environment that is conducive to innovation and gives organisations sufficient flexibility and agility in choosing to work with the best teams.

5.5. However, a direct labour cost approach will exclude payments for R&D services (e.g. the outsourcing of technical R&D work) even when the organisation funding the R&D will own the resulting intellectual property. Such an approach will penalise organisations that are willing to fund R&D but may not have the technical staff and/or resources to undertake the work themselves or have decided to use an outsourcing model for their R&D, as Zespri does.

5.6. A further benefit of using the broader approach is consistency with the previous R&D regime and with the approach taken in Australia.

5.7. Zespri prefers for a sufficiently flexible approach in relation to R&D overhead costs (e.g. giving the ability to choose between allocation methods and / or to choose an allocation method that is "fair and reasonable") when allocating overhead costs.

6. Commercial consideration

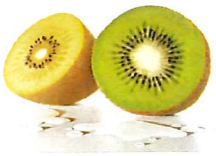
6.1. The Discussion Paper provides that officials are considering strengthening the "at risk rule" by excluding expenditure that relates to R&D activities for which the entity has received or could reasonably be expected to receive consideration.

6.2. Zespri's concern with strengthening the "at risk rule" is that it will potentially exclude businesses that are undertaking R&D to increase profits on the basis that these businesses "could reasonably be expected to receive consideration" from the R&D.

6.3. For example, Zespri undertakes a significant amount of R&D on developing new kiwifruit cultivars that once commercialised will generate license income. Based on the current wording, these costs would be excluded from the R&D tax credit on the basis that Zespri is expected to receive consideration from the R&D.

6.4. There are also questions of how the "at risk rule" will operate in practice. Specifically, are officials envisaging the use of a "claw back" mechanism that will apply if a business claims R&D tax credits but then derives consideration at a later date?

6.5. From a policy perspective, the R&D regime should not include any "clawback" mechanisms. Any such mechanism will create uncertainty and undermine the effectiveness of the R&D tax credit regime. Businesses need to be confident that once they meet the eligibility criteria the R&D tax credit will not be "clawed back" due to the occurrence of some future event. Without this certainty, businesses may choose not to participate in the R&D regime on the basis that the compliance costs and risk of tax credit forfeiture outweighs the benefit from the tax credit.



7. Software costs

7.1. The Discussion Paper has correctly noted that software R&D is an important part of New Zealand economy. Zespri agrees that separate work should be undertaken to understand the best way for applying the R&D definition to software R&D.

7.2. Zespri's initial view is that the R&D regime should not contain a separate "cap" for software expenditure (as there was in the previous tax credit regime). Rather, to ensure a simple and comprehensive regime, all R&D expenditure (including software) should fall under the same general cap.

8. Application of shareholder continuity rules

8.1. Zespri's view is that the shareholder continuity rules should not apply to the R&D tax credit regime, particularly if the tax credit is non-refundable.

8.2. The primary reason for this view is that many companies claiming R&D tax credits are start-up companies that obtain new equity for further expansion prior to earning any revenue from their product. Including a continuity requirement may result in these companies, which have incurred legitimate expenditure on R&D, forfeiting their R&D tax credits due to a continuity breach upon the injection of new equity. This outcome is clearly not the policy intent behind the R&D tax credit regime.

8.3. The same logic applies to established companies that incur R&D but are in tax loss making positions (possibly due to historical tax loss balances) or have no income tax liability due to other legitimate reasons. E.g., large foreign tax credit arising from tax paid overseas. These companies may only have sufficient income tax to absorb the R&D tax credits in the future; however, they may suffer a continuity breach prior to such time.

8.4. From a policy perspective, the R&D tax credit aims to increase spending on R&D in New Zealand up to the desired level. Provided an organisation meets the eligibility criteria at the time it incurs the expenditure, it should not matter which shareholders ultimately benefit from the use of the R&D tax credit. The key outcome is that the level of expenditure has increased, thus achieving the policy intent.

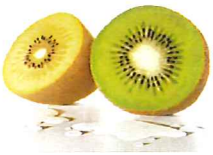
8.5. Applying the shareholder continuity rules will also create additional uncertainty due to the possible forfeiture of the tax credit if there is a future continuity breach. Many organisations, particular those in the circumstances mentioned above, will seriously consider whether the benefit from the tax credit will outweigh the costs of compliance, factoring in the likelihood of forfeiture due to continuity breach.

8.6. Zespri may be open to the shareholder continuity rules applying to the R&D regime if the shareholder continuity rules were sufficiently modified to include a "same or similar business test", similar to the test operating in Australia.

9. Ordering of R&D tax credit

9.1. The Discussion Paper is silent on how the tax credit "ordering rules" will apply to the R&D tax credit. This is a key point that needs clarifying, as it will influence whether an organisation will have sufficient income tax liability to utilise its R&D tax credits.

9.2. Zespri's view is that, for the purposes of the ordering rules, R&D tax credits should arise after the utilisation of imputation credits and tax credits for foreign tax paid but before any provisional tax paid.



9.3. This approach will give taxpayers the option of reducing their provisional tax payments during the year to reflect the reduction in tax from the R&D tax credit.

10. Penalties

10.1. The Discussion Paper provides that the standard penalty provisions are likely to apply to the R&D tax credit regime.

10.2. Zespri acknowledges that penalties are required to protect the integrity of the R&D tax credit regime. However, we are concerned that imposing the standard penalty regime may result in unduly penalising certain taxpayers who make a genuine mistake or take a different technical interpretation to Inland Revenue.

10.3. A possible solution is to modify the penalty provisions to ensure that penalties will not apply where adjustments are required for technical reasons.

11. Administration / compliance

11.1. Generally, for the R&D tax credit regime to be successful, it must be efficient, easy to comply with, and require an appropriate amount of supporting information.

11.2. The Discussion Paper provides that Inland Revenue will administer the R&D tax credit regime with the support of Callaghan Innovation. Zespri's view is that Callaghan Innovation, given its existing knowledge and expertise, should be the main body concluding on any technical R&D eligibility questions.

11.3. Zespri supports any procedures / processes that will provide certainty for taxpayers, including the issuing of rulings and determinations.

11.4. The current process under the Callaghan Innovation funding model requires signoff from an external auditor to confirm the organisation has used the funding appropriately. Zespri suggests that the R&D tax credit regime incorporates a similar optional process (possibly specifying a list of accredited auditors), that, if undertaken, would prevent or reduce future Inland Revenue audits.

11.5. Zespri would also like to see an optional pre-filing review by the IRD built into the regime to allow for additional certainty. This process would provide certainty for larger organisations that incur substantial amounts of R&D expenditure.

From: s 9(2)(a)
To: RD Incentive
Subject: Feedback on Callaghan Growth Grant & R&D Tax Credit
Date: Friday, 1 June 2018 9:17:59 a.m.

Dear Sir/Madam,

Coherent Solutions is develops and manufactures advanced test equipment for the >10Billion USD optical communications device global market.

Our products are exported across the globe (>20 countries) and used in the R&D and production-lines of many global component manufacturers such as Intel, Ciena, Google, & Huawei.

We are Kiwi owned and both our internal R&D and manufacturing is done here in New Zealand.

Since the company was founded in 2012 we have grown to ~$5M revenue in 2018, and currently employ 32 people, many of whom are highly skilled R&D and Production Engineers.

We have established a strong position in our global market through our R&D innovation and are poised to experience >65% CAGR over the next three years.

When the founders established Coherent Solutions, it was with the clear goal of creating a successful technology/manufacturing company located here in NZ which would provide long-term employment for the founders and world-leading team we have built. New Zealand is extremely well suited to the type of high-value manufacturing we do. We are very cost-effective compared to our primary competitors (who manufacture in North America or Western Europe), and we have access to a strong resource-pool of highly skilled FTE's.

As with the majority of technology/hardware driven companies, growth and market-share is largely driven by the companies ability to innovate and rapidly develop new products to offer a unique competitive advantage. Without this, the growth opportunities for such companies is extremely limited.

For most growing companies in markets such as ours, the initial investment required in R&D outweighs the short-term return; leaving the company with two choices:
1. Use external funding/investment to supplement the sales income in the short-term, until sufficient sales profit is generated to support the R&D investment required to support growth.
2. Limit the R&D investment to what can be supported by sales profits. This approach will frequently result in the inability to grow market-share & revenue, leading to the eventual demise of the company.

I do not believe anything I have stated above should surprise you, or contradicts basic the technology business growth models utilized in Europe and the USA - I have been involved in the successful growth of technology companies in both the USA and UK.

Over the last four years Coherent Solutions has been very successful in growing our global market position and revenue - largely thanks to the two Callaghan R&D Grants which we have been awarded.

We are close to completing our second grant, which will take us to our maximum R&D grant allowance of $800K.

We intended to apply for a Growth Grant to support further growth in July 2018.

These grants have been instrumental in supporting the growth of our company, resulting in the addition of ~10 FTE's and positioning us for the significant growth described above through business with companies such as Intel, whose engagement was enabled through the technology developed through our R&D Grants.

The impact of the loss of the Growth Grant and its replacement by a Tax Credit will have a devastating effect to our business. Since founding the company, all operating profits have been re-invested in R&D. Hence we are not a profitable company at this time, so the R&D tax credit will not provide any support to our growth at all.

The initial estimate of the impact of the replacement of the Growth Grant by a Tax Credit is that it will reduce our growth from 65% to ~20% CAGR over the next 3 years, and will result in the loss of 8-12 FTE's, most of which will occur in Q3/Q4 this financial year.

This will leave Coherent Solutions with tho choices:

1. Significantly reduce our R&D investment - which will immediately impact our short-term growth opportunities. In turn, this will impact our market position, limiting our potential to ever reach the point where our sales profits can support the R&D necessary for growth. At this point, we will have lost our future opportunities and the company will become nonviable.

2. Seek additional investment to support R&D investment. This is the most likely outcome - several of our customers/partners have already expressed interest in such an investment/acquisition. However, as all our customers and partners are overseas, it is extremely likely that such an investment would result in a relocation of the company to the USA, or possibly China.

To be blunt, I expect this decision will result in the eventual closing of Coherent Solutions, or its relocation overseas.

Apart from the obvious personal disappointment of the shareholders, we all feel that this is a terrible result for New Zealand. Coherent Solutions has established world-wide credibility and respect in our market, and our high-value manufacturing is well suited to New Zealand; and fitted well with what we considered were NZ's economic growth plans. We are poised to become a world-class company, with the opportunity to achieve revenues >>$200M over the next 7-10 years.

In many ways, I do agree with the governments approach to the the Growth Grant and Tax Credit. However, it is going to leave a significant gap which is likely to engulf Coherent Solutions and many other growing hardware/technology companies in New Zealand.

I believe that this gap is relatively simple to fill, without any significant changes to the government policy - as I understand it.

Make a simple change to the R&D Project Grant to remove the $800K total funding cap, enabling companies to continue to apply for R&D funding for specific projects -

irrespective of how many grants have previously been awarded, or their value.

This would immediately remove the risk to Coherent Solutions and all the other companies in NZ focused on growing their businesses rather than achieving short-term profits.

I would welcome the opportunity to discuss this in further detail, and demonstrate the immediate impact it would have to Coherent Solutions.

Yours Sincerely,

s 9(2)(a)

Kind Regards,

s 9(2)(a)

Coherent Solutions Ltd

s 9(2)(a)

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31 May 2018

R&D Tax Incentive Team
Ministry of Business, Innovation & Employment
PO Box 1473
WELLINGTON 6140

By email: RDincentive@MBIE.govt.nz

Dear Sir / Madam

Fuelling Innovation to Transform our Economy: A discussion paper on a Research & Development Tax Incentive for New Zealand

Air New Zealand Limited (Air NZ) wishes to thank the Ministry of Business, Innovation & Employment (MBIE) for the opportunity to submit on the Discussion Document (DD). Further, we appreciate the time taken by MBIE and IR staff to meet with Ian Walker, General Manager Business Transformation and Helen Day, Manager Taxation in Auckland on 16 May 2018 to discuss the proposals.

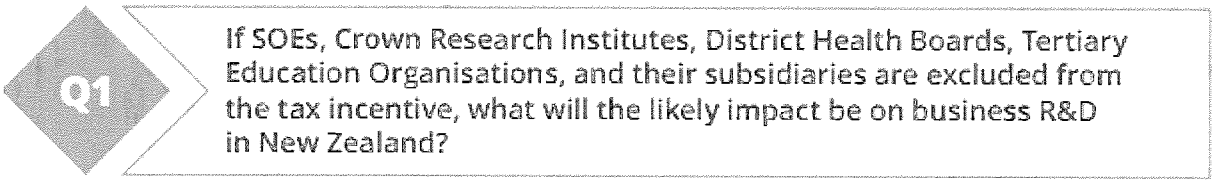
The Corporate Taxpayer Group, of which Air NZ is a member, is also preparing a submission on the policy proposals presented in the DD and, to the extent that the issues impact Air NZ, Air NZ supports the views expressed in that submission. As such, this submission will focus on the most relevant areas to Air NZ, namely Air NZ's potential exclusion from eligibility to the R&D tax incentive due to its 52.1% Government shareholding (DD Question 1) and ensuring that R&D tax incentives are specifically available for software R&D activity where the output of that R&D activity has an internal application (DD Question 13).

We also make this submission at the request of MBIE and IR Officials in order to assist them to clarify an area of apparent confusion around the policy intent for mixed ownership enterprises.

Introduction

This submission has been prepared in response to the policy proposals presented by the Government to achieve its aspiration to increase New Zealand's R&D expenditure to 2% of GDP over the next 10 years. The proposal to offer a 12.5% tax credit for eligible expenditure is aimed at encouraging New Zealand businesses to innovate so that they are competitive and successful in the changing markets of the future. As stated in the DD, encouraging R&D activity broadly across New Zealand businesses will lead to job creation in areas that are "future proofed", industry diversity, international engagement, profitability and overall sustainability in the digital age. Put simply, encouraging a progressive culture of innovation is good for New Zealand and New Zealanders, and Air NZ strongly supports these policy objectives.

Government entities



If the Government is committed to achieving its ambitious target, and increasing the contribution from businesses undertaking R&D, it is vital that the R&D tax incentive applies to all businesses undertaking R&D activity in New Zealand. It does not make good policy sense to encourage some businesses' innovation and effectively disadvantage others, when all business innovation adds to New Zealand's future prosperity and will heavily influence how New Zealand as a whole will emerge from the Fourth Industrial Revolution – The Digital Age.

In relation to the eligibility of Government entities for the R&D tax incentive the DD notes (pg 15):

> *"The focus of the Incentive is on private businesses. The place for entities funded by government needs to be considered. State Owned Enterprises are not eligible for Growth Grants and Crown Research Institutes, District Health Boards, Tertiary Education Organisations, and subsidiaries under their control were not eligible for the 2008 tax credits."*

The principles behind this exclusion from eligibility are that:

i. The R&D tax incentive is intended to stimulate R&D by the private sector in addition to that already funded by Government; and
ii. Entities funded by Crown appropriation are already directly funded by Government for the R&D that has been approved as part of the entities' annual budget and appropriation cycles.

These principles are coherent and when applied to a publicly listed company like Air NZ, should result in Air NZ being eligible for the R&D tax incentive (as was the case for the 2008 tax credits).

It is not apparent from the DD, and in particular Question 1 above, that the intent of the R&D policy is to exclude Air NZ's R&D expenditure from the regime due to its mixed ownership model. It was therefore concerning to learn that some MBIE and IR Officials consider that entities listed in Part B of Schedule 36 of the Income Tax Act 2007 (of which Air NZ is one) should be excluded. If indeed this is the case, Air NZ strongly disagrees with this policy outcome and submits that the eligibility criteria should be consistent with the R&D tax credit regime in 2008 in relation to mixed ownership enterprises.

Key reasons that Air NZ should be eligible for the R&D tax incentive include:

1. Air NZ is not funded by the Crown

Air NZ is an ordinary public company that is funded by equity owned by its shareholders, debt raised in the markets and working capital generated from its business. Air NZ, and Air NZ's R&D expenditure, is not funded by Crown appropriations. The Crown, through the shareholding Minister, is simply an equity investor in Air NZ alongside thousands of other private investors. Alongside and pro-rata with the public shareholders, the Crown receives a dividend return on its equity investment with the rate varying depending on the business performance of Air NZ.

Air NZ is part of the private sector and is not Government funded. It does not meet the two principles for exclusion from the R&D tax incentive outlined above and therefore should be eligible for R&D tax credits.

2. Air NZ would be unfairly disadvantaged compared to its competitors

Air NZ competes fairly in the market for business against other publicly listed and privately owned foreign and domestic companies. Air NZ is focused on innovating and transforming business to attract and retain customers, contributing to New Zealand by ensuring that we have a sustainable world class international airline connecting us to our local and global markets, and providing an investment return to its shareholders. If Air NZ is not eligible for the R&D tax incentive and its competitors such as Qantas / Jetstar are, that would give rise to an unfair competitive disadvantage.

In addition, the Government was able to successfully sell down its shareholding in Air NZ to the public on the basis that the company would continue to be operated independently as a publicly listed company. Differentiating Air NZ from other competitors on the basis that the Crown has retained a 52.1% equity interest disadvantages the public shareholders of Air NZ and may weaken investor confidence.

3. New Zealand shareholders would be disadvantaged compared to foreign companies

The Minister of Research, Science and Innovation (MRSI) has stated that offshore companies will be eligible to receive the R&D tax incentive as a measure to attract international companies to set up and perform R&D in New Zealand (NBR 22 May 2018). That makes policy sense because if innovation is undertaken in New Zealand, New Zealand benefits from the associated "spill over" benefits.

However, if Air NZ is not eligible for R&D tax credits for innovation that it undertakes in New Zealand, but foreign companies are eligible, then Air NZ's public shareholders will be disadvantaged when compared to shareholders in foreign companies that undertake R&D in New Zealand. That would be poor policy and is difficult to rationalise on a fairness or principled basis. It may also pose a political risk for a Government to favour foreign owned businesses over a domestically listed company.

4. Air NZ's efforts to innovate align closely with the Government's objectives to increase R&D in New Zealand

Air NZ is investing in R&D in order to drive innovation in its business and develop and sustain a competitive advantage for the benefit of customers, shareholders and New Zealand as a nation.

Through its R&D activity, Air NZ is gaining international attention due to its desire to innovate and its use of technology to enhance the customer experience and eliminate travel pain points. Examples of this industry leading innovation are a wearable wristband for children travelling by themselves, a mobile app that allows customers to order coffee and pick it up at participating Koru Lounges, biometric bag drops, AI-powered kiosks, a chatbot called Oscar that answers customer questions and a highly interactive Inflight Entertainment (IFE) system.

This innovation is being funded from business revenue and is not Government funded. This is exactly the type of R&D expenditure that aligns with the MRSI's commitment to increasing R&D expenditure to 2% of GDP over the next 10 years.

5. Eligibility to receive a R&D tax credit will increase Air NZ's R&D activity

Being eligible to receive a R&D tax credit for R&D expenditure will have a real and positive impact on the level of R&D activity Air NZ will be able to undertake.

As a commercial business, accountable to our shareholders, Air NZ's senior leadership in conjunction with our Executive Steering Committee must formulate our future digital / innovation plans based on return on investment (ROI), priorities and budget trade-off criteria. Whilst future sustainable growth is dependent on innovation to meet the challenges of the digital age, ultimately our decisions to ready ourselves for that future are financially constrained.

The minimum ROI criteria creates a "waterline" above which prospective projects must float before they will be undertaken. The ability to factor a R&D tax credit into the business case of potential R&D projects will give Air NZ the ability to undertake more R&D activity given more projects will get over the waterline faster. Further, the R&D tax credit will reduce the business risk of true R&D innovation, which given its nature has a high risk of failure. Again, this means that more R&D activity will be undertaken.

6. Benefits of business collaboration would be limited

Any exclusion of SOEs and mixed ownership enterprises from the R&D tax credit regime will also limit the benefit of such entities collaborating with commercial businesses.

Air NZ has recently been collaborating with a New Zealand based technology company, Quanton Limited, to develop robotic processes to automate repetitive tasks such as performing a bank reconciliation. This work is an example of Air NZ undertaking R&D (developing internal software) by utilising the expertise of a New Zealand business that is exactly of the type that the policy is targeting. Therefore, in addition to enabling Air NZ to perform more work of an innovative nature, access to R&D tax credits will also indirectly support the businesses we partner with, which will help the growth of that type of business, create jobs and develop New Zealand's relevant skill base. All of which will drive New Zealand up the value chain and as such should be encouraged and not excluded from the regime.

7. The discussion document is clear in its intent that Air NZ should be eligible

The discussion document is clear in reflecting the Government's intent that State Owned Enterprises (**SOEs**), Crown Research Institutes, District Health Boards, Tertiary Education Organisations, and subsidiaries under their control are not intended to be eligible for the R&D tax incentive.

As a factual matter, Air NZ is a publicly listed company and is not an SOE, Crown Research Institute, District Health Board, Tertiary Education Organisation, or a subsidiary under any of those organisations' control.

We note that Air NZ has never been listed in Part A of Schedule 36 of the Income Tax Act 2007 which specifies State Enterprises for tax purposes. Air NZ was listed in Part B as a Mixed Ownership Enterprise in 2012 as a consequence of the Government's decision to sell a further 20% of its shareholding in Air NZ to the public.

As such, in terms of the Government's policy as expressed in the discussion document, Air NZ is specifically intended to be eligible for the R&D tax incentive.

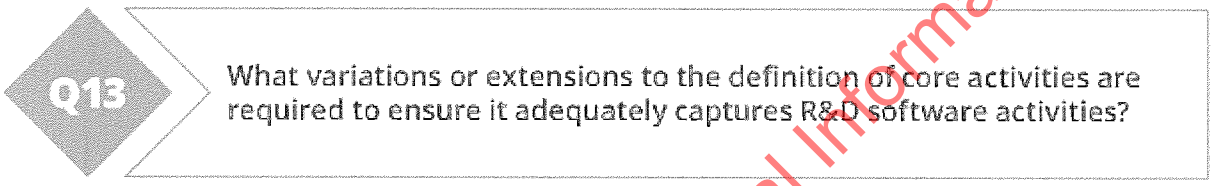
The current uncertainty created by the varying views from Officials must reflect either an undisclosed change in Government policy since the discussion document was released, which would be disappointing, or signal internal confusion about the Government's policy intent, which is unsatisfactory and should be speedily resolved.

Fiscal constraints

Air NZ notes from discussions with MBIE and IR Officials that the rationale behind the potential exclusion of the abovementioned entities appears to be related to fiscal constraints. An exclusion that targets Air NZ (and like Government owned entities) from the regime on the grounds of fiscal affordability offends the basic policy principles of fairness and horizontal equity. Further, it is inappropriate for a policy of this nature, which is promoting the good of all New Zealand to discriminate against the value added to the New Zealand economy by an innovative company such as Air NZ.

Fiscal concerns should be more appropriately managed in a coherent and principled manner through other means, such as reviewing overall caps and the minimum spend thresholds.

Software developed for Internal Use



The DD notes (pg 22):

> *"special treatment for some software R&D activities, such as testing and internal software development is being considered".*

It is understood that this consideration may lead to R&D expenditure of this nature being capped or excluded from the regime.

Air NZ is of the view that the potential distinction between benefits derived from software innovation undertaken to develop products for internal use and external exploitation is arbitrary and is inconsistent with the stated policy outcomes of the proposed regime. Innovation, regardless of the product of that innovation, achieves job creation, develops and extends new thinking (which may lead to further innovation in both internally and externally focused software), and develops a skilled New Zealand based workforce. R&D activity directed towards software developed for internal use is just as essential to New Zealand businesses to achieve future sustainable growth, improved productivity and profitability, and ultimately survival in a highly competitive digital age.

As an example, Air NZ is currently teaming up with Swiss travel start-up company Winding Tree to explore applications based on blockchain technology that could improve the efficiency and security of services such as booking and baggage tracking. Given the nature of this innovation, it is entirely conceivable that these solutions, developed initially for internal use, will springboard into other unrelated applications with both internal and external uses.

On this basis Air NZ strongly submits that all software R&D expenditure that produces the desired outcomes such as increased productivity, sustainable growth and job creation, including activity that creates software developed for internal use, should be eligible expenditure in terms of the policy of the proposed regime. Further, it is submitted that any separate and lower cap on the

amount of expenditure for software development is contradictory to the policy aim of the regime, particularly in the digital age.

Summary

We submit that Air NZ (and similar publicly listed companies where the Crown is an ordinary shareholder) should be eligible for the R&D tax credit (as it was under the 2008 regime), and that the Government needs to clarify this position, for the following reasons:

i. The company is a publicly listed company operating in the private sector;
ii. The company is not funded by the Crown;
iii. Making the company ineligible for the R&D tax credit is an unfair competitive disadvantage for the company and its public shareholders when compared to other market participants (including foreign owned entities and competitors undertaking R&D in New Zealand). The targeted exclusion offends the basic tax policy principles of coherence, fairness and horizontal equity; and
iv. The company is undertaking the type of innovation and R&D that is consistent with the Government's objectives and that the proposed regime seeks to encourage, and eligibility to receive R&D tax credits will increase the company's R&D activity.

Further we submit that any exclusion, or separate and lower cap, for the amount of eligible expenditure for internally developed software is contradictory to the policy aim of the proposed regime, particularly in the digital age.

Please contact Helen Day on 021 724 991 if you wish to discuss any aspect of this submission.

Kind regards

s 9(2)(a)

s 9(2)(a)

Submission to:

Ministry of Business, Innovation and Employment
Email: RDincentive@mbie.govt.nz

Fuelling Innovation to Transform our Economy

A discussion paper on a Research and Development Tax Incentive for New Zealand

New Zealand Forest Owners Association Inc
Level 9, 93 The Terrace
Wellington 6143
Tel 04 473 4769

www.nzfoa.org.nz

31 May 2018

Introduction

1. The New Zealand Forest Owners Association Incorporated (FOA) is the representative membership body for the commercial plantation forest growing industry. FOA members are responsible for the management of approximately 1.2 million hectares of New Zealand's plantation forests and more than two-thirds of the annual harvest.

2. Investment by the industry in research and technology fosters innovation in the plantation forestry sector. This is reflected in the commitment of the FOA and its members to the highest standards of sustainable silviculture, environmental practice and workforce safety.

3. FOA also provides secretariat services to the Forest Growers Levy Trust, a body established to administer the Harvested Wood Products Levy. The levy applies to commercial timber species and is paid at the time of harvest by all forest owners. In 2018 the Forest Growers Levy Trust is allocating approximately 60% ($5.5 million) of the levy to research and development programmes that are organised and funded for the benefit of all NZ forest growers. Substantial industry investment (approximately $1.5 million per annum) into research focussed on phytosanitary options has also been made by the forest growers via a voluntary levy on log fumigant products.

4. FOA is submitting on behalf of our national membership and on behalf of those forest owners who pay the Harvested Wood Products Levy.

Comments on the Research and Development Tax Incentive Proposal

5. The FOA are supportive in principle of the proposed tax incentive for research and development as a way of encouraging greater investment in research and development in New Zealand.

6. Forest owners have a long history of investing directly in research and development alongside government investment and the commercial forest industry New Zealand has today is built on this research effort dating back over many decades.

7. Because of the long-term nature of forest research and the common issues and challenges faced by forest owners, the majority of forest growing sector research is undertaken cooperatively. One of the main reasons for forest growers introducing a levy in 2013 was to improve the funding of research and development, to spread the load across all forest growers and to provide greater funding stability for research and other industry good activities. A collaborative approach also enables the sector to leverage limited expertise across the wider sector for the benefit of all forest owners rather than just a few. The industry does this willingly.

8. Industry research funded by the Forest Growers Levy Trust is almost entirely contracted to universities and crown research institutes and meets the criteria of R&D activity as defined in the discussion paper. The discussion paper also identifies "industry cooperatives (including levy bodies) that receive contributions or levy payments for the purpose of R&D will be eligible for the Tax Incentive"

9. However, these industry cooperatives and levy bodies are generally structured as not for profit organisations because they are set up to facilitate the funding, organisation and dissemination of research outputs for the benefit of the wider industry. Because the proposed tax incentive will provide a tax credit, these bodies will not be able to access the tax credit as it is currently proposed.

10. Our concern is that this will put at risk the model for collective or collaborative research that is common across the primary sector and was one of the significant reasons why the forest growing sector implemented the Harvested Wood Products Levy in 2013. The risk is that those wishing to avail themselves of the tax relief will channel funds away from collaborative research through the levy system and into private consortia.

11. A suggested solution is that industry bodies collecting sector funding that is applied to eligible research provide evidence of the research undertaken and the proportion of total funding received that is applied to research. This would be provided to those paying the levy or grant so that they are then able to claim the tax incentive through their own business activity. Or alternatively, and possibly more practically, that the levy body is provided the equivalent level of support that would have been claimed if it was undertaken through an alternate mechanism

Our Submission

12. The FOA, on behalf its members and those forest owners paying the Harvested Wood Products levy , seeks the inclusion of a mechanism whereby those paying levies or grants to not for profit collaborative or cooperative industry bodies are able to claim that portion of the grant or levy utilised for eligible research activity as a tax credit.

Note on making this submission public

13. The FOA is happy for this submission to be made public.

s 9(2)(a)

R&D Tax Incentive Team
Ministry of Business, Innovation & Employment
Wellington
By email: RDincentive@mbie.govt.nz

Friday 1 June, 2018

LETTER OF SUPPORT: RESEARCH AND DEVELOPMENT TAX INCENTIVE DISCUSSION DOCUMENT

Business Central writes to express our support for ExportNZ, ManufacturingNZ and BusinessNZ's submissions on the Research and Development Tax Incentive consultation. Business Central welcomes the opportunity to submit on the R&D Tax Incentive Discussion Document.

Business Central represents business interests throughout central New Zealand from Taranaki across to Gisborne and down to Nelson. Business Central is one of the four regional organisations comprising New Zealand's peak business advocacy group, BusinessNZ. In Wellington, our organisation operates the Wellington Chamber of Commerce, accredited to the New Zealand Chamber of Commerce network. Our organisation also delivers ExportNZ to Wellington and the Hawke's Bay.

Business Central supports ExportNZ, ManufacturingNZ, and BusinessNZ's submission to the Ministry of Business, Innovation and Employment and wholly endorses these organisation's comments.

This letter of support doesn't seek to necessarily comment specifically on each question asked in the discussion document. However we do wish to raise issues we know businesses are particularly concerned with.

PROPOSAL

The Government is proposing a system of 12.5% tax refunds on company investment in R&D for expenditure over $100,000 a year. The system would work in tandem with the R&D grants administered by Callaghan Innovation, and would replace the current Callaghan Growth Grants. There are pros and cons from moving away from Growth Grants to an R & D tax credit.

It is of the real importance that we look at how this can best benefit industry and move towards a higher-innovation economy. There's no question that New Zealand has got to improve our share of R&D - currently it's 1.28 percent of GDP, compared to an OECD average of 2.38 per cent.

But of course it's always a question of what we do and how we do it. We need to make sure whether a tax incentive system would be easier or harder to navigate than the current system of Growth Grants, especially for small to medium sized businesses.

Feedback that ExportNZ and ManufacturingNZ have received from their Chief Technology Officers Group (CTO) is that many were happy with the current scheme and it was contributing significantly to their ability to increase investment in R & D. It is worth noting the things that the CTO collectively liked about the scheme in case some of the elements can be replicated in the R & D tax credit scheme.

- Low transaction cost to participate in the Growth Grant scheme. Once you met the criteria there was little administrative complexity to contend with.
- Essentially pre-approval of what you would be reimbursed for – along with regular payments which is good for cash-flow. So, good predictability and good cash-flow.

It could also be argued that the larger companies that were eligible for growth grants had the greater commercialisation potential. That said, MBIE statistics indicate that we have less R & D occurring in some of our larger firms than is the case internationally and that our small to medium size firms are quite R & D intensive as a proportion of their turn-over. As the ExportNZ and ManufacturingNZ points out, if this is the case – how do we get these larger firms to intensify their R & D – and if they were not going for Growth Grants, will the tax credit be the incentive they need? It could be, in that some of them were not eligible for Growth Grants – due to the 1.5% of revenue they needed to invest in R & D.

On the con side of Growth Grants, there were a lot of firms doing good R & D or with good R & D potential that were not eligible for support. A tax credit scheme moves away from "picking winners" and spreads the incentive more widely.

We believe the question needs to be asked, whether at 12.5% this tax incentive will be enough to shift the dial and be transformational for the New Zealand economy. Australian tax credits are significantly higher for the SME's – but we also appreciate that if we want simplicity then having a two track approach to large and small firms would increase complexity.

On balance – we would agree with the ExportNZ and ManufacturingNZ submission, that this new approach (R & D tax credits, plus the retention of Project Grants) should be pursued, but aim for a higher rate than 12.5%.

Other issues raised by ExportNZ, ManufacturingNZ and BusinessNZ we wish to draw to your attention to include:

- We do not feel that **excluding 'activities involved in complying with statutory requirements or standards'** would support development, as development regarding

standards was necessary to ensure quality control but can be substantive in the R&D sense. Additionally, a substantial amount of development goes into 'pre-production activities, such as demonstration of commercial viability, tooling-up and trial runs' – exclusion would cut out qualification for an area that companies can invest a lot into developing.

- While we appreciate the stance taken regarding **dual purpose activities** – namely an R&D tax credit would be better targeted if it applies to an activity conducted solely for an R&D purpose – we endorse BusinessNZ's point and strongly urge caution here. In almost all situations, a business will undertake R&D for the purpose of making income as businesses are generally not narrowly defined within just the research space. They have to continuously be nimble enough to look for opportunities in the market whereby R&D is undertaken with the end purpose of commercializing their work. Therefore, to solely apply it to pure R&D purposes only without the other purpose of commercialisation would greatly inhibit almost all businesses from applying.

- As with BusinessNZ, in principle, we agree that **R&D costs incurred overseas** should be eligible for the concession for up to a certain percentage of the total cost of the project if the overseas work is part of an R&D project based in New Zealand and at least half the R&D expenditure within a project is for activities carried out in New Zealand. Overall, we view this as a pragmatic outcome, and we supported a similar stance taken in 2007 given it would be idealistic to think New Zealand can undertake everything. As noted in the paper, New Zealand may not have complete capability to do the work locally, so foreign R&D jurisdiction requirements and customisation of a product for a particular market may need to take place in that market.

- However, a key question is whether the percentage value of 10% as outlined in the Discussion Document is realistic enough in today's global environment? While we appreciate the fact that we do not want a situation where almost all the R&D is done offshore, at the same time we also do not want to see missed opportunities because of the restrictive nature of the 10% limit, thus creating some form of silo mentality when it comes to R&D activity in New Zealand. Therefore, if there are sufficient practical reasons outlined by other submitters that this should be more than 10%, we do not have any significant concerns about this being increased.

- The discussion document, while providing some guidance on the overall intention of the tax incentive scheme, does leave some **vast grey areas in which businesses are concerned around what is to be eligible and what isn't**. We believe it would be useful for the government agencies working on this project to provide some guidance on self-assessment in order to ensure those applying for the scheme will be compliant with regulation.

- Given the current grants are drip fed throughout the year, many of the companies currently receiving grants will be reliant on them to **ensure cash-flow for their current**

R&D projects. We believe this needs to be considered in terms of assisting businesses with the transition to the tax credit system.

- In principle, we agree with the intent of the overall move to tax incentives, in that it will reach more companies and encourage investment in more R&D. However, the risk is in the implementation of the system, the **compliance costs and time** put into applications would be unconducive to the intent of the change. We see it as essential that pre-approvals are in place as soon as possible.

Yours sincerely,

s 9(2)(a)

R&D Tax Incentive Team
Ministry of Business, Innovation & Employment
Wellington
By email: RDincentive@mbie.govt.nz

Friday 1 June, 2018

LETTER OF SUPPORT: RESEARCH AND DEVELOPMENT TAX INCENTIVE DISCUSSION DOCUMENT

The Wellington Chamber of Commerce (The Chamber) writes to express our support for ExportNZ, ManufacturingNZ and BusinessNZ's submissions on the Research and Development Tax Incentive consultation. The Chamber welcomes the opportunity to submit on the R&D Tax Incentive Discussion Document.

The Chamber has been the voice of business in the Wellington region for 161 years since 1856 and advocates policies that reflect the interests of the business community in both the city and region, and the development of the region's economy as a whole. The Chamber advocates the views of its members and obtains that view through regularly surveying members.

We are a business membership association, representing 3,400 members and their interests throughout the Wellington region, as well as being one of the four regional organisations comprising New Zealand's peak business advocacy group, BusinessNZ. In Wellington, our organisation operates the Wellington Chamber of Commerce, accredited to the New Zealand Chamber of Commerce network. Our organisation also delivers ExportNZ to Wellington, the Hawke's Bay and the Central region.

The Chamber supports ExportNZ, ManufacturingNZ, and BusinessNZ's submission to the Ministry of Business, Innovation and Employment and wholly endorses these organisation's comments.

This letter of support doesn't seek to necessarily comment specifically on each question asked in the discussion document. However we do wish to raise issues we know businesses are particularly concerned with.

PROPOSAL

The Government is proposing a system of 12.5% tax refunds on company investment in R&D for expenditure over $100,000 a year. The system would work in tandem with the R&D grants

administered by Callaghan Innovation, and would replace the current Callaghan Growth Grants. There are pros and cons from moving away from Growth Grants to an R & D tax credit.

It is of the real importance that we look at how this can best benefit industry and move towards a higher-innovation economy. There's no question that New Zealand has got to improve our share of R&D - currently it's 1.28 percent of GDP, compared to an OECD average of 2.38 per cent.

But of course it's always a question of what we do and how we do it. We need to make sure whether a tax incentive system would be easier or harder to navigate than the current system of Growth Grants, especially for small to medium sized businesses.

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On the con side of Growth Grants, there were a lot of firms doing good R & D or with good R & D potential that were not eligible for support. A tax credit scheme moves away from "picking winners" and spreads the incentive more widely.

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On balance – we would agree with the ExportNZ and ManufacturingNZ submission, that this new approach (R & D tax credits, plus the retention of Project Grants) should be pursued, but aim for a higher rate than 12.5%.

Other issues raised by ExportNZ, ManufacturingNZ and BusinessNZ we wish to draw to your attention to include:

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- While we appreciate the stance taken regarding **dual purpose activities** – namely an R&D tax credit would be better targeted if it applies to an activity conducted solely for an R&D purpose – we endorse BusinessNZ's point and strongly urge caution here. In almost all situations, a business will undertake R&D for the purpose of making income as businesses are generally not narrowly defined within just the research space. They have to continuously be nimble enough to look for opportunities in the market whereby R&D is undertaken with the end purpose of commercializing their work. Therefore, to solely apply it to pure R&D purposes only without the other purpose of commercialisation would greatly inhibit almost all businesses from applying.

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- However, a key question is whether the percentage value of 10% as outlined in the Discussion Document is realistic enough in today's global environment? While we appreciate the fact that we do not want a situation where almost all the R&D is done offshore, at the same time we also do not want to see missed opportunities because of the restrictive nature of the 10% limit, thus creating some form of silo mentality when it comes to R&D activity in New Zealand. Therefore, if there are sufficient practical reasons outlined by other submitters that this should be more than 10%, we do not have any significant concerns about this being increased.

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- Given the current grants are drip fed throughout the year, many of the companies currently receiving grants will be reliant on them to **ensure cash-flow for their current R&D projects**. We believe this needs to be considered in terms of assisting businesses with the transition to the tax credit system.

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Yours sincerely,

s 9(2)(a)

From: s 9(2)(a)
To: RD Incentive
Cc: s 9(2)(a)
Subject: Research and Development Incentive - Submission
Date: Friday, 1 June 2018 8:33:17 a.m.
Attachments: s 9(2)(a)

Thank you for the opportunity to submit on the proposed R&D tax incentive. We address the specific discussion questions we have a view on below.

Question 1: Exclusion of SOES, subsidiaries etc.

We do not believe SOES etc should be excluded from the R&D tax incentive. We are a limited partnership, owned 50% by Landcorp Pastoral Limited (Landcorp) and 50% through private New Zealand investors. Landcorp is a service provider, and involved in the management of the limited partnership through the general partner. The relationship with Landcorp and management contribution are on arms length, commercial terms as with any other commercial relationship, and draws on the farming expertise of Landcorp. Landcorp and other such government entities are often the primary experts in their field, and so we are concerned that the exclusion proposed would restrict the range of commercial structures open to those working with such entities (including our current structure) and diminish the build up and dissemination of skills in the commercial sector.

Question 2: Application of the R&D definition.

We are concerned that the focus appears to be on research to the exclusion of development of applications . Understanding and applying research to develop new or improve existing technologies is an equally valuable skill, and still ensures understanding of new research is developed in employees.

Question 5: Materiality.

The application of a materiality test to the advancement leg of the proposed definition would create significant uncertainty, especially when the materiality of the impact may well not be known for some time.

Question 9: Exclusions.

The exclusion of dual purpose activities is concerning as, for example, a production run may be undertaken to test the behaviour and properties of a new material and also test commercial viability of the production. We would prefer a primary purpose consideration.

Question 10: Restriction to Labour Cost.

Limiting eligible expenditure to labour costs excludes a significant portion of our research costs e.g. testing, ingredients and leasing equipment for research.

Regards

s 9(2)(a)

s 9(2)(a)

SPRING SHEEP
— MILK CO. —
New Zealand

SPRING SHEEP MILK CO.
WHERESCAPE TOWERS, LEVEL 4, 38 WYNDHAM STREET, AUCKLAND 1010
PO BOX 91129, VICTORIA ST WEST, AUCKLAND 1142, NEW ZEALAND.
SPRINGSHEEPNZ.COM

From: Tom McLeod
To: RD Incentive
Subject: Re: Save New Zealand"s knowledge economy [UNCLASSIFIED]
Date: Friday, 1 June 2018 7:24:09 a.m.

To Whom It May Concern

I understand that the government's R&D position is to not pick winners?

How successful would our hospital system be if we did not pick and train the best doctors.
How successful would our All Blacks be if we did not pick winners.
How successful would businesses be if they did not put more money into their most successful fastest growing products.

Stats:
MBIE's stats show that companies with 50+ employees are 70% more productive and pay 30% higher wages than smaller companies.
A Professor from MIT Boston once told me that 00.04% of all companies will generate 97% of a country's wealth (exports).
Studies show that around 4% of your fastest growing companies will create 60% of your jobs.
A study by GP Bloodhound found that it took $200 million in capital to scale a company to become a billion dollar plus business.

NZ has early stage venture capital but no later stage ($20 million +) to scale NZ companies. So they need to go offshore for capital and we run the risk of losing them. Or they exit early and sell a billion dollar business for $10-20 million with no enduring value created.

Government needs a program to identify our fastest growing winning firms and then back them to scale.

Callaghan Innovation used to be able to put large funding into companies to help level the playing field against bigger offshore competitors and help them scale.

s 9(2)(b)(ii) .

Has anyone at MBIE done a case study on what $11 million did for Weta Workshops and how we now have a billion dollar + movie industry?

Now I understand the most Callaghan can invest in project funding is $800K and then you will have to go to 12.5% tax grant.

NZ's needs a strategy to pick winners (back proven winners) and back them to scale instead of a strategy that funds random R&D in both Universities and Industry to create enduring value wealth.

Cheers
Tom

From: RD Incentive <RDIncentive@mbie.govt.nz>
Sent: Thursday, 31 May 2018 12:34 AM
To: RD Incentive
Subject: RE: Save New Zealand's knowledge economy [UNCLASSIFIED]

Kia ora, and thank you for your recent email to the Hon Megan Woods regarding the R&D tax incentive.

We really value hearing from people in the startup sector, as we want to ensure we get the policy right to support as many businesses as possible to lift their R&D.

We would appreciate your feedback in more detail on our proposals for the R&D tax incentive. It is really important to this process that we have a strong understanding of your concerns, and how different design options could affect your business.

Official submissions close 5pm tomorrow (1 June) on MBIE's website, so we encourage you to get in and make a submission to the questions relevant to you. Or you can respond to this email directly.

If you haven't already, have a read of the Minister's response where she addresses Toby Littin's concerns about startups and loss-making firms.

While the submission period is drawing to a close we're still keen to hear from you throughout process of designing the tax incentive, so feel free to keep in touch with us at this address.

Kind regards,
The R&D Tax Incentive Project Team

SC Bio Limited

|Microbial Solutions

R&D Tax Incentive Submission

May 31st, 2018

RDincentive@MBIE.govt.nz

R&D Tax Incentive Team
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140

Dear Sir/Madam,

R&D Tax Incentive Submission

This submission is in regards to the proposed R&D tax credit and proposal to drop the growth grants.

Background

SC Bio Ltd provides quality control method development services for life science and pharma companies and supply and support quality control reagents. We are currently developing in house manufacturing capabilities in microbiology and hope to produce products currently made overseas. We don't perform research or develop IP.

Despite not performing research we are part of the science and biotechnology industry.

Submission

No R&D Tax Incentive is necessary; I think R&D costs should be treated like a business expense.

Growth grants allow the government to award financial assistance to R&D that has been evaluated as best use of taxpayers money. This system is in the interests of NZ and continuing it allows national needs to be assessed and supported.

Kind Regards

s 9(2)(a)

SC Bio Ltd
24 Balfour Road, Parnell, Auckland
s 9(2)(a)

www.scbio.co.nz

#75

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Friday, June 01, 2018 4:49:12 PM
Last Modified:	Friday, June 01, 2018 4:58:00 PM
Time Spent:	00:08:48
IP Address:	s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals:

Name	s 9(2)(a)
Email address	

Q2 (ii) For organisations:

Name of organisation	**CarbonScape Ltd**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand?	**6 to less than 10 years**
Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners.	**10 - 19**
Q5 (v) What industry sector does your business operate in?	**C Manufacturing**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Project Grant	**2016**

Q7 (vii) Has your organisation ever received any other R&D government support?	**Yes,** If yes, please specify names of grant(s)/support.: NZTE

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?	**Respondent skipped this question**
Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?	**Respondent skipped this question**
Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?	**Respondent skipped this question**
Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?	**Respondent skipped this question**
Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?	**Respondent skipped this question**
Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.	**Respondent skipped this question**
Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?	**Respondent skipped this question**
Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.	**Respondent skipped this question**
Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.	**Respondent skipped this question**
Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.	**Respondent skipped this question**
Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.	**Respondent skipped this question**

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?	**Respondent skipped this question**
Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.	**Respondent skipped this question**
Q21 Q15 Is the minimum threshold set at the right level?	**Respondent skipped this question**
Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.	**Respondent skipped this question**
Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.	**Respondent skipped this question**
Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.	**Respondent skipped this question**
Q25 Q19 Are there any other risks that need to be managed? Please describe.	**Respondent skipped this question**
Q26 Q20 Are there risks with extending penalties to external advisors in this way?	**Respondent skipped this question**
Q27 Q21 What is the right level of information required to support a claim?	**Respondent skipped this question**
Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?	**Respondent skipped this question**
Q29 Q23 What integrity measures do you think Inland Revenue should use?	**Respondent skipped this question**
Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?	**Yes**

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

A mature but pre-revenue development company with a big hoary engineering play; a Supply Agreement with NZ Steel to substitute their fossil fuels, working with WaterCare Services to optimise Activated Carbon to further refine Auckland's water and the first Graphite producer in New Zealand, poised to be a big export earner and under the proposed plan we would have no eligibility for R&D support. Can we talk please?

#76

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Friday, June 01, 2018 11:22:48 AM
Last Modified:	Friday, June 01, 2018 4:58:29 PM
Time Spent:	05:35:41
IP Address:	s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: — **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**Jade Software Corporation Limited**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? — **10 years or more**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. — **100 or more**

Q5 (v) What industry sector does your business operate in? — **J Information media &**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

s 9(2)(b)(ii)

Q7 (vii) Has your organisation ever received any other R&D government support? — **Yes,**

If yes, please specify names of grant(s)/support.:

s 9(2)(b)(ii)

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand? — **Respondent skipped this question**

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

The definition is generally effective, noting the challenge between certainty and unintended consequences.

However, there is currently uncertainty around the potential of exclusion of R&D from dual purpose activities.

There is also uncertainty around the definition of 'commercial consideration' and the 'reasonably be expected'.

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

There is a risk that development of Intangible Assets or Intellectual Property is not clearly included.

The focus of the R&D definition has moved too strongly to the Research side, when it is the development of IP that creates future growth for NZ Inc.

In particular, the Software industry is a crucial area of economic growth for NZ and it is not clear that the development of software will be captured under the existing definition.

It is recommended that a specific development definition be added and that a sub-set clause of that definition specifically deals with the complexities of Software.

Leaving this in its current ambigious state could either lead to lower access to the R&D incentive with attendant loss of R&D opportunities, or worse claims being made which are later overturned and require repayment.

For start-up business operations/products these are the little $ differences that can be make or break.

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Note comment above, the R&D on IP and Intangibles is a key inclusion.

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

Respondent skipped this question

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Respondent skipped this question

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

Respondent skipped this question

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

There is an advantage in simplicity for claiming, but it means that a significant component of cost including professional advice, management support and general overhead components will not be supported. This reduces the likelihood of the incentive actually promoting R&D effort that would otherwise be

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

The percentage basis is a much simpler administration approach and avoids the ability to "game" numbers.

This may provide some skewing of incentive towards industries with higher paid resources (arguably less in need of incentivisation).

There is a risk the % amount is set too low to adequately reflect the true cost of engaging in the R&D activity, which also reduces the incentive available.

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

The currently "reasonably be expected" clause is too loose. Any IP asset should reasonably be expected to receive commercial return at some stage in it's lifecycle, but that period is often long enough away that the R&D incentive is needed to make it commercially sensible to invest. The definition of timing, and what commercial consideration means need substantial tightening.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Pre-accreditation

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

The business start-up and equity raising cycles in software product businesses means continuity rules would be have negative impacts on start-up business.

Q21 Q15 Is the minimum threshold set at the right level? **Yes**

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details. **Respondent skipped this question**

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

A number of businesses in early R&D processes, or risky industries will be tax loss making or have significant carry forward of tax losses. On that basis, a tax credit has no immediate benefit and will not incentivise or support R&D activity.

It is suggested that a number of entities the R&D incentive is designed to assist will be in this position, which means the expected gains from the scheme will be lost.

It is recommended that a cash back or grant scheme be implemented to support businesses in this position.

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

Respondent skipped this question

Q25 Q19 Are there any other risks that need to be managed? Please describe.

Respondent skipped this question

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

There are sufficient uncertainties in the definitions and transition process that mean there is a likely variance in approaches by businesses. Putting the onerous tax penalty regime across such an immature legislation could result in highly punitive impacts from genuine differences of interpretation.

Q27 Q21 What is the right level of information required to support a claim?

A focus on simplicity and ease of administration. The % allocation on top of labour costs would lesson administration efforts.

It is important that there is 'one version of the truth' in accounting preparation and therefore it is strongly recommended that calculation be consistent with IFRS and tax approaches already in place.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

Respondent skipped this question

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,
Contact details:
Ben O'Grady CFO Jade Software Corporation Mobile: +64 27 248 7298 Email: bogrady@jadeworld.com

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

IMPUTATION CREDIT ALLOCATION
The payment of the credit through the Imputation Credit Account has a significant impact on offshore shareholders who may not have the ability to utilise the credits.

The use of a credit to the Imputation Credit account, also creates a benefit for the shareholder not the business itself. That benefit only occurs when dividends are paid which in growth businesses may be many years in the future. This timing impact has the potential to dramatically reduce the efficacy of the R&D incentive scheme.

There is also the risk that decision makers at Board and Management levels see no benefit to the business itself which results in another disincentive.

It is recommended that the tax credit have literal cashback or specific cash cost reduction for the businesses involved.

FOREIGN OWNED ENTITIES
There is a risk that foreign owned entities are impacted by the change from Callaghan Growth Grants. They may be currently eligible for current Growth Grants because they create significant IP assets held in NZ, with funds flow back to NZ and employment of large NZ R&D teams which build world class knowledge in NZ.

The tax credit regime as a result of credits going to the imputation credit account, particularly for loss making entities could result in no incentive being gained in NZ. This is a significant value loss from existing R&D incentives.

12.5% Credit Incentive
It is noted that the 12.5% credit incentive is a significant reduction on the 20% available to existing Growth Grant participants. The 12.5% is a maximum position with tax impacts and R&D definitions, and cost definitions (including proposed labour cost only basis) making it highly likely that the overall incentive to businesses will be a substantial reduction on that currently available. It is strongly suggested that such a low level complex rebate will not drive R&D behaviours.

#77

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Friday, June 01, 2018 4:41:10 PM
Last Modified:	Friday, June 01, 2018 5:16:30 PM
Time Spent:	00:35:20
IP Address:	s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**DROPIT Limited**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? **2 to less than 6 years**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. **1 - 5**

Q5 (v) What industry sector does your business operate in? **S Other services**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2017**

Q7 (vii) Has your organisation ever received any other R&D government support? **No**

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?

We believe that the impact will be detrimental to all New Zealanders. There will be less innovation in NZ companies and less young NZers will be interested in innovative pursuits. We believe that this will cause significant negative impacts on growth of NZ exports.

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

We believe that the definition is too narrow and needs further discussion.

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

Yes, refer to Q2.

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Yes, refer to Q2.

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

The impact would be that areas of research that are not considered to be problems currently would be overlooked.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Yes, research into the arts, being creative arts. We believe that the basis of innovation can have a direct correlation to innovation and should be included e.g. DROPIT is a combination of creative thinking, which is applied by technological research and development and brought to market by software development.

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Does not apply to us.

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

R&D projects need to be supported by support staff and researchers will require somewhere to work.

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

R&D teams require administrative support to be able to effectively undertake their work and deliver results. There are not enough government-funded co-working spaces to fulfil these needs.

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

See Q10.

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Respondent skipped this question

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

It does not adequately capture R&D software activities because, in many cases, the building blocks of many technological developments need to be created using existing systems.

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Yes, this will eliminate over 80% of startup businesses who will not be spending the thresh-hold who will need that funding in their first year.

Q21 Q15 Is the minimum threshold set at the right level?

No,
If 'no', please provide further details.:
$50,000 is more appropriate.

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

We do not think the cap is anywhere near enough to support the types of globally-significant R&D projects that NZ businesses could undertake e.g. developing a space industry off the back of the success of Rocket Labs.

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

Respondent skipped this question

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

That information is still commercially sensitive, even after a two-year period, especially as we are competing in global markets.

Q25 Q19 Are there any other risks that need to be managed? Please describe.

Respondent skipped this question

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

We believe that the current standards are sufficient.

Q27 Q21 What is the right level of information required to support a claim?

We believe that the proposed administration will involve too many government departments and cost too much to administer and should be reviewed.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

We believe that this would add an unnecessary extra layer to the claim process and will cost significantly more money to administer, police, and implement. IRD should be able to streamline this process themselves.

Q29 Q23 What integrity measures do you think Inland Revenue should use?

As per Q22, Inland Revenue should look at ways to develop the software themselves and look to reduce as many processes as possible.

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,

Contact details:

s 9(2)(a)

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

We support the current Callaghan Innovation program and believe that the current program should be maintained and expanded upon.

#46

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Friday, June 01, 2018 3:11:53 PM
Last Modified:	Friday, June 01, 2018 5:29:04 PM
Time Spent:	02:17:11
IP Address:	s 9(2)(a)

Page 2

Q1 (i) For individuals — **Respondent skipped this question**

Q2 (ii) For organisations

Name of organisation	**DROPIT Limited**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? — **2 to less than 6 years**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand? Please include full-time and part-time employees but do not include contractors or the business owners. — **1 – 5**

Q5 (v) What industry sector does your business operate in? — **Other services**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2017**

Q7 (vii) Has your organisation ever received any other R&D government support? — **No**

Q8 How likely is it that your organisation will be in a position to use the full amount of an R&D tax credit in the 2019/20 tax year? (Note, to use the full amount of a R&D tax credit in a given year, your business' tax liability needs to be at least as large of the R&D tax credit you are entitled to claim.) — **Very likely**

Q9 How much R&D does your organisation expect to carry out in the coming year? — s 9(2)(b)(ii)

Page 3: Responses to questions in the consultation document

Q10 Q1 What impact will the proposed transition arrangements have on your business? For example, your cash-flow or internal reporting mechanisms? Please describe.

It will be very disruptive to our business from an internal reporting mechanisms perspective and also we believe that the Callaghan Innovation system is far superior for early to medium-stage startups as ourselves. The R&D tax incentive program will be unattainable for a lot of startups and will hinder R&D activities for current and future generations of New Zealanders.

Q11 Q2 What do you believe to be a necessary transitional period? Please explain the reasons why this is necessary for your business?

We believe that two full financial years would be better than the proposed.

Q12 Q3 What impact will the proposed transition arrangements have on your R&D programme over the next few years?

It will make us reconsider the amount of R&D people that we hire in NZ and the Callaghan Innovation grants have allowed us to hire people in NZ. We are passionate to support growth in NZ and jobs, and support training NZers to pass on their skills and experience in NZ. The realities of business means that we need to keep costs down and the proposed change would mean that we would need to hire offshore talent, which we do not want to be forced into doing.

Q13 Q4 Please provide any other comments about the proposed transition arrangements.

We are not in support of a transition and we will support Callaghan Innovation up until the time that the final decision is made.

Q14 Q5 For businesses in tax loss, what impact will the proposed temporary grant have on your business during the transition process? Please describe.

It will have significant financial burden where (as said in Q3) we would be forced to hire R&D staff in other countries which we are strongly opposed to doing. If this initiative is implemented, it will cost NZ-based jobs and reduce opportunities for NZ to excel on the world stage in innovation and is a step in the wrong direction.

#8

COMPLETE

Collector: Web Link 1 (Web Link)
Started: Wednesday, May 30, 2018 8:39:14 AM
Last Modified: Wednesday, May 30, 2018 2:42:04 PM
Time Spent: 06:02:49
IP Address: s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**Jackson Electrical**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? **10 years or more**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. **50 - 99**

Q5 (v) What industry sector does your business operate in? **C Manufacturing**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2015**

Q7 (vii) Has your organisation ever received any other R&D government support? **Yes,**
If yes, please specify names of grant(s)/support.:
Callaghan student grant

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?

This question could be read in two ways. Firstly, is it asking what the impact would be if these particular entities cannot claim, even if we are not working directly with them, if so there wouldn't be an impact on our business. The other way this question could read is if we were working with a tertiary institution, which has happened in the past. If it is the latter than it would impact us if they were to claim as well as us, this would potentially be perceived as double dipping, this wouldn't be an issue if they were excluded.

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

We would suggest that the definition includes both (a) & (b), so rather than "OR" that it be "AND/OR"

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

No comment

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

No comment

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

This would be an issue, R&D can be around expanding on existing knowledge to create a new or tangential product that needs to be manufactured, this process is also R&D. Materiality test would narrow a project.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Market research, market testing & market development come under support activities and should be included, these techniques could be used to ensure the products are fit for purpose, also there could be technical aspects of market research.
Pre-production activities - this activity should be considered R&D, for example, when you do a trial run, it could still fail at this point and could require further development.

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

No comment

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

If the activity cannot be clearly split out to identify the R&D vs non R&D then business as usual expenses shouldn't be eligible

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

This would be a disadvantage as you are not capturing all of the R&D costs. This would exclude the claiming of materials and machine costs which are covered by the current growth grant. Waste of materials is a cost/risk to the company when performing R&D.

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

We do this currently when calculating the rate for staff hours claimed and believe it is an advantage as R&D uses space/ resources etc so is captured by the overhead portion

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

No, not if you are being paid by a customer.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

If you are developing/modifying software for a unique need, you don't know the outcome and it can be high risk

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

No comment

Q21 Q15 Is the minimum threshold set at the right level? **Yes**

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

There should be a cap, however if there is a clear process, e.g. ministerial discretion, to exceed it in a small number of situations then this would still be advantageous to appropriate NZ businesses. There just needs to be a clear description on when this can happen

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

No comment

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

We understand names are already published, however it is important to have wide bands to ensure some privacy around costs/profit. The evaluation within the short term (following the transition) is not clearly detailed, however it is important to ensure businesses are successfully capturing the relevant data as this was one of our biggest challenges. It would be helpful to identify any problems early on.

#10

COMPLETE

Collector: Web Link 1 (Web Link)
Started: Wednesday, May 30, 2018 10:24:09 AM
Last Modified: Wednesday, May 30, 2018 2:58:38 PM
Time Spent: 04:34:28
IP Address: s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals:

Name	s 9(2)(a)
Email address	s 9(2)(a)

Q2 (ii) For organisations: **Respondent skipped this question**

Q3 (iii) How long has your business been operating in New Zealand? **Respondent skipped this question**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. **Respondent skipped this question**

Q5 (v) What industry sector does your business operate in? **Respondent skipped this question**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant? **Respondent skipped this question**

Q7 (vii) Has your organisation ever received any other R&D government support? **Respondent skipped this question**

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?

The impact is likely to be negligible and this is a good decision. However, I suggest the inclusion of payments by businesses to SOEs, CRIs, DHBs, Tertiary Institutions and their subsidiaries. This has a number of key benefits, but to name only two: 1) the strength of business partnerships with research bodies leads to great innovations and high conversion rates to marketable technologies; and 2) businesses should encouraged in to funding these bodies which will overall decrease the level of funding required by the Government for such R&D projects.

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

The definition is great and should be used.

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

Respondent skipped this question

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

This will depend on the definition and assessment of the scientific method. One possible exclusion is large-scale projects where the scientific method is not feasible due to the impracticality and high-cost of trials. For example, if a business making rockets for launching satellites considers a launch to be R&D because the data collected with resolve scientific or technological uncertainty, it can not feasibly launch multiple rockets in a controlled experiment to test fuel blends. Rather, it might launch one rocket and seek to analyse the performance of the fuel blend (e.g. burn temperature, power, etc.). If this type of test is excluded under the prerequisite for a scientific method, then the definition is incorrect because this R&D work is valuable. Business R&D is almost always of a more ad-hoc and trial and error basis than R&D in a research institution. This should be encouraged by the definition as it is no less important (and possibly more important) for the ultimate goal of economic and social progression through innovation than controlled experimentation.

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

The materiality requirement is good, but must be well defined in guidance and legislation. The materiality of an agricultural problem/advancement (e.g. crop yield) can not be easily compared with the materiality of a computer science problem (e.g. data processing speed). It will be important for MBIE to clearly define who or what decides on materiality using specific examples.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

No. This definition should also extend to exclude animal testing (even when carried out overseas).

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

Dual purpose activities should definitely be eligible for the R&D Tax Incentive. The reclassifying of expenditure and business as usual issues identified by the Government and referred to as dual purpose activities is a misnomer. Businesses often and almost always undertake their R&D as part of wider business projects. For example: 1) data scientists will design faster systems for big clients; or, 2) engineers will design earthquake-mitigating buildings for specific projects. To exclude these activities is very wrong as their being dual purpose has no impact on whether or not the business was seeking to resolve scientific or technological uncertainty, and was bearing an economic risk in doing so. The scheme should in fact incentivise and reward businesses who undertake R&D for dual purposes. MBIE should understand that business driven R&D is not all or nothing (100% investment in activities or no project). Rather, businesses might take a risk on a structure which is 10% stronger or produces 5% lower CO2, invest in this as part of a wider project, yet all the while know that the project will be completed regardless of the success of the R&D activities. I strongly oppose the exclusion of dual purpose activities.

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

Limiting R&D expenditure to R&D labour costs has major disadvantages. Put simply, an R&D project is not limited to R&D labour costs. Consider the costs of materials, tools (where these are not capital expenditure), third parties, utilities, software and research institutes to name a few. These are all costs associated with conducting R&D and there is no reason why these would be excluded.

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

The advantage is simplification. The disadvantage is that this is not a fair reflection. For example, a factory might burn a kiln at high temperatures for an R&D project. This uses a large amount of energy and has a high cost, but as energy is considered an overhead there is risk that the expenditure would not be covered by the R&D Tax Incentive.

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Yes, there is every reason why this should be considered. As mentioned in Q9, a business almost always conducts R&D for a primarily commercial reason which by definition means it will be seeking to gain through commercial consideration. Therefore, excluding R&D for commercial consideration is incorrect.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Respondent skipped this question

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Respondent skipped this question

Q21 Q15 Is the minimum threshold set at the right level?	**No,** If 'no', please provide further details.: The minimum threshold of $100,000 dramatically favours big business and is inconsistent with may NZ start up businesses. The scheme should favour 'the little guys' tinkering away in a garage as much and if not more than big business. A quick look at the start-up culture in New Zealand (see Idealog Magazine for examples) shows businesses which are innovative, disruptive and overall good for the economy which would be below this threshold and so would not benefit from new legislation. Take also for example a viticulturist or winery. The business conducts R&D when the wine makers / owners invest in a new growing process for a unique grape for one of their lots. Assuming (as is common in NZ) the viticulturists are the owner so only incur non-labour costs, this could cost less than $100,000 but should definitely be qualifying for the scheme. This threshold also discounts R&D expenditure which does not follow a financial year. For example, an experiment which requires $100,000 of investment of 3 years (again consider an agricultural science) would not be eligible which is plainly wrong. If the threshold must be imposed at $100,000, it should at worst be for the project, and not confined to a time period. More practically, a threshold of around $20,000 in eligible expenditure (see UK R&D Tax, Australian R&D Tax) would be beneficial to many kiwi businesses.
Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.	**Respondent skipped this question**
Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.	**Respondent skipped this question**
Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.	**Respondent skipped this question**
Q25 Q19 Are there any other risks that need to be managed? Please describe.	**Respondent skipped this question**

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

Yes there are high risks associated with this. Advisors are exactly that - they offer advice to a company for a fee. A company is never legally bound to take that advice in any business model that I have seen. This is a negative approach for MBIE and the Government to take towards advisory businesses whose aim is to help R&D businesses by delivering value and eliminating an administrative burden. Rather, they should work with advisors to create an environment of understanding and relationships with integrity. Overseas R&D Tax schemes do have rogue operators who push the boundaries and intently falsify claims. This is often a case of poor planning and policing by administrative authorities, but in my experience is more commonly companies who refuse the advice offered to them. As a metaphor, extending penalties to advisors is similar to extending prison sentences to the parents, friends and mentors of offenders.

Q27 Q21 What is the right level of information required to support a claim?

Claims should be supported by: 1) a narrative report of R&D which provides examples information on the background, experimentation or scientific method, scientific or technological uncertainty, and results of R&D activities; 2) full financial figures supported by financial reasoning (i.e. how these figures were calculated); and, 3) supplementary information such as details of the professionals involved in the claim preparation. Preparing compliance information to support an R&D claim should not become an overhead burden for a business, especially for technical experts.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

Respondent skipped this question

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,

Contact details:

s 9(2)(a)

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

Respondent skipped this question

#11

COMPLETE

Collector: Web Link 1 (Web Link)
Started: Wednesday, May 30, 2018 3:29:48 PM
Last Modified: Wednesday, May 30, 2018 3:48:15 PM
Time Spent: 00:18:27
IP Address: s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**Ākina Foundation**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? **6 to less than 10 years**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. **20 - 49**

Q5 (v) What industry sector does your business operate in? **M Professional, scientific, & technical**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Project Grant	**None**
R&D Growth Grant	**None**

Q7 (vii) Has your organisation ever received any other R&D government support? **No**

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand? **Respondent skipped this question**

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?	**Respondent skipped this question**
Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?	**Respondent skipped this question**
Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?	**Respondent skipped this question**
Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?	**Respondent skipped this question**
Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.	**Respondent skipped this question**
Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?	**Respondent skipped this question**
Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.	**Respondent skipped this question**
Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.	**Respondent skipped this question**
Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.	**Respondent skipped this question**
Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.	**Respondent skipped this question**
Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?	**Respondent skipped this question**
Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.	**Respondent skipped this question**

Q21 Q15 Is the minimum threshold set at the right level?	Respondent skipped this question
Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.	Respondent skipped this question
Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.	Respondent skipped this question
Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.	Respondent skipped this question
Q25 Q19 Are there any other risks that need to be managed? Please describe.	Respondent skipped this question
Q26 Q20 Are there risks with extending penalties to external advisors in this way?	Respondent skipped this question
Q27 Q21 What is the right level of information required to support a claim?	Respondent skipped this question
Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?	Respondent skipped this question
Q29 Q23 What integrity measures do you think Inland Revenue should use?	Respondent skipped this question
Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?	Respondent skipped this question

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

Social enterprises are organisations that trade for a social and/or environmental purpose. Currently, there is no legal structure specifically for social enterprises, so most need to choose between a charity or limited liability business structure, with some LLC also applying for charitable status, if their impact area met the current charitable definition.

In the case of a social enterprise that is formed as a charity, there is no tax paid, but they may still have a significant revenue stream from the selling of their goods or services to a market. Under this proposed R&D tax incentive proposal, the tax credit would not provide any benefit for the entity to invest in R&D and therefore limit their opportunity for growth, unless they were able to secure a relevant grant.

The Department of Internal Affairs has recently formed a partnership with Ākina to establish the social enterprise sector in New Zealand over the next 3 years. This will examine the need for a legal definition and/or legal structure to remove barriers for social enterprises, as well as provide data on the size and contribution of the sector.

It is Ākina's recommendation that the R&D Tax Incentive project team, work closely with this programme team to be informed by the insights gathered by this programme and understand more of the needs of the social enterprise sector.

#12

COMPLETE

Collector: Web Link 1 (Web Link)
Started: Wednesday, May 30, 2018 2:43:36 PM
Last Modified: Wednesday, May 30, 2018 4:04:26 PM
Time Spent: 01:20:50
IP Address: s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**Tidd Ross Todd Limited**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? **10 years or more**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. **100 or more**

Q5 (v) What industry sector does your business operate in? **C Manufacturing**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Project Grant	**None**
R&D Growth Grant	**None**

Q7 (vii) Has your organisation ever received any other R&D government support? **Yes,**
If yes, please specify names of grant(s)/support.:
We have just had our first Project Grant approved last week TRTOD1701

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?

Excluding SOEs etc would have a negative impact on business R&D

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

Not at all well

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

If we are to 'fuel innovation to transform our economy" then the definition should include the purpose of acquiring the new knowledge.
Australia endorses production activity to help drive R&D

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Respondent skipped this question

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

If only R&D for the advancement of science or technology is to be incentivised the impact on business is a reduction of R&D spend

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Business R&D will normally be focussed on business growth

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

Reduction

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

Respondent skipped this question

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

Major advantage of simplicity

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Business and the economy in general gain through doing things better, faster etc. With the accent being on the word doing.
Business should be incentivised to develop prototypes of a commercially viable product.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Respondent skipped this question

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Respondent skipped this question

Q21 Q15 Is the minimum threshold set at the right level?

Yes

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

Respondent skipped this question

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

Respondent skipped this question

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

Respondent skipped this question

Q25 Q19 Are there any other risks that need to be managed? Please describe.

The discussion document cites NZ's low BERD rate as part of the reason to transition to Tax incentives from the Growth Fund to grow business R&D with a threshold of $100K for eligible R&D expenditure. So how does attracting large international firms to NZ to conduct R&D here benefit business, or the economy or even improve our BERD rate?

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

Respondent skipped this question

Q27 Q21 What is the right level of information required to support a claim?

For business the answer is going to be the bare minimum, with the least interaction and requirement of input necessary to support a claim.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

Respondent skipped this question

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

While never really described as such, our business has been built on extensive R&D which was always either self-funded or paid for by the customer who requested something be done in a better way. As I noted earlier we are embarking on our first Project Grant and looking forward we can see that in the next year or two our company could reasonably expect to transition to a Growth Grant. Some quick calculations on our forward revenue projections and some ROM levels for R&D highlights that for our business, the proposed Tax Incentive would not encourage any further R&D activity. Our numbers indicate that the Tax Incentive might equal only one third of the value of what the current Growth Grant would. At that level it would be questionable for business to invest time in trying to claim R&D incentives.
The tax incentive appears to be targeted towards a wider application by business (more smaller companies) but cites the lack of R&D by larger firms. Surely the requirement is to grow NZ R&D through incentivising larger NZ companies in order that this leads to business/economy growth. An academic R&D incentive for science/technology doesn't necessarily equal growth in the economy.

#13

COMPLETE

Collector: Web Link 1 (Web Link)
Started: Wednesday, May 30, 2018 5:07:18 PM
Last Modified: Wednesday, May 30, 2018 5:23:00 PM
Time Spent: 00:15:41
IP Address: s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals:

Name	s 9(2)(a)
Email address	

Q2 (ii) For organisations:

Name of organisation	**Merlot Aero**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? — **6 to less than 10 years**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. — **50 - 99**

Q5 (v) What industry sector does your business operate in? — **M Professional, scientific, & technical**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2017**

Q7 (vii) Has your organisation ever received any other R&D government support? — **No**

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand? — **Respondent skipped this question**

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

Terribly. Surely New Zealand's main R&D product is software development. To the letter of the law, it seems like a lot of software development falls outside of the R&D definition. For example, a lot of companies so sprint releases, where you will release a minimal viable product, and then do fortnightly releases. Each release will be incrementally better - but by your definition, incremental improvements aren't R&D. It seems like your R&D definition is based on more traditional hardware type development.

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

Sprint development in software.
Almost all SaaS software companies do incremental sprint releases, not major milestone innovation releases.

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Respondent skipped this question

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

What would be the point? To not provide R&D funding to companies only serving a small market? As long as they are investing in R&D, creating jobs and innovative products, why would their need to be a certain size market? Plenty of companies provide great solutions to niche markets.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Respondent skipped this question

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

Respondent skipped this question

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

The disadvantage is that a company is investing more than just the labour cost in to R&D. We have to provide those R&D staff with a desk in an office, and with extra power, and with additional software licences etc. Why would only their labour costs be eligible? All of those costs are supporting the R&D.

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

It might work - but surely some companies have overhead costs that significantly fall outside of that percentage. Has their been feedback that this is hard for companies to manage? It's not hard to calculate this for a company - why make all companies fit inside one box?

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Yes - the fact that the company is investing in R&D that is being commercialised suggests that they are a successful innovation company. Why punish them for making an commercially viable product? By providing R&D incentives specifically for these companies, they will be investing further in more R&D, creating more jobs.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Respondent skipped this question

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Respondent skipped this question

Q21 Q15 Is the minimum threshold set at the right level?

Yes

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

I think companies need to be made aware of the liability that they are generating. A lot of companies might not see this as a liability.

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

Respondent skipped this question

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

Respondent skipped this question

Q25 Q19 Are there any other risks that need to be managed? Please describe.

Respondent skipped this question

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

Respondent skipped this question

Q27 Q21 What is the right level of information required to support a claim?

The current questions on the claim seem repetitive - like the same question is being asked in slightly different ways multiple times.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

Respondent skipped this question

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,

Contact details:

s 9(2)(a)

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

The biggest issue is the impact that this is going to have on loss making, early stage companies. The current scheme provides a huge benefit to these types of companies. The new scheme is only going to be beneficial for profitable companies. This leave a huge gap. I know of a number of companies who are already investigating moving their company to Australia due to the more favourable R&D tax incentives.

#14

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Thursday, May 31, 2018 5:16:03 AM
Last Modified:	Thursday, May 31, 2018 5:40:48 AM
Time Spent:	00:24:45
IP Address:	s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals:

Name	s 9(2)(a)
Email address	

Q2 (ii) For organisations:

Name of organisation	**ThunderMaps**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand?

2 to less than 6 years

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners.

10 - 19

Q5 (v) What industry sector does your business operate in?

S Other services

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Project Grant	**2015, 2016, 2017**

Q7 (vii) Has your organisation ever received any other R&D government support?

Yes,
If yes, please specify names of grant(s)/support.:
Get started R&D $5000 grant Summer intern grants

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand?

A smaller government sector, when compared to the private sector. The lack of Govt transferring money to Govt via application / forms, is likely to be a good this - more efficient not to have a money-go-round.

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

Seems to miss software product companies completely - are they serious??

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

Software product companies. Start-ups. Start-ups are excluded. What??

Xero
Vend
Push Pay
ThunderMaps

These companies above would be excluded.

Growing tech companies, not making a profit are excluded.

Perhaps I'm pointing out the obvious here: R&D is not instantly profit making. This means, by definition, that high R&D business are excluded by this policy.

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Tech companies.

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

More paperwork and accountants going through this paperwork on behalf of large companies.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Respondent skipped this question

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

Respondent skipped this question

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

Respondent skipped this question

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

Respondent skipped this question

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

Of course.

Clients offen pay us to build the product that the vendor keeps the IP of. Basically it's often much more effecient for a large organisation to pay an external nimble software development house to solve their problem, then spin-up and manage their own R&D. This has happened to us a lot.

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Loss making needs to be allowed. Software companies are designed for growth, not profits. The capital markets do not support software product companies that are optimised for profit (excluding growth). Therefore, this policy could be quite damaging to the software product sector in New Zealand.

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Respondent skipped this question

Q21 Q15 Is the minimum threshold set at the right level?

No,
If 'no', please provide further details.:
Why is there a minimum at all?

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

It is very important that loss making companies are also supported. If not, this will impact the software product sector significantly (SaaS sector)

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

Why is a minister needed? Shouldn't we just have something simple and across the board, regarding R&D support?

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

Shouldn't we just have something simple and across the board, regarding R&D support?

Transparency is a non issue, if there are few rules or exceptions, or rules on who gets what.

Q25 Q19 Are there any other risks that need to be managed? Please describe.

It seems to me this policy is not going to support the technology sector at all well. In particular software product companies. This is a significant error in the policy, that is likely to negatively impact New Zealand in the decades to come.

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

Respondent skipped this question

Q27 Q21 What is the right level of information required to support a claim?

Shouldn't the claim process be simple, and across the board? The current IRD tax credit system for R&D is good, why not just extend it for larger claims?

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

Respondent skipped this question

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,
Contact details:
s 9(2)(a) [redacted]

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here:

Respondent skipped this question

#18

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Thursday, May 31, 2018 8:32:33 AM
Last Modified:	Thursday, May 31, 2018 10:08:26 AM
Time Spent:	01:35:52
IP Address:	s 9(2)(a)

Page 2: Your contact details

Q1 (i) For individuals: — **Respondent skipped this question**

Q2 (ii) For organisations:

Name of organisation	**Argenta Ltd**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? — **10 years or more**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand?Please include full-time and part-time employees but do not include contractors or the business owners. — **100 or more**

Q5 (v) What industry sector does your business operate in? — **M Professional, scientific, & technical**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2014, 2015, 2016, 2017**

Q7 (vii) Has your organisation ever received any other R&D government support? — **Yes,**
If yes, please specify names of grant(s)/support.:
Career Grants, Development Grants from 2011 pre growth grant

Page 3: Questions asked in the discussion document

Q8 Q1 If SOEs, Crown Research Institutes, District Health Boards, Tertiary Institutions, and their subsidiaries are excluded from the R&D tax incentive, what will the likely impact be on business R&D in New Zealand? — **Respondent skipped this question**

Q9 Q2 How well does this definition apply to business R&D carried out in New Zealand?

This definition should read 'Core activities AND Support activities' as both are integral to the success of R+D. 'OR' potentially enables a support provider only to qualify

Q10 Q3 Does this definition exclude R&D that you think should be eligible, please illustrate with examples?

Yes; It excludes costs of Intellectual Property protection which is incompatible with the eligibility criteria i.e. 'effectively own the results of the R+D'.
Should also include R+D expenditure undertaken by overseas subsidiaries or specialist institutes who may happen to be overseas.

Q11 Q4 Does the scientific method requirement exclude valid R&D in some sectors, please illustrate with examples?

Respondent skipped this question

Q12 Q5 What would the impact be on business R&D in New Zealand if a materiality test was applied to both the problem the R&D seeks to resolve and the intended advancement of science or technology?

Do not include a materiality limit as this excludes the opportunity for unintended discoveries -the very nature of R+D.

Q13 Q7 Are there any reasons why the exclusions should not apply to support as well as core activities? Please describe.

Yes; legal and admin aspects of patenting and licencing should not be excluded as these activities are essential for the ownership of the R+D results (as per proposed eligibility criteria) and vital to the commercial sustainability of the business.
A number of these exclusions are inappropriate -particularly to the pharmaceutical industry which is highly regulated and which statutory requirements often stipulate the R+D direction. For example registration of new products, pre-production activities (which often generate IP) and subsequent validation.

Q14 Q8 Please provide any examples where social science research is/has been a core part of business R&D in New Zealand?

Respondent skipped this question

Q15 Q9 What is the likely impact on business R&D in New Zealand if dual purpose activities are ineligible for the R&D Tax Incentive? Please describe.

R+D growth will likely be limited by this requirement. Most NZ businesses do not operate as a sole research provider, but have a commercial arm.
How do you propose to audit the undertaking of 'dual purpose' activities ?
Carrying out dual purpose activities is a normal commercial imperative.

Q16 Q10 What are the advantages and/or disadvantages of limiting eligible expenditure to R&D labour costs? Please describe.

We do not understand the discussion document; it appears to contradict its own eligibility criteria.
Would this exclude the allocation of R+D work to an overseas subsidiary and the claiming of those overseas costs? Labour cost is only a small portion of total R+D expenditure. This approach might be the simplest to govern, but the least valuable for NZ businesses undertaking R+D.

Q17 Q11 What are the advantages and/or disadvantages of setting overhead costs as a percentage of R&D labour costs? Please describe.

This is a disadvantage; Calculating overhead costs as a set percentage of direct labour is, in our view inappropriate for determining true eligible R+D costs. We feel the first option delivers a more realistic outcome. For example: tooling, engineering or modelling for Proof of Concept studies in the pharmaceutical industry is capital intensive.

Q18 Q12 Are there any reasons why expenditure related to R&D activities for which commercial consideration is received should be eligible for a tax incentive? Please describe.

If this is designed to exclude R+D costs that have been recovered, then this makes sense. However if this seeks to exclude R+D costs for which there is a future commercial return, then this is nonsense.
Isn't a commercial endpoint the whole purpose of R+D, and where NZ will benefit from said R+D??

Q19 Q13 What variations or extensions to the definition of core activities are required to ensure it adequately captures R&D software activities?

Respondent skipped this question

Q20 Q14 Are there reasons why continuity rules should not apply to tax credits? Please describe.

Not as far as we are aware.

Q21 Q15 Is the minimum threshold set at the right level?

No,
If 'no', please provide further details.:
A true start up company would not necessarily have this kind of funding. We don't believe basing this on a labour unit is appropriate as salary is the last item to be paid in a start up scenario. Around $50000 could be a more realistic figure.

Q22 Q16 How important is a cap or a mechanism to go beyond the cap? Please provide further details.

Provided the expenditure meets the eligibility criteria, why should it be capped? The more R+D undertaken, increases opportunities for benefit to the country.

Q23 Q17 What features of a Ministerial discretion or pre-registration would make them most effective? Please describe.

Pre-registration is preferable to ministerial discretion -to ensure some consistency and continuity.

Q24 Q18 What are your views on the proposed mechanisms to promote transparency and enhance evaluation? Please describe.

We support both.

Q25 Q19 Are there any other risks that need to be managed? Please describe.

In a small market like NZ, there is a risk that transparency will tip off competitors to the nature of sensitive research being undertaken. There should be a data protection clause available.

Q26 Q20 Are there risks with extending penalties to external advisors in this way?

People may see it as a disincentive to provide information to support start up companies.

Q27 Q21 What is the right level of information required to support a claim?

The current Growth grant documentary requirements is sufficient provided people with the right specialist industry knowledge are on the receiving end. This ensures an efficient response.

Q28 Q22 What opportunities are there for customers to submit R&D Tax Incentive claims via third party software?

Respondent skipped this question

Q29 Q23 What integrity measures do you think Inland Revenue should use?

IR should ensure continued use of specialist industry experts i.e. Callaghan support managers to ensure different industries/companies are being assessed fairly.
Why not continue to use the independent review process that Callaghan Growth Grant claims currently utilise, (provided those fees are claimable).

Q30 Q24 Would you be willing to be contacted in future on the R&D tax incentive and/or implementation process?

Yes,
Contact details:
s 9(2)(a)

Q31 Q25 Please provide any other feedback you may have on the proposed R&D tax incentive here.

Respondent skipped this question

#21

COMPLETE

Collector:	Web Link 1 (Web Link)
Started:	Thursday, May 31, 2018 10:08:48 AM
Last Modified:	Thursday, May 31, 2018 10:40:53 AM
Time Spent:	00:32:04
IP Address:	s 9(2)(a)

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Q1 (i) For individuals — **Respondent skipped this question**

Q2 (ii) For organisations

Name of organisation	**Argenta Ltd**
Contact person name	s 9(2)(a)
Position	

Q3 (iii) How long has your business been operating in New Zealand? — **10 years or more**

Q4 (iv) How many employees (FTEs) are employed by your business in New Zealand? Please include full-time and part-time employees but do not include contractors or the business owners. — **100 or more**

Q5 (v) What industry sector does your business operate in? — **Professional, scientific, & technical**

Q6 (vi) Has your organisation ever received a R&D project or R&D growth grant?

R&D Growth Grant	**2014**

Q7 (vii) Has your organisation ever received any other R&D government support? — **Yes,**

If yes, please specify names of grant(s)/support.:
Careers Grant, Development Grant (2011 pre growth grant)

Q8 How likely is it that your organisation will be in a position to use the full amount of an R&D tax credit in the 2019/20 tax year? (Note, to use the full amount of a R&D tax credit in a given year, your business' tax liability needs to be at least as large of the R&D tax credit you are entitled to claim.) — **Very likely**

Q9 How much R&D does your organisation expect to carry out in the coming year?

s 9(2)(b)(ii)

Page 3: Responses to questions in the consultation document

Q10 Q1 What impact will the proposed transition arrangements have on your business? For example, your cash-flow or internal reporting mechanisms? Please describe.

It will have a detrimental impact on our cash-flow.

Q11 Q2 What do you believe to be a necessary transitional period? Please explain the reasons why this is necessary for your business?

The transitional period as proposed is ok

Q12 Q3 What impact will the proposed transition arrangements have on your R&D programme over the next few years?

Hopefully none, but our R+D expenditure could be scaled back due to reduced cash flow.

Q13 Q4 Please provide any other comments about the proposed transition arrangements.

Respondent skipped this question

Q14 Q5 For businesses in tax loss, what impact will the proposed temporary grant have on your business during the transition process? Please describe.

Does not affect us.