The new research and development tax incentive

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GlaxoSmithKline
Tel: 03 9721 4586
Fax: 03 9721 6668
Website: www.gsk.com
Contact: lucinda.e.bilney@gsk.com

GlaxoSmithKline (GSK) commends the Federal Government on developing a new research and development tax incentive legislation. Through the implementation of new incentives such as this one, opportunities exist to reverse Australia's declining competitiveness as a destination for research and development and ensure the long term viability of pharmaceutical research and development in Australia.

GSK is supportive of the suggested changes in the Tax Laws Amendment (Research and Development) Bill 2010, however wishes to highlight three opportunities to further enhance the proposed legislation.

1. **Expenditure not at risk**
   The proposed section 355-405 appears to prevent deductions for R&D expenditure by the local entity where the company expects to receive reimbursement for R&D activities from its overseas body corporate. This may prevent the local GSK entity from accessing deductions for R&D activities performed on behalf of the related foreign companies. This appears contrary to other sections of the legislation such as 1.16 'R&D entities' which allow research carried out by a foreign corporation through a permanent establishment in Australia.

   We understand that this section may have included a drafting error which will be amended prior to the tabling of the Legislation and strongly advocate for changes to the section to be made to ensure access to deductions in these circumstances. We would greatly appreciate the opportunity to review this section again.

2. **'Above the Line' tax credits**
   GSK is disappointed that the government has not taken the opportunity to incorporate the concept of 'above the line' tax credits for R&D, increasing the international competitiveness as initially discussed in the Cutler Review. The advantages of 'above the line' tax credits include cost neutrality for the government whilst increasing the international competitiveness of conducting R&D activity in Australia by ensuring the credit is highly visible and relevant to the R&D decision makers. The increased visibility of 'above the line' tax credits presents opportunities to heighten the perceived value of the tax credit system from an accounting and management viewpoint and maximise the potential of the credit to influence R&D investment decisions. We understand that compliance with new international accounting standards make such recognition difficult; however encourage the Government to continue to monitor this situation and make the necessary changes when practicable.

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3. **Augmented feedstock rules**

   GSK has concerns regarding the broad-brush approach relating to feedstock rulings outlined in the draft legislation.

   The draft legislation will require additional compliance resources to identify and cost individual tasks within R&D processes, the quarantining of identified activities from the feedstock rules, calculation of net R&D expenditure and identification of amounts for foreign R&D which relates to the provision of product rather than new knowledge. GSK believes that the feedstock rules should only be applied to claw back on the cost of materials processed as part of the R&D claim and not against the entire cost of the actual R&D activities.

GSK congratulates the Government on the significant improvements to the R&D tax incentive scheme proposed in the draft legislation and in particular those initiatives such as the four year amendment period which enhance business certainty and aim to simplify the administration of the program. The three opportunities outlined above may improve the impact of the draft legislation and should be considered by the Government in refining the legislation.