

## **Council for Humanities, Arts and Social Sciences (CHASS)**

### **Submission on the New R&D Tax Incentive**

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With more than 80 member organisations, the Council is an active network of specialists across humanities disciplines, creative arts, and research and professional practice in the social sciences.<sup>1</sup>

In this brief submission, in seeking to respond to the call for comment on the R&D Tax Incentive, the Council will concentrate on:

*Question 5:*

*Should the current list of activities excluded from being considered core R&D be... amended in any way?*

The proposed R&D tax incentive continues to specifically exclude R&D conducted within the social sciences, arts and humanities from counting as 'core R&D'. Judging by landmark reports such as *venturousaustralia* and policy packages such as *Powering Ideas*, it is now accepted that innovation policy must take account of much broader sources of innovation, and that reform of outdated aspects of this and other countries' innovation and R&D is necessary.

It is timely to reconsider this exclusion, as it is now widely recognised that much of the growth and innovation in the services economy, but also in manufacturing as both sectors are increasingly intermingled, is derived from the knowledge inputs from the social sciences, arts and humanities (HASS) in combination with business, and often in collaboration with science and technology. New science and new technologies on their own cannot achieve all that the R&D tax incentive aims for, in delivering spill-over benefits of new knowledge and practical advances for business and the wider community.

#### **The overall principles are sound**

To qualify for the incentive, R&D must be systematic, investigative and experimental (SIE). The activity must involve an appreciable element of novelty, a high level of technical risk, and be carried on for the purpose of acquiring new knowledge (whether or not that knowledge will have a specific practical application) or creating new or improved materials, products, devices, processes or services.

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<sup>1</sup> In preparing this response to the consultation paper, we have not undertaken full discussions with all member organisations, and therefore these comments should not be taken as an agreed position for the 81 organisations involved. These comments are consistent with the Council's existing policy position on the inclusion of HASS Research, Design and Development in innovation programs, found in CHASS's submission to the Review of the National Innovation System.

These are unexceptional, and CHASS affirms them as general criteria, submitting that HASS forms of R&D can and should be vetted along these lines. We consider, however, that the term ‘technical risk’ overly and unnecessarily narrows the forms of risk essential to innovation and experimentation. There is no longer justification for this when the latest developments in the OECD guidelines are considered.

### **But Australia’s R&D exclusions are inconsistent with the evolving OECD guidelines**

The Treasury’s consultation paper, and the ATO’s latest Guide to the R&D Tax Concession, are both based on the OECD’s *Frascati Manual* which provides the guidelines for measuring R&D. But advances in incorporating the service sector in the 6<sup>th</sup> edition of the manual (published in 2002) have sought to include HASS inputs.

The manual explains, for example, that R&D in software development often draws directly on HASS activities, and that humanities and social sciences need to be addressed in any contemporary R&D frameworks:

The model on which the Manual was originally based was that of institutionally structured R&D in the natural sciences and engineering leading to tangible technological innovations in primary and secondary industries. Software development has since become a major intangible innovation activity with a high R&D content. In addition, an increasing share of relevant activities draws on the social sciences and humanities, and, together with advances in computing, leads to intangible innovations in service activities and products, with a growing contributions from service industries in the business enterprise sector. (p46)

The social sciences and humanities are covered in the Manual by including in the definition of R&D “knowledge of man, culture and society” [from in Chapter 2, Section 2.1] ... including R&D relating to the knowledge of behaviour and organisations. (p48)

In many cases, R&D findings in service industries are embodied in software which is not necessarily innovative from the technical point of view but innovates by virtue of the *functions* that it performs. (p49)

In a recent response to an inquiry on this matter (attached), the Commonwealth’s position was explained. Apparently it is believed that, although ‘the Government is aware that some work undertaken in the humanities, arts and social sciences field can be vibrant ...there is a concern that if the criteria for activities eligible for the R&D tax concessions were broadened to include humanities, arts and social sciences, then there would be calls from many other sectors to similarly include their activities as being eligible and this would have serious cost implications for the concession’.

The exclusion of HASS on the basis that its R&D activities are not ‘systematic, investigative or experimental’ shows a lack of understanding of what the broad disciplinary group comprising the social sciences actually does. That research in HASS might be counted as ‘supporting’ R&D is not rigorous enough: activities based in HASS should not be subsumed

within routine and supporting activities such as pre-production, quality control, marketing, administration of patents, and cosmetic modifications. There is no question that exclusions should be made to ensure routine business activity is not siphoning off public funds in the name of R&D. These safeguards need to be made independently of categorical disciplinary exclusions.

### **Examples of HASS-based R&D**

The exclusion of HASS R&D from the R&D tax incentive means the following scenarios would not qualify:

- In the context of a social development program based at the University of Queensland (the Triple P Positive Parenting Program), an investment by Triple P International in determining the potential for applying the Triple P approach to a new field. For example, developing a new resource for working with parents who have children with physical disabilities. This is despite the fact that the resource may be unique and may require extensive research to develop and test.
- In the context of human factors and cognitive psychology, companies seek advice on the design of human-centred systems that will enable them to improve efficiency, reduce accident rates, etc. These investments can result in novel solutions and new systems designs that have a specific “pay-off” to the client and possible industry-wide benefits. The experimentation undertaken to develop these systems is highly technical and outside the expertise of physical, biological, chemical, medical, engineering or computer sciences.
- In many areas of human services practice, there are opportunities for companies to develop new ways of providing services. For example, in aged care it may be possible to develop a radically new approach to fostering independent living within retirement homes drawing on knowledge from psychology, sociology and nursing. This new model would have to be developed and then tested to establish whether it worked. Despite the potential commercial value to the retirement service provider and the benefit to the wider community, the provider will not be able to access the R&D Tax Incentive for this innovation. However, the same company may be able to claim the R&D Tax Incentive for developing a simple device that provided retirement home residents with a marginal improvement in physical mobility.
- In the inter-disciplinary combination of computer interfaces with counselling services software is produced to create a new function for online counselling. This combines R&D in interface design, psychology and it tested in several roll-out phases on increasingly larger sample groups, within strict ethical boundaries. The human-software output is then up-scaled and applied by a range of counselling services. Furthermore, it triggers other R&D efforts in related fields such as interface learning in resilience for young people. There is wide appeal with commercialisation, and a start-up consortium

would be boosted by the R&D Tax Incentive, and would give back many benefits to Australia's economy and society, if only they were eligible to apply.

There is also anecdotal evidence that games companies, in seeking to qualify for the current tax incentives, may inadvertently distort their business strategies by focusing too much on technical infrastructure when their competitive advantage lies in R&D in content.

CHASS suggests that the film-production tax credit system administered by Screen Australia (including Producer, Location and PDV (post, digital and visual effects) Offsets, replacing the Refundable Film Tax Offset as of July 2007) is a precedent for a tax credit scheme in the arts field that can work for the good of firms and wider economy.

### **Amend the R&D Tax incentive to enable participation by the humanities, arts and social sciences.**

We recommend removing point (f) of the Income Tax Assessment Act at Section 73B 2C(f): "research in social sciences, arts or humanities" from the list of exclusions.

### **Conclusion**

This review takes place in the wider context of changes in thinking about innovation and R&D around the world. It is now accepted that innovation policy must take account of much broader sources of innovation. With appropriate safeguards to ensure that R&D tax incentive is not overburdened with specious claims, CHASS submits that a more inclusive approach recommended here is a crucial step forward for an innovative Australia.

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