

27 October 2009

General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam

Submission on Research and Development Tax Incentive Consultation Paper

The Federal Chamber of Automotive Industries (FCAI) is the peak industry organisation representing vehicle manufacturers and importers of passenger vehicles, light commercial vehicles and motorcycles in Australia. This submission presents the FCAI's views on key aspects of the Consultation Paper "*The new research and development tax incentive*", September 2009.

The future of the Australian automotive industry lies in its capacity for innovation. Given Australia's standard of living, the automotive industry cannot rely on a low cost production strategy. It must be able to deliver superior value to customers whether they are located in Australia or in overseas markets.

Innovation is not just about improved products through design and engineering, although that is very important, it must also deliver production process improvements, faster and more effective model development systems and for that matter improvements throughout the complete value chain.

The automotive industry in Australia invests over \$600 million in R&D annually which accounts for about 10 per cent of total business R&D in Australia and over 20 per cent of business R&D in the manufacturing sector.

Whilst the automotive industry has access to specific R&D programs including the Green Car Innovation Fund, the industry also accesses the R&D Tax Concession program and believes that it is vital to attracting investment into Australian based R&D activities.

Supporting R&D Activity

The proposed changes to “Supporting R&D” in respect of both its definition and the rate at which it can be claimed, appear to be extremely arbitrary and will have a significant impact on the number and value of R&D activities in the automotive sector.

The supporting costs associated within individual R&D projects are intrinsic to any R&D project and should not be considered to be of a lower value than any other component of either a core or non-core nature. The Consultation Paper seems to indicate that “support” activities provide a lesser benefit to the Australian economy than “core” activities without providing any empirical evidence that this is the case and without recognising the symbiotic relationship between core and support activities.

The administrative burden associated with separately recording core and supporting costs will significantly increase the administrative complexity of R&D activities and require skilled researchers to focus their attention on administrative reporting duties not core R&D activities.

Change of R&D definition

R&D tax incentives have been effective in stimulating investment in R&D in the industry which has underpinned the industry’s growth in product development and exports. The changes proposed to the R&D definition in the consultation paper pose significant concerns to the automotive industry.

A new model development cycle involves both innovation and high levels of technical risk, however, not necessarily at the same stage of the development. With R&D projects extending over many years, elements of innovation and risk may be present in a project however not occur simultaneously. The time frame between core activities involving innovation and those involving high levels of technical risk should not limit an R&D activity complying with the definition of eligible R&D.

Competition within global automotive companies to attract investment, including R&D investment, is intense. Modifying and narrowing the definition is likely to have an adverse impact on encouraging investment in R&D in Australia and in today’s global community, companies can choose to undertake R&D under more advantageous regimes elsewhere.

Other Issues

The FCAI recommends that a statute of limitations be placed on the capacity of the Commissioner of Taxation’s to make amendments to tax returns for an unlimited period. This would provide business certainty without compromising the ability of the Australian government to protect the interests of the broader economy and maintain the integrity of the R&D Tax Concessions.

The FCAI also encourages the Government to review the current “clawback” rules as part of this review with a view to providing a fairer and more transparent outcome for taxpayers.

Conclusion

The R&D Tax Concession has been the cornerstone of the Australian government initiatives to promote business R&D since the 1980s. Whilst there have been changes to the rate of the R&D tax concession and other taxation changes which have impacted on the benefit to business under this program, the FCAI urges the government to proceed with caution in making any changes to this critical program.

The FCAI is particularly concerned by the prospect of reducing the relative attractiveness of the Australian policy environment to attract R&D activity to Australia. Any tightening of definitions or scope of activity may impede these decisions.

Of the changes proposed in the Consultation Paper, the FCAI would be particularly concerned if the scope of eligible activity were subject to new limitations.

Should you have any queries, please do not hesitate to contact me.

Yours sincerely