The new research and development tax incentive

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Introduction

GlaxoSmithKline (GSK) commends the Federal Government on initiating a consultation paper to consider '*the new research and development tax incentive*' and applauds the Government's desire to promote increased investment in innovation. In particular, GSK supports changes to promote small R&D intensive Australian companies which include the biotechnology industry.

Considering research and development tax incentives is both important and timely as it comes at a time when pharmaceutical innovation is continuing to move forward at a rapid pace and is carrying with it the potential to radically change the current health system and the state of the pharmaceutical industry in Australia. At the same time, the process of innovation within pharmaceutical research is subject to unprecedented challenges which have implications for Australia's ability to attract research into this industry.

GSK

GSK is a world leading, research-based pharmaceutical company dedicated to meeting the health care needs of people around the world by helping them do more, feel better and live longer. The company is a global leader in the research, development, manufacture and supply of prescription medicines, vaccines, over the counter medicines, oral care products and nutritional health care drinks.

GSK has a strong presence in Australia with operations in all states and manufacturing facilities at Boronia and Port Fairy in Victoria, Ermington and Castle Hill in NSW and Latrobe in Tasmania. GSK currently employs approximately 2,000 Australians.

GSK are a leading supplier of medicines and vaccines to the Pharmaceutical Benefits Scheme and the National Immunisation Program, providing treatments for conditions such as asthma, COPD, diabetes, HIV/AIDS, infections, breast cancer, pain relief and dental care as well as a wide range of vaccines.

Research & Development

GSK employ approximately 14,500 R&D staff around the world and in 2008 spent more than $7billon to support research Over $500m was invested in clinical trials in Australia in 2008.

However, Australia's competitiveness as a destination for global clinical trials is under severe threat. This is mainly due to timeliness, capacity and cost issues. The number of trials commenced by industry in Australia fell by over 30% in the first half of this year (2009) and without urgent action, global investment in clinical trials in Australia will decline dramatically over the next three to five years.

Immediate implementation of tax incentive reforms will help 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.

This submission will focus on opportunities to enhance the elements of the R&D tax incentive scheme particularly in relation to:

1. 'Above the line' tax credits;
2. Overseas R&D; and
3. Supporting costs.

1. 'Above the line' tax credits

The tax incentive is designed to promote increased R&D in Australia; however, it may be argued that the design of the current system rewards activity that may have occurred anyway. GSK proposes that the new system should be to ensure the incentive is structured in such as way that it is directly attractive to those executives that have the ability to influence R&D investment decisions.

An alternate, 'cost neutral to government' mechanism to increase Australia's international competitiveness would be to enable R&D tax credits to be recorded as 'above-the-line' income. Multinational companies are large and complex organisations and the reduction of tax liability is not always transparent to the decision makers controlling R&D investment. This is not to say that after tax incentives are not effective in attracting R&D investment, they are when one considers the benefits they deliver to the global corporation. However, GSK believes that the delivery of an incentive above the line would, dollar for dollar, yield significantly better returns to the Australian tax payer as it increases is attractiveness of the incentive to the local business entity rather than the global corporate entity. This attractiveness would promote increased and proactive involvement in investment attraction by the local business and potentially increased local co-investment which in turn increases Australia's cost effectiveness when bidding against international locations for investment projects. Ways in which R&D tax credits may be recorded 'above the line' may include the development of a grant or R&D tax refund or the issuing of tax credit certificates with an agreed value for financial reporting .

GSK understands that there are challenges inherent with this proposal but given that there are relatively few programs globally that operate in this way, GSK believes that such a proposal would differentiate Australia and would significant enhance the nations competitive advantage for large multinational corporations. The resultant increase R&D investment offers the opportunity for real economic benefits through increased employment and commercialisation opportunities and increased spill over benefits through collaboration with smaller firms and

academic groups as well as upskilling in the research sector in applied research and commercialisation areas.

2. Overseas R&D

Question 1. Should there be any exceptions to the general rule that eligible R&D activity must be conducted in Australia?

GSK supports the continuance of the current R&D tax concession where a claim in relation to Australian-owned R&D may include up to 10% of activities conducted overseas. However, GSK appreciates that this restriction potentially affects small Australian business, especially where critical development activity cannot be conducted wholly in Australia such as pre-clinical toxicology or clinical trials.

GSK supports the notion that for small innovative Australian companies where ownership of IP is retained in Australia, benefit may be derived from lifting the restriction where companies can demonstrate that the activity in question is not easily able to be conducted in this country. However, GSK also recommends the removal of the pre-approval requirement for overseas conducted R&D as this requirement is difficult to satisfy in practice and therefore the benefit is often foregone.

3. Supporting costs

GSK maintains the view that supporting costs should be capped as a proportion of expenditure on core activities. This would enable the continuance of the principles of the Pharmaceuticals Partnerships Program (P3) industry support program where a capped rate of 30% of expenditure was applied. Benefits of the implementation of an agreed capped proportion of expenditure for supporting costs include enhanced simplifications and a reduction of administrative burden for both industry and government.

Conclusion

This submission addresses a number of key areas highlighted in the consultation paper where opportunities exist to strengthen the R&D tax incentive and thus enhance the nation's ability to attract research and development.

GSK commends the Government on the development of the new R&D tax incentive, particularly those elements of the initiative that aim to simplify the administration of the program.