

Australian Information Industry Association

Submission on

Better targeting the Research and Development Tax Incentive – exposure draft

About the AIIA

The Australian Information Industry Association (AIIA) is the nation's peak body for those in the digital ecosystem, leading strategic policy and advocacy to shape a thriving digital sector. Through strong engagement with government, industry, and the broader community, the AIIA ensures the voice of its members informs decision-making on technology, innovation, and digital capability.

Membership provides direct access to influential networks, premium events, and opportunities to collaborate on initiatives with the sector's best and brightest to drive industry growth, improve productivity, and secure Australia's place as a global technology leader. AIIA members access real collaboration, real connections, and real outcomes.

Executive Summary

AIIA supports the Government's objectives for this reform and several of its measures. Our concern is that the draft pairs those gains with measures that narrow access for technology firms, and leaves out the measures that would address cash flow and certainty.

Three mechanisms in the draft would cut support for exactly the R&D the Incentive should be encouraging. Each relies on a simple rule in place of a judgment about the value of the R&D itself, and each rule falls hardest on firms doing long-cycle, high-risk technology work.

1. **Enterprise age is a poor proxy for whether refundability is needed to induce additional R&D.** A firm's need for cash support does not expire on its tenth anniversary, particularly in technologies with long development cycles.
2. **Removing supporting R&D activities draws an artificial line through experimental work.** Much of the work that makes a software or hardware experiment possible is not itself experimental. Removal is also likely to increase, not reduce, compliance effort.
3. **Absolute expenditure is a weak proxy for impact.** A \$30,000 program can be a substantial commitment for a small firm and immaterial for a large one.

Summary of recommendations

Refundability

1. Extend the fifteen-year refundability period to R&D whose dominant purpose is to generate new knowledge in a field on the List of Critical Technologies in the National Interest. Access should be gated by a Board finding equivalent to new section 28EA of the IR&D Act.
2. Narrow the related-entity start-day rule in subsection 355-100(6) so it prevents resetting the clock without capturing genuine spinouts and new ventures.
3. Provide transitional relief for firms that would lose refundability on the first day the new rules apply.

Supporting activities

4. Replace the removal of supporting R&D activities with a deemed rate: a fixed offset calculated as a ratio of core R&D expenditure.
5. Confirm that new subsection 355-25(2A) does not disqualify an activity that meets the R&D activity test in its own right merely because it also supports another R&D activity.
6. Extend transitional protection to supporting activities within multi-year projects that commenced before the reforms were announced, and to existing Board findings that cover later income years.

Access, collaboration and certainty

7. Introduce a dedicated startup stream from 1 July 2028, with quarterly advance payments and project-based eligibility.
8. Allow a lower minimum expenditure threshold where R&D intensity is high.
9. Introduce a collaboration premium for R&D conducted with registered research organisations, extended to the employment of new STEM PhD graduates.
10. Extend the binding finding model in new section 28EA to technology R&D generally, and remove clawback.

Refundability and the ten-year test

For loss-making firms it affects, the ten-year limit removes cash support entirely. AIIA recommends extending the longer refundability period, which the exposure draft makes available for eligible therapeutic-goods R&D, to critical technologies.

The issue

Under new table item 1A, a firm with turnover under \$50 million loses refundability once any day in the income year falls on or after the tenth anniversary of its start day. It keeps the 23 point rate, but only as a non-refundable offset. For a profitable firm, that is close to neutral. For a firm in loss, it removes the cash entirely.

International evidence indicates that refundability is central to the effect of R&D tax support. OECD analysis found that firms' responsiveness to tax support is close to twice as large where refund provisions are available to firms in loss, and larger again where support is disconnected from a firm's profit position.¹ Withdrawing refundability at ten years therefore weakens the Incentive's influence on the investment decisions it is intended to shape.

¹ OECD, *The Impact of R&D Tax Incentives: Results from the OECD microBeRD+ Project* (OECD Science, Technology and Industry Policy Papers No 159, October 2023) 7.

Age is a poor proxy for whether that cash induces additional R&D, for three reasons.

- **It does not track additionality.** Analysis undertaken for the Strategic Examination found additionality to be strongest among medium-sized firms of 20 to 199 employees, particularly in the manufacturing and services sectors.² That analysis identifies firm size and sector as the relevant indicators of effectiveness; firm age is not among them. A ten-year limit on refundability therefore risks withdrawing support from the firms in which the Incentive generates the greatest additional R&D.
- **It withdraws support where translation capacity is highest.** Established firms hold the plant, staff, supply chains, quality systems and customers that turn R&D into products and exports.
- **It captures firms in transition, not only firms in decline.** A profitable firm can be in loss for several years while it rebuilds a platform, retools, or moves into a new technology. That is exactly the investment the Incentive exists to support.

The draft also accepts that some R&D takes longer than ten years to commercialise, by giving therapeutic goods fifteen years. The same is true of quantum computing and sensing, AI hardware, semiconductor design, advanced communications, robotics and autonomous systems.

Recommendation 1: extend the longer period to critical technologies

AIIA recommends that the fifteen-year period in new subsections 355-100(4) and (5) extend to R&D whose dominant purpose is to generate new knowledge in a field on the List of Critical Technologies in the National Interest.³

AIIA reads the therapeutic goods extension as recognising a general principle. Where R&D takes more than ten years to reach market, a ten-year window withdraws cash support before the investment can pay back. Any field with that development profile warrants the same treatment.

The List is an existing Government instrument, maintained by DISR. Its seven fields include AI technologies, advanced information and communication technologies, quantum technologies, and autonomous systems, robotics, positioning, timing and sensing. It already guides National Reconstruction Fund investment mandates and informs the National Science and Research Priorities. The List states that it will not be used to regulate technologies, and AIIA does not propose it as a self-executing eligibility test. The List would define scope. A Board finding would determine eligibility.

² Expert Panel for the Strategic Examination of R&D, *Ambitious Australia: Strategic Examination of R&D* (Final Report, December 2025) 61 ('*Ambitious Australia*').

³ Department of Industry, Science and Resources, 'List of Critical Technologies in the National Interest' (Web Page, 2023) <<https://www.industry.gov.au/publications/list-critical-technologies-national-interest>>.

Access should therefore mirror the therapeutic goods mechanism:

1. the entity applies to the Board for a finding that the dominant purpose of its registered activities is to generate new knowledge in a listed field
2. the application window, review rights and binding effect match new section 28EA of the IR&D Act
3. the entity must otherwise satisfy the same conditions as a therapeutic goods entity

This approach would apply the same integrity safeguards to critical technologies that the draft applies to therapeutic goods. It would also require no new administrative machinery, as the Board already makes findings of this kind and section 28EA establishes the process.

Recommendation 2: narrow the related-entity start-day rule

Subsection 355-100(6) takes the start day from the earliest of the R&D entity and its connected entities and affiliates. AIIA supports the purpose, which is to stop firms resetting the clock through a new subsidiary.

As drafted, the rule reaches further than that purpose. A startup in which an established company or research institution holds a connected-entity interest inherits that entity's start day, which may be decades earlier. It can be outside refundability from its first income year. It also discourages corporate venturing and partnerships between established firms and startups, both of which strengthen the innovation system.

AIIA recommends narrowing the rule, for example by disregarding exempt entities and applying it only to related entities carrying on the same or a substantially similar business.

Recommendation 3: transitional relief

Firms whose tenth anniversary has already passed, or falls before 1 July 2028, lose refundability on the first day the new rules apply. Many have multi-year R&D programs planned and funded on current settings.

AIIA recommends that firms eligible for the refundable offset immediately before commencement retain it for their first two income years commencing on or after 1 July 2028.

Supporting R&D activities

Removing supporting activities draws an artificial line through experimental work, and is likely to increase compliance effort.

The issue

The draft removes the supporting R&D activity category and renames core activities as R&D activities. New subsection 355-25(2A) provides that an activity is not an R&D activity merely because it is directly related to, or undertaken to support, another R&D activity.

Supporting activities have been part of the Australian regime since its inception. The *Income Tax Assessment Amendment (Research and Development) Act 1986* extended

eligibility to activities carried on for a purpose directly related to the systematic, investigative or experimental work, in recognition that a research program requires work beyond the experiment itself.⁴

AIIA supports the objective of excluding general overhead and unrelated commercial work. The difficulty is that technology R&D relies on work that is essential to the experiment but not itself experimental. Examples include:

- building test environments, harnesses and simulation rigs
- collecting, cleaning and labelling data for model training and evaluation
- instrumenting systems to measure experimental results
- fabricating prototype hardware, boards and fixtures
- integration scaffolding needed to run an experiment end to end
- controlled user testing to validate a hypothesis

The experiment cannot occur without this chain. Under the draft, each link must independently satisfy the experimental test or fall out of the claim. The effect on a claim can be large, even with the higher rate.

Recommendation 4: a deemed rate for supporting activities

AIIA recommends replacing the removal of supporting activities with a deemed rate: a fixed offset calculated as a ratio of core R&D expenditure. Treasury can set the ratio from claimant data, which caps supporting-activity cost as a share of core spend and meets the fiscal objective directly.

A deemed rate removes the need to classify and document each supporting activity, and gives firms a predictable benefit to plan around. The Strategic Examination panel recommended the same approach.⁵

Recommendation 5: confirm dual characterisation is not fatal

New subsection 355-25(2A) could be read as disqualifying activities that are experimental in their own right but also support another R&D activity. AIIA asks that the explanatory material confirm an activity meeting the R&D activity test is not excluded because it also serves a supporting role.

Recommendation 6: transitional protection

Subitem 74(2) preserves supporting activities conducted in income years beginning before 1 July 2028. Supporting work in the same project after that date loses eligibility, even where the project commenced and was funded on current settings.

⁴ *Income Tax Assessment Amendment (Research and Development) Act 1986* (Cth), inserting *Income Tax Assessment Act 1936* (Cth) s 73B.

⁵ *Ambitious Australia* (n 2) 59 (Recommendation 5a).

Subitem 76(2) goes further. Board findings already in force for income years from 1 July 2028 cease to bind the Commissioner to the extent they cover activities that no longer qualify as R&D activities under the amended rules. This may remove certainty previously obtained through existing findings for supporting activities.

AIIA recommends that findings made, or applications for findings lodged, before the measure was announced on 12 May 2026 continue to have effect for the income years to which they relate. Supporting activities within projects that commenced before that date should remain eligible until the project ends or 30 June 2030, whichever is earlier.

A startup stream with advance payments

AIIA recommends a dedicated startup stream from 1 July 2028, built around quarterly advance payments. Some of the draft's narrowing measures, particularly the higher minimum expenditure threshold and removal of supporting activities, may disproportionately affect startups and other smaller R&D-intensive firms.

Why advance payments matter most

AIIA has argued that an offset claimed after the R&D is done, and potentially subject to clawback, is not the preferred vehicle for driving new R&D investment.⁶ Upfront support changes investment decisions. Retrospective support mostly rewards decisions already made.

Cash-constrained startups currently pay advisers to prepare claims and borrow from short-term lenders to bridge the wait for refunds. Quarterly payments through the BAS cycle would remove much of that cost.⁷

What the stream should include

- quarterly advance payments based on business activity statements
- eligibility based on objective indicators, such as investment from a qualified venture capital fund, selective accelerator participation, registered IP and university collaboration, aligned with the existing ESIC and ESVCLP tests
- project-based eligibility, in place of activity-by-activity classification
- eligible expenditure extended to development, deployment, user testing and adoption research
- longer access for deep technology firms with extended development timeframes

The explanatory material describes these amendments as a first stage of reform. Applying the restrictions in 2028 without a startup stream would leave startups bearing the narrowing measures without the offsetting support.

⁶ Australian Information Industry Association, Submission to Department of Industry, Science and Resources, *Strategic Examination of Research and Development* (11 April 2025) 8.

⁷ *Ambitious Australia* (n 2) 59–61.

Recommendation 7

AIIA recommends that Government:

1. legislate a startup stream with these elements, to apply from 1 July 2028
2. release an exposure draft of the stream by mid-2027, to allow proper consultation on eligibility and the payment mechanism
3. confirm that project-based eligibility would apply in place of new subsection 355-25(2A) for eligible startups

Minimum expenditure threshold

AIIA accepts a minimum threshold for administrative efficiency, but recommends a lower threshold where R&D intensity is high.

Absolute expenditure has no necessary relationship to additionality or spillover. A \$30,000 program may be a major commitment for a five-person firm and immaterial for a large one. R&D intensity at least measures the commitment relative to the firm's capacity.

The draft itself accepts that sub-threshold R&D can merit support. Subsection 355-100(2) continues to allow expenditure below the threshold where it is paid to a Research Service Provider or Cooperative Research Centre. That distinction is hard to justify on additionality grounds when equivalent R&D performed in-house is excluded.

Recommendation 8

AIIA recommends retaining a lower threshold for firms with high R&D intensity. For example, the current \$20,000 threshold could continue to apply where notional R&D deductions exceed 10 per cent of total expenses.

Collaboration premium

AIIA recommends a collaboration premium within the Incentive. The draft introduces no dedicated collaboration premium or enhanced offset rate for collaborative R&D.

The premium would be an enhanced offset for R&D conducted in partnership with registered public research organisations. It would extend to the cost of employing new STEM PhD graduates, or equivalent, in their first three years. A similar premium was recommended by the 2016 Review of the R&D Tax Incentive, but not adopted.⁸ The Strategic Examination reached a similar conclusion, proposing enhanced benefits for large firms that collaborate with research institutions and startups.⁹

Recommendation 9

AIIA recommends introducing the collaboration premium in the next stage of reform, covering both research partnerships and the employment of new STEM PhD graduates.

⁸ Bill Ferris, Alan Finkel and John Fraser, *Review of the R&D Tax Incentive* (Report, 4 April 2016) rec 2.

⁹ *Ambitious Australia* (n 2) 63–5.

Certainty for claimants

New section 28EA allows firms undertaking therapeutic goods R&D to obtain a binding Board finding on whether they qualify for the longer refundability period, giving them certainty before a claim is disputed. AIIA recommends extending the model to technology R&D generally, alongside removing clawback.

The underlying problem

The Incentive combines two functions: encouraging R&D, administered by DISR and the Board, and retrospective tax enforcement, administered by the ATO. Firms decide to invest before results exist. Eligibility is settled after results are known, sometimes years later.

AIIA has consistently argued that this unpredictability, including delayed or withheld offsets, discourages new investment. The Australian Small Business and Family Enterprise Ombudsman reached similar conclusions in its 2019 review of the Incentive.¹⁰

A model already in the draft

Under new section 28EA, an entity undertaking therapeutic goods R&D can apply for a Board finding that the dominant purpose of its activities is to generate new knowledge about therapeutic goods. The finding is reviewable and binds the Commissioner when made within four years of the relevant income year. No equivalent mechanism is available for R&D in other fields.

That is the kind of binding certainty technology firms have sought, and it could be made available earlier. Existing advance findings under section 28A address whether activities are R&D activities, but not the wider matters that decide a claim's value.

Recommendation 10

AIIA recommends that Government:

1. **extend binding findings to technology R&D**, through a streamlined application covering the experimental proposition, the eligible activity boundary and record-keeping expectations.
2. **consider accrediting intermediaries** to provide front-end assurance, given the significant proportion of claim value that some firms currently pay to R&D tax advisers.
3. **remove clawback**, so firms that win competitive grants are not penalised under the Incentive.

¹⁰ Australian Small Business and Family Enterprise Ombudsman, *Review of the R&D Tax Incentive* (Report, December 2019).