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LESSENING SUPPORT FOR TECHNOLOGY AND INNOVATION

A TECHNOLOGY SECTOR PERSPECTIVE ON THE 2018 AUSTRALIAN BUDGET

Strategy[61] is a boutique consultancy firm that delivers growth strategy, value creation and deal structures for established or mid-market businesses seeking to gain impact from high-technology, high-growth, transformational business models.

The team has an impeccable track record in supporting businesses who are challenged by the demands of a fast moving and highly competitive global economy which has heightened the focus on entrepreneurship, innovation and commercialisation as the essential component for growth, competitiveness and success.

BUDGET AT A GLANCE

In the last budget before an election, the government has delivered personal income tax cuts for low- and middle-income earners worth $13.4b over the next four years as well as forecast an accelerated a return to surplus starting with a small, $2.2b surplus in 2019-20.

Higher iron ore, coal and LNG prices and the unexpected growth in employment through the creation of 400,000 new jobs has raised the tax take to create surplus in a time of income tax cuts.

Treasury forecasts this growth to continue, with gross domestic product to grow annually by 3.0% over the four-year forward estimates. Oddly, a week prior, the Reserve Bank of Australia forecast the economy to grow more quickly over the same period at 3.25%.

RESEARCH AND DEVELOPMENT TAX INCENTIVE

The Research and Development (R&D) Tax Incentive has been slashed by $2b over the next four years, reducing the program by more than 50%.

Rather than being reinvested in direct funding towards R&D, the savings have been re-incorporated into consolidated revenues.

The changes are in line with recommendations of the April 2016 R&D Tax Incentive Review that were reiterated in November 2017's Innovation and Science Australia's 2030 Strategic Plan. Both reports raised concerns about misuse of the system and that incentives were not stimulating additional research but instead largely funding research that would have been carried out regardless.

The ability of smaller companies to claim R&D offsets will be limited by a new $4m cap on the cash refund available to companies with annual turnover of less than $20m.[1]

Disappointingly, profitable companies with annual turnovers under $10m will see their claims reduced. The offset will be limited to 13.5% above their 27.5% corporate tax rate, down from the implied 16% when the offset was unlinked to the corporate tax rate at a flat 43.5%.

In line with findings that R&D has greatest impact on business growth at high intensity,[2] the changes for companies with annual turnovers above $20m have been designed to disproportionately reward companies undertaking large amounts of R&D. As such, tax offset rates will be determined by the proportion of their total expenditure is on R&D.

R&D intensity (proportion of expenditure)	0% - 2%	2% - 5%	5% - 10%	>10%
Tax offset	4%	6.5%	9%	12%

While this change is key to the $2b saving, it is likely to be beneficial to large technology sector companies, as they likely spend more than 5% on R&D and therefore receive a higher offset than the current 8.5%.

Further, the $100m threshold on eligible R&D expenditure has also been raised to $150m.

The administrators of the scheme, the Department of Industry, Innovation and Science, will also receive new funding for enforcement and granted powers equivalent to the Australian Tax Office to set precedent on claims. This change is important to help resolve current uncertainty, particularly regarding the eligibility of software development activities.

SMALL BUSINESS

The budget also laid out an 8-year plan to reduce the corporate tax rate from 30% to 25%.

Small businesses with aggregated annual turnover less than $10 million will be able to immediately deduct purchases of eligible assets costing less than $20,000. This measure will improve small business cash flow and build productive capacity. All businesses will benefit from the recommitment to cutting the company tax rate to 25 per cent over a ten-year period.

International trade support is strengthened by a $20 million investment in new SME Export Hubs. The Hubs will foster greater cooperation between Australian businesses, helping them grow as they work together to sell their products to the world. There is also $51.3 million to expand the existing network of agricultural trade counsellors in Asia, Europe and Latin America.

[1] Clinical trials are exempted from this cap.

[2] Office of the Chief Economist, *Australian Innovation System Report 2017*, November 2017.

RESEARCH & SCIENCE

For the first time in four years, the budget includes increasing the key research funding programs in line with inflation. Compared with forecast inflation of between 1.9% and 2.5%, funding for the Australian Research Council's Discovery Program grows at 1.6% and its Linkage Program at 2.1% while the National Health and Medical Research Council's funding grows at 1.5% over the next four years.

A headline measure is the National Research Infrastructure Roadmap receiving $1.9b over the next 12 years with $393m to be invested in the first five years. As announced in December 2017, this includes the National Computational Infrastructure and Western Australia's Pawsey Centre receiving $140m for enhanced supercomputing capabilities.

The budget's medical research funding is underpinned by a 10-year, $1.3 billion National Health and Medical Industry Growth Plan, supported by proceeds from the Medical Research Future Fund. Key initiatives include $500m to support the Genomics Health Futures Mission, $240m for the Frontier Health and Medical Research program, $248m for expanded clinical trial programs, $125m for chronic conditions research (particularly diabetes and heart disease) through the Targeted Translation Research Accelerator and $94.3m for biotech and industry research collaborations.

EDUCATION

The $2.1b university tuition subsidy freeze announced in December 2017 has been retained in the May budget. This freeze means that universities will receive their 2017 level of funding in 2018 and 2019 without increases for student enrolment growth or inflation.

The budget includes a range of small Science, Technology, Engineering and Maths (STEM) initiatives, including $4.5m over 4 years for a Women in STEM Ambassador and a Women in Science Strategy.

TARGETED FUNDING

On top of the broad funding measures described above, multiple targeted initiatives are allocated funding in the budget.

Artificial Intelligence research will receive $30m over 4 years, including additional funding to the Cooperative Research Centres Program, and will be informed by the forthcoming Artificial Intelligence and Machine Learning Horizon Scanning Report.

The budget allocates $92.4m to the Digital Transformation Agency's GovPass digital identity program which aims to make the process of proving your identity to government services online simple, safe and secure.

Implementation of precise positioning technology that combines GPS signals with mobile phone and other signals to provide location services accurate to less than 10 centimetres is allocated $225m. Additionally $36.9m is allocated to Digital Earth Australia, a platform that assembles global satellite images of Australia in a user-friendly and publicly accessible way.

The budget allocates $26m to establish a National Space Agency to coordinate domestic space activities and $15m to create an International Space Investment project to provide grants to strategic space projects that generate employment and business opportunities for Australians.

Research into coral restoration and adaptation receives $150m as part of a $536m package aimed at protecting the Great Barrier Reef against the crown-of-thorns starfish, rising ocean temperatures and extreme weather events.

If you have any queries related to this overview, please contact Hugh Sheppard at hugh.sheppard@strategy61.com.au.

Yours sincerely,

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