

Few examples of Australian tax policy are subject to as frequent change as the Research & Development tax subsidy, again [under review](#) by the federal government. Substantive changes to the rules have occurred every five of the past 20 years. By contrast, the US has had essentially the same R&D tax rules since 1990.

Change has a cost. Changing the tax system imposes uncertainty and information costs on business. The greater the number of changes that are built into the R&D tax system and the more nuanced the rules, the more business needs to spend on accountants.

A [2003 study of OECD countries](#) found that variations in R&D tax incentive policy undermined the observed effectiveness of the policy in inducing additional R&D investment.

This year, the rules changed again, including a lowering of the rate of subsidy, and last week's report proposes yet further changes. Are these changes likely to deliver benefits to justify the costs of yet more reform and business uncertainty?

R&D benefits more people than just the business undertaking R&D

Government support for R&D via tax incentives is consistent with a substantial amount of international evidence. Innovation, R&D and technology are critical for [underpinning productivity growth](#) and improving living standards over the long term.

The overwhelming empirical evidence is that businesses benefit from doing R&D and so does the rest of society.

Econometric estimates (undertaken at Swinburne University) of the effects of increasing R&D on business net revenue show a substantial return to the business itself. Numerous international firm-level studies find [similar results](#) .

The business benefits of R&D are good, but they do not justify public spending. The justification for public support exists because consumers, suppliers, and competitors also benefit from a given business's R&D. These are called "spillovers". Yale Economist William Nordhaus [estimated](#) that as much as 98% of the benefit from R&D is captured by consumers, suppliers, and competitors. Research at Swinburne University, using data on more than one million businesses finds that this is also the case in Australia.

The weight of evidence suggests R&D tax incentives are an effective policy to induce more R&D. Correspondingly, R&D tax incentives are now a feature of most OECD economies. Data shows that the Australian R&D tax system creates additional R&D spending by Australian business.

Research on the [additionality of R&D tax policy in Australia](#) has found for every A\$1 of tax not collected by the Australian government, the business spends on average an additional 80 cents to A\$1.90 on R&D. Looking across the research it's fair to say every dollar lost in tax generates more than a dollar in total benefit to all Australians.

What about the recent change to the R&D scheme?

So why change a scheme that's working? Some of the proposed changes simplify the current rules, such as removing the arbitrary A\$100 million cap on tax deductions. Other changes are not well supported by evidence. Capping the refundable element will save the government money, but the economic justification in terms of improving the "efficiency" or performance of the scheme is not strong.

Encouraging collaboration between public research organisations and business is a good thing, but the issue is whether the tax system is the best way to do this.

The tax system is *only one* of several ways R&D, and innovation more broadly, can and should be incentivised. Tax incentives have the advantage that the government does not have to choose which businesses should benefit – the market allocates the subsidy.

Tax system treatments should be simple to use; have low administering costs for the business

R D tax incentives need to be simple and underpin investor confidence

Written by The Conversation

and be market driven. More granular policy treatment, such as encouraging collaboration, is probably better handled by other incentive programs such as loan programs; industry R&D boards and collaboration bodies; research council grants; subsidies for industry groups and trade mission tours.

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