



Australian Government
Department of Industry, Science,
Energy and Resources

R&D Tax Incentive

Guide to Interpretation

A guide to help you assess whether your R&D is eligible for the R&D Tax Incentive



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OVERVIEW

What is the R&DTI?

The Research and Development Tax Incentive (R&D Tax Incentive or R&DTI) encourages companies to conduct research and development (R&D) activities to generate knowledge for the benefit of the Australian economy.

The Department of Industry, Science, Energy and Resources (the department), on behalf of Innovation and Science Australia (ISA), administers the R&D Tax Incentive with the Australian Taxation Office (ATO).

Companies that conduct R&D are often more successful and contribute to economic growth at a higher rate than those that do not. We (the department) want you to plan, conduct and register eligible R&D.

Planned R&D is more likely to generate knowledge that is of benefit to the wider Australian economy. Your business is also more likely to benefit from such R&D. Yet, such research may be a risk for you and may not return a commercial benefit. The R&D Tax Incentive offers a tax offset to encourage you to conduct eligible R&D that you might not otherwise undertake.

Only [eligible R&D entities](#) can apply for the R&DTI. The ATO has information to help you assess whether your business is an eligible R&D entity.

The R&DTI is a targeted tax offset program. It offers a refundable tax offset for R&D entities with an annual turnover under \$20 million. A non-refundable tax offset is available to R&D entities with an annual turnover of more than \$20 million.

These tax offsets are for [eligible core R&D](#) and [supporting R&D activities](#). The *Income Tax Assessment Act 1997* (ITAA 1997) sections 355-25 and 355-30 outline these activities. Activities listed in s 355-25(2) of the ITAA 1997 cannot be core R&D activities. Your activities must meet all of the requirements of the legislation for you to be eligible for the program.

You need to have eligible R&D expenditure of \$20,000 or more to register and claim the tax offset unless you use a registered Research Service Provider (RSP) to conduct your R&D. You can only claim for [eligible expenditure](#). The ATO has guides on eligible expenditure.

The R&DTI supports eligible R&D activities you conduct in Australia. It may also support eligible R&D you conduct overseas. You must apply for and receive an Overseas Finding before you can claim for expenditure on overseas R&D activities.

You may apply for an Advance Finding if you want to know if your R&D activities are eligible. When you apply for a Finding, we may ask for more information. We will then decide if your activities are eligible and explain our decision to you.

How do you apply?

You need to register with us before you can claim for expenditure on your eligible R&D through the ATO. You need to register within 10 months of the end of the income year in which you conduct your eligible R&D activities. We will issue you with a registration number. You will need to enter this number in your annual income tax return.

You are responsible to assess whether you meet all legal requirements before you register for the R&DTI, even if you seek professional advice. Registering with us does not mean your activities are eligible. They remain subject to review.

Registration and review

While the R&DTI is a self-assessment program, we may review your registration. If we do, we will assess whether core R&D activities you describe meet the definition in s 355-25 of the ITAA 1997. We may find some of your activities eligible and others not.

We will work with you to understand your activities. Our guides will help you assess R&D activities you conduct or plan to conduct and register. However our guides provide general advice only. You need to refer to the legislation when you assess whether your activities are eligible.

Why should you read this guide?

This guide will help you assess whether your R&D is eligible for the R&D Tax Incentive. The content in this guide reflects the way we apply the legislation. This is informed where applicable by judgments from the Administrative Appeals Tribunal (AAT) and Federal Court of Australia (FCA). This guide will help you answer four questions:

Q1

Am I an eligible R&D entity?

Section 355-35 of the ITAA 1997 defines the term R&D entity. Only R&D entities can apply for the R&DTI.

Q2

Is my R&D eligible?

The R&DTI allows a tax offset for eligible R&D activities. You need to assess whether activities in your R&D project are eligible and this is the focus of this guide.

Q3

Is my R&D expenditure eligible?

You must register with us for the R&DTI before you can lodge a claim with the ATO for eligible expenditure. The ATO has detailed guidance on eligible expenditure.

Q4

Do I have evidence to support my claim?

We expect you to keep evidence of all activities that you register or plan to register for the R&DTI. Record-keeping is a key part of managing your business and R&D.

How do you navigate this guide?

This guide aims to help you understand key terms of the R&D Tax Incentive.

Each part of this guide covers an aspect of the program. We refer to the relevant sections of the ITAA 1997 and explain the key terms in these sections. When we quote from the legislation we provide the section reference.

We provide hyperlinks to:

- key terms, which appear later in this guide
- our website, the ATO or other organisations

This guide also has visual tools, which include:

- a [self-assessment tool](#) to help you assess if you are eligible to register and claim for the R&DTI
- a way-finder at the top of each page that follows the table of contents – it is a guide to the sections and what comes next

The index at the back of this guide includes key terms and their page numbers. Online, you can click on the page number in the index to find the related term.

Where to get help

We know from experience that the more information and support you have, the more likely you are to register eligible R&D activities. We are here to support you.



For more about the **R&D Tax Incentive, advance and overseas findings**

- **Visit** business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events
- **Visit** *Income Tax Assessment Act 1997* legislation.gov.au/Series/C2004A05138
- You can also read about judgments from the AAT and FCA on our website visit business.gov.au/rdti-external-appeals

SELF-ASSESSMENT

Under the R&DTI, you first need to assess whether your business is an R&D entity. Next you assess if your R&D activities are eligible. Further, you assess whether the associated expenditure on your R&D activities in an income year is eligible. We expect you to keep evidence to support your claim.

The questions in this section will help you assess whether you are eligible to register and claim for the R&DTI. We explain these concepts in later sections.

Q1 – Am I an eligible R&D entity?

The term R&D entity is defined in s 355-35 of the ITAA 1997. Only R&D entities can apply for the R&DTI. Your business is an R&D entity if it meets the following:



R&D ENTITIES

- (1) Each of the following is an R&D entity:
 - (a) a body corporate incorporated under an Australian law
 - (b) a body corporate incorporated under a foreign law that is an Australian resident.
- (2) A body corporate incorporated under a foreign law that:
 - (a) is a resident of a foreign country for the purposes of an agreement in force between that country and Australia that:
 - i. Is a double tax agreement (as defined in Part X of the *Income Tax Assessment Act 1936*); and
 - ii. Includes a definition of permanent establishment; and
 - (b) carries on a business in Australia through a permanent establishment (within the meaning of that definition) of the body corporate in Australia;

is an R&D entity to the extent that it carries on business through that permanent establishment.
- (3) However, an exempt entity cannot be an R&D entity.



For more about
R&D entities

Visit ato.gov.au/rdti

Q2 – Is my R&D eligible?

The R&DTI provides a tax incentive for eligible R&D activities. You need to assess whether activities within your R&D project are eligible, and this is the focus of this guide.

To register [eligible R&D activities](#), you need to conduct or plan to conduct at least one [core R&D activity](#). Some activities are excluded from being core R&D activities. Your [supporting R&D activities](#) must directly relate to your core R&D activities. You must specify your activities when you register them for the R&D Tax Incentive.

Eligible R&D activities may occur over several income years. If you conduct part of an eligible core R&D activity in an income year, explain when and how you will conduct the future parts of your activity.

To be eligible, you must:

- conduct or plan to conduct at least one core R&D activity
- assess that your core R&D activity is not an excluded core R&D activity
- register your core R&D activity
- only register supporting R&D activities that directly relate to a core R&D activity (and, in some cases, that you conduct for the dominant purpose of supporting a core R&D activity)

Q3 – Is my R&D expenditure eligible?

You need to register with us for the R&DTI before you can lodge a claim with the ATO for eligible expenditure. When you register with us, you will receive a number that you will need to quote to lodge a claim with the ATO.

The ATO determines if you have eligible expenditure. It provides a guide to eligible expenditure that will help you assess your R&DTI claim. Your claim will include your R&D schedule and income tax return.

The ATO identifies that an R&D entity's notional deductions may be for expenditure incurred on one or more R&D activities. You must meet all other requirements set out in the ITAA 1997.



For more about
Eligible expenditure

Visit ato.gov.au/rdti



For more about the
R&D Tax Incentive

- Visit business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events

Q4 – Do I have evidence to support my claim?

Record-keeping is a key part of managing your business and your R&D. Applicants who keep records of the activities they conduct, the expenditure on their activities and the connection between their activities and expenditure can support their claims with evidence.

We provide more information about [evidence](#) later in this guide.



For more about **Record-keeping**

- Read more at business.gov.au/taxincentive
- **Visit** the ATO guide at ato.gov.au/rdti

Self-assessment tool

Ask yourself the questions in this tool to help you assess if you are eligible to register and claim for the R&DTI. You can use hyperlinks in the tool to go straight to information about terms. This will help you answer the questions. You should also refer to the legislation as you use this tool and answer the questions to assess whether your activities are eligible.

Q1. Am I an eligible entity?

YES ▼

Q2. Is my R&D eligible?

ASSESS ▼

Does my core R&D activity meet the requirements of s 355-25(1) of the ITAA 1997?

YES ▼

Do I assess that my core R&D activity is an excluded core R&D activity – s 355-25(2) of the ITAA 1997?

NO ▼

I assess that my core R&D IS ELIGIBLE

YES ►

Do I have at least one other eligible core R&D activity that is not excluded?

YES ▼

Could my excluded core R&D activity be a supporting R&D activity?

ASSESS ▼

Do my supporting R&D activities directly relate to my core R&D activities?

YES ▼

Do I assess that my supporting R&D activity produces (or relates to producing) goods or services?

NO ▼

Do I assess that my supporting R&D activity is excluded from being a core R&D activity?

NO ▼

I assess that my core and supporting R&D activities ARE ELIGIBLE

YES ►

Do I conduct my supporting R&D activity for the dominant purpose of supporting a core R&D activity?

NO ▼

I assess that ONLY my core R&D activities ARE ELIGIBLE

NO ►

NO ►

NO ►

NO ►

NO ►

NO ►

NO ►

NO ►

NO ►

I assess that my R&D IS INELIGIBLE

Q3. Is my expenditure eligible?
Q4. Do I have evidence to support my claim?

 I assess that I am **ELIGIBLE** to register for the R&DTI

ELIGIBLE R&D ACTIVITIES

The R&DTI is for eligible R&D activities that you conduct and register. This part of the guide will help you assess whether you conduct or plan to conduct eligible R&D activities.



The main focus of your business may be research and development. However, you will still conduct other business activities that are not eligible R&D activities.

You may vary how much eligible R&D you conduct at different stages of your business journey. For example, you may conduct more R&D in your first year of operation if you are a start-up company that aims to develop a new product. As you start to market and sell your new product, you will likely conduct less R&D. You may then re-invest your sales revenue to conduct more R&D to improve your existing product or develop a new product.

Eligible R&D activities are core and supporting R&D activities. This section of this guide will help you assess whether your R&D activities are eligible.

We explain key terms in the legislation and provide examples. Any examples we provide are for guidance only. Even where your activities might appear like the examples, they may not be eligible for the R&D Tax Incentive. Your activities must meet all of the legal requirements to be eligible R&D activities. You need to assess your activities based on your specific and individual circumstances. You must always assess your activities against the legal requirements.

Core R&D activities

There are key terms that you need to understand under the R&DTI. One of those is core R&D activities. ***You must conduct or plan to conduct, at least one eligible core R&D activity to register for the R&DTI.*** Section 355-25(1) of the ITAA 1997, the law that applies to the program, states:



CORE R&D ACTIVITIES ARE EXPERIMENTAL ACTIVITIES:

- (a) whose outcome cannot be known or determined in advance on the basis of current knowledge, information or experience, but can only be determined by applying a systematic progression of work that:
 - i. is based on principles of established science; and
 - ii. proceeds from hypothesis to experiment, observation and evaluation, and leads to logical conclusions; and
- (b) that are conducted for the purpose of generating new knowledge (including new knowledge in the form of new or improved materials, products, devices, processes or services)

Your activities must meet (a) *and* (b) above to be eligible core R&D activities. They also must not be excluded activities. Section 355-25(2) of the ITAA 1997 lists [excluded activities](#).

Outcome cannot be known or determined in advance

For an activity to be a core R&D activity, a competent professional cannot know or determine the outcome of the activity based on current knowledge anywhere in the world. The outcome needs to be one that you can determine only by applying a systematic progression of work, based on principles of established science.

We expect you to search worldwide for an existing way to achieve your outcome before you start your R&D activity. We expect your records to show you did this.

You need to assess that a competent professional:

- cannot know or determine the outcome of the core R&D activity without an experiment as part of a systematic progression of work; and
- cannot know or determine the outcome based on knowledge, information or experience that is publicly available or reasonably accessible, anywhere in the world

Who is a competent professional?

A relevant competent professional is a person who in their field:

- has knowledge and experience
- has qualifications (if appropriate) or can otherwise act with a reasonable level of skill
- keeps up to date with developments
- has access to knowledge and resources around the world. Such resources include the internet, relevant industry journals and other competent professionals in the field

A competent professional will be a person who has knowledge, skills and experience in a field that relates to your R&D. This might be you or someone else in your organisation or industry sector, a consultant or an academic expert.



How will I know if information is available?

Information that is not reasonably accessible is not available. This may include information that is commercially sensitive and held by a competitor.

If the technical or scientific idea you are testing is in your area of expertise, then you may be aware of whether relevant knowledge, information or experience is available. Even if you or someone in your business is an expert in the field, you will need to research other sources to check that knowledge of how to achieve your outcome does not exist worldwide. You may:

- review scientific, technical or professional literature
- carry out internet searches
- conduct patent searches
- seek advice from an expert or experts

We expect you to keep evidence of your enquiries.

Systematic progression of work

Your systematic progression of work needs to be based on principles of established science. Your systematic progression of work must include the following elements:

Hypothesis

Experiment(s)

Observation

Evaluation

Logical conclusions

All these elements need to be present within your activity. Your activity must meet all of the definition for it to be an eligible core R&D activity.

Your core R&D activity may progress over several income years. You may conduct one or more elements of your systematic progression of work in one income year. We expect you to keep records to show when and how you plan to conduct the other elements in later years.

While the R&DTI is a self-assessment program, we may review your application. If we do, we will review your systematic progression of work as a whole.

We expect your records to show how your activities proceed from one element to the next and how they meet the definition of eligible core R&D activities.



Hypothesis

What is a hypothesis?

Your hypothesis is your idea or proposed explanation for how you could achieve a particular result and why that result may be or may not be achievable.

You may express your hypothesis in a single statement or in several statements that set out what you plan to do and why.

We expect you to explain:

- what result you aim to achieve
- how and why you think you can achieve it, informed by your background research

We expect to see evidence that shows how your background research helped you develop your hypothesis.

Your hypothesis will guide your investigation. You need to develop it before you start your eligible core R&D activities. You need to be able to test it through experiments you conduct to determine the outcome of your core R&D activities.

Experiment

What is an experiment?

An experiment is a scientific procedure that you undertake to test your hypothesis, observe what happens and compare this to what you expect. You may also compare your results to those from previous experiments. We expect you to explain how you conduct or plan to conduct your experiment. For example, you might describe the parameters you vary, those you hold constant, and those you observe or measure.

What you observe and evaluate in your experiment may support your hypothesis, or it may not. That is, you may get the result you expect, or you may get a different result. Either way, your R&D activities may still be eligible for the R&DTI.

You may group a series of experiments in one core R&D activity if each aims to test the same technical or scientific idea.

Where can experiments take place?

Experiments can take place in many environments – from laboratories to process plants, offices or farms. Experiments in these different environments can also take different forms. The details and design of experiments may vary between industries and organisations, but they must aim to test a hypothesis as part of a systematic progression of work.



Observation and evaluation

Observation is where you observe, measure and record information and results that relate to your experiment. Such information can be qualitative (descriptive) or quantitative (numerical data).

Evaluation is where you assess and analyse the results of your experiments. You need to consider what the results of your experiment mean.

We expect your records to show that you evaluate the results of your experiment to understand why and how you achieve or do not achieve your desired outcome. You should analyse how or why something occurs and explain your insights through description. We expect you to analyse numerical data using established techniques. We also expect you to evaluate causal relationships between the parameters you vary, hold constant and measure in your experiment.

Leads to logical conclusions

The final part of the systematic progression of work is to draw logical conclusions about your hypothesis.

When you test your hypothesis through an experiment, your results may support your theory about how to achieve your desired outcome or they may not.

You need to form logical conclusions about why your results support your hypothesis or not. Your logical conclusion may be that you need to investigate different solutions and test a new hypothesis.

You could then test this new hypothesis through new experiments. Your new experiments may be similar enough to include as part of the same core R&D activity. Or, they may be different and need to be part of a new core R&D activity.

Evidence

We expect you to keep records that show you meet the legal requirements to register an eligible core R&D activity for the R&DTI.

Evidence needs to show that you conduct or plan to conduct all the elements of a systematic progression of work. These include:

- hypothesis
- experiment or sets of experiments to test your hypothesis
- observation and evaluation of results from your experiments
- the logical conclusions you draw about your hypothesis

Purpose to generate new knowledge

There are two paragraphs in the legal definition of core R&D activities. Section 355-25(1) of the ITAA 1997 states:



CORE R&D ACTIVITIES ARE EXPERIMENTAL ACTIVITIES:

- (a) whose outcome cannot be known or determined in advance on the basis of current knowledge, information or experience, but can only be determined by applying a systematic progression of work that:
 - i. is based on principles of established science; and
 - ii. proceeds from hypothesis to experiment, observation and evaluation, and leads to logical conclusions; and
- (b) that are conducted for the purpose of generating new knowledge (including new knowledge in the form of new or improved materials, products, devices, processes or services).

Your core R&D activities need to meet both paragraphs (a) and (b) of the definition in s 355-25(1) of the ITAA 1997 to be eligible core R&D activities. They also must not be excluded activities. Section 355-25(2) of the ITAA 1997 lists excluded activities.

Your purpose

You may decide to conduct R&D for several reasons. To be an eligible core R&D activity for the program, one of your substantial purposes to conduct R&D needs to be to generate new knowledge.

Generating new knowledge does not have to be the *sole* purpose of your activity for it to be an eligible core R&D activity. It is key that a substantial purpose to conduct your R&D is to generate new knowledge.

For example, you may have a substantial purpose of generating new knowledge in the form of a new product. If you find that you cannot create that new product, you may still meet the purpose of new knowledge requirement of paragraph (b). If you also meet the requirements of paragraph (a), you may assess that you have an eligible core R&D activity.

You need to have a substantial purpose of generating new knowledge when you conduct your activities. If your *only* purpose at the time you undertake the activities is for a reason other than to create new knowledge, you will not meet the criteria. For example, if you conduct activities for some other purpose and generate knowledge by accident rather than by design, this will not meet the criteria.

Yet, if you go on to plan and conduct core R&D activities to gain additional knowledge, then your new R&D activities may be eligible.

What is new knowledge?

In most cases, your R&D activities will meet the new knowledge aspect of paragraph (b), if they meet the [unknown outcome](#) aspect in paragraph (a).

For example, you conduct your systematic progression of work and find that you do not have support for your hypothesis. If you endeavour to learn why or how you can or cannot achieve your outcome, this can be new knowledge whether you achieve your outcome or not.

New knowledge can be general or applied. It may be new theoretical or practical understanding of a subject. It also may be in the form of a new or improved material, product, device, process or service.

You need to have a substantial purpose to generate new knowledge that does not exist.

Examples:

- Your new knowledge is in the form of a new product if it is a product that does not already exist in the same form.
- You conduct core R&D activities to develop a new or improved *process* to create an existing product or achieve some other outcome. In this case, your purpose of generating new knowledge relates to the process and not to the product that the process may create.

Evidence

We expect you to keep records to show that you meet the legal requirements to register an activity as an eligible core R&D activity for the R&DTI.

We expect your records to reflect what your purposes for carrying out the activities are at the time you start your activities. You need to assess whether generating new knowledge is a substantial purpose *at that time*.

Your evidence will show that your *substantial* purpose for your activity is to generate new knowledge, including new knowledge in a general or applied form.

When you make and keep records, consider that we will want to see evidence of your substantial purpose. Read the [evidence section](#) for examples of records that could support your claim.



For more about the R&D Tax Incentive

- Visit business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events

Is my core R&D activity eligible?

To assess that your core R&D activities are eligible you must assess that each [core R&D activity](#) meets the requirements of s 355-25 of the ITAA 1997. So far in this guide we have provided general advice on how we apply the requirements of s 355-25(1) of the ITAA 1997. In the next section we provide guidance on how we apply s 355-25(2) of the ITAA 1997.



Section 355-25(1) of the ITAA 1997

The outcome of my core R&D activity cannot be known or determined in advance based on current knowledge, information or experience



I can determine the outcome of my R&D activity only by applying a systematic progression of work



My systematic progression of work proceeds from hypothesis to experiment, observation and evaluation. It leads to logical conclusions



I conduct my core R&D activity for the purpose of generating new knowledge



My activity is not an excluded activity listed in s 355-25(2) of the ITAA 1997



I assess that my R&D activity meets the legal definition of a core R&D activity



Exclusions

There are activities that are excluded from being core R&D activities. They cannot be registered as core R&D activities. You must check if any of your activities are excluded from being core R&D activities.

Activities that are excluded from being core R&D activities may qualify as supporting R&D activities if they meet the definition. Read about the requirements for [supporting R&D activities](#) later in this guide. These activities will only be supporting R&D activities if they directly relate to a core R&D activity and you conduct them for the dominant purpose of supporting your core R&D activities. Read the section on [dominant purpose](#) later in this guide.



EXCLUDED ACTIVITIES:

The law, at s 355-25(2) of the ITAA 1997, lists those activities that cannot be core R&D activities for the R&DTI:

- (a) [market research, market testing or market development, or sales promotion \(including consumer surveys\);](#)
- (b) [prospecting, exploring or drilling for minerals or *petroleum for the purposes of one or more of the following:](#)
 - (i) discovering deposits;
 - (ii) determining more precisely the location of deposits;
 - (iii) determining the size or quality of deposits
- (c) [management studies or efficiency surveys;](#)
- (d) [research in social sciences, arts or humanities;](#)
- (e) [commercial, legal and administrative aspects of patenting, licensing or other activities;](#)
- (f) [activities associated with complying with statutory requirements or standards, including one or more of the following:](#)
 - (i) maintaining national standards;
 - (ii) calibrating secondary standards;
 - (iii) routine testing and analysis of materials, components, products, processes, soils, atmospheres and other things;
- (g) [any activity related to the reproduction of a commercial product or process:](#)
 - (i) by a physical examination of an existing system; or
 - (ii) from plans, blueprints, detailed specifications or publically available information;
- (h) [developing, modifying or customising computer software for the dominant purpose of use by any of the following entities for their internal administration \(including the internal administration of their business functions\):](#)
 - (i) the entity (the developer) for which the software is developed, modified or customised;
 - (ii) an entity *connected with the developer;
 - (iii) an *affiliate of the developer, or an entity of which the developer is an affiliate.

(a) market research, market testing or market development, or sales promotion (including consumer surveys);

Market research, testing and development and sales promotion (including consumer surveys) are activities that cannot be core R&D activities for the R&DTI. Sometimes, companies undertake these activities to resolve market or economic uncertainty, rather than technical or scientific uncertainty.

Activities that this exclusion covers include those to:

- discover consumer interest for products or services
- discover consumer preferences about the characteristics of products or services
- promote interest in, or the consumption of, products or services

Example:

You determine that you need to conduct experiments to develop a new product. You use the information you collect from a consumer survey to help you design the experiments you conduct. If your dominant purpose is to support your core R&D activity, then this may be eligible as a supporting R&D activity if it is also directly related to your core R&D activity.

If your dominant purpose for collecting the information is to help you design a marketing strategy for your product or service, it would not be eligible as a supporting R&D activity. This is because your dominant purpose is not to support a core R&D activity.



(b) prospecting, exploring or drilling for minerals or *petroleum for the purposes of one or more of the following:

- (i) discovering deposits;**
- (ii) determining more precisely the location of deposits;**
- (iii) determining the size or quality of deposits**

Your activities that involve prospecting, exploring or drilling for minerals or petroleum, and that you conduct for one or more of the three listed purposes, cannot be core R&D activities.

If your activities involve prospecting, exploring or drilling for minerals or petroleum, assess whether you conduct them to discover deposits, determine the precise location of deposits, or determine the size or quality of deposits. If you do not conduct these activities for one or more of these purposes they will not be excluded core R&D activities. For example, if you drill for samples that you analyse as part of an experiment.

Activities this exclusion covers include prospecting, exploring or drilling activities to:

- find deposits of minerals or petroleum
- pinpoint a more exact location of deposits
- find out how much of a mineral or petroleum is in a location
- analyse how pure a mineral or petroleum deposit might be
- determine the commercial value of a deposit

What is petroleum?

Petroleum is defined in s 40-730(6) of the ITAA 1997 as:

- (a) any naturally occurring hydrocarbon or naturally occurring mixture of hydrocarbons, whether in a gaseous, liquid or solid state; or
- (b) any naturally occurring mixture of:
 - (i) one or more hydrocarbons, whether in a gaseous, liquid or solid state; and
 - (ii) one or more of the following: hydrogen sulphide, nitrogen, helium or carbon dioxide;

whether or not that substance has been returned to a natural reservoir.

The terms prospecting, exploring, drilling and minerals are given their ordinary meaning.

Example:

You drill for mineral samples and analyse the samples to evaluate the quality of the deposit. You then use the information to design, conduct or evaluate experiments within a systematic progression of work to develop a new or improved mineral refining process. Where your dominant purpose when drilling for the mining samples is to support your core R&D activity, then these activities may be supporting R&D activities if they meet all requirements for supporting R&D activities.

If your dominant purpose is to determine whether you will be able to extract the minerals economically using established mining and refining processes, then they will not be eligible supporting R&D activities.



(c) management studies or efficiency surveys;

Management studies and efficiency surveys are activities that cannot be core R&D activities for the R&DTI.

You need to assess whether you conduct activities to collect and evaluate information to help you to make decisions about the business operations of your business or any other business. This exclusion covers those activities.

The exclusion includes studies or surveys you conduct to measure or evaluate certain data. For example:

- the energy efficiency of a business
- the productivity of employees, such as time and motion studies
- management capability
- cost savings for a business
- time-saving measures for a business

The exclusion does not include studies or surveys you conduct as part of a systematic progression of work. For example, to measure or evaluate:

- the energy efficiency of a new or improved electronic product or device that you develop
- the efficiency, productivity or optimal operating conditions of a new or improved process that you develop

Example:

You use the information you collect from an energy efficiency survey to help you to design and conduct experiments to develop a new building environmental management system. If your dominant purpose of conducting the surveys is to support your core R&D activity, then they may be eligible as supporting R&D if they meet all other requirements for supporting R&D activities.

If your dominant purpose is to help you decide how to use energy in your business, then your surveys would not be eligible as supporting R&D activities.



(d) research in social sciences, arts or humanities

Activities that involve experimental and non-experimental research in social sciences, arts or humanities are activities that cannot be core R&D activities for the R&DTI.

When you assess your activities, you need to assess whether you conduct research in these areas, even if this is not your area of primary business operations.

In social sciences, arts or humanities, you conduct research when you gather or compare information, or conduct an experiment or some other inquiry or investigation.

The exclusion includes these subject areas:

- anthropology
- business
- classics
- communication studies
- dance
- economics
- education
- educational sciences
- fine art
- geography
- history
- literature
- music
- performing arts
- philosophy
- politics
- psychology (neuropsychology is not excluded)
- sociology
- theatre
- visual arts

For example, the exclusion covers the activities you conduct that include:

- study of business or economic theory, functions or processes
- design, production or performance of artistic expression
- study of individuals, society, social functions or relationships
- study or production of literature

Examples:

- You develop a mobile app for users to learn languages and your desired outcome is a new method that will result in faster or easier learning. The knowledge you seek is about an education outcome, and your activity would be excluded.
- You conduct a study of the learning styles of individuals. You assess that your study is excluded from being a core R&D activity as it involves research in social sciences. You use the information you collect from the study to help you to design and conduct experiments to develop a new brain sensor. Through your core R&D activities, you aim to develop a sensor that can detect brain wave frequencies to tailor a learning experience for individual users. If your dominant purpose to conduct the study is to support your core R&D activity, then the study may be eligible as supporting R&D. It will need to meet all other requirements for a supporting R&D activity. If your dominant purpose to conduct the study is to help you understand how individuals learn, then it would not be eligible as a supporting R&D activity.

(e) commercial, legal and administrative aspects of patenting, licensing or other activities

Commercial, legal and administrative activities associated with patenting, licensing or other intellectual property (IP) activities cannot be core R&D activities for the R&DTI.

Your ideas and inventions and the new knowledge you generate about them are your IP. If you conduct core R&D activities to generate new knowledge, then that new knowledge is your IP.

You might also generate IP in other areas of your business. Generally, activities that you conduct to *generate* IP are not covered by this exclusion.

Example: Experiments you conduct to develop a new product or process that you intend to protect with a patent are not excluded from being core R&D activities for the R&DTI.

Yet, activities that you conduct to generate IP are not *always* core R&D activities.

Example: You invent a new product or process (your IP). You can develop it without the need for experiments because you can know or determine the outcome in advance. This would not be core R&D activity because it does not follow a systematic progression of work for which the outcome could not be known or determined in advance.

This exclusion includes commercial, legal and administrative activities you conduct to:

- gain rights to use or access IP from another party
- grant rights to another party to use or access your IP
- negotiate an IP sharing agreement
- negotiate non-disclosure agreements
- research, prepare and file an application to protect your IP

Example: You conduct a patent search to gather information to refine your hypothesis and design the experiments that you conduct to test your hypothesis. If your dominant purpose for the patent search is to allow you to design and conduct your experiments, then this may be eligible as supporting R&D. Your activity will need to meet all other requirements for supporting R&D activities. If your dominant purpose is to establish a gap in the market for your products or services, it will be excluded.

What forms of IP are covered by this exclusion?

Forms of IP covered by this exclusion include:

- designs
- domain names
- patents
- plant breeder's rights
- trademarks
- your know-how or proprietary knowledge



For more about
Intellectual Property

Visit the IP Australia website
<https://www.ipaustralia.gov.au/understanding-ip>

(f) activities associated with complying with statutory requirements or standards, including one or more of the following:

- (i) maintaining national standards;**
- (ii) calibrating secondary standards;**
- (iii) routine testing and analysis of materials, components, products, processes, soils, atmospheres and other things**

Activities you conduct to meet a requirement or standard contained in legislation or that are associated with meeting such laws, cannot be core R&D activities for the R&DTI.

Activities that you must conduct to meet requirements or standards contained in legislation are covered by this exclusion. This includes activities that a regulator directs you to conduct as required under legislation.

You may need to comply with legal standards or requirements when you conduct your normal business activities and your R&D activities. Your R&D activities are not covered by this exclusion just because you must conduct them in a regulated manner.

If you conduct R&D activities and need to meet legal requirements on how you conduct your R&D activities, this does not exclude them from being core R&D activities. Activities you undertake to show compliance are excluded.

Examples:

- *Clinical trials you conduct to develop a new or improved drug or device are not excluded from being core R&D activities. Yet, activities that you must conduct to comply with the legal requirements of your clinical trial are excluded. They cannot be core R&D activities. This might include where you prepare and submit your application to a regulator to seek approval to conduct your trial where this application is required by legislation.*
- *Your business is a mining company, and the regulator requires you to produce an environmental impact statement under the relevant environmental legislation to show compliance for your site. You conduct a study to determine the potential impacts on flora and fauna in the area. This would be excluded as a core R&D activity because the law requires you to conduct the study.*

Activities this exclusion covers include those you conduct where required by legislation to:

- show compliance with national standards
- calibrate a secondary standard with reference to primary standard
- routinely test for compliance of your materials, components, products, or processes
- gain certification of your materials, components, products, or processes
- routinely test soils, atmospheres and other things for compliance with a legislative requirement. For example, requirements for environmental protection

Activities covered by this exclusion can be supporting R&D activities if the activities are directly related to a core R&D activity, and your [dominant purpose](#) is to support your core R&D activity. This may include if you gather information such as qualitative or quantitative data you need to allow you to conduct a part of your systematic progression of work.

Examples:

- *You apply to the Therapeutic Goods Administration to gain approval to conduct a clinical trial. If your dominant purpose to gain approval is to allow you to conduct the trial, these activities can qualify as supporting R&D activities. They must directly relate to your clinical trial and your clinical trial must meet all requirements for core R&D activities.*
- *If you collect data from routine tests that will help you evaluate the results of your experiment, and this is your dominant purpose, then these activities can be supporting R&D activities. This is true, even if you also use the information you gather from your activities when you apply to a regulator.*

(g) any activity related to the reproduction of a commercial product or process:

- (i) by a physical examination of an existing system; or**
- (ii) from plans, blueprints, detailed specifications or publically available information**

Activities that cannot be core R&D are those you conduct to reproduce a commercial product or process by examining:

- the actual product or process
- plans, blueprints, detailed specifications or publicly available information

Your activities are not excluded from being core R&D activities if you conduct them to:

- reproduce a product or process in some way *other* than those listed above
- develop a new or improved product or process
- develop a new or improved method for creating an existing product or process

Excluded activities include those you conduct to:

- obtain documents that tell you how a product or process works, or how to produce it
- analyse a sample of a product to gain information about how to make the product
- collect data about the operating parameters of a production process, so that you can replicate the process

Your activities to gather information, including qualitative or quantitative data about an existing product or process, can be supporting R&D activities. They must directly relate to your core R&D activity, and your dominant purpose must be to support your core R&D activity.

Example:

You reproduce an industrial process from the information you find in academic papers or patents. If your dominant purpose is to collect data to help you refine your hypothesis about how to improve the process or develop a new process, this can qualify as supporting R&D. If your dominant purpose is to understand the process so you can replicate it exactly, this will not qualify as supporting R&D.



- (h) developing, modifying or customising computer software for the dominant purpose of use by any of the following entities for their internal administration (including the internal administration of their business functions):
- (i) the entity (the developer) for which the software is developed, modified or customised;
 - (ii) an entity *connected with the developer;
 - (iii) an *affiliate of the developer, or an entity of which the developer is an affiliate.

Activities that you conduct to develop, modify or customise computer software include those to:

- design software
- write new code or modify existing code
- test software
- customise an off-the-shelf software package. For example to make the software perform a different function

If you conduct activities to develop, modify or customise computer software, you need first to assess your dominant purpose to conduct the activities.

If your dominant purpose for the activities is *not* internal business administration for your company or an affiliate company, it is not excluded from being a core R&D activity.

If your dominant purpose is to use the software to administer your company's or an affiliate company's business, then activities you conduct to develop, modify or customise that software cannot be core or supporting R&D activities.

Example: You conduct activities to customise or modify an off-the-shelf software package, which is usually used for internal business administration. Your dominant purpose for modifying the software is to create a new product to sell to other companies that are not affiliates of your company. It is not excluded from being a core R&D activity, as your **dominant** purpose is something other than the day-to-day internal administration of your business or the business of an affiliate. This is true even if you will also use the software in your own business. You will need to assess that the activity meets the other requirements for a core R&D activity for you to register it for the R&DTI.

To determine your dominant purpose to develop, modify or customise computer software, you need to consider all the purposes you have to conduct that activity. You then need to consider the strength of each purpose and how important each is compared to your other purposes.

The exclusion does not apply to activities you conduct to develop, modify or customise software for a dominant purpose other than business administration. This may include software you develop, modify or customise that:

- forms part of an electrical or mechanical device, such as industrial equipment or consumer products
- you used to collect and analyse data from experiments
- you used to provide a service to your customers

Usually, activities that are excluded from being core R&D activities may still qualify as supporting R&D activities. This is not the case for software development, modification or customisation activities that are covered by this exclusion.

If your activity is excluded from being a core R&D activity because the *dominant purpose* for that activity is to use the software in the internal administration of your business or an affiliate's business, then the dominant purpose cannot also be to support a core R&D activity.

You may have several purposes for conducting the activity, but you can only have one dominant purpose.



You may assess your software development activities as core R&D activities that are not subject to this exclusion. If so, we expect to see records that support your assessment around internal administration and your dominant purpose.

What is internal administration?

Internal administration functions include:

- Business applications such as payroll and accounting, invoicing, ordering, quality control reports and information management
- Management information systems
- Enterprise resource planning

Affiliate

Your company is an affiliate with another company if that company acts or you can expect it to act to suit the directions or wishes of your company. This does not apply simply because your company has a commercial relationship with another company – such as with a supplier. **This term is defined in s 328-130 ITAA 1997.** For more information visit ato.gov.au.



For more about the R&D Tax Incentive

- Visit business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events

Supporting R&D activities



SUPPORTING R&D ACTIVITIES:

The legislation, at s 355-30 of the ITAA 1997, states:

- (1) Supporting R&D activities are activities directly related to core R&D activities.
- (2) However, if an activity:
 - (a) is an activity referred to in subsection 355-25(2); or
 - (b) produces goods or services; or
 - (c) is directly related to producing goods or services;

the activity is a supporting R&D activity only if it is undertaken for the dominant purpose of supporting core R&D activities.

After you assess that you conduct or plan to conduct at least one core R&D activity, you can assess whether you conduct any activities that meet the definition of supporting R&D activities.

R&D activities in different years

You can conduct supporting R&D activities before, during or after your core R&D activity.

Directly related to a core R&D activity

You need to identify the core R&D activity to which your supporting R&D activity directly relates. We also expect you to identify the relationship of the activity with the elements in your systematic progression of work.

We expect you to identify and record what that relationship is when you conduct your activities and to explain what that relationship is when you apply to register your activities.

Whether your supporting R&D activity directly relates to a core R&D activity will depend on your circumstances. We expect you to analyse your specific circumstances and keep records to support your claim.

Examples:

- a literature review to refine your hypothesis before you conduct your experiment
- you clean and maintain the equipment you use during experiments
- you decommission and dismantle equipment you used in experiments after you have reached logical conclusions

When you plan your R&D, you may have a multi-year plan that schedules different activities over several years.

You may conduct your supporting R&D activity in a different year to your core R&D activity. You could conduct an activity in a current year to support a core R&D activity that you conduct and register in a prior or future year. If you do this, you should explain this to us when you register for the R&DTI.

Example: You plan to conduct R&D at the same time as you conduct your other business activities. Your plan includes a schedule of your R&D activities over three years. In the first year, you conduct an extensive literature review and consult with experts in the field. You use this information to plan your systematic progression of work. In year 2, you start your core R&D activities and document the experiments that you conduct. Year 3, you continue your experiments, in which you construct a pilot plant and observe results from test runs. In year 3, you evaluate results from your test runs. Year 4 is where you plan to apply the new knowledge you generate and move from pilot to full-scale production if your hypothesis is supported. You may need to conduct further R&D to scale-up production. You will need to assess whether your scale-up activities meet the requirements for core R&D activities. You may not know this until after you evaluate the results of your experiments to develop the pilot plant.

You may register the supporting R&D activity of your literature review and research for year 1. We will expect to see your records that show you plan to conduct eligible core R&D activities in years 2 and 3. Your records will need to show that you meet the requirements as an [R&D entity](#), and you plan to conduct at least one eligible core R&D activity.

What activities are not supporting R&D activities?

Activities that do not directly relate to your core R&D activities cannot be supporting R&D activities. Your activities will likely directly relate to your core R&D activities if they support you to conduct your systematic progression of work.

Examples of activities that will not usually have a direct relationship to a [core R&D activity](#) include:

- a literature review or internet search that you conduct to identify a market niche for a new product
- you clean and maintain equipment that you do not use for an experiment
- you decommission and dismantle equipment that you did not use to conduct experiments

Key aspects of supporting R&D activities

- You may have several supporting R&D activities for each core R&D activity if each satisfies the requirements
- Supporting R&D activities may take place before, during or after your relevant core R&D activity
- Each supporting R&D activity must directly relate to at least one of your core R&D activities

Dominant purpose

When do I need to have the dominant purpose of supporting a core R&D activity?

Supporting R&D activities must directly relate to a core R&D activity to be eligible. You must conduct some supporting R&D activities for the dominant purpose of supporting your core R&D activities. These include activities that:

- are excluded from being core R&D activities
- produce goods or services
- are directly related to producing goods or services

In any of these circumstances, you need to assess whether you conduct each of these activities for the dominant purpose of supporting a core R&D activity.

What is dominant purpose?

Dominant purpose means your prevailing or most influential purpose. Your main purpose of conducting your activities *must* be to support a core R&D activity.

How do I assess my dominant purpose?

To determine your dominant purpose to conduct an activity, you need to consider all of your purposes. You then need to consider the strength of each purpose and how important it is compared to your other purposes.

You need to consider:

- how and when you conduct your activity or establish the need to conduct your activity. This will usually be when you plan or conduct your core R&D activity
- what other purposes you have to conduct your activity and whether one of the other purposes is more influential
- how you conduct your activity for the dominant purpose of supporting a core R&D activity. Ask what your activity involves, and why you need it to conduct an element of your systematic progression of work for your core R&D activity
- whether your activity goes beyond activities you would have conducted if you did not conduct your core R&D activities

Activities that are likely to have the dominant purpose of supporting a core R&D activity include activities that:

- have no other purpose than to assist or facilitate a core R&D activity
- support core R&D activities and where the direct commercial benefit is insignificant
- produce items that you consume, or you expect to consume in your experiment
- create a component to use in a core R&D activity where it serves no other purpose. For example, a part of the experimental apparatus

Activities that are unlikely to have the dominant purpose of supporting a core R&D activity include those that:

- produce a good or service that you do not need to conduct an experiment
- you would undertake if you did not conduct R&D

Activities that produce goods and services

For your supporting R&D activities that produce or that directly relate to producing *goods*, you must be able to show that you conduct them for the dominant purpose of supporting a core R&D activity. This is regardless of the scale of manufacture or the end user.

Also, you must be able to show that you undertake your supporting R&D activities that produce or that directly relate to producing *services* for the dominant purpose of supporting a core R&D activity. This is regardless of the terms of the services or whether those services are for your company.

Whether you conduct an activity for the dominant purpose of supporting a core R&D activity will depend on your specific circumstances. We expect you to analyse and explain your circumstances and keep evidence to support your claim.



For more about the R&D Tax Incentive

- Visit business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events



CASE STUDY: **BAKING STUFF AND A FISHY TALE**

This is a hypothetical case study designed to explain the eligibility requirements for the program.

Sometimes applicants quote our case studies saying that their circumstances are the same. Although your circumstances may appear similar to this case study, your activities may not be eligible. You need to assess your activities based on your specific circumstances. You must assess your activities against the legal requirements.

Summary of case study

Outcome

Baking Stuff seek to create new bread products that contain fish oil as a source of Omega-3.

Current Knowledge

Baking Stuff search worldwide and cannot find current knowledge, information or experience to tell them how to achieve their outcome. Current information suggests that it is not possible to add fish oil to bread. They conclude that they must conduct a systematic progression of work to determine whether they can create new bread products.

Hypothesis

For each core R&D activity, their systematic progression of work proceeds from a hypothesis informed by background searches. They review literature and patents that relate to:

- microencapsulation for controlled release of vitamins
- effect of temperature on microcapsule coatings
- effect of enzymes on microcapsule coatings

Experiments

They contract a Research Service Provider (RSP) to help them design and conduct experiments to test each hypothesis. They produce experimental batches of bread on a separate line of their commercial baking machine.

New knowledge

Their purpose is to generate new knowledge in the form of new products. When they start their R&D activities there is no bread on the market worldwide that contains fish oil as a source of Omega-3. They will also generate new knowledge about how to add fish oil to bread.

Eligible core R&D activities

Core Activity 1 - Microencapsulated fish oil additive for whole-grain bread – dispersion and stability of a fish oil additive in different whole grain mixtures

Core Activity 2 - Understand the enzyme resistance of fish oil microcapsules – laboratory experiments

Eligible supporting R&D activity

Supporting Activity 1 - Background research into the properties of fish oil microcapsules

Self-assessment

Q1

Is Baking Stuff an eligible R&D entity?

Baking stuff is a body corporate incorporated under Australian law. It is not an exempt entity. They meet the requirements of s 355-35 of the ITAA 1997.

Q2

Is their R&D eligible?

Baking Stuff assesses that they have two core R&D activities that meet the requirements of s 355-25 of the ITAA 1997. They also assess they have one supporting R&D activity that meets the requirements of s 355-30 of the ITAA 1997.

Q3

Is their R&D expenditure eligible?

Baking Stuff reviews ATO guidance on eligible expenditure. They register their eligible R&D activities with us and then lodge a claim with the ATO for eligible expenditure.

Q4

Do they have evidence to support their claim?

Baking Stuff keeps evidence of all activities that they register for the R&DTI. They also keep records of associated eligible expenditure.

About Baking Stuff

Baking Stuff is a small Australian company that produces three different kinds of bread for the consumer market – white, whole grain and fruit bread.

Their usual business activities include:

- producing bread products using their purpose-built production line
- market development activities to promote interest in their bread products
- sales and distribution

Results from a recent market survey Baking Stuff conducted shows that consumers want healthier bread options. They identify that Omega-3 is one of the nutrients that consumers would like to see in their bread.

The directors of Baking Stuff decide that they would like to create a bread with fish oil as a source of Omega-3. They have the qualifications, knowledge and experience they need to develop and produce baked goods. They also keep up to date with new developments in food technology and consult with experts in other fields at conferences worldwide. They are competent professionals.

To the best of their knowledge, there is no bread on the market worldwide that contains fish oil as a source of Omega-3. They search for information in food technology journals and consult with other experts in their networks. They find a recent study from an overseas university which concludes that it is not possible to add fish oil to bread without adding a fishy flavour and without it reacting with other ingredients. In their research, they do not find any other studies about fish oil additives in baked goods.

They find an article in a journal about microencapsulation. The article discusses the use of microencapsulation for controlled release of vitamins. The vitamins are sealed in a coating so that they only release once they reach the digestive system.

The directors of Baking Stuff wonder if they can adapt this technology to develop their bread. They form a hypothesis about how they might use microencapsulation to seal fish oil in a coating so that it releases when it enters the digestive system.

The only product on the market that uses microencapsulated fish oil is a vitamin product that is supplemented with Omega-3. The company that produces the vitamin product holds the technology as a closely guarded secret.

Baking Stuff approaches the vitamin company and asks to licence the intellectual property to create microencapsulated fish oil. The company will not agree to license the technology but agrees to supply Baking Stuff with microencapsulated fish oil for their experiments. They also state that they are willing to enter into a commercial supply arrangement if Baking Stuff is successful and starts to produce the bread with the additive.

While Baking Stuff can source microencapsulated fish oil for their experiments, there is no publicly available information about the impact of adding it to their whole-grain bread.

Baking Stuff establishes that they can only determine the outcome of their activities by conducting experiments to test their hypothesis.

R&DTI self-assessment

Baking Stuff thinks that they may be eligible for the R&DTI.

First, they assess that they are an eligible R&D entity.

Next, they check the requirements for eligible R&D activities and review their project plan to assess whether the activities they plan to conduct are eligible.

They consider that some of their activities meet the requirements to be core R&D activities. They assess that these activities meet the requirements of [s 355-25 of the ITAA 1997](#) because:

- they can only determine the outcome through a systematic progression of work that is based on principles of established science and proceeds from their hypothesis
- there is no current knowledge that can tell them how to achieve their desired outcome
- they plan to conduct experiments to test their hypothesis about the use of microencapsulated fish oil in bread
- they plan to evaluate the results from their experiments to reach conclusions about their hypothesis
- they will document their activities and the conclusions they reach
- their purpose is to generate new knowledge in the form of an improved bread product
- they will also generate new knowledge about how to add fish oil to bread
- their activities are not excluded core R&D activities

They assess that they may also be able to register supporting R&D activities and that these activities can occur before, during or after their core R&D activities.

Their idea to create a bread that contains Omega-3 came from their market research, so they wonder whether these activities might qualify as supporting R&D activities. When they check the program requirements, they see that market research is excluded from being a core R&D activity. It can only be a supporting R&D activity if it directly relates to a core R&D activity and is conducted for the dominant purpose of supporting a core R&D activity.

They assess that their dominant purpose for market research was to test consumer preferences. Further, they only had the idea to create a new bread product after they evaluated the survey results. They decide that the dominant purpose of the survey was not to support their core R&D activity. They cannot register it as a core or a supporting R&D activity.

When they commence their activities, they implement a system to keep records to show that their activities meet the requirements of the R&DTI. They also keep records of their eligible R&D expenditure that show the link to their eligible R&D activities.

Eligible R&D activities

For their first core R&D activity, Baking Stuff designs a set of experiments in which they will produce different batches of bread with different mixes of grains and microencapsulated fish oil (the additive). They will also test different baking temperatures and mixing speeds. They plan to produce the test batches on a separate line of their commercial baking machine.

They find information about the micro-encapsulation coating material that suggests the grains might cause it to break down when they mix the additive into the bread. Information also shows that the coating can break down under very high temperatures.

They use this information to help decide how to design their experiments.

They plan to start with a batch that contains fewer abrasive grains and less fish oil, then vary the proportions of fish oil and grains in successive experiments. These are the variables that they think will have the most bearing on whether they can achieve their outcome. They base this assumption on the available information in scientific journals.

As their standard baking temperature is lower than the high temperatures described in the prior information, they decide only to run their experiments at their standard baking temperature.

Baking Stuff cannot find any current information to tell them whether adding microencapsulated fish oil will achieve the result they want. There is no information available to enable them to predict what the possible effects might be. They cannot determine how encapsulated fish oil might react with different grains. This also is not discernible by a competent professional. They can only test the effects of the grains on the fish oil additive if they bake it into loaves.

They know that they need to analyse samples from each test batch to evaluate the effect of the different grain and fish oil mixtures on the final product. Baking Stuff determines that they do not have the equipment and expertise in-house to analyse the samples and evaluate results from the experiments, so they contract a food science laboratory to do this. The laboratory is a Research Service Provider (RSP) for the R&D Tax Incentive. They sign a research services agreement, which states that the laboratory will:

- guide Baking Stuff on how to produce the experimental test batches and take samples
- analyse the samples
- evaluate the results
- provide reports to Baking Stuff with results and conclusions about the experiments

Baking Stuff assesses that the activities under the research services agreement form part of the systematic progression of work that proceeds from their hypothesis about adding microencapsulated fish oil to bread. They also assess that the activities they conduct to produce test batches are part of the core R&D activity. They understand that their core R&D activity will be complete when they reach logical conclusions about the effects of different proportions of fish oil and grains, and different mixing speeds, on the final bread product.

For test batches high abrasive grain content and more fish oil, they find that clumps form in the dough. The RSP determines that the abrasive grains break down the coating on the additive at certain mixing speeds. This causes the additive and grains to clump together. They analyse results from the test batches to determine the optimum mix of grains and additive for the whole grain loaf. They also determine the optimum mixing speed. The RSP could not predict the outcomes of the core R&D activities in advance. They could only determine them through a systematic progression of work based on principles of established science. This concludes the first core R&D activity.

Baking Stuff progress to full-scale commercial production. They set the mixing speed of their full-scale production lines to the optimum mixing speed they determined from their experiments. They add the optimum mix of grains and fish oil additive. They can predict that the bread loaves produced at full scale will meet their desired outcomes in relation to taste, the quality of the loaves, and the integrity of the additive. They do not need to conduct any scale-up experiments.

Once they introduce the fish oil additive into their whole-grain bread, Baking Stuff decides to try it in other products. As their white bread has no abrasive ingredients, they conclude that they do not need to do further experiments.

For their fruit loaf, Baking Stuff is unsure about how the fruit enzymes will interact with the fish oil additive. There is no available information about how fruit enzymes interact with the microcapsule coating. For their second core R&D activity, they contract the RSP to conduct experiments to test their hypothesis about the effect of the enzyme on the coating. Results show that the enzyme breaks down the coating. On this basis, Baking Stuff does not add the fish oil additive to their fruit loaf.

Registration

At financial year-end, Baking Stuff assesses that they have two core and one supporting R&D activity for the R&DTI. They register them with us and claim associated expenditure in their tax return.

For their first core R&D activity, Baking Stuff produces test batches of bread on a separate line of their commercial baking machine. They claim this production of experimental batches as part of their core R&D activity. Baking Stuff keep records to show that the production of experimental batches of bread is part of their core R&D activity. However, the batches of bread they produce on their commercial lines are not eligible as they produce them for commercial purposes, and they do not have a direct relationship to core R&D activities.

When Baking Stuff decides to apply their new knowledge to a white loaf, they assess that they do not need to conduct experiments. This is because they can apply the information they gained from the whole-grain loaf experiments to predict that they can achieve the desired outcome with the white loaf. They do not claim the production of any white loaves as core or supporting R&D activities.

For the fruit loaf, they test how the fruit enzymes react with the microencapsulated fish oil. The RSP conducts experiments in a laboratory. This is an eligible core R&D activity (Core Activity 2). Baking Stuff does not produce any fruit loaves that contain the fish oil additive. They do not claim the production of fruit loaves as a core or supporting R&D activity.

Eligible core R&D activities

Core Activity 1: Microencapsulated fish oil additive for whole-grain bread – dispersion and stability of a fish oil additive in different whole grain mixtures

Core Activity 2: Understand the enzyme resistance of fish oil microcapsules – laboratory experiments

Eligible supporting R&D activity

Supporting Activity 1 – Background research into the properties of fish oil microcapsules

Evidence

Baking Stuff keeps records of their eligible activities at the time they conduct them. They also keep records of eligible R&D costs.

The records they keep when they conduct their core R&D activities show that they are based on principles of established science. They also show that the core R&D activities contain all elements of a systematic progression of work. That is, they proceed from hypothesis to experiment, observation and evaluation, and lead to logical conclusions.

The records they keep include:

- R&D plan to outline the objectives of the project
- internal reports that document the baking trials
- reports from the RSP that show the results of experiments, analysis and conclusions
- extra columns in standard run sheets to record test batch changes
- evidence of payments to the RSP showing activities and expenditure
- expenditure they incur to produce test batches
- evidence of other expenditure they incur on core and supporting R&D activities showing the link to the activities

EVIDENCE

We expect you to keep records of activities that you register or plan to register for the R&DTI. We expect your evidence will show how you conduct or plan to conduct core R&D activities:

- that are based on principles of established science
- whose outcome cannot be known or determined in advance on the basis of current knowledge, information or experience worldwide
- whose outcome can only be determined by applying a systematic progression of work - hypothesis, experiment, observation and evaluation, leading to logical conclusions
- for the purpose to generate new knowledge
- that are not excluded from being core R&D activities

In your systematic progression of work, we expect to see details of how you:

- develop your hypothesis
- design your experiment
- observe and record the results of your experiment
- evaluate your results
- reflect conclusions about your results. Do they support your hypothesis or generate other new knowledge?

We also expect evidence to show that your supporting R&D activities directly relate to at least one core R&D activity and, in some cases, you conduct them for the dominant purpose of supporting a core R&D activity.

We expect you to keep records so that you can provide them to us if we review your application for the R&DTI. Your systems and processes that identify, evaluate and record your eligible R&D activities and expenditure will be evidence to support your claim.

What happens if we review your registration?

When we review or examine your registration or application, we will ask for evidence to show that you have conducted, are conducting or plan to conduct eligible R&D activities. We will assess your activities on the evidence you supply to us. We sometimes also conduct our own research. We will use all available information to assess whether your R&D activities are eligible for the R&DTI.

In our work, we follow principles of procedural fairness. We will allow you to comment on information we find that we will rely on when we assess your R&D activities. We will base our assessment on the legal requirements in the ITAA 1997.

We will work with you to ensure you have the opportunity to provide evidence to support your claim. We may also ask to speak with the technical staff you employ or contract.

Types of evidence we consider if we assess the eligibility of your R&D activities include:

- **contemporaneous:** records you make around the time you plan and conduct activities are your evidence as to why and how you conduct your activities
- **non-contemporaneous:** records that you create outside the period of your R&D activity, yet relate to that R&D activity

We expect that you will make records before or around the time you conduct your activities. These will be the strongest evidence of your R&D activities.

If we find that your records do not support your claim, we will give you the opportunity to provide further detail. If you are unable to supply evidence to support your claim, we may find that you did not conduct or plan to conduct eligible R&D activities.



For more about
**what will happen if we review
or examine your registration**

Visit business.gov.au/taxincentive

Records to show eligibility

We list some examples of records that may show aspects of your R&D activities.. Many of these are general business documents and may not by themselves establish the eligibility of your R&D activities.

Together with other evidence, these documents may support your eligibility.

CORE R&D ACTIVITIES

You have an idea about how you can develop a new or improved material, product, device, process or service. You conducted, are conducting or plan to conduct R&D to test your idea	Evidence: Your records support that you cannot know or determine the outcome in advance, and you need to conduct an experiment or experiments to verify that your concept is possible	Examples: • business case • contracts or research arrangements • emails • experimental protocols or test plans • Gantt charts • letters or reports from competent professional or expert • patent and other searches • technology reviews • journal articles • project approvals or meeting minutes • project plans • prototypes • records of trial runs • reports of test results and analysis • records of regulatory approvals
You conduct your R&D through a systematic progression of work	Evidence: Records of: • hypothesis • experiments • observation • evaluation • logical conclusions	Examples: • contracts or research agreements • email correspondence • enterprise management system records • experimental and research plans that pre-date your activities • laboratory notebooks • photographs and videos • process diagrams • progress reports • project plans • prototypes • records of trial runs • test reports that show results and analysis of experiments
Your purpose is to generate new knowledge	Evidence: Your records support that your substantial purpose to conduct your activity is to generate new knowledge	Examples: • annual reports • ASX announcements • board minutes • contracts • email correspondence • project plans

SUPPORTING R&D ACTIVITIES

Your records establish a direct relationship between your supporting R&D activity and your core R&D activity	Evidence: The relationship is direct	Examples: • annual financial reports • business plans that describe your supporting R&D activities • plans that pre-date the start of your supporting R&D activities • prior year claims • technical project documents
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OTHER GUIDES

This guide is our primary guide to explain the key terms of the R&D Tax Incentive. We have other guides, including hypothetical case studies at www.business.gov.au/taxincentive.

GUIDES	LINK
Agrifood Agrifood is a highly integrated value chain spanning food and beverage enterprises from paddock to plate.	https://www.business.gov.au/rdti-agrifood
Biotechnology Biotechnology includes the subsectors of life sciences, industrial processing, agriculture and environment.	https://www.business.gov.au/rdti-biotechnology
Built environment The built environment is the material, spatial and cultural product of human labour and imagination.	https://www.business.gov.au/rdti-built-environment
Energy The energy sector covers generation, distribution, storage, transport and emerging technologies.	https://www.business.gov.au/rdti-energy
Manufacturing The manufacturing sector produces everything from FMCG to aerospace components.	https://www.business.gov.au/rdti-manufacturing
Software development	https://www.business.gov.au/rdti-software-development
External appeals Learn about judgments from the Administrative Appeals Tribunal (AAT) and Federal Court of Australia.	https://business.gov.au/rdti-external-appeals
Federal Register of Legislation	https://www.legislation.gov.au/
Australian Taxation Office	https://www.ato.gov.au/rdti



For more about the
R&D Tax Incentive

- **Visit** business.gov.au/taxincentive
- Contact us on **13 28 46**
- Or attend one of our events or information sessions visit business.gov.au/rdti-events



For more on
**expenditure related
record keeping**

- **Visit** ato.gov.au/rdti

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