

AUSTRALIAN INDUSTRY
GROUP

Pre Budget Submission

The 2006-07 Budget

November 2005

Executive Summary

Ai Group estimates the starting point for the Budget is a fiscal surplus comfortably above \$10 billion in 2006-07 and in 2007-08. With expectations being for steady if unspectacular growth, the 2006-07 Budget should capitalise on budgetary strength and take decisive steps in two key policy areas.

The Budget should complement the Government's wider reform agenda and in particular its reforms to industrial relations and welfare eligibility by:

- Reducing the marginal rate of personal income tax applying to lower income earners from 30% to 15%;
- Improving access to work-related training programs for people transitioning to the workplace; and,
- Boosting the incentives faced by low-income individuals considering investing in their own work-related skills.

The Budget should also help lay the foundations for the next phase of Australia's economic development by:

- Facilitating the development of Australia's business capabilities;
- Improving the focus on the ongoing skill development of existing employees;
- Making the Australian innovation system more effective; and,
- Addressing barriers to greater global engagement by Australian businesses.

Supporting Lower-Income Earners

Ai Group's proposal to reduce the tax rate applying to lower income earners from 30% to 15% will slash the effective marginal tax rates faced by members of low-income families and will provide greater rewards for people moving from welfare to work. In addition, low and middle-income earners will receive a sizable rise in disposable incomes.

- By boosting incentives to work and improving after-tax incomes, this measure will complement the Government's workplace relations changes aimed at making workplaces more flexible and productive.
- By cutting the effective marginal tax rate barrier to workforce participation, the measure will also complement the increased emphasis on encouraging recipients of income support payments to find work.

As a leading advocate of workplace relations reforms and of measures to reduce Australia's relatively high levels of welfare dependency, Ai Group believes an emphasis on providing tax relief, improved incentives and training opportunities to lower income earners will improve the effectiveness of the overall policy mix.

Investing in Productivity: the Key to Future Growth

Ai Group's proposal for the Government to become more active in preparing the foundations of the next phase of growth is based on our recognition of the profound shifts in the global economy and of the extent to which they are challenging existing businesses and industries.

These global shifts are occurring alongside the demographic changes that demand an increased emphasis on domestic productivity growth.

Ai Group will shortly launch two major initiatives *Manufacturing Futures* and *World Class Skills for World Class Industries* in which we will put forward detailed policy measures aimed at boosting Australia's productivity performance over the next phase of Australia's economic development.

These policy initiatives will:

- Lift Australia's business capabilities across the full spectrum of industry and particularly among small and medium sized businesses;
- Place a greater emphasis on the ongoing re-skilling of existing workforces;
- Improve the effectiveness of Australia's innovation system; and
- Reduce existing barriers to greater global engagement by Australian businesses.

Budgetary Position and Outlook

Ai Group believes the Government can embark on these changes while still making small contributions to the Future Fund and maintaining a strong budgetary position.

The major risk to this strategy is one of adding to any additional inflationary pressures that build up over the coming months. Two factors help to offset this risk:

- In the present environment of consumer caution, a sizable share of higher disposable income will be directed to reducing existing household debt; and
- Ai Group believes that a tax cut that delivers significant increases in disposable incomes for lower-income earners will help ease some of the existing pressures on wages and business costs.

Clearly a close eye needs to be kept on inflationary pressures between now and May. If inflationary risks accumulate faster than anticipated, Ai Group would support a phased introduction of the measures put forward in this submission.

Summary of Budget Proposals

Personal Taxation and Taxes on Superannuation

(Fact Sheet 1)

- Increase the low income tax offset.
- Raise the threshold at which the 30% tax rate applies.
- Reduce the 47% tax rate.
- Commit to a phased removal of the 15% tax levied on superannuation contributions.

Fostering Greater Global Engagement by Australian Business

(Fact Sheet 2)

- Building effective export promotion programs by revamping the Export Market Development Grant Scheme.
- Removing tax barriers to offshore investment by Australian-based companies.

Building Business Capabilities

(Fact Sheet 3)

- A new Ai Group proposal to enrich the capabilities of Australian businesses across the full spectrum of industry and particularly among small and medium-sized businesses. The proposal includes:
 - a whole-of-government strategy using advisers to assist business with growth strategies and link them to industry and government initiatives to support their business plan; and,
 - the development of nationally networked regional and industry collaboration clusters.

Skilling the Australian Workforce

(Fact Sheet 4)

- A new focus on the ongoing re-skilling of existing employees to complement attention given to entry-level skills.
- Greater business involvement in skills development strategies.
- Improved recognition and authentication of skills.
- Improved incentives for individual and business investments in skills.

Sharpening Australia's Innovation System

(Fact Sheet 5)

- Making the Research and Development Tax Concessions effective.
- Streamlining the compliance costs of innovation programs.
- Improving linkages between business and public sector research including by addressing barriers to public/private research collaboration.

The Economic Setting

Longer Term Forces

The continuing emergence of China and India along with strong growth from Brazil and the substantial scope for Eastern European catch-up looks set to underpin an extended era of strong global growth.

While these profound global developments present an embarrassment of potential opportunities for Australians, they also present competitive challenges to existing paradigms and call for a reinvigoration of economic direction and productivity growth.

As with other developed economies, Australia is facing these new dynamics in the global economy at the same time as internal demographic forces are beginning to exert their dampening impact on economic growth. These demographic pressures are also challenging the medium and longer-term sustainability of current budgetary settings.

Averting a collision course with our “demographic destiny” requires a greater emphasis on raising productivity; improving workforce participation; lifting national saving and ongoing fiscal discipline.

Fiscal Discipline

Ai Group supports giving continued strong attention to fiscal discipline. This discipline is needed both to help stem the rising tide of Australian taxation and to strengthen Australia’s budgetary position as demographic trends unwind.

Nevertheless, an emphasis on fiscal discipline should not stand in the way of making worthwhile expenditures that help boost economic activity and saving. Appropriate expenditure targeted to improving productivity; workforce participation and saving is consistent with longer-term fiscal discipline. Consequential faster growth in GDP will help stem the continuing rise of the share of total tax in GDP and it will help in sustaining ongoing funding of worthwhile government programs.

In this context Ai Group reiterates the view that it is often appropriate that governments borrow funds in excess of recurrent revenues in order to make net-worth enhancing investments in infrastructure.

In the immediate term, with a substantial pipeline of projects already evident and skill shortages already quite severe in the relevant industries, Ai Group does not see much scope for additional investments. We continue to support better planning and coordination of infrastructure development at all levels of government.

The Medium Term

The economy looks on track to make steady if unspectacular progress over the next couple of years.

- Both the Commonwealth and the States and Territories have very strong budgetary positions with a standard fare of surpluses, low debt and provisioning for superannuation liabilities.
- The housing bubble is unwinding relatively gently.
- Growth in non-residential construction has covered much of the slack left by a retreating residential sector.
- Surging consumer spending has come back to sustainable levels;
- While the current account deficit remains of concern, its recent entry into record territory looks to be behind us as export volumes seem to be edging higher (albeit across a narrow range of goods and services). In addition, some of the steam has gone out of consumer imports.
- Capital investment has been healthy compared with recent years.
- Employment growth, so strong for so long, is moderating and unemployment has begun to edge upwards.
- In this environment skill shortages, which are widespread, are likely to remain a significant barrier to business development.
- Wages growth has been generally moderate – particularly for this stage of the cycle.
- Businesses appear to have absorbed a good share of higher energy prices and the strong price rises of other material inputs.

Australia's Current Account Deficit

The weakness in the current cycle and the major source of concern for the medium term is the poor current account performance.

- The disappointments with the current account deficit (CAD) are compounded when the strength of the terms of trade is taken into account. Limited capacity in the minerals sector and in areas of bulk commodity export infrastructure have, to date, limited the domestic supply response to surging demand from the emerging economies.
- At the same time, continuing drought has restrained the export contributions of the rural sector.
- Exports markets for services and manufacturers have eroded in the face of more intense global competition and a currency at challenging levels.
- Continued growth of domestic consumer demand, cheaper import prices and the strength of the currency has seen a rise in import penetration and an erosion of market share of many domestic producers.
- The high growth in income outflows, attributed to high profits paid to foreign investors, adds to the trade imbalance.

The other side of the external account coin is the very low levels of domestic saving. While this has been related to a domestic “wealth effect”, much of the additional borrowing appears to have gone towards

residential housing and consumption rather than income-producing investments. Australia's external imbalance is supported by the continued willingness of foreign investors to provide funds. Adding to the other advantages of Australia, investors have been attracted, and rewarded, by solid interest rate differentials between Australia and most of the rest of the world.

A downward correction in the currency – driven by a fall in commodity prices and/or a reaction by foreign lenders to a lower interest rate advantage, would help Australian exporters and import competing businesses regain some export market share. This would bring welcome relief to many businesses in the manufacturing and service sectors.

At the same time a fall in the currency would add to inflationary pressures and may also slow the rate of investment in imported capital equipment. It is likely that, even if the currency fell back to below \$US 0.65, this would not, of itself, recover the full loss of market share that has occurred over the past few years. Thus, for manufacturing and the services sector to recover the lost export territory and position themselves for further gains, a clear lift in productivity will be required.

If, on the other hand, the currency remains high (whether due to commodity prices being sustained over a "super cycle" or merely because of a lagged response to commodity price corrections) productivity improvements across the economy will assume an even greater importance. In their absence, we risk a "hollowing out" of capabilities in these important sectors and a higher dependence on a narrower range of commodity exports.

Implications for Policy

The re-emergence of the CAD at a time when the terms of trade are particularly favourable is a warning sign for the Australian economy. In the new global environment we need to push for further productivity improvements and we need to boost national saving.

These directions, together with an emphasis on greater workforce participation and ongoing fiscal discipline, are the same priorities required to respond to our demographic challenges.

Ai Group's approach to the 2006-07 Budget is therefore aimed squarely at improving productivity, workforce participation and national saving while maintaining fiscal discipline.

Budget Outlook and Strategy

Ai Group anticipates that the 2006-07 Budget will reveal strong budget positions for 2005-06 and for 2006-07. We anticipate the starting point for the fiscal balances for each of the 2005-06 and 2006-07 years will be comfortably above \$10 billion. This is about \$3 billion above the levels anticipated in this year's Budget papers.

In September this year the fiscal balance for the 2004-05 year was revealed to be \$10.8 billion. This was around 55% above the \$7.0 billion fiscal balance estimated in May 2005. This strong surplus above expectations was mainly due to the surge in company tax collections - continuing an extraordinary acceleration of company tax payments over an extended period.

- Over the past decade company tax collections have risen at an average annual rate of 10% (from \$15.6 billion in 1994-95 to \$40.4 billion in the 2004-05 year).
- Over the period 2000-01 to 2004-05 alone, company tax collections yielded in excess of \$168 billion.

Ai Group expects the strong position for the 2005-06 year and the strong starting position for the 2006-07 and following year to be underpinned by continued strength in revenue collections.

- In the absence of further significant income tax relief, we expect total tax collections will exceed \$650 billion over the period from 2005-06 to 2007-08; for personal income tax collections to be in excess of \$350 billion and for company tax collections to yield over \$150 billion over the same period.
- There is a very strong possibility that company tax collections will exceed \$50 billion for the first time in the 2005-06 year – this would be an increase of almost 25% on the level of collections in the 2004-05 year.

In light of the robustness of the revenue base and assuming a continuation of moderate restraint over the growth of expenditure, there is considerable scope for further taxation relief and for selective investments in the productivity; participation and savings generating programs proposed by Ai Group.

At the same time the Government could afford to make some contributions to the Future Fund from recurrent revenue in the 2006-07 and 2007-08 years while still reporting disciplined fiscal balances.

The expectation of inflation reaching towards an annual rate of 3% over the coming year clearly needs to be borne in mind in considering the timing and degree of expansionary tax relief and spending measures.

Ai Group would generally support returning taxpayers' funds to taxpayers earlier rather than later. Nevertheless, if over the next six months inflationary pressures accumulate sufficiently to sharpen the likelihood of

an interest rate rise, the disappointments of a slight delay in the return to taxpayers of taxpayers' funds, would be outweighed by the benefits of lower interest rates.

Immigration

Ai Group remains a very strong supporter of the Government's approach to skilled immigration and applauds the procedural changes that have improved the ability of business to support skilled immigration directly. With skill shortages still on the rise, levels of immigration must remain at least as high as they are currently.

Ai Group feels that there is room for a moderate increase in settler arrivals of 20,000 a year above current levels. This is essential to build more rapid population growth and to meet the requirements of continued economic growth.

Personal Taxation and Taxes on Superannuation

Summary of Proposals

- Raise the threshold from which the 30% tax rate applies and extend the range over which the 15% rate applies.
- Increase the low income tax offset from \$235 to \$435 (to be phased out between \$21,600 and \$25,950).
- Reduce the 47% tax rate.
- Phase the removal of the 15% tax levied on superannuation contributions.

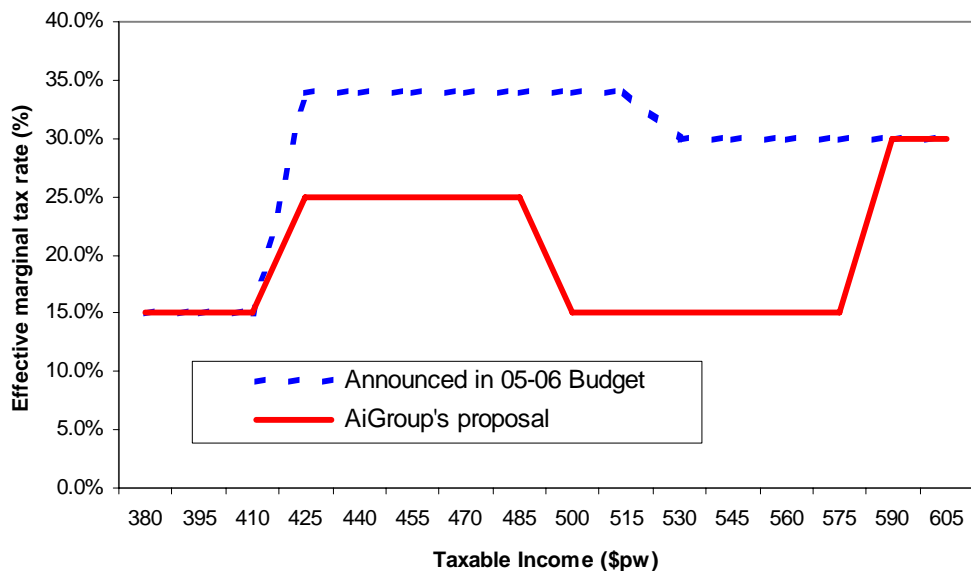
Lifting the 30% Threshold

Raising the threshold at which the 30% rate begins to apply would represent a significant boost to incentives faced by lower-income Australians.

This, together with the changes to the Low Income Tax Offset proposed by Ai Group, will slash the effective marginal tax rates faced by people with taxable incomes between \$410 per week and \$575 per week).

Chart 1 compares the effective marginal tax rates faced by low-income earners (not subject to income support means tests) from the middle of 2006 under the income tax scale already announced by the Government with the changes proposed by Ai Group. Chart 1 incorporates changes to the Low Income Tax Offset discussed below.

Chart 1. Low Income Earners' Effective Marginal Tax Rates (from 1 July 2006)



Low Income Tax Offset

The Low Income Tax Offset (LITO) provides effective relief to very low-income taxpayers without imposing the large costs associated with raising the tax-free threshold. Ai Group's proposal would lower the tax burden for taxpayers earning below \$21,600 while substantially reducing the effective marginal tax rate over the phase-out range for the LITO.¹

Table 1 shows the impacts of Ai Group's tax changes for low-income earners.

Table1. Ai Group's Proposed Income Tax Cuts for Low-Income Earners

Taxable Income (\$pw)	Income Tax Cut (\$pw)	Increase in Disposable Income (%)	Reduction in Income Tax (%)
150	0.73	0.5%	100.0%
200	3.84	2.0%	46.6%
250	3.84	1.6%	24.4%
300	3.84	1.4%	16.5%
350	3.84	1.2%	12.5%
400	3.84	1.1%	10.0%
450	7.05	1.8%	13.4%
500	11.78	2.7%	16.9%
550	20.36	4.4%	23.8%
600	24.17	4.8%	24.0%
650	24.17	4.5%	20.9%
700	24.17	4.2%	18.5%
750	24.17	4.0%	16.6%
800	24.17	3.8%	15.0%
850	24.17	3.6%	13.8%
900	24.17	3.4%	12.7%

The cost of Ai Group's proposed changes to the Low Income Tax Offset and to the threshold at which the 30% rate cuts is estimated at about \$8.5 billion.

¹ Currently the LITO phases out at 4 cents in the dollar for incomes above \$21,600 and the current effective marginal tax rate over the LITO shade-out range (currently from \$21,600 to \$27,475) is 34 cents in the dollar. With the marginal tax rate above \$21,600 falling to 15 cents in the dollar, there is scope to reduce the effective marginal tax rate from 34% to 25% while simultaneously reducing both the LITO shade-out range (by around \$1,500) and the number of people affected. As a consequence the effective marginal tax rate faced by people earning between \$25,950 and \$27,475 would drop from 34% to 15%.

Reducing the 47% rate to 42%

If the budgetary position permitted, the 2006-07 Budget could also lower the top rate of personal income tax to 42% from its present level of 47%. This is a relatively inexpensive measure (estimated to cost around \$0.5 billion).

Ai Group expects that economy-wide benefits in the form of improved incentives to invest, save and work would increase taxable activity and recover some if not all of this estimated cost.

Commitment to Phase out the Tax on Superannuation Contributions

Ai Group also proposes that the Government build on the welcome announcement in the 2005-06 Budget to remove the superannuation surcharge by committing to a phased reduction in the 15% tax levied on superannuation contributions.

This tax subtracts directly from saving; it decreases future tax revenues and increases future age pension payments.

When fully implemented, the measure would cost between \$2 billion and \$3 billion in 2006-07 prices. Ai Group does not propose that this measure take effect immediately but that a program of phased removal be announced. The measure could be funded by reversing some of the real growth in Government expenditure that has occurred in recent years.

Fostering Greater Global Engagement by Australian Business

Summary of Proposals

Ai Group will put forward a suite of measures designed to foster greater global engagement by Australian business as part of our forthcoming publication *Manufacturing Futures*. The two measures listed below are those with larger budgetary implications.

- Building effective export promotion programs by revamping the Export Market Development Grant Scheme.
- Removing tax barriers to offshore investment by Australian-based companies.

Effective Export Programs

A robust policy response is required to help turn around the current decline in Australia's export performance.

For example, in recent years we have seen a substantial drop in the annual growth of manufactured exports, which in volume terms have averaged around six percent, in contrast to growth of around 11 percent through the 1990s. The current money value of annual manufactured exports is running at around \$2 billion below its peak in 2001.

The reasons for this slump include China's global export market penetration and the appreciation of the Australian dollar. Ai Group believes that a paring back in recent years of the Government's principal export support program, the Export Market Development Grants (EMDG) Scheme, has added further pressure on companies confronting this testing environment.

Ai Group urges the Government to significantly revitalise the EMDG Scheme, including increasing its annual budget. A yearly allocation of \$300 million would be more appropriate for what is the keystone of Australia's efforts to foster and develop a diverse and sustainable export sector. This increase in funding would enable an urgently-needed widening of the eligibility requirements for participation by existing and potential exporters in the Scheme.

A key aspect in succeeding to bring new entrants into export markets is the leverage new entrants often receive from the activities of existing exporting companies. Ai Group believes that the present restrictions on eligibility have substantially resulted in a situation where it is becoming difficult to disburse the Scheme's existing budget. The uncertainty surrounding full payment of eligible claims and the long lags in receiving the rebate further undermine the efficacy of the Scheme.

The Scheme has proved to be both effective and successful over many years in building Australia's export base. For it to be revitalised, Ai Group

believes the Scheme should be funded appropriately and its accessibility to exporters improved so that it can continue to perform this crucial role.

Ai Group recommends the following changes to the EMDG Scheme:

- Increasing the turnover ceiling on eligible companies to from \$30 million to \$50 million;
- Raising the maximum grant payable under the Scheme from \$200,000 to \$300,000;
- Extending the eligibility period for funding from seven to eight years;
- Allowing companies to re-enter the Scheme when they are attempting to enter new markets, or when they are entering existing markets with new products;
- Permitting companies to commence a new claim process when there has been a substantial change in ownership or policy, and three years have elapsed since the first or second claim;
- Reducing the level of spending that is required before being eligible to claim for a grant from \$15,000 to \$10,000 over the first three years;
- Making eligible claims relating to the marketing of intellectual property in cases where an overseas subsidiary of an Australian company has IP rights assigned to it;
- Extending eligibility to cover the costs of international registration of patents and trademarks;
- Creating a new category of eligible expenditure of export skills professional development and training for staff; and
- Increasing the Market Visit Allowance from \$200 per day to \$300 per day.

Removing Tax Obstacles to Offshore Investment

In the past couple of decades a growing number of Australian companies have embarked on international expansions.

In the soon-to-be-released *Manufacturing Futures* report Ai Group will discuss extensively the strategy of offshore investment that many manufacturers are embarking upon. This strategy has the potential to contribute to a new phase of success for Australian manufacturing.

While the strategy of greater global engagement through direct investment abroad carries significant domestic benefits, a number of tax barriers face companies interested in the pursuit of this strategy. The leading barrier arises from the inequitable tax treatment of dividends paid to the Australian owners of Australian companies investing abroad.

Whereas the Australian imputation system provides relief against the double taxation of dividends paid from domestic income, equivalent relief is denied when dividends are paid from income earned abroad.

In 2003, the Review of International Tax Arrangements (RITA) conducted by the Board of Taxation at the request of the Treasurer recommended

that this inequity be addressed to “ensure that Australia's dividend imputation system does not impede the ability of Australian companies to attract capital for offshore expansion.” The Board recommended that the Government “provide a credit of 20 per cent for unfranked dividends paid out of foreign-source income (FSI) ... and allow streaming of fsi.”

In making this recommendation the Board of Taxation noted that: “The Board considers that the bias in the imputation system of restricting franking credits to Australian source income increases the cost of capital for Australian companies wishing to expand offshore - for example, to expand to achieve economies of scale to compete more globally or to grow.”²

Ai Group supports this recommendation as a key element in the modern agenda to support the development of Australian business and to remove the barriers to its global engagement.

² The Board of Taxation, 2003, *Review of International Taxation Arrangements: A Report to the Treasurer*, Volume 1 p.10.

Building Business Capabilities

Overview of Proposal

The proposal to build Australia's business capabilities is a new Ai Group initiative that will form part of our forthcoming *Manufacturing Futures* publication.

The proposal is designed to improve Australia's innovation performance and to propel Australian enterprises to the frontier of business practice.

In part Ai Group's proposal would underwrite greater business uptake of the variety of government capability building programs (at the Commonwealth and the State/Territory levels) and it would improve the value of these programs to business.

The new proposal will lay the foundations for greater productivity by enriching the capabilities of Australian businesses across the full spectrum of industry and particularly among small and medium-sized businesses. The proposal will include:

- a whole-of-government strategy using advisers to assist business with growth strategies and link them to industry and government initiatives to support their business plan; and,
- the development of nationally networked regional and industry collaboration clusters.

Ai Group's proposal would draw on the experiences developed under the Commonwealth's Small Business Assistance Program (SBAP), run through AusIndustry. This program links small businesses in regional and remote areas to Australian and State and Territory Government programs with an emphasis on developing the business skills of small business operators. The program is supported by a network of around 60 Small Business Field Officers who provide assistance in regional areas on a range of activities from business diversification to preparing for exporting, e-commerce and taxation.

Ai Group's proposal to build business capabilities would not be confined to small businesses and would also assist the many metropolitan businesses upgrade their performance through the development of a broad range of business skills. Ai Group proposes that networks should be linked closely to grass-roots industry bodies to facilitate strong engagement by individual businesses.

Skilling the Australian Workforce

Overview of Proposal

Ai Group has undertaken a detailed analysis of current and emerging skills requirements. As part of our *World Class Skills for World Class Industries* initiative, Ai Group will shortly unveil a new suite of training initiatives to complement the substantial contributions we have made in this area in recent years.

These measures will include:

- A new focus on the ongoing re-skilling of existing employees to complement attention given to entry-level skills.
- Greater business involvement in skills development strategies
- Improved recognition and authentication of skills.
- Improved incentives for individual and business investments in skills.

Ai Group envisages a budgetary cost of the measures to be put forward in *World Class Skills for World Class Industries* of less than \$300 million in a full year.

Sharpening Australia's Innovation System

Summary of Proposals

As part of our *Manufacturing Futures* initiative Ai Group will shortly release details of a variety of improvements that should be adopted to further invigorate Australia's innovation system. These improvements will include:

- Making the Research and Development Tax Concessions effective;
- Streamlining the compliance costs of innovation programs; and,
- Improving linkages between business and public sector research including by addressing barriers to public/private research collaboration.

Only the first of these will have a significant budgetary cost.

Making the Research and Development Tax Concessions effective

Australia's imputation system operates to ensure that the real value of the R&D tax concessions is much smaller than is frequently assumed. (Conversely, the cost to the revenue of these tax concessions is also much smaller than is frequently assumed.)

Ai Group proposes to make the concessions genuinely effective.

- For each \$100 of eligible expenditure on R&D, the Standard 125% concession available delivers a bottom line benefit at the company level of \$7.50 (30% of the extra \$25 deduction).
- However, while the company's tax bill is reduced and its own bottom line is lifted, its franking account is \$7.50 lower than it would have been if the tax concession were not available.
- As a result of the lower franking account balance, *domestic* shareholders stand to pay \$7.50 *more* tax on dividends received.
- If the company distributes all its profits *or if it exhausts its franking account and pays partially franked dividends*, the value of the tax concession is fully clawed back by the higher amount of tax paid by shareholders. In these cases no net benefit arises from the concession.³
- A similar shortcoming applies to the premium 175% tax concession.

This "clawback" at the shareholder level of the R&D tax concessions means that investors in companies that receive the benefit of the concession are themselves disadvantaged because of the higher amount

³ The situation is somewhat different if the company retains profits *and* does not pay partially franked dividends or if it has foreign shareholders (who do not get the full benefit of franking credits). However, even in these cases the value of the tax concession is partially eroded as a result of the clawback (either now or in the future).

of tax they have to pay on their dividends. As a consequence the interests of the company and the shareholders diverge and shareholders are less likely to be sympathetic to proposals by the company to invest in R&D (or may be less likely to invest in companies who make R&D investments).

The R&D Tax Concessions can be made effective simply by allowing companies to credit their franking accounts by the amount of company tax saved as a result of the R&D tax concession. This measure is administratively simple and would carry no additional paperwork burden for business.

While the value of the standard R&D concession would still amount to 7.5% of eligible R&D expenditure, this 7.5% would no longer be clawed back at the shareholder level. As a result investors in companies making investments in R&D would not be disadvantaged and the interests of both the company and its shareholders in supporting private sector R&D would be aligned.

Ai Group estimates that the cost to the revenue (in the form of lower collections from investors who would receive the benefit of the removal of the "clawback") would be in the order of \$400 million in a full year. This assumes some degree of wastage of the extra imputation credits.