Expenditure

The total combined expenditure from all your projects will prepopulat all correct and only for eligible R&D expenditure.





Research and Development Tax Incentive Eligible Expenditure Brief



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- 2 Types of Eligible Expenditure, (Depreciation, R&D Project Losses or Costs, Amounts Paid to Employees)
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1 ELIGIBLE EXPENDITURE

IRD's Eligible Expenditure Guidance

IRD advise "The IRD advise "To have eligible research and development (R&D) expenditure, you must have:

- Incurred expenditure on an eligible R&D activity, and
- Expenditure included on the list of eligible expenditure, and not included on the list of ineligible expenditure. Specific rules apply for R&D in a commercial production environment, contracted R&D and foreign R&D.

A tax credit is only available on expenditure of \$50,000 or more, unless you use an approved research provider. There is a cap on eligible expenditure of \$120 million in an income year, unless you obtain approval to exceed the cap."

Expenditure Incurred on an R&D Activity

To determine if you have eligible expenditure, you need to consider the extent to which the expenditure is incurred on an eligible R&D activity.



1 ELIGIBLE EXPENDITURE - APPORTIONMENT

Apportionment

A tax credit is allowed to the extent that expenditure is incurred on an eligible R&D activity. To the extent allows you to apportion expenditure between R&D and non-R&D activities. If your eligible R&D activity is done in a separate or self-contained area, so the expenditure incurred only produces benefits related to the R&D, you will not need to apportion the expenditure.

There are no specific rules for how the apportionment must be applied. It is up to you to apportion the expenditure in a way that is fair and reasonable, by reference to the advantages you have gained from the expenditure. Your apportionment method could be based on:

- a percentage of time
- floor area used for the R&D
- days/units of usage
- volume used
- unit sales
- dollar value, or
- activity-based costing principles.



1 ELIGIBLE EXPENDITURE - APPORTIONMENT

Apportionment

Your apportionment does not need to be made with absolute precision. You must however be able to point to an appropriate basis upon which your apportionment has been made, or you will not be able to claim any of the expenditure. This apportionment method must be supported by an audit trail of source documents and working papers.



1 ELIGIBLE EXPENDITURE – TYPES OF ELIGIBLE EXPENDITURE

Relationship between the R&D Activity and the Expenditure

"There must be a sufficient relationship between the expenditure incurred, and the R&D activity. This will depend on the circumstances. Expenditure that does not have a direct connection to the R&D activity will not qualify."

Meaning of Incurred

Expenditure is incurred where you are definitively committed to the expenditure and it can be reliably estimated.

Types of Eligible Expenditure

Expenditure must be included on the list of eligible expenditure to be eligible for the tax credit. The categories of eligible expenditure are:

- depreciation loss for items used in performing R&D
- expenditure or loss on acquiring goods and services used in performing R&D, and
- amounts for employees performing R&D."



Notes



2 TYPES OF ELIGIBLE EXPENDITURE – Depreciation on Assets

Depreciation on Assets used in Performing R&D is Eligible for the Tax Credit.

The calculation is based on the time the asset is used for R&D as a proportion of total use. Availability for use does not factor into the calculation. Depreciation attracts the tax credit on two types of assets:

- · facilitative assets, and
- end-result assets.

Facilitative Assets

Facilitative assets are used in the R&D process, but are not the object of the R&D. For example, test equipment used to analyse results such as a spectrograph.

End-result Assets

- the object of the R&D
- used in the R&D process (for example a prototype), and
- also used in the business's other activities.



2 TYPES OF ELIGIBLE EXPENDITURE

Expenditure or Loss to Acquire Goods and Services used In Performing R&D

Expenditure or Loss to Acquire Goods and Services used In Performing R&D

Expenditure on non-depreciable goods and services used in performing R&D is eligible, such as:

- the cost of goods consumed in R&D activities (refer to the feedstock rule, as this reduces the amount you may claim)
- overheads, to the extent they relate to R&D activities, and
- the cost of materials incorporated into prototypes used solely for R&D.

Overheads cover any expenditure directly related to the R&D activity, such as:

- rates
- utilities
- insurance
- lease payments
- security costs
- cleaning
- repairs and maintenance, and
- corporate services, such as human resources.



2 TYPES OF ELIGIBLE EXPENDITURE

Expenditure or Loss to Acquire Goods and Services used In Performing R&D

Expenditure or Loss to Acquire Goods and Services used In Performing R&D

Expenses must have a direct relationship with the R&D activity to be eligible. An apportionment is required where the goods or services are also used in non-R&D activities.

Unexpired Amounts

Expenditure you have incurred on a good that has not been used at the end of the income year (and has not been destroyed) or on a service that has not been performed, is not eligible for the R&D tax credit. The amount is eligible once the relevant good or service has been used or performed.



2 TYPES OF ELIGIBLE EXPENDITURE - Amounts Paid to Employees

Amounts Paid to Employees

Amounts for employees are eligible, to the extent they relate to performing R&D. This includes:

- salary and wages
- bonuses
- employee share schemes
- · employee recruitment and relocation costs
- overtime
- holiday pay
- long-service pay, and
- superannuation contributions.

If an employee works on eligible R&D for part of their time, only the portion of the employee's pay that relates to their time spent on R&D is eligible. You must demonstrate that you have used an appropriate apportionment method to identify the employee's time spent on R&D.



2 TYPES OF ELIGIBLE EXPENDITURE - Amounts Paid to Employees

Amounts Paid to Employees

Appropriate methods might be based on the dates when eligible activities were done, or on records such as timesheets, project reporting, or other time recording data. If you can provide supporting evidence that work patterns were consistent over a period, apportionment might be based on information derived from a sample period.

Unpaid Time Not Claimable

If you or anyone else has contributed unpaid time to your R&D, you cannot attribute a value to those hours and include it in your claim. Remuneration must have actually been paid to be eligible expenditure.



2 TYPES OF ELIGIBLE EXPENDITURE - Amounts Paid to Employees

What Expenditure in Relation to your Employee's Contribution to the R&D Means

Expenditure in relation to your employee's contribution to the R&D means the remuneration you pay to that employee to perform R&D, such as:

- salary and wages
- bonuses
- employee share schemes
- employee recruitment and relocation costs
- overtime
- holiday pay
- long-service pay, and
- superannuation contributions.

It does not cover the cost of contractors you engage to perform the R&D. It is expected that the time employees spend on eligible R&D is recorded on a contemporaneous (timely) basis.

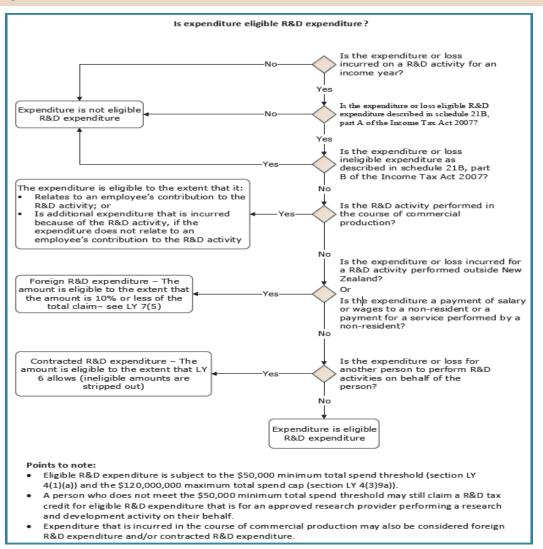
Time recording which distinguishes between eligible R&D and other duties is one example of how this might be done but time sheets are not essential.



Notes



3 IRD's Eligible Expenditure Flow Chart





Notes



4 INELIGIBLE EXPENDITURE

Ineligible Expenditure

Refer to the section of the IRD's Guide entitled "Ineligible Expenditure". The types of expenditure and depreciation loss not eligible for the R&D tax credit are listed below.

- The GST input portion of expenditure.
- Expenditure which is eligible expenditure of someone else.
- Amounts incurred by a person and their associates on R&D to the extent the amounts exceed \$120 million or the person's approved research and development cap.
- Expenditure incurred in acquiring depreciable property.
- Expenditure that contributes to the cost of depreciable tangible property.
- Depreciation on property, to the extent the cost of the property is eligible R&D expenditure.
- Depreciation on pooled property where an item in the pool is not used solely in performing R&D.
- Depreciation from an asset being written off or sold below its adjusted tax value.
- Certain amounts of depreciation on property acquired from associates.
- Profits on R&D services and property provided by associates.



4 INELIGIBLE EXPENDITURE

Ineligible Expenditure

- Amounts in excess of market value for leasing property from associates.
- Expenditure to purchase land.
- Interest and other financing costs.
- Professional fees in determining a person's entitlement to an R&D tax credit.
- Expenditure on acquiring an interest in intangible property other than software.
- Expenditure on bespoke software.
- Internal software development expenditure incurred by a person and their associates, to the extent it exceeds \$25 million.
- Expenditure on goods or services to the extent it exceeds the market value of the goods or services.
- Gifts.
- The cost of acquiring technology that is used as a basis for further R&D activities.
- Expenditure to commercialise the results of an R&D activity.
- Expenditure that relates to a government or local authority grant.
- Expenditure on inputs used, or subject to a process or transformation, to the extent the expenditure does not exceed the value of the output from that expenditure (feedstock rule).
- Expenditure for which a person has received an R&D tax credit for from another country.
- If a person's eligible expenditure is less than \$50,000, expenditure or loss under \$50,000 that is not for an approved research provider to perform an R&D activity on behalf of the person."



Notes



COMMERCIAL PRODUCTION ENVIRONMENT - The Commercial Production Rule

Commercial Production Environment - The Commercial Production Rule

Legislative reference Income Tax Act 2007 Section LY 5(1)(c)

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Where an R&D activity is performed in the course of commercial production, the amount you can claim is limited to:

- the expenditure in relation to your employee's contribution to the R&D, and
- the additional expenditure you incur because of the R&D.

What "in the course of commercial production means".

Commercial production means producing products or services for sale. "In the course of" refers to time and location. If you perform your R&D in conjunction with a commercial activity, that R&D will have been performed in the course of commercial production.



COMMERCIAL PRODUCTION ENVIRONMENT - The Commercial Production Rule

Commercial Production Environment - The Commercial Production Rule

Examples of a commercial production environment include:

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- R&D performed on a production line that at the same time was producing products for sale
- R&D performed as part of the process of designing, developing or building something where there is a contract in place for the result or it is for sale.

It is unlikely that an R&D activity would be considered as having been performed in the course of commercial production if the:

- items produced will not be sold or incorporated into another product that will be sold (the fact that the knowledge gained from the R&D is subsequently incorporated into items for sale does not mean that the original R&D was in the course of commercial production)
- R&D activity is performed in a separate space (or on a separate production line) dedicated to R&D
- R&D activity is not performed at the same time as the commercial production activities, or
- good or service produced by the activity is not widely offered for sale. For example, selling the product produced by your R&D to a select market for the purposes of field testing and further improvement will not be considered in the course of commercial production.



Notes







Drafting Tools for Responding to this Brief

We have drafting documents to assist your team to provide their contributions and inputs to this briefing.

These include:

- Microsoft Word Templates
- Microsoft Excel Templates
- Adobe pdf documents

To obtain your copies of our document drafting templates for this briefing contact us.



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Refrigeration Engineering

Retail Seafood Shipping Software Technology

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REFERENCES & SOURCES

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Ministry of Business, Innovation and Employment

Inland Revenue

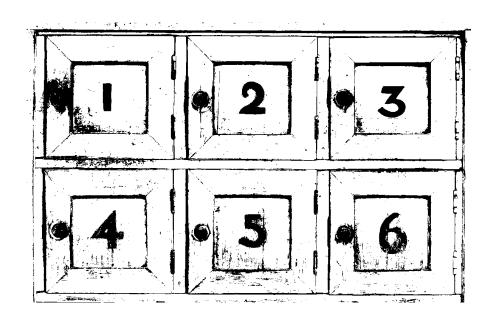
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