



By TOM PULLAR-STRECKER - The Dominion Post | Monday, 29 September 2008

Software R&D tax break guidelines 'inadequate'

Inland Revenue's guidelines for businesses claiming tax breaks on software development have been criticised by consultancy Deloitte. It says the advice is inadequate and amounts to saying that "it's not what you do, it's the way that you don't do it" .

This year, for the first time, companies will be able to claim 15 cents in every dollar they spend on research and development as a tax refund. Inland Revenue has forecast 2500 businesses may claim \$630 million under the scheme.

Deloitte tax expert Catriona Ewen says software development now accounts for about a fifth of research and development spending but Inland Revenue's advice on what types of software development might qualify "falls short of meeting taxpayers' needs".

The classification of software development is a problem the world over, where tax breaks apply, because of the intangible nature of software.

"Despite hopes and prayers that specific guidance would clarify the tax position for software developers", the latest guidelines add "few new insights", she says – beyond those setting out how research and development will be assessed in general.

"It was never expected Inland Revenue would provide dedicated software development rules. However, we would have expected more guidance on how the existing rules apply, not simply that they do apply. Other than making it clear what is not eligible, they do little to assist developers in practice."

Ms Ewen says Inland Revenue's emphasis on the method rather than the output of development activities means that finding innovative new uses of existing technology would not qualify as research and development.

Three of New Zealand's most successful software developers – Auckland health software exporter Orion Health, which turned over \$53 million last year, Christchurch's Jade Software (\$42 million) and Endace (\$24 million) – are expecting markedly different results from the tax scheme.

Ian McCrae, chief executive of Orion Health, expects the tax breaks will be worth "millions of dollars" to the company this year. Endace forecasts a US\$1 million rebate, and Jade chief executive Rod Carr expects a more modest \$350,000 boost.

There is a \$3 million cap on claims from any company in a single tax year.

Inland Revenue programme director Ron Grindle says the guidelines are only a draft, and the department is welcoming feedback.

"We have always recognised the need for additional guidelines for the information technology sector, to help them identify eligible research and development expenditure.

"Fast-changing technology and the broad range of activities encompassed in software development can make it difficult to be completely definitive about eligibility until the specific claim is presented."

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