

# BusinessPlus+ Newsletter



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## Issue 210 - May 2022

### Early Stage Innovation Company – Part 4 (Continuing from Issue 209)

#### The Principles Test

The company may have decided to move straight into the “Principles Test” after completing the “test time calculation” or it may not have accumulated 100 points under the “Gateway Test” and it can now move into the “Principles Test”.

The “Principles Test” is normally used by very young companies that have not yet had the opportunity of conducting some of the detailed activities that are listed under the “Gateway Test” but nevertheless a significant amount of work has been undertaken for which various documentation can be produced.

The “Principles Test” requires the documentation to be submitted to the Australian Taxation Office to obtain their approval that the company meets the requirements to be classified as an Early Stage Innovation Company. This application process normally takes around six weeks.



The questions asked in the “Principles Test” which require individual answers – normally considered to be at least an A4 page are:

- ✚ Is the company genuinely focused on developing for commercialisation one or more new, or significantly improved products, processes, services, marketing, organisation or methods?
- ✚ Does the business relating to these products, processes, services or methods have a high growth potential?
- ✚ Can the company demonstrate that it has the potential to be able to successfully scale that business?
- ✚ Can the company demonstrate that it has the potential to be able to address a broader than local market, including global markets through that business?
- ✚ Can the company demonstrate that it has the potential to be able to have competitive advantages for that business?

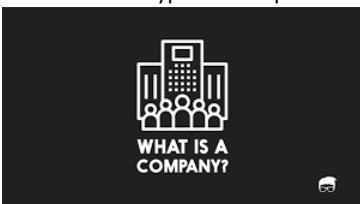
Full details of the status of the company under the “test time calculation” together with the answers to these five questions need to be included in the submission made to the Australian Taxation Office.

It is dangerous to be negotiating with investors prior to receiving an Early Stage Innovation Company status certificate from the Australian Taxation Office because if an investor has already invested they may find that the company was not approved and therefore they will not be entitled to the taxation benefit.

### Entities to Operate a Small Business – Part 2

#### Companies

There are two types of companies that could be utilised for the operation of a SME business



- ✚ Private Company – which is the most popular company entity type used by SMEs.
- ✚ Unlisted Public Company – which has some advantages especially if the directors intend the company to grow and to seek to raise capital from venture capitalists and possibly list on a Stock Exchange.

Companies must have directors who are in charge of the day-to-day operations of the business and companies have shareholders.

Companies are governed by the rules and regulations contained within the *Corporations Act*.

Private companies and Unlisted Public Companies can apply to a Crowd Sourced Funding Intermediary for approval to list the company on the Intermediary's website to raise capital as a Crowd Sourced Funding Equity Raising Company.

Private companies that comply with the regulations for an Early Stage Innovation Company can complete the due diligence requirements and if they satisfy the requirements under the “Gateway Test” they can self-assess their eligibility to be classified as an Early Stage Innovation Company. However, these companies should ensure that they have full documentary evidence for each step within the “Gateway Test” because this documentation will ultimately be required by the Australian Taxation Office.

If the private company complies with the initial regulations and then completes the “Principles Test” the due diligence review is required to be lodged with the Australian Taxation Office who will issue a determination (normally takes six weeks) as to whether the company qualifies as an Early Stage Innovation Company.

If the company has self-assessed under the “Gateway Test” or has been issued an approval letter by the Australian Taxation Office that the company qualified under the “Principles Test” the company is then able to finalise negotiations with potential investors to invest in the company and gain the special benefits that are available to Sophisticated Investors or Retail Investors in qualifying Early Stage Innovation Companies.

## Research and Development

If you are undertaking or contemplating undertaking research activities it’s a good idea to have a discussion with us as soon as possible so that we can discuss with you the rules and regulations relative to businesses being able to claim the Research and Development Incentive Offset.

As we explained in the first edition of this series only companies can claim Research and Development Incentive Offset.

For companies with turnovers less than \$20,000,000 the Research and Development Refundable Tax Offset is 43.5% of the eligible research and development expenditure.

This refundable component is highly prized by entrepreneurs and researchers because companies undertaking research and development can potentially receive a cash refund of the research and development expenditure from the Australian Taxation Office if they are trading at a loss.



The government is so serious about research and development that it has instructed the Australian Taxation Office to ensure that these refunds are paid within thirty (30) days of the company lodging its income tax return.

The refundable component is only available companies with annual turnovers of less than \$20,000,000.

For companies with turnovers over \$20,000,000 the non-refundable Research and Development Tax Offset is the company’s corporate tax rate plus an incremental premium.

This incremental premium is based on the company’s “research and development intensity”. The “intensity” is a percentage of the company is eligible research and development expenditure as a proportion of the company’s total expenditure for the year.

For these companies all eligible research and development expenditure, up to a 2% research and development intensity, will receive a non-refundable Research and Development Tax Offset equal to the company’s corporate tax rate +8.5% premium.

Eligible research and development expenditure above 2% research and development intensity will receive a non-refundable Research and Development Tax Offset of the company’s corporate tax rate +16.5% premium.

In the March edition we indicated that “not all of the expenditure that is incurred as part of a “total research activity” may qualify as “eligible research and development expenditure”. We indicated that we would discuss these issues further in this edition.

To claim the Research and Development Incentive Onset it is necessary to conduct the research activities as a “systematic progression of work”.

To be considered a systematic progression of work to prove or disprove a hypothesis the experiments are required to relate to additional activities other than:

- ✚ Just collecting data
- ✚ Tests that use “trial and error” alone
- ✚ Testing and modification of existing product lines
- ✚ Commercial, legal and administrative aspects of patenting, licensing or other similar activities
- ✚ Research funded by a third party
- ✚ Market -related research, testing or development
- ✚ Management studies or efficiency surveys
- ✚ Development that doesn’t relate to functionality
- ✚ Utilises an activity that is not designed to prove or disprove a hypothesis which is one of the crucial requirements of an eligible research and development project.

Where data only is collected, this could be part of supporting research and development activities.

If you have been undertaking research and development activities during 2021/22 please contact us as soon as possible so that we

can review the records that you have maintained and if need be make suggestions on changes that you could make to the record-keeping process.

If you are contemplating commencing research and development activities during 2022/23 it is a good idea to have a discussion with us before you commence these activities so that the record-keeping process can be implemented from an early-stage.

Please do not hesitate to contact the accountant in our organisation do you normally work with

## Level of Business Fitness Is Important

The 2022/23 financial year commences in about eight weeks' time. How fit is your team to meet the challenges of a new financial year?

Now is a good time to do a "fitness test review" to determine whether some extra work needs to be done to ensure that all members of the team are "match fit" whether it's in product knowledge, social media communication skills for business purposes, digital marketing, leadership skills, understanding financial reports, customer relationships or any other of the myriad of issues that confront business operators – just like your favourite football team goes through eight weeks before the start of the new season.

If they are not match fit the footballers, netballers, basketballers suffer injuries and then have to sit on the sidelines whilst they recover from those injuries. Businesses are very similar. Key employees can be affected by injuries, lack of knowledge, fatigue, illness and other issues which affect their individual performance.



When we look at businesses on an overall basis there can be issues relative to the business organisation that could be improved to make life a lot easier for everyone involved in the business whether they are team members, leadership persons, customers, suppliers etc.

Where do you start on determining the "current business fitness level" of your business?

The key to running an effective business is the:

- ✚ Leadership team
- ✚ People
- ✚ Strategies to make the business run efficiently
- ✚ Determination of appropriate policies to implement those strategies
- ✚ Ongoing awareness of the cash available to fund the business operations – this means having regular access to Budgets and Cash Flow Forecast so you know if you are going to encounter any cash shortages so that you can do something about it.

The keys for a great business include:

- ✚ The leadership team is healthy and aligned  
Alignment is very important what are the key issues that have to be attended to today, tomorrow, in a weeks' time, or within the next three months? Does everyone know and understand the importance of those activities in meeting the businesses overall goals?
  - ✚ Alignment on the "number 1 strategy/ thing" to be accomplished in the next three months is vital for the leadership team
  - ✚ Implementation of communication patterns – a "pattern of meetings"
    - Daily
    - Weekly
    - Monthly
- To be conducted for the various groups within the business:
- Leadership team
  - Team groups
  - Board of Advice (if you have one)  
(If you do not have a Board of Advice it is something worth thinking about)
  - Board of Directors (if you have one)
  - Customers Advisory Committee
  - Suppliers
  - Bankers/Financiers
  - Professional Advisers
- ✚ Allocation of accountability spread around the leadership team and other people so as to ensure that not everything is allocated to the one person which normally appears to be the CEO or equivalent
  - ✚ Team member input – what are customers saying? Ask the team members what would they do differently if they were the boss?
  - ✚ Analysing customer feedback

If you would like our assistance in preparing a business fitness report for your business, please contact the accountant in our firm that you normally communicate with.

## It's Business Planning Time Again!

It's May a great time for the preparation of a Business Plan – why because it encourages you to sit down and think about what's happening within your business – to ask questions – to seek input from team members, customers, suppliers, professional advisers.

What do these people think about how your business has been run – what changes would they make if they were in charge or held certain positions within the organisation?

There is still a lot of challenges confronting businesses relating to COVID-19 and the general health of the community as well as the normal challenges that confront businesses.

Now for the first time in many years we have that word called “inflation” that has not been part of the vocabulary for some time, but it has re-emerged again!



Interest rates are also on the rise. The Reserve Bank had not lifted interest rates for ten years and now they have done so and financial experts are forecasting they will continue to raise interest rates each month to the end of the year.

What is all this going to do to your business? The older members of the business community can remember interest rates being over 20% for general business activities and in some cases around 24% on commercial bills.

Some businesses will fail in these conditions – how you set your business plans will have a significant impact on your survival of these challenges.

If you would like to discuss with us the assistance that we could give you in the development of your Business Plan for the new financial year where we could act as the “facilitator” and/or play a “devil’s advocate” role in encouraging debate on various aspects of how your organisation operates, please do not hesitate to contact the accountant in our organisation that you normally deal with so that discussions could commence to explain the process that we would suggest.

## What Do You Know About Grants?

Grants are very important for small businesses because a grant recipient can access “free money”

Grants are offered by the Australian, State and Territory governments and by some local government organisations.

Most grants require a financial contribution to be made by the recipient – normally 50%.

Business grants can be accessed by all types of business entities but the most popular entity for government grants is a company.

Grants normally comply to a set procedure to determine eligibility which includes:

- ✚ Entity type
- ✚ Years in business
- ✚ Number of employees
- ✚ GST registration?
- ✚ ABN?
- ✚ Annual turnover
- ✚ Industry
- ✚ Business Industry Code

We have access to a product which enables us to enter this type of information and the system produces a report on grants that might be available for a particular client. If you would like to have a discussion with us about what government grants might be available for your business please contact the accountant in our organisation that you normally deal with.



### An Important Message

*While every effort has been made to provide valuable, useful information in this publication, this firm and any related suppliers or associated companies accept no responsibility or any form of liability from reliance upon or use of its contents. Any suggestions should be considered carefully within your own particular circumstances, as they are intended as general information only.*

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