New Zealand

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What's new?

Summary of updates/Changes to R&D and government incentives from 1 January 2019 through 31 October 2020

- The most significant update is the introduction of broader refundability of the 15% tax credit on eligible R&D expenditure as from the 2019–2020 income tax year.
- A tax bill before Parliament is proposing other changes to the R&D tax incentive regime, including allowing expenditure on employee costs contributing to the cost of tangible property to be eligible for the regime.
- Other changes proposed in the tax bill include bringing forward the due date for applying for criteria and methodologies approval, amendments to the schedule of excluded expenditure, and amendments to the definition of eligible R&D expenditure to meet the policy intent.

Featured government incentives

Incentive name	Description	Maximum percentage	Qualification standards	Key exclusions or issues
R&D tax credit	Tax credit, with limited refundability	15%	Employees performing R&D, depreciation of items used in R&D, expenditure or loss on acquiring goods and services used in performing R&D	Majority of the work must be performed in New Zealand Unable to claim costs capitalized as tangible fixed assets unless used entirely in R&D (it is proposed that capitalized employee costs will become eligible costs), and restrictions on trial costs Minimum expenditure of NZD 50,000 and maximum of NZD 120 million Refundability is available in many circumstances and subject to a payroll cap
R&D tax loss cash out	Ability for unlisted companies to "cash out" their tax losses arising from qualifying R&D expenditure	28% of the lesser of the following amounts for the company for the tax year: • Net losses; • Total R&D expenditure; or • 1.5 times total R&D labor expenditure	R&D expenditure based on definition under accounting standards	Only for New Zealand companies that are spending 20% of their salary and wages on R&D Must return the value of the cash-out loss when profitable, or in the event of future specified shareholding or IP ownership changes
Project Grants	Cash grant for a business's qualifying R&D project costs	Up to 40%	Includes labor costs, materials and consumables, depreciation, and new lease costs	Must have been carrying out R&D activities for less than three years, or have spent less than NZD 800,000 on average on R&D for the last three years

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Industries most often affected by government incentives in country

	Technology, Media & Telecom		**Financial Services**
●	Telecom, Media & Entertainment	●	Banking & Capital Markets
●	Technology	●	Insurance
	Consumer		Investment Management
●	Consumer Products		Real Estate
	Retail, Wholesale & Distribution		**Life Sciences & Health Care**
●	Automotive	●	Health Care
	Transportation, Hospitality & Services	●	Life Sciences
	Energy, Resources & Industrial		**Government & Public Services**
●	Power & Utilities		Health & Social Care
●	Mining & Metals		Defense, Security & Justice
●	Oil, Gas, & Chemicals		Civil Government
●	Industrial Products & Construction		International Donor Organizations
		●	Transport

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Type	National incentive?	State, provincial, regional or local incentives?[1]	Filing deadlines imposed?	Is the claim made in advance or arrears?[2]	Nature of incentive	Maximum benefit available to large enterprises	Maximum benefit available to small and medium-sized enterprises
Innovation							
Research & development (R&D)	🟢	🔴	🟢 ⚪	National: Varies Local: Not applicable	New Zealand has an R&D tax credit incentive regime Eligible entities include most private sector businesses that perform a core R&D activity in New Zealand themselves (or through an R&D contractor in New Zealand), have a fixed establishment in New Zealand, and own the results of the R&D activity (or other ownership conditions are met) Eligible expenses are those incurred on an R&D activity and included on the list of eligible expenditure (and not on the list of ineligible expenditure)	The tax credit is 15% of qualifying R&D expenditure, with the minimum spend being NZD 50,000 and the maximum NZD 120 million (but large enterprises can apply to Inland Revenue to exceed the cap). In many cases, the benefit can be paid out in cash if the claimant is loss-making	The tax credit is 15% of qualifying R&D expenditure, with the minimum spend being NZD 50,000 and the maximum NZD 120 million. In many cases, the benefit can be paid out in cash if the claimant is loss-making
R&D grant: national or EU	🟢	🔴	🟢	Varies	New Zealand has an R&D Project Grant available, providing a cash grant for up to 40% of a business' qualifying R&D project costs A business is eligible if it has been carrying out R&D activities for less than three years, or has spent less than NZD 800,000 on average on R&D for the last three years Relevant expenses include labour costs, materials and consumables, depreciation, and new lease costs	Up to 40% of a business' qualifying R&D project costs	Up to 40% of a business' qualifying R&D project costs
R&D Tax Loss Cash-Out	🟢	🔴	🟢 ⚪	National: Arrears Local: Not applicable	Ability for unlisted companies to "cash out" their tax losses arising from qualifying R&D expenditure Only for New Zealand companies that are spending 20% of their salary and wages on R&D Incentive is realized by a "cash out" of tax losses from qualifying R&D. This has to be repaid when the company becomes taxpaying or other criteria are met, e.g., sale of company or IP	28% of the lesser of the following amounts for the company for the tax year: (i) net losses; (ii) total R&D expenditure; or (iii) 1.5 times total R&D labor expenditure	28% of the lesser of the following amounts for the company for the tax year: (i) net losses; (ii) total R&D expenditure; or (iii) 1.5 times total R&D labor expenditure

Key: 🟢 = PERMANENT INCENTIVE = TEMPORARY INCENTIVE = NEGOTIABLE 🔴 = NO 🟡 = LIMITED APPLICABILITY ⚪ = NOT APPLICABLE

Notes:

1. Green means that this incentive is currently in effect. Yellow means that the incentive has limited applicability, i.e., the requirements for this incentive limit its value to most companies. Red means that there is no incentive.
2. If the response is advance, this means that the government must approve the award of the incentive prior to the commencement/completion of the project/activity. If the response is arrears, this means that the award of the incentive is determined at the end of the tax period or after the completion of the qualifying project or activity. Most tax incentives are considered to be claimed in arrears because they are reported on tax returns.

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Country background

The standard corporate income tax rate in New Zealand is 28%. The most significant change to R&D tax incentives has been the introduction of a broader refund mechanism as from the 2020–21 tax year, as explained further below.

Innovation Incentives

Research & Development (R&D)

Nature of incentives

A 15% R&D tax credit is available as from the 2020–21 income tax year. There is a minimum R&D expenditure threshold of NZD 50,000 per year (NZD 7,500 tax credit), and the maximum claim is NZD 120 million of qualifying R&D expenditure (NZD 18 million tax credit). Businesses that exceed the cap may request approval from Inland Revenue to make additional claims.

The R&D tax credit generally is available as an offset against income tax liabilities. If a claimant is in a tax loss position, it can claim a refund, subject to various caps. The tax credit must first be applied to other tax liabilities before being refunded. To meet the refund criteria, a business must be in a tax loss position or a tax-paying position with surplus tax credits, and not have outstanding tax liabilities.

A new "payroll taxes" cap has been introduced for tax year 2019-20 and later, allowing a refund up to the amount of labor taxes paid by the claimant (e.g., pay as you earn (PAYE), employer superannuation contribution tax (ESCT), fringe benefit tax (FBT)) and labor taxes paid by companies that the claimant controls or that sit within the same wholly-owned group.

There is an alternative limited refund option available for the 2020–21 tax year only, with the claimant having a choice of which option to apply. For entities that meet the criteria, up to a maximum of NZD 255,000 can be refunded (NZD 1.7 million of qualifying R&D expenditure). The entity also must meet corporate eligibility and wage intensity criteria, i.e., the company must be a New Zealand tax resident and 20% or more of its labor costs must be related to R&D.

If a claimant is in a refund position and does not meet the refund criteria, it can carry the credit forward to future years, subject to shareholder continuity requirements.

Pre-approval mechanisms for claims have been introduced as from the 2020–21 tax year, including criteria and methodologies approval.

Proposed changes

The government has proposed changes to the R&D tax incentive regime, including allowing expenditure on employee costs contributing to the cost of tangible property to be eligible for the regime as from the 2019-20 income year. Other minor changes are proposed, including:

- Clarifying the definition of eligible R&D expenditure to ensure that, to be eligible, the expenditure is closely connected with conducting an R&D activity (in line with the policy intent);
- Clarifying the exclusion of mining development activities;
- Other amendments to the tangible depreciable property exclusion to clarify the scope of the exception for expenditure that contributes to the cost of property intended for use as a prototype;
- Amendments to the schedule of excluded expenditure; and
- Bringing forward the due date for submitting an application for criteria and methodologies approval.

Eligible industries and qualifying costs

The R&D tax credit is not sector or industry specific, i.e., the regime is designed to target all businesses carrying out R&D activities, provided the relevant requirements are met.

Eligible entities are those that carry on business through a fixed establishment in New Zealand and perform a core R&D activity in New Zealand or through a contractor there. To benefit from the R&D tax credit, the activities must meet the definition of core R&D activities or they may be supporting R&D activities. The definition of core R&D is:

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- An activity that is conducted using a systematic approach;
- Has a material purpose of creating new knowledge, or new or improved processes, services, or goods; and
- Has a material purpose of resolving scientific or technological uncertainty.

The definition does not include activities if the knowledge to resolve uncertainty is publicly available or deducible by a competent professional in the relevant scientific or technological field. It does not include an activity to the extent that it is performed outside of New Zealand (subject to the 10% concession below) or activities that are included on a list of excluded activities.

An activity that does not meet the definition of a core R&D activity but is required for core R&D still may qualify for the tax credit as a supporting R&D activity. A supporting R&D activity is one whose sole or main purpose is to support the core R&D activity and is required for and integral to the core R&D activity.

There is a list of qualifying expenditure, which includes:

- Employees and contractors (subject to the contractors carrying out R&D on behalf of the claimant) performing R&D;
- Depreciation for items used in performing R&D;
- Allocated overheads; and
- Expenditure incurred in the acquisition of goods and services used in performing R&D.

Inland Revenue has prescribed recordkeeping requirements that go beyond what is ordinarily required for tax purposes and has stressed the importance of contemporaneous recordkeeping. The records must show that the business is eligible to claim the R&D credit, that the R&D activity qualifies, and that the R&D expenditure is eligible.

There are several specific expenditure restrictions, including the following:

- Feedstock rule: Where items are used, processed, or transformed as part of R&D activities, only the net expenditure is eligible for purposes of the R&D tax credit. The net cost of inputs essentially is the excess of input costs over the value of the outputs, where inputs are costs that have gone through the process or transformation and outputs are the sales proceeds or market value of the output.
- Commercial production: Where an R&D activity is performed in the course of commercial production, the amount that can be claimed is limited to expenditure incurred on an employee's contribution to the R&D, and any additional expenditure incurred because of the R&D.
- Capitalized expenditure: While qualifying expenditure capitalized as an intangible fixed asset is eligible, expenditure capitalized as tangible property is not eligible unless it is solely used in performing an R&D activity or, subject to the proposed change being enacted, if it relates to labor costs.
- Internal software: Software development for the purpose of internal administration of a business is excluded from eligible expenditure for purposes of the R&D tax credit. The exclusion captures routine administration functions such as payroll, accounting, enterprise resource planning, and inventory systems, but does not include software development that enhances non-digital services to customers. A NZD 25 million expenditure cap applies to software developed for the purpose of enhancing non-digital services to customers. There is no cap (other than the general NZD 120 million limit) for expenditure on software developed for sale.

IP and jurisdictional restrictions
The claimant or a company in the corporate group must own the results of the R&D activities. If the owner is a company in the group, it must be resident in New Zealand or a country that has concluded a

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tax treaty with New Zealand. Alternatively, the ownership criteria can be met if the claimant is able to use the results of the R&D activities at no extra cost above the R&D expenditure for the activities.

The majority of the R&D must be undertaken in New Zealand. There is scope to include R&D performed overseas provided it does not exceed 10% of total qualifying expenditure.

Other R&D incentives

Aside from the R&D tax credit, there are other incentives administered by Inland Revenue and Callaghan Innovation. These are subject to specific eligibility requirements and are listed below.

R&D loss cash-out

In addition to the R&D tax credit, Inland Revenue allows unlisted loss-making companies meeting certain criteria and engaged in R&D to “cash out” their losses and receive a refundable tax credit. Where a company is engaged in intensive R&D, it will be able to cash out 28% of the lesser of the following amounts for the tax year:

- Its net loss;
- Its total R&D expenditure; or
- 1.5 times its R&D labor cost.

The maximum credit is NZD 476,000 for the 2019–2020 income tax year and NZD 560,000 as from 2021.

To qualify for the cash-out, a company must meet the corporate eligibility and wage intensity (20% or more of labor costs must relate to R&D) criteria. Only the net loss for the relevant year may be cashed out, meaning that carried forward tax losses cannot be cashed out. The definition of R&D for purposes of the cash-out is based on accounting standards.

The cash-out is repayable by the claimant when it becomes profitable, or in the event of specified shareholding or IP ownership changes.

The R&D loss cash out and refundable R&D tax credit can be claimed at the same time and on the same expenditure. However, the two regimes have differing criteria for what they define as qualifying R&D expenditure.

Growth Grants

Growth Grants formerly were a key R&D funding opportunity from Callaghan Innovation. While they remain in place for existing recipients until 2021, they are not available to new applicants. Claimants (and those associated with them) cannot receive a Growth Grant and the R&D tax credit in the same year, subject to transitional rules for the phasing out of growth grants.

Project Grants

Project Grants provide funding from Callaghan Innovation for up to 40% of eligible R&D project costs, for businesses in the early years of undertaking R&D. Payments from Callaghan Innovation to claimants are made monthly or quarterly in arrears.

R&D Loan Scheme

As a result of COVID-19, a temporary R&D Loan Scheme has been introduced to address businesses whose R&D funding has been impacted by COVID-19 (they must be able to show a drop of 30% or more in available funding for eligible R&D activities). The loan amount is up to $400,000 (subject to other forms of government R&D support), with interest charged. The loans must be repaid within 10 years and the funds are to be spent on eligible R&D between 1 July 2020 and 30 June 2021.