

CallaghanInnovation

New Zealand's Innovation Agency

Guidelines

Evidencing R&D and RDI for Growth Grants

Version > 3.3
Date > August 2019



**Rukuhia te wāhi ngaro,
hei maunga tātai whetū.**

*Explore the unknown,
pursue excellence.*

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1. Introduction

The objective of the Growth Grant is to increase New Zealand businesses' investment in research and development (R&D) to support long term economic growth.

The Growth Grant is a rules-based, market led incentive for increasing R&D investment in businesses that are experienced in investing in R&D.

To have eligible research and development (R&D) expenditure you must have:

- Incurred expenditure on an eligible R&D activity; and
- Expenditure must not be in the list of general or specific inclusions.

These guidelines are based on the Ministerial Direction but include additional clarification. They are not intended to be exhaustive, and you are encouraged to **discuss any matters with Callaghan Innovation directly**.

2. Transitional Eligibility Requirements - Evidencing Criteria Met

For those contract holders who applied under the Transitional scheme the following information is required to be submitted (as per the contract conditions in the funding agreement):

- A review report that is certified by an independent chartered accountant to the directors of the entity for the period relating to the transitional period (Appendix One)
- A confirmation of eligible R&D for the period relating to the transitional period that is signed by your director(s). (Appendix Two)

These must confirm eligibility (\$300,000 R&D expenditure and R&D expenditure at least 1.5% of revenue) within the transitional period (first 12 months of the contract period)).

They can be met at any time during the 12 months, for example if you have met the threshold(s) in the first 3 months of the contract period, you can submit the documentation to be reviewed.

Please ensure that you review any other conditions requirements that may be due alongside the eligibility criteria.

3. Annual Year End Claim

Along with quarterly claims and reporting, a Growth Grant recipient is required to complete an annual end-of-year claim which verifies the claims made and releases the retentions deducted for the period. You must supply the following documentation to show that you continue to meet all criteria for the year-end claim:

- Financial statements for the period relating to the year-end claim (see below note for financial year-ends that do not match Growth Grant period*)
- A review report that is certified by an independent chartered accountant to the directors of the entity for the period relating to the year-end claim. (Appendix One)
- A confirmation of eligible R&D for the period relating to the year-end claim that is signed by your director(s). (Appendix Two)
- Completion of the online claim in full (with all required documents uploaded to the claim) and sufficient detail to enable Callaghan Innovation to assess the progress of the businesses R&D programme.

*Where the Growth Grant contract period anniversary does not coincide with a grant recipient's financial year-end, a grant recipient can elect to provide the required information for a part year (i.e. 3-9 months) or up to an 18-month period to enable alignment of the financial year-ends and the Growth Grant year-end reporting.

4. Eligible R&D

The following extract from the [Ministerial Direction \(October 2018\)](#) defines eligible R&D as follows:

“DEFINITION OF ELIGIBLE RESEARCH AND DEVELOPMENT EXPENDITURES FOR R&D GROWTH GRANTS

Eligible R&D expenditure is defined as those meeting the New Zealand Equivalent to International Accounting Standard 38 (NZ IAS 38) definition of research and development and expensed under that standard.”

Is the activity an R&D activity?

The NZ IAS 38 definitions of R&D are:

- > *Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.*
- > *Development is the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.*

Clarifying Principle

If necessary, when seeking to distinguish R&D from non-R&D, the further advice provided by the New Zealand Financial Reporting Standard 13 (NZ FRS 13) should be applied;

R&D is distinguished from non-R&D by the presence or absence of an appreciable element of innovation. If the activity departs from routine and breaks new ground it is normally R&D; if it follows an established pattern it is normally not R&D."

To further clarify, the activity is likely to be R&D if the knowledge required to resolve the problem is not publicly available and cannot be worked out by a competent professional in the relevant field, without undertaking a systematic process to generate new knowledge or test a possible solution.

Is the expenditure eligible?

To claim under the Growth Grant, the expenditure needs to be connected to eligible R&D activities and not be on the list of general or specific exclusions.

4.1 General Exclusions

The following types of expenditure are not eligible for Growth Grants:

- > Any expenditure that is, or would be, capitalised as an intangible asset under NZ IAS38

These are resources controlled by the entity and from which future economic benefits are expected. Examples include patented technology, computer software, databases and trade secrets; trademarks and licensing or royalty agreements. Expenditure on acquiring an interest in intangible property, such as purchasing, leasing or obtaining a right to use, including royalty payments is not eligible.

- > R&D undertaken outside of New Zealand

R&D activities performed outside New Zealand are not eligible

- > R&D funded through an enforceable levy paid by another entity

- *Enforceable levies for R&D paid to another entity*
- *Any R&D funded by a grant or other payment provided by an entity that is not part of the same consolidated group of entities as the applicant. However, R&D funded by the R&D Growth Grant, an R&D Project Grant that the business receives for a Collaborative R&D Project or an R&D Student Grant is eligible. Expensed funding for R&D contracted out by the applicant to another entity is also eligible.*

The GST input portion of expenditure is not eligible.

4.2 Specific Exclusions

To provide further clarification on the definition, some specific activities are excluded. This list is not exhaustive. Activities not specifically excluded are only eligible provided they meet all other features of the definition. Specific activities excluded are:

- > Engineering follow-through in an early phase of commercial production.
- > Activities related to the construction, relocation, rearrangement or start-up of facilities or equipment other than facilities or equipment solely used for the businesses R&D (which may be included).

Pre-production activities that occur before production but after scientific or technological uncertainty has been resolved are excluded. Excluded activities include: demonstrations of commercial viability; tooling-up for commercial production; planning the production process; developing control systems; undertaking start-up procedures; and commissioning new equipment.

- > Routine, on-going efforts to refine, enrich, or otherwise improve on the qualities of an existing product or process, or to make cosmetic or stylistic changes to it.

Where a competent professional knows that it is possible to successfully develop a product or adapt a process or recipe, and testing is only required to confirm or optimise the results, the activities are not eligible.

- > Routine design of tools, jigs, moulds and dies, or seasonal or other periodic design changes to existing products. However, expensed design activities involved in developing a new product or process are eligible.
- > Activities involved in ensuring that existing products or processes comply with statutory requirements or standards, and quality control, routine testing or troubleshooting during commercial production. However, testing in search of significant product or process improvements is eligible.

Tests to commission equipment, calibrate, fine-tune, or optimise processes or production systems are not eligible.

- > Adapting an existing product or process to a particular customer's need or site.

Activities to adapt an existing product or process to a customer's need or site using standard engineering approaches for problem solving are not eligible.

- > Supporting, de-bugging or making minor improvements to existing computer software.

Activities using known methods to de-bug, support or make minor improvements to existing software using methods that a competent professional familiar with that type of software knows could achieve the minor improvement are not eligible.

- > Market research or surveys, market testing, market development or sales promotion, management studies, efficiency surveys or the routine collection of information.

This exclusion targets activities conducted to investigate consumers' preferences and/or potential interest in a product or service, or activities designed to encourage the consumption of products or services.

- > Any costs involved in protecting, licensing, selling or defending intellectual property or of acquiring or using external intangible assets (e.g. patent licences).

This exclusion is concerned with the commercial, legal and administrative activity associated with taking steps to protect your own intellectual property; and granting rights to another party to use or access your intellectual property and covers patents, trademarks, designs and plant breeders' rights. Patent searches that are undertaken to discover the existing state of knowledge may be eligible.

- > Interest expenses or lease payments of any kind, and any overheads that are not closely linked to R&D activities.

Exclusions include interest and other financing costs and any overheads that are not closely linked to R&D activities.

- > Prospecting or exploring for minerals, petroleum, natural gas or geothermal energy.
- > Research in the social sciences, arts and humanities.

4.3 Eligible Activities

Activities that would typically include R&D are described below. If this guidance does not fit your situation, contact Callaghan Innovation to discuss.

- > Research activities in New Zealand for which the primary purpose is to inform the technical development of the product
- > Research aimed at discovery of new knowledge
- > Searching for application of new research findings or other knowledge
- > Formulation and design of possible new or improved product or process alternatives
- > Testing in search of significant product or process improvements or alternatives
- > Evaluation of product or process alternatives
- > Design, construction and testing of pre-production prototypes and models
- > Development of a software system/platform, architecture and new code
- > Design of tools, jigs, moulds, and dies involving new technology as distinct from routine design of tools, jigs, moulds, and dies.

5. Expenses and Overhead Expenses Calculation

If an expense relates to performing R&D, it should be charged directly rather than included in an overhead rate.

Examples of expenditure that should be claimed directly as eligible R&D expenditure are:

- Employee costs - wage records should include timesheets that must accurately identify the number of hours an employee spends on R&D. Employee costs that are eligible to the extent they relate to performing R&D include: salary and wages, bonuses, employee share schemes (where this is paid as part of the employee's salary package), employee recruitment and relocation costs, overtime, holiday pay, long-service pay, and superannuation contributions.

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.

- Contracted R&D or external labour. The expenditure incurred by the contractor is subject to the same exclusions as expenditure you incur yourself. Where you engage a contractor associated to you, you can only claim the lesser of what you paid the contractor and the contractor's costs. All the profit margin is removed.
- The cost of goods or materials consumed in R&D activities or used solely for R&D activities. Goods purchased overseas to be consumed in R&D activity in New Zealand is eligible expenditure.
- Travel and training expenditure that is directly related to the R&D activity. Note that travel and training undertaken outside New Zealand is excluded. For example, the costs to attend an overseas conference are not eligible even if, for example, airfares were purchased from a retailer in New Zealand. Travel costs paid by loyalty scheme points are not eligible expenditure.

Expenses which should be included in an overhead calculation are activities that are associated with the R&D activity such as:

- Insurance
- Rent leases
- Repairs and maintenance
- Utilities
- Telephone expenses
- Printing and stationary
- ACC levies
- Rates
- Accounting fees
- Office cleaning
- Security costs
- Corporate services, such as human resources

An apportionment is required where the goods and services are also used in non-R&D activities. The overhead expense calculation can use either an estimation of percentage of use or percentage of employees who are R&D FTE to total FTE. If you calculate overheads differently please discuss your method with Callaghan Innovation.

EXAMPLE

Company has 100 FTE of which 15 are wholly R&D FTE and 5 are part time (50% of their time is spent on R&D and 50% of their time is spent on non-R&D. These part time R&D staff equate to 2.5 R&D FTE).

The eligible overhead expense rate would be 17.5% $(15+2.5 \text{ FTE}/100 \text{ FTE})$.

Note: If your R&D intensity fluctuates throughout the year it may be appropriate to re-calculate your overhead rate for each quarterly claim.

IMPORTANT – no matter how a grant recipient/applicant chooses to calculate the overhead rate and other expenses claimed, you must keep sufficient records to easily demonstrate to an independent party how you have made the calculation and why it is reasonable.

Ineligible overhead expenses include:

- Advertising and marketing expenses
- Bad debts
- Entertainment expenses
- Interest expenses
- Legal expenses
- Directors fees
- Freight & delivery expenses not related to performing the R&D activity
- Motor vehicle expenses
- Directors liability insurance
- Recruitment expenses not related to performing the R&D activity
- Travel expenses not related to performing the R&D activity

5.1 Depreciation and Amortisation

Depreciation on assets used in performing R&D should be charged directly not as an overhead.

The calculation is based on the time the asset is used for R&D as a proportion of total use. Expenditure incurred in acquiring or creating an asset that is used solely in R&D is eligible. If this expenditure is claimed directly, any depreciation relating to the subsequent use of that asset is not eligible.

Questions have been raised in respect of claiming amortisation on intangible assets capitalised under IAS 38.

"Development" expenditure (per NZ IAS 38 definition) on internally generated intangible assets must be capitalised if it meets the criteria in NZ IAS 38 para 57. This asset may then be subsequently amortised. If anything is capitalised in accordance with NZ IAS 38 para 57 then any amortisation of that asset is not eligible R&D expenditure (as the original cost of the asset is an excluded expense).

Intangible costs that may be capitalised as they were either:

- separately acquired (NZ IAS 38 paras 25-32), or
- acquired as part of the business combination (paras 33-37)

may subsequently be amortised (provided they are not indefinite life intangibles). These may be included as eligible R&D, provided they are used as part of the activities that qualify as eligible R&D. There must be a clear reliance of subsequent eligible R&D on the "asset" that had been acquired.

6. R&D Intensity (RDI)

Operating revenue is all income that a company receives from its normal business activities including revenue from sale of goods and services, dividends and royalties paid to you by other companies.

$$\text{RDI} = \frac{\text{Eligible R\&D}}{\text{Operating revenue}}$$

There may be some instances where operating revenue derived overseas by subsidiaries of a group may be excluded. Discuss this with your account manager and should this apply, Callaghan Innovation will provide written advice.

7. Appendix One – Review Report to the Directors of the Entity

An example of an R&D Growth Grant application certificate / annual review certificate required to be provided by a registered practicing chartered accountant. This template can be downloaded from your client report in the Investment Management System (IMS) or downloaded from [the Callaghan Innovation website here](#)

Review Report to the Directors of [entity]

We have reviewed the Confirmation of Eligible Research & Development Expenses dated [ddmmyy] for [Entity] which states eligible R&D expenditure of [\$] for the period [ddmmyy – ddmmyy].

The Directors have confirmed to us that they have prepared the Confirmation in line with:

- *Ministerial Direction to Callaghan Innovation – Criteria for Assessing Proposals for Funding dated 3 October 2018* ("Ministerial Direction")
AND

Growth Grant Funding Agreement dated [ddmmyy] between the [Entity] and Callaghan Innovation ("Funding Agreement") – (where this review report is to support an annual Confirmation).

The Board of Directors of [Entity] is responsible for the preparation of the Confirmation.

We do not express an audit opinion on the Confirmation. Our responsibility is to express a conclusion on the Confirmation based on our review. We conducted our review in accordance with ISRE (NZ) 2400 / 2410 / 3000 / 3100 [delete non-applicable].

This report has been prepared solely for the exclusive use of [Entity] to meet its obligations under the Ministerial Direction and Funding Agreement). We agree that a copy of this report may be provided to Callaghan Innovation for their information, but we do not accept any duty, liability or responsibility to Callaghan Innovation in relation to this report. This report is not to be used for any other purpose, recited or referred to in any document, copied or made available (in whole or in part) to any other person without our prior written consent. We accept or assume no duty, responsibility or liability to any party, other than you, in connection with this report, including without limitation, liability for negligence.

Because of the inherent limitations of any limited assurance review it is possible that fraud, error or non-compliance may occur and not be detected. A review is not designed to detect all instances of non-compliance with the *Guidelines – Evidencing Eligible R&D and RDI for Growth Grants*, as it generally comprises making enquiries, primarily of management of [Entity], and applying analytical and other review procedures. The opinion expressed in this report has been formed on the above basis.

Our procedures included analytical review, discussion with management and agreeing financial information on a sample basis to supporting records. These procedures have been undertaken to form an opinion that nothing has come to our attention that causes us to believe that the Confirmation does not present fairly, in all material respects, the operating revenue and research and development expenditure of [Entity] for the period [ddmmyy – ddmmyy] in accordance with the Ministerial Direction and the Funding Agreement/Proposed Funding Agreement (delete non-applicable).

We confirm that the preparer of this report has no direct or perceived conflict of interest whether this be personal, professional and/or financial interests in [Entity] other than providing professional accountancy services.

We confirm that the preparer of this report has read and fully understands the Guidelines for Evidencing R&D and RDI for Growth Grants specifically version 3.3 dated August 2019.

Dated: [ddmmyy]

[Independent Chartered Accountant]

8. Appendix Two - Confirmation of Eligible Research & Development – For Year End Claims

An example of Confirmation of Eligible Research & Development letter for R&D Growth Grant year end claims. This template can be downloaded from your client report in the Investment Management System (IMS).

[Company letterhead]

[Date]

Callaghan Innovation
Business R&D Grants
PO Box 11529

Manners Street
Wellington 6142

Confirmation of Eligible Research & Development Expenses Claimed Under Growth Grant for Year End Claim

We confirm that the below table is an accurate statement of the eligible Revenues and Research and Development expenditure (in line with the *Ministerial Direction to Callaghan Innovation – Criteria for Assessing Proposals for Funding dated 3 October 2018* "Ministerial Direction") of [Entity] "The Entity" for the period [ddmmyy to ddmmyy].

The Entity is part of a Group and the confirmation and financials supporting this confirmation have been reported accordingly. [Delete if not applicable]

\$000	
Operating revenue	\$
Total Research and Development	\$
Less General Exclusions (Ministerial Direction)	\$
Less Specific Exclusions (Ministerial Direction)	\$
Eligible R&D Expenditure	\$
RDI	%

To reach this conclusion we confirm the following:

- We have appropriate knowledge of the Funding Agreement entered into by The Entity for an R&D Growth Grant and the obligations of The Entity under this agreement.
- We have reviewed and understand the document *Guidelines – Evidencing Eligible R&D and RDI for Growth Grants*. Where necessary we have sought clarification from Callaghan Innovation.
- We have appropriate knowledge of The Entity's accounting systems and accounting records and understand how management makes accounting estimates in line with the Ministerial Direction to determine eligible Revenues and Research and Development expenditure.
- We have made enquiry with management and staff within The Entity, as appropriate, and evaluated the evidence obtained.
- Nothing has come to our attention that causes us to believe that the claims made under the Growth Grant Funding Agreement, are not, in all material respects, in accordance with the Funding Agreement and Ministerial Direction.

(All documents referred to are available to be downloaded from [the Callaghan Innovation website here](#))

[Name]

Director

[Name]

Director



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