Exclusive

PwC slashes R&D staff after being targeted by ATO

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Professional services giant PwC laid off more than 30 staff and two partners resigned from its division advising companies on research and development incentive applications as clients were hit with government audits forcing them to pay back millions of dollars.

The mid-year staff cuts came as Australian technology start-ups like online jobs marketplace Airtasker were stunned by an apparently tougher focus from the Australian Taxation Office and AusIndustry, towards the self-assessed incentives, in a bid to claw back $2.9 billion from dubious claims.

Amid the shock of the apparent removal of the local start-up software sector's most important form of government assistance, questions have been raised about the role of consulting firms, who had charged some clients over $100,000 for advice on making ultimately unsuccessful R&D claims.

Sources say PwC was told as early as 2016 by the ATO that its R&D advice marketing was too aggressive. **Roger Stonehouse**

While numerous firms have been advising local companies on their R&D claims, *The Australian Financial Review* understands PwC's cuts were the culmination of problems that arose in the way its practice was run, which brought its clients under the auditors' microscope.

Sources said PwC was told as early as 2016 by the ATO that its R&D advice marketing was too aggressive and risked breaching tax promoter penalty laws, put in place to prevent firms advocating tax exploitation schemes.

ATO has 'narrow approach'

While PwC promptly stopped the promotional material, the issue led to the ATO putting a heightened focus on its clients' R&D claims.

The *Financial Review* has been told that a number of start-ups learned during the audit process that PwC advisers had unchecked a box on their application forms to hide the fact that they advised on their claims.

This was then confirmed by a number of sources familiar with PwC's operations, who said advisers were informally told not put the firm down as the tax advisers for R&D claims for a period of around a year.

Approached about the dramatic reduction of its R&D practice, a spokeswoman for PwC said the ATO and AusIndustry had taken "a far narrower position in relation to the application of the scheme" and created a "level of uncertainty for business".

"This change in approach by AusIndustry and the ATO, together with the changes announced in the May budget, which restricted the ability of large businesses to avail themselves of the R&D concession, lead to a material reduction in the demand for R&D services which, in turn, resulted in PwC restructuring its R&D business," she said.

"As a result of this restructure a number of partners retired from the firm and a number of staff were made redundant."

Airtasker co-founder and chief executive Tim Fung last week said that while the company could afford to pay back the millions in incentives it had been awarded since 2014, it would make him reconsider the viability of Australia as a base for his fast-growing company.

While Mr Fung declined to publicly out the advisers, the *Financial Review* has independently confirmed that it was PwC that advised Airtasker on its rejected claims.

Mr Fung said he remains frustrated with his advisers over the consequences of its advice, and actions since the audit got serious.

"We did believe that there was a differentiated advantage from going to someone with that kind of brand, reputation and expertise behind it. There probably are some cowboy advisers out there but we went to a top-tier one so there wouldn't be an issue. But ironically, that hasn't been the case," he said.

Mr Fung said he viewed the main problem facing the local tech industry to be AusIndustry's rigid application of its R&D eligibility requirements, and that he believed the advisers "were absolutely trying to do the right thing".

PwC advisers 'uncontactable'

However he said the debacle Airtasker currently faces was upsetting, in the context of having dealt with a high priced, top of the range advisory firm.

When problems arose with Airtasker's claim PwC asked for further payments to remedy the situation. Mr Fung has since moved Airtasker away from the firm and is working with different advisers to try and resolve its case.

"We're pretty upset by the whole situation to be honest. I mean, to receive advice, then take responsibility for that advice, to not have any outcome from that advice, and to then incur penalties, and to not be reimbursed for previous costs, let alone charged more fees, is definitely surprising," Mr Fung said.

"In the case of the top-tier firm that we used, somewhat mysteriously the department that handled all the work that we did was disbanded and all of the people are now uncontactable."

PwC's spokeswoman refused to comment on the circumstances behind the departure of the two R&D partners, saying the firm has a policy of not commenting on "partner retirements". The partners in question are currently aged 33 and 48, while the firm has an unofficial retirement age of 55. The firm is understood to refer to any partner departure as a "retirement".

She denied the firm had been told by the ATO to stop promoting certain R&D advice and also that the firm submitted R&D applications without indicating they were the adviser.

The firm continued to provide R&D services "with six partners and associated teams in this business today," she said.

PwC takes on ATO

PwC has has been fighting the ATO on other fronts over its tax advice. In October, PwC admitted it was behind an "aggressive" tax structure, which triggered an investigation into the firm and its clients.

The firm has also received formal requests from the ATO over activity that could potentially breach tax promoter penalty laws, as well as being in the spotlight over its alleged role in a tax restructure by Swiss mining group Glencore.

In 2017, the ATO become so alarmed at the role of consultants in R&D claims that four of the five taxpayer alerts it published that year were about the incentive.

A February 2017 alert warned the Tax Office planned to review R&D claims from software companies amid concerns that advisory firms were encouraging companies to claim for work that didn't count as pure R&D.

In the same month, another alert around R&D claims in the construction industry clarified the rules around what could be claimed, and warned that the Tax Office was targeting companies that used advisers who applied "high-risk practices" when preparing claims. However the change in tone of R&D policy has hit the emerging tech start-up sector particularly hard.

Head of community and partnerships at financial technology start-up industry group FinTech Australia, Rebecca Schot-Guppy, confirmed that many of its members, which had previously been successful in claiming R&D grants, were now having those claims contested and claimed back by the ATO.

She said R&D incentives and grants had become the lifeline that provided the runway for many fintechs as they headed towards a capital raise or a launch date. She said it was reasonable for such companies to rely on R&D expert consultants to help with their claims.

"Founders can't do it all. It would be difficult for start-ups to grow without the assistance of advisory firms and other agencies. We see this as a normal practice of business," Ms Schot-Guppy said.

"The advice we offer our members is to ensure they do their due diligence before taking on an external provider. We would also advise them to leverage their networks to help track down best advice possible."

Veteran advisers in the area feel that the rules established by AusIndustry and the Tax Office are not unreasonable but are not suitable for companies developing software, and need to be reformed.

R&D incentive timeline

December 2015

Former Prime Minister Malcolm Turnbull announces an "ideas boom" and sets a focus on science, research and innovation as long-term drivers of economic prosperity, jobs and growth.

Software and tech start-ups encouraged to apply for grants under the government's R&D scheme, which has been around in some form since 1985.

January 2017

AusIndustry targets Airtasker with an audit for the company's two most recent R&D rebates, dating back to 2014.

February 2017

The Australian Taxation Office send out an alert, which said it planned to review R&D claims from software companies amid concerns that advisory firms were encouraging companies to claim for work that didn't count as pure R&D.

May 2018

The government announced changes to the R&D tax incentive in the May budget designed to save $2.9 billion over 2018-19 to 2020-21 by reducing grant levels for many claimants and beefing up compliance and enforcement measures.

October 2018

Airtasker faces paying back millions of dollars, plus a potential 75 per cent penalty for making "erroneous" claims.

AusIndustry provides no explanation other than saying the claims didn't meet the requirements.

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