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Utilising Plantation Timber - Australia's Renewable Resource

General Manager
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The Treasury
Langton Crescent
PARKES ACT 2600

2nd February 2010

To Whom It May Concern

On behalf of Austicks Pty Ltd, I welcome this opportunity to provide feedback on the exposure draft of the Tax Laws Amendment (Research and Development) Bill 2010 released 18 December 2009 ("the exposure draft").

Austicks Pty Ltd (Austicks) is a privately owned company based in Gladstone, Queensland, who currently employs around 50 people, and produces high quality ice-cream sticks from hoop pine, generating an annual turnover of around $9m. Austicks has been manufacturing ice cream sticks and coffee stirrers in Gladstone since 1997. The company's operating objective is to continually strive for better utilisation of available timber resources.

Austicks produces 1.2 billion units annually for the global market, and is the last remaining wood processing plant of its kind in Australia. With fierce competition from Canada, China and Europe, Austicks has remained competitive by identifying and implementing new technology and efficient processes to achieve greater productivity, lower operating costs, and a more sustainable future. Accessing the R&D Tax Concession has assisted the company make the improvements in its business necessary to remain competitive.
Austicks considers itself to be an SME and representative of the profile of company the Government desires to further assist through these changes. Austicks' R&D means the company can remain competitive and continue to employ 50 people in the Gladstone area. Further, when conducting R&D, Austicks uses local service and equipment providers to assist it to deliver improvements to its business.

Our company commends the Government's stated intent in delivering a "more generous, more predictable, and less complex tax incentive", however we do not believe the legislation achieves this intent in its present form.

Whilst we understand the Government's intention to tighten eligibility in order to focus incentives on worthy activities which will benefit the broader Australian economy, we believe the combination of *the high number* of tightening measures contained in the exposure draft serves to drastically reduce the generosity, accessibility and attractiveness of the R&D Tax Incentive program.

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Major concerns

Within the exposure draft, there are now five key ways in which eligibility has been significantly tightened and claims will be curtailed, making the system *less generous, more complex and less predictable* to Australian businesses.

1. The requirement for 'considerable novelty' in place of 'innovation' – this both raises the bar for eligibility of potential claimants, while increasing uncertainty by replacing a well understood and defined term. Innovation is a well understood term, and the relationship between innovation, productivity and growth is similarly well understood, across OECD countries and in a local context. The shift in term seems to favour the "blue sky" R&D common in academic settings over business innovation – the incremental improvements which are vital to business competitiveness;
2. The introduction of the "and" test for the eligibility test of considerable novelty <u>and</u> high levels of technical risk. We believe that this change to the definition will lead to the exclusion of many genuine R&D activities that should be supported and are currently eligible for support under the existing R&D tax concession. As a stand alone measure, this change may be acceptable, but in combination with the other new eligibility restrictions, it will exclude too many meritorious R&D endeavours and overall support for innovation will be considerably reduced. If this change is to be adopted, then other proposed restrictions should not be introduced otherwise the aim of the new tax credit to provide a more generous concession will not be fulfilled.
3. The introduction of the "dominant purpose" test for supporting activities. This represents a significant tightening over the existing test in the current program, which only requires that a support activity be carried out for "a" purpose directly related to the core R&D activities. This new test will greatly reduce the amount of eligible support activities that may be claimed, and will also impose a severe evidentiary burden on claimants of the new R&D tax credit. Many support activities will have a commercial purpose as well as an R&D purpose and providing evidence that one purpose is clearly dominant over the other will be almost impossible in many cases. This introduces considerable uncertainty over the eligibility of claimed supporting activities and is highly undesirable as a consequence. Please note, this uncertainty is acknowledged in the discussion of the new test in the Explanatory Memorandum.

4. The apparently arbitrary exclusion of a large number of activities from being either core or supporting activities, via the repurposing of the former s73B(2C) of the Income Tax Assessment Act 1936 (ITAA 1936). We believe that this change, while having obvious negative consequences for the computer science and information technology industries in Australia, also has (possibly unintended) consequences, including that:

    a. s355-35 (2)(l) renders clinical trials ineligible as they are performed for (amongst other purposes) the preparation of a regulatory requirement of the Therapeutic Goods Administration;

be quarantined (and not included in the feedstock calculation) being labour and plant depreciation.

If the above changes are made to the exposure draft, the Government will be able to achieve its objectives for the new tax credit – that is, implement a more generous, more predictable and less complex incentive that targets additionality and spillovers whilst maintaining revenue neutrality.

However, if the Exposure Draft is implemented in its current form, the direct outcome would be a significant lowering of the support for innovation in Australian businesses. As a result,, the Government risks losing scientific, information and engineering and other technical industries (and jobs) offshore, as well as reducing the development of products, technologies and processes which will boost productivity – the very lever which the Government has stated will support an aging population. Reduced effectiveness and uptake of the R&D Tax Incentive will also negatively affect Australia's Business Expenditure on R&D ("BERD").

If you would like to discuss this submission, please feel free to contact me on **0749727777**.

Yours sincerely

Madeleine Spry
Financial Controller