General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

5 February 2010

To Whom It May Concern

On behalf of Hyne & Son 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").

Hyne & Son is an important innovator and employer throughout the east coast of Australia. I am writing to you to express my concern regarding the proposed R&D tax incentive changes and the impact this will have on our R&D and our operations.

For many years Hyne & Son has invested significant resources in R&D at its Tuan (Maryborough Qld), Tumbarumba NSW, Mary Valley Qld and our Brisbane Virginia operations. Our R&D programs have focused on improving plant productivity, reducing energy and water usage, improving product quality and developing new product lines to meet changing market demands and challenges in local and foreign competition.

R&D at Hyne

To provide examples of the great R&D Hyne & Son undertakes:

- Hyne's Virginia operation has undertaken significant R&D in developing its production process to enable finger-jointing of a new feedstock developed in-house at our Tuan mill (T2 Blue). The new T2 Blue product is a treated structural product which repels termites. Virginia manufactures I-beams from this feedstock – its kerosene base causes significant issues with the feedstock slipping in the traditional press process carried out at Virginia. To overcome this Hyne developed an entirely unique two stage press production process that would enable the finger-jointing of T2 treated feedstock with the same strength specifications as untreated feedstock, but with the benefit of termite resistance – an important differentiator in our markets. This involved significant resources and achieved a reduction in associated wastage from 15% to 5%.
- The Tumbarumba operation is currently undertaking significant development in adapting Linear High Grade (LHG) technology for the Radiata species at its Dry Mill. The success of this project will enable us to automatically scan and grade feedstock thereby greatly improving the accuracy of our production process. A major component of this R&D necessarily involves software development to put into effect the grading rules and process automation.

- The Mary Valley operation is a world leader in developing optical grading and processing technology as part of the Super-Cut Line upgrade. This operation is the fastest and most effective of its kind in the world. However, it has taken many years and significant time and effort to get to this stage. During this development period Hyne & Son has incurred substantial expenditure and tolerated reduced production.

It's initiatives like these that keep these plants viable. We rely on funding from the R&D Tax Concession claims to foster innovation and support projects like this.

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. We believe the combination of *the high number* of tightening measures contained in the exposure draft, will drastically R&D being undertaken in Australia.

Impact

Based on our estimations the changes to the R&D incentive program will reduce our claims from $30m to $1.2m per year. We do use the tax savings from the R&D Tax Concession to fund further R&D in our business, meaning we will have $2m less per annum to spend on R&D. This will also have a detrimental impact upon the culture of R&D at our organisation – the use of the R&D Tax Concession to provide project managers with budgets to conduct further R&D effectively incentivises project managers to undertake R&D, to develop great ideas, and to share learning's within the company and industry. Hyne has a history of fostering great ideas and successfully developing these into world first technologies, improved products and processes and commercialising these for the benefit of the Australian economy – the impact of the draft law will see funding for R&D diverted away from companies like Hyne to companies who fail at their R&D.

Major concerns

Within the exposure draft, there are two 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. Software and Pre-production Exclusions

Many of the projects undertaken involve the development of new manufacturing equipment. These projects almost always involve PLC logic work, which is fundamental to the automation of the equipment and the integration with the existing infrastructure. These activities would now be specifically excluded and it is difficult to see the rationale for this – surely automation and the associated productivity is something the Government would support?

The proposed Legislation also excludes "pre-production" including trial runs. Our concern is that this exclusion is very broad, and if interpreted literally could exclude legitimate experimentation. We don't believe this is the Government's intention.

We believe the tightened definitions of core and supporting activities adequately eliminates activities from receiving concessional treatment where there is questionable merit for public support.

2. Augmented Feedstock

Due to the unique nature of timber feedstock Hyne frequently needs to trial new or improved equipment and manufacturing processes in a production context. The augmented feedstock rule will significantly impact Hyne's claims and as such, its ability to fund further R&D. All funding from the R&D Tax Concession is diverted to new R&D initiatives, without this funding we will do less R&D.

Submission Request

There is, presently, a unique opportunity to draft the legislation precisely and specifically to meet the policy intent – this opportunity should not be missed. Given the above issues and complexities in the current exposure draft, we submit that the Government should:

1. Remove the exclusions for software and pre-production activities;
2. Revert to the existing feedstock provisions of s73B of the ITAA 1936 which, we believe, effectively limit incentives to net cost of trials or alternatively quarantine labour and plant depreciation from the feedstock calculation.

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 07 41 211 201.

Yours sincerely

Trevor Dixon
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Hyne & Son Pty Ltd