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Dear Representatives of the Government,

R&D: Draft legislation to significantly reduce R&D benefits for companies with turnover greater than $20m

Sentek Technologies is an Australian company, founded in the early 1990's to meet the commercial demand from farmers for real insights into their irrigation decisions. Since then, the company has grown to export to over 80 countries while continuing to manufacture in Adelaide, South Australia.
With a team of specialists across agronomy, soil science, and irrigation technology, our products are designed to provide insights to support better irrigation decisions. With 36 employees as at December 2019, Sentek relies heavily on the R&D tax incentive to allow it to invest aggressively in research and development, and to continue to grow as a company.

Investment in innovation is an important part of our corporate strategy. Last financial year alone Sentek spent over one million dollars on eligible R&D expenditure. Companies such as Sentek that operate in the advanced manufacturing industry require a far greater degree of R&D investment than companies positioned in more traditional industries. If Sentek is to remain a world leader in its field, it must continue to invest aggressively in research and development, that will ultimately result in more innovative products that benefit society as a whole.

The R&D Tax Incentive has supported our R&D effort for an extended period and has allowed us to pursue projects that we may not have otherwise have pursued due to inherent technical risks. Undertaking these R&D initiatives has allowed us to remain at the forefront of precision measurement and management of water and salinity dynamics. Over the years Sentek has forged strong ties with universities, as a result of its continued commitment to invest in research and development. Further, we have found the certainty provided by the program to be greater than that provided by grant or loan programs, which are usually highly competitive and time consuming to apply for.

We are extremely concerned by the Government's proposed changes to the *R&D Tax Incentive Programme*, as announced in the *Treasury Laws Amendment (R&D Tax Incentive) Bill 2019* introduced to parliament on 5 December 2019. This Bill seeks to reduce the cost of the program to the detriment of companies actively trying to innovate in Australia. Indeed, **we estimate a 47% reduction in the R&D tax benefit** we receive that will in turn impact our ability to undertake R&D projects. **This reduction is a direct consequence of the proposed 'intensity measure' calculation**.

The current Bill is almost identical to the *Treasury Laws Amendment (Making Sure Multinationals Pay Their Fair Share of Tax in Australia and Other Measures) Bill 2018 introduced in* September 2018, which was universally criticised and rejected by all areas of industry, and the tertiary and research sectors. That Bill was also recommended for deferral by the Senate Economics Legislation Committee until further examination and analysis of 'unintended consequences' was undertaken. We note that the Committee's key recommendations have not been considered in the current Bill.

Some key insights as to how the proposed changes will adversely impact our business:

- **Intensity measure will reduce our ability to employ technical staff and maintain or grow our R&D spend**: The proposed intensity measure will have the opposite impact of that intended by the R&D incentive – at 4% benefit, we will have limited ability to invest in R&D and employ talented staff in Australia. We will need to reconsider the location and quantum of R&D employment and spend in Australia.

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- **Uncertainty around R&D intensity:** There are many variables that impact our business and cannot be predicted in advance of the financial year. This makes it impossible to accurately predict our R&D intensity as we won't know our 'total expenses' until after the end of the income year. Thus from a planning perspective it will be extremely difficult for us to be incentivised to spend more on R&D when it is not possible to predict the ultimate tax benefit that will be received until after our financial year end. This is particularly challenging for longer-term projects.

- **Australian companies unfairly disadvantaged:** As an Australian-based entity we take pride in paying the correct amount of tax calculated from our domestic and international income. However, under the proposed changes, foreign-based multinationals will be unfairly advantaged as compared to their Australian contemporaries in accessing the R&D Tax Incentive. This inequality results from the current mechanism to calculate the rate of R&D intensity, which will require us to include total group business expenses, which in turn serves to reduce our rate of intensity as compared to foreign-owned multinationals conducting R&D in Australia, who will only need to include their Australian-based expenditure within the calculation. The calculation method results in an inequitable outcome and will place us at an immediate and distinct disadvantage compared to our foreign-owned competitors, who will receive a greater benefit in relation to their Australian-based R&D activities.

- **Retrospectivity and impact on current R&D projects:** We have a number of projects underway that involve R&D activities and for which we have budgeted in the R&D Tax Incentive. If enacted, the Bill will take effect for income years commencing on or after 1 July 2019. This will have an immediate impact on our current projects, potentially resulting in us reducing the scope of our R&D and/or relocating it to another country. Furthermore, given that the central policy objective of the R&D Tax Incentive is to promote additional investment in R&D, it is difficult to reconcile how a retrospective application would serve the program's additionality target or spillover. Any proposed changes to the R&D Tax Incentive should be widely consulted on and have a commencement date at least a year or more into the future to allow companies to plan for it.

In the current economic climate, business needs Government leadership and support, especially where it will help drive commercial innovation. The Government should **increase** its support for R&D via the R&D Tax Incentive, not reduce. **We therefore strongly oppose the *Treasury Laws Amendment (Research and Development Tax Incentive) Bill 2019* in its current form.**

We would welcome the opportunity to discuss our company and the value the R&D Tax Incentive provides to us.

Yours Sincerely,

[redacted]

Nick Ktoris

Managing Director