Since 1948

MONTAGUE

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26th February 2020

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Via email: economics.sen@aph.gov.au

Dear Committee,

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

Montague Bros. Holdings (Pty) Ltd (Montague) is a large Australian grower of a variety of Apples and Stone fruits, most notably being an Australian grower of Jazz Apples. Montague operate orchards at various locations throughout Australia in various climates, providing apples year-round and stone fruits throughout the warmer months. We have an annual turnover of $170,000,000 and over 200 employees.

Investment in innovation is an important part of our corporate strategy. To date, we have invested in order to improve upon our current capabilities, and ensure we produce some of the highest quality apples and stone fruits in Australia. We also invest in projects to develop methods to improve yield. In FY19 alone, we invested over $500,000 on R&D, a material sum for a private family owned company.

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 been pursued due to inherent technical risks. Undertaking these R&D initiatives has allowed us to remain a leading grower of apples in Australia. Furthermore, 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 that a 47% reduction in the R&D tax benefit we receive will in turn impact our ability to undertake R&D projects. This reduction is a direct consequence of the proposed 'intensity measure' calculation.

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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: Inherent disadvantage due to our cost base: The intensity measure fails to take into account recommendations by the Senate Committee to incorporate a methodology capable of offsetting the adverse impact to different industries that may be disadvantaged as compared to low cost input sectors. For growing agri-businesses like ours, it will be increasingly difficult to exceed the 4% R&D intensity premium by nature of our cost base. This would limit us to a 4.5% benefit compared to the current 8.5% benefit.

- 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 4.5% benefit, we will have limited ability to invest in R&D.

- 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.

- 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.

- Integrity measures: We also note that the Bill includes various integrity measures. While we support measures to improve integrity of the program, we note the recent report of the Australian Small Business and Family Enterprise Ombudsman which found both the ATO and AusIndustry approached reviews prejudicially as a cost saving exercise. We urge both regulators to use additional funding to improve their review processes and restore industry's faith in their administration of the program.

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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.

Regards

[redacted]

Frederic Meuwly
Chief Financial Officer
Montague