



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

**HOUSE OF
REPRESENTATIVES**

STANDING COMMITTEE ON INDUSTRY, SCIENCE AND
RESOURCES

Reference: Increasing value-adding to Australian raw materials

THURSDAY, 28 JUNE 2001

CANBERRA

BY AUTHORITY OF THE HOUSE OF REPRESENTATIVES

INTERNET

The Proof and Official Hansard transcripts of Senate committee hearings, some House of Representatives committee hearings and some joint committee hearings are available on the Internet. Some House of Representatives committees and some joint committees make available only Official Hansard transcripts.

The Internet address is: **<http://www.aph.gov.au/hansard>**

To search the parliamentary database, go to: **<http://search.aph.gov.au>**

HOUSE OF REPRESENTATIVES
STANDING COMMITTEE ON INDUSTRY, SCIENCE AND RESOURCES
Thursday, 28 June 2001

Members: Mr Prosser (*Chair*), Mr Cadman, Mr Hatton, Mr Lloyd, Mr Morris, Mr Nairn, Ms Roxon, Mr Cameron Thompson, Dr Washer and Mr Zahra

Members in attendance: Mr Cadman, Mr Lloyd, Mr Morris, Mr Prosser, Ms Roxon, Mr Cameron Thompson and Mr Zahra

Terms of reference for the inquiry:

To inquire into and report on the prospects of increasing value-adding to Australian raw materials. The Committee will start with an evaluation of the current state of value adding in Australia, and how that compares internationally. This will provide a base from which to evaluate the following topics:

- incentives and impediments to investment;
- intellectual property rights;
- national/international marketing factors which may encourage or hinder Australian value-adding;
- government intervention, both nationally and internationally;
- the location of value-adding industries and projects in regional Australia;
- resource licensing/permit arrangements;
- the impact of vertical integration within particular industries; and
- the Australian skills base and any associated impediments.

WITNESSES

ANTIOCH, Mr Gerard Januarius, Manager, Business Income Unit, Treasury.....	375
COOPER, Mr Ian Donald, Segment Leader, Innovation Segment, Large Business and International Line, Australian Taxation Office.....	375
EDWARDS, Dr Russell Thomas, General Manager, Program Management, Department of Industry, Science and Resources	375
JENKINS, Ms Carolyn Joy, Manager, Tax Task Force, Innovation Policy Branch, Department of Industry, Science and Resources	375
LOWNDES, Mr Terrance Anthony, Division Head, Industry Policy, Department of Industry, Science and Resources	375
MILLER, Mr Geoffrey John, Assistant Commissioner, Law Design and Development, Australian Taxation Office.....	375
RYMER, Dr Les, General Manager, Minerals Development Branch, Department of Industry, Science and Resources	375
TUNE, Mr David John, General Manager, Business Income and Industry Policy Division, Treasury.....	375

Committee met at 11.39 a.m.

COOPER, Mr Ian Donald, Segment Leader, Innovation Segment, Large Business and International Line, Australian Taxation Office

MILLER, Mr Geoffrey John, Assistant Commissioner, Law Design and Development, Australian Taxation Office

EDWARDS, Dr Russell Thomas, General Manager, Program Management, Department of Industry, Science and Resources

JENKINS, Ms Carolyn Joy, Manager, Tax Task Force, Innovation Policy Branch, Department of Industry, Science and Resources

LOWNDES, Mr Terrance Anthony, Division Head, Industry Policy, Department of Industry, Science and Resources

RYMER, Dr Les, General Manager, Minerals Development Branch, Department of Industry, Science and Resources

ANTIOCH, Mr Gerard Januarius, Manager, Business Income Unit, Treasury

TUNE, Mr David John, General Manager, Business Income and Industry Policy Division, Treasury

CHAIR—I declare open this public hearing of the inquiry into value-adding of raw materials in Australia and thank the officials from the Taxation Office, Treasury and Department of Industry, Science and Resources for their attendance. I am obliged to remind to you that the proceedings here today are legal proceedings of the parliament and warrant the same respect as proceedings in the House. The deliberate misleading of the committee may be regarded as a contempt of parliament. The committee prefers that all evidence be given in public, but if at any time or at any stage you wish to give evidence in private please ask to do so and the committee will give consideration to your request. I invite you now to make some introductory remarks before we proceed to questions.

Mr Tune—I might start, Mr Chairman. We did have a brief discussion beforehand amongst the three departments to discern whether we needed an opening statement, and I think we came to the view that we did not, but of course we are happy to help you in any way we can.

CHAIR—Thank you for that. I now invite members of the committee to pose questions. As you are aware, in our previous meetings we were very keen to get to the value of tax incentives or concessions, particularly in the area of R&D, looking at value adding to Australian industry—particularly resources.

Mr ZAHRA—There has been a bit of talk about different approaches which can be employed to try to provide incentives for companies to involve themselves in various types of business activities in rural and regional Australia. Some of that has involved the application of different tax rates and different incentives for some regions, based on zones. Can any of you

provide a view as to whether or not you think this is a good and smart way to go, based on international experience or based on perhaps some understanding you might have of trying to apply similar programs over the last 30, 40 or 50 years?

Mr Tune—I will start and others might like to add to this. I am aware of a number of proposals that are around, but the one in particular that I have seen is the one put out by the Institute of Chartered Accountants and the Municipal Association of New South Wales on enterprise zones. I understand there are others. Various proposals have been put forward over the years.

Mr ZAHRA—For our benefit, could you clarify what those proposals are that you have heard about, just to make sure we are talking about the same thing?

Mr Tune—The one that I am aware of is the enterprise zones one that I just mentioned. I understand the NFF put a statement out earlier this year as well.

Mr ZAHRA—What does the enterprise zone consist of in that proposal?

Mr Tune—As I understand it, it is to highlight the regions with particularly high levels of unemployment and provide some tax incentives to assist industry to locate in those particular regions. That is the proposal we have seen, and that is on the public record, as I understand it.

There are a couple of issues with those sorts of proposals, from a Treasury perspective. Firstly, there are issues around administration of those sorts of things. Whenever you move to set things up on a zonal or regional basis you always have boundary issues, which are difficult to define. You always have people who are just outside that zone, so therefore you have areas of discontent as a result of that, and any adjustment to the boundaries to pick up that area of discontent will create another boundary with another set of issues surrounding that.

Mr ZAHRA—Would it be Treasury's view that that is difficult to administer on that basis?

Mr Tune—I do not know. You would have to ask the tax office about administration per se, because they administer the zone rebate at the moment and it does have boundaries. I am looking at it from the policy viewpoint that you do have these problems of unfairness and inequity for a person on one side of the street, particularly with this proposal. As I understand it, some of the assistance could stretch into the verges of the major cities where you have an LGA that may be partly rural and partly metropolitan. You could well have situations where two industries or two plants are on opposite sides of the street, and one would be in and one would be out.

CHAIR—We could probably do it through rebates, couldn't we, because of the implications to the Constitution?

Mr Tune—I am not a lawyer, so I do not know if I can comment on the constitutional issues. As I understand it, there is debate about the constitutionality of these sorts of issues. I do not know if it is a clear-cut issue.

Mr ZAHRA—Can I interrupt you just for a moment? We have the representatives from the Australian Taxation Office here as well, and this is really the purpose of this roundtable. In relation to the effectiveness or efficacy of those programs, and the difficulties that are encountered in terms of picking which areas get the benefit or the rebate and which areas do not, I invite the ATO to offer a comment as to whether or not it is effective, straightforward, simple or none of those things when you apply that type of public policy.

Mr Miller—As you discussed the last time we met, I have spoken to the areas which administer it and they do not have any particular problem administering the current zone rebate. We have produced a tax ruling which sets out virtually every town in Australia and says, if you are in that town, whether you are in or out of the zone rebate. Once that ruling was done, it became fairly simple for people to determine whether they were eligible for a rebate or not. Apart from having to go to some detail in determining which towns are in and which towns are out—which was something done initially when the zone rebate came in—there is no other inherent administrative problem.

CHAIR—Aren't Port Douglas and Cairns in a zone rebate area?

Mr Miller—I do not know; I do not have the ruling with me.

Mr ZAHRA—Mr Miller, are you referring to the diesel fuel rebate when you talk about 'the rebate'?

Mr Miller—No, I am talking about the income tax zone rebate.

CHAIR—In the A and B zones?

Mr Miller—Yes, the A and B zones.

Mr ZAHRA—Do the Treasury representatives, or any of the people we have here, have a view as to whether or not they are effective instruments of public policy in terms of providing incentives and delivering on the outcome of creating new jobs and new investment in those areas that are zoned as enterprise zones, or in terms of international experience?

Mr Tune—I am not aware of international experience—there could well be some, but I am not aware of it. The other issue that we would raise in relation to this is that the particular scheme that I mentioned at the outset—the enterprise zones—is one that is based on industry assistance rather than individual assistance, which is what the zone rebate is about. You create another set of problems in doing that in that you may have a business that has plant in many locations so there is increased complexity for that business in dealing with its tax affairs if you set that up.

Mr ZAHRA—Could you explain to me how the zone rebate that you are talking about works?

Mr Tune—The tax zone rebate?

Mr ZAHRA—Yes.

Mr Tune—The ATO can probably do that best.

Mr Miller—I do not have the details with me. There is a zone A and a zone B. If you fall within a zone A you receive a rebate—and I do not even recall the amount of that rebate—

CHAIR—The highest you can get back is \$1,600-odd and the norm is about \$300. It was put in place, as I understand—and you can correct me—to recognise the cost of living and the hardship in those sorts of areas, whether it be airconditioning or whatever.

Mr Miller—That is correct; even those words are used in the act itself to say why the zone rebate is there.

Mr ZAHRA—So you get that money back via your tax return?

Mr Miller—That is correct.

CHAIR—If you do not pay tax, you get nothing back.

Mr Miller—Yes, that is correct.

Mr Tune—There is an analogous provision in the social security system that provides a remote area allowance for pensioners, for example, who live in those same zones who do not pay tax. They can pick it up as a direct payment through the social security system as well.

CHAIR—In looking particularly at the tax plan that was put up by local government and at the New South Wales model—and I know that Ireland looked at some of these or may have in place some of these arrangements—has there been any work done to indicate whether a tax zonal arrangement is beneficial to the competitive success of the company, rather than a tax or money being directed towards another problem, and that may well be unemployment? Has the Treasury done any work to really say, 'If you have got an unemployment problem, let us address that and the overall economy, the competitiveness of the country or the region,' rather than artificially trying to fix the problem?

Mr Tune—We have not done any analytical work on these precise issues but perhaps I can make some general comments that might assist. Our view in general is that the appropriate way to provide assistance in these sorts of situations is to provide direct assistance that is targeted to the specific problem, preferably through an outlays program rather than through a tax expenditure or tax assistance of some kind. While we do not hold that view universally, it is an issue that we have in the back of our minds when we start analysing these sorts of issues.

The reason for that is largely twofold. One is that providing general tax concessions can create issues of cost control. It is very hard to control the cost of a tax expenditure, much harder than it is with an outlays program. Generally with tax expenditures there are also issues of transparency, so they tend to get hidden away, whereas outlays programs are much more overt. Treasury has put some work in over the years to try and increase the transparency of these sorts

of measures through a publication it puts out called *Tax expenditure statement*, which comes out annually. It tries to describe these tax expenditures and put some sort of estimate of the cost involved against them. They are general issues that we would be thinking of.

If you move towards targeted tax concessions, there are also issues that we are going to be changing the relative prices of whatever you are assisting—particularly if it goes to a specific industry or a specific zone—and that can have resource allocation implications which may be undesirable. You really need to look at these things on a case-by-case basis; but I do not think there is much doubt that any targeted tax concession to a particular industry or a zone of some kind will alter relative prices and that that may have some undesirable resource allocation issues.

In relation to enterprise zones as well, there is an issue of whether you actually end up with a net benefit overall in terms of the macro-economy. You may just be inducing some industries or companies to move from one region to another. They may be induced for tax reasons to move somewhere which may be seen in an open market as being an inefficient location for them. So the tax system is inducing them to do something that may alter the efficiency of that company and hence also impact on the efficiency of the economy. They are the sorts of general issues we would take into account when looking at these issues.

Mr ZAHRA—Do you have any advice on whether some of the schemes that used to be around years ago to provide incentives for TCF companies—for example, to set up in parts of rural and regional Australia—have delivered exactly the type of outcome that you are talking about: creating a non-market situation which, as soon as the subsidy runs out or the tax rebate is taken away, means that those TCF plants close? Do you have any experience or any information you can provide us with about that?

Mr Tune—I do not but my colleagues from Industry, Science and Resources may be able to comment.

CHAIR—The good example is that, once tariff barriers came down, if companies were not internationally competitive they had to make a commercial decision and either get better or close.

Mr Lowndes—You have made one of the points I was going to make. There are examples of firms where assistance has been withdrawn, and tariffs is a case in point as there have been some firms that have ceased to operate. On the other hand, some have adjusted to these changes and continued. In terms of specific TCF experience, I would have to take that on notice.

Mr ZAHRA—Are you aware of the program that I make reference to? I think it was a Victorian state government program, which provided a—

Mr Lowndes—There have been a lot of programs of one kind or another related to TCF. I am not an expert on them, but I can certainly take on notice whether there has been anything at the federal level.

Mr ZAHRA—It is something that we are seeing a lot of right now. In my electoral district, for example, the Givoni clothing factory has just closed down. I know that in Nicola Roxon's

electorate there has been a shake-out of the TCF sector as well. It would be interesting to see if the department would not mind preparing some information for us as to what the contribution of those types of schemes has been to the problems which are being experienced in the TCF sector right now. From my point of view, that sort of information is extremely important to us now in considering our deliberations and our recommendations.

Mr CAMERON THOMPSON—Is there someone here who can tell me roughly, on a global Australia-wide scale, how much is being spent every year in luring companies from overseas into Australia, using the same sorts of incentives that we may, for example, apply on a regional basis within Australia? We have had some recent examples in both Queensland and New South Wales: we have seen movie areas set up, we have got a movie area now being set up in Victoria and there are many industries that are being lured from overseas using these sorts of packages. Does anyone have a total value that is being allocated annually to that sort of pursuit?

Mr Lowndes—The difficulty with your question is that, as you pointed out, you have packages of that type being offered on a state basis, and there are also activities of the Strategic Investment Coordinator at a federal level. To my knowledge, we do not have a collated value of the total amount that would be spent. Essentially, you do have these things occurring on both a state basis in the different states and also at the federal level.

Mr CAMERON THOMPSON—What is the federal cost?

Mr Lowndes—There are a number of projects that we have supported, but again, in terms of working out what the annual cost is, I think I would have to take that on notice. It is certainly something we can respond to very quickly.

Mr CAMERON THOMPSON—Can someone then give me an idea of why conducting those sorts of pursuits internationally is so much more worthy than reorganising our affairs internally to suit our local priorities, as well as getting the business in the first place from overseas?

Mr Lowndes—I can only really talk about the Strategic Investment Coordinator. The assistance provided there will target both international companies locating here and Australian businesses expanding their operations; it is not as though it is purely directed at an international business. For example, the Visy pulp mill in Tumut received some support, and that is essentially an Australian operation. So it does vary. The criteria really relate to the sort of benefit of the investment for Australia as distinct from it necessarily being internationally based or domestically based. So, in terms of our particular program, it is not specifically targeted at international investment. That is the Strategic Investment Coordinator's actual investment support role.

In terms of what we might call marketing, the Invest Australia division within my department does engage in what we call marketing and facilitation activities. These are essentially directed at the international investment market. The international focus of that particular activity is based on a presumption that there will be many international investors who are not fully aware of the benefits, or of what Australia has to offer, whereas firms who are already in Australia will be more aware of that. So, in terms of what we might call investment promotion, the international flavour to that is reflecting a perception that the international investment community will be less

well informed about Australia's attractions than companies who are already actively operating here.

Mr CAMERON THOMPSON—If I were to ask you on notice to provide me with at least what the Commonwealth's allocations to that area have been over the last five years or so, would you be able to get that information for us?

Mr Lowndes—The strategic investment coordinator's activities are all public. I cannot answer the question now because I do not have the figures with me, but there is no problem.

Mr LLOYD—Submission No. 28.6 is from the Department of Industry, Science and Resources. Under the heading 'The R&D tax concession: roles and responsibilities', it states:

The R&D Tax Concession program is jointly administered by the Industry Research and Development Board (The Board) and the Australian Taxation Office (ATO) ...

It basically says that, if the ATO has any concerns about a company accessing R&D, it refers it back to the IR&D board for determination. What triggers that concern from the ATO? Is there a definition? How do you actually raise those concerns in the first place?

Mr Cooper—Basically if an audit is being undertaken, or we receive any other information which suggests to us that the activities being carried out by the company in question are not R&D or do not satisfy the requirements under the definition, after consideration of that we would then refer that on to the board.

Mr LLOYD—How do you make a decision through the audit that there is something wrong there if, in fact, the determination is made by another body? I am just having a little bit of trouble getting my mind around how you actually make that decision that there could be a problem.

Mr Cooper—It is based on the auditor's assessment at that particular time with regard to what is in the definition of R&D.

Mr LLOYD—So you take it on the advice of the auditor?

Mr Cooper—Yes.

CHAIR—And I presume there are consequences if they breach or vary in any way from the private binding ruling. I noticed in some of these submissions here that the ATO gives private binding rulings with regard to a particular project, particularly when it involves some R&D and some unproven technology.

Mr Cooper—Generally, it is any ruling which is given as to whether an activity qualifies under the R&D definition. That is, again, in the province of the Department of Industry, Science and Resources. They have a system which is akin to the ATO private binding ruling system, which provides a taxpayer with the certainty that they require or otherwise.

Mr ALLAN MORRIS—But being private, no-one else knows.

Mr Cooper—Up until this point they would probably be aware that there have been changes to the ruling system, which will result in the basic information behind the rulings being made available—that is, rulings from within the tax office.

Mr ALLAN MORRIS—But precedents established previously will not be known to other possible investors or to other possible companies?

Mr Cooper—No, that is true.

Mr ALLAN MORRIS—Wouldn't it be wise to make any of those now public, given the fact that you are changing the system?

Mr Cooper—This will be in the hands of the Department of Industry, Science and Resources. As I said, in terms of gaining certainty as to what is R&D, that is an ISR issue and they have a ruling system akin to the ATO one.

Dr Edwards—Perhaps I can just clarify that. I think there is a premise behind your question that I would like to clear up a little—that is, the board only makes determinations where the tax office refers a problem to it, and that is not the case. That would be the minority of things that the board looks at. The board is charged with administering the tax concession program, and that is a broad brush duty that it carries, which includes promoting the tax concession quite aggressively to market. The bulk of the companies that the board looks at and makes a decision about—whether it is R&D that the board consider fits the definition—come through its own activities, not by referral from the tax office. The board has its own compliance regime that is worked through AusIndustry, and that throws up a number of cases where the board, or its tax concession committee, may look at the R&D and make a determination of whether it is R&D under the definition of the act. By and large, most of the companies that are looked at by the board and its committees come through its own compliance activities.

Mr ALLAN MORRIS—Following the same theme, perhaps you could give us a hypothetical example: the write-off at Port Hedland, where the pre-tax and after-tax figures were quoted by BHP. From recollection, they were \$2.5 billion and \$1.6 billion after tax, so there were \$800 million of tax concessions. Would that have been just a straight company loss or a project loss, or would it have involved R&D? BHP published the result; therefore they would not be offended by the methodology. But for many of us who read these things, we do not quite know how the calculations are made and therefore what the implications are. For a \$2½ billion loss, there was an \$800 million net tax contribution and \$1.67 billion from the company after tax.

Mr Cooper—I am not across the particular details of the claim that you are talking about. I guess the general principle is that if the expenditure qualifies for deduction under the R&D concession, there is a write-off available at 125 per cent.

Mr ALLAN MORRIS—I have raised this issue with Taxation before. I would have thought you would at least be aware of this one. It is the biggest industry investment the country has made for a very long time and there was not much of a choice about it. I am not averse to it. I am just trying to understand how it was calculated because people have asked me, 'How come

that was written off?' I honestly do not know. I would have thought that if it were public policy the methodology would be made visible.

Mr Cooper—That would certainly be the basis of calculation.

Mr ALLAN MORRIS—But it would not necessarily be R&D. Some people say that Port Hedland was not an R&D project.

Dr Edwards—There are some difficulties in talking about tax matters of specific companies, which I am conscious of, because our act does not allow me to do so. Certainly, in very large projects of that nature, where the board went in to look at whether there was R&D, the question usually was not, 'Is the entire thing R&D?' It was, 'How much of it is R&D?' And the board makes a determination. I am generalising about very large infrastructure projects but, by and large, there is some R&D and there are some normal commercial activities. The board does take on the role of defining how much of it is really R&D.

Mr ALLAN MORRIS—Will the AMC magnesium plant at Gladstone be a full R&D project? It has not been done before.

Dr Edwards—Until we look at it, it is hard for me to comment. If they register for the tax concession and if, for some reason, the board decides in its compliance regime to look at it, then it will look at those activities that the company says are R&D. This is a self-assessment program and the company will register and say, 'We believe we've done so much R&D in this project.' The board's role is to register them, and then if it comes up in their compliance regime as a company that they should go and have a look at, they will just assess what the company has said is R&D and make a determination as to whether or not that is R&D.

Mr ALLAN MORRIS—Dr Edwards, are you aware of the contradiction that this poses to companies? On one hand, they want to say to their investors, 'This is a safe project.' If they say to you that it is an R&D project, therefore they are also saying that it is a risky project. I have just been waiting for comments on an article, which you would have read, in this morning's *Sydney Morning Herald*. I do not doubt that you would have read Elizabeth Knight's article this morning on AMC.

Dr Edwards—I did not. I apologise for that.

Mr ALLAN MORRIS—I will just give you a copy of it, then. Dr Edwards, one issue we have been trying to come to terms with, with great difficulty—and it is part of the reason we are all here now—is that it is very difficult to come to terms with investment in new product development. A thing like magnesium is an excellent example of the kind of quandaries. In her article, Elizabeth Knight goes through the investment potential of AMC and she says that their financing bodies put very high penalties on them, which makes it difficult. When we spoke to AMC, they want to give confidence that their technology is absolutely assured. They have done everything they possibly could to test it, but the financing bodies say, 'This is very risky. You're going to put up a half-billion dollar premium for capital risk,' and that is a conundrum that is very difficult to handle. In amongst all that are the R&D board, the ATO and the department. What is your answer?

Dr Edwards—I am not sure of the question, but I will make a comment. The tax concession is a self-assessment program. The company decides themselves, within any project, how much they believe of that project is R&D, and they register for it. They make that assessment knowing what the tax concession program will support.

Mr ALLAN MORRIS—We will take a step back. The fact that you do not know the question is disturbing because I thought your department, in particular, was trying desperately hard to get investment in areas like adding value to magnesium, from \$50 a tonne to \$3,000 a tonne. This has major potential for the country. We have all been racking our brains to try and encourage and find ways and all the rest of it. That is the question, but you keep talking about a tax regime. I am talking about an investment regime of which tax is one component. You keep talking about a tax regime which investment does not actually come into.

I guess that is the issue: how do we ensure that our systems are there to encourage investment in forward looking technologies—in, if you like, new economy technologies or whatever? We argue, in such great detail, about what we call R&D. We end up with this really difficult interpretive matter, and the emotive matter, of saying to the investors, ‘This is very risky. It has to be really risky before you can write it off or before you get tax concessions.’ In other words, you would be mad to invest in it, because the government is going to give it a high risk rating. The conviction with respect to that is monumental and the outcomes are predictable; people do not want to invest in it. Isn’t that what is happening? BHP can do it because it has the money, but, historically, anybody else who has tried to raise the money has had great difficulty. This is the nub of it. What we are talking about now is the nub of why that is so difficult.

If you talk to any technology company—for example, Austeel, Protech, Kingstream, or if you talk to the people with petrochemicals in the north-west—they will give you exactly the same answer: unless you have the money yourself to bankroll it, you are going to have trouble raising it in the Australian capital market.

CHAIR—But all lenders will put a premium on risk.

Mr ALLAN MORRIS—The fact is, Chair, we do not get anywhere. Other countries seem to actually get somewhere; we do not seem to and we always have an excuse for it. I am saying that the aim of policy is to develop investment where you have viable technologies. That is the question, Dr Edwards: What should we put forward to the parliament?

Dr Edwards—I do understand your problem and your question. I feel that, as the deliverer of the industry programs which I represent, which is AusIndustry, I am not in a position to answer that. All I can say is there are a range of programs that do help defray risk in those areas. There are granting programs, and a number of those have gone into the minerals areas to help set up. For example, the R&D Start program has supported a number of minerals projects, in both the iron and magnesium area, and in other areas such as shale oil. There is a range of granting programs where the government has chosen to accept part of the risk and offer up to 50 per cent of project costs as a grant; those programs are also run through the board. There are other programs that do help with the risk, but, as the program deliverer, I will have to leave your broader question to my policy colleagues.

Mr ALLAN MORRIS—So who does answer it?

Ms Jenkins—I can comment in relation to the tax concession policy. My substantive position is to do with R&D tax concession policy which I can offer most information about. The wider question of definition of technical risk is one for the committee to consider. What we look at with the R&D tax concession is the objective of the concession to encourage business R&D. The aim of the program is to support business R&D that would not otherwise be supported through other means such as commercial endeavour. The definition of higher levels of technical risk is very specific to the concession. I imagine a bank would have a much wider definition of technical risk, so there are going to be different kinds of criteria operating and that may present a dilemma for industry. The aim of the concession is to provide Australian taxpayer support to induce additional R&D, not to support what would otherwise be supported through commercial means.

That definition of risk is very specific, and it is set out in the act. I think we have tabled the extract that is relevant. It is going to support activities where there is an uncertainty about obtaining the outcome, where that can only be removed through a program of systematic, investigative, experimental activities. There has certainly got to be a sufficient element of risk, which is an important part of the criteria to obtain the concession. But, as I say, that is confined to the program that is—

Mr ALLAN MORRIS—But can you see the point I am trying to make? One company loses \$800 million effectively of development taxpayers' funds with no scrutiny whatsoever after the event. Another company is trying to attract investment with a new technology, which is no less risky or no more risky probably than the other, and it has to fight this massive case and in doing so undermines its own credibility. That is the contrast of our policies. Clearly this does not make logical sense. Our policies seem to be more about protecting revenue than organising investment and value adding, and it just does not add up. You are asking us to find the answers, and I would have thought the answers are between you. Why one earth aren't we addressing the real question, which is: what policies should we adjust?

I read all the stuff and it is all about protecting what you cannot do and protecting revenue. We just lost \$800 million on one project alone. We lost three or four times your budget in one project, and we are getting all this nitpicking, if you like, stopping people being able to access financial support in policy terms. It does not add up; there has got to be a better answer.

Mr CAMERON THOMPSON—Allan, why don't you ask them to comment—

Mr ALLAN MORRIS—I am trying to. Do you want to look at our papers? Have you read about the stuff they have put back? I will just give you a contrast: can you explain to me why the bargaining power with magnesium tariffs is any less equal than our bargaining power on lamb? We spent a massive amount of resources, energy and media coverage for \$100 million worth of lamb exports into America, yet you say it is not even worth arguing about magnesium tariffs in America. Is that correct? That is what it says in here, that a lack of bargaining power is not worth pursuing, in answer to Mr Lloyd's question about American tariffs on magnesium. Who penned that? Who said it was not worth pursuing? Which officer?

CHAIR—It did go on to say, in fairness, that we are currently in bilateral trade negotiations with the US. It is really a question of tariffs, not so much of the tax concessions.

Mr ALLAN MORRIS—Cameron was asking: what is the answer? I am saying that we should come back to the questions and look at the answers we have got so far to the questions we have asked. One of the questions asked—

CHAIR—A very nice answer would be global free trade, I could tell you that, but that is a Utopia.

Mr ALLAN MORRIS—That is not the question. To one of the questions asked of DISR concerning magnesium tariffs they replied that an assessment of our relative negotiating strength suggests it may be unrealistic to expect the United States to withdraw tariff protection for its domestic magnesium industry on the basis of our request. So we spent a massive amount on lambs, but nothing on magnesium tariffs—with the same country.

Mr Lowndes—I will comment on that. The issue with the lamb arrangements did throw up aspects of consistency with international obligations under the WTO. I am not fully familiar with the details of what protection the Americans actually offered, but it was clearly quite substantial, and we had, in discussions with them, a lever in terms of their protection being inconsistent with international obligations under the WTO rules.

Mr ALLAN MORRIS—You did not negotiate, you had a court case. You put a lot of money into a court case, which you may have lost, but magnesium tariffs do not warrant that.

Mr Lowndes—I am simply noting that, in the case of the magnesium tariffs, the Americans are not in breach of any particular international obligation, in which case it does become a matter of what we can and cannot negotiate with them. In the case of lamb, we had a little more on our side than just trying to persuade.

Mr ALLAN MORRIS—To be honest, this response is really second rate because the WTO and the GATT agreement require countries to downplay their tariffs. I would have expected a comment as to what the requirements under GATT are for America to lower tariffs over what timeframe to what levels on magnesium. What you do say, though, is that we are not big enough to argue. This is a public document and this is what you are saying in public. This is what you are telling the manufacturers: 'We won't fight for your magnesium, but we'll go through hell and high water for lamb.' Jim Lloyd asked that question, and that is the answer you get.

CHAIR—To be fair, we won that case against the Americans, because the Americans on lamb were in breach of the WTO rules.

Mr ALLAN MORRIS—Yes, but only after a massive public investment by the government.

CHAIR—Because it was a case we could win. The US are not in breach of WTO in regard to the tariffs.

Mr ALLAN MORRIS—No. There would be a WTO requirement and expectation for the US to downgrade their tariffs, as there is for us, which our car manufacturers are getting and which our other manufacturers are getting constantly. Why isn't that in here? What is the requirement for America to downgrade tariffs on magnesium? It is not even mentioned. The answer given to us and to the public at large is, 'They're too big to fight,' but they were not too

big to fight on lamb. From the effort that was put into this response, the message to every manufacturer is very clear: the government really is not interested in fighting them on these issues. It is similar with BHP steel and the Americans' restrictions on steel imports. Talk to your cement manufacturers about dumping and see how much concern they feel the government is putting in to protect them. I just think that all the way through here we have been trying to encourage the department to give us some advice and some answers which are compatible, and we basically get reasons why you cannot.

Mr ZAHRA—In relation to the research and development tax concession, do you have a view as to whether or not you could provide an additional concession or an additional incentive in certain parts of rural and regional Australia? What would your view be? Would someone put up their hand and offer to respond to my question? What would the general view be about that? What we are trying to do here in this committee is to look at ways in which we can encourage research and development and add value to Australia's raw materials. I think it would be fair to say that we are particularly keen to see a lot of that value adding take place in rural and regional Australia. What would you think about that?

Ms Jenkins—The current policy for the R&D tax concession as an incentive to induce business R&D is that its very attractiveness is in its broad based, entitlement based, self-assessed nature. To select particular sectors or areas would be counterproductive to that.

Mr ZAHRA—It would be counterproductive?

Ms Jenkins—Yes. Its attractiveness is its general availability at the 125 per cent rate, providing certain criteria are met.

Mr ZAHRA—I am saying that it would still be generally available at the 125 per cent rate, say, but if you were to build something in the Latrobe Valley or another place which does not have as great a need but still has need—Wide Bay, for example, in Queensland—it would receive a concession as well, and maybe an additional concession.

Ms Jenkins—Yes.

Mr ZAHRA—What would the view be about that? It would not affect the 125 per cent rate, but it might provide an additional incentive to try to help tackle some of the high unemployment problems in those districts.

Ms Jenkins—It is certainly an option. What I would draw your attention to is that the government and the relevant agencies have looked very hard at how we can enhance the existing tax concession. Having looked at all the analyses, overseas experience, and at how effective it has been as an incentive to induce business R&D in Australia while maintaining support at the 125 per cent level, there has been a decision to focus on additionality. So those companies that increase their R&D expenditure will get an increased benefit—indeed, at the 175 per cent rate. There has also been a close analysis of those companies who are teetering on tax profit/tax loss. In order to address that need to provide sufficient cash flow to keep those companies buoyant, an R&D rebate has been introduced. It is an approach based on looking at the program as a broad based entitlement program and recognising that R&D performance, that

is inducing R&D across the board, has not been as good as we would like for the country. We really need to look at getting that extra effort as well as supporting routine R&D, if you like.

Mr ZAHRA—What we are keen to see is not so much that jobs get created in rural and regional Australia, although that is important in itself. I do not think that rural and regional Australia is going to have much of a future if its employment base is increasingly made up of just footloose industries like call centres, for example, which can be based pretty much anywhere. In my view, if we want to strategically set these regions up as viable operations, we need to try and get more of the research and development, the science and technology, and innovation out there. What I am particularly keen to pursue is whether or not we can use the taxation system, support from the department and other levers to try and achieve that.

Earlier on, Mr Tune, you made some comments in relation to the administration of zonal taxation. How would it be if we tried to use that zonal taxation idea, instead of it just being an enterprise zone? I do not know whether it is necessarily a good idea just to try and provide incentives for general enterprise. I think research, science, technology and innovation are the sorts of things which governments should be more directly involved in trying to encourage and get development of. Just to use a simple example: in my district, unemployment is pretty easily identified with one municipality, which obviously has its own boundary and is in quite a discrete area. How would it be if you increased the research and development tax concession from, say, 125 to 150 just in the municipality of the city of La Trobe? How hard would that be? You talked about one side of the street and the other side of the street; municipal boundaries are at least a little different from that. What would your view be about that?

Mr Tune—I think the difficulties are basically the same as the ones I outlined earlier. As I understand, the proposition or the option would be that you take the existing R&D tax concession arrangements which, as a colleague from Industry, Science and Resources just explained, already has a number of tiers to it. You have got the 125 general concession, and then you have the 175 loading for additional R&D. This would add an extra tier to that for the electorate or the local government area of La Trobe. So all those issues surrounding whether that would actually add investment to the country as a whole, and difficulties for people who are—

Mr ZAHRA—I am sorry to interrupt. It is not so much the country as a whole; it is more trying to use the idea of zonal taxation and the rebate as an instrument to try and achieve a public good, which is a reduction of unemployment in those areas of particularly high unemployment.

Mr Tune—The issues of concern that I raised earlier would apply to this particular proposal. It is a variation on the theme of using a particular tax concession, there being a regional dimension to it. I am not saying it could not be done, but there are issues that would need to be thought about pretty carefully if anyone were going to put that forward. I have not seen any proposals of that type in the past.

Ms Jenkins—Can I add a couple of comments there? Just to reinforce the rationale for the current approach, it is of a non-discriminatory nature. It is not singling out particular areas, and I think that is a first principle that needs to be considered. The other thing that you have to look at is the return for what you are putting out. What is the rationale for increasing it to 150 per se?

You have to weigh up the cost of doing that versus the benefit. As I say, the kinds of analysis that are most rigorous in this area point to incremental schemes as being more likely to induce that additional effort, rather than simply increase the rate of the concession.

Mr ZAHRA—I would like to point out to you what our experience has been—and I am sure the experience has been the same in other areas like the Latrobe Valley. We have fantastic growth rates in our districts and it does not matter. Unemployment goes down to 6½ per cent nationally and it makes no difference to our districts. Prosperity is everywhere but not where we live. So what I am saying is that it might take a special effort. My argument is that I do not think it is in the public interest for there to be persistently high levels of unemployment in certain and very easily geographically defined districts. So I do not accept the sort of welfarist mentality that the way that you help these people is to try and do more cuddly welfare stuff over there. I think it really needs to be based around research, development, science and technology. This is the stuff that will drive development in these communities and not just provide a sort of bandaid there for a year or two, but will really set up those communities to be vibrant and to attract new, highly skilled people who will drive economic development in those areas.

Mr Tune, I would like to come back to you again. I cannot understand exactly why it is hard to do something like that. Surely it is not too difficult. Maybe the ATO have got responsibility for the implementation of it.

Mr Miller—I was just going to mention that. The ATO would have some concerns. Whenever you draw a line and put a concession on one side of the line and not on the other, there is going to be a natural tendency to try and blur that line or to set up avoidance opportunities. For example, if you just move the rate in one area from 125 per cent to 150 per cent, there is a possibility—and there are probably ways of stopping this, but it starts to get complicated—that someone could set up a company inside the zone and then contract for R&D outside the zone. So basically, they will funnel everything through those companies that are sitting inside the zone so that they can get the higher percentage. Obviously, we could do various anti-avoidance measures and things that layer over the top, but it just gets more—

Mr ZAHRA—We have got that situation right now, haven't we, with so many parts of the taxation system where people exploit loopholes and do all manner of things—some very professional people: barristers, merchant bankers, et cetera? So I think those are problems which are generally relevant to the entire taxation system. We do have zonal taxation as it applies to the diesel fuel rebate, don't we?

Mr Miller—I am not sure.

CHAIR—No, it is use. It is qualifying use no matter where you are and it is only a selected group of industries.

Ms ROXON—I have a question on that same point, or were you going to ask one?

Mr CADMAN—Has any consideration been given to the micro-economic aspect of the production of e-business efficiency within the Australian exporting industries and whether or not there are tax concessions, apart from the general write-off of running expenses for the

development, say, of web sites, e-commerce and interactive transactions. Are there any concessions or is it just a normal write-off?

Mr Tune—There are no particular concessions that we are aware of.

Mr CADMAN—So there are no depreciation rates for, say, a big, comprehensive web site which may have factors that change over a period and will want constant maintenance?

Mr Tune—That is an expense—

Mr CADMAN—Is there a depreciation factor there?

Mr Antioch—Web sites and web development costs would just be part of software development. That gets a special write-off. So it would qualify in that way.

Mr CADMAN—Would you check that? I am told, and I do not know whether this is right, that web site developments are regarded as capital costs rather than running costs.

Mr Antioch—I am not aware of the specifics there. There might be some issue that—

Mr CADMAN—It would depend on whether it was in-house or out-of-house, I suppose.

Mr Antioch—I believe there are those sorts of boundary line issues. But generally, you would get some sort of deduction, I think.

Mr Tune—We will check that for you.

Mr CADMAN—Thank you. I wonder, from an industry perspective, whether any particular examination has been made of the competence of Australian exporters in this regard.

Mr Lowndes—Sorry, what do you mean?

Mr CADMAN—How competent we are: recent reports indicated that we were about 30 per cent users of e-commerce and e-business and that, particularly if we look at the distances we need to handle, that is the area Australians should become very proficient in.

Mr Lowndes—Generally, the sort of industry development side of e-commerce is done in the Department of Communications, Information Technology and the Arts and not in ISR. In terms of the general point, Australia is quite proficient in using e-commerce. There have been a lot of studies of relative use rates of ICT, and Australia is right near the top in terms of users. We are not big producers, but we are major users of ICT.

Mr CADMAN—It is just that I have noticed a continual theme through our exporters that technology and international competitiveness are key factors mentioned by them all.

Mr Lowndes—Absolutely. Many of our exporters, particularly in the mining industry, are world class in using information technology and e-commerce at all stages of production.

Mr CADMAN—What about the wine industry and the dairy industry? I do not know that the committee has investigated the competence of those industries in e-business, have we?

CHAIR—No, we have not.

Mr CADMAN—If you could examine any information you may have that could assist the committee, I would appreciate that.

Mr Lowndes—Yes.

Ms ROXON—I want to come back to the comments that Ms Jenkins was making about the R&D tax concession and its attractiveness; being that it was broadly based and non-discriminatory, which I query. I think ‘non-discriminatory’ is a term that we actually misuse greatly. The way I understand the additional rate working is that it really provides an extra incentive to companies that currently are not undertaking any research and development. Companies in my electorate that have come to talk to me about it have said, ‘We already invest a high percentage of our income in research and development, and we have to double that’—or whatever the figures might be—‘to be able to get the extra tax benefit.’ Whereas a company that is doing none only has to increase its investment by what is, in their view, a small amount to be able to access the money. Wouldn’t a properly non-discriminatory process actually say, ‘Any company that spends X per cent of its income or profit’—or however you work it out—‘is entitled to a concession at this rate; anyone who spends double that is entitled to the concession at another rate’? That is my first question.

Surely it is a matter of choice where those lines are and where we choose to discriminate. I can understand that it creates problems for the ATO, but I think it creates problems for the ATO having the different rates anyway, so it is more a policy decision than a practical one. I just wanted to check whether that was, in fact, right: that it is non-discriminatory. It appears to me that companies that are already investing heavily in research and development do not get the rewards for that. We reward the companies that are not already technologically advanced by encouraging them to spend more money on research and development, but we do not have a policy that says we will reward the ones who are already good and help them invest more. I would like you to comment on that.

The second thing, and I do not know which person would be able to comment on it, is: do we have any feedback yet about the sorts of applications or the numbers of companies that are actually seeking the additional tax concession rates? Are people saying, ‘We are actually spending more on our research and development and we want to claim the additional concession’? I would be interested in any feedback you—and I do not mind whether it is the tax office or anyone else—might have about whether that incentive has already started to have some impact or not.

Ms Jenkins—I can answer that second question first. In regard to the announcements that occurred on 29 January through the Backing Australia’s Ability innovation statement, they included the announcements regarding the new tax concession. In terms of the effective date, the changes to the definition of R&D and plant would be in effect from 29 January for any new activities from that time subject to the passage of legislation. The new measures—that is, the

R&D tax rebate and the 175 premium—commence from 1 July, subject to the passage of legislation.

Ms ROXON—So we would not have seen anything on those yet?

Ms Jenkins—That is right. The ATO and ISR are embarking on a series of information seminars, which commence tomorrow, to explain the new initiatives and things like transitional arrangements and time frames for registrations. But the first time that they could claim the 175 and the rebate would be July 2002. That is predicated on the basis that the legislation goes through.

Ms ROXON—I am not sure whether you or someone else would be able to comment on the first point, about whether we are effectively giving more of an incentive to companies that have not spent very much on research and development.

Ms Jenkins—Just before I answer that, to clarify the criteria for the 175 per cent premium R&D tax concession, companies who wish to claim must have a three-year claim history. I think it is just worth noting that. That is to ensure that there is a commitment to R&D at that basic level and that we are not rewarding companies for sporadic effort: it is for that continued longer term effort. The 175 percentage rate is then paid on the additional R&D expenditure over the average performed over the last three years. So it is designed to be fair across the board. The analysis that has been done indicates that it is about as non-discriminatory as you could possibly make it. Companies are going to be at different growth phases, and the economic cycles and the vagaries of the environment will impact; but, in terms of encouraging that longer term commitment and encouraging additional R&D, that is the philosophy.

Ms ROXON—I guess I could put it in a very simple way. I am using these figures as an example; they are not based on anything. If you have a company that for the last five years has spent 10 per cent of its profit investing in research and development and it increases its investment to 11 per cent, will it receive the same beneficial treatment as a company that has invested 1.5 per cent of its profit in research and development for the last five years and then doubles or triples that to three per cent or 4.5 per cent—still less than half what this other company is doing? Won't the second company actually receive the higher concession rate?

Mr Tune—I would like to make a comment that might clarify it. There has been a change in the way that the 175 per cent concession will operate. I wonder whether the comments you are receiving from companies in your electorate are based on the previous announcement by the government, which has been superseded by an announcement that was made straight after the budget and is reflected in the bill that is currently before the parliament. The original approach, as announced in *Backing Australia's Ability*, was that there was going to be an increase in R&D expenditure as a proportion of a company's turnover—not its profit, but its turnover. That could lead to different effects. In the consultations that were undertaken about the measures, leading up to the development of the legislation, there was a lot of input from companies raising the sorts of points that you have raised. As a result of that, the government has changed it so that it is now straight dollars of expenditure. So the situation that you were putting would not arise. If a company were spending 10 per cent of its turnover on R&D and increased that to 11 per cent, or indeed if a company spent more dollars on R&D but its turnover was increasing at a faster

rate, it would still get the 175 per cent concession as long as it was an increase in R&D expenditure.

Ms ROXON—That answers my question. Those concerns were raised quite a while ago, so it is possible that that was what they were based on.

Mr ALLAN MORRIS—There are two strands that I would like to clarify. If BHP invests in a project and blows \$1.6 billion it can write half that off as tax, so the actual company loses 50 per cent of its extra investment, its risk investment, if you like, and still has the plant. But say a new company like AMC is formed—and I am talking hypothetically here because I do not know AMC very well at all—and goes to the market and raises capital. If it went the same way it would not be able to write off its capital losses because it is not making a profit and, equally, the shareholders could not. The system seems to suit only a big company that can write off, against its profits, that loss and not a start-up company that has no profits against which to write off a loss. Therefore, shareholders would be smarter to invest in BHP than in a new company because, if BHP made a mistake or something went wrong, at least their investment is protected, to some degree, by taxation systems. Is that a fair interpretation of it?

Mr Cooper—That is right.

Mr ALLAN MORRIS—Wouldn't that seem to be a massive disincentive to people to invest? I will read one paragraph from that article this morning:

And the bankers to this project have insisted on so many buffers as to leave equity investors with the impression that this is a particularly risky play.

Here we are, us parliamentarians and you departmental people, trying to get people to invest in new technologies and things of this nature, but we are actually saying now publicly—out loud and on the record—that our system discourages that kind of investment in new companies and gives a substantially better result to people investing in existing companies, and perhaps even more so for companies offshore—that may be even stronger. That is not what we intended; that is not what we thought we were doing. We would not do that consciously, would we? Would we consciously choose to prefer an existing company to a new company? Would that be a policy or is that just unintended?

Mr Tune—If I could make a brief comment. There might be issues about start-up assistance that is provided by the Department of Industry, Science and Resources that you might want to add to this. I would have thought that, in the case of an existing company, just by its very nature and the fact that it exists and has diverse operations, the tax law is set up so that losses can be offset against gains. That is an inherent part of the tax system which, judged on its own, seems a perfectly reasonable thing to do. To juxtapose that against the operation of the new one is, I think, a touch misleading. I take your point though that governments have for many decades been trying to assist start ups, and I think that is a valid point. But to use the other one as the counterpoint, I am not sure I would accept that.

Mr ALLAN MORRIS—Except that it makes plain why we do not get very far: because we only keep going with existing companies. Whether it be IT or almost any new technology, the only ones who seem to do it are the multinationals or the existing companies. We never seem to

get very far in those fields. Who is going to do magnesium? Unless BHP do it no-one will because, as a shareholder, why would you put equity into a company where you are totally exposed and where you cannot write it off? Wouldn't it make as much sense to have a class of company or a class of shares where you would allow the shareholder a level playing field so that the shareholder in that company has the same tax back-up as has a shareholder in BHP? Because that is what we are doing; we are actually saying to the shareholder in BHP, 'We'll protect you, but we won't protect him.' Is that correct?

Mr Tune—I am not sure what the point is. The shareholder in the new company—

Mr ALLAN MORRIS—The point is pretty simple. If you want to get magnesium, the only chance you have is through an existing company, because who would invest in a new company when they are 100 per cent exposed? When they are an existing company they are only 50 per cent exposed. We are basically saying to investors, 'Don't invest in AMC.' That is what the article highlights. In other words, it is government policy that is doing that. It may well be a longstanding one; do not take it wrong. To me, this inquiry is about investment more than anything else. When I look back over the years that I have been involved, what I come up with every time is that it is impossible to get investment, particularly in new technology, in new products and in new areas of value adding. We got wine because wine already existed, but if we were starting wine from scratch we would not have got it. The existing wine companies were picked up by existing companies, not by new ones to any large degree. What would you do to try to correct that consequence?

Dr Edwards—There is a range of other industry assistance programs targeted very much at the early stage start-up company or the smaller company. I understand the point you are making, but things like the Start program are definitely there for smaller companies. It provides 50 per cent—

Mr ALLAN MORRIS—We are talking about \$1.2 or \$1.5 billion—this is not a small company. Magnesium is big and that is why we need it. What program does that?

Dr Edwards—Sure, but one of the points you are making is: what assistance is there for smaller and start-up companies? There is a range of programs specifically targeted to those small end start-up companies. There are granting programs like Start, there are investor ready programs like COMET and there are programs through which the government is trying to stimulate the venture capital industry to invest in higher tech start-up companies like the IIF (Innovation Investment Fund) program. Certainly tax concessions are available for companies with an asset base of less than \$50 million, for which investment is via pooled development funds. So there is a range of programs that we market as AusIndustry that do help with that earlier stage or start-up of the company. In some cases we help them quite considerably: in the Start program, for example, with 50 per cent of the project costs. In COMET, for a very early stage start-up company, to get the business investor ready we will put in up to 80 per cent. So there is a range of companies there. I accept that they may not meet the gap that you are talking about, but there is at least a range of programs now.

Mr Lowndes—I would like to add to what Dr Edwards said. We do provide assistance in other ways, not just through these AusIndustry Start programs. The AMC project has received assistance, with additional money provided through the CSIRO to assist in the

commercialisation of the venture. So the government has actually been involved with the AMC. There is another example of our being involved, through the Strategic Investment Coordination process that I talked about earlier, with a technologically driven project relating to gas-to-liquids technology.

Mr ALLAN MORRIS—I am very aware—and Mr Cadman and the chairman would be aware—that the previous government put \$25 million into that particular project through CSIRO and through the AIDC. What I am trying to raise is that this is actually a share market capital thing. I am mindful of the programs that Dr Edwards spoke about, but they are all pretty small beer, and they are not about the investors we are talking about. Is it reasonable or does it become possible to have a class of shares or a type of project about which the government would say, ‘Because of its nature, because it is a new technology and because of the risk involved, rather than differentiate between an existing company and a new company, given the dimensions of it, we would make any capital losses on those shares able to be written off by the investor’? If the company cannot write it off because of a lack of profits, it can be downstreamed to the investor, because that would then put AMC and BHP on an equal footing for attracting investment into a thing like HBI or Austeel or Protech. A number of companies looking at investing in new steel technologies have exactly the same problem as this company. If you talk to any of them, they will tell you the same story: once you start talking about large investment in anything of this nature, people will just run for their lives. Unless you are BHP or Rio Tinto you really cannot do it, and that is because of the discrimination in the share write-off system. Would it be possible, say, to have a class of shares for which you could transfer the capital loss to the shareholder in certain cases because of the national interest of the project involved?

Mr Antioch—There is another way, of course. Joint ventures are often undertaken when greenfields technologies are to be exploited: a new company teams up with, typically, an existing company to share the risk and also to share the benefits that come out of exploiting that new technology.

Mr ALLAN MORRIS—That is often the case when the overseas company owns it—the Australian company loses. That is why we invested in AMC—do you remember, colleagues?—because the American technology would not be allowed to be used here. You could not use the overseas technology here.

Mr Antioch—But it need not always be an overseas partner; it can be a local partner. That is an essential feature of the tax law.

Mr ALLAN MORRIS—At the moment, if you go around Australia and look at Austeel, Protech and Ausmelt, we are talking about \$3 billion, \$4 billion or \$5 billion worth of investment per project. They are all going to be start-up companies with no existing losses to write it off to—and they are all having exactly the same trouble as AMC. Don’t you think we would start to learn a way of doing it? We let BHP write off \$800 million of taxpayers’ money with no questions asked. Why do we not allow that for others? Why should we judge these people and say, ‘You are not to have that. BHP can have it but you cannot.’ Is that fair? Is that good policy? Is that a good national development strategy?

Mr Antioch—But, of course, BHP cannot stream its losses to its shareholders; it is trapped in the company.

Mr ALLAN MORRIS—But shareholders know that, if BHP makes a cock-up, only half is going to be at their expense. AMC shareholders know that, if they make a cock-up, they lose the lot. That is the difference. Why would you do that?

CHAIR—Yes, but it was reflected in the share value, which absolutely collapsed.

Mr ALLAN MORRIS—Sure, there is some loss, but they do not lose the whole lot, whereas this company would lose—

CHAIR—If shares keep going down, it will collapse. I would think that the shareholders of HIH don't reckon that their shares are worth anything now.

Mr ALLAN MORRIS—But the fact is that the taxpayers put \$800 million into one project and nothing into another of equal value. That is the question. Why would we do it that way? Why would we so discriminate? We are not supposed to pick winners. If we picked the winners, it would be BHP, but we would not pick AMC.

CHAIR—We did not pick a winner. They supplied—

Mr ALLAN MORRIS—The system picks BHP and gives it a concession because they have an existing profit stream. It does not give the same concession to somebody else but it costs the taxpayers money just the same. It is the taxpayers who backed up BHP with its capacity to write off its losses. The taxpayer does not back up—

CHAIR—This is a scheme of deductions, not a scheme of grants.

Mr ALLAN MORRIS—I am saying this is all about protecting revenue. On the one hand we watch revenue bleed by \$800 million and do not say a word. Nobody is saying, 'This is something that is not right.' But another company has said to the government, 'We cannot raise money because we are totally liable,' and we say 'bad luck'. It just does not make any logical sense. As a country trying to add value to its resources, the policy is totally counterproductive.

CHAIR—We have to start to wind this up.

Mr ALLAN MORRIS—There is a second stream I want to test, but I will wait for Cameron.

Mr CAMERON THOMPSON—I wanted to get off the R&D stuff and talk more generally about value adding. There has been a series of projects—I am sorry Christian is not still here because I thought this would interest him—and a range of recent packages through which we have provided assistance, such as the dairy RAP scheme. Projects are being backed through the dairy regional assistance program and a lot of them involve value adding. The pork industry package, which was so successful after the problems that the pork industry had in 1998, was all about value adding, giving them an export opportunity and those sorts of things. We have had the forestry structural adjustment grants announced in the last week that all involve value

adding. I heard what you said before about putting boundaries on a map and talking about enterprise zones, which is what the ICA apparently was proposing. Instead of that, why don't we have a more generalised look at industries before they get right down in a hole like pork was or like dairy is? Why isn't there a more general approach made to finding these kinds of value added opportunities and dealing with them up front rather than these sorts of bushfire contingencies that we come up with after the fact? Does anyone want to comment on that? Have there been any examples?

Mr Tune—I do not know the details but I think there are both at the moment. That is my understanding of the situation, without knowing the detail. There are issues around the structural adjustment for particular industries that are in decline and so forth, but there is also a lot of work being done on emerging technologies and new industries that are emerging from those. It is not just a one-way street; there are things happening on both sides. With biotechnology, for example, there is work being done within the ISR portfolio and ICT in the communications portfolio—

Mr CAMERON THOMPSON—I have gone right away from R&D and those sorts of areas; I am talking about value adding to existing industries and simple things—

Mr ALLAN MORRIS—These are the ad hoc programs. They cost money.

Mr CAMERON THOMPSON—They provided an export capacity to pork abattoirs and therefore assisted with the value of the pork product coming out the end. There is one example in my electorate where, through forestry structural assistance, they are taking hardwood products and turning them into I-beams, and the government gives them \$666,000. They get that additional money, therefore they get the added value and the community gets the benefit. But we have gone through a series of specific projects where there is lots of money going into industries in order to pick them up when they are in crisis. What I am asking you is: has there been any effort made to look at a more generalised program to address these things and add value to worthy industries at times when they may not necessarily already be in crisis?

Mr Tune—My answer was that I understood there were things going on but I was not aware of the detail of them. Perhaps others could comment on some of the detail.

Mr Lowndes—In a sense, most of the basic active industry policy interventions tend to be generic in that you have a range of support for research and development, there are export market development grants, there are programs to facilitate biotech, et cetera. We do have some particular structural packages of the type that you pointed out but, generally speaking, at the Commonwealth level we do not target particular industries. The approach is that we try to establish what we believe is a competitive business environment generally; and provide support for what we believe falls into the category of drivers of growth, such as R&D, support through training, export market developments, development grants and so forth. Having set that basic climate, it then becomes in a sense a market decision as to where resources are allocated, which industries grow and so forth. There are a number of programs through which, if industries do downsize or experience difficulties, the government often intervenes to try to ease any downsizing and to try to ensure that those parts of industries that can remain competitive do so. Those are the sorts of packages you are talking about. But the general philosophy behind industry policy has the markets allocating resources to particular projects as distinct from the

government deciding that this is a sector that we are going to identify as one that is going to grow.

Mr CAMERON THOMPSON—I understand what you are saying. I am just picking up more or less on what Christian said before. Part of the purpose of this inquiry is trying to figure out ways that we can assist our value adding in Australian industries. We have heard already from Mr Tune that putting a line on a map is very difficult. What I am saying is looking at the difficulties of individual industries and trying to encourage them to add value through a bit of judicious pump priming might be appropriate.

Dr Rymer—It is worth commenting that, while there is not any specific program, there is the action agenda process that does work. It brings together industry and government to look at the impediments that might exist to the development of an industry and at what actions government and industry can take jointly to help overcome those impediments. For example, at the moment there is a light metals action agenda which is trying to identify what impediments exist to the further development of both the upstream and the downstream light metals industry in Australia. At the moment there is a strategic leaders group led by industry which has been developing papers and is at the stage of formulating a set of recommendations and proposals looking at what actions the industry and government might take to help the industry develop further and faster.

Mr CAMERON THOMPSON—Light metals is something that we have already heard is unique, has this massive potential, is new and all those sorts of things. But is that action agenda open and available to other more traditional existing industries that, for example, might see a problem with the way their growth is occurring? Is there an opportunity for them to go along and raise issues?

Mr Lowndes—The way the process works is that particular industry sectors are identified to have an action agenda. There are 23, I think, at the moment. They are quite extensive, although obviously they do not cover every sector. It is a process that is sector specific. There is a light metals industry action agenda. I think there has been one on wood products. There has been one on petroleum refining. They are looked at.

Mr CAMERON THOMPSON—Could you give us a list of those?

Mr Lowndes—We certainly can.

Mr CAMERON THOMPSON—Thank you.

Mr ALLAN MORRIS—You are all aware of EFIC, which is the capacity to insure an Australian contractor against an overseas country collapsing or contract collapsing, in simplistic terms. I have been racking my brains to think of ways in which we might be able to encourage investment in risk projects, which the capital market puts an extra cost on before it even starts, as it does with AMC's project. I think the extra cost they are talking about there is \$400 million or \$500 million in extra capital before they start—just in case—which becomes a massive burden. The government runs a system to allow companies to insure against almost exactly the same thing with the collapse of a country or a contract in another country. We do it for offshore people. How hard would it be to have a similar thing for high risk value added projects of a

large nature; that is, to offer some kind of insurance system for the capital risk component so that we could actually try to contain the capital raising cost? The capital costs, of course, feed back into the costs of the product and often make it uncompetitive, apart from the risk. The hard part is raising capital. Who has got the freedom to talk about that? It is with freedom that we want to hear ideas, not necessarily just departmental dogma.

Mr Tune—I do not think I am in a position, from Treasury's point of view, to comment at this point in time. We would certainly be prepared to have a look at it and send something back to the committee.

Mr ALLAN MORRIS—But the EFIC thing is a risk matter for the government, isn't it?

Mr Tune—Yes, I agree.

Mr ALLAN MORRIS—The government is exposed in terms of the risk of a company in, say, Bangladesh falling over and not completing a ship building contract, for example.

Mr Tune—Or wheat sales or things like that. I understand the option or the proposal you are putting; I am just not in a position where I could comment on the spot.

Mr ALLAN MORRIS—We put that forward on a national interest basis, don't we, because we are encouraged as a country in the aid program and therefore we do not want companies to be destroyed. Much of the ingredients in national interest and credibility terms are the same. But, if you had to raise an extra \$400 million or \$500 million in an AMC project on, say, magnesium simply because the bankers said this was risky, if AMC could take out an EFIC type insurance policy on that capital risk—which would be repayable and would have all the other provisions you could make to it—it might make the capital raising easier and not as expensive.

Mr Tune—I would be happy to take that on notice, give consideration to it and get back to you.

Mr ALLAN MORRIS—We have canvassed that only briefly. As I said, I have been racking my brains because everybody I talk to in value adding in a major way comes up with this capital problem. If the tax system works against them and the departments work against them, they do mickey mouse little projects which are really tiny. You do not have a hope in hell for anything big and decent. Unless you are Woodside, Rio Tinto or BHP, then forget about it. There has got to be an answer because of the potential we have in value adding. We talk about new economies and so on. We do not have a hope in hell other than to be mickey mouse players, because our systems mitigate against people investing substantially unless they are multinationals or existing companies. The existing companies do not want the new technologies; they are making their money on the old ones. They are still earning off their previous investment. If Mr Tune can respond to that, that would be great. We trust they understand our frustration. We trust they share our frustration with a system which does not let them achieve either.

CHAIR—I would like to thank the witnesses for their attendance today. You will be sent a copy of *Hansard* which you can check for details of grammar and fact.

Resolved (on motion by **Mr Thompson**):

That this committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at public hearing this day.

Committee adjourned at 1.10 p.m.