



Australian Dairy Industry Council Inc.

Submission
to the
Productivity Commission Inquiry
into
Australian Government Research and Development Corporations Model

by the
Australian Dairy Industry Council

7 July 2010

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To the Productivity Commission,

Dairy Industry Response to the Rural Research and Development Corporations PC Issues Paper

On behalf of the Australian Dairy Industry Council (ADIC) I welcome this opportunity to participate in the Productivity Commission Inquiry into the Australian Government Research and Development Corporations' Model (the Review).

As the national policy and advocacy body of the Australian dairy industry, ADIC represents the interests of Australian dairy farm families and businesses, dairy manufacturers and traders across all states and territories. The ADIC has since the mid '80s striven to ensure that dairy RD&E has remained focused, affordable, supported and relevant.

This submission is written in support of Dairy Australia, a Rural Research and Development Corporation, and thus a subject of the PC Review. Dairy Australia is an industry owned service body investing in Research, Development and Extension (RD&E) and data acquisition and analysis on behalf of the whole of dairy Australia's dairy industry value chain. DA as an RDC is primarily funded through levy funds from farmer stakeholders and Federal Government 1:1 matching funding.

It is the contention of the ADIC that the current RDC funding model:

- Delivers significant public benefits in both the short and longer term even though being primarily directed at delivering benefits for the respective sponsoring industries,
- Should not be compared directly with other industries or taxation models given the extraordinary circumstances of agriculture, farming businesses, and its susceptibility to extrinsic factors such as drought and climate change. Agricultural research and R&D cannot be made subject to controlled environment experimentation that can be conducted in a laboratory,
- Does not preclude collaboration. For example the Australian Dairy industry collaborates extensively with the dairy industries of other countries, and
- Delivers significant benefits directly and indirectly to the wider community even though each RDC is operating with a vested interest in advancing and promoting the productivity and profitability of the respective industry.



Australian Dairy Industry Council Inc.

When examining the community benefits derived from investment in the rural RDC model from a dairy industry perspective, it is pertinent to note that:

- Dairy is one of Australia's leading rural industries in terms of adding value through further downstream processing. Much of this processing occurs close to farming areas, thereby generating significant economic activity and employment in country regions. ABARE estimates this regional economic multiplier effect to be in the order of 2.5 from the dairy industry.¹
- Dairy is the largest single export from the Port of Melbourne, Australia's largest container port. While Australia contributes just 2 percent of world milk production, it accounts for around 10 percent of world dairy trade, ranking third behind New Zealand and the European Union.²
- Environmental and resources stewardship is intrinsic to the dairy production system.
- Dairy farms are predominantly small, family businesses that are vital to the sustainability of regions.
- The integration between farm and manufacturing is unique to the dairy industry and consequently farmers are comfortable investing throughout the supply chain where they can see this will ultimately result in benefits to farmers.
- As an exporter of nutritious dairy products to over 100 countries and with capacity to grow, the Australian dairy industry has an important role to play in meeting food security and improved nutrition needs on a global basis.

The ADIC contends that the current model works well for both government and rural industries, and has enabled the dairy industry to achieve significant leverage and support of its R&D investment through external agencies. However, ADIC holds grave concerns that changes to the model will disenfranchise this support and even alienate industry stakeholders. For example, under the current model dairy farmers regularly vote on whether to keep paying a levy, and do so with the knowledge that the funds raised will provide benefits to their own businesses and to the broader industry. A framework which prioritises the needs of these levy-payers as secondary to broader community benefits or dissipates their investments amongst other agricultural commodities would need to be accompanied by a strong case for why individual levy-paying farmers should continue to invest at the same level.

In addition, the current model and ancillary government programs and policies recognise, and go some way to compensate agricultural industry for, the market failure that occurs with RD&E in regional Australia as it applies to issues such as natural resource management, climate risk and small business. In this context, the ADIC would argue strongly that the current RDC model is the most effective vehicle for the Federal Government to direct and facilitate farmers to invest prudently and profitably on the behalf of their industries and indirectly for the wider community. This position has previously been acknowledged by the Productivity Commission in its

¹ <http://www.dairyaustralia.com.au/Our-Dairy-Industry/The-Australian-Dairy-Industry.aspx>

² http://new.dpi.vic.gov.au/data/assets/pdf_file/0007/33298/DPI-services-to-dairy-farmers-report_WEB.pdf, page 9



Australian Dairy Industry Council Inc.

recommendation that, “significant public funding be provided for agricultural research, development and extension. There are sound rationales for governments to assist farmers to build their capacity through funding research, development and extension.”³

We would welcome the opportunity to discuss this submission with you in person.

Yours sincerely,

Wesley Judd

Chairman

³ Government Drought Support Inquiry Report, Productivity Commission, 12 May 2009, P. 284.

Contents

1	Introduction	6
2	Key Representative Bodies in Dairy Industry Value Chain	6
2.1	The Australian Dairy Industry Council (ADIC)	7
2.2	Australian Dairy Farmers Limited (ADF).....	7
2.3	Australian Dairy Products Federation (ADPF)	7
3	Investment in dairy R&D	7
4	Wider Community Benefits.....	10
5	Comparison with other industry R&D incentive schemes	10
6	Scope for duplication of administration and service provision in current model	12
7	Consultation and Contestability.....	13
8	Conclusion.....	14

1 Introduction

The Australian Dairy Industry Council (ADIC) welcomes the opportunity to provide a submission to the Productivity Commission on Rural Research and Development Corporations Model. The Australian dairy industry is Australia's third largest rural industry, with a farmgate value of production of \$4 billion in 2008/09 and directly employing 40,000 people. The through-chain value of dairy is significantly higher, as the industry directly and indirectly employs approximately 100,000 people and produces dairy products valued at \$9 billion a year. The industry exports approximately 50% of total milk production and will continue to be a significant contributor to the national economy⁴. In a time of global financial and anticipated global food crisis, the importance of continued, targeted R&D in dairy cannot be underestimated. Continuous improvement in farm productivity is a key objective of dairy industry RD&E and ADIC sees this activity as vital to maintain competitiveness and to enable the continuing production of high quality, nutritious food for Australian and world markets.

Dairy is one of Australia's leading rural industries in terms of adding value through further downstream processing. Much of this processing occurs close to farming areas, thereby generating significant economic activity and employment in country regions. ABARE estimates this regional economic multiplier effect to be in the order of 2.5 from the dairy industry⁵.

The submission is written from the perspective of the ADIC which clearly delineates its policy and advocacy role from the RD&E investment and management role of Dairy Australia. This submission should be read in conjunction with its covering letter.

2 Key Representative Bodies in Dairy Industry Value Chain

A list of the key representative bodies of the Australian dairy industry is presented here to clearly differentiate their composition, relative responsibilities, and activities. This then serves as the authority by which ADIC makes this submission with regard to DA and how it is perceived by the industry.

⁴ www.dairyaustralia.com.au

⁵ www.dairyaustralia.com.au

2.1 The Australian Dairy Industry Council (ADIC)

ADIC is the peak industry organisation where dairy farmers and dairy companies come together to agree whole of industry policy. ADIC comprises Australian Dairy Farmers Limited and the Australian Dairy Products Federation Inc. which are the peak policy bodies for Australian dairy farmers and dairy companies, respectively. Policy agreed through the ADIC is used to represent and advocate the interests of all sectors of the dairy industry to state, national and international Governments and organisations.

2.2 Australian Dairy Farmers Limited (ADF)

ADF is the peak industry body of Australia's dairy farmers constituted from the six state dairy farmer organisations (NSW Farmers' Association Dairy Committee, Queensland Dairyfarmers Organisation, United Dairyfarmers of Victoria, Tasmanian Farmers & Graziers Association Dairy Council, South Australian Dairyfarmers' Association and Western Australian Farmers Federation Dairy Section). ADF's primary purpose is to represent the interests of dairy farming businesses and families, and is the long established voice of Australian dairy farmers. As a member of the National Farmers' Federation (NFF), ADF has contributed to and supports the main contentions of the NFF submission to this review.

2.3 Australian Dairy Products Federation (ADPF)

The ADPF is the peak policy body for commercial/non-farm members of the dairy industry. Its role is to develop policy and represent members on issues of collective interest. Membership is open to entities operating in Australia that are engaged in the manufacture, marketing or trading of dairy products and/or dairy related products. Currently there are 26 Member organisations that account for over 90% of the milk collected and processed in Australia.

The ADPF's objectives are to:

- provide input into policy formulation that impacts on profitability, viability and sustainability of members' dairy operations and the dairy industry,
- develop strategies that address key issues confronting members and the dairy industry,
- represent and promote the dairy industry at all levels, both nationally and internationally, and
- work with governments and related industries and other stakeholders to achieve mutually beneficial outcomes for the dairy industry.

3 Investment in dairy R&D

The role of Dairy Australia is to help the dairy industry to be collaborative, innovative, sustainable and competitive against both international dairy industries and substitute products. Dairy Australia undertakes industry-level activities where a collective approach delivers more effective and valuable

commercial and social outcomes than action taken by individual members. This collective approach also generates synergies and savings through cost economies and the effective capture and sharing of knowledge. At the request of the industry, DA maintains a presence in every dairy region. These Regional Development Programs (RDPs) facilitate the involvement of local dairy farmers in the delivery and execution of DA's RD&E programs. ADF and ADPF through the auspices of the ADIC provide input and direction into DA via:

- participation in the DA Board Selection Committee,
- active involvement in the development and evaluation of DA's Strategic and Annual Operating Plans,
- consultation and active engagement with the business groups of DA, and
- resolutions put to DA's Annual General Meeting.

Given the uneven international playing field on which the Australian dairy industry competes – against the subsidised production of milk and milk products, trade quotas and other non-tariff barriers to trade - R&D that keeps our production systems world-class is vital for competitiveness in world markets. The ADIC perceives 'world-class' to mean high levels of production that are cost-effective, profitable, environmentally-sound and meet domestic and international community expectations and quality standards.

The dairy industry has carefully cultivated a dynamic and constructive relationship between ADIC and DA, and so ensured the investment in RD&E has been profitably targeted at the collective good of the whole of industry value chain.

Further, DA plays the lead role in funding and coordinating essential RD&E for the industry ensuring the investments made are consistent with both the Australian Government's rural priorities, and its constitution, which demands active strategic input from the industry through ADIC. DA's funding comes not only from levy funds and matching Federal Government grants but from other government agencies and commercial companies which is used to gain leverage for specific RD&E projects. The makeup and focus of dairy's portfolio of RD&E investments is reflective of industry involvement and DA's "big picture", technical input.

Dairy Australia spends around \$30-35 million a year in R&D projects for the benefit of Australian dairy farmers and manufacturers. Dairy Australia invests in and co-ordinates industry research in three areas:

- **Farm** - feed, animal genetics, resource management, farming systems and business practices.

- **Manufacturing** - pre-competitive research in biosciences, processing, bulk and functional ingredients, functional foods, cheese starters and fermented products, sustainable production processes, health and nutrition.
- **Technical issues** - quantitative risk analysis, control measures for contaminants, development of analytical methods, and animal health and welfare⁶.

A study commissioned by Dairy Australia in 2007, offers the following holistic assessment of dairy investment in RD&E.

- Total input of professional staff into all dairy RD&E in 2006-07 was **703.1 FTE**, comprising:
 - 242.6 FTE in Manufacturing R&D
 - 205.7 FTE in Farm Production Extension
 - 194.4 FTE in Farm Production R&D⁷
- The total value of RD&E expenditure across all projects and partnerships in the dairy industry was **\$154.96 million** in 2006-07.
 - This represents an increase of 31.7 per cent in dollar terms, and an increase of 2.3 per cent in real terms (adjusted for CPI) compared with the previous 1998-99 study.
 - As well as the \$15 million provided by taxpayers to match its own levy, the industry has leveraged significantly more funding towards R&D from other sources, including direct industry investment⁸.

The above investment levels suggest that government funding, combined with the compulsory levy, does have a role to play in inducing additional R&D activity⁹. A prime example is to be seen in DA's direct investment in two Cooperative Research Centres (CRCs) where highly strategic, but commercial, research is being conducted in Natural Resource Management, plant and animal genomics, etc.

In the Australian dairy industry the current model of RDC funding, complemented by clearly defined responsibilities for the peak industry bodies can be seen to be effectively investing in RD&E on behalf of the industry. The ADIC contends therefore that it would require a significant argument to change the current funding arrangements which serve the industry well.

⁶ www.dairyaustralia.com.au

⁷ Juffs and Oates, Updating of Expenditure and Infrastructure Data for Dairy RD&E in Australia, 2010

⁸ Juffs and Oates, *Ibid.*

⁹ PC Issues paper, 2010, p10.

4 Wider Community Benefits

Dairy farmers and the wider dairy industry provide benefits to the community in so far as they are responsible custodians of natural resources, drivers of economic productivity, direct (and indirect) employers, and located in (and thereby supporting the viability of) rural communities. The Productivity Commission asks whether this should be reflected in R&D. **The ADIC considers that such benefits are often intangible and it is vital that the Australian dairy industry, like other sectors of the economy, has the opportunity and freedom to determine its own R&D priorities whilst recognising overarching government rural priorities.** However, a recent study in 2007 found that R&D investment in certain social and environmental areas was occurring but, importantly, noted that it was driven by different funders (generally working in partnership together.)

*“The input by the dairy companies into Productivity issues was proportionately slightly higher than the input by either the DPIV or other States DPIs. However, the dairy companies’ input into Environmental/NRM issues was much lower, and into Social/Community issues much higher, than the input by either DPIV or the other States DPIs.”*¹⁰

While we might expect, in 2010, that industry-driven R&D into Environmental/NRM issues would have grown significantly, it remains that the funding priorities of governments and industry will not always coincide exactly. **However, the important issue is that one area of wider community benefit was driven more strongly by industry than government. Allowing industry to continue to set our own industry R&D priorities is not to forego wider community benefits of such research and development; in some cases it is to strengthen their achievement.**

5 Comparison with other industry R&D incentive schemes

The importance of rural industries, and more specifically, the role of the taxpayer in co-funding rural research and development is an area which the Productivity Commission invites consideration. The ADIC refers the PC to the benefits of rural R&D that are acknowledged in the various studies cited by the PC¹¹ as well as those benefits pertaining to dairy, dairy communities and the Australian economy cited in this paper.

One question posed by the PC (*“Is the case for government funding support for rural R&D stronger than in other parts of the economy and, if so, why?”*) suggests that rural industries receive a

¹⁰ Juffs and Oates, page 21

¹¹ PC Issues Paper, Box 2, p9)

disproportionate share of the government R&D dollar compared to other industry sectors. The ADIC firmly rejects this suggestion. **The current government R&D model ensures the taxpayer derives a minimum \$2 R&D value for every \$1 invested by government. Furthermore, the community can be assured that this R&D will be consistent with the Rural R&D priorities set by Government in 1994, and reviewed in 2007. These priorities, by definition, “ensure R&D objectives of the Australian Government are met” and “to better target agricultural, fisheries, forestry and food industry R&D efforts.”**¹²

Compare this model, which doubles the dollar value of R&D and ensures that R&D takes places within a clear priority framework set by government, to those that apply to non-rural industries. For example, “the Australian Government allows companies to deduct 125 per cent of eligible expenditure incurred on R&D activities when they lodge their corporate tax returns. In some circumstances, the tax offset for a portion of spending may be increased to 175 per cent.” In 2007, more than 6,295 companies with a reported R&D spend of \$9.2 billion were registered for these tax concessions¹³. ADIC does not dispute the importance of this R&D, or the appropriateness of government funding. In light of the PC question however, we note that the Australian taxpayer ultimately paid the company for undertaking the R&D (as opposed to receiving equal co-investment from the company concerned) and was not involved in setting broad R&D priorities as with those that apply to rural R&D. Finally, the ADIC notes that the combined reported R&D investment by government to rural RDC’s \$1.7 billion is comparable to the Government-reimbursed company R&D estimated in 2007. **This paints a picture of rural industries aligning their R&D more closely to government priorities than other sectors of the economy and being arguably more answerable to the community.**¹⁴

In addition, the current model allows RDCs the ability to provide a voice for industry to influence and oversee the implementation of the new national R&D framework in the best interests of the industry and the community.

¹² www.daff.gov.au/agriculture-food/innovation/priorities

¹³ www.dfat.gov.au/facts/research_development.html

¹⁴ www.dfat.gov.au/facts/research_development.html

6 Scope for duplication of administration and service provision in current model

The ADIC considers that the administration and internal structures of RDCs are rightly the purview of the RDC Board, in this case Dairy Australia. In our role as a key stakeholder to DA and representing levy payers, ADIC believes firmly that value for money must be achieved and measured by RDCs. However, the detail of how this is achieved should be a function of the Board and managers it appoints.

However, for the purposes of engaging in the dialogue intended by the Issues Paper, ADIC has examined the question of whether there is scope for duplication of administration and service provision in the current RDC model.

While at first glance it may seem an obvious area for efficiencies, ADIC considers that maintaining separate but parallel administrative and service functions of RDCs is important. **This is not to discount the benefits of informed, voluntary collaboration and cooperation on RD&E projects where there are advantages to all parties. This currently is the way Dairy Australia operates to good effect both domestically and internationally and has been useful in enabling DA to lever its available funds by as much as 300%.**

A simplistic overview of the current RDC arrangements would see RDCs like the Australian Wool Corporation, Meat and Livestock Australia, and Dairy Australia all providing investment in advancing grazing industries across the continent. All are driving, to a lesser or greater extent the development and growth of the business of their respective commodities which involves animals eating pastures, silage and grain in varying proportions. Further it can be said that all dairy farmers are beef producers – as they are, through the use of culled dairy cows and calves as meat for human consumption. But this is where the similarity ends.

At its most basic the whole farm management and husbandry regimes are different. Most overtly the differences between dairy and meat lie *inter alia* in the:

- frequency of handling animals
- farm systems
- farm infrastructure and technology
- nutritional requirements
- veterinary and hygiene requirements
- quality assurance procedures and requirement (dictated locally and internationally)
- herd genetics and improvement
- frequency and nature of access to market
- breeds of animals
- technical knowledge requirements of farm managers
- profit margins

- farm labour inputs
- operational intensity
- risk management techniques and opportunities

This to say nothing of the regional climatic and soil quality differences which impose a huge complexity to how the variables listed above must be interpreted and accommodated on a sustainable basis. It is overly simplistic to suggest that RD&E devoted to resolving the problems of the beef industry at a farm level can be applied to the dairy industry and vice versa.

Clearly methodologies pertaining to the resolution or understanding of issues such as emissions of methane by grazing animals, genetic improvement of pasture species' performance, or nutritional properties will have cross-commodity applicability. Mutually beneficial opportunities between dairy and other livestock industries for collaboration in such areas have been and will continue to be pursued. Collaboration is a means to an end and is not a goal in its own right.

Centralisation or amalgamation of administration or research management will hinder, if not prevent, individual commodity groups responding to opportunities as they arise. For example Dairy Australia has a major review of the industry strategy and priorities every 3 years. Each year there is a review of the annual operating plan, and on an as needs basis, as issues arise DA enhances focus on particular problems or even shifts focus. **The fine-tuning and responsiveness which is so critical for the profitability of the industry will not work in a cross-commodity administration dealing with an unpredictable and competitive matrix of business and climatic variables.** The notion of cost-effective amalgamation also presumes that a third party or combined administration, with its separate commodity advisory and policy bodies, will understand the dairy industry better than the dairy industry itself.

Maintaining separate administration of the RDCs facilitates greater levels of transparency and accountability for performance. Any cost savings achieved through removing duplication may lead to reduced operational effectiveness if priorities are not aligned.

7 Consultation and Contestability

In its Issues Paper, the Productivity Commission raises questions relating to how well RDCs currently consult with industries in setting R&D priorities and implies that there may be some wider-community benefit in allocating a degree of the current level of government funding on a competitive basis.

The ADIC, as the combined voice of dairy farmers and dairy manufacturers, is fully seized of its responsibility (enshrined in the Dairy Australia constitution) to provide strategic input to setting the R&D objectives for the dairy industry. Exercising this responsibility collaboratively with DA works well in the dairy industry and, we consider, ensures that the immediate, medium and longer term requirements of the industry are best catered for. Any change to the current formalised consultation arrangements between industry and our RDC would be of grave concern to the dairy industry and a dialogue we would seek to be closely involved in.

The PC issues paper suggests that a pool of funds for which RDCs could competitively bid may be considered. **ADIC considers that such an approach should operate outside of the RDC model which utilises matching funds for the industry that has raised the initial R&D investment. For example, ADIC considers that it is in the interests of the dairy industry that those funds raised against the level of milk production be quarantined for use by the industry.**

8 Conclusion

ADIC strongly contends that rural research and development should be recognised as an area of R&D that brings benefits to the broader community, contributes significantly to the national economy and constitutes an equal partnership between government and industry. In this respect, agriculture can be argued to 'pays its way' more than other sectors of the Australian economy.

Moving forward, ADIC suggests that any improvements to the RDC model be considered in:

- the context of equity with other sectors of the economy,
- a coherent vision for rural research and development co-funding that is established in consultation with RDCs, industry stakeholders and the wider community,
- with a commitment from Government to, as a minimum, maintain current levels of R&D investment, and finally recognising
- the successful and comprehensive delivery of RD&E and related services that DA achieves for the Australian dairy industry through the Government's current RDC funding model.