



The Hon Steve Whan MP

Minister for Primary Industries
Minister for Emergency Services
Minister for Rural Affairs
Member for Monaro

MOC10/3856

RDC Inquiry
Productivity Commission
LB2 Collins Street East
MELBOURNE VIC 8003

- 2 DEC 2010

Dear Commissioner

Thank you for the opportunity to make comment as part of the public inquiry into Rural Research and Development Corporations.

The NSW Department of Industry and Investment supports a number of the recommendations in the Commission's Draft Report, including that there should be skill based Boards, that there should be Commonwealth appointment of Directors on Boards and the proposed streamlining of levy arrangements and more flexible ways of changing levy arrangements.

However, the Department holds strong concerns in relation to: the recommendation to halve Commonwealth funding to the current RDC's; the view that projects that have net benefits to industry require no public funds; the establishment and funding of a new RDC (Rural Research Australia); and the suggested mechanism to better inform and coordinate funding for rural R&D.

The attached submission outlines the Department's response to the Commission's Draft Report.

If there are aspects of the submission you wish to consider in more detail please do not hesitate to contact the Director General of the Department, Dr Richard Sheldrake.

Dr Sheldrake may be contacted by telephone on 02 8289 3905 or via email on richard.sheldrake@industry.nsw.gov.au.

Thank you again for the opportunity to make a further submission to the inquiry.

Yours sincerely

Steve Whan MP

Minister for Primary Industries
Minister for Emergency Services
Minister for Rural Affairs

Encl

Further Submission in response to the Productivity Commission Draft Report on Rural Research and Development Corporations



**Industry &
Investment**

**Submission by
Industry & Investment NSW**

November 2010

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Main Authors: Philip Wright & Ruth Frater

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INTRODUCTION

The NSW Department of Industry and Investment (I&I NSW) welcomes the opportunity to make a further submission to the review into Rural Research and Development Corporations (RDCs).

This submission is framed in response to the Commission's Draft Report and addresses the issues that are of particular importance to I&I NSW.

1. Recommendations supported

I&I NSW are supportive of a number of the recommendations in the Commission's Draft Report. These include:

- The establishment of a process for assembling and maintaining robust data on total funding for rural R&D (Recommendation 5.2);
- The principles to guide the future operation of the RDC program, in particular the implementation of board selection processes that result in skill based boards (Recommendation 8.1);
- Some of the specific changes that help give effect to the principles, in particular that there should be Commonwealth appointment of directors on boards (Recommendations 8.2-8.7); and
- The proposed streamlining of levy arrangements and more flexible ways of changing levy arrangements (Recommendations 9.1-9.4).

2. Concerns

I&I NSW holds significant concerns regarding several recommendations including:

- The recommendation to halve Commonwealth funding to the current RDC's
- The Commission's view of "Additionality" and the view that projects that have net benefits to industry require no public funds
- The establishment and funding of a new RDC
- The establishment of a mechanism to better inform and coordinate funding for rural R&D

2.1 Reduced Funding

I&I NSW believes it is inconsistent for the Commission to suggest that "*It would not be appropriate to establish a target level for overall spending on rural R&D – nor a target for rural R&D intensity*" (PC 2010) when in fact the consequence of the Commission's recommendations is to reduce public funding to the overall system by at least \$60 million per year. This is in effect a recommendation for a very significant reduction which is not supported by analysis by the Commission nor by the overall view that the current system is sound.

I&I NSW agrees that it is difficult to make recommendations about the overall level of funding required but the evidence – eg. correlation between reduced government spending in agricultural R&D and the decline in agricultural productivity growth and absence of evidence of declining rates of return - points to the requirement for higher levels of funding rather than lower (I&I NSW 2010). The Cutler (2008) review notes that a strong research

sector is an underlying requirement for Australia's productivity and economic growth and that the ongoing reduction in government support for the public research system is out of step with most other OECD economies. Cutler also identified that "*We must also ensure that our most globally competitive industries, such as mining, agriculture, education and tourism receive adequate research funding support to keep them at the cutting edge.*"

The Commission's view that halving the funding to current RDC's will provide an incentive for industry to increase its contribution is not supported by evidence. Further, this view is driven by the belief that industry will increase funding because of the well established high rates of return on investment for rural research. I&I NSW argues that there is little evidence of farmers being willing to increase levies that they pay despite the high rates of return. In fact as Mullen (2007) argues many economists view the high rates of return that have persisted over decades as an indicator of market failure and underinvestment in R&D from both an industry and societies perspective.

The recommended reduction in funding is likely to have far reaching negative impacts including: a slowing in productivity growth in the sector which will have economy wide implications (as R&D investment is a key driver of productivity growth); and, a cascading reduction in other parties investments (eg. CSIRO, State jurisdictions, and Universities) in rural R&D. This second point receives little mention in the Commission's draft report yet it is likely to be critical to the overall Australian rural R&D system. Any reduction in the current dollar for dollar matching of levies by Commonwealth funds will have a very broad impact not only in unbalancing the portfolio but in dramatically reducing the overall effort on rural R&D. The RDCs provide cash into the system, which leverages investment from other research organisations such as state DPI's and universities. Removing or reducing the RDC cash will create a multiplier reduction in R&D effort.

The recommendation to reduce public funding is particularly difficult to understand given that Australian agriculture has amongst the lowest levels of government assistance of agriculture worldwide and must compete against heavily socialised agriculture in many countries including the US and the Eurozone. As argued in our initial submission (I&I NSW 2010) the modest expenditure of Australian governments on rural R&D is a far cheaper and less distorting approach than that taken by most other nations. In essence Australia has opted for low levels of support to agriculture with some of this support being via Government R&D expenditure. I&I NSW argues that this is a highly effective approach by the Commonwealth and its partners in rural policy. The current R&D model provides a bundle of industry and public goods ensuring that community priorities (economic, social and environmental) are addressed in a way that result in rapid adoption by industry because of the private industry benefits. As such rural R&D provides an effective substitute for more coercive or distorting approaches.

2.2 Additionality - No public funds for projects that have any level of net benefits for Industry

I&I NSW believes as argued in its initial submission (I&I NSW 2010) that one of the key strengths of the current model is its ability to provide a tight bundling of industry and public goods. The presence of government investment encourages public good outcomes that are adopted rapidly by industry in a way that will not occur if industry funds projects alone. Projects with reduced public funding will not be designed to provide as broad a range of community benefits. In economic terms a partnership between government and industry is

required to fully capture the non-rival benefits of rural research that spills over to the community (Mullen 2010). I&I NSW believes that public investment is not crowding out investment by industry but is a significant inducement to industry to invest.

2.3 A new RDC?

The creation of a new RDC (Rural Research Australia) to sponsor non-industry specific rural R&D has some merit but I&I NSW has a number concerns about the proposed nature of the split between RRA and the "industry" RDC's which are proposed to focus on research of direct benefit to levy payers. We do not believe that rural research can be simply classified into entirely industry good projects or entirely public good projects. As we argued in our initial submission to the Commission (I&I NSW 2010) the real strength of the current model is that it allows for most projects to deliver both outcomes. This bundling together of outcomes has the advantage of a higher rate of industry acceptance and adoption of non-industry specific outcomes.

As such I&I NSW would prefer a model where the majority of public good research is delivered via the industry specific RDC's with a relatively small RRA focussed on public benefit only R&D and cross cutting issues that are unlikely to be addressed by individual RDCs, as well as having an oversight and coordination role. Such R&D might include the modelling components of climate change and some aspects of water, soil and landscape R&D.

Addressing most issues through existing RDCs, would facilitate the simultaneous achievement of both production and public good outcomes within projects, with a likely higher rate of industry acceptance and adoption. Separating the two is likely to lead industry based RDCs to focus more strongly on solutions with only industry benefits, while a separate non-industry specific RDC could struggle for industry relevance and adoption of outcomes.

It is agreed that some broader rural research has been under-provided by the current arrangements, particularly as noted in the area of coordinated natural resource management. The incorporation of non-specific industry rural R&D objectives into projects under the existing RDC structure can be achieved and could add an increased relevance to industry specific research as NRM issues and industry community and environmental objectives align.

2.4 Mechanism to better inform and coordinate funding for rural R&D

I&I NSW believes there are significant opportunities for the National Primary Industries Research, Development and Extension (NPIRDE) framework – being developed by the PISC R&D subcommittee – to assist in coordination and strategy development across the rural innovation system. The framework has a number of strengths compared to other possible coordination models in that it:

- a) Brings all parties who invest (eg industry, commonwealth and state government) together in a way that enables cooperation and collective action (as opposed to more bureaucratic, costly and coercive approaches);
- b) Enables the development of both sector and cross sector strategies in a collaborative and comprehensive manner; and,

- c) Is already developing strategies for common evaluation and data collection protocols across the rural R&D system.

The Commission's report notes the need for a mechanism to better inform and coordinate the totality of government funding for rural RD&E. I&I NSW believes the framework approach developed under the PISC R&D subcommittee is the best placed mechanism to achieve this in a way that prevents adding additional layers to the current system and is truly representative of all the major investors.

3. Conclusion

The current RDC model for rural research and development based on a mixture of industry levies and government (both state and Commonwealth) contributions has served Australia well and represents a relatively modest public investment (eg., government expenditure on all agricultural issues represents about 1.6% of total government expenditure and research is only a small proportion of this) that sees Australian agriculture with the second lowest level of government support in the OECD. Rural R&D provides government and the community with a "clever" way to deliver a mixture of industry and public benefits that is likely to be more effective and less distorting than more coercive approaches such as increased regulation or subsidies.

I&I NSW supports the Commission's recommendations that are aimed at improving governance, data collection and flexibility. However, I&I NSW is seriously concerned about some recommendations particularly those that will erode government investment in the system. We are strongly of the view that government investment should not be reduced especially as broader Australian productivity appears to be stalling and the sector along with the Australian community, face a rapidly changing world that is fiercely competitive, full of uncertainty, and contains major challenges including: climate change; and, energy, water and food security issues. The need for a sound rural innovation system is increasing not diminishing and the market failure context relevant to primary industries is becoming more complex and persuasive rather than less so and requires ongoing government investment.

4. REFERENCES

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