25 November 2010

Know-how for Horticulture™

Mr. Philip Weickhardt
Commissioner
Productivity Commission
Locked Bag 2
Collins Street East
Melbourne VIC 8003

Dear Commissioner,

I am please to submit Horticulture Australia's response to the Commission's draft inquiry. We and the many industries we comprise appreciated the opportunity to meet with you and Commission staff to provide an understanding of horticulture, and to present our views on the Commission's findings.

Horticulture Australia Limited has contributed to the response of the Council of Rural Research & Development Corporations to the Productivity Commissions draft report on Rural Research and Development Corporations.

In this submission HAL seeks to provide additional specific commentary on those issues which reflect on the Horticulture industry in particular. HAL has focused its response to the Productivity Commission's draft inquiry report on key principles and issues. Our response is based around five key areas:

- The fundamental rational for public investment in rural research and development
- The proposed Rural Research Australia
- The role of HAL in the broader research and horticulture environment
- Voluntary contributions
- The flexibility of the current RDC model.

Rationale for public investment in Rural R&D

Conventional rationale for mandatory levies and matching government funding of rural R&D is the existence of failures in the market for R&D goods and services. The presence of these failures will, if not attended to, result in national investment in rural R&D being substantially less than the economic optimum.

As outlined in our response to the Issues Paper for this review, the market failures affecting the level of Horticultural R&D include non-excludability/non-exhaustion and the non-divisibility of research costs. These factors are further exacerbated by increasing product diversity, a long and fragile supply chain, and the small size and low net capital value of the average horticulture enterprise.

In addition to investing in industry specific R&D, governments have also sought to use rural R&D to promote the achievement of national policy objectives such as growth in regional economies and employment, improved global food security, better environmental stewardship including adjusting to climate change, and enhanced food safety and nutrition (spillovers).

The current RDC model provides a mechanism to both address market failures and to achieve spillovers. The matching funding from the Commonwealth provides encouragement for industry participants to act collectively to address failures.

As outlined in our first response, horticulture industries are continuing and increasing their support for statutory levies (as well as voluntary levies). This trend indicates that current arrangements *and* the matching incentive are addressing market failure, however the PC has not assessed the risk of these market failures being sufficiently addressed going forward under a reduced level of matching funding. There has been no explicit consideration of the potential unintended consequence of reducing the levy to a level that may not be sufficient to encourage collective action.

The proposed Rural Research Australia

The Productivity Commission in its draft report identified that a key strength of the current RDC model is strong linkages with primary producers. It agreed this helped to ensure that money was not wasted on ill-conceived research, or research of limited practical value. It acknowledged industry linkages can also encourage greater or faster uptake of research outputs by primary producers.

Conversely, the Productivity Commission's draft report also included a recommendation to create a new RDC, Rural Research Australia (RRA), to be funded from a redirection of Commonwealth funds from industry RDCs to a new entity.

HAL does not support the formation of a new RDC that is independent of industry however recognising that there is a desire to deliver on public good R&D, it will be important for any entity charged with this task, regardless of the breadth of its portfolio, to have structured consultative mechanisms in place to ensure that the linkages with the end users of research is maintained.

It will also be critical to have structured mechanisms in place to consult with industry RDCs. In the absence of such a mechanism, there is a significant risk of duplication of efforts or gaps in the overall research portfolio. Strong links with industry RDCs can help facilitate input from producers, and ensure that research portfolios are aligned.

We would observe that this new RDC would also add to overall industry costs as well as inevitably diminish the critical mass of existing RDC's.

Any R&D entity charged with delivering public good should be encouraged to not duplicate efforts to increase agricultural productivity since clearly this should be the increased focus of the current levy based RDCs.

The role of HAL in the broader research and horticulture environment

The Productivity Commission recognised in its draft report that RDCs are major players in the overall R&D framework, and they have performed a broader coordinating function, with benefits extending beyond their immediate R&D activities.

HAL is the only institution that brings together the breadth of the horticulture sector at the national scale. Governments rely on HAL as a focal point for the sector. Without HAL, the horticulture industry is diffuse, which can create difficulties in coordinating issues such as market access, trade, biosecurity and food safety.

As a member of the National Horticultural Research Network, HAL plays a major role in shaping the priorities of other investors in horticulture research through this process. NHRN has a key role in the National Primary Industries RD&E Framework and National Strategic Rural R&D Investment Plan, working towards increased coordination and reduced fragmentation.

In making a recommendation to reduce government support of RDCs, HAL believes that the Productivity Commission has not explored or assessed the potential for the erosion of these benefits. HAL recommends that more robust consideration of the possible unintended consequences of changing the model, particularly the government matching funding should be undertaken.

Voluntary contributions

The Productivity Commission calls into question the continuation of voluntary contributions on the basis that these contributions (and when matched) are more to subsidise R&D that is heavily oriented to the particular needs of an individual commercial entity.

In formulating this view, HAL believes that the PC has overlooked the role of the voluntary contributions mechanism in horticulture industries.

HAL manages investment through voluntary contributions in the order of $20 million per year. HAL currently has 12 B-Class members, representing small or emerging industries that are yet to form a statutory levy. The Voluntary Contribution mechanism provides a "stepping stone" for these industries. Since HAL's inception, eight industries have transitioned from contributing voluntary levies to statutory levies and four industries have introduced statutory levies for both R&D and marketing purposes.

In the case of smaller or emerging industries that would otherwise not have the ability to raise a levy, the access to the matching dollar for voluntary contributions has resulted in opportunity for significant investment in R&D.

Voluntary contributions are also able to be made to HAL by value chain participants. This provides a key mechanism to attract the participation of the value chain in industry wide activities, and increases the connection between the farm gate and the consumer. Benefits arising from voluntary contributions funded R&D flow throughout the value chain from input suppliers through to consumers and are not restricted to the benefits of the voluntary contributions contributor.

HAL recommends that the PC explore in more detail the role of voluntary contributions in participating industries. We believe that the commentary presented in the draft report does not fully reflect the role of voluntary contributions as a stepping stone for horticulture industries.

The current model has sufficient flexibility to adapt and evolve

In its draft report, the PC makes a series of recommendations relating to ongoing improvements in the RDC model, including increased and consistent reporting and evaluation.

HAL's view is that the current RDC model is sufficiently flexible to enable further change and improvement, including those flagged by the PC.

Within the current model, HAL makes the effort to improve the way it does business. The performance review required under the Statutory Funding Agreement identified areas of focus for improvement, and the Company has considered and explored each of these recommendations. Board practices, providing improved guidance and support to industry planning activities, and governance arrangements for the relationship between HAL and Peak Industry Bodies are examples of these.

HAL is an active collaborator with other RDCS. This includes:

- Strategic collaboration and direction - to set RD&E policy and investment priorities;
- RD&E investment programs – formal contractual co-investment and collaboration that informs planning and operational management of RD&E program managers; and
- The harmonisation of RDC administration.

HAL recommends that the PC's numerous recommendations about improved performance, increased reporting and evaluation should be fully scoped and mechanisms within the current model be explored to implement any potential changes.

Conclusion

HAL commends the recommendation by the Productivity Commission to retain the RDC model as an effective means to support agricultural RD&E in Australia.

To paraphrase a past Primary Industries Minister (Mr John Kerin) "research is a long term game" and "practice change and the adoption of institutional and economic change is (even) slower". For this fundamental reason HAL believes that the support the mechanism of government matched funds provides is vital to the long term sustainability and future growth of Australian horticulture industries.

We acknowledge there is always room for improvement but believe the model, which is the envy of our counterparts' overseas, works well. We would add:

- The premise that the Australian government is bearing too great a share of the overall funding for horticulture R&D pays scant regard to the benefits flowing to the wider community.

- Given the disparate nature of Horticulture and the long and fragile value chain involved it is unfounded for the PC to assume that its primary producers would fund the R&D themselves. Similarly there is no evidence of any" crowding out" caused by public funding. Reductions in government funding, with greater reliance on industry will have important ramifications on the stability of funding given that the government component provides some buffer against poor seasons and low prices, both of which are common and have an impact on statutory and voluntary levy collections.

- There is already a shortage in horticultural scientists and students. Uncertainty of funding is already having an impact on attracting suitable people to research and on the continuity of research programs. Greater uncertainty will only exacerbate Australia's waning capacity over the long term.

- In considering investment by the private commercial sector (not industry funds), by implication the Report indicates that this area of investment will be increasingly important in future and yet it provides scant analysis of the opportunities or barriers to achieving this potential.

HAL is supportive of the Commissions suggestion that further investigation be made to explore the benefits of combining R&D and Marketing levies, and the impact of allowing an RDC to vary the allocation of funds between the two without seeking levy payer formal approval.

We would welcome the opportunity to provide further information relating to the matters raised above.

Yours faithfully,

Selwyn Snell

Chair