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Business tax Working Group Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

[email BTWG@treasury.gov.au]

Business Tax Working Group Discussion Paper

Arrium welcomes the opportunity to comment on the Business Tax Working Group (BTWG) Discussion Paper (DP). Our comments are limited to the proposals to make change to the research and development (R&D) tax incentive.

Submission

Arrium opposes any further reduction of the support provided by the R&D tax incentive program. Arrium was continually involved from the time of the Cutler Report in the redesign of the R&D program which resulted in the new legislation implemented on 1 July 2012. The restrictions made to R&D eligibility under the new legislation have already reduced the support provided by the program. The design of the restriction was to focus the program more fully upon innovation that has spill-over benefits for the wider Australian community. Arrium supports those goals.

Arrium believes the R&D program provides significant incentive and support to manufacturers, large and small, to undertake additional R&D activities and to do so in Australia. It is not correct to say that the R&D program does not incentivise and support R&D in larger organisations. Our engineers do not want for ideas for innovation. However, the pressures of business and the risks involved mean that funding for such possibilities needs to be weighed carefully with other opportunities. The R&D program has been central to underpinning Arrium's significant and continuous focus on R&D and seen Arrium undertake a wider range of R&D activities than it otherwise would have done. There is a risk that if the R&D program is further reduced these activities will be done in countries that encourage these activities.

Arrium understands the mandate of the BTWG is to seek measures by way of reduction to existing deductions to fund a proposed cut in the corporate tax rate. Whilst supporting a corporate tax rate cut, Arrium feels the mandate given to the BTWG is inappropriate as the various current deductions canvassed in the DP for reduction/removal all have their own purpose. Notwithstanding this and Arrium's objection to any further reduction of the R&D program, Arrium would consider a \$10bn turnover threshold or an annual \$300m cap as workable options.

Arrium's response to the R&D options in the DP is as follows:

BTWG Option	Arrium Response
Abolish the 40% non-refundable tax offset for companies with turnover greater than \$20m	Arrium opposes this option
Impose a turnover threshold (perhaps \$10bn) above which the 40% non-refundable tax offset could not be claimed	A \$10bn turnover threshold could be considered
Impose a cap on the amount that can be claimed annually under the 40% non-refundable tax offset	A \$300m annual cap, before feedstock adjustments, could be considered.
Cut the rate of the non-refundable tax offset to 37.5%	Arrium opposes this option

Background on Arrium's R&D Activities

Arrium is a mining and materials company with three key businesses: Arrium Mining, Arrium Mining Consumables and OneSteel Steel & Recycling. Arrium has annual revenues of over \$7 billion and employs more than 10,000 people in Australia. Most of Arrium's R&D takes place in OneSteel Steel & Recycling which includes vertically integrated steel raw materials, steel manufacturing and metal products distribution.

Arrium has always been an active participant in R&D, as well as its policy development. In order to compete domestically and internationally, Arrium is continually investing in new plant, new products and in programs of continuous improvement to manufacturing efficiency.

Since 2000, Arrium's R&D program has seen the development of many new and improved products and processes, including:

- Following the closure of steelmaking operations at Newcastle in the late 1990s a billet casting plant was installed at the Whyalla Steelworks to extend the range of products produced from a slab, structural and rail steel maker to include the feed material for the rolling mills in Newcastle. These included many different high-grade steels for local manufacturers whose products would otherwise have been imported.
- Environmental projects such as the elimination of coal tar contamination from fence posts on farms, the treatment and handling of waste materials to be suitable for reuse and the continuing reduction of dioxin emissions to world's best practice levels.
- The design and installation of a new type of heavy mining rope plant in Australia allowing Arrium to continue to be a world leader in this specialist market.
- Ongoing development of grinding media for the world's resources industries which is another specialist market in which we are a world leader.
- Development of new mining techniques for iron ore.
- The extension of the life of Whyalla Steelworks with a major program to convert from hematite to magnetite as the source material for operations and at the same time to reduce significantly the impact of operations on the ambient dust levels in Whyalla. This program has also had major regional economic impact and secured the future of operations to at least 2027.

More recent projects include the following:

- Development of the new Duragal Platinum product, which provides a thicker zinc aluminium coating for tube products sufficient to meet the durability requirements of an R3 rating as defined in AS/NZS 2699.3: this means that these products have a better corrosive resistance for coastal areas. The R&D incentive was utilised to support this development and as a result these new product coatings are now manufactured in Australia and available to the Australian market.
- In Whyalla, Arrium is mining and manufacturing in a dry area. As such Arrium is continually developing new or improved processes to improve water consumption practices and to rely less on SA Water.
- In 2011, Arrium undertook a significant repair of the blast furnace in Whyalla. This repair technique has been internationally recognised.
- Arrium has undertaken the development of new and improved railway wheels. With the increased requirements to meet advanced technology in railway rolling stock components and the expansion of export opportunities, Arrium performed R&D activities to improve the design, physical properties and manufacturing processes associated with railway wheels, including:
 - development of a process to produce wheels, sets and axles in compliance to international specifications
 - development of a process to produce consistent hot shape wheels with 3mm machining.

These internationally competitive wheels are manufactured in Newcastle.

- Arrium has R&D initiatives throughout the steelmaking processes. These R&D activities have:
 - developed new grades of steel for new products
 - used alternative raw material inputs that have reduced input costs without compromising quality
 - developed new chemistries that have resulted in high quality downstream products
 - improved energy consumption rates in an Electric Arc Furnace
 - developed a high speed strength micro-alloyed rail grade of steel for railway tracks. This grade of steel is new to Australian manufacturing and allows Arrium to compete internationally in this market.

These developments have allowed Arrium to continue to be a large scale Australian manufacturer. We supply many other manufacturers with products as well as delivering to the infrastructure, construction, mining and agricultural industries. Many of our plants and distribution centres are located in regional Australia.

The R&D tax concession is factored into project evaluations and, as such, contributes directly to the assessment of the viability of projects and acts as a variable in the decision as to whether to fund the developments.

Conclusion

Arrium appreciates the opportunity to make this submission in response to the DP. We fully support the availability of the R&D incentive for Australian business. Arrium is particularly concerned that any further reduction in the R&D program will incentivise business to relocate R&D activities offshore or reduce the level of R&D activities carried out.

We are fully available to participate in any consultative processes that occur following the submission closing date of 21 September 2012 and would welcome the opportunity. If you have any queries or require elaboration on any aspect of this submission, please call Steve Ashe, General Manager Investor Relations and External Affairs on (02) 9239 6616, or Damien Baxter, General Manager Tax on (03) 9673 0419 or me on (02) 9239 6612.

Robert Bakewell
CFO Arrium Limited

CC patrick.sedgley@treasury.gov.au