

*Submission to the Joint Standing Committee on Foreign Affairs, Defence and Trade's inquiry into
Government support for Australian defence industry exports*

QinetiQ Australia welcomes the opportunity to make a submission to this inquiry. As one of Australia's largest independent providers of specialist technical advisory services to Defence, we work at the forefront of Australia's defence industry. *QinetiQ* is a trusted partner to the Australian Department of Defence and other governments globally.

QinetiQ – Our Views

QinetiQ accepts the need for effective mechanisms to regulate the sale and transfer of defence goods and services. Our company is part of a global group that has significant experience in providing defence services internationally and we uphold export controls. We are a values-based company that complies with anti-corruption legislation. *QinetiQ* also actively limits its international trade to countries with values that align with those of the *QinetiQ* Group and the countries in which we are based.

Given the regulatory environment, trade barriers, international taxation regimes and fierce competition in the global market we consider that the Australian Government has a critical role to play in the success of Australian defence industry exports. *QinetiQ* believes there are four key areas in which the Australian Government should assist growth in exports of defence goods and services:

1. Defence, Austrade and other relevant agencies should work cooperatively with industry ahead of major Australian and international defence trade shows to ensure a strategic approach and that Australian exhibitors receive similar support to their competitors from other countries.
2. Defence and other agencies should provide greater support to Australian defence industry participants seeking export opportunities across the region.
3. Wherever possible, goods and services delivered under the Defence Cooperation Program should be linked to Australian defence industry involvement.
4. Requests by Australian defence companies for Intellectual Property (IP) licenses related to Foreground IP developed pursuant to work contracted by Defence should be agreed, unless it would prejudice the security, defence or international relations of Australia.

QinetiQ believes that a strong export market is necessary to maintain a viable domestic defence industry. Given the monopsonistic nature of the market, Australia's defence industry has two options to maintain viability: diversify or export. The Government has a key role to play in supporting growth in the export market.

Background

QinetiQ entered the Australian defence market in 2008 through the acquisition of local defence consulting and engineering companies. We are a growing Australian business of around 300 expert 'People Who Know How' that can draw on support from our UK parent and US colleagues to broaden and add depth to the services we offer in Australia. *QinetiQ* has continued to grow in the Australian market since 2008 and we believe that there is potential to export our services to other markets in the Asia-Pacific region.

However, differing taxation regimes, systems of government and political and economic circumstances, impact on the potential to export services. Understanding the market place and different cultures across government and business is important in determining approaches to market entry. In some cases those conditions might not be conducive to pursuing international sales. Government can play a key role in supporting Australian defence industry to understand the international environment.

It should also be acknowledged that companies sometimes confront unethical behaviours and business practices in certain markets. QinetiQ carefully manages such risks in order to comply with the law and meet company ethical standards. We do not seek to do business in environments that do not reflect our values.

Foreign Taxation Regimes

International expansion enlivens a range of issues that constrain the ability of Australian companies to conduct business profitably. Many countries (including New Zealand, Canada and Singapore) operate withholding tax regimes which obligate purchasing organisations to withhold local tax from payment for goods or services, often in the order of 10 – 20 per cent of the contract price. The service provider must then prove its tax status and demonstrate that it is not established in the country before seeking to recover the withheld tax. Withholding tax can have a significant impact on a company's cashflow, particularly for small to medium enterprises.

In practice, this can represent a substantial administrative burden that can only be avoided by either increasing the price of the services to absorb the amount of tax to be withheld or by accepting the payment of the contract price and foregoing efforts to recover withheld tax. The former case reduces the competitiveness of Australian business while the latter erodes profitability. Local tax regimes in many countries also require a service provider to establish their own employees in-country. This requires the exporter to establish a local "shadow" payroll system that complies with local regulations and often represents a substantial cost. Although these issues represent the cost of doing business, they can act as a disincentive to pursuing export opportunities.

Building Brand Presence

The global defence market is a deeply competitive environment. To be successful, a company must establish its credentials with potential customers and hope to dislodge existing competitors. That can involve a substantial investment. Structured opportunities to exhibit at major international defence trade shows can present a valuable opportunity to increase brand recognition with a variety of potential customers and generate sales.

QinetiQ attended the 2014 Singapore Airshow to scope possible opportunities in the regional market. We observed that the atmosphere at the Singapore Airshow was more buoyant than similar events in Europe and the United States and that there was seemingly a strong focus on concluding business. During the event, *QinetiQ* staff met with representatives of Austrade and Team Defence Australia – which brought together officials and representatives of the majority of Australian industry exhibitors (mostly small to medium enterprises) in one location.

Although we support the initiative, *QinetiQ* judges that the level of government support for Australian industry exhibitors was not to the same standard as that provided by other nations, including the UK. Given the importance of the event to the regional export market, we believe that the Government should make a more significant contribution to ensure that Australian exhibitors have the best opportunity to compete with their international competitors. This might be achieved through support for export marketing and investment strategies developed in conjunction with the companies involved.

Recommendation 1 – Defence, Austrade and other relevant agencies should work cooperatively with industry ahead of major Australian and international defence trade shows to ensure a strategic approach and that Australian exhibitors receive similar support to their competitors from other countries.

Identifying Opportunities, Establishing Networks and Meeting Potential Clients

In addition to participating in major regional trade events, increasing Australian defence industry exports would be greatly assisted by more regular interaction between Australian companies and prospective clients. Although such activities are properly the responsibility of companies seeking to export their services, as are associated costs, government officials can play a vital role in facilitating opportunities for customer engagement. Many companies would benefit from the advice of Austrade and Defence staff at Australia's diplomatic posts, in better understanding the local market. Notwithstanding that companies should rightly assume full responsibility for their commercial activities, the export of goods and services is a net benefit to the Australian economy. Staff at Post are best placed to provide briefings on the local political and economic context and to facilitate introductions to host government ministers and officials.

QinetiQ believes there is also an opportunity for Australia's network of defence attaches to provide greater advice about possible opportunities for defence exports. The UK's approach to promoting defence exports is based on clear cooperation between its defence attaches and trade-focused staff at diplomatic posts. As part of their responsibilities, UK defence attaches are directed to provide support to UK defence companies abroad. They provide background briefing on political and economic context and can facilitate introductions. This does not entail engagement in commercial activities, but it does ensure that the UK's international network of defence staff actively consider opportunities in their regions for defence exports.

We believe that a significant proportion of the effort of Australian staff posted overseas with responsibility for Defence industry-related matters is focused on possible acquisitions (imports) to a greater extent than on identifying opportunities for export. In our view, giving greater emphasis to possible export opportunities will become increasingly important as we renew efforts for defence engagement and try to increase our levels of military interoperability with regional partners.

Clear direction should be given to Australia's Defence attaches and advisers on the need for them to be pro-active in the identification and pursuit of opportunities for Australian industry in their host countries. This is not a suggestion that Embassy and High Commission staff should become salespeople, more that they should understand and be able to promote the merit of Australian solutions to the capability and service requirements of their host governments. In that respect, a strong understanding of Australia's defence industry should be one of the criteria upon which Australia's Defence attaches are chosen.

Recommendation 2 – Defence and other agencies should provide greater support to Australian defence industry participants seeking export opportunities across the region.

Linking the Defence Cooperation Program to Australian Industry

One method of increasing opportunities for Australian defence industry exports would be to require, wherever possible, that goods and services provided under the Defence Cooperation Program (DCP) are tied to Australian industry involvement. Although *QinetiQ* accepts that the majority of activities that occur under this program remain at the military-to-military level, we believe that Australian defence industry products and services should be used wherever industry support is needed. The Government may wish to consider setting a target for defence industry involvement in DCP activities.

Recommendation 3 – Wherever possible, goods and services delivered under the Defence Cooperation Program should be linked to Australian defence industry involvement.

Access to Intellectual Property Licenses

QinetiQ's business revolves around the world-leading expertise of its people. We are predominantly providers of technical advisory services to Defence in support of all stages of the capability life-cycle for major platforms in the land, sea and air domains. Under existing contractual arrangements, the intellectual property that we generate in the conduct of such work (Foreground IP) vests in the Commonwealth. Given the sensitivity of some of our work, and the monetary value of the contractual arrangements, we accept that this is an appropriate model.

However, there may well be opportunities for *QinetiQ* to export similar services where it does not prejudice the security, defence or international relations of Australia. Our company is currently aware of one case of another regional country which is seeking our services to deliver a similar product for their defence force. That approach occurred through the Department of Defence and we understand that Defence is in the final stages of issuing us with a license to use the Foreground IP. This example highlights the extent to which potential Australian defence industry exports are dependent upon the processes of relevant government agencies.

Although we support the need for robust regulation to secure the transfer of strategic or defence goods, technologies or services, we believe that the Government should provide a framework that promotes the licensing of IP as a key enabler in exporting defence expertise. That framework should consider security, defence export regulations and strategic collaboration with Australia's defence partners to enable increased defence exports. One approach would be to alter the current contracting model to provide companies with an "assumed IP license" for Foreground IP generated under contract, unless otherwise determined by the Commonwealth on a case-by-case basis at the point of contract. Other regulatory obligations would still exist, so companies would need to seek export licences as necessary, but the presumption of IP licensing for contracting companies would shorten the timeframes necessary to seek approval ahead of the pursuit of export opportunities.

Recommendation 4 – Requests by Australian defence companies for Intellectual Property (IP) licenses related to Foreground IP developed pursuant to work contracted by Defence should be agreed unless it would prejudice the security, defence or international relations of Australia.