Chapter 16

Environmental and farming community concerns

16.1 The committee's main focus has been on the collapse of some of the large agribusiness MIS and their effect on retail investors. In this chapter, the committee turns its attention to farmers and landowners who had leased their land to an agribusiness scheme and to the environment and communities affected by the activity of agribusiness MIS including when a scheme failed. It considers the consequences for the agribusiness sector, particularly the forestry industry, and the future prospects for, and possible role of, agribusiness MIS in Australia.

16.2 Mr Hirst informed the committee that farmers, as landowners, certainly jumped at the opportunity to be involved in the MIS industry. Ms Davis noted that the farmers regarded leasing their property to an MIS as a business proposition on the basis of a standard business lease. She explained that from the farmers' perspective they were providing a service 'as simple as mowing the lawn':

> We have leased you our land, you grow your trees. Get on with it. It pays the rent and it is a straight business transaction.[1]

16.3 Experiences have shown, however, that the agreements with landowners were not straightforward and the consequences stemming from a failed scheme have been far reaching.

Environmental and social consequences

16.4 Mr Sean Cadman from the Cadman and Norwood Environmental Consultancy informed the committee that:

> In 1990 the National Plantations Advisory Committee was established to investigate the opportunities for integrating forestry and farming commercial wood production on cleared agricultural land.[2]

16.5 The advisory committee was to examine sustainable opportunities for expanding Australia's plantation estate. Mr Cadman, who represented the Australian Conservation Foundation on that committee, highlighted the importance of understanding that:

> …as early as 1990 there was recognition in the terms and references of the committee and in the reports that were undertaken to inform the recommendations of the committee, that a poorly managed rollout of a

1 *Proof Committee Hansard*, 5 August 2015, p. 25.

2 *Submission 105*, p. [1].

> plantation development agenda could lead to very perverse outcomes for the environment and the long term sustainability of an Australian plantation estate.[3]

16.6 According to Mr Cadman, specific concerns were raised, or advice given, at that time including, but not limited to:

- plantation establishment should NOT drive land clearing;
- the taxation treatment of the time was a disincentive to investment because the tax all fell due at the point of harvest;
- any taxation changes to incentivise plantation should not become an end in themselves and plantation establishment needed to be based on business models that did not require the continuation of tax deductibility for the business model to succeed;
- specifically that taxation incentives needed to be phased down to zero over a 10 year period;
- to be sustainable plantations needed to be established to provide inputs to industrial processing plants and that just growing for wood chips for exports was unlikely to be sustainable;
- site selection should be based on realistic growth rates, specifically that the costs of pest control should not be underestimated and that rainfall and soil parameters need to be within a certain range or economic growth rates would not be realised (CSIRO modelled the sites in Australia that would be most likely to succeed); and
- communities needed to benefit clearly from any large plantation establishment program because of negative community experiences in the past.[4]

16.7 Researchers similarly warned of the potential that, eventually, the benefits of investor tax concessions could 'show up as subsidies to higher cost structure operations and/or returns to operators of such schemes, rather than inducing expansion of efficient investment'. They cited numerous complaints about the harmful effect of agribusiness MIS schemes on traditional farming activities, including 'giving an artificial tax-induced boost to agricultural land prices'.[5]

16.8 Evidence before the committee clearly shows that the concerns identified in the 1990s were justifiable and ultimately, in many cases, the failure to heed them

3 *Submission 105*, p. [1].

4 *Submission 105*, pp. [1]–[2].

5 Christine Brown, Colm Trusler and Kevin Davis, 'Managed Investment Scheme Regulation: Lessons from the Great Southern Failure', 29 January 2010, p. 11, http://kevindavis.com.au/secondpages/workinprogress/Great_Southern_JASSA-v2-28-1-10-3.pdf (accessed 9 December 2014).

contributed to the downfall of some very prominent MIS with wide ranging environmental consequences.

Damage to environment and reputation of agribusiness MIS

16.9 Mr Cadman referred to the collapse of the schemes and the high probability that most of the lots would be 'cleared and revert to either agricultural production or become derelict weed-scapes'. He also noted the concomitant destruction of faith in the forestry sector, observing:

> Hundreds of thousands of hectares of land was cleared in Tasmania and on the Tiwi Islands at a huge environmental cost. The Australian Public has almost nothing to show for the millions of dollars of tax incentives given and gullible investors pursued by unscrupulous financial advisors have lost millions.[6]

16.10 Likewise, the TFGA lamented the aftermath of the failure of some schemes, noting that many plantations have died or stopped growing while others have received little or no ongoing maintenance. It stated:

> In the specific case of the forestry schemes, there have been a raft of perverse and detrimental outcomes which have been magnified by the collapse of Gunns Ltd. Many private landowners who had arrangements with Gunns have now been left with a devastating economic and emotional legacy. Coupled with the impacts of significant sovereign risk as a result of government decisions, this leaves scars that will ensure that further plantation expansion and replanting on private land will be limited if non-existent. Many have been so adversely affected that the thought of planting another tree on their property is too much to bear.[7]

16.11 In the association's assessment:

> Much of the original speculation with the MIS plantation arrangements within Tasmania was that the estate would become a resource for downstream processing. The main component of this was promoted to be the proposed Tamar Valley pulp mill, with other minor processing options adding to the overall industry. In hindsight, the reliance on one project, and the establishment of vast plantations to feed it, was clearly strategically poor. Silver bullet solutions rarely work. The schemes should have been accompanied by concise research on what other options were available for downstream processing. Had that been the case, then in the process a natural diversification of options would have been developed. This would have ensured that the failure of one project and or company would not have put at risk a whole industry.[8]

6 *Submission 105*, p. [3].

7 *Submission 24*, p. 4.

8 *Submission 24*, p. 5.

16.12 Noting one of the key underpinnings of the forestry MIS—to enhance investment with the objective of increasing the area of commercial trees to levels that were not being met by normal market forces—the TFGA explained:

> The idea was that allowing tax deductions would enhance this objective; and at the same time provide a valuable timber source into the future. While it is debatable that such a market failure was real, the fact remains that we now find ourselves in a situation where the bulk of the plantation estate in Tasmania is an asset that is rapidly collapsing.[9]

16.13 Mr Lawrence, an economist, tax accountant and more recently a public policy researcher, was critical of the ATO for failing to monitor the schemes once they were established to ensure they were being run in accordance with the product ruling. He recalled visiting plantations where 'trees had died, cattle were in there, horses were in there'.[10] Mr Jim Crowley, whose property is surrounded by plantation developed land through an MIS, also drew attention to:

- no demonstrated responsibility for the on-going maintenance of shared boundary fences;
- no maintenance of fire-breaks;
- no weed or wallaby control;
- an increased fear of fire [the plantation land was previously cleared pasture]; and
- massive irritation that my 'neighbour' does not pay council rates.[11]

16.14 Similarly, Mr Paton listed the by-products of forestry MIS and related schemes, which included:

- vast tracts of land in Western Australia, Victoria and South Australia now converted back to pasture because of failed plantations;
- huge kangaroo plagues in the Albany, Great Southern region of Western Australia and the Green Triangle region in Victoria/South Australia; and
- local community dislocation in townships such as Hamilton, where huge flurries of investment activity initially occurred, distorting land values, artificially ratcheting farm rentals and taking high value farmland out of production into passive monocultures such as Blue Gums.[12]

9 *Submission 24*, p. 4.

10 *Proof Committee Hansard*, 5 August 2015, pp. 3 and 4.

11 *Submission 7*, p. [1].

12 *Submission 149*, p. 5.

The committee visited a plantation outside Launceston. In this instance, the failure of the FMIS led to the foreclosure and sale of the property. The visit also provided an example of where tree growth rates did not meet the expectations outlined in the prospectus.

16.15 In Mr Paton's view, agribusiness MIS should be 'shut down once and for all in every aspect'.[13] In contrast, however, some submitters envisaged a promising future for such schemes. Even so, they recognised that changes were required.

16.16 Clearly, forestry MIS failed to achieve the overriding strategic goals of *2020 Vision*—to have a plantation industry with a sound reputation as a credible investment destination and to have 'well-informed investors willingly participating in well-run and profitable managed investment plantations projects'.[14] The collapse of a number of significant agribusiness MIS companies has severely undermined investor confidence in such schemes. According to NewForests:

> With major MIS companies being liquidated and most MIS investors losing much of their investment, it is unlikely that the sector will ever recover. The opportunity for institutional investors is to rationalize the land and forestry assets—1 million hectares of timber plantation—into a consolidated timberland asset.[15]

16.17 As noted in chapter 2, since the introduction of MIS in 1998, agribusiness schemes have raised approximately $8 billion. To appreciate the magnitude of the financial loss that stemmed from failed agribusiness MIS, the particular schemes that have collapsed raised:

- Timbercorp, just over $1 billion;
- Great Southern, $1.8 billion;
- FEA Plantations, $426 million;
- Rewards Projects Limited, $291 million;
- Willmott Forests, about $400 million; and
- Gunns Plantations, about $1.8 billion.[16]

16.18 A number of major participants in agribusiness, but particularly in the forestry sector, argued, however, that the aims and objectives spelt out in *2020 Vision* remain valid. They recognised the significant contribution that the Australian forestry industry currently makes to Australia's overall economic development.[17]

---

13 *Submission 149*, p. 6.

14 *Plantations for Australia: The 2020 Vision*, an Industry/Government Initiative for Plantation Forestry in Australia, p. 15, http://www.agriculture.gov.au/Style%20Library/Images/DAFF/__data/assets/pdffile/0009/2398185/plantations-australia-2020-vision.pdf

15 NewForests, 'Rationalizing Timberland Managed Investment Schemes: The changing Landscape of Australia's Forestry Investment Sector', p. 1, http://www.newforests.com.au/wp-content/uploads/2014/09/Rationalizing-the-MIS-20140908.pdf (accessed 15 November 2014).

16 *Proof Committee Hansard*, 14 October 2015, p. 18.

17 AgriWealth, *Submission 138*, p. 1.

Viability of schemes after liquidation and sale

16.19 Mr Ian Farquhar, Tasmanian farmer, informed the committee that in his opinion the underlying motives for the schemes remain valid, which were to address two needs:

- to return more trees to the Australian landscape—although, in his view, MIS may not be the most appropriate vehicle to meet this need of rural landscape management; and
- to remedy the significant deficiency in the long term base capital in Australian primary industry.[18]

16.20 According to Mr Farquhar:

> The MIS successfully identified an availability of funds in our cities for investment in primary industry. It is unfortunate the MIS structure attracted many who primarily sought to avoid taxation rather than invest in rural business.[19]

16.21 Mr Farquhar noted that 'a few well managed businesses have demonstrated that this vehicle can be used to develop successful, productive enterprises'.[20] Likewise, Mr Bryant suggested that MIS:

> As a form of investment…are important to the growth of this country. It goes to the heart of what regulation there is around entities being able to do business in this country. That is what has gone wrong here. The regulation around how Timbercorp could operate and grow to the size it did was clearly inadequate.[21]

16.22 Since the collapse of Australia's major agribusiness MIS in 2009 and 2010, Timberland Investment Management Organisations (TIMOs) have purchased a significant area of the MIS plantation estate. The Department of Agriculture informed the committee that, while the trend in MIS investments was based mostly on individual investors, after 2009:

> …the majority of the MIS companies which have gone into receivership and liquidation have had their assets purchased by a small number of TIMOs backed by institutional investors. The institutional investors were generally offshore superannuation funds, pension funds, university endowments, foundations, hedge funds, as well as high net worth individuals and families.[22]

---

18 *Submission 3*, p. 1.

19 *Submission 3*, p. 2.

20 *Submission 3*, p. 2.

21 *Proof Committee Hansard*, 12 November 2014, pp. 30–31.

22 *Submission 135*, p. 6.

16.23 The liquidators of the Timbercorp Group, KordaMentha, informed the committee that while the schemes did not continue, the 'sale assets to well-resourced operators was ultimately to the benefit of the industries and communities of which they were a part'.[23] It noted that similar to the restructure of the olive asset, there has been:

> …the sale of the assets relating to the forestry, almond, citrus and table grape MIS to operators with the financial capacity to properly maintain and harvest the crops, and provide employment opportunities in rural communities, into the future.[24]

16.24 Likewise, the ANZ informed the committee that the underlying agricultural plantations sold by the Timbercorp liquidator were operating successfully 'after market conditions improved and the drought broke'.[25]

Reforming the system

16.25 The Australian Forest Products Association also acknowledged the damaging and disruptive effects of the collapse of many forestry MIS companies on investors and across the broader plantation forest products industry.[26] It formed the view, however, that 'subject to appropriate standards of due diligence and corporate governance, the MIS structure and plantation taxation arrangement should continue to be available to support new plantation investment'.[27] It referred to an issue that had been raised previously, but not addressed by changes to the tax act following the Plantation Taxation Review—the appropriateness of the upfront fee model used by most forestry MIS companies for projects that have a lifespan of 10 years. It stated:

> While the main costs associated with a forestry MIS project are incurred in the first three years, related to plantation establishment, including forming access roads, site preparation, tree planting and clearing of competing vegetation, there are also some ongoing costs, such as lease payments for land, maintaining fire breaks and monitoring for pests and disease. Given the financial challenges faced by many major forestry MIS companies following the GFC, questions were asked as to whether forestry MIS companies maintained sufficient cash reserves to cover these ongoing costs.[28]

16.26 According to the Australian Forest Products Association such concerns and doubts about the viability of established forestry MIS projects could be addressed. It proposed that forestry MIS companies that accept upfront payments from retail

---

23 KordaMentha, additional information provided on 4 December 2014, paragraph 19.

24 KordaMentha, additional information provided on 4 December 2014, paragraph 21.

25 *Submission 145*, paragraph 19.

26 *Submission 126*, p. 2.

27 *Submission 126*, p. 2.

28 *Submission 126*, p. 17.

investors to cover the life of a project 'be encouraged to maintain a reserve account, with sufficient funds held in trust to cover any ongoing costs'. As an alternative, it suggested that companies managing retail forestry MIS projects 'be encouraged to adjust their fee model, to involve a large initial payment to cover plantation establishment, as well as a small annual payment to cover ongoing costs such as land lease payments'.[29]

16.27 Addressing the particular matter of long-rotation crop, Ms Davis noted that any future tax concessions need to be considered 'really long and hard'. In her view, if there were to be tax concessions, they needed 'to be targeted to the production, not to the tax benefit that comes out at the end'. In essence, they would need 'to be much more agriculturally focused than commercial-output driven at the end'.[30]

16.28 Trees Victoria also argued that despite the disappointing performance of a number of MIS, the 'model still has merit and it should not be a case of "throw the baby out with the bath water"'. It noted that the key driver for new plantations is Australia's need to expand its commercial forest plantation estate to meet the forecast future demand for timber and related products.[31] Trees Australia observed that in the wake of the MIS collapses, most new entrants were not interested in establishing new plantations because they understood the schemes were 'too risky' and the returns not sufficiently high. It noted that current interest was directed at purchasing and managing the established MIS estate and 'reaping the rewards of picking up a distressed asset'.[32]

16.29 Based on its experience in the forestry business, Trees Australia recognised the 'difficulty of having any organisation invest in the establishment of new plantations, without a tangible incentive'.[33] It explained that the managers of both government and the larger privately owned plantations have problems finding the funds to re-establish harvested plantations let alone expand into new areas, and further:

> The 'missing link' is investment in the creation of the plantation and development in the early years. **MIS is and must remain one of the mechanisms for creating new forestry managed investments in Australia**.[34]

16.30 Overall, Trees Victoria argued that, with improvements to procedures and better targeting of appropriate investors, the basic MIS concept has 'a valid and

29 *Submission 126*, p. 17.

30 *Proof Committee Hansard*, 5 August 2015, p. 26.

31 *Submission 137*, p. 1.

32 *Submission 137*, pp. 1–2.

33 *Submission 137*, p. 2.

34 *Submission 137*, p. 2, (emphasis in original).

important role to play in the future development of new plantations'.[35] It recognised that the taxation incentive was a very important factor in attracting investors and should be 'fine tuned' in order 'to increase the pool of sophisticated investors who will invest in the long rotations plantations'. Trees Victoria cautioned that legislation should not generate unintended consequences and suggested:

> The initial focus of MIS on short rotation eucalypt timbers largely for export has been shown to be the wrong direction. For long term (25 years plus) forestry investments, such as softwood plantations being grown for sawlogs, the missing link may be the first 15 years of the plantation. Once a softwood plantation is around 15 years old and been thinned, and is a well-managed plantation in a location where there are stable long term timber markets, then those plantations become attractive to the kind of companies which have purchased the large scale forestry plantation assets in Australia over the past 10 years or so.[36]

16.31 AgriWealth also contended that there was nothing wrong with granting a tax deduction to plant trees. It rejected the notion that the recent MIS collapses arose because the legislation allowed an investor a tax deduction to plant trees. It argued that the collapses arose because of the mismanagement by those entrusted with the responsibility to manage the respective plantations properly. It also observed that recently institutional investors were 'primarily acquiring the plantations established by the failed MIS companies'. It reasoned that:

> Those same plantations will deliver significant profits to their purchasers. There is nothing wrong with the plantations—only those who could not carry out their stewardship in a commercially responsible manner. The tax incentive was offered so as to attract capital into establishing plantation timber—the incentive achieved its actual purpose.[37]

16.32 Recognising that many of the individuals who invested in MIS suffered significant financial losses, AgriWealth suggested tightening regulation around the actions of financial advisers, including better disclosure, or alternatively restricting the offer of MIS to wholesale investors only.[38] AgriWealth noted:

> Forestry MIS projects form an integral part of plantation timber production. Whilst institutional investors participate in the forestry/timber sector they generally enter the sector after establishment risk has been eliminated. For example, in relation to long-term saw log timber institutions generally enter the market when the trees are around 15 years of age. At this time the institutions are able to more accurately determine the growth rate of timber for each specific plantation and therefore the relevant purchase price. Their entry occurs after establishment risk has passed.

---

35 *Submission 137*, p. 2.

36 *Submission 137*, pp. 3–4.

37 *Submission 138*, p. 2.

38 *Submission 138*, p. 2.

> Institutional investors will not replace individual investors in fulfilling the need to plant new plantations. Without incentives being offered to individual investors no new capital will be attracted to new plantation establishment other than from government.
>
> We consider that the forestry MIS sector is an important and valuable contributor to plantation establishment, production and the growth of carbon sequestration. The establishment of more plantation timber in Australia will benefit rural and regional employment, Australian GDP, Australian self sufficiency of saw log timber supply and allow Australian individual taxpayers exposure to a high performing asset class.[39]

16.33 Chartered Accountants Australia and New Zealand (CA) supported the concept of managed investment schemes as they provide 'an option to bring capital to rural Australia which would not otherwise occur'. It also noted other benefits such as increased employment opportunities. CA conceded, however, that aspects of the MIS appeared to 'skew parts of the industry and that the agribusiness industry grew to become larger than the intended objectives of the original model and structure'.[40] Given the apparent distortions caused by MIS schemes, CA suggested that arguably the schemes 'should only be allowed where there is a national interest element, such as becoming self-sufficient in wood pulp production, or preventing the destruction of rainforest in other countries'.[41]

16.34 TFS, the biggest sandalwood grower and manager of Indian Sandalwood in the world, has transitioned from 'a pure MIS operator to a more diversified business including Sandalwood production and marketing and an institutional investment programme'.[42] In recent years, it has diversified its funding base to include institutional investors, arguing that:

> …this mix of Institutional and MIS investment is a reciprocal vindication of this forestry investment model and one that will ensure TFS' strength as it evolves into an industrial company in a truly Australian venture.[43]

16.35 According to TFS, while the MIS philosophy had, in many cases, been poorly implemented, the socio-economic aspirations that drove it were 'as valid today as they were at its inception'. In its own words:

> TFS has tried Forestry MIS and TFS has succeeded. Investors and rural communities have benefitted, and are benefitting from the TFS version of Forestry MIS.[44]

39 *Submission 138*, p. 3.

40 *Submission 143*, p. 2.

41 *Submission 143*, p. 2.

42 *Submission 132*, p. 6.

43 *Submission 132*, p. 6.

44 *Submission 132*, p. 4.

16.36 Addressing the potential weakness of an up-front fee model, TFS has independently introduced measures whereby growers pay one year's management fees and rent up front. It noted that this measure:

> …allows for time to replace the responsible entity in the event of its failure. Similarly the registering of all leases on title provides a further measure to protect the interests of investors. These are measures that could be implemented more widely.[45]

Previous reviews

16.37 In 2005, the government undertook a review of the taxation policy of plantation forestry and, in 2008, conducted a review into non forestry MIS.[46] Since then, there have been major developments that have exposed flaws either in taxation policy and/or its implementation. Now, with the benefit of hindsight from the MIS collapses, the committee suggests it is time to examine the tax incentives and any unintended consequences that flowed from them. In particular, this proposed review should look at the extent to which the tax concessions created distortions.

Conclusion

16.38 The committee identified numerous factors that underpinned the failure of a number of high profile agribusiness MIS, which have caused significant damage to investors, to farmers, neighbouring communities as well as the overall reputation of agribusiness MIS. In this chapter, the focus was primarily on the implementation of the policy designed to attract capital into forestry schemes. There was, however, no single cause for the failure of a number of agribusiness MIS, but a combination of factors including those related to the overall policy designed to encourage investment in MIS:

- poorly managed implementation of the policy objective;
- inadequate tracking of, and reporting on, project performance resulting in poor quality information available to investors and policy makers; and
- poor monitoring and understanding of the tax incentives and whether they were having unintended adverse effects, such as investment in non-commercially viable products or inflating up-front costs.

16.39 As noted earlier, the MIS structure has a number of advantages particularly the pooling of investment funds to achieve economies of scale. Should the

---

45 *Submission 132*, p. 5.

46 In the 2005–06 Budget, the government announced that it would conduct a review of the application of taxation law to plantation forestry in the context of the government's broader plantation and natural resource management policies, Treasury, *Review of Taxation Treatment of Plantation Forestry*, 22 June 2005, http://archive.treasury.gov.au/contentitem.asp?ContentID=997&NavID (accessed 22 September 2015).

government determine that agribusiness or forestry MIS warrant continued government support, then important lessons must be drawn from the MIS failures. First and foremost, policy makers must have before them solid research on, and analysis of, the operation of tax incentives offered for agribusiness MIS.

Recommendation 21

16.40 The committee notes that neither the ATO nor Treasury have undertaken a comprehensive review of the tax incentives for MIS and whether they had unintended consequences such as diverting funds away from more productive enterprises; inflating up front expenses; or encouraging poorly-researched management decisions (planting in unsuitable locations). The committee recommends that Treasury commission a review to better inform the policy around providing tax concessions for agribusiness MIS.

Recommendation 22

16.41 The committee recommends further that the proposed review consider the approach to the incentives offered to investors in agribusiness ventures by other countries such as the United Kingdom to inform the review's findings and recommendations.

Recommendation 23

16.42 In addition to the above recommendation, the committee recommends that the government request the Productivity Commission to inquire into and report on the use of taxation incentives in agribusiness MIS. As part of its inquiry, the Productivity Commission should identify the unintended adverse consequences, if any, that flowed from allowing tax deductions for agribusiness MIS. For example:

- **the potential for mis-selling financial products on the tax concessions;**
- **the incentive for retail investors to borrow, sometimes unwisely, to fund their investment;**
- **whether the taxation concessions:**
  - **became an end in themselves rather than the business model;**
  - **showed up as subsidies to higher cost structures, operations and/or returns to the operators of the schemes; and**
  - **distorted land values and diverted high value farmland into passive monoculture such as Blue Gums.**

16.43 The main purpose of the inquiry would be to draw not only on the experiences of the failed MIS but also the successful schemes to determine whether there is merit in reforming the system of tax incentives and, if so, what those reforms should be.