

I am inspired to make this submission in the face of the substantial adverse publicity that is targeted at this sector of the market annually around this time – and more virulently since the ‘collapse’ of both the Timbercorp and Great Southern structures.

There are a number of advisers and investors who participate (and I suspect will continue to participate) in this market both for financial reward and for altruistic satisfaction. Those of us who are likely to continue their association with the sector will do so provided the financial expectations, measured against the understood risks, satisfy the strategic requirements of the investment portfolio structures we recommend.

Outcomes from an Inquiry such as is being conducted by the Joint Parliamentary Committee will, one would trust, reveal the facts and expose the myths that surround recent reporting about the sector. Importantly, any legislative or regulatory changes to the sector resulting from the findings of this and any related inquiry, should strengthen the sector and give greater confidence to the public to invest in large-scale efficient agribusiness operations.

In the course of this submission I refer to what I believe would give rise to an operating structure that is understandable by advisers, able to be satisfactorily explained to investors and efficiently monitored by regulators.

In my view this is an important part of the economic structure of the agricultural sector in this country: both at the horticultural level; and at the forestry level. The horticultural schemes offer significant levels of efficiency and economic certainty to export markets (subject to the requirements of proper research, use of appropriate land and resources, adequate knowledge and experience in the sector and other key commercial issues). The forestry schemes importance is at least as significant as past governments have confirmed in the establishment of their 2020 Vision for the national plantation estate – and more.

I am further inspired to make the submission on the basis that there has been too much hysteria about the collapse of two commercial enterprises – and the consequent effect on the investors who will lose so much as a consequence of those collapses. At the end of the day, the collapses were of commercial enterprises with whom investors had placed money after having opportunity to consider a range of investment and agricultural risks. Most significantly, the flow-on effect (or contagion) from this hysteria is that investors in surviving schemes, even those with companies (Managers) who operate under totally different models from the two failed entities, have to face the continuous barrage of adverse publicity – in spite of the fact that they have invested ‘with their eyes open’ and will most likely see these investments through to a successful outcome.

In the course of my submission I make the following points in relation to each of the Terms of Reference:

1. business models and scheme structures of MIS:
 - MIS projects should be operated in a way that the financial failure of any one entity in the structure is not fatal to the continuation of the project
 - I have set out details of what I believe would constitute a viable structure for these schemes
2. the impact of past and present taxation treatments and rulings related to MIS:
 - I make the point that the ATO Product Rulings are important to the process and should issue in a timely manner
 - Tax deductibility of relevant costs paid by growers is important in mitigating the 'normal' agricultural pursuits risks
3. any conflicts of interest for the board members and other directors:
 - Conflicts of Interest should be able to be 'structured' out of the process
4. commissions, fees and other remuneration paid to marketers, distributors, related entities and sellers of MIS to investors (including accountants and financial advisers):
 - I put the case that there is reason for paying commissions for adviser distribution of these schemes
 - There appears to be scope for a revision of the way the commission payment is timed
5. the accuracy of promotional material for MIS, particularly information relating to claimed benefits and returns (including carbon offsets):
 - It would be appropriate for government to legislate within any 'carbon credit' scheme as to the appropriate statements that can be made relative to any real or potential benefits to growers
6. the range of individuals and organisations involved with the schemes, including the holders of the relevant Australian Financial Services Licence:
 - Promoters of MIS projects should be precluded from granting Authorised Representative status to 'advisers' who are not otherwise qualified to provide professional financial planning advice
7. the level of consumer education and understanding of these schemes:
 - With a longer sales period, facilitated by earlier issue of ATO Product Rulings, adequate education programs could be provided for potential investor-growers;
 - Requirements of licencees should include demonstration that clients have been afforded an appropriate level of education in relation to the MIS product they are committing to buy into

8. the performance of the schemes:

- Normal rules relating to the 'claim' as to likely performance should equally apply to MIS schemes as to other investment products

9. the factors underlying the recent scheme collapses:

- The collapses are at two levels: and each needs to be understood – the manager needs regulatory prudential control; and the projects themselves should be protected from subscription by entities/ individuals who may not be able to perform their financial commitments to the program;
- Independence of the 'scheme' participants from the management structure is important

10. the projected returns and supporting information, including assumptions on product price and demand:

- Perhaps some guidelines and/ or oversight need to be provided to promoters in this regard
- Whilst some operators have provided reliable data and information, there is a sense that not all have been as open and 'honest'

11. the impact of MIS on other related markets:

- This is an area that requires considerable research and input by economists and residents in the allegedly affected areas

12. the need for any legislative or regulatory change:

- Regulate the structure of MIS projects to protect the investors – and the broader market
- Restructure commissions so that they are paid more in line with the level of activity relevant throughout the course of the project
- Consider a 'cooling off' provision

1. business models and scheme structures of MIS;

The current position in relation to MIS structures is generally accepted to include a Responsible Entity (RE), a Manager and may/ may not include other entities between those and 'the Grower'.

In MIS projects where there is a one-off payment required, such as applies with most forestry schemes, the financial viability of the project is fairly much in the hands of the Manager (as to how well they manage the plantation) and the market.

MIS projects that accept Growers who commit for a particular level of involvement on payment of an 'upfront/ plantation establishment' followed by ongoing annual contributions to the management and land rent costs, are vulnerable to the financial viability of all of their fellow growers as well as the above exposures – to Manager; and market.

This situation is exacerbated by poor prudential practices in the approval process by the RE when considering Grower applications to invest in the project. It is further jeopardized when the Manager (or entities associated with the Manager) becomes one of the Growers with anything more than a 'minimal' share of the project.

It is my opinion that the following entities should be the minimum that should be allowed to make public offers in agribusiness (or for that matter, any) MIS project/ investment (and Table 1 sets out their characteristics and responsibilities/ function):

Trustee
Responsible Entity
Manager
Project structure
Contractors
Growers

Without doubt, each project offered by a particular Manager should be independent of all other projects operated by that Manager: each should be able to demonstrate its 'stand alone' viability.

Table 1 (page 1 of 2)

Entity	Characteristics			Responsibility/ function
	Relationship within structure	Financial structure	Governance	
Trustee	Independent: commercial arrangement	Adequately financially resourced to carry out duties and responsibilities independently of project viability	Appropriately qualified and experienced 'directors' with no Conflict of Interest issues; prudentially regulated	Interposed between Grower and RE; and between Manager and RE. Receives and distributes (or authorizes distribution of) all monies whether by way of investment subscription, product sale proceeds, or expenses allowed under the various commercial contracts involved. Responsible for proper allocation/ use of monies but not for project viability.
Responsible Entity	Separate from Manager: commercial arrangement	Adequately financially resourced to carry out duties and responsibilities independently of project viability	Appropriately qualified and experienced 'directors' with no Conflict of Interest issues; prudentially regulated	Interposed between Grower and Manager. Accepts responsibility that the project is viable; then oversees the implementation process and certifies to Trustee that all commercial obligations and requirements have been met to warrant disbursement of monies. May have role of physical payment of the monies so flowing.
Manager	Commercial arrangement	Minimum capital requirement relative to commitments within the project (each project compounding the financial requirements test)	[Commercial risk for Grower's consideration]	Designs, Costs and Markets the project(s); ensures all necessary approvals in place; engages appropriate contracting services/ advisers to implement the project through to completion – to the satisfaction of the RE. Provides reports and updates to Growers, RE and regulators.

Table 1 (page 2 of 2)

Entity	Characteristics			Responsibility/ function
	Relationship within structure	Financial structure	Governance	
Project structure	Publicly subscribed entity bringing Growers together	Subscribed to minimum requirements to ensure project viability	Controlled by the RE	Accounts for the financial and contractual transactions undertaken for the effective implementation of the project PDS.
Contractors	Commercial arrangement: any involvement by Manager in this capacity to be on 'at arm's length' terms	Commercial risk of Manager	Not important	Fulfill commercial obligations as contracted by the manager
Growers	Owners of specific aspects of the project: whether trees, crops etc – possibly under 'licence'	Ability to fund obligation for entire term of project	Not important	Meet financial obligations undertaken in respect of project; support RE and Trustee as required; respond to reports provided from time to time.

2. the impact of past and present taxation treatments and rulings related to MIS;

As a financial adviser, I have recommended clients to participate in a limited and select group of agribusiness MIS offerings from only two managers. Since entering this industry in 2002, I have researched at least five other manager's offerings: either because clients engaging me for financial advice already held such investments; or in the course of considering suitable options for our clients' financial planning needs, I was seeking information about them.

The projects that I have embraced were recommended to clients on the basis of their structure, their projected financial performance, their compliance with requirements making them eligible for tax-deductibility – and that they made commercial sense.

Agribusiness MIS investments are subject to all the risks of any agribusiness pursuit: climatic conditions; pests; fire; economic factors; environmental issues; markets and so on – apart from the financial concerns of 'co-operative' ventures. The taxation deductibility has, in promoting their use in diversifying our clients' portfolios, been perceived by us as some contribution to ameliorating those risk factors.

The only concern we have with the Product Ruling process is that it appears to take too long from when the Manager submits to the ATO until a ruling is finally published. The ruling is perceived by our clients as serving one purpose only – and that is to confirm the level of deductibility of the investment: at no time do they have a view that the commercial viability of the project is assured by the issue of the ruling.

The present regime for the issue of Product Rulings; and the issues determining the proportion of deductibility – are adequate for current purposes and should not be altered and certainly not withheld. (In relation to the national forest plantation goals, I believe this aspect to be critical to achieving as significant a portion of the 2020 target as is currently on schedule. Withdrawal of the tax deductibility under the PR situation will seriously hamper the attainment of that goal in my view.)

3. any conflicts of interest for the board members and other directors;

The key entities in the structure, being the Trustee, the Responsible Entity (RE) and the Manager should be – and be seen to be – independent in their roles and in their governance.

In Table 1 to this submission, issues such as Independence and Conflict of Interest (COI) are addressed.

Future structures that ensure avoidance of COI issues will provide a higher level of trust and restore confidence in this industry. Managers offering structures that do not have these features will limit the range of potential investors able to be attracted to their offerings.

4. commissions, fees and other remuneration paid to marketers, distributors, related entities and sellers of MIS to investors (including accountants and financial advisers);

I can only speak of my own experience in this area, although I am aware of rumour and speculation about other scenarios. As a financial adviser I have not been offered a situation where any action I take in relation to the commission payable in respect of the investment will have any impact on the price payable by the Grower for their investment.

The majority of projects offered – and substantially that used by our firm – have paid an upfront commission (of between 5% and 10%); and in one case, subject to the level of support from our practice in marketing the project, assistance with the costs of the marketing, not exceeding 2% of the ‘sales’ made. In none of these cases was any ‘trailing’ commission offered.

Whilst the majority of the professional responsibility in respect of any project is accepted and undertaken in the initial year, there is rarely a situation where investors from years previous are not seeking information or guidance in subsequent years.

I would see a situation where a lesser upfront commission is paid, supplemented by a significantly smaller ‘trailing’ commission, would be financially beneficial to financial advisers – and have requested our preferred Manager to consider offering their projects under this model.

5. the accuracy of promotional material for MIS, particularly information relating to claimed benefits and returns (including carbon offsets);

The information that is provided by the two Managers that our firm and/ or our clients have invested with has been substantially accurate in my opinion. It is the information that is not provided that is more concerning.

Where a Manager intends to invest as a Grower in their own right (or through a vehicle within their corporate structure) additional disclosures and notices should be required – and additional, timely audit reporting to fellow Growers to provide assurance as to the ‘going concern’ viability of the entity (and the group).

Whilst there are reports that the claims in some of the promotional material have been misleading, what has been provided by way of support has always (with the Managers we have used), cautioned against accepting provided projections: and have provided ‘calculators’ that allow the prospective investor to enter their own assumptions and ‘stress test’ the investment.

The claims and disclosures regarding carbon offsets by the forestry Manager that our firm has supported has been quite clear about the ‘remoteness’ of any financial benefit from the investment – merely assuring investors (in recent years at least), that where such a financial credit arises at some future time in respect of their project, their share of such benefit is specified.

6. the range of individuals and organisations involved with the schemes, including the holders of the relevant Australian Financial Services Licence;

Our firm is a Corporate Authorised Representative of an Australian Financial Services Licencee; and individually, our financial planners are licensed under the ASIC regime. The agribusiness MIS products we offer to our clients are required to be listed on the agribusiness Approved Product List (APL) under the Policy and Compliance guideline regime of our Dealer Group licencee.

7. the level of consumer education and understanding of these schemes;

To the extent that there has been a shortcoming of consumer understanding of the agribusiness MIS schemes, it at least to some part occurs because of the timing of the availability and the link to the year-end tax planning process.

If the projects were available all year round, there would not be the rush by financial advisers to comprehend the project and the issues involved in the offering – and the client education process could be more effectively delivered.

Of some interest in considering this term of the Committee's reference in this Inquiry, is what aspects of 'the schemes' the investor should be expected to be educated about: should it be significantly different from what they might understand about a 'traditional' managed fund for instance? Or, should there be special requirements to understand the agricultural risks?

The Dealer Group through which our firm is authorized to advise on such schemes, requires us to assure that the financial risk profile of the client is sufficiently high to be able to cope with the elevated risk features of such investments. They also impose financial limits on the allocation of the clients' investment in such assets in any year: and is borrowing is used to fund the investment, we have to satisfy the Dealer Group that the client has the capacity to meet their ongoing obligations.

Ultimately, clients seeking professional advice expect to be able to leave some of the knowledge about the products used in implementing their investment strategies in the hands (and files) of their professional advisers.

8. the performance of the schemes;

Whilst this should be a matter for the public record, the fact is that many of these schemes are only recently reaching their maturity.

A forestry company with which we are familiar has harvested its first agribusiness MIS project; and has sufficient plantation data regarding the second to reasonably calculate its outcome – to show that investors in those two projects (in the first case, have already; and in the second case, should) realise in excess of 7% p.a. compound from their investments on an after-tax basis, calculating for tax at the highest Marginal Tax Rate both with the original investments and on receipt of 'harvest' proceeds.

9. the factors underlying the recent scheme collapses;

I could only speculate on this front – and join a large number of people who suggest that the Global Credit Crisis may at least be in part to blame for the collapses. For me, I trust that the respective insolvency practitioners' reports may give us the real reasons: and that your inquiry might also shed more discerning light on the underlying factors.

The only information that I can see that is of concern for Growers and that was not obvious – or even apparent – prior to the lodgement of recent Court documents, is that it was inappropriate for Timbercorp to be a significant Grower in its own right in the Almond and Olive schemes. Their insolvency has at least in part, resulted in the likely winding-up of those schemes to the detriment of the 'retail Growers'.

10. the projected returns and supporting information, including assumptions on product price and demand;

In making personal and professional investment decisions in relation to these products, we have exercised conservatism in our projections for clients: the basis of the investment decision takes into account all of the risks – and never focuses on any promise of significant returns. Returns in any investment product can come in either of two forms: a return based on the original capital (that is, it is preserved at its original level; it shows growth – which may or may not compensate for inflation in the interim; or it is discounted by economic or market activity); and on income.

Agribusiness investments usually only arise from the sale of 'produce'. The returns from this are for investment purposes, calculated relative to the original capital committed to the project.

Any promotion of these projects on the promise of any level of return could be misleading: reporting of actual returns from past projects – and of the factors that prevailed in those circumstances, relativity to current promotions – are legitimate in my view. Legitimate though, subject to the proviso that past performance is no guarantee of future results.

As stated earlier in this submission, there are reports that the claims in some of the promotional material have been misleading, but my experience with the Managers our firm has used, has been that the guidance has cautioned against accepting projections at face value: and they have provided 'calculators' that allow the prospective investor to enter their own assumptions and 'stress test' the investment.

11. the impact of MIS on other related markets; and

Agribusiness MIS investment appears to be undertaken by two categories of investors within my experience: there are those who do not trust equities and only participate in the traditional investment market through their compulsory superannuation accounts; and the others who use agribusiness MIS for a variety of investment strategies, including diversification.

In the former case, the investment has no impact on the other investment markets; in the latter, the impact has the effect of reducing the volatility of the portfolio – but also the amount available to be invested into it.

No doubt, in relation to the markets for the actual products resulting from these projects, there are impacts such as lower-cost efficiencies from broad scale agribusiness pursuits; certainty of economic quantities for product from a grower of produce with a predictable quality standard; quantities of produce viable to sustain the market for, and generate export income – and to those extents, will have impact on the other operators in the respective industries.

12. the need for any legislative or regulatory change.

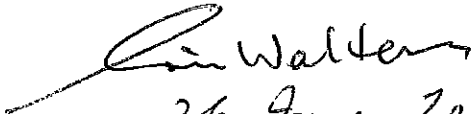
It appears to me that some of the practices that are rumoured to have existed as between certain MIS managers and advisers 'distributing' their project products (and that have been widely reported in the daily media), that there are elements of the distribution remuneration process that require regulatory attention.

Those who distribute these projects and who are motivated mainly by the commission receivable for such activity, will be less inclined to under-educate their clients if –

- a) the projects are available for a longer duration each year; and
- b) the commission receivable rewards them:
 - a. reasonably for the significant workload to initiate the investment; and
 - b. adequately for the ongoing support of the client during the term of the investment.

I believe that the project availability duration will have a greater impact on the level of understanding by the ultimate grower-investor than the commission payable to the adviser.

A further legislative or regulatory change that might effectively be contemplated, would be to facilitate a 'cooling-off' period of up to 28 days where the project is available for a period in excess of 180 days before its closure for any particular financial year (as measured from the date of release of its Product Disclosure Statement, accompanied by the Product Ruling from the ATO).


26 June 2009.