

Victorian Farmers Federation Sunraysia Horticultural Branch

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Submission to the Australian Treasury Review into Non Forestry Managed Investment Schemes.

History of Branch Opposition to MIS

This branch has opposed the continuation of taxation benefits for horticultural MIS since the industry developed and accelerated over the last decade in the North West of Victoria and neighbouring regions.

The branch has been particularly concerned about the take up by MIS of the scarce water resource, the distortion of commodity markets including for wine grapes, and the ongoing removal of economic opportunity for legitimate non subsidised producers. This concern has been heightened given the context of the Sunraysia district's ongoing economic decline and the continuing downward spiral in the terms of trade confronting producers.

The branch has been politically active in opposing MIS, and was instrumental in having the benefits removed in February 2007. Notably, the benefits were reinstated until June 2008 following outcry from the industry and MIS activity has since intensified.

Reservations Regarding the Treasury Review and the Issues Paper

The issues paper relating to this review presents the substantive issues surrounding MIS as being as yet undecided and still open to debate. This is not in fact the case; the previous government was compelled to withdraw benefits for Horticultural MIS for good reason after many reviews involving intensive research and objective debate.

This review is going over old ground, though it does have the advantage of being able to witness the ongoing explosion of MIS activity vis a vis the catastrophic decline in the Murray Darling Basin water resource.

This review is referred to the work already done on MIS by the Rural Industries Research and Development Corporation (RIRDC Publication No. 05/078, project No AWT-1A)

This document, entitled the Economic Effects OF Income Tax Law on Investments in New and Emerging Industries sufficiently summarises the legislative and regulatory background circumstances of the MIS industry, and the history of government review.

The RIRDC report, taken together with previous work by government, ongoing input and commentary in industry publications and submissions to government, ongoing attention and commentary in academia and in the financial press and industry trade press, puts the case incontrovertibly that-

- 1) The MIS industry is an arm of the tax avoidance industry, artificially creating and bundling tax deductions for on selling to investors interested primarily in obtaining a taxation advantage

- 2) resources of capital and water are being allocated on the basis of the obtaining of taxation advantages, and that therefore

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- 3) Those scarce resources are, ipso facto, being misallocated. This misallocation is to the economic disadvantage of a) the taxpayer and the government, and b) existing producers.

An egregious example of disadvantage to existing producers was the open ended activity in the temporary water market by MIS in November of 2007 which pushed the price of temporary water to \$1100 for legitimate producers.

- 4) MIS effectively have open slather to sell deductions, unrestrained by an effective regulatory framework. Three brief points from the RIRDC report worth noting are that a) “..it is odd and disturbing that no meaningful data on the performance of MIS is sought or maintained by ASIC.”
b) “..there is no tracking system whereby key data defining economic performance of schemes is supplied by MIS operators and made publicly available”
c) “... of those MIS for which performance data could be gained, the overall performance against budget, and hence return to investor, is poor.”

Economies of Scale

The Issues Paper presents uncritically the MIS so called argument about economies of scale. That is, that MIS can afford large scale production and achieve economies of scale. The argument is a furphy on several grounds.

- 1) if valid economies of scale do exist in a particular sector of horticultural production, they are available to any enterprise with a conventional financial structure, and not just to MIS.

Conventional enterprises taking advantage of possible economies of scale are far more likely to achieve a valid economic outcome with respect to the resources consumed than are MIS because the imperative driving conventional enterprises is a return on funds invested directly in the enterprise.

In contrast, the MIS enterprise is one entity in a chain of entities artificially constructed in order to yield tax deductible items for sale in order to yield profits for scheme promoters. Most of the money gets blown in fees, charges and commissions. This artificiality is another aspect of MIS the Issues Paper has failed to properly reference

- 2) Economies of scale is an overused and invalid propaganda item employed by MIS promoters to advance their position. Successful enterprises are predicated on involvement and commitment, as with conventional corporate farms and owner operated enterprise. In fact diseconomies of scale are a real factor militating against the economic validity of MIS enterprises.

Reservations as to the True Purpose of the Treasury Review

Given the above points relating to the format and tone of the issues paper, this branch has doubts as to the bona fides of the Treasury Review. These doubts are amplified by

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the absence from the issues paper of any reference to the intense political activity and financial patronage of politicians conducted by MIS promoters and their supporters.

The review is shaping up to be the instrument by which the present government, in response to this ongoing intense lobbying and patronage by the MIS lobby, could move to accommodate and validate Horticultural MIS through new legislation. Such legislation will purport to tighten the legislative framework in which MIS operate. In reality the legislation will be a payoff for MIS patronage and will enable the continuation and acceleration of the taxpayer funded corporatisation of resources and opportunity in rural Australia

The branch has firm views about the economic, social and political realities surrounding MIS which it is keen to emphasise to the review in the remainder of this submission.

The Political and Economic Realities of MIS in Sunraysia and Other Regions

The core business of MIS is the creation and on selling of tax deductions. MIS have achieved hegemony at all levels of government including local government, and have penetrated and control, or are influential, in most industry groups and representative bodies including HAL and HAC.

MIS donate heavily to political parties, and patronise influential charities and sporting and other groups in order to curry favour and spread influence.

MIS have direct and highly influential lines of communication and influence with government, notably in Sunraysia with the Victorian Department of Primary Industries and the Department of Sustainability and Environment.

The expansion of MIS activity in irrigated horticulture is heavily relied on and promoted as the primary economic driver around the Swan Hill region by government. The Swan Hill City Council has an economic development board whose primary focus has been to attract around \$2 Billion in MIS development over the last eight years.

Mildura Rural City Council likewise has a similar development body (SMEDB) keen to attract MIS development. Government is working with these bodies to recast Sunraysia's destiny as a centre for corporate horticulture.

This will be achieved by using Lower Murray Water (incorporating the recently wound up First Mildura Irrigation Trust) as the vehicle for expanding irrigation to the South and West of Mildura. The plan is premised on supplying tax advantaged farms (MIS) as distinct from non MIS enterprises because of the high cost of supplying water to the new regions, over \$400 per Meg.

MIS are Subsidised and Distortionary and Lead to Corrupt Economic and Social Outcomes.

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MIS are subsidised and distortionary by definition. They present themselves as superior operators out competing conventional enterprises on a level playing field, but the reality is that they operate on a completely different principle and do not compete at all in any real commercial sense in that there is no overriding imperative to obtain a legitimate, accountable return on funds invested. Examples of failure abound.

One current example of MIS failure the review should note is Palandri **Vineyards** in Western Australia.

Wine Grape Over Supply

The review is also referred to the work of wine sector specialist valuer Sam Paton of Sam Paton and Associates (Ballarat). Paton and other wine industry operatives and growers analysts attribute the wine industry production overhang of around 20% to the unscrupulous activity of the MIS industry (Grape Grower's Magazine April 2007). One example of wine industry distortion involving MIS was the purchase of the Tandou vineyard at Lake Cullulleraine in Northern Victoria by Great Southern for \$7000 per HA, and the on selling to investors interested in taxation benefits for \$70,000 HA.

The wine industry is currently in surplus despite the drought, yet currently thousands of hectares are being developed by MIS in Sunraysia and the Barossa Valley and elsewhere, over inflating production capability and destroying the prospects of existing growers and their communities.

The HAL Report into MIS (Econtech 2007)

This review is directed to the supposedly independent HAL Report into MIS. This review was in fact paid for by the AIMA, the MIS industry association and is a whitewash and a self serving restatement of MIS industry propaganda.

The HAL report made a point of not including wine grapes in the commodities studied, not surprising considering the devastation wrought on growers in the Murray Valley by MIS induce overproduction, especially in the years 2005 and 2006.

David Cornish, Robert Belcher (SACA)

This review is likewise referred to commentary on MIS by David Cornish of Mike Stephens and Associates Ballarat, and by Mr. Robert Belcher of Sustainable Agricultural Communities of Australia.

These commentators have proven beyond doubt that MIS are subsidised to compete unfairly with non subsidised conventional producers for resources and economic opportunity, and together with Forestry MIS have devastated and continue to devastate rural communities and dominate water supplies.

MIS in Sunraysia. Water Barons. Non MIS to be Forced Out.

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The government's position on MIS following the completion of this review will determine the future viability of non MIS enterprises in Sunraysia and other irrigated regions along the Murray Valley.

Should the government permit continuation of taxation benefits for horticultural MIS, then the result will be the progressing of current and new projects around the Swan Hill Boundary Bend Region. This expansion will take plantings from around 30,000 HA using 300 GL of water to up to 60,000 HA using 600 GL of water.

Around Mildura, the resultant expansion of irrigation would see an additional 40,000 HA of plantings requiring 400 GL of water in less than 10 years, and in as little as 6 to 8 years.

Given that the typical MIS product has a life of 20 years, the net result of the taxation regime would be that up to one thousand gigalitres of increasingly scarce and valuable water would be gifted in perpetuity to the tax avoidance industry courtesy of the tax payer.

This would be an economically and socially unacceptable outcome which this branch rejects totally.

POLICY SUBSTITUTE

MIS have been and continue to be an easy option for government to exploit in order to attract investment to regional areas. This has been increasingly the case as the rural downturn deepens and broadens on the back of the government's foolish and destructive commitment to the unilateral pursuit of Free Trade.

As efficient and committed growers are driven out of business by subsidised imports and one sided FTA's, governments and politicians continue to promote MIS as the replacement for the economic and social disinvestment their policies have caused.

This branch demands that government acknowledges the destruction its misguided trade unilateralism has caused and continues to cause, and address trade policy in a balanced and pragmatic way. This continued promotion of MIS as a substitute for genuine engagement and pragmatic policy formulation must cease.

Conclusion.

Given the above, the view of the branch is that this review must find that horticultural MIS are economically and socially invalid. The review should accordingly recommend unequivocally that the government move to legislate against the reinstatement or continuation of the artificial taxation benefits which make horticultural MIS possible.

Yours faithfully, W. T. McClumpha 11/09/08.