SUBMISSION

BY

TULLY SUGAR LIMITED

TO THE

SENATE RURAL AND REGIONAL AFFAIRS AND TRANSPORT COMMITTEE

INQUIRY INTO

"THE IMPLEMENTATION, OPERATION AND ADMINISTRATION OF THE LEGISLATION UNDERPINNING CARBON SINK FORESTS AND ANY RELATED MATTER"

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28th July 2008

Summary:

This submission is made by Tully Sugar Limited to the Senate Rural and Regional Affairs and Transport Committee inquiry into “The implementation, operation and administration of the legislation underpinning Carbon Sink Forests and any related matter”.

Tully Sugar wishes to place information before the Senate Committee regarding Forestry Managed Investment Schemes (MIS) and the threat posed by these taxation subsidised schemes to the future sustainability of the Sugar Industry in the Tully region of Far North Queensland. We believe that the intrusion of Forestry MIS into the sugar industry in the Tully area is a related matter being investigated by the Senate Committee. The threat to the sugar industry posed by the taxation subsidised Forestry MIS already exists. What is being proposed by the favourable taxation treatment for Carbon Sink Forests will place even more pressure on the viability of Tully Sugar Industry and the long term economic stability of the local Tully community. It will further increase the loss of Good Quality Agricultural Land (GQAL) available for sugar cane production and reduce the areas and indeed the Nation’s capability to produce food, fuel and energy from the sugar cane crop in future years.

Tax assisted forestry schemes have been established in many regional communities in Australia and have impacted on the agricultural businesses and the economies of those communities. The motivation for these schemes has been the taxation benefits which have been preferentially provided to the Forestry MIS investment model rather than a profitable business investment. A typical investment promotion by these Companies is attached (Appendix 1).

Tax subsidised Plantation Forestry Companies are now being attracted to the sugar cane growing areas in Central and Far North Queensland because of the abundance of rainfall and water in these areas and consequently Good Quality Agricultural Land (GQAL) is being lost.

Tully Sugar wishes to emphasise the following points –

- Since 2005 the Tully sugar industry has lost 3,000 ha of cultivated Good Quality Agricultural Land (GQAL) from sugar cane growing to MIS Plantation Forestry and a further 2,525 ha of potential sugar cane growing land to MIS Plantation Forestry.

- There are three Companies, Great Southern Managers Australia Limited, ITC Timberlands Pty Limited and The Ark Fund (Rewards Group) operating in the Tully area.

- The agricultural land market in the Tully area has been distorted by the capacity of the MIS promoters to offer short term taxation benefits to investors which has resulted in large cash raisings for the purpose of establishing plantation forests on Good Quality Agricultural Land.

- Sugar cane growers who wish to expand their land ownership and improve their economies of scale in their businesses have been unable to match the land prices offered by the MIS Companies.

- The land lost from sugar cane production to plantation forestry is permanently lost for future food production and future renewable energy production from the sugar cane plant in the form of either renewable electricity or ethanol.

- The Centre for International Economics (CIE) report "Sugar v's Forestry in Queensland" commissioned by Australian Sugar Milling Council in October 2007 identified the following scenario for a town (like Tully) built around the sugar industry:

    - eventual mill closure as a result of production area loss;
    - growers unable to recover their investment in their current sugar cane production;
    - stranded sugar producing assets;
    - lost local economic activity;
    - declining town populations; and
    - redundant town infrastructure.

- The Australian Government needs to correct the unfair taxation laws which are creating the imbalance in favour of the Forestry MIS industry over the sugar cane growing sugar production industry.

- The largesse provided by the Australian Government on an unconditional basis to entrepreneurial investment in the agricultural sector by retail fund managers is threatening this crucial national resource. It must stop before it is too late!

Background:

The Tully Sugar Industry is located in the new Queensland regional shire of the Cassowary Coast Regional Council which was an amalgamation of the Cardwell Shire Council (centered in Tully) and the Johnstone Shire Council (centered in Innisfail). In the last ten years, cane production has ranged from 1.518 million tonnes cane from 23,774 hectares in 2001 to 2.415 million tonnes cane from 24,843 hectares in 2005. In the same period sugar production has ranged from 200,000 to 315,000 tonnes sugar per year. Production in 2008 season is forecast at 250,000 tonnes sugar from 1.950 million tonnes cane from an available 22,300 hectares.

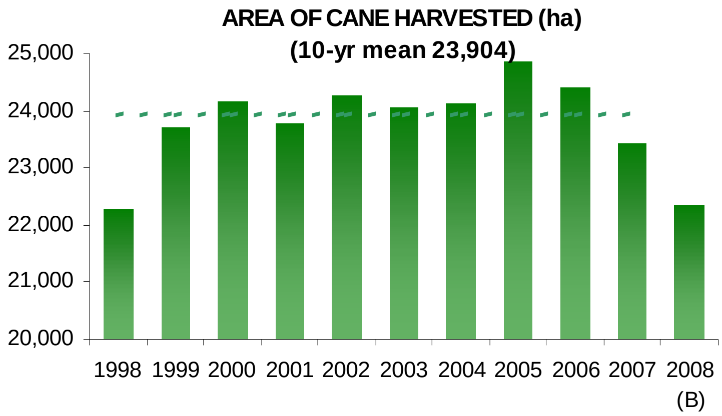
The Tully Mill was constructed in 1925 by the Queensland Government and was privatised in 1931 to become Tully Co-operative Sugar Milling Association Limited. It was registered as a public unlisted Company (Tully Sugar Limited) in March 1990. This change in Company structure facilitated an expansion of the industry following deregulation of the Sugar Industry Act at that time.

The Company provides full time employment for 200 people, increasing to 300 in the cane crushing season (mid June – mid/late November). It is estimated that approximately 1,200 people are directly and indirectly employed in the local sugar industry in the cane growing, harvesting, milling, product transport and associated service industries.

Tully Mill has significantly diversified its income base into value added opportunities such as the development of a domestic molasses business for the beef and dairy industries and the production of renewable (green) energy into the Queensland electricity grid.

Since 2005 the Tully Sugar Industry has lost access to 3,000 hectares of Good Quality Commercial Cane Farming Land as a result of this land being purchased by the promoters of Plantation Forestry Managed Investment Schemes (MIS). The activity of Forestry MIS in the Tully area accelerated in 2007 following the abolition of taxation advantages for non forestry MIS. This saw investments seeking tax advantages transfer to the Forestry Managed Investment Schemes.

The variation in harvested cane area in Tully in the period 1998 to 2008 (B) is shown in the following graph.



The area available for harvest in 2008 season includes an area of approximately 1,100 hectares from the non traditional Tully area that has transferred to Tully Mill for crushing under commercial cane supply arrangements. The forecast 2008 season cane crop in Tully is 1,950,000 tonnes which is based on an average cane yield of 87.5 tonnes cane per hectare and available area of 22,300 ha.

The three Forestry MIS Companies active in Far North Queensland, have indicated a combined requirement for 3,000 ha of land per year in the region Ingham to Innisfail in each of the next 15 years.

Three sugar production companies operate in this region, CSR in Ingham with two mills Victoria and Macknade, Tully Sugar Limited with one mill in Tully and Bundaberg Sugar Limited in the Babinda/Innisfail area with two mills, South Johnstone and Babinda. If it is assumed that only 1,000 ha of this land is acquired each year from the commercial cane farming land available in the Tully area then in 15 years the cane area supplying Tully Mill would reduce to approximately 7,000 hectares. Such an area, in an average year, would produce a cane crop of 612,000 tonnes (7,000 ha x 87.5 t/ha).

However the reality is that the Tully Mill would have been forced to close well before this 15 year horizon due to the unsustainability of operations at low available cane tonnages.

This serious scenario is a direct consequence of the short term tax offset benefits for investors into the forestry MIS. The favourable treatment for investors in Forestry MIS over commercial cane farming activities has created a distortion in the market for quality agricultural land in the Tully area in Far North Queensland.

Proof that the Managed Investments Schemes are responding to demand for tax minimisation offsets rather than attempting to maximise economic benefit from land use in the area has been highlighted when cane was harvested and destroyed in April/May this year on two farms purchased by ITC Timberlands Limited in the Tully area. This operation was completed to expedite tree planting ahead of the end June 2008 taxation year deadline.

The proof is in the following photos of Farm 1 and 2. Is this an example of healthy competition on a level playing field?

Farm 1:

Mature cane crop being harvested and dropped on the ground prior to 30th June to obtain tax breaks. Note cane railway line in foreground.

Cane destroyed by burning on ground.

Trees now planted on former cane growing land.

Farm 2:

Mature cane crop being harvested and dropped on the ground.

Extent of cane area harvested.

Depth of destroyed cane on ground.

Trees now planted on former cane growing land.

In all approximately 12,500 tonnes cane was destroyed. The value of the lost sugar production from this cane is approximately $500,000 (value 12,500 tonnes cane @ 13.00 ccs @ $305 tn = $495,625). When the value of value added opportunities lost such as molasses and electricity co-generation are included the gross value of the lost cane is $540,000.

Since mid 2007 Tully Sugar Limited has been campaigning vigorously against the unfair tax advantage granted to the Plantation Forestry MIS. Company Chairman Dick Camilleri and myself as General Manager have written to State and Federal Politicans in the major Parties, provided press releases and conducted media interviews in attempts to increase political and public awareness about the potential plight of communities built around the sugar industry.

At the workplace, Unions are becoming increasingly concerned at the loss of skilled job prospects in the Mill as the available cane crop diminishes. This prompted a resolution from the AMWU (Australian Metal Workers Union) at the recent Queensland State ALP Conference seeking the restriction on further sale of prime agricultural land to non food growing activities.

At the Community level similar concerns have been raised at the local Chamber of Commerce meetings where members are fearful of the impact that reduced economic activity will have on local businesses.

Politically there is an increasing awareness that the unfair taxation system provided to Plantation Forestry Managed Investment Schemes has provided “unintended consequences” for the sugar industry in Central and Northern Queensland and has already diminished the Nation’s capacity to produce food, fuel and energy in the future.

<u>The Sugar Industry and Climate Change</u>:

Much has been said recently about the impacts of Climate Change on our future way of life. The sugar industry has the capacity and capability as a generator of renewable energy to play a significant role through incentivised capital intensive projects to increase the amount of renewable energy generated in Australia.

Further, at the Australian Government 2020 Summit Canberra earlier this year the significance of the wet tropics in particular and northern Australia in general, in providing future food production for Australia and the Asian region in a time of reducing and unpredictable rainfall in southern areas was recognised.

Continuation of a Federal Tax policy that encourages investment in timber plantation on good quality agricultural land in a potential food bowl ignores this recognised national imperative and threatens the availability of this crucial national resource.

Sugar Mills already export renewable electricity into the National Electricity Market which avoids an equivalent of 1.1 million tonnes of carbon dioxide (CO_2 e) that would otherwise be produced by coal fuels. Tully Sugar Mill is an efficient and very reliable source of renewable energy. We now export up to 10 MW per hour through a dedicated 10 MW Siemens steam turbine generator during the crushing season. At this level Tully Mill is actually providing power to 4,000 homes in the local area. For example from the 2005 season Tully Mill exported 33,390 MW which in effect meant that the 4,000 households at an average usage rate of 2.5 Kw of 2.5 Kw per hour were powered for 139 days (33,390 MW/2.5 x 24 x 4,000) by renewable electricity generated at Tully Mill.

We see potential to significantly increase our renewable electricity generation with consequent positive climate change outcomes from an expansion of our current generating capacity. The recently announced extension to the renewable energy target and the policy settings contained within the scheme moves sugar mills, including Tully Mill, closer to realising the potential. However Tully Sugar will not be prepared to risk the investment required for increased co-generation with the continued threat of Plantation Forestry MIS continuing to expand in our area and replace cane production.

There is a body of opinion in the Australian and global community that planting trees is an effective means of offsetting/neutralising CO_2 e in the atmosphere. This is evidenced by the taxation benefits proposed for carbon sink forests which is the subject of the matter before the Senate Committee.

Tully Sugar Limited contends that it is premature to provide such support to Carbon Sink Forests without a review and assessment of sugar cane, which is a renewable crop, to provide a form of carbon sequestration.

The further promotion of tree plantations in our area through the provision of taxation advantages will further aggravate the economic and social impacts on the Tully Sugar industry and associated community caused by the loss of cane growing land to Plantation Forestry MIS.

The Way Forward:

We understand that the former Federal Government planned a review of Forestry MIS by the end of 2008. We urge this Senate Committee to recommend that such a review be expedited because of the ongoing consequences of the existing policy in distorting the market place for land in Tully and threatening the survival of the Tully sugar industry and local community.

One option that the Committee could consider for recommendation to the Government would be to more closely define the eligibility criteria for MIS Forestry taxation arrangements in a way which ensured there is a recognised and valid regional and national benefit from such activities that exceeds the taxation revenues foregone which support them. It is also proposed that Plantation Forestry be restricted to marginal lands and hence protect commercial farming operations on Good Quality Agricultural Land (GQAL). Such an approach is being proposed in Tasmania following a recognition that the States ability to produce food in the longer term is being undermined by the expansion of MIS.

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within reach of everyone

Most Australians would like to benefit more from the income they earn throughout the year and many seek ways to maximise their annual tax refund. Others take this a step further and utilise tax planning strategies to help reduce their taxable income and provide a foundation for creating wealth.

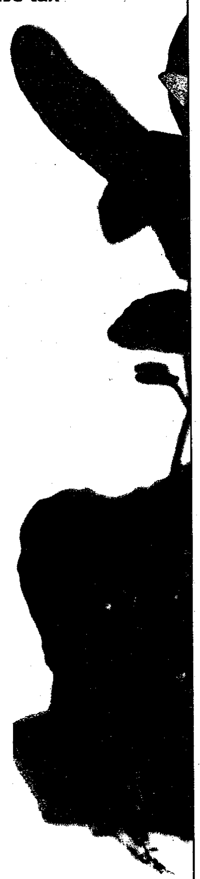
The goal of tax planning is to create wealth by generating more out of the income you earn and reducing the amount being taxed at your highest marginal tax rate. If you thought this type of planning was reserved for the wealthy, you should think again - tax planning is within reach of everyone.

An increasingly popular solution, which combines the benefits of tax planning with a diversified investment in an emerging asset class, is a 100% tax deductible agribusiness investment. Last year alone tens of thousands of Australians invested in agribusiness.

These investments have historically been driven by plantation timber, which is generally harvested and sold as woodchip for use in the production of fine quality paper. Today, investors can choose from a variety of products including wine grapes, organic olives and almonds.

Importantly, the 100% tax deductible nature of agribusiness investments (supported by Australian Taxation Office Product Rulings*) opens numerous tax planning and wealth creation possibilities.

How it works: an individual who invests in an agribusiness managed investment scheme, choosing a finance option to suit their cash flow needs, receives a tax deduction on the investment cost (over varying years). This reduces their taxable income, resulting in a tax benefit. In addition, in years to come, the individual is expected to receive an income from the sale of the underlying commodity.



Case Study

Michael earns a salary of $95,000. He and his wife Jenny have recently had twins and are looking for a long term investment that will help to fund the expenses of their rapidly growing family.

In addition, Michael would like to free up cash flow now so he can contribute additional funds to mortgage repayments to relieve financial pressure for the years to come.

Michael invests in one woodlot in a managed investment scheme ($12,500 + GST), and registers for GST. He finances the investment with a 7 year principal and interest loan, with repayments not commencing until July 2008.

Due to the 100% tax deductible nature of the investment, Michael receives a tax benefit of $5,188 in his 2008 tax return.

He is also expected to receive returns from harvest proceeds from commercial thinnings during the life of the Project and from final harvest approximately 17-19 years after planting.

Salary	$95,000	$95,000
Tax deduction from investment		($12,500)
Taxable income	$95,000	$82,500
Tax on income	$26,524	$21,337
After tax position	$68,476	$73,633
TAX SAVING		**$5,188**

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