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SELECT COMMITTEE ON AGRICULTURAL AND RELATED
INDUSTRIES

Reference: Food production in Australia

FRIDAY, 23 OCTOBER 2009

MELBOURNE

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**SENATE SELECT COMMITTEE ON
AGRICULTURAL AND RELATED INDUSTRIES**

Friday, 23 October 2009

Members: Senator Heffernan (*Chair*), Senator O'Brien (*Deputy Chair*), Senators Fisher, Milne, Nash and Sterle

Participating members: Senators Abetz, Adams, Back, Barnett, Bernardi, Bilyk, Birmingham, Mark Bishop, Boswell, Boyce, Brandis, Carol Brown, Bushby, Cameron, Cash, Colbeck, Jacinta Collins, Coonan, Cormann, Crossin, Eggleston, Feeney, Ferguson, Fielding, Fierravanti-Wells, Fifield, Forshaw, Furner, Humphries, Hurley, Hutchins, Johnston, Joyce, Kroger, Lundy, Ian Macdonald, McEwen, McGauran, McLucas, Marshall, Mason, Minchin, Moore, Parry, Payne, Polley, Pratt, Ronaldson, Ryan, Scullion, Siewert, Stephens, Troeth, Trood, Williams, Wortley and Xenophon

Senators in attendance: Senators Colbeck, Heffernan, Milne and O'Brien

Terms of reference for the inquiry:

To inquire into and report on:

Food production in Australia and the question of how to produce food that is:

- a. affordable to consumers;
- b. viable for production by farmers; and
- c. of sustainable impact on the environment

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Committee met at 9.05 am

CHAIR (Senator Heffernan)—Ladies and gentlemen—and the thousands of people in the audience—I declare open this public hearing of the Senate Select Committee on Agricultural and Related Industries. The committee is hearing evidence in relation to the current inquiry into food production in Australia. I welcome you all here today. This is a public hearing and a *Hansard* transcript of proceedings is being made.

Before the committee starts taking evidence, I remind all witnesses that in giving evidence to the committee they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to a committee and such action may be treated by the Senate as a contempt. It is also a contempt to give false or misleading evidence to a committee. The committee prefers that all evidence be given in public but, under the Senate's resolutions, witnesses have the right to request to be heard in private session. It is important that witnesses give the committee notice if they intend to give evidence in camera.

If a witness objects to answering a question, the witness should state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer, having regard to the ground which is claimed. If the committee determines to insist on an answer, a witness may request that the answer be given in camera. Such a request may of course be made at any other time.

[9.06 am]

**HANRAHAN, Dr Pamela, Senior Executive Leader, Investment Managers Group,
Australian Securities and Investments Commission**

MEDCRAFT, Mr Greg, Commissioner, Australian Securities and Investments Commission

CHAIR—I welcome the representatives of the Australian Securities and Investments Commission. I remind senators that the Senate has resolved that an officer of a department of the Commonwealth or a state shall not be asked to give opinions on matters of policy and shall be given reasonable opportunity to refer questions asked of the officer to superior officers or to a minister. This resolution prohibits questions asking for opinions on matters of policy only and does not preclude questions asking for explanations of policy or factual questions about how and when policies were adopted. Officers of the department are also reminded that any claim that it would be contrary to the public interest to answer a question must be made by a minister and should be accompanied by a statement setting out the basis of the claim. Do you want to make an opening statement?

Mr Medcraft—Thank you, Mr Chairman. Yes, I would like to make a brief opening statement, if I may. My responsibilities extend to a number of areas with ASIC, including the investment managers team, which is most relevant to the issues before us today. Pamela leads a team of 30 people whose primary responsibility is the regulation and supervision of collective investments in Australia.

First of all what I would like to do is reflect back to 15 July 2009 when we appeared before the Parliamentary Joint Committee on Corporations and Financial Services inquiry into agribusiness managed investment schemes or MISs. At that inquiry Tony D'Aloisio, the chairman of ASIC, made an opening statement where he observed that, looking back at the MIS industry, with the collapses of Timbercorp and Great Southern there were three emerging policy issues for consideration and analysis: firstly, the business models and the way liquidity and capital were managed by MIS operators. Chairman D'Aloisio noted that MISs, along with numerous other market linked investments, fell on the other line drawn following the Wallis inquiry, and that line distinguishes APRA regulated entities—banks, insurance companies and superannuation entities—and other market linked investments from, basically, MISs, which are subject to a separate regime under the Corporations Act.

In brief, the Corporations Act regime is premised on an economic philosophy that markets drive efficiencies and markets operate most efficiently when there is a minimum of regulatory intervention, hence the regime administered by ASIC is designed to promote market integrity and consumer protection solely through the conduct and disclosure regulation. Of course, conduct and disclosure regulation does not involve any guarantee that regulated products and institutions will not fail and that promises made to retail investors will be met.

The PJC report on agribusiness MISs suggested that there was a strong argument for a kind of prudential oversight of agribusiness MIS schemes to be developed in the future to prevent such failures. However, the committee have reserved making any further recommendations until they

have concluded their own separate inquiry into financial products and services. The second issue that was noted in July was the role of financial advisers and the way they promoted MIS products. This issue is obviously much broader than just MIS and is the focus of the PJC's attention at present. ASIC has made substantial submissions to the PJC and we can provide the committee with further information on this point if required.

The third issue goes to whether, given the current policy settings, further consideration is needed about whether certain products are suitable for retail investors at all. The question for policymakers and government is whether there needs to be greater thought about whether some financial products are not suitable for retail investors and whether greater protection for retail investors might be needed. These three issues are, essentially, policy issues which are still being debated. Where the debate ends will ultimately be decided by government. If reforms occur, there is a reasonable chance that MISs will be affected.

Before taking questions I would like to, if I may, provide the committee with a brief overview of the way MISs are regulated. The regulatory framework that applies to MISs is the same as other types of collective investment, like property trusts and equity funds. Any collective investment scheme with more than 20 members must generally be registered with ASIC and must be operated by a public company that holds an Australian financial services licence. This company is the responsible entity.

Before registering a scheme, ASIC must be satisfied that the MIS constitution and compliance plan meet the legal requirements as set out in the Corporations Act. The process requires ASIC to conduct a legal assessment of the documents used to govern the operation of the scheme rather than a commercial assessment of the MIS business model. If the legal and licensing requirements are met, the MIS must be registered by ASIC.

If the MIS is sold to retail investors, the responsible entity must prepare a product disclosure statement containing information about the investment set out in the Corporations Act. ASIC does not vet PDSs at all. We have powers to place stop orders on PDS where they contain misleading and defective statements.

I previously mentioned that MISs must have a compliance plan. This document sets out measures that a responsible entity of the MIS should follow to ensure the scheme is operating in accordance with the Corporations Act and the MIS constitution. Where the responsible entity of an MIS comprises a majority of non-independent directors, the MIS is required to have a compliance committee comprising a majority of external independent parties. The committee's role is to monitor compliance with the MIS compliance plan. This is an important self-regulatory aspect of the Corporations Act regime.

A further requirement is imposed on top of this. Each year the RE must obtain an audit of its compliance with the MIS compliance plan. The auditor must opine on whether the responsible entity has complied with its obligations of the compliance plan and the general adequacy of the plan with regard to the nature of the scheme.

So, to summarise, the regulatory regime sees ASIC's role in respect of MISs as taking on four main components: (1) we license the responsible entity; (2) registering the MIS following a legal assessment of the MIS constituent documents; (3) monitoring the MIS disclosure to ensure the

disclosure meets the legal standards of the Corporations Act; (4) supervising the conduct of the RE and its officers to check whether they are complying with their legal obligations in relation to the scheme.

ASIC's job is supported by a number of self-regulatory structures imposed on MIS by the Corporations Act, as I mentioned, the compliance committee and the compliance plan auditors, as well as duties imposed on licensed entities to report to ASIC on any significant breaches of the Corporations Act. Going back to the first point that I raised before, the regulatory structure associated with MIS is an outcome of the self-executing nature of the Corporations Act. It is left to market participants to comply with the law. The rules we enforce are around disclosure and market abuse. I want to borrow from Tony D'Aloisio's words again, 'ASIC, unlike APRA, is an oversight and enforcement body. We are not a prudential authority,' and several things flow from this difference. Inevitably, ASIC come in after a collapse has occurred. We are there as an oversight body to see the law is complied with and, as such, we will often arrive at the scene of the accident—that is, after the accident has occurred and to see who caused it. Our powers are limited to act ahead of time. For example, we do not have power to regulate capital adequacy or to prohibit certain business models.

Having made these observations, it is important to recognise that we see a clear role arising out of the MIS collapses. In that respect we have taken a fairly focused approach on the MIS collapse situation in three respects. We have established a cross-ASIC task force that is headed by me. That involves groups that are relevant from across ASIC—the insolvency area, the misconduct and breach of recording, financial advisers and investment managers, communications. We meet weekly and our approach is to focus on the key participants in the value chain, from the issuers to the experts, to financial advisers, to research houses et cetera. The priorities that we look at in terms of our focus we actually call our 2-1-3 approach: (2) being the current issues that we need to focus on, (1) being what has happened in the past, and (3) being what can we do looking forward.

So applying that 2-1-3 approach, at the moment we have been focused on the immediate issue of ensuring that affected grower interests are being protected in the wake of the collapses. That is a process that we have conducted by supervising the external administrators and making sure that it is transparent and fair to all parties, having regard to their legal rights. We have also been looking backwards in terms of inquiries and assessments into past conduct of failed MIS operators. Then, looking forward, we have been reviewing our policy guidance in terms of what has happened in the last 12 months and looking to see what we may do going forward. In fact, one of the things we are looking at is an 'If not, why not?' disclosure regime in the future, looking at benchmarking and best practice. Thank you for permitting me to make these opening statements, Mr Chairman.

CHAIR—Thank you very much for coming today and I might say, with three-quarters of an hour, we will probably have you back again because I do not think we are going to get there today. In 2003 there was a Senate report which predicted all the things that have happened in the MIS industry. Did you take any notice of that report, or was it given to you?

Dr Hanrahan—Yes. We have had work under way since 2003.

CHAIR—Andrew Murray was the driver of it, you will recall.

Dr Hanrahan—Yes, we did receive that. We are talking about before my time but, having looked back over the work that ASIC has done over the last five years in the MIS space, that certainly was something that came into our planning.

CHAIR—So where is the evidence of what action you took of the warnings that were in that report?

Dr Hanrahan—ASIC took various actions across the period of time, particularly coming out of 2003. I might just ask Rupert to refer me to the page in our notes as to the work that we have done there.

CHAIR—While you are finding it, Mr Marshall or whoever it was predicted that what usually happens in these schemes is that the boss flees with the money eventually and that is precisely what happened in the case of Great Southern: from having summonsed the former chair and Richard Mews the former non-executive director, who resigned in protest that Mr John Young, before full disclosure to the market, sold his shares, took off, cashed out and then went back into the market under Javelin Pty Ltd to buy back the misery and prosecute the people that put the money up in the first place—all of that was predicted back in 2003. So we would like to see the paper trail, if you could table the paper trail to this committee, of action that you actually took in view of the warnings that were given.

Mr Medcraft—As I understand it, what happened in 2003 was that the report was concerned with two things—disclosure by investment managers in the agribusiness schemes and the advice given by financial advisers. I believe that is correct. What ASIC found was that there was poor disclosure of commissions and there were a number of instances where people were put into schemes as a result of poor advice. What I have been informed of is that apparently we undertook surveillances in 2004 and did a substantial amount of work with the sector in 2004 in improving disclosure.

CHAIR—All right. We have got a young bloke that was going to appear today and he is typical of what has happened. He in fact invested \$2 million—good luck to him!—in the various MIS episodes, advised by an accountant and a financial planner that this was the way to go and the way of the future. That was just in the last couple of years. So whatever you did in response to what you have just read out came to a bucket of custard, because nothing happened and the financial planners were still reaping the rewards with commissions et cetera. Are you disappointed in what has happened, given the authority that you have to prevent it from happening?

Senator MILNE—Chair, it is Senator Milne. I have to disconnect for a minute. If I could get the secretariat to ring me back in five minutes.

CHAIR—No worries.

Senator MILNE—Thank you.

Dr Hanrahan—Greg in his opening comments talked about the role that the securities regulator plays in this. The way our regulatory system works is that we try and ensure a high level of disclosure for investors in order for them to make an informed choice about whether

they want to invest in a particular product or not. So you require, hopefully, good quality disclosure. Investors go and see financial planners and get advice about whether an investment is suitable for them. But it is not for the securities regulator to say to people, at least under the current policy settings, ‘Look, this investment is not suitable for you,’ or—

CHAIR—No, I am not saying that you should say that, but I am saying that as far back as that report in 2003, it flagged all of what is happening. I have not got the details in front of me and that is why we will have you back. They said that if you get a certain set of advice and it does not suit you, you just go and buy another set of advice. It is like competing science. That is precisely what happened in that case. You are powerless to do anything about that?

Dr Hanrahan—Sorry. When you say ‘advice’, are you referring to the experts’ reports in the disclosure documents or the advice to the investor?

Senator O’BRIEN—Dr Hanrahan, I believe what the Chair is saying is that the promoter in its PDS refers to so-called independent advice which rates the product and talks about whether it is a viable scheme that is being proposed. What the Chair is suggesting is that there is nothing to prevent the promoter of a scheme from shopping around for the best so-called independent advice to use in their PDS. Whether that is bona fide, genuine, well advised or in fact professional is another question. I take it ASIC is aware of these issues and what can be done, given you have said in your submission that you do not actually make an evaluation of a PDS. Is that right?

CHAIR—Yes, that is it. He is much more articulate than I am.

Dr Hanrahan—Thank you. The law imposes liability on people who make statements in PDSs, so that is the way it works. It says, ‘If you make a statement as an expert in a product disclosure statement and that statement is misleading or deceptive or otherwise defective, then liability attaches to that.’ I suppose that is the answer to that question. We have a law in there that says, ‘What you put in the PDS has to be reliable and accurate.’

CHAIR—So if it is well paid for and it is garbage, it is okay?

Mr Medcraft—I think what Dr Hanrahan is saying is that ASIC does not actually assess the fundamental of this current framework, which we administer.

CHAIR—No, I appreciate that.

Mr Medcraft—As I have mentioned, that is largely a self-regulating framework and if you do something wrong within that framework within the law, basically either we or the courts will come after you. In the case of, say, an independent expert’s report being wrong, then essentially the recourse is to sue for false and misleading or misleading and deceptive conduct. If the whole PDS is wrong, there is issue again in terms of false and misleading conduct. In our current investigations into MISs, with all the schemes that have got into trouble, in terms of the powers that ASIC has, what we are looking at is, within those, whether there have been breaches of the act, through things that have gone wrong.

Senator O'BRIEN—Firstly what you are saying is: take for example—we will not name a company—someone who is in a scheme that has fallen over and has been induced to invest because an independent adviser has been quoted in the PDS as saying, 'This product has the potential to return X,' when any reasonable assessment of the facts will show that that was never a possibility; those people who are aggrieved by a failure of the scheme could sue the independent adviser? That is what you are saying, is it?

Mr Medcraft—For false and misleading conduct, yes.

Senator O'BRIEN—And are you saying that in your review of Great Southern and Timbercorp you are actually looking at those particular issues?

Mr Medcraft—What I have said is that we are looking at issues associated with the collapse, looking backwards. What I said is that we are looking at the participants in the value chain, from the issuer to the experts to the financial advisers to the research houses; all the participants in the value chain. We are looking backwards to see whether there have been any breaches of the law. Sorry, I cannot, other than going into specific operational matters—

CHAIR—We do not want to mess up your investigations.

Mr Medcraft—I think you get the general drift. I think it is pretty clear what I am saying.

CHAIR—But your approach is a solidly dry, legal approach. We have people wanting a commonsense approach.

Mr Medcraft—The commonsense approach would have been not to invest in it.

CHAIR—No, you are not allowed to have commonsense.

Senator O'BRIEN—I can assure you that the committee wants a solid, legal outcome in this.

CHAIR—Yes.

Mr Medcraft—That is what we are aiming to get.

CHAIR—Someone rings up and says, 'I've invested \$2 million.' It is hard to believe some of this stuff, especially self-managed super funds that have done it. 'My accountant told me. He referred me to Joe Bloggs. I put in \$2 million into the various things and then I started to get these accounts in the mail per quarter'—this bloke who put a lot of money in—'of 100-and-something thousand dollars a quarter.' He said, 'I started to pay them but I didn't really know what they were for.' Of course, it has all blown up. He is in serious trouble. He is not here today because he has taken it to court. Obviously, as Senator O'Brien has said, there has to be some serious rejigging of the equation.

Could I just take you to your submission that you have made to the other committee, towards the back of it, on page 59 of today's proceedings, which is under 'Recent collapses to agribusiness MIS', clause 173. Could I just have a procedural pause to let Senator Milne back into the game.

Mr Medcraft—Was that paragraph 173?

CHAIR—Yes, Great Southern Managers Australia Ltd. Are you there, Senator Milne?

Senator MILNE—Yes, I am here, thank you. Sorry about that.

CHAIR—Righto. If I could go to that, you have a little precis of what happened to Great Southern. Then you have a table, table 8. Do you have that?

Mr Medcraft—Yes.

CHAIR—Then you have size and location of GSMAL's agricultural operations. Where are the cattle?

Mr Medcraft—As I understand it, the cattle were inside, not separate. At this stage they were not MISs any longer, because they had been exchanged for shares in the company, so the cattle were actually part of the assets of the company.

CHAIR—So in any reasonable, sensible report of ASIC of the complete confounding and misleading of investors—\$3.7 billion we are talking about—you decide to overlook cattle on a technicality?

Mr Medcraft—No, I do not think so.

CHAIR—Shouldn't cattle be in there?

Mr Medcraft—This is a report in respect of the collapse. When they collapsed, they were not an MIS scheme.

CHAIR—But they are not part of your precis of Great Southern. This cattle scheme is a serious fraud and it will be the greatest cattle duffing operation that people are going to get away with in Australia's history, yet you have decided not to even put an appendix in Great Southern's MIS history to the greatest scam they had, which was the cattle.

Mr Medcraft—This was looking at agricultural MIS schemes and that is what we were reporting on.

CHAIR—I would have thought cattle belong in agriculture.

Mr Medcraft—Just on your question, I think we did cover it in the submission. I cannot remember. Did we actually cover the project?

CHAIR—Yes, you said there were four cattle schemes.

Mr Medcraft—Did we cover Project Transform in the submission?

CHAIR—I am going to cover it if you have not.

Dr Hanrahan—I think this table was a snapshot as at the time of the collapse of the assets that were in MISs at the time.

Mr Medcraft—Yes.

CHAIR—But can I tell you, like some of the processes from the investors, this is very misleading. In the other committee—I sat through your hearing—they gave you a light touch because they did not know what they were talking about in this stuff. They gave you a very light touch. You are going to come back; we are not going to give you a light touch. This is a serious issue. So I want to go cattle and I want to go back to the advice that you have given in clause 148:#

ASIC has published a number of publications on its consumer website warning people.

When did you issue those warnings?

Dr Hanrahan—I believe that it goes back over a number of years, back to about 2003 or so, on the consumer website.

CHAIR—You said to people:

Agricultural schemes usually grow the product on land which the grower leases but does not own. The land could be sold or mortgaged without any notice to you, unless the lease is registered on the land title—

and this is all just ordinary stuff for bush people; we know all this—

or some form of caveat ... is placed on the title. Without this safeguard, you could lose your investment.

How well did you publicise that and when did you publicise that?

Mr Medcraft—We can come back to you on that. All I know is that the information is on our website. As you have mentioned, we have three publications, *Investing in agricultural investment schemes*; *Investing to reduce your tax?*; and *Investment Schemes: buyers beware*. We will come back to you on when those publications were made available and when it came back onto the website. I should mention that every year in the peak tax product sale season, May to June, we do publish media releases warning investors of risks of investing in tax-effective products. We will come back to you on that as well.

CHAIR—Thank you very much for that. The difficulty is that the person who walks in blind to the accountant, who then gets referred to a financial planner, does not get to see any of that. So if the financial planner and whoever else is associated with the deal for the commission decide that this person needs a tax deduction and they are driven by the tax deduction—which most of them are, except in market based schemes like Wilmotts et cetera—they do not look at the detail. We are going to have evidence today from someone who has got 1,700 clients who are distressed and feel completely betrayed by ASIC—completely betrayed.

Yours is a very dry, post-operative in a lot of cases, operation. I want to take you to something that Senator O'Brien eloquently referred to earlier, which is expert reports. We had KPMG in in Canberra and they talked about the Transform arrangement. The Transform arrangement was a super con job; it was never going to work and, because they have done the Transform arrangement on the cattle scheme—and I do not expect you to be familiar with cattle, except that they eat grass and they taste good—

Senator O'Brien—Mostly.

CHAIR—Mostly, yes—except if you get into too much budget beef; that is not so good. The cattle scheme, to summarise quickly, was that you bought a drove. You had a serious tax deduction problem, so you bought a drove for \$5,000 and that entitled you to lease four cattle for seven years and the progeny therefrom, except that half of the progeny that were born to that had to go back as an administrative cost. They could never possibly have made anything out of it. It was not possible to make a profit. It was quite misleading the way they flew people to King Island and said, 'Wow, look at those Angus cattle in that green paddock,' when all but 14 per cent of the cattle were in the Northern Territory in rangelands where they have, at best, 60 per cent calvings.

So they had two calvings. The first calving was a 50 per cent calving; the second calving was 60 per cent. You put in the average cost per year for the lease of the cow for seven years, with financials, at \$200 and a mighty good price for a seven-month-old weaner in the Northern Territory would be \$300, but let's say it is \$400 because they have to grow them out. And then, 'Oops, the drought's come along.' The Barkly Tableland was completely obliterated with the drought. 'Oops, what are we going to do?' So the best you could do is, if you got a 50 per cent calving, you would put in \$200 for the cow and you get a \$400 calf, half a calf per cow, which is \$200. Then you give half of that for the management plan, so you are back to \$100 for your \$200. This is outrageous. Then you have got all the follower fees and they wonder why they are disappointed. So that is the sort of shape and form of the proposition.

Then I ring Mr Sterling Buntine—who was appointed by his brother-in-law to manage the stock—and he tells me that the money started to pour in so much to Great Southern that he was instructed to get out and get more country and get more cattle because he did not want Great Southern to have to send the money back to the investors. So he said, 'I got stuck into it. It was like manna from heaven,' and he bought and leased places and then leased them on to Great Southern. Then when it all turned to custard, McGrathNicol employed him. When I asked McGrathNicol why they employed him they said, 'Because he's the only one that knows where the cattle are.' Then they did the Transform arrangement.

The Transform arrangement was that—I am coming back to KPMG—advised by KPMG, Great Southern passed on to the investors—not the shareholders: the investors, the bunnies—that, 'We will buy back in return for shares in the company not the leases but the value of your investment likely to be at the end of the investment. So you get back the shares now.' In the time that it took for Transform to take place, the shares fell by 50 per cent, while the advice was being given. So we asked KPMG, who were good enough to front up, like yourselves today, for which we are eternally grateful, 'How did you get the expert opinion advice to give to Great Southern to give to the investors?' and they said, 'Well, we employed an independent outside expert,' and they said whoever it was—Agricultural Pty Ltd or whatever.

So I then said, ‘No, I’m not interested in the company. I’m interested in people.’ So 20 minutes later—I think it was, Kerry—they came back with the name, and it was Ross Ainsworth and another character, who I had had a long yarn to. I said, ‘Would that be the same Ross Ainsworth that was actually on Great Southern’s payroll at the time, as their pastoral supervisor?’ and they said, ‘Mm. Well, perhaps.’ And he was. The last time I rang Ross Ainsworth, he was on the wharf at Darwin loading cattle and I said to him, ‘Mate, many cleanskins going on the boat?’ He said, ‘Oh, well, there’s some.’ I said, ‘Any NLIS tags?’ ‘Oh, Bill, we don’t need NLIS tags’—that is, identification—‘as long as they come from the property of origin.’ ‘But how do we know they come from the property of origin?’ ‘No-one knows.’

So that is the guy that KPMG go to—he is doing the job for Great Southern—to get advice, to tell Great Southern, ‘It’s okay to get the investors, because we’re running out of money, boys, to put your investment back into shares,’ which happened.

Then Great Southern rushed around, knocked on people’s doors—and we will get plenty of that evidence—to say, ‘We will forgive you your debt even if you agree to this Transform to change the constitution so that we can then do this Transform arrangement.’ So by doing that, we will never know whether the cattle existed, because these properties were bought walk in, walk out. When they tried to sell them, one of the people who went to sell them—I will not name the person; a very experienced pastoralist in the north—said, ‘Bill, I’m not going near that property because the cattle are not there.’

We have got one breeder who leased into the system 1,000 cows and he was told, ‘We don’t know where they are.’ Then they run out of money, so they say, ‘Look, in lieu of the lease money for the properties, Mr Buntine, that we are leasing’—this is Great Southern back from you and now McGrathNicol—‘we’ll give you cattle.’ So I ring Elders up—I will not say where—and say, ‘G’day, mate.’ ‘How’d you find my number?’ I did not bother to explain to him how I worked out where he was, but I had made a lot of phone calls. He is tucked away in behind, out in the back of Queensland. I said, ‘Mate, I’ve only got one question for you. In this in lieu of cash for cattle arrangement, who is counting the cattle and who is valuing them?’ and the phone just went dead.

This is a scam and yet it is not included in your paperwork for the other committee or this committee. So I guess I have got a serious problem. Would you like to comment on the fact that KPMG thinks that independent advice can be obtained from someone else who is on the payroll of the person who they are advising about?

Mr Medcraft—There are a fair few things in there. Pamela can add some comments. I think it does get back to the whole issue about independent expert reports and that the legal system says that, if they are misleading and deceptive or if there are questions about independence, there are legal remedies available. I do not know whether you want to comment about that, Pamela.

Senator MILNE—Chair, can I make a comment here?

CHAIR—Away you go.

Senator MILNE—When you say there are legal remedies available, to whom? Does ASIC accept any responsibility for the fact that these managed investment scheme reports are riddled with inaccurate so-called expert advice? Did you ever look at that?

Mr Medcraft—What I might comment on, Mr Chairman, is what action we did take in Project Transform. Would that interest you?

CHAIR—Yes.

Mr Medcraft—In relation to Project Transform, the transaction that was conducted was obviously a contractual arrangement, so it did not fall within ASIC's role to review the relevant documentation under the Corporations Act. However, the transaction did come to our attention because Great Southern had to get licensing relief to enable the independent directors to provide advice to members in the form of a recommendation to vote in favour of the transaction. In granting that relief, ASIC imposed a condition that ASIC should be given the opportunity to review the documentation to be sent to the members in connection with the transaction.

I remind you that our two tools are conduct and disclosure. The purpose of that was to allow ASIC to monitor whether there was clear, concise and effective disclosure of the risks and the benefits of the transaction. As a result of our review we obtained additional disclosure of risks and benefits of the transaction in the documents before they were actually sent to members. In relation to the independent experts' reports, in particular what we got was prominent disclosure of the independent expert's report as having assessed a high-end value of interests being surrendered compared to the shares being issued under the proposed transaction. So we actually asked for that to be given prominence—that there was a very high-end value on the shares.

We also asked for prominent disclosure, which was given, about the independent expert's assessment of whether the consideration offered was fair, based on the independent expert's assessed low-end value of the interest being surrendered. On one side you actually had a very high-end valuation and on the other end you had a low-end valuation on the assets that were being surrendered. So we did actually say that this had to be given prominence.

Senator O'BRIEN—So you were saying to the person involved in the transaction that they were giving up something of much higher value than what they were getting.

Mr Medcraft—Basically a valuation was undertaken and, as in any valuation, you have got a range of valuations. As I understand it, what was given up was: the valuer proposed a valuation at the low end of the range and what they had actually been receiving was at the high end of the range. We clearly saw that and within the powers that we have, which is disclosure—concise, fair and effective—we basically wanted that to be made prominent, because clearly that was recognised.

The other thing that we asked for is that it be strongly emphasised that the historical prices and the trading patterns of Great Southern shares were not necessarily indicative of future prices of those shares and that previous share prices therefore may not be indicative of future trading prices. This was obviously particularly significant given that the transaction itself might significantly change the profile, the register, of the company and the value of its shares. We also asked the reasons why the independent expert did not use another valuation methodology other

than the discounted cash flow methodology to value the member interest scheme and we continued to monitor the transaction after they announced their full-year 2008 results. So we basically did take steps.

CHAIR—When did you do that?

Dr Hanrahan—During the lead-up to the vote for the transaction. So, in order for Transform to occur, the company—

CHAIR—So this is after the general manager had quit?

Dr Hanrahan—This is in the last quarter of 2008 when the transaction was under consideration. So I think what Mr Medcraft is saying is that when the company came to ASIC to request a variation around its licence to enable the transaction to go ahead, ASIC actually took a proactive stance to review the documentation that was being sent to members.

CHAIR—In the last quarter of 2008?

Dr Hanrahan—This is specifically around the Project Transform.

Mr Medcraft—Project Transform.

CHAIR—In the last quarter of 2008?

Mr Medcraft—This was in relation to the exchange.

CHAIR—I am well aware what it is in relation to. This was in the last quarter in 2008 you gave that advice?

Mr Medcraft—It was when Project Transform—

CHAIR—When did Transform complete?

Dr Hanrahan—The meeting was held February, January.

CHAIR—Right.

Dr Hanrahan—So during this period. So the transaction came—

CHAIR—Yes, I am well aware. I want to go somewhere else.

Mr Medcraft—Just to be clear, ASIC was focused on looking at what we could do within our powers to protect investors.

CHAIR—Yes, I know you do not have the powers. I understand that.

Mr Medcraft—But within what we had—

CHAIR—Yes, I understand. You were doing the best with what you have got. You have got to get a lot more. So 2008 you say to them, ‘Be careful.’ Senator O’Brien put the sensible question, ‘Well, what is the valuation of what you’re giving up?’ and you have warned in your earlier warning—which we will get a date on and the details of—saying, ‘If you have got investment on lease country you might lose your lease because you don’t own the country. Possession is nine-tenths of the law.’

So, in this case, at the end of 2008 you gave the warning; KPMG gave the advice, advised by someone who works for the person that they are advising about; the shares start to fall; the CEO has quit; he’s cashed out. They then don’t have the numbers at the meeting before Christmas to get the numbers, so they adjourn the meeting. You are still in the game. So they rush around and offer these people discounts on their follower fees et cetera—‘Mate, come along and vote yes,’ and in one or two cases, ‘We’ll forgive the debt altogether.’ In the meantime the shares fell another 50 per cent. So then they have the meeting to change the constitution and 10 minutes after they have the meeting, as it were, they have the meeting to enact Transform. Shouldn’t they have gone back to ASIC and said, ‘Look, we’re changing our constitution. Could you approve this?’ before they enacted what the constitution was about?

Dr Hanrahan—Should they have come back to ASIC and asked—

CHAIR—Yes. The question is: ‘Well, I have a memorandum and articles—declare an interest.’ Can I just muck around with my constitution and not refer it to you and then go and bleed someone to death? Shouldn’t it have been referred to you?

Dr Hanrahan—The power to amend the constitution belongs to the members of the scheme and they exercise that. Our role is to ensure that they exercise that with the best possible information available to them. So ASIC had continued to monitor the disclosure in the lead-up to the meeting and, after the meeting was adjourned and there was movement in the financial position of the company, ASIC required the preparation of a supplementary expert’s report as at 12 January. So additional disclosure was provided to members. The circumstances around how the members were encouraged or otherwise influenced to exercise their votes in a particular way is something that we would prefer not to comment on for reasons I am sure you can understand. But in terms of the disclosure, the members did get additional disclosure leading up to their decision, which belonged to them, to amend their constitution in the way that they chose—in some schemes, but certainly not the majority—to do.

CHAIR—But you did not get a look at it because it happened at the meeting and then 10 minutes later—

Senator O’Brien—Was there a requirement for you to see the change?

Dr Hanrahan—No, because the power to amend the constitution belongs to the members. It is their scheme, so they exercise that power.

Mr Medcraft—It does not require our approval.

Dr Hanrahan—That is right. Then it is lodged with us.

CHAIR—So if it is unfair it does not matter to you?

Mr Medcraft—As I said in my opening statement, what you have to remember is that the law here is largely self-regulated and basically our powers come down to conduct and disclosure and we do not make an assessment of the business models that are involved.

CHAIR—Yes, okay.

Mr Medcraft—I hate to say that again, but it so much pervades through a lot of what your issues are.

CHAIR—I understand.

Mr Medcraft—It really comes down to, as you said, that this is the legal framework we have to work with and we do strenuously, within the framework we have, look to do what we can to protect investors.

CHAIR—I do not know how you blokes know that your supplementary advice got to the shareholders or whether it just got to the financial planners or the accountants. Do you know how it was disseminated?

Dr Hanrahan—There is a notice of meeting that has to be sent out.

Mr Medcraft—By law.

Dr Hanrahan—And the company was a listed entity, so there is disclosure at the stock exchange level.

CHAIR—So do you think that it is okay to go out to someone and offer them an inducement to change their mind, which is not disclosed to everyone? I think that is a criminal inducement and I think it is a matter for you fellows to take up. Because you have manipulated the shareholders by offering some a deal which you have not offered others and you have done it clandestinely, with various incentives from a two per cent drop in the interest that these poor buggers have been charged on money that they did not know they owed, to full forgiveness of the debt, isn't that an inducement that might approach criminality?

Mr Medcraft—Unfortunately, we cannot comment on that, Mr Chairman.

CHAIR—Has anybody raised that with you?

Mr Medcraft—I cannot comment on it because it is an operational matter.

CHAIR—Christine, it is over to you.

Senator MILNE—Thank you. I want to go to this issue of disclosure, because I wrote to you—ASIC—over Great Southern, in particular pointing out that they were supplementing the returns on timber plantations and supplementing the returns from the sale of the early-year plantations with investments from following years in order to boost the returns to investors. I

alleged that it was a Ponzi scheme at the time. I also pointed out that, in their documentation, they had so-called independent expert foresters and after they had supplemented the returns with future investment money they still used this forester to say that the projected growth rates and harvest rates and returns would be as in the prospectus, even though they knew at that time that that was not correct. I wrote to you about all of that and gave you the figures. You sent me back a letter saying, 'It's all under control,' more or less and then the whole thing collapsed. What I had alleged and what other people had alleged came to pass. So how is it that, when I point out to you that the disclosure is inadequate in terms of the returns and that the promises in relation to harvest rates were wrong, you still found in favour of Great Southern?

Mr Medcraft—In response to your question, I cannot comment. In reply to your letter to us in December, we set out what our processes were. But at this stage, it very much is an operational matter related to Great Southern and our ongoing investigations in relation to Great Southern.

Senator MILNE—Obviously you are taking action on it now, but my frustration is that people were telling you a long time ago that this was happening. Do you accept that ASIC has got to bear some responsibility for failing to oversee these managed investment schemes on the disclosure issue? Your answer to me on that forester was, 'Oh, well, people have to read the small print,' and blah blah. The point is that this was a so-called independent forester who, after the event, was misleading the public.

Dr Hanrahan—I might say something briefly about what happened, following your letter, in the time before the company went into voluntary administration, in terms of ASIC's attention to the disclosure in the PDS.

Senator MILNE—Okay.

Dr Hanrahan—Your letter, I believe, we received in November or early December of last year. We responded with some information obviously then. What I can say is that from that time onwards the content of the product disclosure statement came under what we would describe as active supervision within ASIC, so we set about making inquiries as to the accuracy or otherwise of the PDS and had various discussions with the company. The upshot of those discussions was that in May of this year the company agreed to withdraw the PDS. So, while we are constrained in what we can say about the disclosure because it might be the subject of some future attention, we can say that there was ongoing discussion between our agency and the issuer and that that resulted in the issuer withdrawing the PDS.

Mr Medcraft—I joined ASIC in February this year. One of the things we did do with Dr Hanrahan on MISs was that, before the current fundraising season this year, we undertook a very significant surveillance of existing PDSs in the market. We went out and queried what was in their PDSs in terms of their projections and also their financial capacity to deliver on the PDSs. As a result of that, PDSs were withdrawn, PDSs were revised, so in fact some of the things that we saw happening we did take action on. Do you want to add to that, Pamela?

Dr Hanrahan—Of course, the primary responsibility for ensuring that the PDS is not misleading or deceptive rests with the people who prepare that document and the experts who agree to be named in that document. ASIC has a supervisory function, as we have mentioned, so we will review documents from time to time.

Sometimes that review will result in a voluntary withdrawal of the document while it is fixed. Sometimes, if we cannot get to that point and we think there are grounds on which we can establish misleading and deceptive conduct, we might issue a stop order or an interim stop order. That is the process that we go through with the disclosure.

Senator MILNE—If I could just return to issuing the stop order, that information that I provided to you about them setting up a subsidiary company in order to be able to increase the returns to investors and alleging it was a Ponzi scheme, surely at that stage that should have rung a lot of bells. I was not the only person alleging it at the time. Why wouldn't a stop order have been put on that, if you did an immediate investigation and it was demonstrated that that was precisely what they were doing?

Dr Hanrahan—I think the answer to that is that you do have to conduct the inquiry. ASIC has powers that it can exercise to stop product disclosure statements, but those powers have to be exercised on the basis of having conducted an inquiry and satisfied ourselves as to the grounds.

Senator MILNE—Yes, of course.

Dr Hanrahan—We can certainly say that during the first part of 2009 we were engaged in an active process around the quality of the disclosure in the PDS.

Senator MILNE—Thank you.

CHAIR—Senator Milne, I apologise. We are going to come back. This is only round 1.

Senator O'BRIEN—I have a couple of questions. In your submission to the other committee, you list the horticultural schemes, which obviously are heavily weighed to grapes, almonds and olives. Are you able to give us some sort of idea as to how much of that market lay with Great Southern and Timbercorp?

Mr Medcraft—The horticultural schemes in total? I know they represented over 50 per cent of the total agricultural MIS schemes.

Senator O'BRIEN—Yes.

Mr Medcraft—Great Southern represented over half.

Senator O'BRIEN—Great Southern and Timbercorp.

Mr Medcraft—Represented a total of more than half of agricultural MIS schemes.

Senator O'BRIEN—Can we assume from this—is this somewhere in your submission that I have missed?—that the remainder continue to operate?

Mr Medcraft—Yes. Australian Bight Abalone has got into trouble. If you look at some of the other ones, in terms of robustness I think you need to look at the business models, and the business model of Great Southern and Timbercorp: why it declined and the way it was structured in terms of the way they priced the future service delivery—basically, taking it up-front. They

clearly underestimated what it cost to do what needed to be done and there was also the issue of the way they managed their working capital and not having inadequate working capital. Hopefully the ones that are still around have addressed those issues. We have not seen them go under.

Senator O'BRIEN—In terms of product disclosures, I take it from your evidence generally that it has been your role to try and ensure that those disclosures have been accurate and that the liability for them failing to be accurate is a civil liability rather than one through ASIC. Is that right?

Mr Medcraft—Essentially, under the act, if it is misleading and deceptive, that is where the liability lies.

Dr Hanrahan—For defective disclosure, if there is a problem in a PDS, then you have really got three things that you are looking at.

The first is ASIC's power to stop the document—that is, to have the offer document withdrawn from the marketplace—and that can be exercised once various grounds are established after an investigation. The investors then, of course, have their own civil remedies under the act. There are certain defences to liability but, basically, if the document is defective and you have subscribed for interests on the basis of that then you can establish a civil claim.

Mr Medcraft—What is the section of the act that they can claim under or that they can sue under?

Dr Hanrahan—It is 102(2)(a).

Mr Medcraft—That is for misleading and deceptive—

Dr Hanrahan—It is for defective PDSs, yes. In terms of public law sanctions, can ASIC or the government punish people for defective disclosure? The answer to that is yes. The settings are slightly different but, yes, there are powers under the act to bring action against—

Mr Medcraft—There is action against directors or against management as well.

Dr Hanrahan—Yes.

Mr Medcraft—Under the Corporations Act there are civil penalties and there are also criminal penalties under section 180.

Senator O'BRIEN—What is the section?

Mr Medcraft—There are criminal penalties that we can go to as well, for breach of director's duty under section 184, I think.

Dr Hanrahan—Yes.

Senator O'BRIEN—Have they been tested?

Mr Medcraft—I believe they have.

Dr Hanrahan—Yes.

Mr Medcraft—I know of cases we are currently looking at, so I believe they have been. We are constantly looking at whether we pursue a criminal or civil route.

Senator O'BRIEN—In relation to an MIS scheme?

Mr Medcraft—No. But, sorry, that is not ruling out how we may proceed in the future in relation to our investigations.

Senator O'BRIEN—You may wish to take this on notice. I understand it is not your role to make particular recommendations about the form of legislation, but are there any issues with the legislation and the powers provided to ASIC in the pursuit of directors in those PDS type circumstances?

Mr Medcraft—Yes, I will take that on notice.

CHAIR—Thanks very much. Who would be the right people to ask the question of in terms of whether Mr Ross Ainsworth would be considered an independent adviser for KPMG? If you cannot answer it, who can?

Dr Hanrahan—I do not think that it is that we cannot answer it, Chairman. I think it is just because it relates to the specific circumstances of that transaction and we would prefer not to.

CHAIR—This is only round 1. In terms of Javelin buying back the riskier Bendigo and Adelaide Bank loans—that is, the former chairman who cashed out for \$30-odd million formed a \$2 company and thought, 'I'll get back in and get some more of this,' so he's taken up \$30-odd million worth of the bad debt for \$10 million from Bendigo Bank—is there a role for due diligence in that?

Mr Medcraft—That is an operational matter, Chairman, that we cannot comment on. We are aware of it.

CHAIR—In terms of the Transform arrangement for the cattle, which do not officially appear in your report—even though they are a serious problem, they are mysteriously not there, even as an addendum—they only had two calvings.

Mr Medcraft—That is not an MIS at the point which we are reporting on.

CHAIR—A lot of the timber was in the same position as cattle but they are in the report.

Mr Medcraft—Because they were an MIS.

CHAIR—Are you telling me that the cattle scheme was not an MIS?

Mr Medcraft—It was not an MIS when it collapsed.

Dr Hanrahan—There were some confidential annexures to our submission to the PJC that dealt specifically with matters relating to particular corporate collapses. I wonder, Chairman, whether you do not have those.

CHAIR—We do not. Do they include cattle?

Dr Hanrahan—I can say that there is a discussion of the cattle in the confidential annexures to the earlier submission.

CHAIR—Could we have this confidential document?

Dr Hanrahan—I would need to check with the chairman, I suspect.

Mr Medcraft—We will come back to you.

Dr Hanrahan—There is some discussion of the transaction to which you refer. It is not omitted from the earlier material. It is just not public.

CHAIR—As you might expect, unlike the other committee you were before, I am very familiar with the cattle.

Mr Medcraft—I am sure you are.

CHAIR—This is my question on the Transform arrangement and you can take it on notice. The second calving generally starts after the wet, or January. They wean them in August before the heat and the low protein comes in. The Transform thing started in the last quarter of 2008. The market started to collapse—the price of the shares of Great Southern. ‘No, but it’s a great deal, mate. You take these shares in return for your calves.’ The second lot of calves, when they hit the deck, were the property of the investors, not of Great Southern or the scheme. They were the property of the investors and yet they were swept in with Transform and, in my view, they had no right to be swept in because they did not own them to sweep them in. The Transform arrangement was to surrender the value over seven years, but legally, once the calves hit the ground, Great Southern did not have the legal say over them, the investors did, and yet they just got swept away. You might just give consideration to that. I think that was thieving cattle. Thanks very much, for today.

Mr Medcraft—Thank you, Mr Chairman.

CHAIR—Round 1.

Dr Hanrahan—Thank you, Mr Chairman.

Senator MILNE—Chair, unfortunately I have to disconnect now and go to my other meeting, so good luck for the rest of today.

CHAIR—Thanks very much, Senator Milne.

[10.11 am]

WILSON, Mr Robert Thomas, Private capacity

CHAIR—I welcome Mr Robert Wilson. I apologise that we are a little behind. If you would like to, make an opening statement and then we would like to ask you a few delightful questions.

Mr Wilson—Certainly, Mr Chairman. The dairy industry is my life. I grew up in Tasmania and I was born into a dairy farming family and was associated with the market milk industry before pasteurisation laws were in. So my first experience was as a young person in the fifties, delivering raw milk around the streets of Hobart out of a bucket. As things changed and I grew, I became interested in the technology side of the industry. I graduated from Hawkesbury as a dairy technologist in the sixties and went to work for Tasmania's largest market milk processing company.

I got involved in the early stage of my career with UHT and was a participant in the first UHT operation in Australia, which occurred in the sixties and was based in Launceston, exporting UHT milk out of the state internationally. The challenge of that particular technology led me to leave Tasmania in the late sixties and I worked internationally in UHT technology, setting up recombinant plants and working as a freelance troubleshooter and consultant throughout South-East Asia, Africa and other parts of the world, including Canada, Ireland and so on. In that area of my career I became involved with the operators of companies that were purchasing Australian raw materials for onward manufacture and so on.

Then, returning to Tasmania, I commenced again back with the Bakers Milk company, which later on became part of a larger organisation, which led to various company changes, which grew into today's National Foods. In the seventies I became a member of the Tasmanian Dairy Industry Authority as a foundation member. That authority was put into being by the Tasmanian government with the specific purpose of removing milk quotas to allow all dairy farmers to participate in the lucrative market milk business. It was the first step probably towards deregulation of the industry in Australia and that occurred in Tasmania.

The company changed hands and became bigger. I left and again went out and worked independently in my own field as a technologist and a troubleshooter and spent a lot of time again travelling to places like Pakistan, the Philippines, Taiwan and Korea, working with companies that were involved in making long-life dairy products. They were involved in buying Australian raw materials for onward manufacture and so on. I did all of that work from Tasmania.

In the late eighties I was instrumental in setting up a company in Tasmania called Classic Foods. This was a joint venture company set up to operate out of a small factory in the far north-west of Tasmania. Our specific business was contract packaging. We started our first production in 1990. We purchased bulk milk out of the existing Tasmanian cooperative system and grew that company until I retired on the sale of the company some three years ago. In that 15-odd years the company grew to be a buyer of some 40 million litres of milk a year in Tasmania and

used that milk as an ingredient for making a lot of value added products which were sold in the Australian and international markets.

I am basically retired from the industry today. I am aware of some of the issues that face the industry today and there are many aspects of deregulation which concern me enormously. There are aspects of the current issues which concern me enormously. The dairy industry, unfortunately, has an emotional side, from both the supply and the customer end and, as such, in many cases people are expressing concerns which relate more to symptoms of the industry than to some of the causes, but I am willing to explore some of those aspects of my opinion with you through questions.

CHAIR—Thank you. Can we go to questions?

Mr Wilson—Please do.

Senator COLBECK—From your experience within the industry, particularly in recent times, could you give us a sense of some of the costs in the value chain. The farmers have been pointing out recently that they are getting in the low 20s—cents—as far as the price of the milk is concerned. You still see it on the supermarket shelf for \$2.10, \$2.20. Supermarket branded milk is 50c or 60c cheaper than the company branded product. Can you give us a sense of some of the costs within the supply chain once the product leaves the farm gate: the pick-up process, the package, that sort of stuff. Have you got any figures that you could provide to the committee that would give us a sense of what those costs might include?

Mr Wilson—It is very difficult to give you accurate costs today. I have not been purchasing packing material or running factories in detail for some years now. But in a broad sense if you take the industry now, when it ends up with the farm-gate price which farmers get, it is expressed in many different formats. So you see the term ‘cents per litre’, but in actual fact the industry is paying for the protein and fat, and if you buy a litre of milk with a high protein and fat level it can be standardised to give you a greater volume than a litre of milk with a lower protein and fat level. Within industry it is standard practice to adjust those things, so when you talk about a benchmark or a reference price, what is being published at the moment is very confusing.

All the industry today, under the deregulation terms, has to equate back to some form of benchmark price and, because we are deregulated, the industry is using the export earning price as that benchmark and that, of course, has dropped dramatically in the last couple of years because of all sorts of issues. But, if you take a farm-gate figure for farmers, the expectation of many farmers today of getting high levels per litre in the current deregulated situation is out of context to reality. It was obvious two years ago that the high prices paid to farmers were going to be subjected to some pressure and would not be sustainable and needed to come back or would come back one way or the other.

The global financial crisis probably accelerated that. But, if you are a student of the industry, it has been going through seven- to nine-year cycles of highs and lows since the industry has been recorded, so it is nothing new to have a high, and everybody invests and expands and grows, and then there is a low. The influences on the highs and lows have been varied, from the European agriculture policies to what happens from the United States with the way they conduct their

industry, to the growth in Asia and the various financial crises that have hit the region over the last 20 years.

If you forecast these highs and lows, you should be able to plan, and I think the Australian industry has lost sight during the previous three or four years of the fact that, as these increased prices were achieved because of large expansion, high demand for protein and so on, there would be a point at which those prices would reduce.

So there is an alarm there now because people are being paid less, but it was inevitable that that would come down. You are then faced with a lower price at farm gate and different companies have different ways of paying their farmers in that area.

If you talk about the people that are in the market milk industry, following deregulation or before deregulation occurred they were realising that they would have access to milk whose benchmark pricing would be tied to international returns rather than a fixed farm-gate price or a contract between company and farmer. There were a lot of people in Australia who planned aggressively in the market milk industry prior to deregulation. There were many companies that planned aggressively to enlarge their manufacturing facilities to be able to supply market milk in all states of Australia, particularly all the capital cities, because deregulation was coming, the supermarkets with their buying power would want national contracts, therefore who was in the best position to be able to offer that contract?

So there was a lot of manoeuvring and there was a lot of investment. In fact, one could say that the market milk processing and packaging facilities were overcapitalised in that pre-deregulation period, where companies invested in additional and new factories, processing and packaging systems to enable them to offer a national supply to a chain. In doing that, as deregulation evolved and company ownerships changed, you then had the other manoeuvres of getting national contracts, so there was fierce aggression between the market milk companies and there has been change of ownership, as we all know, in the last couple of years of that structure.

The pricing mechanisms that flow out through all of that change are difficult to pin down, but what is known is that farmers are getting less at farm gate. Within a factory, if you include your increasing capacity and your marketing aims to go national and you are going to increase your volumes, it is possible to negotiate favourable terms for volume buying of packing material and it is possible to invest in new equipment to give you better efficiencies through a factory.

So, between the receiving of the milk and the discharge of finished product, efficiencies have been made in most factories and there have not, in my opinion, been large increases in costs. There would be increases in costs of packaging material and labour and energy closely aligned with the CPI indices that we have experienced in other industries. If you are looking at a farm-gate price plus a processing and packaging cost so that you get an ex factory price, including a reasonable margin on that part of the business, in my opinion there have not been any great price rises.

Then you look at how milk is distributed and retailed, how that functions, and of course today the industry is faced with the enormous if not obscene buying power of the chains, and how they want to nationally buy and market both the brands of the supplier and their own house brand

products, and how they are strategically marketing that to use it in their general basket of products that they offer to consumers.

A lot of those intimate costings in that area are difficult to evaluate. One of the interesting things that I have observed is that some years ago there was a fund set up prior to deregulation to assist farmers out of the industry. That was funded within the industry by putting a levy on the sales of market milk and that levy has recently been removed. In recent times, if the cost of milk has gone down and that levy has been removed, one should have seen a significant change in retail price of milk and I do not think that is evident. There has been some reduction in the retail prices of milk, but in my opinion it is not in balance with the removal of that levy and the opportunity for companies to buy cheaper milk. In my opinion, there needs to be further transparency in understanding how that pricing mechanism has got to that level.

Senator COLBECK—We did have a quick chat to the ACCC about that last night, so that might be something we can come back and have another look at later in our inquiry. So in the context that you say that processing packaging prices have not moved that much, if you could take us back to a time where you were perhaps more familiar with the industry—say, two or three years ago and even if we were to apply some adjustment figures on that—and give us a sense of the costs that you would have incurred at that point in time to access the milk, put it through your plant and put it out the door at the other end?

Mr Wilson—We ran an unusual business at Classic Foods because it was a specific contracting business. We had a milk supply agreement that was put in place with Tasmania's largest access to milk, the old United Milk Tasmania cooperative. Our contract allowed us to offer UMT a premium price for the milk so that we would be guaranteed supply. So we paid basically on their farm-gate returns that they distributed to their farmers, including quality premiums and winter production premiums, and on top of that we paid a percentage, which was quite significant. So we were actually able to buy milk equivalent to a far better return than they could get by putting the milk into other products. That was our basic price.

If I step you back to when we first started in the early nineties, we were probably paying in the low 30c per litre for milk in our business then. We then had a processing and packaging system which probably incurred, at that stage, about equal costs for packaging and processing. In those days it was about 12c to 13c a litre for both. So if you add the processing and packaging together you had about 25c or so to add to the price of milk. So, ex-factory, excluding external wrapping and some handling and warehousing in Tasmania before we moved it across Bass Strait, we were probably handling milk at about 65c to 70c a litre and it would have cost us another few cents to move it around. So we were able to supply UHT milk to supermarkets in Australia and South-East Asia for a price which then allowed them to market it in quite a competitive way. But we were paying a premium for the milk, which got back to the farmers because we paid a co-op.

My personal issue today is that, if you look at how this works, I do not think the farmers and their returns are considered enough by both supermarkets and current processors in terms of that particular aspect of the market milk industry today. Farmers are paid what is left over; they are not paid a price that is based on what would be a good benchmark for them to get a good return. That is the Australian market.

One of the issues that must be addressed in all of this when you get down to pricing and so on—it is all very well for me to quote prices a few years ago and maybe to look at what is there today—is that approximately half of Australia's milk is exported and finds its way into the world market, which is subject to world prices, which we have to live with because we cannot change those. The other half of the milk that is consumed in Australia finds its way into the domestic market in many forms. A major part of it is market milk. In addition to market milk, you have all of the other products that we have, which are value added: the desserts and yoghurts and ice-creams and all of these other products which contribute to value adding. Then you have the manufacturing products that are used within Australia to add value to other foods, and here I include confectionary and bakery products and so on.

If you look at that sector it is using nearly half of Australia's milk. The Australian economy, despite the drought and the other influences, has been fairly static and stable. So why should, in that sector of the industry, an international vagary in pricing upset the ability of the Australian market to return a realistic value to farmers?

CHAIR—Can I ask a pretty dumb question?

Mr Wilson—Certainly.

CHAIR—Two things, if you do not mind.

Mr Wilson—Go for your life.

CHAIR—Obviously in Tasmania you have got two big operators: one is more focused on cows than calves.

Mr Wilson—Yes.

CHAIR—So they really do not compete, although you can say there are two people in the marketplace. One of them sent out a letter saying to the people they supply in July saying, 'Oops! We've got to put the price up to you because there's so much demand in the market,' yet at the same time people are getting a letter to say, 'If you don't sign this contract it's 20.8c,' or whatever. If I go to Coles or Woolies or Aldis or somewhere there is a variation in milk. I checked it on Sunday. You can buy 650 mls of milk at Civic in the supermarket for \$1.79. You can buy three litres of milk for \$5-odd. You can buy two litres of milk for \$3-odd. You can buy one litre of milk for \$2.90. There are various brands, some a lot cheaper than others. How does a consumer know, other than if he is on a budget and wants to buy the cheapest milk, what he is buying?

Mr Wilson—It is very difficult. Milk is standardised to various ingredient levels. So you have whole milk or low-fat milk and the list goes on, and there are 20 or 30 different varieties. Then there are the different packaging systems. The input costs of packaging vary certainly, so usually the smaller the package the higher the packaging cost.

CHAIR—I understand that.

Mr Wilson—And also, when you compare paperboard with polyethylene, like blow-moulded plastic bottles and so on, the cost there changes dramatically. But here we are talking about just a few cents per litre.

CHAIR—So when there are two one-litre bottles or two two-litre bottles and there is \$1 a litre or there is a huge difference in the price, why is that?

Mr Wilson—You would have to ask the supermarkets their policies on those issues, because it cannot be explained usually by the processor who dispatches that milk. You would have a price differential between your range of products, which would be based on your length of run, cost of packaging and all the other bits and pieces in the factory, but at the end of the day, again if you refer to a litre or a two litre as a benchmark, these are cents per litre.

CHAIR—Obviously not dollars.

Mr Wilson—No. No way.

CHAIR—And yet at the supermarket shelf it turns up as a dollar or—

Mr Wilson—The strategy of volumes is important. In some operations they may do all of one particular size or packaging run in one factory and then it may come from another factory if it is another product and then there is transport and so on. But in Tasmania this does not occur.

CHAIR—In the same supermarket there were the 650 mils and then there were the little fellows like 500 mils or something.

Mr Wilson—That is correct.

CHAIR—One was 85c and another was \$1.49 and they were supposed to be both whole milk. When you take the water out of the milk as part of the processing and put it back into some other milk to permeate—and we manufactured milk—should that all be better branded?

Mr Wilson—This has always been controversial. The original regulations that people lived with many years ago were very simple. Standardisation or adjusting milk was not legal.

CHAIR—Yes.

Mr Wilson—This became an issue because of the great variation between farmers within a district and districts within a state, and so on. So over the years there have been various local authorities and states that have set minimum fat and protein levels for market milk and there are regulations overseeing that. When you make any other dairy product, you do standardise. Even if you are making a batch of milk to do a run of cheddar cheese, you standardise the fat to protein ratio and so on. So if you take a litre of milk that is produced ex farm—and you used Tasmania as an example—because of the advanced methodologies of the farmers, AI breeding and so on, an average litre of milk now contains 10 per cent or more of protein than it did 15 years ago and it contains more fat. Therefore, if you buy a litre of milk, in volume terms you can standardise it to give you more than a litre and sell a legal product.

CHAIR—By putting permeate in them.

Mr Wilson—By adjusting the fat out, by putting other things in. Then there is the legal question of whether you can put permeate in or whether you can use this much—

CHAIR—In arguing the case for the farmers—every time they milk the cows, they are losing money under certain circumstances—how the hell does the farmer argue with Coles and Woolies when they say the milk is the same price because they have got milk that is \$5 and milk down here, the same thing, is \$3?

Senator O'BRIEN—Mr Wilson, your earlier evidence was in fact that the milk at farm gate is more likely to be priced on protein and fat content than volume.

Mr Wilson—This was, hopefully, going to be the benchmark for the industry some years ago, because before that it was only ever fat, which became a rather difficult payment system when you realised that you could make very good products from protein and protein was more valuable. So then we swept over to fat and protein and then, again, that has metamorphosed into milk solids, which is a New Zealand term, which is again confusing because that adds the two together, but then at what ratio, because the ratio in milk varies? So, without getting too technical, if you pay for fat and protein, which is what the farmer produces, that is a realistic pricing mechanism for all milk, for all products in all markets. So then the processor puts the protein and fat to various streams of products and sells and makes their margins and declares that. In a cooperative, that usually flows back to what you pay the farmer. But in non-cooperative type companies, it is whatever they can use the ingredients for to make the most money, so if you take fat out of a product you can divert it into cream or other fat-absorbing products and get a premium for that. But you may not reflect that back to what you pay for the milk.

Senator O'BRIEN—Mr Chairman, can I go on?

CHAIR—You certainly can.

Senator O'BRIEN—In terms of 'the market', given the structure of ownership and what is taking place, are you able to make any comments about what has happened in the market and the impact on the competition for farmers' milk in Tasmania?

Mr Wilson—In Tasmania, what has happened in recent times of course is the involvement of National Foods in purchasing lactose. That has created a mechanism where National Foods have a greater number of farmers supplying a larger volume of milk than they had when National Foods had just their market milk operations.

With a levelling off of market sales in soft cheeses and probably in export, as far as the lactose cheese operation was concerned, it would mean that they would be faced now with having farmers that were originally farmers supplying lactose now supplying more milk than perhaps they could sell as a highly value added soft cheese or fancy cheese. So you would have to revert back then to a more basic product—cheese type—which you could store or use in other markets and get less for.

So that mechanism has affected them. They would get less profitability from the lactose cheese operation in today's market than perhaps was being achieved at the time they purchased. That extra milk has to be handled somewhere.

Senator O'BRIEN—Not because of competition but because of a shift in the market. Is that what you are saying?

Mr Wilson—Yes, a change in circumstances in the market. So you are then faced with—like most dairy companies are when you lose sales for whatever reason and you still are taking in your farmers' milk—what we call 'surplus milk' or additional milk to what you can convert to contracted product or markets. The traditional way of taking that surplus milk was to find something to do with it. You need to store it, so very often the obvious two products would be a fat product and a powdered product and the old traditional ones were skim milk powder and butter and hydrous milk fat. Nowadays, whole milk powder and powder from milk concentrate, which is whole milk concentrate powder, or whey protein powders are storable. Then you hope that, as the next cycle of the market changes, you can contract those out and place them. So you would buy the milk at the base price and store it, cover the cost of storage and then recoup that money. If the market was on an incline or an increase when you resold them, the cooperatives were able to pay the farmers a better step-up. But if you are caught now in a movement where you are not seeing that on the horizon and you have to sell off that surplus milk, you are in the hands of the buyer.

So in Tasmania, if National Foods have surplus milk, they would have to unload it to Fonterra in Tasmania or others, to make into a product, and then they would have their own internal pricing for that which certainly would not be above the low prices that they have opened the season with.

CHAIR—I want to ask a question about how the hell we get milk to be in the supermarket at the cost of production plus a profit, given that it has not moved much in the supermarket despite the variations in the international market. In much the same way as if you are a smart enough operator in the saleyards with lambs and you buy hoggets and can get them branded as lambs and sell them as lamb in the butcher shop, it sort of takes the edge off someone that is doing the premium product. The retailer is having home brand Black & Gold type milk, which is really permeate added to all the leftovers from all the processes—which I have had people come into my office in Sydney with and it certainly does not taste like normal milk but it is sold—and it is cheap, so mum buys it because she has got a budget. Isn't that one of the problems? We have absolutely destroyed the integrity of the A1 product by having a B-minus product which is like budget beef which is old broken frizzled bull and old broken mouth cows in the same market. Isn't it the same thing that is happening with milk?

Mr Wilson—That is right. My personal feelings are that the deregulation movement, be what it may and however you argue with the economic pragmatists, the deregulated market, does not give you a level playing field, so people can manipulate it. If the opportunity is there within the constraints of the regulations and business, they do that.

If you believe a level playing field is there because of deregulation, you must belong to a flat earth society. It does not happen that way. So there has to be some form, a more transparent form, where the community and business can see how farmers are getting a fair price for the fat

and protein they produce and how it finds its way to the consumer in the range of products that they buy. This is a complex issue and I do not know how you do it simply. I have got no idea.

CHAIR—I am hoping that out of this process and the good work of these Tasmanian senators will come some good, because I am sure that people like Lion Nathan who have a good—like the Qantas tail—image in Australia will tussle with this. How do they in their own corporate fairness deliver a reasonable outcome to dairy farmers?

Mr Wilson—If you sell to a supermarket chain and you are a large processor of dairy products, you usually are selling a basket of products, not one. You are selling a basket. In terms of the liquid milk market and the fresh market, that basket of products can range from plain milk to modified milks to various sizes, shapes, labels and prices, depending on volumes, discounts and so on, plus yoghurts, plus drink milks, plus flavoured milks, plus soft cheese and so on. So when you sell a basket then a buyer can offset margins in his retail because—

CHAIR—You can have a loss leader.

Mr Wilson—A discount. And that goes on. So when a company sells the basket, hopefully they would price their wholesale price or delivery price in an attractive way—which they do, because they have got to fight for the business—but then the retailer may choose to put a margin on this and take a margin off that.

CHAIR—So buying the basket with consolidated retailing is part of the problem. If you have a nice, family oriented little supermarket next to Coles and Woolies, selling milk at a certain price, under the basket arrangement the supermarket can discount the milk so that when people go into the family one they say, ‘Oh God, that milk’s dear. We’ll go next door to the supermarket.’

Mr Wilson—That is right. This can then be exploited, because if that approach to the market in dairy products continues, then you lose all understanding of where a fair price is being paid.

CHAIR—Exactly. As I said in a previous hearing, the dearest water I have struck is \$2.50 for 350 mls on Virgin Airlines. If you take the bottle home, you can fill it 400 times out of the tap for what it costs you on the plane. People will do that, yet will not pay a fair dinkum price for milk.

In terms of the 20-odd cents that it is worth at the farm gate—and it is aggregated, not disaggregated, for market versus manufactured milk—which turns into an average of \$2.50 to \$2.90 in the supermarket, is there a trail of costs that leads to the \$2.90 being justified? Can you identify the various step-ups so that 26c becomes \$2.90 by the time it gets to the supermarket?

Mr Wilson—It is an in-house issue which is not in the public domain any more. Some years ago it was, because it was regulated. In traditional markets under the old market milk regimes of state authorities there was a price paid for the milk. There was a price which was a semi-wholesale price ex the factory. There was a wholesale price and a semi-wholesale price and then there was a recommended retail price. When there was a change in the price of liquid milk, it usually made the front page of the paper.

CHAIR—So should the ACCC have a look at this? The ACCC in, for instance, Canada, when looking at retail consolidation looks at not just the impact at the retailer end—which is being manipulated now, I would suggest, with the various add-ons and takeaways, the ‘What is milk?’ They look at that, sure, but they also look at the impact on the producer, because if you consolidate the market enough and you have only got one or two people—in the case of Tasmania—to sell to, they have got you, as they say, by the you know what.

Mr Wilson—You are right. To me, over the last few years there have been some changes in the industry which are extremely relevant. Farmers in areas that were not suited for dairying and farmers that were ineffective were encouraged out as the deregulation came in and they were assisted with the payments from the fund that was created for that. So you have dairy farming now being concentrated in the best areas in Australia and, water aside and climate change aside, there has been huge investment in areas that are best suited for producing milk.

If you take Tasmania, which I know best, it has the lowest input costs for a kilogram of fat and protein, I think, of anywhere in the world—if you farm using grass and the modern methodology; if you do not get excited and feed too many additional food rations. So if we have an industry that is one of the best in the world in terms of input costs, and the quality of the milk is as good as anywhere else in the world, yet we cannot make a living from that enterprise, something is wrong with the system. If you then look at the conundrum we have, where half our milk is finding its way into the export market where we are subjected to the vagaries of that market, you have to look at the other half of the industry that is in the Australian market to get more transparency in how these costs are broken down.

I do not know the answer, but if I can just relate some experiences: the recent levy that was put on market milk to assist farmers out prior to deregulation, the levy that has just been removed, was one of the easiest levies to administer from a company’s point of view, easier than any of the other schemes that we had under the old Dairy Corporation and product stabilisation programs and so on. It was a very simple system to administer and manage. There was a levy put on milk which was charged by the processor and recouped by the retailer. If that principle could be worked again, it should be worked across all dairy products sold in Australia, not just liquid milk, and the levy that is applied has got to be in a system that goes to the farmer, that does not come back through the system of retailer, processor.

Senator O’BRIEN—Without discounting the other price.

Mr Wilson—Correct.

Senator COLBECK—From the evidence you have given us this morning, because of their investment in new technologies, better pastures, feeding, and particularly artificial insemination, farmers are effectively now producing a higher value product because of the higher protein and fat in each litre of milk, so the dairy companies are now buying a higher value product per litre.

Mr Wilson—Yes.

Senator COLBECK—Because of the work that the farmers have done over a period of time to produce it.

Mr Wilson—True.

Senator COLBECK—But in the context of the price and the time when you were buying a premium product at the 30-odd cents that you mentioned in your evidence before, in terms of value for the product, they are actually getting paid significantly less at this point in time because of the pressures that are being applied through the pricing mechanisms of the dairy companies.

Mr Wilson—Correct. I cannot understand how a dairy company that is not involved in major exports of products which are getting a low return can use that argument to not pay farmers that put milk into their business, which is going through the retail chain, which has not changed very much at all.

Senator COLBECK—So, given that the companies effectively deconstruct the milk when they buy it and then reconstruct it into the products that they want, they are getting much more value per litre out of the milk that they are buying than they would have been 15 years ago.

Mr Wilson—Yes, correct.

CHAIR—We are grateful for your attendance and the effort you have made to get here. We just hope that out of this may come some explanation of what the hell is going on with dairying.

Proceedings suspended from 10.52 am to 11.22 am

RAINSFORD, Dr Katrina, Private capacity

Evidence was taken via teleconference—

CHAIR—I welcome Katrina Rainsford. Could you give your name, rank and serial number and the capacity in which you appear.

Dr Rainsford—My name is Katrina Rainsford. I am a vet and a farmer from 256 Melville Forest Road, Cavendish and I have a business in Hamilton.

CHAIR—You have got a good season there, haven't you?

Dr Rainsford—We are having an excellent season. We have got feed up to our knees. It is great.

CHAIR—God help us. Would you like to make an opening statement? Then we will ask you some questions.

Dr Rainsford—When I heard Garnaut say that the Carbon Pollution Reduction Scheme or climate change policy was the worst case of policy making in Australian history, I thought it was probably second to the managed investment scheme policy.

CHAIR—Can you tell us why you have drawn that conclusion?

Dr Rainsford—From my perspective, it was a well-meaning policy to save old-growth forests and have a timber industry developed. There was no discussion with local communities. There were no environmental impact studies done. I think there would probably be fairly scant economic or environmental analysis. And it was one of the few targets. I cannot recall any other Howard government specific targeted policies that had to replace the \$2 billion of imports by 2020 or something like that. There was no other target that I can recall in the Howard years. The interesting thing is that the suppliers were never tied to the product. Even now there is nothing tying the people who are buying Timbercorp and Great Southern to continue to produce timber.

CHAIR—In terms of the impact, have you been in the press—like in the *Weekly Times* and features like that?

Dr Rainsford—My history with managed investment schemes is that I was a councillor with West Wimmera shire from 1997 to 2000. We had some high-rainfall sandy rubbish country around Dergholm, Dorodong. I am a vet and it was always a trace element problem area and it already had some pine forests in it. That was the first land in our shire that was engaged with blue gum plantations and I was not negative to the industry then. I thought it was a legitimate industry that had a legitimate, profitable end. It was only when I started asking questions and a lot of the questions could not be answered that I realised it was actually a fairly engineered industry with questionable outcomes. So in 2005 I put a submission in to the taxation review.

I do not know how much of the history you want. My background is family farming in the West Wimmera; grew up in a soldier settlement area. I have been a vet in the south-east of South Australia for many years. I have worked through the rural property trusts. Remember the Western Australian model where soup companies bought farms and people leased them back? I had clients in the south-east of South Australia and western Victoria that got engaged with foreign loans all through the early nineties rural crisis and they sold their properties to rural property trusts, leased them back and it all ended up in tears. Everybody moved on and everything fell over.

CHAIR—In your experience in your district, that would have been one of the early rotations. Was that Timbercorp or Great Southern? That would be Timbercorp, would it?

Dr Rainsford—We have got both Timbercorp and Great Southern in our shire. There is only a little bit of harvesting that has happened so far. It has not been a huge amount. It would be on the precipice of it now.

CHAIR—So in terms of the wind-up of these companies, are your concerns about prime agricultural land being sold off overseas?

Dr Rainsford—That particular issue, yes. It is appalling that we have subsidised the conglomeration of land and the receivers are only offering it in one-job lot. There are plenty of farmers in this area that would have a crack at buying that land back, but they are not getting a look-in. I am appalled that local, state and federal governments all had a part to play in this and they have all just stood back and let the receivers tidy up the mess. And they cannot wait to get it off their books. It is incredible. If you had actually gone to an electorate with a policy that, ‘We’re going to amalgamate land and then sell it off and, by the way, it will be a global financial crisis and the only people with any money are some of the players that were involved in the global financial crisis, but you local people are not going to have a look-in because it will not be 1,000 hectare lots, it will be 150,000 hectares’—

CHAIR—I want to throw this to Senator O’Brien but, before I do, I want to ask about the first one or two rotations on that sandy soil. I presume the sandy soil really was not capable of supporting the forest that was planted on it. The rush was to get the tax deduction and get the trees in the ground.

Dr Rainsford—I do not know the figures from the harvesting there. I do not know whether it has actually been harvested yet. A lot of that land is going over to pine, too. SAPFOR was buying quite a lot of that lower West Wimmera country for pines. That is a different rotation. It is probably a higher value and drives an industry, but it is a lot more extended lot rotation. So I am not sure. It seems to me that the forestry industry has always had to be subsidised and this is what we should be debating: how much subsidy do we give it and do we re-evaluate what timber industries we can afford? I call it woodchip welfare.

When it comes to woodchip production they seem to have transferred a low-value, highly subsidised woodchip industry from public land to private land and it has come out in evidence that nobody could afford to hold the asset, the public land. Somebody had to take a loss. If they knew all along that people had to make a loss, that is incredibly wrong. But the debate we need to have is: what is the true value of providing toilet paper or providing glossy high-value printing

material that drops out of the middle of your magazine and nobody reads it? What is the true environmental cost of these glossy magazines?

If somebody has to be losing money along the way, it is fine when private industry rip each other off—I suppose that happens and sometimes people will sue each other—but when a government promotes a policy and taxation laws and then turns a blind eye when these deals are going on, I think that is appalling. They should come clean and say, ‘Look, we have to subsidise this and somebody has got to take a loss and, by the way, it will be the investors in the city that think they are saving old-growth forests or people with a tax problem.’

Senator O’BRIEN—Or people who want to make some money. The evidence we have had so far in this inquiry is indicating that it is probably fairly lineball in terms of employment over the longer term between plantations and, say, agriculture, depending on what type of agriculture, given the general decline in employment in agriculture and the increasing size of properties, bigger tractors et cetera. What can you tell us about your region and employment available in both the plantation industry and in agriculture?

Dr Rainsford—I do not think anybody has done the figures well enough. I am in the Southern Grampians Shire Council and the Southern Grampians shire now. I do not think Hamilton has missed a beat as far as the hiccup with harvesting. Jobs that were involved with trucking stock or carting fertiliser for pastures and those sorts of industries have been replaced with another. It was sitting in limbo for a while. But we have not had a huge unemployment problem. I think the main issue is that there have been some maintenance and heavy machinery industries that have geared up to service the perceived forestry employment and I have heard that a business had a forced sale the week before last in Casterton—had to sell half their plant. I know that a local nursery that has been in the front page—ERA, I think that one was—has not been paid for some of its work. There are small creditors that have lost out. I do not think that it has really brought a huge amount of employment. I think there have been more ads and advertorials about the impact of the new industry than there has been actual employment.

But what should have been a sustainable diversified industry has not ended up that way. There is another issue: we still do not have any planning controls. There are water issues to do with plantations. Professor Sherwood’s report—the land use change, water, plantability study—has been done with the CMAs and some shire support and models the impact on catchments. I think that is a really relevant issue and there are still no planning regulations that will protect that. We have a huge increase in the number of foxes, and for wild animals which are protected species, particularly kangaroos and wallabies, there are a lot more car crashes and things like that.

There is a very small area of Australia that is high-quality, reliable—in inverted commas—food production. It maps the same area in which perennial rye grass will grow. I cannot quote you the figure but it is a very small percentage of the Australian landscape and we have now put a percentage of that into forestry, which has a history of being subsidised, and we are going to have to continue to subsidise it in some way, even if it means that we have 10 per cent of our most productive and food producing area producing woodchips or those sorts of products. Maybe it will be high-value timber. You have reduced your economic return in that area.

Some areas benefit, like Mount Gambier, Tarpeena and Nangwarry. It is a concentration of industry and it is not necessarily where the product is. It is a huge footprint that has to go into

producing those jobs in those big regional centres. Hamilton has not actually got a huge boost in employment out of the forestry industry. There has been some but it is only small numbers and we are not sure whether there is sustainable ongoing work. Our shire is pro the forestry industry; I am pro a sustainable industry.

If it means that the investors have to lose money or we have to lose valuable water resources and we lose some other lifestyle attributes along the way, I am wondering how valuable it is.

This is another point that I really want to emphasise: what is the future? How are future companies going to manage these businesses if there is no government policy which makes them sensitive about how they manage those plantations, if it is only a regulatory role to control foxes and vermin and fire control? My feeling is that these industries lived and died by political power because they were in favour of the political parties of the day and their existence depended on government policy. I realise that the family farmer is dead meat because we are not dependent on government policy. Our removal and the new players are dependent on government policy, but we did not need political parties to exist because we did not need a bit of legislation that said we could exist, or we had a tax advantage to exist. The new corporates with the superannuation funding or the managed investment scheme funding have a decree of parliament, so they lobby parliamentarians for their very existence.

What worries me is that down the track, if there is no public policy that decrees their existence, they have the title to land by law and they have the right to do whatever they like with that land under the local government laws of the day. And currently there are no restrictions in Victoria at all, so they will just do whatever they like with the land. If it is a fox haven, there are not going to be pressures for them to go out and do the poisoning. That worries me. The fire risk is a huge issue.

But the other issue is that, from what I can gather, the land sold at about a third of the value of what they were paying for it 12 months ago. Our shire rates have been going up because of the need for the shire to increase their rates by five or six per cent a year. The valuations on agricultural land has gone up and most of the rate revenue comes from the farmer landholders, but from what I can gather the timber industry would challenge the rate valuation just about every year, saying that they were being overvalued. What concerns me is that, now they have actually bought the land for, say, \$1,400 a hectare and the fellow next door is going to be valued at \$3,000 to \$4,000 a hectare, they are not going to be paying a fair share of their rates.

Senator O'BRIEN—But you would challenge that, wouldn't you, because it was not a genuine sale of individual properties? It was a job lot, a fire sale effectively, because of a liquidation of assets.

Dr Rainsford—Who is going to challenge it?

Senator O'BRIEN—I would presume all of the local government bodies would be challenging or resisting any attempt to downgrade valuations, as would, effectively, local landholders who had not been given an opportunity to purchase at fair market value, which is what your evidence is.

Dr Rainsford—I can only hope so.

Senator O'BRIEN—I would presume that. The other thing I should draw to your attention is that we have evidence from Dr Jacki Schirmer about studies into employment in areas where the timber industry has been established, comparing that to employment in agriculture, and I can refer you to the *Hansard* of this committee so that you can have a look at that. I am not proposing to debate it with you now.

Dr Rainsford—A lot of that is all about perceptions.

Senator O'BRIEN—No, I think it was more than perceptions. It is not a point that we can debate without you looking at the evidence, so all I am doing is drawing it to your attention so that you can have a look at it. In terms of the issue of productive land in your area that has gone to forest, I think you described it as some sort of rubbish country with high rainfall that initially went—

Dr Rainsford—The Dorodong area initially was low fertility, but there is a little pocket of higher rainfall there. That is where it started. It had a little area between Penola and Casterton that had good, high rainfall.

Senator O'BRIEN—Other than that, what sort of country has been converted from farming to forestry? Can you tell us what industry, what agricultural pursuits, were previously conducted on the land?

Dr Rainsford—It was the West Wimmera, the initial country, that mainly went. In the southern part of that was the better drained cattle country, but it was also sheep country. It is going from Powers Creek near Edenhope—traditionally it would have been getting a 600-millimetre rainfall but now has probably only been getting 300 mils—right down to the coast. So it is dairying. There is a lot of dairy country that has gone and a year ago that was fairly profitable and will come back again; so dairy, beef prime land and also cropping country. But also it is over around the Ararat area, a long way from any commercially viable trucking. The transport of the product is an issue. The plantations have basically been planted outside the rainfall zone and the transport zone because initially the mantra was 800 mils of rain and 100 kays from Portland. So from the local government's perspective I am concerned, too, that the development has not been tied to the local infrastructure development and we may not get our industry developed down at Portland after all.

Senator O'BRIEN—Do you assume that, if a viable plantation sector is not being created, there will be a reversion of land from plantation to agriculture, as is occurring in part in New Zealand because of the higher value of agricultural operation that is available for competing land?

Dr Rainsford—The local farmers that have all been here for years thought that there would be some pretty cheap country come on the market and they would have to work out how to get rid of the stumps. I would be telling them—and these are my fellow councillors—'It's corporate land now. You won't necessarily get a look-in.' I thought Timbercorp would stay for the long run and actually go into other farming. Great Southern had shown that they were interested in other pursuits as well. So I thought they would just go into other farming and there would be a corporatised farming area. I beef about it, being a family farmer and being more interested in Australians owning Australian assets, particularly land and water. I cannot understand why

Australians do not value actually owning the land and water of Australia and why we are not marketing our produce and having a bit more authority. That is my personal belief.

So you are asking me: what sort of country? Everything. There was no restriction. It was whoever was selling. It was based on whoever was retiring. Macquarie Bank or the Macquarie investment group, whichever they are, seem to target one particular area and then go and visit everybody until the price is up. Then they are looking for job lots of about 10,000 hectares or something. They are still buying in this area and they have still got ads in the local paper for purchasing land. What also concerned me was that agents for the timber companies would go and visit people and sometimes they were quite elderly people, in their 90s, living on their small property down in Macarthur. They would have people visiting them and pressuring them to sell.

Anyway, I want to look at the future. I am interested in the future, to make sure that the ratepayers are not disadvantaged—the ones that did not take the big money.

The value of their land has increased and the developers have actually decreased the value of their land next door. We could be paying more rates in proportion and I am glad that we will be able to challenge that, but we will have to do the work to do it, and I am concerned that Great Southern will be sold just like Timbercorp to foreign investors and that was not the primary reason for our giving tax advantages. And I question, once all of the subsidies and everything are gone, that it is actually a higher value than food production.

CHAIR—It will not be. I am going to throw to Senator Richard Colbeck, a smart young man from Tasmania. Could I just ask, though, in terms of your experience as a local vet, have you dealt with many people on the burnt-out end—that is, the people that made the investment and lost their dough?

Dr Rainsford—No. I heard there were a few people that sold and then reinvested, but I have not tracked them down.

CHAIR—No worries.

Dr Rainsford—I heard that a lot of the investors were in the mining industry and from Western Australia, on 150 grand and looking for an investment, so I have not necessarily come in contact with them. I know city investors. I know some children and friends of mine with young families that invested in them and would have done their dough. The locals knew it was too good to be true and I think most of them would have put their money—

CHAIR—Yes. You will at least be pleased to know that the CEO that was at Great Southern is now doubling up, because he is coming back to sue them all to collect the loans that he has bought off Bendigo Bank.

Senator COLBECK—Ms Rainsford, the plantations are, what, 10 or 11 years old now, roughly? That would be about the age, if they are coming to maturity for harvest. Is that about right?

Dr Rainsford—Yes. I took a picture yesterday of Keranda, which was 1999, so it is 10 years old, and they look pretty spindly. That was between Dergholm and Poolajelo.

Senator COLBECK—Okay. It just gives me a sense of the time frame. Going back to your comments with respect to selling it all out as one job lot, is it your view that it might attract a higher value, although perhaps take even longer to get rid of, if it were to be sold in smaller lots?

Dr Rainsford—Definitely. From reports in the media, in the horticultural area there were people willing to offer more than what was received. Yes, there are a lot of young and middle-aged farmers who are still pretty excited about farming and looking for opportunities to grow and develop. We are all a bit uncertain of what the real value of our land is now because, whilst the timber companies were not buying it all, they were making other people compete up to the market, so farmers competed and paid up to that money to make sure they kept the land in farming, especially if it were neighbouring property. So we are not sure what the real market is now, but they would definitely have a crack at it. I am sure of it.

Senator COLBECK—There is some evidence that the committee received last week or the week before that might assist you in that process with respect to land values. It might have been the same research. Was it? Yes. In respect of the company challenges to the land values on rating, I just want to clarify whether that is occurring now or whether that was an annual occurrence.

Dr Rainsford—It is very difficult for me to expand too much on that. It is only word of mouth and hearsay, but you probably know the people that you would contact.

Senator COLBECK—The reason that I ask is that there is plenty of printed evidence of what the companies said their land was valued at. But if, at the same time as putting that value on their books, they were saying to you that they did not think it was valued at that for the purposes of rating, it does raise some other questions. That is the reason I was asking.

Dr Rainsford—Yes. I would really like you to investigate that. You should be able to do that through the Valuer-General's office, because it should be all on record, shouldn't it?

Senator COLBECK—It should be. If they were achieving outcomes, that would be right.

Dr Rainsford—Yes.

CHAIR—Is there anything further that you would like to add?

Dr Rainsford—No.

CHAIR—What has happened to Nareen?

Dr Rainsford—Nareen has got a lot of blue gums.

CHAIR—Oh, bloody hell!

Dr Rainsford—It is about to get a lot of wind towers, possibly, and it is still more sparsely populated. You are talking about the Nareen grazing property?

CHAIR—Yes.

Dr Rainsford—That is still in farming.

CHAIR—Is it? Yes, the dear old Lloyd's of London did not work out too well and I was wondering if they then slipped to MISs.

Dr Rainsford—No. I think that all changed hands. What I am concerned about is that we had a retirement plan for agriculture, not a vision for agriculture. If we had had a plan for cluster settlements—at least people had been off to fight a war and serve their country to get three per cent interest rates for 30 or 40 years or whatever. At least they have done something useful for their country. What I would really hope is that we have a vision for agriculture and that we value that it is Australian farmers. I do not see why you should not have that as part of your constitution and values of all political parties. I would like to ask a question of the Labor senator.

CHAIR—We actually ask the questions!

Dr Rainsford—Yes. I would like to ask you all to think hard about whether you actually value that Australian land and water is in Australian hands. And these are farmers that have arrived from New Zealand and become Australian. We have the English immigrants come and buy land. That is wonderful. Importing actual farmers is a great thing.

Senator O'BRIEN—Ms Rainsford, I am a Tasmanian senator and I can tell you, we have an awful lot of New Zealand dairy farmers who have come to Tasmania. I do not know that they are currently all Australian citizens, nor are they required to be.

CHAIR—But they are here.

Senator O'BRIEN—I do not think the Labor Party is the only party that envisages that people other than Australians will own assets in this country.

CHAIR—Don't let all these people make their self-justifying statements to you! This committee is all about how in the hell in the future, if we have got nine billion people, do we provide food that is affordable for an environment that is sustainable and a farmer that is viable. So there you go. We are all as concerned as you are.

Dr Rainsford—That is right. The thing that I am concerned about is that the managed investment schemes policy is still live and if we have that combined with an ETS. The farmers are looking for alternatives and we were looking for diversification with forestry. You are aware of the Timber 2000 Group, or some such name: family farmers all grew a few trees and they lasted for about 10 years and then they wound up because their marketing was not good and there was the issue of the managed investment schemes competition. Farmers thought, 'Yes, we'll take a piece of the action. We can incorporate that into our farming program,' and they have the same attitude to carbon trading: 'Yes, we can incorporate that and do some trees for sequestration and we think we can incorporate that into our farming equation,' but if there is a huge tax incentive or carbon trading incentive, it will be just like managed investment schemes.

CHAIR—It will be a lawyers' and a bankers' feast.

Dr Rainsford—Yes, it gets pushed aside. It is easier for a bunch of suits in Melbourne or Sydney to deal with this handful of landholders, or one landholder, and not a thousand.

CHAIR—We have to go. I thank you for participating at very short notice. You are also the president of the local VFF, aren't you?

Dr Rainsford—Yes, currently the DC president.

CHAIR—God bless you! If it gets too wet there, can you send some rain back up towards Wagga?

Dr Rainsford—No, you want to send some stock. We have got too much feed and we need some agistment cattle down here.

CHAIR—You pay too much, though. You charge too much. I will do a quick deal with you: \$3 a head a week and I will send you some!

Dr Rainsford—Thanks very much for the opportunity. I hope it made some sense.

Senator O'BRIEN—You are not allowed to do trading at the Senate committee's expense, thank you.

Dr Rainsford—We are depending on all of you.

CHAIR—Thank you very much.

Proceedings suspended from 11.56 am to 12.18 pm

DONNISON, Mr Bruce, Managing Director, Fonterra Ingredients Australia, Fonterra Australia Pty Ltd

MALLINSON, Mr David, Financial Officer, Australia New Zealand, Fonterra Australia Pty Ltd

Evidence was taken via teleconference—

CHAIR—Welcome. If you would like to make an opening statement, we will then go to questions.

Mr Donnison—Thank you, Mr Chairman. Thanks for inviting us to appear before the committee. Unfortunately, as you can appreciate, we could not be there physically, but we do thank you for accommodating us on the phone. My name is Bruce Donnison. I grew up on a dairy farm in the Waikato in New Zealand and was a farmer myself prior to joining Fonterra.

CHAIR—You barrack for the All Blacks, by the sound of you.

Mr Donnison—Yes, I do.

CHAIR—Righto. You have to get that on the record early!

Mr Donnison—Thank you. I have worked for Fonterra for 22 years and have been in Australia since 2003. Today I am the Managing Director of Fonterra Ingredients Australia, which means I have responsibility for all our dairy commodity business and milk collection in Australia. My colleague here with me today is David Mallinson, the CFO for Fonterra Australia and New Zealand business. David also has had 15 years of experience in the Australian industry, having started his career with United Milk in Tasmania.

Fonterra is a dairy cooperative based in New Zealand. In Australia we operate 12 dairy manufacturing sites. We employ some 2,000 people in Australia and more than 1,500 of our employees are in regional areas. We collect around 20 per cent of the milk produced in Australia and last year we paid out more than \$700 million to 1,500 Australian farmers for their milk. The Australian manufacturing milk price is predominantly dictated by the global price of commodity products, set in US dollars. There is a direct correlation between dairy commodity prices and the farm milk price that we pay. Fonterra has some of Australia's leading cheese, butter and yoghurt brands, but ultimately two-thirds of the milk that we collect goes into bulk dairy commodities such as powder, proteins, bulk butter and cheese.

Over the past three years dairy commodity prices have experienced extreme volatility. Due to the global recession, dairy commodity prices fell more than 50 per cent in 2008 and this volatility has been a major challenge for the entire industry and has impacted farm-gate milk prices. Fonterra is acutely aware that many of our suppliers are experiencing financial hardship as a result of the current milk price. Farmers affected by drought or high debt are finding it

especially tough. Fonterra has little control over the key factors affecting farm-gate milk price—that is, the global commodity prices and the Australian dollar. Positively, though, we have seen some strengthening in prices recently, but a lot of upside has been lost with the Australian dollar having peaked in excess of 90c in recent times.

Fonterra is a cooperative and has always had strong cooperative principles. As a result of this parentage, we take a proactive farmer approach in our dealings with Australian farmers. Our current manufacturing milk price remains above the average rate paid by other processors. We are contractually obligated through our agreement with Bonlac Supply Co., to pay a competitive manufacturing price in Victoria and Tasmania and in recent years we have exceeded our obligation, demonstrating our commitment to our Australian suppliers. Last year we exceeded our minimum price obligation by some \$28 million.

On top of this, we have extended our access to interest-free loans to our suppliers, created a special payment for drought-affected farmers in northern Victoria and continue to provide free on-farm support through our field staff scattered throughout Australia. I would like to thank you for the opportunity to make these opening remarks and leave it with you, Mr Chairman.

CHAIR—Thank you very much.

Senator COLBECK—You have talked to us and your submission talks about the volatility of the international market. Can you give us a bit of a sense on where things are tracking now and give us a bit of a precis of what has been happening with your auction system over the last few months as far as clearance is concerned and pricing?

Mr Donnison—Sure. The current market as it stands at the moment has been one of recovery. The market price itself is very much determined on the dynamics of supply and demand. Over the last 12 months we did see significant demand drop off as a result of the financial crises around the globe. Most commodities were affected, not too different to what we saw with the dairy commodities. Right now, however, we are seeing a recovery in pricing, which is great news. We have seen a significant shift from the lows for whole milk powder, for example, at about US\$1,850 back in March this year to where we see it today which is around US\$3,000. So we have seen some significant movement in the price. We are also getting out to our farmers that demand is coming back. We are seeing a lot of the customers that disappeared in the latter half of last year come back into the pipeline and that is all good news for demand for dairy products.

The global trade system that Fonterra operates is one of transparency, where a very small proportion of product coming out of both Australia and New Zealand is presented to the global trade. We have a select few customers on that particular system. Basically, it is set up to give a transparent view as to what the market is paying for dairy commodity prices at that particular point in time.

Senator COLBECK—Is that information available for us to have a look at? Is the site that shows that publicly available, or are you able to give the committee some results of that process over a time frame, say, from the beginning of the year to now?

Mr Donnison—Sure. We can give that information should the committee select it. We can give you access to the website. There is a website that anybody can go to. In terms of the activity

in the website, obviously it is confidential from the perspective of the trading partners that we have on that system, but the website itself can be made available.

Senator COLBECK—But you can see the results of it, without seeing the trading activity that goes behind the process?

Mr Donnison—Absolutely.

Senator COLBECK—You mentioned demand returning. Can you give us a sense of who slipped out and who is coming back in?

Mr Donnison—I think it is the case that we need to go back some 24 months. In the last 24 months, the behaviour of our customers has been such that we have seen prices go to record highs. If you recall, powder prices got to as high as \$5,000 a tonne.

Senator COLBECK—Yes.

Mr Donnison—When we see price escalation like that, we do see behaviours with our customers. Obviously, they are looking for security of supply. However, when the global financial crisis came and hit us in the latter half of last year and we started seeing prices depressing but also demand falling off quite significantly, that is when the prices basically depressed quite significantly, between November and March this year.

Senator COLBECK—You mentioned the spike to \$5,000 a tonne and the current price sitting at about \$3,000. Where does the \$3,000 sit as far as the long-term supply price curve?

Mr Donnison—Dairy Australia would have a lot of this information in terms of giving a view as to what the long-term run is for at a historical level for whole milk powder, for example. We see whole milk powder in the long-term forward view—and long term for us is something like 12 to 24 months—sitting in the range of US\$2,800. The big driver here, however, is not necessarily the commodity price but what is also happening with the Australian dollar. The movement in the Australian dollar and the appreciation against the US dollar has significantly diluted any gains that we have seen in commodity prices.

Senator COLBECK—Is the New Zealand dollar doing the same thing?

Mr Donnison—Yes.

Senator COLBECK—It is? So in that context, I note that you have given an end price to your farmers in New Zealand. How come if the New Zealand dollar is doing the same thing as the Australian dollar you cannot do the same thing here?

Mr Donnison—We run a slightly different system between the two countries when it comes to milk price. The New Zealand system is very much based on a commodity milk price plus the value added contribution from businesses from all around the globe. That feeds into the milk price for New Zealand. Here in Australia we start off with a view as to where the price is going to be. We take into account all sorts of dynamics, including a view on foreign exchange, and

give an opening price to our farmers and proceed with step-ups in due course as a result of market conditions.

Senator COLBECK—So that return that you are talking about from sites all around the globe is effectively an assessment of what profits you are going to make in each of those units and that gets fed back into the price that you quote to New Zealand farmers?

Mr Donnison—I will just hand over to David Mallinson.

Mr Mallinson—The price that is declared in New Zealand is a total milk price which has two components—a manufacturing price and what we call a value-add component. The manufacturing price at the moment is forecast at NZ\$4.65 for milk solids and the value-add is 45c. The 45c essentially is the dividend that Fonterra pays to its shareholders for its global investments. It is outside this milk collection in New Zealand.

Senator COLBECK—Those investments outside of New Zealand include the investment that Fonterra has in Australia?

Mr Mallinson—It does, yes.

Senator COLBECK—Okay.

CHAIR—So that would include that any extra profit that you can get out of a margin in Australia goes back to shareholders in New Zealand. There is no opportunity, is there, even though we have plenty of people over here that barrack for the All Blacks, under your charter for any Australian farmer—even though they might be a Kiwi—to be a part of your co-op?

Mr Donnison—Currently the structure that Fonterra has with its shareholding is limited to farmers within New Zealand. There is no opportunity currently under the share structure to allow a holding or an ownership level in Fonterra outside of New Zealand.

CHAIR—So given that we have this open trade between us and we are almost blood brothers, why wouldn't you allow an Australian farmer—it would be great signage, shall I say, for Fonterra—to be on an equal footing? But they could not be a member of the co-op.

Mr Donnison—I appreciate the question. Unfortunately, I am not the right person to answer that. It is very much a government decision.

Senator COLBECK—Can I just go back to the price: is that in New Zealand dollars?

Mr Donnison—The prices I quoted were in New Zealand dollars, yes.

Senator COLBECK—Is it possible to get a break-up of the 45c based on source of return?

Mr Mallinson—I would have to take that away and check. I think you will find that it is going to be reasonably confidential. We have joint ventures with other parties around the world, but we could probably give the proportion relating to Australia.

Senator COLBECK—If you can give us that on notice, I would appreciate that. That would be great. You mention in the submission that you have given to us that you are aware of some cheese product that was being brought in from the US, bulk cheese to a local manufacturer. Do you have any sense of the volume of that sort of product being imported into the country?

Mr Donnison—From my perspective, what has happened in the last two years—and you can get this information from Dairy Australia—when prices were higher we did see a significant increase in dairy products coming in from other sources outside of Australia. At this particular point in time, a lot of that would have been going to all sorts of customers here in Australia and they would have been taking the opportunity to be able to source their products, if they could find it more cost efficient for them.

CHAIR—That may have been subsidised product from those countries.

Mr Donnison—It is pretty hard to comment. I only look at the import numbers—where it has come from. I am not too sure. I would have to clarify it with Dairy Australia.

Senator COLBECK—That would depend on the country of source, I suppose. Your submission also says that in the 2008-09 season you had a record seven price step-ups in that period, but that was also the first time that you ever had a step-down, wasn't it?

Mr Donnison—That is correct. That is in the previous 12 months, yes. A record seven step-ups, if I can just clarify, would have been for the previous year, the 2007-08 year.

Senator COLBECK—Okay. Your submission says 2008-09.

Mr Donnison—That is incorrect. For clarity, that would have been the 2007-08 year. That is when we saw record prices internationally. 2008-09, which is the year prior to this one that we are currently in, is the year that we had that step-down.

Senator COLBECK—Okay, that is fine. That is a good clarification.

Senator O'BRIEN—Just another clarification: when was the price of powder, as you put it, US\$5,000 I take it a tonne?

Mr Mallinson—Sorry, what was the question again?

Senator O'BRIEN—You talked about the high in the market of \$5,000 per tonne, which I presume is US\$5,000 per tonne.

Mr Mallinson—Yes. That occurred in the 2007-08 year.

Senator O'BRIEN—Yes. What part of the year?

Mr Mallinson—From memory, Bruce, this would be December through to about March?

Mr Donnison—That is correct, yes.

Senator O'BRIEN—What was the currency at that time?

Mr Donnison—The currency would have been reflected. I think I understand where the question is going but the answer would be—

Senator O'BRIEN—Yes, because there was not much difference in the value of the currency then and what it is now, was there?

Mr Mallinson—In 2007-08 it probably traded between 70c and 80c.

Senator O'BRIEN—In 2007-08? You are saying that in the latter part of 2008-08 it was in the range of 80c?

Mr Mallinson—No. In the later part it actually did get up to 95c for a brief period of time—

Senator O'BRIEN—Yes, that is right.

Mr Mallinson—before it slipped back to 65c.

Senator O'BRIEN—Yes. It did slip back to 65c, I know, because I happened to go overseas just as it did, in September. In the lead-up to that, I was looking forward to a rate somewhere around 90c. So at the latter part of 2007-08 it was closer to 90c than 80c, as I recall it.

Mr Mallinson—The latter part, yes.

Senator O'BRIEN—The international price was US\$5,000 a tonne. What were you paying in milk price then?

Mr Donnison—Just a point of clarification: that would have been at the end of the financial year.

Senator O'BRIEN—Yes.

Mr Donnison—Those sales would not have been recorded until the next financial year. So the impact of that \$5,000 a tonne and the 90c rate would not have been seen until the next milk price, which was in the following year.

Senator O'BRIEN—2008-09.

Mr Donnison—Correct, yes. What we saw then was some depression in market prices from August in 2008.

Senator O'BRIEN—So in July when the dollar was high, and the international price was high, what were you paying?

Mr Mallinson—In the 2007-08 year, in kilograms of milk fat we paid a bit over \$12.

Senator O'BRIEN—Twelve dollars. You make the argument about currency.

Mr Mallinson—Yes.

Senator O'BRIEN—But it does not seem to line up when you look at those circumstances where the dollar was high and the price was high and, at the same time, the return to producers was high. Now we have a high dollar and we have a low price and a disproportionately low price to producers. How does that work out?

Mr Mallinson—I am not sure if you have our submission in front of you, but page 5 has a graph correlating both milk price and whole milk powder price where milk price is in Australian dollars and the whole milk powder price is in per kilograms of milk fat.

Senator O'BRIEN—I have not got one with page 5 on it. Which submission are you talking about?

Mr Mallinson—The Senate—

Senator O'BRIEN—There are a couple of Senate committees going.

Senator COLBECK—It might have been the references committee.

Mr Mallinson—It is the Economics Committee.

Senator O'BRIEN—Okay. We will have a look at that.

Mr Donnison—Just for clarification again, milk price is governed on the basis of variables, not necessarily on one point in time but it is a culmination of pricing over the 12 months. The effect of climate change also has an effect over a 12-month period. It is very much determined on the terms of contracts and what rates we actually set for contracts.

Senator O'BRIEN—As a layman looking at this, it is a bit like trying to follow 'thimble and pea'. I would have to say that when the price is high internationally and the dollar is high internationally and at one point the producers' price is high, trying to understand why it is not high in comparable circumstances later is a bit difficult.

Mr Donnison—The price itself, the dollar rate per tonne, is very much a demand driven dynamic.

CHAIR—So in July of this year would you blokes in your market intelligence have thought there was increasing demand and increasing costs that would have compelled you to say to your customers, the retailers, that you sell to, 'We are going to have to put the price up'?

Mr Donnison—In terms of the milk that we collect that predominantly goes into manufacturing milk, over two-thirds of our milk goes into commodity driven products and that is what we set our price on. It is based on market returns for those commodities.

CHAIR—So in July of this year was there any increase in demand and cost to you for market milk?

Mr Donnison—We are a very small player in market milk—less than five per cent.

CHAIR—So in terms of the manufactured milk then, if there was increasing demand and decreasing farm-gate prices, the margin would go to the shareholders in New Zealand?

Mr Donnison—No. What we actually saw at the beginning of this year and July this year was that demand was still volatile. We did not see demand moving until around September. We saw prices starting to move in August and September as well and, as a result of that movement, after the opening price letter went out in June, we did a step-up on milk price in September.

Senator COLBECK—You mentioned that two-thirds of your milk goes into commodity driven products. For what proportion of your sales would you actually control the price versus what you have to take a market price for?

Mr Donnison—In terms of our business, all of our prices are based on market return.

CHAIR—Is it five per cent that is market milk?

Mr Donnison—Roughly five per cent of our milk in Australia goes to drinking milk. Let's call it 'drinking milk' for clarity. The other 25 per cent of our milk that would end up in the consumer business goes to retail products like cheese and butter.

CHAIR—So, if I am Woolies or Coles, do you sell me a package which includes a deal on market milk as well as cheese and whatever else?

Mr Donnison—The categories are not bundled. They are sold separately to the retailers and within that package there is a combination of our brands and their own house brands. The house brands are generally tendered products. It is an open tender process between all processors, so the lowest price gets it.

CHAIR—In terms of market milk, in that process, in tendering out to Woolies or Coles, do they say, 'We want so much brand milk and we want so much' whatever you market your Fonterra under 'in the same truck delivery' sort of thing?

Mr Donnison—They put out a tender for house brand between every one and three years, depending on which supermarket it is. Everyone tenders for that separately and then the branded products have to be dealt with separately; they are not bundled. Because you own the house brand, you do not necessarily get your brands there. And, vice versa, people that do not own the house brand can get their brands in there.

CHAIR—So in the house brands that you successfully win the tender for, are you able to reconstitute with permeate et cetera that milk to meet the specification to be able to brand it as retailers' branded milk?

Mr Donnison—The only house brand tender we have in Australia is based in Western Australia and we do not use permeate in Western Australia.

CHAIR—So where do you use permeate?

Mr Mallinson—If we do use permeate, it is when we have variability in composition coming off farm to standardise protein or fat content to make sure that we have a consistent product going out to our customers. Where we use permeate would be on those occasions where we do have that variability coming off farm.

CHAIR—So what sort of an additional profit margin can you get by skimming a bit of the extra protein fat, or whatever it is you skim out to put with permeate, to reconstitute milk to come up to whatever the standard market milk specification is? We have had complaints that ‘black-and-white milk’, sort of thing, really does not taste like milk.

Mr Mallinson—The only time we do this is actually in our plant in Wagga. The amount of liquid milk we have at that plant is very minimal, so the amount we can make under this practice is very small.

CHAIR—Does it bother you that in Wagga, for instance, where there is a daily collection of milk, I understand from evidence that there may be milk that comes in from Victoria or somewhere else that might be three or four days old and mixes in? Is that just a normal practice? You transport interstate into Wagga, do you?

Mr Mallinson—We do not take three-day-old milk. Our milk is processed generally within 24 to 48 hours. The only time we move milk from Victoria up to Wagga is at points of the year where we do not have enough local milk to fulfil local demand.

CHAIR—Bear in mind we have taken evidence from people there. What is the average lapse between when it is milked in Victoria and hits the bottle in Wagga, compared to the local Wagga milk hitting the bottle in Wagga, which can be batched up?

Mr Donnison—Are you looking for a time?

CHAIR—Yes.

Mr Donnison—It would be less than 24 hours.

Senator O’Brien—In terms of the manufactured product, if it is not commercial-in-confidence could you give us a bit of a breakdown of the range of products by proportion of your production in Australia? I mean how much powder, how much cheese, butter et cetera?

Mr Donnison—I will not be able to give you the exact proportions, but I can source that information for you.

Senator O’Brien—That would be good.

Mr Donnison—Just to give you an overview, we have a varied portfolio of commodities, ranging from bulk butter to bulk cheese—those two particular products going to export. We have powder—that is, skim milk powder and whole milk powder. We have also started producing in Australia infant formulas and growing-up milk powders for our customers, particularly into the Middle East and South-East Asia.

Senator O’Brien—Obviously most of those bulk products are exported. What about production for the local market?

Mr Donnison—Are you talking directly with domestic ingredients that we have here?

Senator O’Brien—Yes.

Mr Donnison—We have the same sort of range as well that is offered to our domestic customers on those same commodities.

Senator O’Brien—How does it break down proportion-wise at the retail market and the whole manufacturing market et cetera, if I can call it that?

Mr Donnison—In terms of the ingredients that we produce, it is about a third in each of the domestic ingredients and food services and to the domestic consumer business, being our cheese and butter business, and about a third into exports.

Senator O’Brien—So it splits fairly neatly into thirds.

Mr Donnison—Approximately, yes.

Senator O’Brien—So about two-thirds is exported?

Mr Donnison—No.

Senator O’Brien—Sorry.

Mr Donnison—Just for clarification, of that 100 per cent, only a third of our commodities are exported; a third goes into our branded business, being the cheese and butter; and a third goes into those customers in Australia that also buy ingredients from Fonterra.

Senator O’Brien—It is fair to say that one-third of that is the domestic consumer. It is not so much an international market; it is a domestic market.

Mr Donnison—Very much so. However, the price of those commodities is still very much weighted towards what is happening internationally.

Senator O’Brien—They have not really gone up and down that much, compared to the international price that you just told us. Indeed, that is the evidence that National Foods gave us. Is it your experience that the price you have been getting from the supermarkets has varied to the extent of, for example, your dry milk powder price?

Mr Mallinson—Obviously what will drive the shop price for retail products is the house brand products. The consumer will only pay a certain premium for products above that. I think if you have a look at the dairy prices that were advertised yesterday, or reported yesterday in the *Australian Financial Review*, where Woolworths have been quoted here that they have seen dairy prices come down significantly over the last 12 months, it would be fair to say through the period where we experienced very high commodity prices the margins were affected within most of the consumer businesses in Australia and you are not able to take pricing up by 100 per cent; in effect, that was what happened with the commodity prices.

Senator O'BRIEN—Are you saying that Woolworths said that the prices they charged for the commodities had come down or that the prices they paid to companies like yours had gone down?

Mr Mallinson—The shelf price had moved down.

CHAIR—I have got to say that is rubbish. As a consumer and someone that really monitors this stuff and who sees one litre of milk now \$2.99, it has not come down. Are you pulling our legs or are Woolies pulling your leg?

Mr Mallinson—I am only reciting here what the *Financial Review* published yesterday.

Senator O'BRIEN—I would have to say that I just cannot line that up with my own experience—not that I have conducted a survey, but just observation would tell me that that is not correct. However, the line that I was pursuing was to get an understanding of the breakdown. In terms of the third of your market where you are selling a commodity to businesses that process food in Australia, how is that affected by international price? Is there serious international competition in that market?

Mr Donnison—Absolutely. Our customers are also global customers. Our customers range from organisations like Nestle and Kraft et cetera. However, we are not immune from the impact of global prices when we sell domestically, simply because it is a globally traded commodity. Our customers here, even though we might sell them domestic ingredients, can well source those products internationally if they choose to do so. We did see some of that happen two years ago when prices were high.

Senator O'BRIEN—Is a significant amount imported in competition, or is it just the threat of the price that keeps the market down?

Mr Donnison—The bottom line is that, regardless of where you are—whether it is internationally or domestically here—commodity prices are very much influenced by a market return that is internationally set.

Senator O'BRIEN—I am not sure, but with some commodities the cost of freight would be a significant component, wouldn't it—refrigerated transportation et cetera?

Mr Donnison—Could you repeat that, please?

Senator O'BRIEN—I am assuming that the cost of refrigerated transport for perishables that have a shorter shelf life would push that price up somewhat.

Mr Donnison—And are you referring to cool liquid milk and yoghurts, or cheese?

Senator O'BRIEN—I am talking about cheese and butter, for example. That still has to be refrigerated, doesn't it?

Mr Donnison—Yes, it does.

Senator O'BRIEN—So is that a significant factor in the price? The opportunity cost of imported product would have to factor that in, wouldn't it?

Mr Donnison—Absolutely. But when you are freighting around the world, it is a significant cost if you are an exporter. But then it is definitely factored into the competitive dynamics in terms of shipping product into Australia or, for that matter, out.

Senator O'BRIEN—Yes. You have to bear it when you are shipping to another market, but so do importers to this country have to bear it when they are bringing product in.

Mr Donnison—That is correct.

Senator O'BRIEN—So what sort of factor is that in terms of cost?

Mr Donnison—I am unsure.

Senator O'BRIEN—I suppose it depends on international circumstances.

Mr Donnison—I would not have that information in front of me.

Senator O'BRIEN—It wouldn't be insignificant, would it?

Mr Donnison—I only know the rates that we would pay internationally from Australia. Obviously, that is confidential. I cannot give you that number, but I would say it is on a similar rate. It is not insignificant, no.

Senator O'BRIEN—It is not insignificant, no. The obvious area where you are really at the mercy of the international market is the exported product, where you are competing with product sourced from other countries which may in fact be closer and have a lesser freight rate.

Mr Donnison—That is a real possibility. But just for clarity again for the committee, the commodity business here and the manufacturing milk that we process in Australia is all governed by what is happening internationally in terms of prices. On top of that, the big effect, in terms of international exporting from Australia, has been the strength of the Australian dollar currently.

Senator O'BRIEN—Are there particular markets that product from Australia goes to, in terms of the majority volume?

Mr Donnison—From my perspective and Fonterra Australia's perspective, we export a lot of our product into Asia, in particular—Japan, China, South-East Asia. We do not have a lot of product that goes into South America. Most of our product goes into the Asia and/or Middle East markets.

Senator O'BRIEN—Is that different from New Zealand?

Mr Donnison—Fonterra as a whole has a presence in 140 countries. It has a global network. We leverage out of Australia because of the significant advantage that it presents to us as a business here in Australia.

Senator O'BRIEN—Sorry. I am not sure what you mean by 'leverage out of Australia'. Could you explain that?

Mr Donnison—We leverage the Fonterra sales network so we can place products from Australia into our customers.

Senator O'BRIEN—So you are using the general international market of Fonterra New Zealand to source the product from Australia?

Mr Donnison—That is in part, but we also leverage the capacity, the capability that Fonterra has at a global level—its supply chain network.

Senator O'BRIEN—Thank you.

CHAIR—We may have some questions that we will put on notice to you. Could you repeat what you said earlier. Can you explain to me what Woolworths told you?

Mr Mallinson—It is referencing an article that Sue Mitchell wrote in the *Australian Financial Review* yesterday—22 October—in an interview with Michael Luscombe.

CHAIR—What does it say?

Mr Mallinson—It is a fairly long article. It draws conclusions, from what Michael said to Sue, about pricing in general; how they are negotiating pricing with their suppliers.

CHAIR—The essence of what you said earlier was that Woolies in the *Financial Review* said the price of milk in the supermarkets has gone down.

Mr Mallinson—No, I said dairy prices. It does say milk and wheat. It mentions quite a bit in here.

CHAIR—We might take that up. As part of the operation of Fonterra—this may be commercial-in-confidence—how much profit goes out of Australia back to the cooperative shareholders annually?

Mr Mallinson—I can answer that one. Our accounts at year ended—we have a financial year ending end of July—have not been finalised yet, but I can certainly give you last year's results. Last year our EBIT was \$59 million.

CHAIR—That was the dividend that left Australia?

Mr Mallinson—No, it was the earnings before interest and tax.

CHAIR—Yes.

Mr Mallinson—And that is on a debt and equity base of \$1.52 billion.

CHAIR—Where did that finish up? Back in the hands of the shareholders in Kiwiland?

Mr Mallinson—After the interest is paid up and tax is paid, whatever is left is paid out as part of that value-add component in milk price.

CHAIR—So you do not have that figure, or it is commercial-in-confidence?

Mr Mallinson—I need to send it over. I have not got the tax figure on hand at the moment.

CHAIR—When you transfer that money, do you pay tax on it here or over there?

Mr Mallinson—Here.

Senator COLBECK—Can you just give us a sense, in the Tasmanian market, of the profile of market concentration of buyers of milk? There are effectively yourselves, National and Cadbury.

Mr Donnison—There are a number of smaller players, but primarily Fonterra Australia purchases, of the total volume in Tasmania, around 65 per cent.

Senator COLBECK—You do not know what the other players are at?

Mr Donnison—I am unclear of the actual percentage because it just does not roll off my head, but I know that National Foods would have about 70 or 80 million litres and Cadbury between 60 and 70 million litres, and you have, obviously, a number of other smaller players in Tasmania.

Senator COLBECK—We have had allegations of, effectively, collusion between yourselves and National Foods. How do you respond to that? I mean, effectively, in the context of you putting out a price and them sitting on their price until you have put yours out. Whether you call that collusion or not is another question, so I will qualify the comments with that, but it is an allegation that has been put to us, not one we are making.

Mr Mallinson—Can I just clarify that? The collusion, you are saying, is that we set our price and then they set theirs off ours?

Senator COLBECK—It has been put to us in that context, and they have told us that they wait for you to set your price before they set theirs. Dismiss it if you want to. That is fine.

Mr Donnison—Our milk price is based on market returns and that is based on the international price and taking into account what is happening with the Australian dollar. What other companies do in terms of their milk price is entirely their business.

Senator COLBECK—That evidence that you have just given me—that you actually do calculate costs in your business and apply it to setting a price—is what I am looking to.

Mr Donnison—The price that we set for our Tasmanian suppliers is very much one that we give to our suppliers both in Victoria and Tasmania. The Tasmanian milk price, through Bonlac Supply Co., was a negotiated milk supply agency agreement where the price was the same as Victoria, although in Tasmania we do have two points of the price where we have an adjustment to the milk price based on energy cost and farm milk collection, and that is about 0.55c a litre, simply because of the costs incurred with longer distances and the higher energy costs for running our plants.

Senator COLBECK—How do you see your price sitting comparatively in the market?

Mr Donnison—Today we see ourselves paying a leading manufacturing milk price.

Senator COLBECK—So you would say you are paying the highest price in the market?

Mr Donnison—I would not say we would be paying the highest but we are definitely paying a leading milk price. And I would like to qualify there that it is a leading manufacturing milk price. Considering the business that we are in, we cannot compete with the fresh liquid milk business.

Senator COLBECK—Can you give us a comparison with where you sit in other states?

Mr Donnison—Sorry?

Senator COLBECK—Prices.

Mr Donnison—Yes. Where other dairy companies sit?

Senator COLBECK—You.

Mr Donnison—We are currently paying \$3.74/kg of milk solids today.

Senator COLBECK—Nationally?

Mr Donnison—That is for Victoria and Tasmania. We have other milk prices dependent on the competitive dynamic with the Wagga and/or the Western Australian milk price. How that compares with our competitors? Again, I am not at liberty to actually have that comparison in front of me right now.

Senator COLBECK—You do not have the comparison in front of you or you are not at liberty to tell us what it is?

Mr Donnison—I do not have it in front of me at the moment.

Senator COLBECK—National Foods, for example, claim they pay 3c a litre more than you do on an annualised basis. How do you respond to that?

Mr Donnison—They are in a different business to us. We are in the commodity milk business and we pass those returns on the commodity international market through as the milk price.

CHAIR—Would the dividend returned to the New Zealand co-op shareholders be that 3c a litre? How much a litre would the dividend be that leaves Australia and goes back to New Zealand?

Senator COLBECK—That is if the 3c a litre is real, Bill, so it does not necessarily come into—

CHAIR—But I am asking: related to \$59 million, you pay the tax; do all the things that you want to do with it; the money actually hits your account, which you then distribute to your shareholders without commission. How much does that relate to? Is it a 1c a litre or 5c a litre? What would it be in terms of the milk that it represents here in Australia?

Mr Mallinson—Certainly nowhere near 5c a litre. 1c a litre, to us, is close to \$20 million.

CHAIR—So it could be a couple of cents a litre?

Mr Mallinson—Not after interest and tax it is not, no. The earnings before interest and tax probably get it there, but we have got a debt level here of close to a billion dollars which we have to service, and then we pay tax on whatever is left.

CHAIR—Yes, but you have quarantined that debt to Australia and isolated it from New Zealand—and that is your business. I guess that is a tax arrangement. So it could be, before tax, 3c.

Mr Mallinson—If you look at the money Fonterra has put into Australia over the last seven or eight years since the original deal with Bonlac, it is approaching \$2 billion.

CHAIR—Yes, and I appreciate that.

Senator COLBECK—Can I come back to the annual milk price that we talked about earlier. You have given us figures of NZ\$4.65 plus the 45c production—

Mr Mallinson—Just to clarify that, \$4.65 or \$5.10 is the forecast. That is not what they are actually paying; it is a forecast.

Senator COLBECK—Yes, I understand that is a forecast. That is why I am coming back to that: as a season price forecast. Again, I am just trying to get my head around why, given that

you have similar market conditions, with dollar fluctuations, in New Zealand as you do here, you do not see that you can do the same thing in Australia as you do in New Zealand. I am not interested in the 45c production dividend. We understand what that is for or where it comes from.

Mr Mallinson—\$4.65 converted to Australian dollars at the current rate is not that far away from what we are paying here in Australia.

Senator COLBECK—It is sitting at about \$3.74, so they are very similar numbers. You said earlier that you paid about \$20 million over your obligation in one of the preceding years. That was based on what your opening price was and taking into account the step-ups?

Mr Donnison—No. The \$28 million that I mentioned before was based on what we are contractually obligated to do through the milk supply agency agreement with Bonlac Supply Co., where the arrangement is that we have a competitive dynamic in there. Over and above that commitment we paid out a further \$28 million to our suppliers in Victoria and Tasmania.

Senator COLBECK—Can you explain to me how that works? If it is not as part of step-ups, I just want to get my head around how it actually works.

Mr Donnison—Fonterra Australia and Fonterra in Australia is here to stay. We want to build a sustainable supply chain and that means that we need to have a sustainable farmer as well as a sustainable customer base. We did recognise at the time that, particularly in northern Victoria, there were some hardships being experienced, like drought, and over the last couple of years we have helped out our farmers through all sorts of mechanisms, whether they be interest-free loans or paying a milk price over and above what we are obligated to.

Senator COLBECK—Just to quickly go back through to the structure: so you have got Fonterra New Zealand. What are the structures that sit underneath that within Australia?

Mr Mallinson—The strategic business unit that we belong to is called Fonterra Australia New Zealand, which comprises the Australian business which we are talking about here and all the consumer businesses within New Zealand itself.

Senator COLBECK—I am just trying to get my head around the supply structures and what entity the \$28 million came out of.

Mr Mallinson—The \$28 million is recorded from an identity called New Zealand Milk (Australasia), which is our holding company in Australia, which lodges its accounts with ASIC.

Senator COLBECK—So effectively what has happened there is that the \$28 million that could have gone back through into that productivity dividend element to New Zealand has remained in Australia and been paid as a bonus on top of production. Was it based on supply for the previous 12 months?

Mr Mallinson—Yes.

Senator COLBECK—Now I understand how that works.

Senator O'BRIEN—What has Fonterra's approach been to production capacity of farmers, particularly farmers in Tasmania? Has there been an encouragement to increase production or has Fonterra tried to cap production? How have you approached it?

Mr Donnison—If I go back to when I first came into Australia back in 2003 there was a great opportunity in Tasmania to increase production and allow our suppliers to grow. We have got two plants down there, being Spreyton and Wynyard. At the time Wynyard was full but Spreyton was not and we actively pursued more milk should the suppliers choose to grow their business. In recent times we have had incremental plans on the two existing sites to increase capacity. However, as a result of last year's global financial issues we had to delay capital. There was some \$10 million mentioned in the last 12 months that we were going to be spending at the Wynyard and Spreyton operations to increase capacity to be able to keep up with the growth. We are obligated to pick up every bit of milk that the Bonlac Supply Co. suppliers have in Tasmania. This year in particular we were expecting to be full at both plants and we have plans over the next two years to increase the capacities at each of those plants.

Senator O'BRIEN—So there was in the past an encouragement. When did that cease?

Mr Donnison—It has not ceased. If Bonlac Supply Co. suppliers still want to grow their business they are free to do so. We are obligated through the milk supply agency agreement to pick up every drop of milk that they produce.

Senator O'BRIEN—The rider being that they will get paid at the rate you strike, having regard to international factors.

Mr Donnison—That is correct.

Senator COLBECK—One final thing: can you give us a sense of your involvement in the development of the dairy industry plan, particularly in Tassie, that was developed and I think released about two or three years ago. So that would have been part of the encouragement that you have been working on with the industry that you talked about a moment ago.

Mr Donnison—Absolutely. I think you are referring to Dairy Tas 500.

Senator COLBECK—Yes, that is it.

Mr Donnison—The perspective there is that Fonterra has been an active participant of Tas 500 and, from my perspective, this is a great initiative for the industry down there to see the dairy industry grow. It is unfortunate that we are in a particular point in time where our suppliers are going through a little bit of stress with climactic conditions down in Tasmania currently, hit with obviously what is happening with the financial crisis and the returns on commodities. So we will see a little bit of a dampening of growth. But Tasmania offers a great opportunity for both Fonterra and our suppliers to grow dairy in Tasmania and we are looking at it quite seriously from the perspective of where we head in terms of capacity. We have plans for the next couple of years in terms of incremental capacity on our existing two plants and are looking forward to a bright future for the industry down there.

CHAIR—Thank you very much. In terms of New Zealand government treatment versus Australian government treatment in the emissions trading complexity of dairy farming, do you have an understanding of what the difference in the treatment of dairy farmers between the two countries is going to be or is planned to be?

Mr Donnison—If I can sum it up by saying that the impact on the emissions trading within the Australian dairy sector is unclear at the moment, although there are policy statements out there. We are working very actively with representative bodies here in Australia. The Fonterra business in New Zealand has allowed us to have free access to their information and we have actively involved those bodies in Australia to see that information. In terms of the actual effect it will have on dairy farmers both here and/or over in New Zealand is yet to be seen.

CHAIR—But if you get concessions that we do not get, that could be a major distortion, couldn't it?

Mr Donnison—The answer to that is yes.

CHAIR—Thanks very much. Finally, as part of your PR for Australia, will you be putting some money towards the sponsorship of the Wallabies?

Mr Donnison—We do not even sponsor the All Blacks.

CHAIR—Thank you for your evidence today.

[1.12 pm]

WILLEMSSEN, Mr Ron Gerard, Principal, Macpherson and Kelley Lawyers

CHAIR—Welcome. Would you like to make an opening statement and then we will ask you some questions.

Mr Willemsen—As at yesterday we have 1,968 files opened for individual investors across Australia who invested in managed investment schemes sold by Timbercorp. There are more files being opened today and into next week. So I am here really as a representative for all of those investors for whom we act. On behalf of our clients we will be filing a class action writ in the Victorian Supreme Court against Timbercorp Securities Ltd (in liquidation), Timbercorp Finance Pty Ltd (in liquidation), and Robert James Hans, Sol Rabinowicz and Gary William Liddell as directors of each of those companies. I will elaborate on the basis of the claim during today's hearing, but it essentially concerns nondisclosure of material financial information to the investors. Investors made fresh financial commitments throughout 2007 and 2008, not knowing the Timbercorp group was on the verge of collapse. Their long-term projects were going to cost the investors a lot of money and were not going to deliver the expected returns, or anything remotely near the expected returns. I will tender some documents to illustrate Timbercorp's deception of the investors and I propose also to say something on behalf of all of the clients of Macpherson and Kelley about an inherent problem with the managed investment scheme model for agribusiness investments, especially as it concerns the responsible entity being in a conflicted position and its liquidators likewise being in a conflicted position. Sections 601FC and 601FD of the Corporations Act impose duties which I believe cannot be properly discharged by someone who seeks to serve two masters: first, the banks as secured creditors and, secondly, the MIS investors who have a stake in the projects and claims against the responsible entity and its related parties. That is my opening statement.

Senator O'BRIEN—You did not mention it in your submission, but I am interested to know whether your clients claim to have been deceived in product description statements, particularly by the description of independent reports of the likely returns on their investment.

Mr Willemsen—No, I did not mention that, but I think the product disclosure statements are more notable for what they do not say than what they do say. The case is essentially about nondisclosure of material financial information that we believe ought to have been disclosed about the viability of the company at the time. We have, among the documents that I propose tendering, some evidence already to hand which illustrates that the investors were not told things that they ought to have been told that the directors of Timbercorp knew at the time.

Senator O'BRIEN—Can you elaborate?

Mr Willemsen—Yes.

CHAIR—If you need to have the opportunity to go in camera, if you are concerned about court proceedings or—

Mr Willemsen—Yes, I understand that.

CHAIR—We are happy to receive it—

Senator O'BRIEN—We would prefer it in public actually.

CHAIR—We would prefer it in public.

Mr Willemsen—Yes. These documents are available on the internet essentially and they have been lodged with ASIC. Some of them are public, but they just need things pointed out about them. So I am happy to stay in open hearing. The reason why we say that the investors should have been informed about these things is that these MIS projects essentially operated as a joint venture between the investor on the one hand, the landholding company on the other and the responsible entity as the other party. The investors were very passive in this exercise—they put the money up—but the responsible entity was the one that had control of the purse strings and knew all about the business.

So if I could just start with an annual report of the public company, Timbercorp Ltd. I have some copies to hand up. This is not the full copy. It is quite a bulky document if I was to print the whole lot, but I just want to make reference to a couple of key pages within the bundle that I have distributed. It is the annual report of Timbercorp Ltd for the year 2008. I might say that the company's financial year was to 30 September. If we look at page 51, towards the bottom there is a subheading called 'Going concern basis'. These are in the notes to the financial report. It sets out a couple of opening paragraphs there, but if you then look at the number of bullet points with the introductory words:

The Directors believe the going concern basis of preparation to be appropriate after consideration of the following factors:

Then there is something about the appointment of an investment bank to look at a sale process and lease-back. The next bullet points are:

- The cash flow forecasts which indicate that the Group is able to pay its debts as and when they fall due on the basis of the asset sale and debt reduction program in place;
- In the event that the asset sales do not proceed as planned, or only proceed in part, management are confident of the continued support of its financiers subject to agreeing alternative plans acceptable to its financiers; and

That is quite an important point. Then there is a final bullet point about a wider strategic review. The next paragraph is an important one, if I may read it:

Having assessed the uncertainties relating to the matters noted above, the directors believe that the Group will continue as a going concern.

Then it talks about the sale of selected assets et cetera and the rest is fairly straightforward on that page. If you look then at the next extracted page, which is page 105 of the report, under item 35, dealing with events subsequent to the year end, the year end being 30 September, the first subheading 'Revised banking term sheets', it reveals that an agreement was reached only on 27 November 2008 for the waiver of certain bank covenants. So certainly between 30 September

2008 and 27 November 2008 the company was in breach of its bank covenants. That information was not conveyed to the investors in any of the MIS projects. The auditors were more scathing and the report from Deloitte appears next. It was published in page 106 and over the page, page 107, of the annual report. The important part for our purposes today is on page 107, 'Material uncertainty regarding continuation as a going concern'. This is signed-off on Christmas Eve 2008. If I can read this paragraph:

Without qualifying our opinion, we draw your attention to Note 1 in the financial report—

which is the one I have already taken you to—

which indicates that the consolidated entity, in the absence of waivers, would have breached certain bank covenants at balance date. The consolidated entity has, subsequent to year end, obtained waivers for the breach of covenants as at 30 September 2008 and varied future covenants and terms. This includes an undertaking to sell selected assets and apply a portion of the proceeds to reduce debt. These factors, along with other mitigating factors being relied on by management to address these issues, are as set forth in Note 1 "Going Concern". In the event that the mitigating factors as disclosed in Note 1 do not eventuate as management anticipate, there exists a material uncertainty about the company's and consolidated entity's ability to continue as going concerns and whether they will realise their assets and extinguish their liabilities in the normal course of business and at the amounts stated in the financial report.

So, Christmas Eve. This report essentially to the shareholders would have become public knowledge in the January of 2009. Meanwhile, the day after the company's year-end balance date of 30 September there were invoices sent by Timbercorp Securities Ltd as the responsible entity to all investors in the horticultural projects.

That is your almonds, olives, citrus, mangoes, avocados. Every year they sent these invoices for ongoing operational expenses. They were supposedly to cover a 12-month period; eight months in advance, four months in arrears.

Then there were management fees and licence fees for the use of the land, and the cost of temporary water. In light of this information that we have just been reading from in the annual report, you would have thought that something would have been said about the instability of the group to the investors who had put a lot of money into these projects. About a week or so before the October invoices were sent to the investors, there were financial reports issued by Timbercorp to each investor setting out the situation in respect of each project.

I hand up copies of an example report. This is something that is lodged with ASIC and after the first few pages you will see a copy of a report for a particular project which is for the 2008 Timbercorp Olive Project lodged with ASIC on 18 September 2008. It covers financials and there is a particular page I draw your attention to, which is page 5 of the actual report. It is a directors' declaration for the period from 26 February 2008, being the formation date, to 30 June 2008, signed on 12 September 2008, not long before the year end balance date, signed by 'Sol C Rabinowicz, Director', and the text reads:

The directors of the Responsible Entity declare that:

a) in the directors' opinion, there are reasonable grounds to believe that the project will be able to pay its debts as and when they become due and payable ...

I have grave doubts about the accuracy of that statement. There is another report, which gets closer to the date the companies were placed into voluntary administration, which was 23 April 2009. I hand up copies of this later report to do with the same project. This was lodged with ASIC on 13 March 2009. It is in the same format as the earlier report. Again I take you to page 5: the signature again of Sol Rabinowicz as director, dated 5 March 2009, and the same declaration in the same form of words about the responsible entity being able to pay its debts as and when they become due and payable.

There is no mention in either of these reports that Timbercorp Ltd was in breach of its bank covenants. There was no inkling whatsoever of anything being wrong inside Timbercorp, no hint of imminent collapse, and the investors have been kept in the dark. They were asked to pay their October 2008 invoices as usual and, in accordance with the normal practice of Timbercorp, they offered for investors to take borrowings from Timbercorp Finance Pty Ltd to meet the October invoices for those that wished to have finance. Most of the clients for whom we act did take borrowings from Timbercorp Finance. Other people just paid with their own money. So that is the sort of nondisclosure we are talking about.

We will be bringing these matters to the attention of the court in relation to 2008. During the court process we will seek discovery of documents and see what we can find in relation to 2007, but we are confident enough to formulate the claim to cover the period from February 2007 onwards. The significance of early 2007 is the government announcement that the application of the tax laws was going to change for horticultural MIS projects. The up-front tax deduction was no longer going to be allowed, which had a very significant impact on the sales of new MIS projects outside of forestry, and it seems that Timbercorp, and many other agribusiness companies like it, relied heavily on the new sales revenue in order to fund the ongoing operations of their business.

So that is illustrative of the nondisclosure. The case is not dependent on proving what was in the product disclosure statement. It is really broader than that and it looks at the relationship between the parties in this joint venture structure per project as to the sort of information that the investors ought to have been given by the only party that had access to all the relevant information, which was the responsible entity.

What I would also like to mention is that the loan book of Timbercorp Finance Pty Ltd was charged in favour of a number of security holders, the primary one being ANZ Bank, to the tune I believe of 87 per cent and there were smaller percentages held by Perpetual as security holder to 10 per cent and Trust Company to three per cent. This leads into the position of conflict. I hand up another report. Again, it is only extracts of key pages from an otherwise bulky document and it is publicly available; it has been widely distributed. It is a report by KordaMentha as administrators, dated 18 June 2009. In this document, apart from the cover page, we go straight to page 31, section 3.8, 'Reports as to affairs'.

KordaMentha have control of the entire group of the companies within the Timbercorp group and they say:

The Directors have provided Reports as to Affairs ("RATAs") of the companies to us. The RATAs provide information on the financial position of each company within the Group as at the date of our appointment.

That was 23 April 2009. They have attached at appendix 9 the reports as to affairs on an individual company basis. So if we go straightaway to appendix 9, on the next page is the cover and the last page is the actual report as to affairs by way of summary. If you look down the bottom half of that page, about the middle of the page, you will see ‘Timbercorp Finance Pty Ltd’ and the first line talks about ‘Assets not specifically charged’. Has everyone got that? Mr Chair, have you found the spot? It is the last page of the—

Senator O’BRIEN—The second to last page of the document that you gave us.

CHAIR—Yes.

Mr Willemsen—Timbercorp Finance is shown in the central position at the bottom half of that page. The first line is ‘Assets not specifically charged’.

CHAIR—Yes.

Mr Willemsen—Book value \$89 million. ‘ERV’ is the estimated realisable value. In the directors’ opinion it is written as \$43.49 million. So the directors were thinking that the bulk of the assets of Timbercorp Finance, which would be the loan book, were not going to be recovered. Then there is ‘Assets subject to specific charges’, \$140 million at book value. In the directors’ opinion the estimated realisable value is a mere \$62.9 million.

The next page is appendix 18, which shows the money collected by KordaMentha as administrators in the early part of their administration. In respect of Timbercorp Finance Pty Ltd, it shows a summary of the receipts and payments for the period 23 April 2009 to 31 May 2009. Two-thirds of the way down the chart, you will see three entries that are called ‘distributions’. One is ‘Distribution to Chargeholder (ANZ)’. It received from KordaMentha \$3,779,864.76. The next charge holder listed was Perpetual, which received a distribution of \$427,043.69 and the third one was to Trust Company of \$120,806. My calculation of that distribution aggregate shows that 87 per cent went to the ANZ, 10 per cent to Perpetual and three per cent to Trust Company. The ongoing efforts of KordaMentha as liquidators to collect the money, we believe, are seeking to look after the security holders of the loan book, primarily the ANZ. They have been keen to tell everybody that has borrowings from Timbercorp Finance that they need to pay these loans back.

Recently there were a series of meetings for the growers as to the future of the almond projects, the olive projects and the forestry projects—three separate meetings. Mark Korda was present at those meetings and spoke, as did a number of other representatives. This was in the context of the break in the Supreme Court proceedings about the future of the almond and olive projects, where the liquidator originally sought to have all of the projects immediately wound up. But through the efforts of the Timbercorp Growers Group, led by Mr Chris Garnaut as chairman, there was some time given to explore other options—the sale of assets or a recapitalisation or replacement responsible entity and the like.

I attended each of those meetings and one question which I asked of Mark Korda, on behalf of all the Macpherson and Kelley clients, was whether he would be seeking to recover outstanding amounts under loans made to the growers and his answer was, ‘Yes.’ He also said, in answer to my question, that ‘Timbercorp Finance is obliged to collect the money.’ I take issue with that.

The provisions of section 601FC of the Corporations Act, which reflect fiduciary obligations owed by the responsible entity to investors in managed investment schemes, require that the responsible entity act in the best interests of the investors. If there is a conflict between the interests of the investors and the interests of the company—primarily creditors and shareholders—then the interests of the investors in the MIS projects are to be given priority.

Mark Korda has known for quite a considerable period—and long before I asked this question at the recent meetings—that the Macpherson and Kelley clients seriously challenged the validity of the loans and, indeed, the sale of new MIS projects in the years 2007 and 2008, yet he is insisting that people pay 100c in the dollar for the loans that were made to investors in these MIS projects. He says he is obliged to collect the money. The only one that obligation can relate to is the secured creditors and the main beneficiary there would be ANZ Bank. If he truly is acting in the interests of the investors, he should be challenging the validity of the loans, because that is an unrealistic scenario because it would mean that he has to sue himself. As liquidator of Timbercorp Securities Ltd, he would have to sue himself as liquidator of Timbercorp Finance. I cannot see that happening.

He has shown no willingness to give any concessions to any of our clients. He has instructed his lawyers Mills Oakley, the lawyers for Timbercorp Finance Pty Ltd (in liquidation), to recover money and there were a number of writs filed in the Victorian Supreme Court against individual investors who had loan arrears.

One of those investors is and continues to be a client of Macpherson and Kelley. We have put in a defence on behalf of that person, and a counterclaim which mirrors what will be the class action claim on behalf of all of our clients, which will be filed next Wednesday.

The other odd thing about the attitude of the liquidator and the cosiness of the relationship with the bank is that the directors themselves thought that the majority of the loan book was unrecoverable and these serious challenges to the validity of the loans have only been made after the date this report as to affairs was submitted.

The situation of the conflict raised its head in the case of Environinvest, which was another agribusiness MIS company. It so happens that KordaMentha also had a role to play there, in that case as receivers of Environinvest, and there was comment made by Justice Judd in the Victorian Supreme Court in a decision of 12 February 2009, reported at [2009] VSC 33. I do not have copies to hand up of this, but suffice to say that in a debate before the court it was recognised that the same insolvency practitioner could not realistically act in the best interests of the secured creditor and at the same time act in the best interests of the investors in the MIS projects, so the judge proposed that an independent liquidator be appointed.

There may need to be some revisitation, I think, to the laws governing the regulation of managed investment schemes, particularly in an insolvency context. In this Timbercorp case you have only one firm of insolvency practitioners controlling the whole group of companies. The contrast can be made with Great Southern, where there are different firms acting as administrators on the one hand, and McGrathNicol as receivers.

There is something else I wanted to distribute which is of significant concern to the investor clients and really, I guess, was a lot more influential in their decision to make an investment than

anything said in the product disclosure statement, and that is a cash flow forecast. I will hand up copies: one to do with 2008 Timbercorp Olive Project and one to do with 2004 Timbercorp Table Grapes Project. The feature of these is that they put numbers in for the potential investor to see over each and every year of the long-term duration of these projects, like 24 years duration for the 2008 olive project, which show in the end, without borrowings, an expected return of 14.3 per cent and, with borrowings, an expected return of 12.48 per cent after tax. That is the olive project 2008, and the other one, which has some percentages as well, is the 2004 table grapes. I hand these up by way of illustration and example.

From many people I have heard over recent months all the various reasons why they invested in these projects. It was designed to, and they believed that they would, gain a return in the long term after doing the hard yards early, getting the infrastructure set up and the establishment costs for the projects and making some losses in the initial phase; but the projects would eventually reach break-even and then yield a return and the investors would then pay tax on their earnings in the future years. But they would still make a return after tax. That was the expectation.

These documents were produced from Timbercorp templates and they show a fair bit of detail. As I say, I think these were far more influential for people who saw them than anything written in the product disclosure statement. It was sold as an asset class investment. People could diversify into agribusiness MIS projects instead of putting all their money in shares or property or whatever other investments—their own businesses—and you have got the collapse of Timbercorp in 2009. We say they were well and truly on the verge of collapse throughout 2008 and, after the court case, we might find that they were also doomed to fail as early as 2007. So people put in a considerable amount of money, expecting to earn some income in most of the years through the next 15, 20 years for these agribusiness projects.

The table grapes is interesting in itself, in that that project seems to have been accepted by Timbercorp as a failure pretty much from its earliest stages. The way it was put to me by one of our clients was that Timbercorp were particularly embarrassed by their failure with the table grapes 2004 project, to the extent that they cancelled the management fees for the second year and the clients never received a further account thereafter. That part of it seems to be true, but then when Timbercorp became desperate for money in 2008 one of the steps they took was to send notices of default to the table grape investors, saying they have got overdue money, they had better pay up, otherwise severe action would be taken. Those default notices were sent out to this client on 21 August 2008. We may have more to say about the table grape project and some other projects as time passes, but I just raise that now because I thought it was opportune.

I would like to mention another thing. I do not have anything to hand up here, but, again, this is a publicly available document and it is part of the regulatory regime for responsible entities in MIS projects. It is the Australian financial services licence for Timbercorp Securities Ltd, licence No. 235653, effective 6 February 2008. You would think that this might provide some comfort for people, but it depends. Condition 19 concerns professional indemnity compensation requirements and this is to do with insurance:

The licensee must maintain an insurance policy covering professional indemnity and fraud by officers that:

(a) is adequate having regard to the nature of the activities carried out by the licensee under the licence;

I have not seen the insurance policy that was taken out for Timbercorp Securities Ltd or its officers. It is very hard to imagine, though, that whatever policy it is will be adequate, given the size of the Timbercorp operation, to cover people who have claims for misleading or deceptive conduct and breach of duty. In the 2008 year alone, Timbercorp sold new MIS projects to the value of something like \$125 million across almonds, olives and timber. It is going to need to be a mighty big policy if people are going to get all their money back—and that was just the 2008 investors. So this is another serious issue that needs addressing, I believe, to make sure that other investors in other MIS operated companies do not miss out if things go horribly wrong elsewhere. I think, Senators, that was about the extent of what I wished to put today and the documents that I wished to hand up. But I would be happy to take any further questions.

CHAIR—Thank you very much for that. By the way, KordaMentha have been invited to these proceedings.

Mr Willemsen—Yes.

CHAIR—They say they are too busy.

Mr Willemsen—I am very busy, too, but I thought it was important on behalf of all of our clients that I say something for their benefit.

CHAIR—In the financial statement to 30 September 2008, on page 52, ‘Summary of accounting policies’, ‘Going concern basis Continued’, it actually flags there in that document:

If the sale of selected assets and the consequent repayment of debt do not proceed as planned there is material uncertainty in relation to the Group continuing as a going concern.

And bear in mind that is backed up with the Timbercorp statement by Sol Rabinowicz:

a) in the directors’ opinion, there are reasonable grounds to believe the project will be able to pay its debts ...

When in fact if it did not come to an arrangement, it would be trading while it was insolvent, wouldn’t it?

Mr Willemsen—Yes.

CHAIR—So, if you issue debt notices to people while you are actually trading while insolvent, aren’t you breaking the law?

Mr Willemsen—I would think so.

CHAIR—So it would be fair to say that this will become a serious legal entanglement. I am a wool classer and a welder, but commonsense would say that if you put out a notice in your financial statement of 2008 which said, ‘If we can’t sell something, we’re dead’—

Mr Willemsen—Yes.

CHAIR—to then raise accounts straight after that—on 12 October, was it?

Mr Willemsen—1 October. They are all dated 1 October.

CHAIR—1 October. I would have thought that you would have to solve this problem before you sent the accounts out, because otherwise you will go to jail for trading while you are insolvent.

Mr Willemsen—The one who has the power to issue those sorts of proceedings for trading whilst insolvent is the liquidator and, if he refuses to do it, creditors can make application to run the action themselves. That is a different action to the one that we are about to launch next week. But it would be an available action.

CHAIR—So in KordaMentha's report on page 31 at 3.8, KordaMentha is saying:

Given the complexities of the Group's structure and operations and the need to understand the position of grower investors' rights in respect of each MIS ... we are not in a position to comment on the Directors' estimate of realisable value of assets and liabilities, other than to say it appears the RATAs have included intercompany loans as realisable assets. Given all the companies in the Group are in administration, the collectability of these intercompany assets is highly doubtful. Additionally, we note that contingent liabilities including guarantees ...

Isn't that proof that they are trading while they are insolvent?

Mr Willemsen—I think they did trade whilst insolvent.

CHAIR—We are just a bunch of senators. We have a guy, who may become one of your clients, who put a couple of million dollars into this and kept getting these quarterly accounts for a hundred and something thousand. He did not even know what they were for and he kept paying them. Talk about a lack of information and a lack of direction from whoever the financial planners were. Then you have a document that says—and it has been well documented in the press and the *Weekly Times*—people have \$50,000, borrow the money up-front; in a few years time you owe \$220,000.

Mr Willemsen—Yes.

CHAIR—Some of that you have paid while someone is technically insolvent, but the prospectus which you have given us on table grapes, or whichever one it was, said, 'If you borrow the money, you'll get a 12 per cent return,' so why wouldn't you borrow the money and get a tax deduction—it would cost you nothing—versus no loans and you get 14 per cent?

Senator O'BRIEN—Can I get some clarification of one of the documents that you have given us? It is the KordaMentha document.

Mr Willemsen—Yes.

Senator O'BRIEN—The page you referred us to where assets and liabilities of Timbercorp Finance Pty Ltd are set out in book value and estimated realisable value. Do you know what the assets were that they were referring to? Were they the loans?

Mr Willemsen—Yes.

Senator O'BRIEN—They do not actually have physical assets, do they?

Mr Willemsen—No.

Senator O'BRIEN—So the book value of the loans was \$140 million but the estimated realisable value was just under \$63 million.

Mr Willemsen—Yes.

Senator O'BRIEN—So the company was estimating that they could not recover the loans from the individuals.

Mr Willemsen—Yes.

Senator O'BRIEN—Is that right?

Mr Willemsen—Yes—which suggests that there were many people already not paying, long before the companies went into voluntary administration, which is another thing that probably should have been disclosed to those paying customers.

Senator O'BRIEN—Do you know what the historical position was—what was expected to be realised on the loan book?

Mr Willemsen—What do you mean exactly by 'historical'?

Senator O'BRIEN—Timbercorp Finance Pty Ltd in the year preceding—let's say 2008—

Mr Willemsen—Yes. No, I have not looked that up, I must say.

Senator O'BRIEN—The authors of this document were—

Mr Willemsen—This is a summary by the administrators, I think, of the reports as to affairs that were completed by the directors. So this information would have been extracted from the directors' report as to affairs.

Senator O'BRIEN—And it sets out the position at a particular date? Do you know what date?

Mr Willemsen—This is at the date of the companies being placed into voluntary administration, which was 23 April 2009, which is usual for when the company is placed into an insolvency.

Senator O'BRIEN—Do you know who the unsecured creditors of Timbercorp Finance Pty Ltd to the tune of \$158-odd million were?

Mr Willemsen—No. I think that might be one of the inter-company loans, but I am not sure about that.

CHAIR—So where do you think ASIC fits into this?

Mr Willemsen—The investors took a lot of comfort from the fact that there were product rulings issued by the tax office. A lot of people misunderstood that to be that the tax office thought it was a commercially viable project. And ASIC being the regulator, and with licensing arrangements and the monitoring role that ASIC had, people had comfort that this was a safe investment. I believe ASIC ought take quite an aggressive stance and make people accountable for their actions in relation to what, after all, is called a ‘responsible entity’.

These directors seem to have got away with murder. They have taken so much money from so many people—18,000 Timbercorp investors, I believe there were, in MIS projects—and really they ought to put a blowtorch over what happened to expose what happened in 2007 and 2008. They were years when solid sales were still being made, certainly in forestry. There were declining sales in horticulture but, for the years prior, a lot of people put a lot of money into horticultural projects.

As to this whole episode recently of having to have a Timbercorp Growers Group formed and to stave off the unholy haste with which the liquidator had to try and wind up all of the schemes, I think that, if ASIC had stepped in earlier or really kept a keen watch on what was happening in the MIS space, some of these problems may have been exposed earlier and people would have had a more realistic opportunity to take steps to replace Timbercorp Securities as the responsible entity, find someone that might have been able to manage the projects far better and far less expensively and give the projects some realistic opportunity of surviving, with people then staying in for the long term. They might not have got their 14 per cent return but if they got a five per cent return it is better than having lost everything.

CHAIR—Yes. So, instead of all that, there has been a fire sale.

Mr Willemsen—Yes.

CHAIR—And, unlike Ferrier Hodgson and McGrathNicol, the person who has done the whole thing, which is KordaMentha, has got no possibility of looking after the interests of the investors. The ASIC obligation to the directors and shareholders of the company is at complete odds with the investors if you are the receiver and the liquidator.

Mr Willemsen—Yes.

CHAIR—I would have thought that even a wool classer and a welder could work that out!

Mr Willemsen—And maybe ASIC should have stepped in and appointed a temporary responsible entity early.

CHAIR—If they indeed were trading while they were insolvent—because there is a criminal proceeding—if everyone was on the ball, what right would the receiver, then being appointed as the liquidator, have to sell the assets when they could be seen to be stolen assets?

Mr Willemsen—Justice Robson in the Victorian Supreme Court recently gave approval for the sale of the almond assets to go ahead to the Singaporean company because there was no

better chance of salvaging some value, but he said, 'Look, the sale proceeds should be kept in trust. Let everyone come back and speak to me later on. We'll have another hearing and we'll work out how much should go to the banks and how much should go to the investors.' So that is still an open issue. But, beyond that, so far the banks have been fairly well looked after, I believe, out of the asset sales.

The investors are scrambling around to get the best they can get from the scraps and that is why we believe that their best chance of getting anything of value out of the whole mess is through this class action, which will be on behalf of all investors, whether they were borrowers from Timbercorp Finance or not. The borrowers are probably better placed to get some value if they can be excused from having to pay their loans, whereas the nonborrowers will only stand to get compensation in a real sense if there is adequate insurance in place, which is something that ASIC should have had its eye on, particularly given the size of the operation of Timbercorp as an ASX 200 company.

CHAIR—Sadly, we have run out of time. I think we could spend another couple of hours on this, and I am sure that if we need to we will, but for today we have to wind up. We are very grateful for your excellent material and evidence. I can only say that it appears to me that this is a disgrace, in which as big a loser as any is the taxpayer.

Mr Willemsen—Yes.

CHAIR—So they have transported the taxpayers' generosity overseas now at a fire sale price. Thank you very much.

Mr Willemsen—You are welcome, and I agree with the word 'disgrace' as a fair summary of the whole situation.

CHAIR—Thank you very much.

Mr Willemsen—Thank you.

CHAIR—I declare this hearing closed.

Committee adjourned at 2.13 pm