



Review of the Taxation of Plantation Forestry
Attention: Mr Matthew Collett
C/- Department of the Treasury
Langton Crescent
PARKES ACT 2600

18 August 2005

Background

Integrated Tree Cropping Ltd (ITC) is one of Australia's largest hardwood plantation forestry managers and timber processors, with operations in all Australian states. ITC's plantation and woodchipping activities are located across Australia. The Company has green and dry sawmills in Victoria, Tasmania and New South Wales, selling processed timber products predominantly into the Victorian domestic market.

(a) Plantations Division and Managed Investment Scheme Activities

With a plantation estate spanning mainland Australia of approximately 120,000 hectares, ITC's plantations division has managed forestry investments on behalf of private and retail investors for 14 years. Plantings as a result of ITC's successful 2005 product offering will see the total estate under management expand by more than 20,000 hectares this financial year.

Since making its first managed investment scheme (MIS) offering in 1992, ITC has maintained its focus solely on forestry and forest products. Throughout this time, ITC has invested extensively in research and development aimed at enhancing ITC's silvicultural practices and genetic stock. Seeking to achieve increased plantation yields and operational gains, ITC has one of Australia's leading advanced-generation breeding programs and has established extensive trials.

As the manager of 38 different MIS projects, ITC is engaged to establish and maintain timber plantations, and then harvest, process and market the woodchips on behalf of its investor growers. The Company manages pulpwood, solidwood and Indian sandalwood projects.

(b) Processing Division

ITC's timber processing division is the largest timber processor in Australia, producing quality sawn timber products for domestic and export markets. With production capacity to receive more than 250,000 cubic metres of logs in Victoria, Tasmania and New South Wales, it specialises in the processing of native regrowth eucalypts.

ITC is focussed on the development of new timber products for domestic and global markets. The Company recently commissioned a green mill at Southwood, Tasmania and also installed scanning technology, the most advanced of its kind in Australia, into its Victorian sawmills.

Founded more than 80 years ago as the Neville Smith Group, ITC Processing continues to supply timber product predominantly to the furniture, flooring and construction markets.

Submission to the Review

ITC is a member of Treefarm Investment Managers Australia (TIMA) and the National Association of Forest Industries (NAFI). ITC supports the submissions made by these organisations to the Review. There are however two key points in relation to the terms of reference to which ITC wishes to draw particular attention.

Importance of the Twelve Month Rule to sustainable plantation development

ITC firmly supports the removal of the sunset clause currently applying to the 12-month prepayment rule in order to provide certainty to the Australian MIS plantation forestry industry. The 12-month rule is an important contributor to the responsible establishment and management of plantations on behalf of investors, allowing for planting to occur most effectively to maximise survival and minimise any potential adverse yield impact resulting from poor establishment techniques. The matching of climatic and seasonal weather conditions to the establishment program of a plantation company such as ITC is important to optimise plantation performance in this regard.

Additionally, the application of the 12-month rule provides protection to MIS plantation companies by affording some security when undertaking major capital outlays for land to establish plantations. If there is to be encouragement for plantation companies to bring longer rotation solidwood projects to market, the 12-month rule is required to align more closely the capital outlay requirements for land with the take-up of such investment opportunities (ie. MIS sales). This will likely support a more proactive marketing approach for such projects.

Impediments to investment in longer-term rotations which produce higher value products

The nature of MIS investment is such that it is predominantly a retail-level oriented investment as distinct from wholesale. As such, the investment opportunity must offer terms and rates of return that appeal to this market segment. One of the main contributors to the success of pulpwood plantation projects as distinct from longer rotation projects is the relatively short rotation length of ten years. Conversely, this presents an impediment to longer rotation projects being attractive to potential investors, given that the value proposition must be presented in terms of advantages over rates of return and rotation length of pulpwood projects in the marketplace.

Concurrent with this, MIS plantation investments have poor liquidity due to the lack of a secondary market for the projects. Any attempt by a grower to transfer interests to another party is a complex and often lengthy process, which serves as a significant disincentive to invest in MIS plantation projects upfront. To this end, ITC views the establishment of and our participation in a secondary market for plantation investments as crucial to the encouragement of investment in longer-term rotation projects.

As a fully integrated forestry business ITC has a strategic commitment to value adding through down stream processing. Contrary to the trend of recent years for timber processors to divest their plantation assets, ITC believes that significant opportunities exist for a plantation resource to be processed domestically, albeit not for current MIS projects under ITC's management or for plantations managed on short rotations such as ten years. Indeed, the proposition to value-add plantation timber forms part of ITC's vision.

ITC encourages a reinterpretation of Paragraph 48 of the ATO Ruling 2000/8. This ruling as presently interpreted does generate concern regarding the deductibility of investment costs if there is an intention to sell a plantation before income is due to flow to an investor. Such interpretation means that a forestry manager such as ITC cannot seek to purchase a grower's wood at the end of the investment period (say 10 years for a pulpwood project investment) and then in fact grow the plantation on for a longer period to achieve a solidwood product output.

This scenario is exacerbated by the inability to effectively establish a fair and transparent pricing model due to a lack of data flowing from an established secondary market.

Finally, any moves to encourage longer-term rotations will also require a more sophisticated product structure, ideally with income flows to the grower from thinnings throughout a rotation. Such a structure would likely provide an incentive to potential investors to make and hold their investment for a longer period. This is important given that most solidwood projects will require a rotation length of approximately 20 years.

In summary

1. ITC encourages the removal of the sunset clause currently applied to the 12-month Rule to provide ongoing certainty for the plantations industry;
2. ITC supports a review of Paragraph 48 in consultation with industry and all stakeholders to remove any undue constraints on developing secondary markets consistent with Federal taxation and forestry policy.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Tony Price', with a long horizontal line extending to the right.

Tony Price
Chief Operating Officer – Plantations