



12<sup>th</sup> September 2008

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Dear Sir,

Re: Review of Non-Forestry Managed Investment Schemes  
Business Tax Division

Maccacorp Ltd (Maccacorp) operates a Managed Investment Scheme (MIS) in the macadamia industry. The company was established by macadamia growers in an attempt to expand the macadamia industry. Currently Australia is the leading producer of macadamia nuts and exports approximately 90% of the Australian crop to countries such as USA, Japan, Korea, Germany, China and United Arab Emirates. Whilst the macadamia industry only accounts for approximately 1% of the world tree nut market, the Australian industry generates over \$200 million in export revenue for Australia

Please find attached my company's submission that is designed to address the issues contained in the Review of Non-Forestry Managed Investment Schemes Issues Paper prepared by Treasury.

It is our position that the MIS platform expands the base for those wishing to invest in Australia's agriculture in particular the macadamia industry which assists Australia to improve its balance of payments and provide investment (including employment) in rural Australia.

Should you require any additional information, please do not hesitate to contact me

Yours faithfully,

Donald K Ross  
Managing Director

**Submission by Maccacorp Ltd**

To the

**Review of Non-Forestry Managed Investment  
Schemes  
By the Commonwealth Government of Australia**

12 September 2008

## **1 TAX ADVANTAGE**

Maccacorp believes that the tax advantage and risks that MIS participants have is consistent with traditional macadamia farmers and that tax law applies in the same way to traditional farmers

### **RISKS**

The risks, climatic and weather, assumed by MIS participants are the same as those assumed by people engaged in traditional agricultural enterprises as are generally the risks associated with selling the products. However, many MIS schemes have attempted to reduce the risks to investor associated with selling and marketing the product by establishing off-take agreements with processors or supermarkets. These agreements can take many forms but generally guarantee that products generated by the MIS will be sold.

For the individual investors, in the case of Maccacorp, the yield from all the orchards is pooled and distributed amongst all investors. This minimises the investors risk exposure as should a problem occur on one orchard, such as hail damage, they will still get some return from the overall pool. In contrast , many traditional operators only one property and should a problem arise then their exposure to risk can be quite high.

Maccacorp considers that the level of risk for MIS participants and traditional farming operations are similar

### **LEVEL OF INVOLVEMENT**

The level of involvement of MIS participants maybe considered less than those engaged in living on and operating farms but is similar to or greater than seen in many absentee landlord manager arrangements that are a feature of the Australian non forestry agricultural industry. Absentee landlord arrangements, where the owner lives in a capital city and either employs a manager or management company to look after their property, are particularly common. Whilst the owners may visit the properties most other contact taking place over the telephone or through accountants.

Maccacorp considers that the level of involvement for MIS participants is similar to many traditional agricultural operations

## STRUCTURE

MIS are structured in a similar way to many absentee landlord arrangements which are common in non-forestry agriculture. Most absentee landlords employ a manager or management company usually on a vague common law contract with minimal safeguards and with no agreed targets or budgetary arrangement. Accountability in these situations is often low. In contrast, the managers of MIS schemes have legal accountability requirements through the use of external reviewers, and auditors and it is considered to be in a better situation than absentee owners.

In an MIS scheme the rights of the investor are clearly defined in law as are the duties and responsibilities of the management company and the Responsible Entity. The investors receive reports which measure progress against an agreed set of performance guidelines. The whole process is independently audited, by external experts as to the agricultural progress of the scheme, legally and financially by compliance committees and external auditors.

Agriculture is becoming an asset class in its own right and MIS is only part of the spectrum of the types of investment found in agriculture.

## TAX TREATMENT

All non-forestry agricultural operations are subject to the provisions of the *Income Tax Assessment Act 1997* (Cth) ('the Act') and *A New Tax System (Goods And Services Tax) Act 1999* (Cth) ('the GST Act'). The maximum benefit received by a participant in an MIS is only comparable to the tax benefit equivalent to the investors' rate of tax whether personal or corporate. The tax treatment in all cases is the same and in accordance with the provisions of the Act and the GST Act and the cost of compliance is considered similar.

The tax treatment applying to MIS is considered similar to traditional non-forestry farming.

## USE OF MIS TO FINANCE OPERATIONS

The cost of an MIS scheme is higher than the cost of setting up a traditional non-forestry operation since the company must comply with the provisions of the *Financial Services Reform Act 2001* (Cth). Few traditional businesses have used MIS due to the complexity and cost of establishing a scheme. There is the cost of obtaining and compliance cost of maintaining an AFS licence or employing a Responsible Entity who has a licence. These costs can be substantial and most traditional businesses do not have the capital or capacity to

undertake such a process. The complexity of the process is also quite daunting and is probably outside the bounds of normal experience from most traditional rural enterprises.

The independent auditing of schemes by external experts as to the agricultural progress of the scheme, the legal compliance, the financial audit and the establishment of a compliance committee adds extra cost to the MIS.

Most traditional finance for agriculture has come from the banking sector, and in particular the rural banks that were a feature of state governments, last century. The demise of these financing mechanisms coupled with greater profitability and reliability for banks from other sectors of the economy is possibly one of the contributing reasons for declining investment in agriculture by the rural sector.

Large companies have invested in the rural sector as they have been able to finance the purchase of large properties and or property amalgamation costs and then provide the associated additional investment that has resulted in financially viable and sustainable operations. These investments have also provided a level of financial security as land costs over time in many areas have risen with or exceeded inflation thus minimising risk.

The use of a MIS provides for economies of scale and greater financial security which can attract a level of investment which can offset the additional costs associated with a non forestry enterprise

Maccacorp considers that the MIS provides an option to attract investment in agriculture that provides benefits to rural Australia and our economy

## FEE STRUCTURE

The fee structure of an MIS usually consists of an initial once off fee and an ongoing annual rental and management fee. The initial fee is charged to assist with the cost of preparing the land for planting, installing irrigation and planting trees. This is similar to the establishment of conventional non forestry property where initial expense is incurred to establish the property. The advantage of the MIS is that it can access economies of scale in establishment. The ongoing fees meet operating costs and ensure viability of the project.

Demand for finance in conventional farming operations are directly linked to the vagaries of weather and the fluctuation of the economic conditions. MIS have a regular flow of funds that allows the scheme operator to better react to the climatic and economic conditions without resorting to Government assistance or refinancing with banks

It is considered that the fee structure of the MIS provides greater protection for the investor and reduces the dependence on Government assistance in difficult times.

## 2 Performance of Non-Forestry MIS

Maccacorp considers that Non-Forestry MIS can provide superior performance when well structured and managed

Non Forestry MIS projects encounter the same challenges as traditional operations in respect to site selection, establishment, access to water and maintenance of the property and equipment. The advantage that an MIS has is the economies of scale allow the engagement of professional services that provide irrigation design, soil analysis, fertiliser programs and pest monitoring. The continued use of external consultants is considered appropriate to ensure a project keeps pace with industry best practice.

Project access to a secure water source for irrigation needs aids the management team in minimising year-to-year yield variation and has a positive impact on kernel recovery and kernel quality, which are key factors affecting project returns. All planning, budgeting and expected returns provided to investors are based on the managers exceeding the industry average production per hectare. In the macadamia industry the average production is relatively low, less than 3.5tonnes/ha nut-in shell (NIS) per annum. Maccacorp is budgeting to exceed 4.5tonnes of NIS per annum.

Maccacorp has entered into a long term take off agreement with the largest processor and marketer of macadamia nuts in Australia. The structure of the MIS provides that all proceeds from the sale of product are returned to the grower investor.

Production per employee is usually higher with an MIS compared to privately owned farms. In addition the increased equipment available to an MIS is a reflection of the higher investment in MIS managed properties.

When examining labour use on MIS properties as compared with small family owned properties care needs to be taken as there is often significant underreporting of the amount of time, particularly by female members, spent in running family property.

MIS can outperform conventional farming operations and provide a better return to growers

### **3 THE IMPACT OF MIS ON INPUTS, THE ENVIRONMENT AND REGIONAL AREAS**

The MIS promoted by Maccacorp is an environmentally sensitive project that generates income for Australia, provides regional employment and inputs at least \$1million into the local economy

Maccacorp is based in Bundaberg in Queensland. The companies in the group operations employ only local people and provide jobs for 8 permanent employees and up to 10 casual employees. The casual employees are engaged to assist with planting and maintaining of the orchards. Casual employees will be required during harvesting. The company's operating budget expenditure exceeds \$1million per annum which is invested into the Bundaberg economy

The land purchased by the company was originally used to grow sugar cane. Sugar cane as a crop compared to the production of macadamia nuts uses at least 50% more water. The land has been converted to macadamia plantations with state of the art water monitoring systems. In addition the macadamia industry is adopting pest control procedures utilising developments made by CSIRO to reduce the use of pesticides compared to other crops.

Maccacorp is a significant contributor to the rural economy of Bundaberg in Queensland

## 4 Effect of MIS on commodity markets

Maccacorp considers that the MIS structure is required to provide additional investment into growing Australia's agricultural industry and improve the Australia's balance of payments.

### MACADAMIA INDUSTRY

#### Background

Macadamia nut trees grow best in sub-tropical climates where rainfall is gentle and plentiful during the spring flowering season and early autumn just prior to harvest. Cold climates are not suitable for macadamias as frost can severely damage the root system which is fairly close to the ground surface.

Approximately 250 - 300 trees are planted per hectare, depending on desired spacing, to create the neat and tidy plantations that are the hallmark of the Australian industry. Mature macadamia trees grow to heights of 12-15 metres; The annual growing cycle takes some 9 months. The first flowering occurs in early spring with nut formation in clusters during early summer. Harvesting commences in late autumn and through the winter months. Modern machinery is used to gather the nuts and the soft outer husk is then removed on the farm before the nuts are placed in storage silos awaiting delivery to the processing plant. The hard, round, nut-in-shell is transported by truck to the factory where they are weighed and samples from each farm are analysed by the laboratory for quality and moisture content. At a suitable time nuts are moved from storage silos to drying silos where heat is applied to dry them down from 10-15% moisture to 3% moisture in preparation for cracking.

After drying, a specially designed cracker breaks the rock hard shell with minimal damage to the delicate kernel. Both shell fragments and kernel travel along conveyors past an air separation system and through modern, hi-tech, electronic colour sorters which separate the shell fragment from the kernel. These sorters differentiate between the dark brown colour of shell and the creamy colour of kernel and remove the shell fragments with a burst of compressed air. A final hand sorting inspection is carried out, to remove poor quality kernel, just prior to grading the kernel for packing.

Macadamia kernel is graded into Styles numbered from 0 to 8 which represent the sizes of the kernel pieces. Style 0 is large whole kernel, style 2 is a mixture of wholes and halves, style 4 is primarily half kernels and higher numbers relate to various sizes of chips and small pieces. Once sorted into styles the kernel is vacuum packed into poly lined, foil bags then into sturdy shipper cartons ready for sale to manufacturers of various value added products such as chocolates, biscuits, snack packs and ice cream

## Annual Production

There are about 700 macadamia farms in Australia, varying in size from 200 trees to huge plantations in excess of 50,000 trees. At an average of 250 trees per hectare there are approximately 3 million macadamia trees planted in Australia, of which some 70% are mature, yielding at least 15 kg of nut-in-shell per tree annually. The following table provides nut-in-shell production estimates to demonstrate the growth of the industry.

<b>Year</b>	<b>Tonnes NIS</b>
<b>1987</b>	<b>4400</b>
<b>1988</b>	<b>5200</b>
<b>1989</b>	<b>6800</b>
<b>1990</b>	<b>12000</b>
<b>1991</b>	<b>10000</b>
<b>1992</b>	<b>13000</b>
<b>1993</b>	<b>14500</b>
<b>1994</b>	<b>19000</b>
<b>1995</b>	<b>17500</b>
<b>1996</b>	<b>20500</b>
<b>1997</b>	<b>25400</b>
<b>1998</b>	<b>24500</b>
<b>1999</b>	<b>33000</b>
<b>2000</b>	<b>29100</b>
<b>2001</b>	<b>34400</b>
<b>2002</b>	<b>29500</b>
<b>2003</b>	<b>34000</b>
<b>2004</b>	<b>43000</b>
<b>2005</b>	<b>33500</b>
<b>2006</b>	<b>43900</b>
<b>2007</b>	<b>41800</b>
<b>2008</b>	<b>38000(est)</b>

## .Quality Assurance

Both the growing and processing sides of the industry are focused on preserving the clean, green, healthy image of Australian macadamias. This is achieved by growers working to a Code of Sound Orchard Practices and by processors adopting Quality Assurance Certification programs to ISO 9002 and HACCP.

## Research and Development

Horticultural Australia Limited (HAL) funds research and development on the basis of equal cost sharing by industry and government up to a maximum level set at 0.5% of the industry's gross level of production. HAL funds are collected from the macadamia industry via a statutory levy on all nuts processed. The Australian Macadamia Society, representing the entire industry, exerts a major influence on how, where and on what projects the HAL funds are used.

## Commodity Markets

At the beginning of 1991 some 85% of bulk Australian sales of macadamias came from the USA. During 1992 the industry focused on Asia, in particular Japan, and Europe to develop awareness of the product as an ingredient in confectionery, bakery products, snack packs and ice cream. Overseas agents and brokers were appointed to develop new business and as the industry grew more nuts the demand was created in overseas markets.

Australia has doubled the crop of 1991 and the industry now exports product to USA (35% of its sales), Europe accounted for another 30% while Asia purchased approximately 20% with the rest sold locally on the domestic market.

The following tables present industry data on production by region and sales by region

Region	Tonnage (nut in shell)	Tonnage (Kernel)	Percentage	Comment
Australia	40,000	11,000	42	Quality supplier
Hawaii	24,500	8,000	26	Established supplier Part of USA allowing free trade
South Africa	11,000	2,250	11	Low cost supplier Quality improving Roasting is an issue
Kenya	5,800	1,250	6	Low quality
Other	14,700	2,500	15	
Total	96,000	25,000		

<b>Geographic Region</b>	<b>Product</b>	<b>%</b>	<b>Opportunities</b>
Europe	Snack Packs	30	Expansion into Spain, UK, Scandinavia, Holland, France, Italy, Middle East and India Market is attractive
USA	Confectionery Bakery Products	35	Direct marketing to consumer Improved knowledge of consumers
Australia	Raw & commercial grade	15	Mostly raw kernel for use in chocolates or snack packs
Asia	Raw kernel Confectionery	20	Nut in shell to China Tight specification product for Japan

Australia needs to increase its production by more than 33% to improve its position as the largest producer and marketer of macadamias in the world.