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## **SUBMISSION TO AUSTRALIA'S FUTURE TAX SYSTEM**

Australian Forest Growers (AFG) is the national association representing around 1200 small private forest growers from 22 regional branches across Australia's forest growing regions. AFG's members include farm plantation growers, private native forest managers and private commercial plantation companies. Since 1969, AFG has been advocating responsible establishment and management of forests on private land, which provide the multiple outcomes that the community increasingly demands. The growing of commercial plantations and active management of private native forests by our members has been delivering improved landscape health outcomes for decades, as well as complementing existing productive agricultural land use practises.

AFG welcomes the opportunity to contribute to Australia's Future Tax System and recognises the challenges and opportunities associated with the reform. Currently there are a number of inequities in the tax system relating to private forestry. A number of long-standing tax issues affecting private forestry remain unresolved, despite AFG's efforts over, in some cases, nearly two decades. These include, in particular, the need to recognise the unique interaction of the tax system with private forestry, especially the inequity created by so-called 'lumpy returns'; and the need to resolve the uncertainty impeding the use of *profit a prendre* as a means of enhancing the liquidity of plantation investments. A Board of Taxation review of the small business tax concessions failed to address a number of recommendations by both AFG and the National Farmers Federation. AFG will continue to advocate to the Government its responsibility to address these issues in order to remove discriminatory treatment of private forestry and enhance its attractiveness as a viable land use option.

AFG recognises that the Henry Review is a high level review and that some of the issues raised in this submission may fall outside the terms of reference. The issues articulated herein are longstanding and fundamental issues for the private forest growing sector and thus require attention from any review of the taxation system. In particular there is an imperative that the inequity that the superannuation system applies to long term appreciating assets such as private forests suffer under the current regime.

AFG will continue to argue that for any future arrangements in tax law structure, there is a critical need to consider and address the long term investment nature of forestry and its ongoing market failure in respect of investment.

AFG defines private forestry as the establishment of plantations in woodlots, strips or another model; the regeneration and management of native forests; and the ongoing sustainable management of existing native forests; which occur on privately held land, whether by ownership, leasing, renting or some other mechanism.

Australian Forest Growers advocates that the Australian Government:

1. (i) explicitly recognises the complex and unique characteristics of forestry investment and its interactions with the tax system;  
(ii) confirms that the same basic tax treatment (ie the year-or-expenditure general business tax deduction against other income) will continue to apply to private forestry as it does to other harvested agricultural crops;  
(iii) acts to ensure the tax system makes it possible for a diverse range of business models to be used to attract new forestry investment from a variety of investors with different investment requirements.
2. (i) amends the ‘active asset’ condition of the small business CGT concessions to either (a) allow that a farm would still qualify as an active asset when leased; or (b) delete the requirement of the retiring taxpayer to have an active asset at the time of the sale of transfer of the property;  
(ii) removes or raises the arbitrary asset value threshold in relation to private forestry to account for the appreciating nature of the asset.
3. considers as a priority the Ralph Review recommendation on the tax treatment of ‘rights’ such as profit a prendre, and issues a clear determination that resolves lingering uncertainty restraining the use of forest rights to enhance the liquidity of plantation investment.

### **TAX AND ‘FORESTS AS SUPERANNUATION’**

*Australian Forest Growers advocates that the Australian Government:*

- (i) *explicitly recognises that amending the taxation rules applying to superannuation and biophysical self-generating assets (such as private forests) can help achieve its retirement policy objectives;*
- (ii) *amends the rules applying to self-managed superannuation funds (SMSFs) so that plantation forests established and managed to provide retirement income can be transferred to SMSFs;*
- (iii) *implements further revision to the conditions of the Farm Management Deposits Scheme as per the following to remove discrimination against private forestry;*
  - a) *enabling FMDs to be made on behalf of partnerships and family companies;*
  - b) *redefining the withdrawal threshold in relation to death or retirement from primary production (allowing roll-over into superannuation funds of the beneficiaries), with a special provision for forestry (or any characteristics) of, say, three years; and*
  - c) *increasing the maximum limit on funds held in deposits from \$360,000 to \$500,000 or annual farm turnover.*

Many private forests have been, and continue to be, established and managed as an important element, and in some cases the totality, of the growers’ superannuation. Despite this admirable intention, such growers are subject to severe discrimination within the superannuation regulatory system. This failure takes two major forms. One is the endemic problem of ‘lumpy returns’, whereby the grower receives

‘superannuation’ income at harvest in one lump sum, almost all of which is taxable at the highest marginal rate, rather than at any form of concessional rate such as that applying to monies withdrawn from a superannuation fund. This problem is made worse for most private plantation growers by the limited and highly conditional access they have to the major income averaging provision available to other primary producers with ‘off-farm’ incomes less than \$65,000, which eliminates most private plantation growers. Second, any eligibility quickly evaporates if the grower doesn’t carry on primary production after final harvesting (most common), because any income placed with an FMD must be withdrawn within only 120 days of when primary production ceases.

The second most important manifestation is the treatment of a private plantation with respect to its contribution to a grower’s self-managed superannuation fund (SMSF). Although a private forest may be part of an SMSF in circumstances where the forest operation is commenced by the fund, transfer of an established forest into an SMSF can only occur in very specific and very rare circumstances that satisfy a number of the SMSF tests, such as ‘sole purpose’, ‘related party’ and ‘business real property’.

Most private plantations now approaching harvest age were established well before the contemporary SMSF ‘revolution’, and have no chance of being made to fit the current SMSF conditions that would allow the growers to take advantage of the tax treatment of superannuation funds.

For more than a decade, policy makers in Australia have realised that, with an ageing population that will live longer, steps must be taken to encourage individuals to fund their own retirement.

Over roughly the same period, State and Federal Governments and industry have driven a plantation industry development strategy, *Plantations for Australia: The 2020 Vision*, and have recognised the simultaneous contributions that private plantations and farm forestry can make to natural resource management as well as social and economic development objectives.

However, many of the private growers who established long-rotation plantations decades ago in order to ‘fund their own retirement’ are now suffering personally from that decision. They are confronted by a tax regime that penalises ‘long-term forestry with one final harvest’, and that also prevents them converting an older form of superannuation (plantation forestry) into a more contemporary form (SMSF). One perverse example of this is a former AFG President who, having undertaken his harvest was then unable to vest his net returns in his superannuation fund because he was too old, at 75, to meet the eligibility requirements for investment in his superannuation fund.

Further, anecdotal evidence abounds that many potential farm foresters and private plantation growers are being discouraged from growing plantations because they learn from existing forest growers of the severe tax penalties they will face at the time of harvest.

It beggars belief that in the context of an ageing and more long lived population there are serious flaws in the superannuation schemes that seek to actively discourage long term investments to provide for retirement.

### **NON COMMERCIAL LOSS AND THE COMMISSIONER'S DISCRETION**

*Australian Forest Growers advocates that the Australian Taxation Office should streamline the process by which private forest growers secure the Commissioner's discretion under the non-commercial loss legislation.*

The non-commercial loss provisions of the Tax Act enable a taxpayer to seek the Tax Commissioner's discretion to claim business losses in the year they are incurred for a business activity that has a 'lead time' between the losses claimed and the tax to be paid on revenue earned from the activity. Private forestry is the most common primary production activity for which the Commissioner's discretion is sought.

Where the private forestry activity involves the common widely used 'commodity' tree species, such as radiata pine, blue gum, shining gum, and other species about which there is a substantial body of scientific and commercial information, private growers by and large are successful in being granted the Commissioner's discretion.

However, private forest growers whose forestry activities involve species and forestry configurations that are less well-known and less researched continue to face a difficult time with Australian Taxation Office (ATO) staff, involving repeating ATO requests for more information from different independent sources. The lack of available information creates consistent and repeated challenges for the forest grower applicant, who must be able to compile sufficient independent evidence and cash flow information for the Commissioner's discretion to be granted.

The administrative and financial burden imposed on many private forestry applicants for the Commissioner's discretion is unnecessarily onerous and unacceptable. Australian Forest Growers is engaged in discussions with the ATO on this matter, and has the ATO's agreement that an applicant's case would be strengthened by relying on evidence provided by AFG as to the commerciality of the diverse silvicultural regimes for various forest tree species around Australia. It is important that a mechanism be found by which private forestry applicants can more easily satisfy the Commissioner's requirements in cases where there is very little available 'independent evidence' to support the applicant's claim to be carrying on a commercial forestry operation.

### **NATURAL RESOURCE MANAGEMENT – GREATER THAN 100% TAX DEDUCTIBILITY**

Historically the Commonwealth has allowed greater than 100% tax deductibility for minimum tillage equipment and fodder storage. A similar concession should be made available to encourage environmental stewardship for NRM outcomes. This may take the form of riparian or other environmentally beneficial establishment of trees that will allow a more biodiverse and yet productive integrated agricultural landscape.

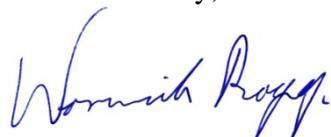
### **CONCLUSION**

AFG seeks a tax regime that recognises and corrects the 'period inequity' that applies to long-term private forestry investment; enhances the liquidity of private forestry;

and encourages private investment in forestry at any scale. AFG advocates a more willing and sympathetic ATO treatment of private forestry applications for the Commissioner's discretion under the non-commercial loss provisions, when the applications are supported by evidence derived from an AFG 'reference guide' to private commercial forestry activity. AFG calls on the Australian Government to recognise that amending the tax rules applying to superannuation and biophysical self-generating assets (such as private forests) can help achieve its retirement policy objectives. AFG supports a Farm Management Deposits Scheme (or equivalent) that recognises and accommodates the unique characteristics of private forestry and does not discriminate against forest growers. AFG seeks a stable, predictable and neutral taxation environment.

Thank you for the opportunity to make a submission. Please do not hesitate to contact the undersigned on 6162 9000 should you wish to discuss any of the issues raised. Please find attached Australian Forest Growers policies pertaining to taxation (Attachment A – Taxation General, Attachment B – Non Commercial Loss and the Commissioner's Discretion, and Attachment C – Tax and 'Forests as Superannuation').

Yours sincerely,



Warwick Ragg  
**Chief Executive**

**ATTACHMENT A - AFG POLICY STATEMENT No. 27  
TAXATION GENERAL**

**ATTACHMENT B - AFG POLICY STATEMENT No. 28  
NON COMMERCIAL LOSS AND THE  
COMMISSIONER'S DISCRETION**

**ATTACHMENT C - AFG POLICY STATEMENT No. 29  
TAX AND 'FORESTS AS SUPERANNUATION'**

## ATTACHMENT A - AFG POLICY STATEMENT No. 27

### TAXATION GENERAL

*Australian Forest Growers* advocates that the Australian Government:

1. (i) explicitly recognises the complex and unique characteristics of plantation investment and its interaction with the tax system;  
(ii) confirms that the same basic tax treatment (ie the year-of-expenditure general business tax deduction against other income) will continue to apply to plantation forestry as it does to other harvested agricultural crops;  
(iii) acts to ensure the tax system makes it possible for a diverse range of business models to be used to attract new plantation forestry investment from a variety of investors with different investment requirements.
2. (i) gives priority to implementing the recommendations in the FWPRDC report 'Impediments to investment in long-rotation timber plantations';  
(ii) amends the tax legislation in whatever way is necessary so as not to impede or discourage the free trading of immature plantations by any class of buyers and sellers, thereby helping to attract more private investment in longer rotation sawlog plantations.
3. (i) amends the 'active asset' condition of the small business CGT concessions to either (a) allow that a farm would still qualify as an active asset when leased; or (b) delete the requirement for the retiring taxpayer to have an active asset at the time of the sale or transfer of the property;  
(ii) removes or raises the arbitrary asset value threshold in relation to private forestry to account for the appreciating nature of the asset.
4. considers as a priority the Ralph Review recommendation on the tax treatment of 'rights' such as profit a prendre, and issues a clear determination that resolves lingering uncertainty restraining the use of forest rights to enhance the liquidity of plantation investment.

### Background

The AFG submission to the Government's 2005 Review of the Taxation of Plantation Forestry made several recommendations, four of which are covered in this policy. The AFG 2005 and 2007 Policy Forum resolved that it endorses these recommendations. Some others are covered elsewhere in these policy statements. For a full list of the submission's recommendations (some of which have already been acted upon or overtaken by events), refer to: <http://www.afg.asn.au/submissions/submissions.html>.

Detailed tax policy in relation to forestry managed investment schemes (MIS) is the provenance of Treefarm Investment Managers Association (TIMA).

### Discussion

A number of long-standing tax issues affecting private forestry remain unresolved, despite AFG's efforts over, in some cases, nearly two decades.

These include, in particular, the need to recognise the unique interaction of the tax system with private forestry, especially the inequity created by so-called 'lumpy returns'; the need to recognise and remove tax impediments to the trading of immature standing plantations ('secondary markets'); and the need to resolve the

uncertainty impeding the use of *profit a prendre* (refer AFG Policy Property Rights) as a means of enhancing the liquidity of plantation investments.

A Board of Taxation review of the small business tax concessions failed to address a number of recommendations by both AFG and the National Farmers Federation.

AFG will continue to advocate the Government its responsibility to address these issues in order to remove discriminatory treatment of private forestry and enhance its attractiveness as a viable land use option.

**Preferred Outcome**

A tax regime that:

- (i) recognises and corrects the ‘period inequity’ that applies to long-term private forestry investment;
- (ii) enhances the liquidity of private forestry; and
- (iii) encourages the private investment in forestry at any scale.

## **ATTACHMENT B - AFG POLICY STATEMENT No. 28**

### **NON COMMERCIAL LOSS AND THE COMMISSIONER'S DISCRETION**

*Australian Forest Growers will work with the Australian Taxation Office to streamline the process by which private forest growers secure the Commissioner's discretion under the non-commercial loss legislation.*

#### **Background**

The non-commercial loss provisions of the Tax Act enable a taxpayer to seek the Tax Commissioner's discretion to claim business losses in the year they are incurred for a business activity that has a 'lead time' between the losses claimed and the tax to be paid on revenue earned from the activity. Private forestry is the most common primary production activity for which the Commissioner's discretion is sought.

Where the private forestry activity involves the common widely used 'commodity' tree species, such as radiata pine, blue gum, shining gum, and other species about which there is a substantial body of scientific and commercial information, private growers by and large are successful in being granted the Commissioner's discretion.

However, private forest growers whose forestry activities involve species and forestry configurations that are less well-known and less researched continue to face a difficult time with Australian Taxation Office (ATO) staff, involving repeated ATO requests for more information from different independent sources. The lack of available information creates consistent and repeated challenges for the forest grower applicant, who must be able to compile sufficient independent evidence and cash flow information for the Commissioner's discretion to be granted.

#### **Discussion**

The administrative and financial burden imposed on many private forestry applicants for the Commissioner's discretion is unnecessarily onerous and unacceptable. Australian Forest Growers is engaged in discussions with the ATO on this matter, and has the ATO's agreement that an applicant's case would be strengthened by relying on evidence provided by AFG as to the commerciality of the diverse silvicultural regimes for various forest tree species around Australia. It is important that a mechanism be found by which private forestry applicants can more easily satisfy the Commissioner's requirements in cases where there is very little readily available 'independent evidence' to support the applicant's claim to be carrying on a commercial forestry operation.

AFG is developing the means to provide private growers with material to support their applications for Commissioner's discretion.

#### **Preferred Outcome**

More willing and sympathetic ATO treatment of private forestry applications for the Commissioner's discretion under the non-commercial loss provisions, when the applications are supported by evidence derived from an AFG 'reference guide' to private commercial forestry activity.

## ATTACHMENT C - AFG POLICY STATEMENT No. 29

### TAX AND 'FORESTS AS SUPERANNUATION'

*Australian Forest Growers* advocates that all relevant legislation should enhance the capacity of private forest growers to utilise their forests as a form of superannuation.

*Australian Forest Growers* advocates that the Australian Government:

- (i) explicitly recognises that amending the taxation rules applying to superannuation and biophysical self-generating assets (such as private forests) can help achieve its retirement policy objectives;
- (ii) amends the rules applying to self-managed superannuation funds (SMSFs) so that plantation forests established and managed provide retirement income can be transferred into SMSFs;
- (iii) implements further revision to the conditions of the Farm Management Deposits Scheme as per the following to remove discrimination against private forestry;
  - (a) enabling FMDs to be made on behalf of partnerships and family companies;
  - (b) redefining the withdrawal threshold in relation to death or retirement from primary production (allowing roll-over superannuation funds of the beneficiaries), with a special provision for forestry (or any primary production enterprise with long-term/lumpy return characteristics) of, say, three years; and
  - (c) increasing the maximum limit on funds held in deposits from \$365,000 to \$500,000 or annual farm turnover.

#### Background

Many private plantations have been, and continue to be, established and managed as an important element, and in some cases the totality, of the growers' superannuation.

Despite this admirable intention, such growers are subject to severe discrimination within the superannuation regulatory system. This failure takes two major forms.

One is the endemic problem of 'lumpy returns', whereby the grower receives 'superannuation' income at harvest in one lump sum, almost all of which is taxable at the highest marginal rate, rather than at any form of concessional rate such as that applying to monies withdrawn from a superannuation fund.

This problem is made worse for most private plantation growers by the limited and highly conditional access they have to the major income averaging provision available to other primary producers. First, Farm Management Deposits (FMDs) are only available to primary producers with 'off-farm' incomes less than \$65,000, which eliminates most private plantation growers. Second, any eligibility quickly evaporates if the grower doesn't carry on primary production after final harvesting (most common), because any income placed with an FMD must be withdrawn within only 120 days of when primary production ceases.

The second important manifestation is the treatment of a private plantation with respect to its contribution to a grower's self-managed superannuation fund (SMSF). Although a private forest may be part of a SMSF in circumstances where the forest operation is commenced by the fund, transfer of an established forest into an SMSF can only occur in very specific and very rare circumstances that satisfy a number of the SMSF tests, such as 'sole purpose', 'related party' and 'business real property'.

Most private plantations now approaching harvest age were established well before the contemporary SMSF 'revolution', and have no chance of being made to fit the current SMSF conditions that would allow the growers to take advantage of the tax treatment of superannuation funds.

### **Discussion**

For more than a decade, policy makers in Australia have realised that, with an ageing population that will live longer, steps must be taken to encourage individuals to fund their own retirement.

Over roughly the same period, State and Federal Governments and industry have driven a plantation industry development strategy, *Plantations for Australia: The 2020 Vision*, and have recognised the simultaneous contributions that private plantations and farm forestry can make to natural resource management as well as social and economic development objectives.

However, many of the private growers who established long-rotation plantations decades ago in order to 'fund their own retirement' are now suffering personally from that decision. They are confronted by a tax regime that penalises 'long term forestry with one final harvest', and that also prevents them converting an older form of superannuation (plantation forestry) into a more contemporary form (SMSF).

Further, anecdotal evidence abounds that many potential farm foresters and private plantation growers are being discouraged from growing plantations because they learn from existing forest growers of the severe tax penalties they will face at the time of harvest.

All of these problems are separate from but not unrelated to the fact that the tax system also discourages trading in immature standing plantations ('secondary markets'), which, if it were readily achievable, would provide more flexibility and choice for private plantation growers, and perhaps diminish pressure for 'superannuation' change.

### **Preferred Outcome**

- Australian Government recognition that amending the tax rules applying to superannuation and biophysical self-generating assets (such as private forests) can help achieve its retirement policy objectives.
- A Farm Management Deposits Scheme (or equivalent) that recognises and accommodates the unique characteristics of private forestry and does not discriminate against forest growers.