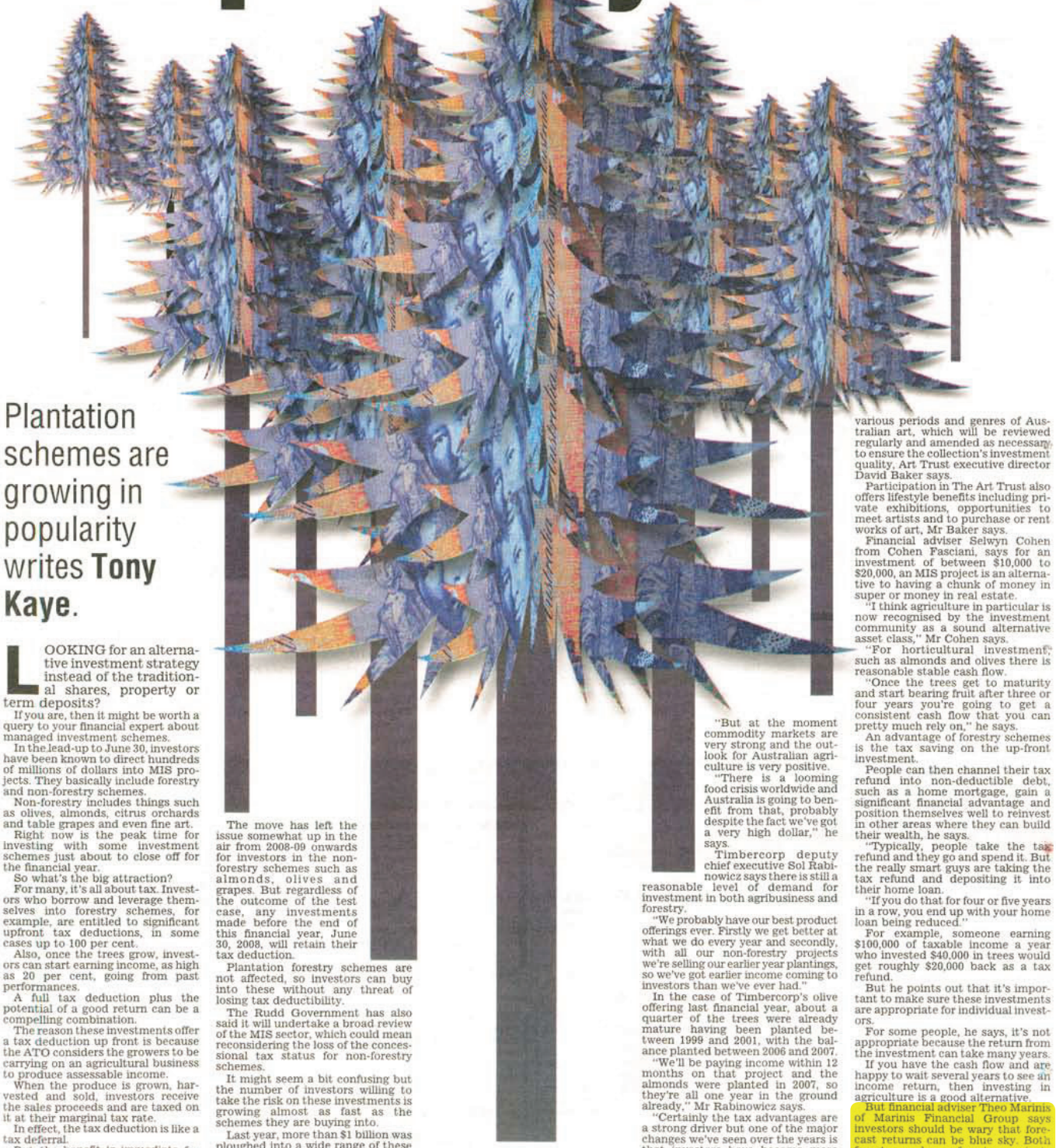
Reap what you sow



Plantation schemes are growing in popularity writes **Tony Kaye**.

LOOKING for an alternative investment strategy instead of the traditional shares, property or term deposits?

If you are, then it might be worth a query to your financial expert about managed investment schemes.

In the lead-up to June 30, investors have been known to direct hundreds of millions of dollars into MIS projects. They basically include forestry and non-forestry schemes.

Non-forestry includes things such as olives, almonds, citrus orchards and table grapes and even fine art.

Right now is the peak time for investing with some investment schemes just about to close off for the financial year.

So what's the big attraction?

For many, it's all about tax. Investors who borrow and leverage themselves into forestry schemes, for example, are entitled to significant upfront tax deductions, in some cases up to 100 per cent.

Also, once the trees grow, investors can start earning income, as high as 20 per cent, going from past performances.

A full tax deduction plus the potential of a good return can be a compelling combination.

The reason these investments offer a tax deduction up front is because the ATO considers the growers to be carrying on an agricultural business to produce assessable income.

When the produce is grown, harvested and sold, investors receive the sales proceeds and are taxed on it at their marginal tax rate.

In effect, the tax deduction is like a tax deferral.

But the benefit is immediate for investors who need to defer tax on income earned and the likelihood is that the income generated from the scheme down the track (potentially up to 12 years in the future) will more than offset any tax due.

However, this financial year could be the last tax hurrah for the non-forestry schemes.

The former federal government moved to abolish the preferential tax status of these schemes with effect from the start of the new financial year.

However, this decision will soon be tested in the courts in a case brought by the industry against the Australian Tax Office.

The move has left the issue somewhat up in the air from 2008-09 onwards for investors in the non-forestry schemes such as almonds, olives and grapes. But regardless of the outcome of the test case, any investments made before the end of this financial year, June 30, 2008, will retain their tax deduction.

Plantation forestry schemes are not affected, so investors can buy into these without any threat of losing tax deductibility.

The Rudd Government has also said it will undertake a broad review of the MIS sector, which could mean reconsidering the loss of the concessional tax status for non-forestry schemes.

It might seem a bit confusing but the number of investors willing to take the risk on these investments is growing almost as fast as the schemes they are buying into.

Last year, more than $1 billion was ploughed into a wide range of these agricultural investments.

Industry expectations are that the level of investment this financial year will be roughly the same as last year, although they could be slightly down because of the uncertain tax situation and the overall decline in the financial markets.

Most forestry investment schemes are through listed companies such as Timbercorp, Gunns, Great Southern Plantations and Willmott Forests and more than a dozen unlisted groups.

Australia now has 1.9 million hectares of plantations, including one million softwood, mainly radiata pine, and 900,000ha of hardwood, predominantly blue gums.

Most of this is controlled by the large listed companies, which are adding tens of thousands of hectares in new plantings every year.

Shane Kelly, managing director of research house Adviser Edge, says from an investor's perspective the main thing is to spread your risk by investing across regions, managers and industries.

"You don't approach agribusiness trying to pick winners, Mr Kelly says.

"You need to adopt the approach of diversification to reduce the potential impact of any one project hurting your portfolio should something like a drought occur or a significant shift in commodity prices.

"But at the moment commodity markets are very strong and the outlook for Australian agriculture is very positive.

"There is a looming food crisis worldwide and Australia is going to benefit from that, probably despite the fact we've got a very high dollar," he says.

Timbercorp deputy chief executive Sol Rabinowicz says there is still a reasonable level of demand for investment in both agribusiness and forestry.

"We probably have our best product offerings ever. Firstly we get better at what we do every year and secondly, with all our non-forestry projects we're selling our earlier year plantings, so we've got earlier income coming to investors than we've ever had."

In the case of Timbercorp's olive offering last financial year, about a quarter of the trees were already mature having been planted between 1999 and 2001, with the balance planted between 2006 and 2007.

"We'll be paying income within 12 months on that project and the almonds were planted in 2007, so they're all one year in the ground already," Mr Rabinowicz says.

"Certainly the tax advantages are a strong driver but one of the major changes we've seen over the years is that investors have become more sophisticated in ensuring that the underlying investment is sound, irrespective of the tax deductions.

"Investors have a fair number of options available in terms of the tax-effective investment market, so they're going to properly assess those options against what's going to give them the best return."

For something a bit different, another MIS investment option just launched is the Art Trust, Australia's first public art investment fund. It hopes to raise between $30 million and $50 million to invest directly in Australian art.

The Art Trust will adopt a diversified investment strategy covering various periods and genres of Australian art, which will be reviewed regularly and amended as necessary to ensure the collection's investment quality, Art Trust executive director David Baker says.

Participation in The Art Trust also offers lifestyle benefits including private exhibitions, opportunities to meet artists and to purchase or rent works of art, Mr Baker says.

Financial adviser Selwyn Cohen from Cohen Fasciani, says for an investment of between $10,000 to $20,000, an MIS project is an alternative to having a chunk of money in super or money in real estate.

"I think agriculture in particular is now recognised by the investment community as a sound alternative asset class," Mr Cohen says.

"For horticultural investment, such as almonds and olives there is reasonable stable cash flow.

"Once the trees get to maturity and start bearing fruit after three or four years you're going to get a consistent cash flow that you can pretty much rely on," he says.

An advantage of forestry schemes is the tax saving on the up-front investment.

People can then channel their tax refund into non-deductible debt, such as a home mortgage, gain a significant financial advantage and position themselves well to reinvest in other areas where they can build their wealth, he says.

"Typically, people take the tax refund and they go and spend it. But the really smart guys are taking the tax refund and depositing it into their home loan.

"If you do that for four or five years in a row, you end up with your home loan being reduced."

For example, someone earning $100,000 of taxable income a year who invested $40,000 in trees would get roughly $20,000 back as a tax refund.

But he points out that it's important to make sure these investments are appropriate for individual investors.

For some people, he says, it's not appropriate because the return from the investment can take many years.

If you have the cash flow and are happy to wait several years to see an income return, then investing in agriculture is a good alternative.

But financial adviser Theo Marinis of Marinis Financial Group says investors should be wary that forecast returns can be blue sky. Both forestry and non-forestry projects can be affected by factors such as drought.

He adds that there can be a drain on an investor's cash flow because the best immediate tax break is achieved by borrowing to invest, which means ongoing loan repayments.

"They're a classic geared borrowing situation and for every winner there's plenty who don't get the return they were hoping for," Mr Marinis says.

"Also, I don't believe in investing just for a tax deduction. The investment numbers have to stack up and the tax return should be just the cream on the cake."