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22 October 2012

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Dear Greg

TAX TREATMENT OF THE CONTRACT TRANSFER POLICY

You have requested our initial high level advice on the likely tax implications associated with Dairy Farmer Milk Co-operation (“**DFMC**”) members transferring a milk supply contract pursuant to the DFMC Contract Transfer Policy dated 21 October 2012 (“the **Policy**”).

Please note that our advice is high level and has been limited to considering the tax implications associated with the transfer of a milk supply contract. Further, our high level advice does not contemplate the individual circumstances of the various DFMC members that may participate in this type of transaction. Consequently, we would strongly recommend that DFMC members obtain specific taxation advice that considers their particular circumstances before undertaking any such transaction.

Background

Based on the Policy as it currently stands, we understand the following:

- DFMC has drafted a Policy which contemplates allowing a DFMC member (“the **Exiting Famer**”) to transfer or otherwise disposes of certain supply contracts it has with DFMC, to another DFMC member (“the **Acquiring Famer**”), providing certain criteria are met.
- The Policy facilitates that this arrangement between the Exiting Farmer and the Acquiring Farmer can be for an amount of consideration as negotiated by the parties.
- DFMC will only approve the transfer of the supply contracts providing certain criteria are met. One such criterion is that the Exiting Farmer is genuinely exiting the dairy industry.
- The Exiting Famer holds the milk supply contract on capital account.

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Our Ref: Draft DFMC Advice- Transfer Of Milk Supply Contract.Docx

Please inform us if our understanding of the facts is incorrect so that we may consider the impact, if any, on our advice.

For the avoidance of any doubt, you should note that we have limited our advice to only the high level tax implications associated with the transfer of the milk supply contracts and have not considered the tax implication associated with transferring or otherwise disposing other assets necessary to operate a dairy farm, including stock for example. Again, these should be considered having regard to the specific circumstances of the Exiting Farmer.

Conclusion

In our view:

- The sale, transfer or otherwise disposal of the milk supply contract will be subject to capital gains tax for the Exiting Farmer.
- CGT rollovers and concessions may apply to the Exiting Farmer depending on their individual circumstances.
- In the first instance, the Exiting Farmer will need to remit GST in connection with this transaction. There may, however, be circumstances where sale of the milk contracts are considered to be part of a broader transaction such that the transaction in its entirety will be considered as being a sale of a going concern.
- This transaction may be subject to stamp duty in the relevant state. We recommend that specific advice is sought having regard to the particular circumstances of the transaction.
- Care should be taken to ensure that this transaction does not jeopardise DFMC's ability to qualify as a co-operative. Based on our understanding of the facts, we consider the likelihood of this to be low.

We set out our detailed analysis of this matter below.

Analysis

Capital gains tax ("CGT")

The milk supply contract that the Exiting Farmer has entered into with DFMC is a capital gains tax asset of the Exiting Farmer. As such, the sale, transfer or disposal of the milk supply contract will be a CGT event for the Exiting Farmer. Broadly, the capital gain or loss will be calculated as the difference between the sale proceeds received as consideration and the cost base of the supply contract. The cost base of the supply contract is likely to be limited to legal fees incurred in connection with bringing the supply contract into effect.

Any CGT gain derived by the Exiting Farmer in connection with the sale of the milk supply contract should be able to be offset against any carry forward tax losses. The Exiting Farmer may also be entitled to a CGT discount to the extent that the Exiting Farmer has held the milk supply contract for longer than 12 months and does not have sufficient tax



losses to offset against the gain. Please note that a CGT discount will not be available for the Exiting Farmer where the legal owner of the milk supply contract is a company.

Care should be taken to ensure that both the Exiting Farmer and the Acquiring Farmer are negotiating the terms of the transfer on an arm's-length basis. The market value substitution rules, which if applied, may deem that the transaction to have occurred at the market value despite the cash proceeds actually received, for the purpose of the Exiting Farmer calculating their CGT liability. This is particularly pertinent where say, the transfer of the milk supply contract occurs between related parties (i.e. between members of the same family). We would recommend that an independent valuation is prepared and held in all instances where the sale of the milk supply contract occurs between related parties.

Depending on the particular circumstances of the Exiting Farmer, there may be opportunities to access certain other CGT concessions and rollover, such as the small business concessions.

We note from the Policy that one condition precedent that needs to be satisfied before DFMC will approve the transfer, is that the Exiting Farmer must be genuinely exiting the dairy industry. There are likely to be a number of other tax implications that need to be considered in addition to those associated with the transfer of the milk supply agreements. Again, these should be considered on a case by case basis, having regard to the specific circumstances of the Exiting Farmer.

Goods and services tax ("GST")

The transfer or otherwise disposal of a milk supply contract will be subject to GST. As such, the Exiting Farmer will need to provide the Acquiring Farmer with the tax invoice on completion of this transaction. It is extremely important to note that the onus to remit the appropriate amount of GST on this transaction will be the Exiting Farmers. As such, care should be taken to ensure that each party understands the GST consequences in connection therewith. The Exiting Farmer should have an appropriate GST gross-up clause in any agreement to allow for an additional amount for GST to be received from the Acquiring Farmer.

Please note the sale of the milk supply contract in itself is unlikely to qualify for the going-concern exemption (GST will be charged at 0%). Notwithstanding this, the going-concern exemption may be available after having regard to the specific circumstances of the individual transactions. There are certain advantages for the Acquiring Farmer for the sale to be treated as a going-concern should that transaction also be subject to stamp duty.

Stamp duty

The transfer of a milk supply contract may be regarded as a dutiable transaction having regard to the specific circumstances of the transaction. If this was the case, the Acquiring Farmer will be liable for stamp duty, which will be calculated on the GST inclusive price of the transaction. We would recommend that the Acquiring Farmer obtains advice on the stamp duty implications of the proposed transaction in the relevant state.



Other

Finally, care should be taken by DFMC to ensure that any transactions of this nature do not affect its ability to continue to qualify as a co-operative. For the avoidance of any doubt, DFMC is unlikely to qualify as a co-operative in any income year where the business with its members is less than 90% of its total business.

Based on our understanding of the Policy as it currently stands, the risk of this occurring appears low given that the Policy states that the Exiting Farmer's Contract will be deemed to have terminated from the date that DFMC consents to the transfer of the milk supply contact.

We are happy to discuss this in further detail if required.

Disclaimer

This letter sets out our comments in relation to Australian taxation law as applied to DFMC Contract Transfer Policy dated 21 October 2012. It is based on the policy information provided and we have not reviewed the underlying documents.

The analysis contained in this letter is based upon applying the current legislation, judicial authorities and Commissioner's rulings to the facts and circumstances as noted. However, it must be recognised that there is no guarantee that such implications will last into the future and/or that the Commissioner may hold a different view as to how such authorities should be interpreted.

This letter has been prepared for the sole use of DFMC as at the date of this letter, and is not to be relied upon by any other person or body corporate without the express written permission of Grant Thornton Australia Limited.

General

Please contact Aaron Davies on 8297 2744 or me on 8297 2509 if you have any further queries or would like any matters clarified.

Yours sincerely
GRANT THORNTON AUSTRALIA LIMITED

Peter Berg
Partner - Taxation