



IRISH CATTLE AND SHEEP FARMERS' ASSOCIATION

Submission on the Agri-Taxation Review

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Introduction

It is ICSA's position that the Irish tax regime with reference to agriculture should:

- Incentivise hard work and entrepreneurial spirit;
- Assist those who have invested in developing and expanding their farms;
- Support efficient farm transfer between the generations without punitive capital taxes;
- Feature VAT / excise duty / carbon tax that makes Irish agriculture more competitive and;
- Encourage long term land leasing, farm partnerships, land consolidation and installation of young farmers

Since the beginning of the fiscal/economic crisis there has been a significant increase in the level of personal income taxation. While Government policy is to put more emphasis on expenditure reduction rather than tax increases, the reality is that this objective is circumscribed to a significant and even decisive extent by the Croke Park agreement and by the policy of no cuts to headline social welfare rates.

Government policy in terms of tax increases is that any increases should be achieved through a broadening of the tax base rather than increases in income tax. Hence the household charge was introduced in 2012 as a pre-cursor to a full-blown property tax due which was introduced in 2013. Nonetheless, the cumulative effect of budgets introduced since 2007 has been to substantially increase the marginal rate of tax/PRSI/USC. In 2007, the marginal rate of tax/PRSI/ Health Levy on incomes in excess of €48,800 was 43%. By 2012, the marginal rate on incomes was in excess of €32,800 is 52% for PAYE and up to 55% for self employed.

These are substantial increases and give lie to the notion that there has been no effort made to get extra tax from the better off. Unfortunately, in the Irish tax system, better-off is essentially marked by a cut-off point of €32,800 (reduced from €36,400 in 2011). However, it is now clear that income tax rates are at a level that are killing the incentive to work and moreover, creating huge pressures on middle income families that are bearing the brunt of the adjustments and have no benefits such as medical cards, exemptions from property taxes and other charges.

Income tax rates are now also at levels that are extremely onerous on unincorporated sole traders such as farmers. This is particularly so in the contest of enterprises trying to pay down principal on borrowings out of after tax income. Accelerated capital allowances have been phased out (e.g. 3 years for Farm Waste Management Scheme Expenditure) and there are no allowances for land purchase for example. Farm income volatility is also a huge issue that is impacted by tax levels. As volatility increases, farmers who have profit in a good year should ideally set aside some of this for the almost inevitable downturn in future years.

In the context of the above points, ICSA notes that some aspects of current taxation policy has the capacity to undermine entrepreneurial endeavour and should be reviewed, with particular reference to the agri-food sector; support for primary producers will be key in delivering upon the objectives of Food Harvest 2020, and this can be facilitated via a forward-thinking and non-punitive tax regime.

Responses to consultation questions

Question 1 - What current agri-taxation measures are working effectively and why?

Stamp duty levels: ICSA welcomed the Budget 2012 reduction in stamp duty on agricultural land transfers to 2%. This significantly reduced the potential upfront cost of purchasing land for many farmers. The specialised consanguinity relief of 1% stamp duty for transfers between blood relatives is considered to be of additional benefit, but there is concern that it is being abolished from 31 December 2014.

Young trained farmer stamp duty relief: For farmers under 35 with a green cert or equivalent that commit to not less than 50% of their time farming land transferred into their name for five years, no stamp duty is payable at all. This measure is seen as an effective method by which transfer of land and the expansion of a farm holding is encouraged for young farmers.

Income tax relief for long-term land leasing: The existing regime wherein farmers over 40 who enter a leasing arrangement of 5 to 10 years is seen as an efficient system by which land may be more productively used. Access to land remains one of the key restrictions within Irish agriculture and this measure contributes to facilitating better access whilst also reducing the risk of rising land rental prices.

Capital acquisitions tax agricultural relief: The agricultural relief applied via a 90% reduction in farm asset value for the purposes of CAT is a useful tool and prevents a significant number of farmers being saddled with high tax costs from the transfer of a productive asset such as farmland. However, there are concerns regarding the lack of targeting of this measure towards active farmers; this is addressed under Question 3.

Relief for Farm Restructuring: The 2013 Finance Act provides for relief from Capital Gains Tax where land is sold in order to finance the purchase of land closer to home. This can be achieved by way of an exchange of land between two farmers or by means of a sale and purchase. This is a very necessary relief and should be continued into the long term.

Question 2 - What current agri-taxation measures are not working effectively and why?

Overall capital acquisitions tax levels: From December 6, 2012, the Group A (parent-child) tax-free threshold was reduced to €225,000 (progressively down from €434,000 in 2009), while the CGT tax rate has been increased incrementally from 20% to 33%. Both of these measures increased the risk of significant tax liabilities for farmers who take over the family farm, either by way of gift or inheritance. The above changes mean that a young farmer taking over the farming business where land and other assets exceed €2.5 million is at risk of a substantial tax liability on the excess at a rate of 33%. Such taxes have the potential to undermine the viability of the young farmer and could set back plans for investment and farm development, which are vital for increasing exports and in the longer run should lead to more taxable income.

Capital gains tax retirement relief: Budget 2012 provided for the introduction at the end of 2013 of a new upper limit of €3 million where the person transferring is aged over 66. ICSA regards this as a bizarre tax, which penalises a farmer who hands over the farm to the next generation without any financial consideration. While the measure was presented as an incentive to transfer before age 66, the

reality is that there are many factors influencing farm transfer, including the age and circumstances of the successor.

A potential tax hit to a farmer of 66 who may not have access to a pension other than the contributory old age pension may in fact cause transfer to be deferred until death rather than encourage transfer before 66. While early transfer of farms is preferable in some circumstances this is not always the case and may not be feasible for a variety of reasons. The introduction of a penalty on those aged over 66 is rather arbitrary and should be reversed, as it is likely to cause more cases of delayed transfer than early transfer.

While there is comfort from the fact that the retirement relief change only applies on assets which exceed €3 million, there is a concern that once the principle is established, the tendency is to reduce the threshold.

Income averaging: Income averaging is a tool used to ensure that the tax liability over an extended period takes account of fluctuations in income and ensures that one good year in three does not lead to an excessive tax burden relative to the longer term income generation on the farm. However, it is questionable as to whether it is proving sufficient to deal with the extremes in product price and input cost volatility seen in the past 4 to 5 years. It is recognised that income averaging can lead to problems for farmers when incomes are decreasing and there is a need to re-examine whether farmers should be allowed flexibility in opting out without penalty in cases where incomes have fallen sharply in twelve months. Moreover, it does not adequately facilitate “rainy day” planning which is becoming more vital for farm enterprises subject to increasing extremes of volatility. Events such as the prolonged winter of 2012-2013 also point to the need for farmers to build up funds to cope with extremes in product price, cash flow challenges, weather events etc.

Employee Tax Credit: ICSA believes that the Employee Tax Credit discriminates against the self-employed, including full-time farmers. There is no longer any justification for this discrimination which potentially costs an individual full-time farmer €1650 in extra tax, assuming a tax liability. ICSA believes that the employee tax credit should be replaced with an earned tax credit, in line with the Commission on Taxation, although it should be phased in quickly rather than over time.

Question 3 - How could the tax system better influence activity in any of the key policy areas of:

Encouraging and attracting young farmers and new entrants to farming; Land mobility – transfers via the market, whether by sale or long-term leasing; Succession – earlier lifetime transfers within families (and non-family transfers also where no apparent successor is available)

Land Purchase:

The key issues on land purchase are:

- Stamp duty
- Tax treatment of land purchase.
- Farm restructuring relief

The stamp duty issue has been considerably relieved by the introduction of a rate of 2%.

However, the tax treatment of land purchase remains extremely onerous and certainly is a factor for farmers who wish to expand their holding. There has been some improvement to assist with farm consolidation which allows essentially for relief on capital taxes where land (typically an outside piece of land) in order to finance the purchase of an adjacent piece of land. This is extremely important in the context of the inefficiencies associated with fragmented holdings.

However, it does not deal with the more typical situation, which is a straightforward purchase of land. A farmer who buys land gets no tax relief on the capital cost of the land. However, the purchase of land is an investment in the viability of the holding and moreover, is a pre-requisite to planning for expanding production. It is almost impossible for a farmer to purchase land where land costs of the order of €10,000/ acre- out of after-tax profits when tax rates are 52% on income in excess of €32,800. Land purchase is limited to a great extent to those with inherited wealth or windfall gains from non-farming sources. This is not a desirable situation.

It is submitted that capital allowances should be available for the purchase of land, which would reflect the typical repayment periods for land of 10-15 years. This would essentially mean that tax relief would remain constant over the entire loan repayment period whereas at present, the tax burden increases on a year-by-year basis as the interest portion of the repayment diminishes and the principal portion increases.

Moreover, capital allowances on land purchase would create the potential for profitable farming enterprises to buy land using farm profitability as the means of finance. While the majority of farms will never have the income potential to achieve this, it is likely that commercial dairy farms will be capable of generating income in the 52% tax bracket.

Farm Restructuring Relief: There are two problems here. First the relief is only available until 31st December 15 – this needs to be extended indefinitely. There is no reason for a short term incentive; farms can only be restructured when the opportunity arises and when it coincides with the financial wherewithal.

Second, the relief does not provide for sale and purchase of entire farms. However, it is clear that in many cases this will be the most efficient route to consolidating a farm holding. ICSA therefore submits that such transactions should also be facilitated.

Stamp duty consanguinity relief: At present, it is proposed to abolish this special relief at the end of 2014. This proposal should be shelved so as to not adversely affect land mobility between relatives.

Income tax relief for long-term land leasing: The relief provides that farmers who are aged over 40 shall be relieved from income tax in respect of leasing income, where long-term leases are entered into. The levels of relief depend on the term of the lease. Income of up to €12,000 is subject to tax relief in respect of 5 year leases, €15,000 in respect of 7 year leases and €20,000 in respect of 10 year leases. The tax relief is designed to encourage long term leasing because it is widely accepted that the short term (conacre) system does not facilitate forward planning by the leasee, nor does it encourage best land management practices and more intensive production. The lack of fixity of tenure was recognised as a problem in the 19th century but it is an extremely regrettable feature of Irish land policy that it is still an intractable problem in the 21st.

The tax relief, however, has not had the desired impact to date. One problem is that the highest level of tax relief applies to relatively long duration leases (10 years). A potential solution could be to introduce a once-off three-year window whereby those who enter into 5-year leases would be allowed the full level of relief (€20,000) in order to encourage them out of the conacre system. Once the practice of long-term leasing becomes established, the likelihood is greater that it will be continued whereas the present problem is that no consideration is given to changing from conacre.

It is also submitted that the tax treatment of short-term rental should be reviewed, possibly with a focus on whether tax reliefs should be tightened up or removed altogether for the land-owner who repeatedly rents all land on a conacre system.

Capital acquisitions tax relief: The current qualification test for agricultural relief is carried out on a purely financial basis, leading to concerns over recipients with little or no interest in farming; the 80% agriculture-related asset test is also problematic. To better target relief towards young/active farmers, requirement for a green cert or equivalent should form part of the relief assessment. Given the reduced CAT thresholds described under Question 2, the Department should review the possibility of raising the thresholds for specific land transfer cases, with particular reference to encouraging lifetime transfers of farmland; i.e. Gifts of farmland from parent to child should be incentivised through more efficient taxation, as opposed to the current situation where there is no benefit compared to transfer through inheritance. For example, the €225,000 CAT threshold should be increased to €300,000 for lifetime transfers to trained, young farmers.

It is also vital that the 90% agricultural relief remains in place. Any changes to this could have devastating impact on farm transfer.

Capital Gains Tax: The trend in recent budgets to increase the rate of CGT from 20% to 33% has been extremely damaging on a number of fronts. It is questionable whether the change will actually provide sustained increases in overall tax take from CGT; the experience in the past was that reducing the rate from 40% to 20% increased total revenues. Clearly, total revenues are primarily influenced by the way in which assets increase in value but there is also an important secondary influence in that the higher the rate, the more likely it is that individuals will refuse to realise a potential gain by selling or transferring an asset.

It is also likely that the appetite for investment is dimmed by higher CGT rates and this is not beneficial to growth in the economy. From a farming point of view, the higher rate of CGT reduces the incentive for retired farmers to sell land. It is well documented that Ireland's agricultural land market is relatively dysfunctional in terms of the lack of land sales and the very limited opportunities to expand farm holdings.

Capital Gains Tax is also giving rise to a problem in the changeover in Pillar One payments under CAP whereby land and entitlements are leased out in full in 2014 and the recommended solution is for the lessor to permanently transfer (i.e. sell) to the leasee. However, this potentially gives rise to a 33% tax bill to the lessor even though the motive is to ensure the retention of potential CAP payments for the leasee.

Stock relief: Budget 2012 introduced an enhanced stock relief of 50% for registered farm partnerships, which initially catered exclusively for dairy partnerships but which subsequently has been extended to cover other farm partnerships.

Young trained farmers continue to avail of 100% stock relief and other farmers are limited to 25%.

The key problem with stock relief is that the regime continues to be subject to an ongoing instability. Stock relief is typically up for review on a regular basis at Budget time and it seems that there is no real reason why this should be so. It is clear that farms, which expand stock numbers, are making an investment into the long term that will benefit the economy by increasing exports and supporting more jobs. Therefore, stock relief regimes should be put in place for 10-year periods.

Alternative farming models - collaborative farming such as farm partnerships, share farming, contract rearing or cow leasing; also farm business structure, i.e. sole trader or incorporation

The discrepancy in income tax rates between sole trader and corporation tax is substantial and is forcing farmers down the incorporation route in the case of the more profitable dairy enterprise. This has disadvantages for farmers but it also poses a threat to tax take from a revenue perspective. For that reason, tax policy should look at reducing the rate of income tax, particularly for middle income levels and also at providing additional incentives/ reliefs to the sole trader. (see proposal for “rainy day” relief under question 4)

Environmental sustainability

Carbon and excise duties: The increase in Carbon Tax in recent budgets has been very damaging to the viability of farms and agricultural contractors. Excise duties are also damaging. The double tax refund available against the carbon tax is extremely cumbersome and not well understood. It is manifestly preferable to simply reduce carbon tax and excise duties on agricultural fuel.

Smart Farming - encouraging innovation, improving skill levels and maximising the adoption of best practice.

ICSA suggests that the payments for participation in BTAP/STAP or similar discussion groups should be exempted from income tax.

Question 4 - Are there any other priority areas or future challenges that the tax system should seek to address?

The most obvious anomaly is that the Irish economic strategy (for which there is broad agreement) holds that low corporation tax rates of 12.5% are absolutely essential as an incentive to invest and to create jobs yet there is no apparent understanding that marginal tax rates of 52% on incomes above €32,800 are extremely damaging to enterprise, hard work and re-investment on family businesses/ sole traders where incorporation is not suitable.

ICSA submits that “rainy day” planning should be encouraged as an alternative to income averaging. This would be facilitated by allowing an unincorporated farmer to invest a proportion of profits in a good year tax free into a special account, which could be accessed in future years by one of three methods:

- Farmer withdraws money in a bad year for living expenses, which is subject to normal income taxation

- Farmer uses funds in the special account to invest in land purchase or farm development. This money would be available tax-free provided that it is directly invested in land, livestock purchase, farm buildings or reclamation. In the case of re-investment in buildings or reclamation, the normal capital allowances would not apply up to the amount funded from the special account.
- Farmer uses funds from the special account to cover exceptional costs such as extra feed in an extreme weather event. This money would be subject to income tax but it is likely that it would be set against the costs of buying extra feed.

A condition of this scheme would be that funds could not be accessed within 18 months of the end of the financial year in which the profit occurred. This would guarantee the “rainy day” nature of the scheme.

It is submitted that the extent to which profits could be invested into the special fund would be capped at a maximum of 50% of the net farm profit for the year.

Question 5 - Is there a high awareness of agri-taxation measures among a) farmers and b) professionals dealing with farmers; how can awareness of agri-taxation reliefs be raised?

In general, there is room for improvement in the awareness of agri-taxation measures, among farmers and in some cases, among professionals dealing with farmers. For example, the benefits of tax exemptions from long-term leases of farmland by persons over 40 years of age seems to be unappreciated given the ongoing propensity to short-term rental.

One possibility to increase awareness is to make tax planning a subject of discussion group meetings. (e.g. BTAP, STAP meetings)