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Consultation on the implementation of the Agri-taxation Review 2014 and income stabilisation and taxation

Dear Sir/Madam

We welcome the opportunity to provide input to the Consultation on the implementation of the Agri-taxation Review 2014 and income stabilisation and taxation. In preparing this submission, we have engaged with our members who advise the farming community and agri-business.

Background

Food Wise 2025 has set ambitious growth targets for the Irish agri-food industry, including increasing the value of agri-food exports by 85% to €19 billion by 2025. The global demand for food is expected to increase significantly, because of continued global population growth and economic development, especially from emerging economies, presenting significant opportunities for the Irish agri-food sector.

The next few years are therefore a crucial time for this industry and an efficient and highly productive farming sector is vital. Increased investment in farming will be required for these opportunities to be realised and targets met.

The consultation document highlights a number of significant challenges currently facing Irish agriculture, including:

- Income stabilisation, given increasing commodity price volatility in agricultural markets;
- Brexit, given the agri-food sector's reliance[1] on exporting to the UK and

[1] 39% of total sector exports in 2016 – see consultation paper.

- Climate change, given agriculture is the single biggest contributor to non-ETS greenhouse gas emissions which Ireland is legally bound[2] to reduce.
- Impact of recent severe and extended winter weather and resulting fodder crisis

It is important that these challenges are addressed if the ambitious targets for the sector are to be realised. Tax policy plays an important role in tackling these challenges and in supporting and encouraging activity and investment in the farming sector. It is critical to ensure that the tax system does not act as a barrier or an unnecessary impediment to the expansion of the sector.

In the detail of our submission, we have set out comments on the key tax reliefs and measures which can drive the government's policy objectives for the sector. We have structured our comments around the following policy goals:

1. Continuation of policies and reliefs which encourage new entrants to farming and earlier life-time transfers.
2. Promoting alternative farming structures - leasing and partnerships.
3. Increasing farm investment to deliver sustainability, innovation and growth

We have also highlighted the important measures, such as CGT Farm Restructuring Relief, Stamp Duty Relief for Young Trained Farmers and Stock Relief which are due to expire over the next two years. We strongly recommend that these reliefs which are critical to safeguarding the succession and viability of many Irish farms, should be retained into the future.

1. Continuation of policies and reliefs which encourage new entrants to farming and earlier life-time transfers

Capital Acquisitions Tax (CAT) Agricultural Relief

CAT Agricultural Relief reduces the market value of agricultural property by 90% for the purposes of calculating CAT. The relief is key to ensuring that CAT does not create a barrier to the transfer of agricultural property by way of gift or inheritance which could otherwise result in farmland having to be sold to pay a CAT liability.

CAT Agricultural Relief is a corner-stone of the tax regime for farmers and it is essential that relief at the 90% level is retained to help support the policy of farm transfers into the future.

Capital Gains Tax (CGT) Retirement Relief

CGT Retirement Relief provides for an exemption from CGT on the disposal of a business by persons aged over 55 provided certain criteria are met. These conditions include a requirement that the person making the disposal must have used the assets for business purposes (or been a director in the company) and owned the business assets for a minimum period of time prior to the transfer.

The relief encourages the lifetime transfer of farm land by farmers to the next generation rather than leaving the land to pass by inheritance. It is a very important relief which

[2] Ireland has a legally binding target to reduce non-ETS greenhouse gas emissions by 20% by 2020 (on 2005 levels) under the EU's Climate and Energy Package. This target increases to 30% by 2030 – see consultation paper.

removes or reduces the potential CGT charge on the transfer. Absent this relief, the lifetime transfer or disposal of most farms would be uneconomic.

However, there is a key issue that should be addressed to ensure the improved operation of the relief in circumstances where land is transferred between spouses and held in joint names.

Where assets pass between spouses/civil partners by way of **inheritance,** the legislation permits the recipient spouse to include the other spouse's ‘period of ownership’ and ‘period of use of the asset’ to determine the availability of retirement relief on a subsequent disposal.

In contrast, where a **lifetime transfer** of the assets occurs between spouses, the recipient spouse cannot include the other spouse’s period of use of the asset for this purpose. A similar distinction occurs when shares of a company are passed between spouses.

This distinction between inheritances and lifetime transfers should be removed to help facilitate the lifetime transfer of lands and joint ownership between spouses/civil partners in certain circumstances, such as, family farm transfers under section 599 TCA 1997.

CGT Farm Restructuring Relief

CGT Farm Restructuring Relief is a measure to support farmers consolidating their farm holdings. It provides for an exemption from CGT on disposal of agricultural land as part of a farm restructuring. The exemption applies where the proceeds are used within a two-year period to purchase different agricultural land which results in consolidating or improving the efficiency of the farmer’s holdings. The relief also applies to qualifying exchanges of land by farmers.

The relief is due to expire on 31 December 2019. The Institute suggests that consideration be given to extending CGT Farm Restructuring Relief beyond 2019.

In addition, we recommend that the interaction between CGT Farm Restructuring Relief and CAT Agricultural Relief should be examined, so that there is a more integrated approach taken to the operation of the reliefs. Even though a young famer may qualify for CGT Farm Restructuring Relief in circumstances where he/she may wish to consolidate his/her farms holdings, the same land disposal can create a clawback of agricultural relief for CAT purposes, if the disposal takes place within six years of the original land transfer from a parent. In circumstances where the farm restructure satisfies the conditions of the CGT farm restructuring relief, no clawback of agricultural relief should arise.

Stamp Duty Relief for Young Trained Farmers

Stamp duty relief for young trained farmers provides an exemption from stamp duty on transfers of farm land and buildings to young trained farmers. A young trained farmer is defined as a person under 35 years of age who has a relevant agricultural qualification. The farmer must subsequently spend more than 50% of his/her working time farming the land for the 5 years after the transfer, for the relief to apply.

Without this exemption, a significant upfront stamp duty cost could arise on the transfer of land until it can pass by inheritance. This would have the effect of reducing the level of capital available to the new farmer to invest in the farm. It is therefore important that this relief is retained beyond 31 December 2018 to avoid creating an additional barrier to farm land mobility.

Furthermore, some farm businesses are carried out by companies that farm land owned by the shareholder. The farmers in question spend the majority of their time engaged in the farming activities as employees of the company.

The availability of young trained farmers stamp duty relief in such circumstances is not certain and clarity would be welcome on this issue. Otherwise, the uncertainty could serve as a disincentive to making some transfers of land to young trained farmers when the land is farmed by a young trained farmer as an employee / shareholder of the farming company.

Stamp Duty Consanguinity Relief

Finance Act 2017 amended stamp duty consanguinity relief to provide for a 1% fixed rate of stamp duty to apply to land transfers between family members until 31 December 2020.

Presently, farmers above the age limit to qualify for stamp duty relief for young trained farmers, can avail of consanguinity relief to reduce the stamp duty cost on receipt of farm land from relatives. To limit the potential for stamp duty to discourage lifetime transfers of farmland, this relief should be extended beyond 2020, if necessary, for a further fixed period.

2. Promoting alternative farming structures - leasing and partnerships

The promotion of farm leasing and farm partnerships can play a key role in achieving the identified objectives for the sector. Such measures can help to increase the number of young farmers actively farming and greatly increase land mobility and productivity. Below we have outlined some proposed amendments to current measures which could further support this objective.

Farm Land Leasing Income Tax Exemption

The farm land leasing income tax exemption was amended from 1 January 2015 to allow individual landowners who lease farm land for a period of 15 years or more to be exempt from income tax on rental income of up to €40,000 per annum. A limited version of the exemption is available where the lease granted is between 5 and 15 years in duration. A qualifying lessee can be an individual or a company since 2015. Additionally, the lessee must not be connected to the lessor and must use the land as part of a farming trade.

This exemption is an important measure in facilitating more widespread long-term leasing of farm land. Encouraging long term land leasing to active farmers also helps to ensure that farm land is actively used for agricultural purposes. Leasing can make it more achievable for certain active farmers to increase their farm-holdings and farm productivity, who are not otherwise in the position to bear the up-front cost of purchasing land.

Incentivising long term leases to family members could encourage the earlier transfer of land with the parent having the security of a guaranteed income stream. To achieve this objective, the extension of the land leasing exemption to family members should be considered and we believe this could be achieved without under-mining the objective of ultimate transfer to the child.

Furthermore, while a parent might pass the family farm to a child to continue the farming business, a close relative such as an uncle or aunt with no immediate family of their own may gift or bequeath a farm to another sibling of the child who is farming. Often, that sibling may not wish to farm those lands and while the lands may be in close proximity to the home farm, the individual is incentivised to lease the land to a third party to avail of the farm leasing income tax exemption rather than to their sibling. If the exemption was extended to family members, it may ensure or enhance the viability the active farmer's livelihood.

Succession Farm Partnerships

A new Succession Farm Partnership model came into operation last year, following State Aid approval. It allows farmers to enter into a partnership, with an appropriate profit-sharing agreement that provides for the transfer of the farm to a younger farmer at the end of a specified period.

An income tax credit worth up to €5,000 per annum for five years is allocated to the partnership and split according to the profit-sharing agreement. At least 80% of the farm must transfer within 3 to 10 years and the successor must not have reached 40 years of age on entering the partnership.

Feedback from our members is that the requirement for farmers to be in a Registered Farm Partnership for three years before they can avail of a Succession Farm Partnership is proving somewhat problematic and impacting the current take up of the scheme. We also understand that there are some practical difficulties with the Specimen Agreement which need to be considered and further engagement should take place in this regard.

As the implementation of the scheme is still at an early stage, we would recommend that this partnership model be closely monitored over the coming months to assess whether the scheme is working as policymakers intended.

3. Increasing farm investment to deliver sustainability, innovation and growth

Food Wise 2025 has set ambitious targets to increase the level of exports from the Irish agricultural sector. It is vital that tax measures facilitate and support the increased capital investment by farmers that will be required if these objectives are to be met.

Additionally, tax measures which free up working capital for farmers are important to ensure that farmers have sufficient cash to make capital investments to increase production capacity.

Tax incentives for farm investment

Section 658 TCA 1997 provides that farmers can claim capital allowances in respect of qualifying expenditure on farm buildings over a 7-year period. Farmers are also entitled to claim standard wear and tear allowances for farm plant and machinery over an 8-year period.

Accelerated capital allowances

As outlined above, Food Wise 2025 sets ambitious targets for increased agri-food exports. For these targets to be achieved, substantially increased levels of farm investment will be required over the next few years.

If accelerated capital allowances were introduced for farm investment made before 2025, this could provide a significant incentive to encourage much needed investment. Allowing capital allowances to be claimed for farm buildings and for farm plant and machinery over a shorter period would result in a beneficial tax cash flow saving for farmers.

Enhanced deductions/tax credits for farm investment

Enhanced deductions/tax credits for farm investment could also provide an important incentive to encouraging farm investment during this critical period. We appreciate that EU State Aid provisions must be considered in this regard. However, the EU Guidelines for State Aid in the agricultural and forestry sectors[3] could be referenced to support this case.

The Guidelines makes clear at paragraph 143 that targeted aid for "the improvement of overall performance and sustainability of the agricultural holding" is allowable within limits. Investment in farm buildings and plant and machinery is listed as an allowable cost for such aid at paragraph 144.

An enhanced deduction or tax credit for eligible investments made before 2025 would provide important support and incentive to farmers to make investments in improving farm productivity. This could perhaps be based on certain criteria including income or restricted to fulltime farmers without off-farm income.

Promoting sustainability and environmental protection

The consultation paper notes that sustainability is one of the core themes of Food Wise 2025. Food Wise 2025 recognises that a significant increase in food production cannot be considered in isolation from its environmental impact. Tax incentives in the form of accelerated capital allowances and enhanced deductions or tax credits could encourage investment by farmers to improve environmental protection. The Commission's EU State Aid Guidelines[4] for the agricultural sector recognises "aid for agri-environmental-climate commitments", as being objectives, for which targeted aid can be given.

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[3] European Union Guidelines for State aid in the agricultural and forestry sectors and in rural areas 2014 to 2020 - 2014/C 204/01 – Part II, Chapter 1

[4] European Union Guidelines for State aid in the agricultural and forestry sectors and in rural areas 2014 to 2020 - 2014/C 204/01 – Part II, Chapter 1.

The extension of the scheme of accelerated capital allowances for certain energy efficient equipment[5] to include sole traders was a welcome move in Finance Act 2016, allowing farmers to avail of a full tax deduction for capital expenditure on certain listed equipment in the first year. Consideration should also be given to providing other tax incentives such as further accelerated allowances, enhanced deductions or tax credits to support this policy objective of sustainable rural communities.

Working Capital Supports

Working capital is a crucial issue for farmers. If farmers are concerned about having sufficient working capital to operate their day to day business, they will be reluctant or unable to make capital investments to improve the farm. A number of tax measures provide important support to farmers in managing their cashflow and working capital and it is important that these are retained.

Income Averaging

Income averaging is a scheme which brings important tax stability for farmers. It provides that, instead of paying tax on their farming profits that arise in the year, farmers can elect to pay tax on the averaged profit and losses of their farming trade over a period of 5 years. Given the increasing volatility of farm income in Ireland, income averaging should be retained and enhanced.

However, income averaging legislation is prescriptive in defining certain individuals to whom the relief does not apply. Where a farmer, or their spouse, carries out another trade or profession or owns more than 25% of the share capital of a trading company, income averaging is unavailable. The scope of the restriction is quite broad and excludes individuals from the relief in circumstances that can create hardship. We believe that the availability of the relief should be broadened within certain defined criteria.

We understand that ICOS are currently working on an updated version of their 555 scheme which would apply across all sectors to help deal with farm income volatility. Given that commodity price volatility is likely to continue, further measures, such as the new ICOS scheme should also be considered.

Furthermore, we understand that there are a number of other schemes operated internationally which deal with farm income volatility, such as in France, Australia and New Zealand. It might be useful to explore whether such schemes could work in an Irish context.

Stock Relief

Stock relief is a relief given to farmers in respect of increases in the value of farm trading stock. It is given as a deduction equal to 25% (50% in the case of Registered Farm Partnerships) of the increase in the value of the stock between the beginning and end of an accounting period. This relief helps to reduce the cash flow cost for a farmer of having to account for tax on increases in stock value that have not yet been realised. This relief is due to expire on 31 December 2018. It is very important that this measure is retained,

[5] Section 285A TCA 1997.

particularly as farmers seeking to expand are likely to invest heavily in stock in the next few years.

Stock Relief for Young Trained Farmers

An enhanced version of stock relief is available for young trained farmers. These farmers can claim a deduction for the full 100% of the increase in stock value. A young trained farmer is defined as a person under the age of 35 with a relevant farming qualification. The relief applies for the first 4 years in which the farmer is engaged in farming.

The relief provides an important incentive for new farmers who are likely to invest heavily in stock early in their farming career. In the absence of the relief, the resulting tax charge could create significant cash flow issues for farmers and hamper their ability to invest in their farms.

There is some inflexibility inherent in the relief at present. It applies automatically in the first 4 years of farming. During this period the farmer may also be making significant capital investments which may not leave them in a position to invest in stock until subsequent years or quite simply may not have the financial wherewithal to fund stock increases. Greater flexibility could be introduced so that a young farmer could elect to claim the relief in any 4 of the first 6 years of the farming trade. This would provide greater flexibility to the farmer in deciding commercially whether to invest in stock or capital improvements to the farm without losing the benefit of this relief.

Additionally, where a farmer begins farming just after the age limit to be a young trained farmer, enhanced stock relief is not available. For example, a 36-year-old qualified farmer who just begins to farm is not entitled to claim any enhanced relief. By contrast a 36-year-old qualified farmer who has been farming for 2 years is entitled to claim the enhanced relief for two further years. We believe that transitional measures should be introduced to allow farmers who narrowly miss being eligible for the relief to claim the enhanced stock relief for a limited time period.

Furthermore, this relief is due to expire on 31 December 2018. It is an imperative that this measure is retained, particularly as young farmers seeking to expand are likely to invest heavily in stock in the next few years.

Purchase of Dairy Co-Operative Shares following the Abolition of Milk Quotas

While farmers are no longer required to purchase milk quotas following their abolition in 2015, they still face compulsory capital costs in order to increase their production of milk. Prior to the abolition of milk quotas, dairy farmers were not required to invest in the dairy co-operative before they could supply milk to that co-operative.

Following the abolition of milk quotas, some dairy co-operatives compelled farmers to make additional financial contributions as a pre-condition of supplying increased levels of milk. Dairy farmers must now purchase shares in the co-operative before the co-operative will agree to collect their milk. As the acquisition of such shares is directly linked to milk production, they should be considered agricultural property for the purposes of CAT and

CGT reliefs but the application of the reliefs to these shares is not certain and therefore, clarity would be welcome.

Brexit Tax Considerations

Brexit has the potential to cause significant disruption to the agriculture sector. The effect of possible tariffs is likely to have a significant impact. Depending on the final agreement reached with the UK it may also bring, not only customs and excise but also, VAT implications and knock-on effects for certain Agri-tax measures.

Even though the final Brexit package has yet to be brokered, with still many unknowns, there are some tax issues that we can reflect on now, such as property issues. For example, land in Northern Ireland will no longer be land in the EU and this could create CAT issues when evaluating agricultural relief.

Irrespective of the outcome of the EU/UK negotiations, we could begin the work to identify and consider the tax policy of such issues. This could be achieved by establishing a Working Group between practitioners and the Revenue Commissioners to discuss and explore such matters. A similar forum was set up at the time of the introduction of the new Companies Act in 2014 to identify how Irish tax law needed to be aligned and updated for the provisions in the Companies Act. We recommend that such a forum is established in the coming months, in advance of the UK's exit from the EU in March 2019.

Conclusion

For the reasons outlined above, we recommend that the key Agri-tax reliefs and measures should be retained and enhanced to help drive the government's ambitious policies for the sector over next few years. Undoubtedly, increased investment in farming will be required to realise the growth targets set and address the challenges of Brexit and climate change and it is essential that the tax regime does not act as a barrier to the expansion of the sector.

The Institute would be happy to engage further in this consultation through stakeholder meetings or direct discussions. Please contact Anne Gunnell at agunnell@taxinstitute.ie or (01) 6631750 if you require any further information.

Yours truly

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President