Teagasc
Agriculture and Food Development Authority

AN tOLLAMH GERRY BOYLE M.R.I.A
STIÚRTHÓIR
An Cheannoifig
Páirc na Darach, Ceatharlach, Co. Cheatharlach, Éire
PROFESSOR GERRY BOYLE M.R.I.A
DIRECTOR
Head Office
Oak Park, Carlow, Co. Carlow, Ireland
Tel: 059 918-3401 Fax: 059 918-2098
Tel. Int: 00353+59 918 3401

Agri-Taxation Review
Fiscal Division
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2

Emailed to: agritaxation@finance.gov.ie

25 March 2014

Dear Sir/Madam

We are writing to you to express our views on the agri-taxation consultation as part of the current ongoing review of taxation aspects in the agricultural sector.

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

1.1 Stock Relief

This relief allows tax relief for increases in stock values. It is a critical relief in recognising the uniqueness of farming activity and is an effective substitute for capital allowances available in other industry sectors.

Increase in agricultural output is a key objective of Harvest 2020 and stock relief is an effective means of managing the potential increases in total values of core business livestock held without adversely affecting cash-flow. Building up stock levels on farms has a significant detrimental effect on cash flow and reducing the adverse effects of potential higher taxation on this cash-flow is required. Stock relief goes some way towards achieving this.

1.1.2 Income tax exemption for farm leases

The income tax exemption for farm leases is a very effective measure to encourage non-active farmers to rent their lands and hence, to allow for farm consolidation and expansion. As the amount of the lease income that is tax-free is dependent on the length of the leases, it encourages letting for longer periods so that the tenants can focus on long-term production strategies for the leased land and generally ensures greater productivity from this land.

1.1.3 Age exemption provisions

Elderly farmers continue to benefit from the income tax age exemptions in the same manner as other individuals. We recommend no restrictions to this exemption and the retention of current limits.

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1.1.4 Farm Income Averaging

The election to allow for farm profits to be computed based on average profits over 3 years is a measure which is effective and required given the cyclical nature of farm activity. In our view, support from the taxation system to address the volatility of farm activity is key and we have outlined some of the international measures in 2.1 below which are relevant to Ireland.

1.1.5 Retirement Relief

Although not specific to farming, Retirement Relief is a capital gains tax ("CGT") relief which allows for the transfer of farms by farmers who are aged over 55 years of age. In our view, this is a critical relief so as to avoid significant tax costs on farm succession where there is no underlying cash to pay such liabilities. Amendments to enhance this relief are outlined below.

1.1.6 Agricultural property Relief

This relief allows for a 90% reduction in the gift/inheritance tax payable on the receipt of farm lands provided a number of conditions are met. This relief is essential in order to achieve the farm consolidation objectives of Harvest 2020.

1.1.7 VAT – Flat rate farmer and farm buildings

Specific repayment provisions apply to VAT incurred on expenditure on the construction/improvement of farm buildings, fencing, drainage and land reclamation. The objective of the provisions is to put farmers on a par with other trades in terms of VAT recovery.

Similarly, if a farmer does not opt to register for VAT, the farmer is entitled to a flat-rate addition of 5% on sales to VAT registered persons to compensate for loss of VAT input credits on purchases.

In our view, both are effective and required measures.

1.1.8 Stamp Duty: Young Farmer's relief and Consanguinity Relief

In our view, the following reliefs are important reliefs to facilitate the introduction of new farmers and also the succession of farms to the next generation:

- The Young Farmers Relief provides for an exemption from stamp duty on the transfer of farms provided the individual is under 35 years of age and has met the various education requirements.

- Stamp duty payable is reduced by 50% on transfers of non-residential property between certain related persons. The relief is due to be abolished from 1 January 2015.

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1.1.9 Capital allowances for farm buildings

Capital allowances for farm buildings are available over a 7 year time-frame. This regime acknowledges that expansion is required and encouraged in order to meet the objectives of Harvest 2020. This relief should be retained in expectation of the increased level of investment as part of the future expansion plans of many farms.

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

1.2.1 Tax exemption for start-ups

The current income tax relief for start-ups is ineffective for farming activity. The corporation tax exemption only applies at the maximum if there are 8 employees involved and this is not realistic for farms.

1.2.2 USC provisions

Introduction of consistency between income tax and USC is required so that a USC exemption also applies where leasing income is exempt from income tax.

1.2.3 Farm exchanges

In **2013 (Section 604B TCA 1997) Relief for Farm Restructuring** provided relieving provisions which are specific to farmers who are consolidating their holdings. The provisions allow for farm land to be exchanged for other farm land without a charge to CGT arising. The objective is to facilitate the more orderly restructuring of farm land. The provision was required given that CGT tax roll-over relief no longer applies. In our view, this relief is crucially required and its uptake could be greatly improved if a number of modifications were made to the operation of the relief.
The relief, in its current form, does not allow for a farmer with a fragmented holding to **sell his entire holding and invest in one enlarged consolidated farm** which is less fragmented. Hence, a technical amendment is required in order for these provisions to operate effectively and to allow for farm consolidation in the above case.

1.3 How could the tax system better influence activity in any of the key policy areas of:

1.3.1 Encouraging and attracting young farmers and new entrants to farming

- **Stock relief** is due to expire on 31 December 2015 and we recommend its continuation.

- Maintaining the 100% **stock relief for young farmers** but increasing the 4 year time-frame to 6 years.

- Currently, the use of **enhanced stock relief** means that capital allowances and existing losses are lost if stock relief is claimed. Given that losses and capital expenditure are required in order to increase farm trading size, it is critical that these restrictions are removed so that the tax position of the farmer is based on the actual expenditure over a period of time with the additional benefit of stock relief.

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- The **CGT Relief for Farm Restructuring** only applies to a person who spends at least 50% of that person's normal working time farming. We propose that the definition is amended to an Active Farmer with the same definition as for the Single Farm Payment and under other EU Schemes to ensure consistency. Consistency of definitions is key for tax, grant-aid and other purposes. The exception is the farmer definition for Agricultural Relief which we propose is retained in its current form in order to encourage new entrants.

- We recommend that the requirement for 8 employees to obtain the maximum corporation tax relief is abolished for start-ups where an active farmer is involved. The **Start-up Exemption** only applies where a new trade is involved and a trade is not taken over from another person. In order to facilitate the transition of family farms we recommend that it is specified that this requirement is met where there is a change in ownership of the farm e.g. transfer from one generation to the next. This is recognition of the specific circumstances of farm ownership.

  We also recommend that the corporation tax exemption is extended to farm trades carried on as sole traders/partnerships given that farming is primarily a non-incorporated activity.

- **Seed Capital Relief** provides tax relief for investment in a new corporate business against employment income earned by that individual in the 6 years prior to the investment. We propose the **extension of the relief to include investment in farming trades** notwithstanding that seed capital is currently just available for corporate investment. This amendment is required given that farming trades are primarily in non-incorporated forms. The objective is to facilitate farm expansion once an individual, who was previously an employee, wishes to become a farm owner or a partner in a farm partnership and invest in expansion. Seed capital relief currently does not extend to successive business ventures and in our view, the legislation should be amended to allow for the offset of investment in a new business against income earned in a previous business venture. In this case, there is also merit in recognising that the investment is often in an asset rather than cash form which could be the case where a young farmer has built up equity in the form of livestock/ machinery while farming in collaboration with another farmer or on leased land and subsequently wishes to set up a new business.

1.3.2 Land mobility – transfers via the market, whether by sale or long-term leasing.

- In order to retain the benefits of **Agricultural Relief from Capital Acquisitions Tax**, there is a requirement to retain the lands for 6 years (10 years if development potential).
  In order to free up agricultural land after a death of the farmer and transfer to those who would use the lands for farming purposes, we propose that this holding period is reduced to 3 years where an inheritance is involved. We are not proposing any changes to the holding periods for Retirement Relief given that CGT does not arise on death.

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- In relation to **Retirement Relief**, from 1 January 2014, there is the limit of €500,000 which applies to disposals to third parties where the transferor is aged over 66 years of age. The

- €750,000 only remains for those under 66 years of age. In our view, the €750,000 level is crucially required in order to retain land mobility on life-time transfers and all the more important given the increased capital gains tax rate of 33%. If we assume land values at €10,000 per acre, then the reduced limit only allows for third party life-time mobility in relation to 50 acres compared with 75 acres for the existing limit.
  Therefore, we propose that the €750,000 limit is retained for farmland regardless of whether the age limit of 66 is exceeded or not. In addition and in relation to retirement relief, it is critical that the €3 million limit which applies to disposals to the next generation once an individual reaches 66 years of age is not reduced further.

- Short term rental arrangements, while providing useful avenues for land access for farmers in some circumstances do have negative consequences in terms of lack of security for the lessee and these arrangements often result in declining land productivity over time. We propose the enforcement of the registration **(stamping) of all agricultural land rental agreements**. To encourage compliance there should be a requirement introduced that in order for a lessee to claim the rental expense as a tax deduction, (a trading expense against gross income) the land rental agreement(s) must be stamped. Revenue Form 11 should highlight the need for a stamped agreement. As land rental can often be transacted through word of mouth, landowners may now want to engage a legal representative as all land conacre agreements must be in writing to be stamped. This may unduly increase costs due to the "Conveyancing Conflict of Interest". For the purpose of ensuring compliance with the new "Conveyancing Conflict of Interest" regulations, short term rental (conacre) should be considered exempt as a 'conveyancing transaction'.

1.3.3 Succession – earlier lifetime transfers within families (and non-family transfers also where no apparent successor is available)

- **Extension of the income tax exemption** (but at a lower level to the current exemption) for lessors aged less than 40 years. The objective is to encourage the release of land by those who have inherited lands but do not wish to farm the lands.

- It is important that there is **no increase in the rates of gift tax, inheritance tax or CGT**. We also recommend that existing thresholds for life-time gifts/inheritances are retained as further reductions would affect family successions. Although not specific to the food and agricultural sector, there is merit **in revising the base year for the purposes of aggregation of previous gifts/ inheritances** from 1991 to 2010 so as to ensure that thresholds are not fully eroded by artificially high value transfers in the intervening years.

- The broadening of **Retirement Relief** to include nephews and nieces in the same manner as currently available for a child. Currently, there is a requirement for nephews/nieces to work on the farm for the prior 5 years. We recommend the broadening as recognition that many

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- farmers do not have children. Also, in relation to Retirement Relief, the definition of chargeable business asset in Section 598 TCA 1997 is extended to include a trade carried on by a farm partnership of which the individual is a member. The amendments to Retirement Relief in Finance Act (No.2) 2013 were welcome.

- Extend the **tax exemption for leasing income** to include lettings to lineal descendants but only where the rent does not exceed market value, the land is used by a farm partnership (with the parent/child as partners for at least a 5 year period), the lineal descendant in question carries on the farming and after the lease term, in order to avoid a clawback, the lands transfer eventually transfer to the same lineal descendant. We propose that this income tax exemption would only be available for a maximum of 7 years.

- In our view, the **leasing income exemption** should also be available where the tenant is a company (providing not connected with the lessor – connected party rules as per s.10(3) TCA 1997), whose controlling director had a prior lease of the same lands with the landlord so that companies (who are more readily associated with large scale farm operations) are not disadvantaged when a retiring farmer is considering leasing.

- Extension of **Consanguinity stamp duty relief** beyond 2014. At a minimum, we suggest that the amendment applies to the succession of family farms.

- Section 792 TCA 1997 provides for an income tax deduction where an individual divests himself/herself of part of his/her income by transferring to another person under a **Deed of Covenant**. In summary, the Deed of Covenant must be a legal commitment to transfer funds for at least 6 years in order for the relief to be available.

  The provisions apply if the recipient is:
  - aged at least 65 years of age OR
  - Permanently incapacitated by mental or physical infirmity

  The maximum relief available is limited to 5% of the donor's total income in the first case with no such restriction in the second case.

  We propose the extension of this provision to apply without the 5% restriction for recipients aged at least 65 where the annuity is payable by the transferee as part of an agreement to transfer farm lands to the next generation. The provisions would only apply to inter-generational transfers given that third party transfers would continue to result in upfront payments.

  In our view, the introduction of this proposal is critical to ensure the timely transition of family farms. Currently, transfers are deferred with a loss of economic value due to the uncertainty relating to the financial position of the transferor. Our objective is to manage this uncertainty by encouraging the payment of a guaranteed sum to the transferor.
  We also propose that a specific exclusion is made so that no withholding tax applies to the payments, possibly in the form of amendments to Chapter 1, Part 8, TCA 1997.

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

- Increasing the **stock relief for farm partnerships** from 50% to 100%, regardless of whether a Young Farmer is involved, in order to support a collaborative partnership approach to farming and maintaining the 100% rate for the duration of the partnership. This is also required to balance the €7,500 restriction.

- **Farm partnerships** should continue to be seen as the optimal operating arrangement for farms. In accordance with the 2004 partnership model/tax guidance notes for Milk Production Partnerships and as you are aware, the lands/buildings are retained outside the partnership, livestock/ machinery are transferred to the partnership and the trading activity is carried out in the partnership. The partners could be either family members, where the percentage ownership is changed over time, or nearby unrelated farmers. If family members are involved, the parents have the security of retaining the lands in personal ownership.

  Where the land ownership percentage is changed over time due to gifts between family members and the land continues to be used by the partnership, we propose that there is the option of the **Capital Acquisitions Tax** and **stamp duty** arising on the transfer to be based on either the lesser of the value of the land at the time of the transfer or the value of the land at the earlier date of the creation of the partnership.

  In our view, this is an incentive for families to work within family partnerships, as the recognised farm operating model, at an early stage. Once the partnership is established, the land value subject to gift tax and stamp duty can be frozen. Hence, a tax cost does not arise if the transfer of the land is deferred in order to retain security and certainty for the parents. This measure would generate confidence for parents to engage with their next generation in formulating a strategy for farm operation and land transfer. The key point is that there is an incentive to form the trading partnership at an early stage and introduce the next generation to ownership of the farm operation.

- See 1.3.1 for proposals to **extend the income tax exemption** for farm partnerships if certain conditions are met.

1.3.5 Environmental sustainability

The 25% **R&D credit for R&D expenditure** can be used to reduce the level of corporation tax payable by companies. We propose that this R&D tax credit is specifically extended to costs incurred by farmers in rendering their business operations in conformity with environmental objectives particularly in the area of energy saving technologies, water recycling / purification and alternative energy production technologies for energy intensive farm

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businesses.
Teagasc is involved in the development and promotion of Carbon Navigator assessment tools to assess the 'carbon footprint' of individual farms. Promotion of farm level technologies to encourage carbon awareness and monitoring at farm level could be promoted using this credit.

1.3.6 Smart Farming – encouraging innovation, improving skill levels and maximising the adoption of best practice

- We propose that **accelerated capital allowances** are available for expenditure on buildings (which have obtained a Department of Agriculture Grant and comply with Department specifications) where the expenditure is incurred solely to facilitate increased production and scale. We are conscious that EU approval is required for this measure but in our view, it is only by introducing accelerated capital allowances that significant expenditure on such buildings will be encouraged. We propose the same regime that applied to expenditure on buildings to control farm pollution as was in place until 31 December 2010 is extended to farm buildings required to increase milk production.

- Introduction of a **tax credit** to a for a period of five years where a qualifying farmer completes a certified business planning course complete with 5-year business plan for his farming business or completes a course which focuses on either specialist farm production only or farm innovation. As for environmental sustainability (see 1.3.5 above), the credit would be given under current provisions for R&D tax credits (rate of 25%) and used to reduce income tax or corporation tax payable by farmers.

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

Income volatility is an ever present issue at farm level and managing cash flow to ensure that all farm operating and debt repayment commitments in years with low product price/ high input price/extreme weather event years can be extremely difficult. Cash flow pressures resulting from the need to meet tax obligations and juggle the other cash flows, particularly in years where there is downside income volatility can put farm businesses and their owners under significant strain. While the income averaging measures already in place do assist many farmers in smoothing out their taxable incomes, the increased volatility in many enterprises, particularly dairying, has reduced the effectiveness of this measure and has led many farmers to examine incorporation as an option.

As an alternative to the company option we would propose a new **Income Equalisation Scheme** embracing the principles that are already in operation in similar schemes in other countries (see section 2.1). The main principles of the scheme would be that a farmer can remove taxable income from the charge to tax in high trading income years by "locking it away" in a deposit/bond and that this could then be subsequently "cashed in" in low trading

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income years to meet farm and personal drawing requirements with the relevant tax paid in the year of drawdown.

1.5 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 our view, there is an awareness among farmers and related professionals of taxation matters. However, in our view, the tax advice is often provided by solicitors and accountants who are not tax specialists, particularly in the farm area. Therefore, we agree that the raising of awareness is important and could be achieved through presentations/conferences by specialist tax advisers targeted at professionals, who front face with farmers.

2. Provide details of any alternative approaches or options you feel might be beneficial in dealing with the issues being addressed.

2.1 The International Experience

There is merit in reviewing international regimes adopted over the years. In particular, a number of countries such as Australia (Farm Management Deposits), New Zealand (Income Equalisation Deposit Fund), Canada (Flexible Inventory Program where a tax deduction for inventory can be increased/decreased depending on whether low income years or high income years are involved and also an Income Stabilisation Account) and France (tax relief for a savings deduction up to a limit, which is taxed on withdrawal). In our view, similar proposals are relevant to Ireland.

Also, the UK has a 100% exemption for the inheritance of agricultural land and no gift tax if the transferor gifts more than 7 years before death. As a result of the UK March 2014 Budget, the 100% capital allowance regime for plant & machinery in the year of expenditure (Annual Investment Allowance) applies for up to £500,000 of expenditure and 100% year 1 allowances also apply for plant & machinery costs incurred where the business is located in Enterprise Zones. This supports that accelerated allowances are still effective policy instruments.

2.2 Tax Accounts

We would welcome the introduction of standardised accounts preparation packages which would allow the preparation of farm tax returns while simultaneously producing simple management accounting measures to allow a farm to assess its financial performance. Teagasc produce management accounts using their Teagasc eProfit Monitor system and it would be useful if tax accounts preparation systems could also provide the input data for such a system. The objective is to ensure an industry standard which promotes farm business financial performance analysis.

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3. Provide details of relevant issues not covered in this paper

None.

4. If possible, provide some analysis of the Exchequer cost/yield of your preferred option.

Once the Department has considered the proposals in this paper, we welcome the opportunity to discuss the likely Exchequer cost/yield at that point.

5. Comment generally on the direction you would like to see tax policy in this area develop.

The 2005 OECD report on agriculture outlines some useful principles on related tax policy:

- The role of tax policy in agriculture is not to enhance the income of the taxpayer but tax policy can be used as a farm policy instrument to encourage change.
- Income smoothing measures may be a less costly measure for dealing with volatility.
- Permanently low income levels should be dealt with through the social welfare system.
- Structural adjustments to farm ownership could be dealt with by the removal of inheritance tax.

With the above principles in mind, we would like to see Tax Policy aligned with the objectives of Harvest 2020 by the introduction of the measures outlined in this paper. However, it is important that tax remains an incentive only to encourage alignment of farm industry practice to Harvest 2020. It is also important that there is awareness among the industry of the commercial issues with a real connection between the tax and commercial aspects when making decisions.

We would welcome the opportunity to meet with you to discuss the above proposals further or to participate further in this consultation through stakeholder meetings or direct discussions. In the interim, if you have any queries please contact my colleague, Kevin Connolly at kevin.connolly@teagasc.ie / (047) 81188) or myself.

Yours sincerely,

G Boyle

Prof Gerry Boyle
Director