Irish Co-operative Organisation Society Ltd

Pre-Budget Submission 2020

September 2019

Executive Summary

The Irish Co-operative Organisation Society (ICOS) is the umbrella for the co-operative movement in Ireland and celebrates its 125th anniversary in 2019.

The agri-food sector is facing enormous challenges due to low income across the main production sectors, volatile incomes in the dairy sector, the prospect of a damaging No-Deal Brexit and the need to transition towards a low carbon future.

The co-operative model remains central to the success of the agri-food sector, as it continues to grow in scale and complexity.

Farmer owned and controlled co-operatives do require the support of Government, if they are to continue to provide the structure and organisation, which the success of the sector is built upon.

In recent years, ICOS has been extremely disappointed by the failure by the Government to introduce an income stabilisation tool. The introduction of this measure is long overdue, especially as the sector faces into the headwind of a No-Deal Brexit.

Furthermore, we call on the Government to examine the tax treatment of co-operative shares as a priority.

The ICOS Pre-Budget Submission calls for a range of policy measures including:

- The introduction of an income stabilisation tool in Budget 2020 to enable primary producers to grow and manage their business, while having a more reliable and stable cashflow to aid them in decision making, resulting in a wider positive economic impact on the rural economy.

- The inclusion of qualifying co-operative shares to be classified as qualifying assets for the purpose of calculating CAT agricultural relief and CGT retirement relief. In addition, the qualifying shares to be eligible for appropriate capital allowances.

- A range of practical measures to assist the agri-food sector during a No-Deal Brexit including a dedicated Brexit Adjustment Fund, additional supports for market diversification, export finance and appropriate levels of investment into Ireland's customs infrastructure to ensure minimal disruption and delay.

- The Introduction of incentives for community renewable energy projects such as tariffs and price supports for those community projects generating renewable energy, utilising the electricity levy to strategically promote renewable energy consumption and a "Green Tax Credit" for renewable electricity generation. We also call on the Government to ensure Ireland realises its potential as a world leader in biomass production through the provision of a range of supports and incentives.

1. ICOS Income Stabilisation Proposal

ICOS strongly calls on the Government to introduce a new strategic risk management tool for primary producers. The measure proposed by ICOS, would be available to enable a farmer to use periods when market returns are higher to create a modest "rainy-day" fund, to support them during periods when market returns are weaker.

The measure will permit a farmer to voluntarily defer up to 5% of their gross receipts in any one year. The deferred funds can be drawn down at any time within 5 years and subject to income tax at the time of draw down, but in any case, must be drawn down within 5 years.

It is envisaged that the tool could operate in conjunction with the income averaging tool currently available to the sector. This measure is urgently needed as family farm income fluctuates from year to year due to circumstances outside the control of the farmer. External forces such as weather, geopolitical matters, currency, feed and oil prices, disease and macroeconomic factors can conspire to cause income volatility.

For example, in 2018, farm income fell significantly across all the main farming sectors due to a series of extreme weather events with dairy farm income falling by 31%[1]. A No-Deal Brexit outcome will increase the likelihood of income volatility in the foreseeable future.

The ICOS income stabilisation tool is a strategic measure aimed at supporting the economic sustainability of the rural economy and the family farm model. The measure proposed by ICOS is a prudent, counter cyclical option designed specifically to help the farming sector manage the worse effects of volatility.

There is established precedent for key elements of the ICOS proposal contained in the Milk Quota Regulations, which permitted co-ops to retain a portion of the farmers milk cheque until the final milk quota liability was established. Furthermore, the European Commission has endorsed the concept in its Communication on the Future of the Common Agricultural Policy and has encouraged Member States to examine the concept[2].

In 2018, a joint economic study by Teagasc, CIT and UCC, stated that the proposed measure has the potential to significantly reduce the volatility of after-tax household disposable income and support farm investment, without greatly affecting the overall tax contribution[3].

ICOS Income Stabilisation Measure – Proposed Broad Concepts

ICOS proposes that the income stabilisation measure would operate based on the following broad concepts:

1. A milk, grain or livestock supplier can enter into a voluntary agreement with their co-operative (or approved purchaser of primary agricultural produce) to defer up to 5% of their gross annual income in order to stabilise their annual farm income.
2. The deferred income shall not exceed 5% of annual gross receipts.
3. The deferred income can be drawn down at any time, with the provision of a reasonable notice period, and subject to income tax at the time of draw down.

[1] Teagasc National Farm Survey – 2018 Results
[2] European Commission, Communication on the Future of Farming, November 2017 (link): https://ec.europa.eu/agriculture/sites/agriculture/files/future-of-cap/future_of_food_and_farming_communication_en.pdf
[3] Teagasc, CIT, UCC, An evaluation of suitable tools to manage price/income volatility at farm level in Ireland, August 2018

4. The maximum period that the deferred income can be retained in the scheme is 5 years from the date the deferred income is introduced to the scheme (the scheme will operate on a 5-year rolling, first in-first out basis).
5. The scheme is flexible and can operate with or without income averaging.
6. The accumulated or combined funds will be retained in a bank account kept for the specific purpose of the scheme.
7. As part of the annual audit, the auditor would verify the bank balance and ensure it reconciles to the deferred creditor account.
8. As a Revenue approved scheme, the funds must be protected and secure.
9. In a scenario where a farmer is not trading with a co-operative or where co-operatives are not active in that production sector, so as not to disadvantage farmers, it is appropriate that an alternative model should be provided through financial institutions.
10. EU state aid rules would apply with respect to the interest value of any deferred taxation associated with income deferral. ICOS, having examined the matter, is quite satisfied that the sums involved are extremely modest and should comfortably come under the De-Minimis threshold.

Evaluation of Income Stabilisation in Budget 2019

In October 2018, the Department of Finance published a Progress Implementation Update of the Agri-taxation Review 2014.

As part of this report, the Economics Division of the Department of Finance carried out an economic analysis of the income stabilisation tool proposed by ICOS. ICOS welcomes the evaluation, which is an extremely important analysis as it outlines the potential impact of the proposal on the exchequer. We have a number of comments and observations on the evaluation.

- The evaluation states in the context of estimating the cost of the proposal to the exchequer that **"putting a cost for the next year is very difficult for a scheme such as this as forecasting the price of milk, as well as volumes and dairy farm income is a near impossible task".**[4] This is correct and is equally true for the primary producer who from year to year is unable to plan and grow his business based on a stable cashflow situation. The objective of the ICOS proposal is to address this **"near impossible task"** by providing a degree of stability in relation to income for the farmer and the exchequer.

- The evaluation identifies that **"a farmer could incur higher cumulative tax liabilities than a PAYE employee with similar average earnings over the medium to long term because his/her income is less stable"[5].** This is clearly unfair and the ICOS proposal will help address this inequality. Additionally, a PAYE employee is able to avail of the maximum credit of €1,650 whereas the Earned Income Credit available to farmers currently is at €1,350. ICOS would propose that the Earned Income Credit be aligned with the PAYE credit.

- The evaluation when discussing the step out to income averaging acknowledges the **"stress"[6]** severe income volatility has on family farms. The ICOS proposal will help to reduce the stress of volatile income on farmers and their families during periods of low income.

[4] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 39.

[5] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 31.

[6] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 32

- The evaluation resulted in greater advantages for the farmer when income averaging and an income stabilisation tool was combined and further states that **"this combined regime therefore also has the highest exchequer cost to the state in terms of revenue foregone"[7].** ICOS strongly maintains that the cost to the exchequer is marginal and, in some years, the cost will be negative. Despite this, it is ultimately a policy decision by the Department of Finance as to whether the schemes should operate independently or in conjunction with each other.

- The evaluation states that "**the aim of the scheme is to produce a more optimal tax scenario for the farmer where they can utilise more of their credits and reliefs each year"[8].** ICOS disagrees with this statement. The aim of the scheme is to allow a farmer to grow and manage their business, while having a more reliable and stable cashflow to aid them in decision making. This will have a wider positive economic impact on the rural economy as the farmer will be in a better position to plan the costs of his business such as labour, feed, capital expenditure etc.

- It is noted in the evaluation that **"dairy farmers are now choosing to incorporate, mainly for tax reasons"[9]**. ICOS agrees that the introduction of the income stabilisation tool would act as an incentive for farmers to remain as a sole trader resulting in an overall tax saving to the exchequer, which is not captured in the evaluation costings.

- The evaluation identifies that "**in years of higher income, there is exchequer revenue foregone and in years of lower income there are additional exchequer revenues than otherwise would have been the case"[10].** ICOS agrees with this statement. However, over time the revenue will level out making it easer for the exchequer when preparing the Budget.

- ICOS acknowledges that the evaluation assumed 100 percent up take among dairy farmers in year one of the scheme's introduction. However, it is important to take into consideration that this is extremely unlikely based on the take up of new taxation measures such as income averaging in the past.

SUMMARY:

ICOS calls for the introduction of an income stabilisation tool in Budget 2020 to enable primary producers to grow and manage their business, while having a more reliable and stable cashflow to aid them in decision making, resulting in a wider positive economic impact on the rural economy. Additionally, we propose that the Earned Income Credit be aligned with the PAYE credit.

[7] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 32

[8] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 34

[9] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 35

[10] Budget 2019, Report on Tax Expenditures incorporating outcomes of certain Tax Expenditure & Tax Related Reviews completed since October 2017, page 3

2. SHARE STANDARD – TRANSFER OF AGRICULTURAL PROPERTY

ICOS calls on the Minister for Finance to amend the legislation to classify co-operative shares as qualifying assets for the purpose of calculating the CAT agricultural relief (“agricultural property”) and CGT Retirement Relief (“qualifying assets”) on the transfer of the agricultural property.

In addition, ICOS proposes that co-operative share be made eligible for appropriate capital allowances similar to that for “Milk Quota” in the past.

Since the abolition of the Milk Quota, many co-operatives have made it a condition of their Milk Supply Agreement (contract) that the milk supplier must possess a minimum number of shares per litre of milk supplied, typically 2 to 4 cent in shares per litre produced, or 10,000 to 20,000 shares for a typical 500,000 litre supplier. This scenario is analogous to the Milk Quota regime which existed until 2015, whereby a milk supplier had to hold a Milk Quota certificate, as a licence to produce milk.

The Milk Quota was treated as agricultural property and transferred at the same time as the land, farm buildings, crops, farm machinery, livestock and all other assets necessary to produce and sell milk, when claiming agricultural relief. Retirement relief is available for those who are involved in a “milk production partnership” (in certain circumstances), we would request that retirement relief is available to members who dispose of the qualifying shares.

The co-operative share has become in many instances a requisite asset to sell milk, comparable to the previous obligation to hold a Milk Quota certificate. Accordingly, it is appropriate what where the holding of a certain amount of Co-operative shares is a condition of a Milk Supply Agreement (MSA), or terms of supply, or a requirement of the co-operative’s Rulebook, that number of shares should be classified as qualifying assets for the purpose of agricultural and retirement relief.

In addition, the capital expenditure incurred on the purchase of the qualifying shares should be eligible for capital allowances. Milk Quota qualified for capital allowances, the cost was written off over a 7-year period, at a rate of 15% per annum over 6 years and 10 per cent in year 7. ICOS would propose similar treatment for the qualifying shares.

Under the Milk Quota regulations (SI. No. 94/2000 – European Communities (Milk Quota) Regulations, 2000), "a milk quota shall be deemed to be attached to the land used for milk production". In the case where land was transferred the quota was transferred at the same time as the land.

ICOS would propose that in assessing the relief the qualifying shares be treated similarly to the conditions placed on Milk Quota under the pre-existing regulations.

SUMMARY:

ICOS calls for the inclusion of qualifying co-operative shares to be classified as qualifying assets for the purpose of calculating CAT agricultural relief and CGT retirement relief. In addition, the qualifying shares to be eligible for appropriate capital allowances.

3. Brexit Preparedness and No-Deal Contingency Actions

With a No-Deal Brexit more likely than ever before and with the resulting uncertainty continuing, it is vital that Budget 2020 places a key focus on supporting the businesses and sectors most exposed through this time of insecurity and economic disruption.

Irish co-operatives sitting as they are at the heart of the agri-food industry and rural economy, are very much exposed to the risks of Brexit due to strong trade links with the UK and business structures which operate on both sides of the border.

ICOS welcomes the action which has already been taken by the Government over the past year, including the various loan and grant schemes, as well as the advisory services and trainings provided by Bord Bia and Enterprise Ireland to assist businesses in their Brexit preparations. As a next step, we call for Budget 2020 to include the following:

- **A Brexit Adjustment Fund:** No matter the outcome of the Brexit negotiations, businesses will need to re-align their business models with the new trading reality. However, this will become extremely challenging in a No-Deal Brexit scenario. Therefore, a dedicated Brexit Adjustment Fund must be established. This fund must prioritise businesses most effected by the UK's exit and should focus on capital investment for implementing supply chain and logistical adjustments, including for example expanding storage and distribution capacity, to ensure the continuation of cross-border trade with the UK. In particular, adjustment funding will be needed to maintain all-Island supply chains in the event of a No-Deal Brexit in order to ensure the survival and stabilisation of rural economies in border areas.

- **Market Diversification:** We welcome the efforts made by the Irish Government to better promote international trade, and the support which has been provided to Bord Bia to help promote Irish agri-food exports on new markets. This work should be further built on through the direct funding of marketing and promotional campaigns for exporting businesses. Assessing and establishing a brand or a product on a new market takes time and capital before it can begin to generate value. Financing marketing campaigns to bridge this gap accelerates this process. In addition, funding should be directed not at once-off trade events, but on campaigns which involve "boots-on-the-ground" and long-running engagement, which has a proven higher pay-off in terms of value creation.

- **Export Finance:** A national export credit insurance scheme should be established to assist businesses in expanding to new global markets. Accessing new markets can put a strain on cashflow, due to upfront logistical, marketing and regulatory costs. Government backed export finance, in the form of loans, guarantees and insurance policies would ensure businesses have affordable and secure finance to manage cashflow and therefore reduce risks.

- **Investment in Infrastructure and Capacity:** Ireland's customs infrastructure requires further investment in order to be able to be able to deliver in the event of a No-Deal Brexit. Budget 2020 must account for investment in personal and technical capacity at our ports and airports in order to ensure as smooth as possible a transition to new the EU-UK trading regime with minimal disruption and delay.

SUMMARY:

ICOS calls on Budget 2020 to introduce a range of practical measures to assist the agri-food sector during a No-Deal Brexit including a dedicated Brexit Adjustment Fund, additional supports for market diversification, export finance and appropriate levels of investment into Ireland's customs infrastructure to ensure minimal disruption and delay.

4. Renewable Energy

ICOS, as the umbrella body representing rural co-operative businesses, strongly believes that it is time that Government policy is re-evaluated to lend greater support to the adoption of renewable, clean, green heat and electricity technology by co-operative businesses in Ireland as a cost effective and sustainable model for the development of local renewable energy production and subsequently, the rejuvenation and maintenance of employment in rural Ireland.

It is clearly reported that the supply of energy internationally needs to be addressed. Limited remaining oil and gas resources combined with the security threat in not being able to self-supply energy means that as a country, Ireland needs to develop a sustainable plan in the creation of energy to supply homes and businesses across the country.

Community Energy

The co-operative model in Ireland has seen great commercial successes in agriculture and the model has been used extremely successfully internationally with the establishment of renewable energy co-operatives (both energy production and energy supply) in communities in countries like Germany, the Netherlands, Belgium, Scotland and Spain.

National energy production and supply developments in recent times in Ireland have seen varying degrees of support from local communities. The most recent proposals by Eirgrid to establish their Grid Link project which entailed building large pylons in the south east saw large scale community discord with the proposals. Proposed large scale wind farms in the midlands were also met with protests from the rural communities. As a result of these protests, the Eirgrid project has been returned for further community consultation and the midlands wind project has been suspended.

The above examples clearly illustrate that community ownership and approval of large-scale energy production projects is necessary for them to succeed. It is in projects like these that it becomes clear that community ownership of and engagement with energy projects is essential at the planning stage. Communities need to be reassured that their area will not be adversely affected by proposed developments and they should be able to benefit from any development that occurs in their locality.

ICOS maintains that new and existing co-operatives can play a strong, leading role in assisting Ireland reach its renewable energy targets. They ensure that profits of any enterprise remain in the locality and will educate citizens as to the importance of a sustainable, local energy supply.

With this in mind, we would propose the following schemes and incentives to be included in the upcoming budget to increase usage of renewable heat and electricity supplies:

- Introduce a tariff system for community based renewable projects.
- Prioritise community based renewable projects for planning and grid access.
- Restructure planning requirements for community renewable projects to bring these requirements into line with other EU Member States.
- An additional allocation to the DAFM budget, to introduce a framework to promote capital investment in renewable energy generation at farm level.
- Deliver price supports for farm-scale and community-based renewables and to ensure the delivery of the Teagasc MACC climate roadmap.

The potential for the creation of employment by developing the renewable energy sector is substantial. Further to this, if the co-operative model is utilised, profits from any enterprise stay within a community and subsequently support unrelated businesses.

GREEN TAX CREDIT

ICOS supports the proposal by farm organisations to introduce an immediate measure needed to kick start our efforts to meet our renewable energy targets. Due to current economic limitations, Ireland's potential for generating renewable energy is being restricted and as a result, a very low proportion of energy is currently derived from agriculture sources. Therefore, the introduction of a "Green Tax Credit" would remove a barrier entry nationally in terms of costs and access to the grid. Pending the introduction of a feed-in-tariff and grid access. For example, each unit of surplus energy produced through renewable energy would accrue the energy generator an equivalent income tax credit.

BIOMASS/RENEWABLE HEAT

In the development of biomass power, the income benefits reach several different people from the forestry grower, harvester, timber processor, plumbers, biomass machinery technicians and the savings being delivered to the company/home using the biomass fuel. This economic activity surrounding the biomass sector alone has the ability to generate increased economic activity and employment that is unmatched by any other fuel sector.

In this context, the following should be implemented:

- The development of regional Biomass Trade and Logistics Centres (BTLC) should be prioritised in Budget 2020. The BLTCs would increase efficiency and ensure consumer confidence in the supply chain.
- A long-term support tariff system to allow the renewable heat industry realise its full potential.
- An appropriately resourced Support Scheme Renewable Heat is essential to reduce dependency on imported oil and gas and create sufficient scale in the renewable heat market.
- Commit adequate resources to develop Ireland's biomass economy and facilitate rural communities in finding diverse income streams while enabling Ireland to meet its renewable energy and emissions targets along with the provision of low-cost loans.

SUMMARY:

ICOS calls for the Introduction of incentives for community renewable energy projects such as tariffs and price supports for those community projects generating renewable energy, utilising the electricity levy to strategically promote renewable energy consumption and a "Green Tax Credit" for renewable electricity generation. We also call on the Government to ensure Ireland realises its potential as a world leader in biomass production through the provision of a range of supports and incentives.

About ICOS

ICOS serves and promotes commercial co-operative businesses and enterprise, across multiple sections of the rural economy. In total, ICOS represents 130 co-operatives with a combined turnover of €14 billion and a membership of 150,000 people, with ICOS affiliated co-ops employing 12,000 people in Ireland and a further 24,000 abroad.

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