NILF-report 2002–8

Taxation of Agriculture in selected countries

Study of The United States, Canada, Australia, Germany, United Kingdom, Ireland, France, Switzerland and Italy with relevance to the WTO

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Title	Taxation of Agriculture in selected countries**.** Study of The United States, Canada, Australia, Germany, United Kingdom, Ireland, France, Switzerland and Italy with relevance to the WTO
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Project	Skatteordninger i landbruket (L034)
Publisher	Norwegian Agricultural Economics Research Institute
Place of publication	Oslo
Year of publication	2002
Number of pages	123
ISBN	82-7077-489-8
ISSN	0805-7028
Key words	taxation, agriculture, comparison, WTO

About NILF

- Research and analyses on agricultural policy, food industry, commodity trade, economics, farm management and rural development.

- Documentation of economical results in the agricultural sector at national and farm level. This includes acting as secretariat for the Budget Committee for Agriculture and publication of annual Account Results in Agriculture and Forestry.

- Publication of research reports and analyses. Development of tools for farm management and accountancy.

- Funded by the Ministry of Agriculture, the Research Council of Norway and by assignments for public and private clients.

- Main office in Oslo; regional offices in Bergen, Trondheim and Bodø.

Preface

This report is the result of an effort to describe and compare taxation of agriculture in some selected countries. In addition one chapter gives a short presentation of WTO regulations and how they may affect national taxation policies in this sector.

The report is financed by the Norwegian Ministry of Agriculture, for which we are thankful.

Several staff members at NILF have contributed to the publication. Frode Veggeland has written chapter 4 regarding the WTO and taxation of agriculture. Leif Jarle Asheim has written the country reports relating to the US and Canada, Klaus Mittenzwei the country reports relating to Germany, France and Switzerland and Finn G. Andersen the country reports relating to Australia, United Kingdom, Ireland and Italy. Finn G. Andersen has also contributed to parts of the country reports concerning the US and Canada and written the chapters 1, 2 and 5.

Sjur S. Prestegard has read the report and made useful comments and corrections. Charlotte Nymoen and Berit Grimsrud have been responsible for the final lay out of the manuscript for publishing.

Oslo, September 2002

Leif Forsell
Director

Contents

Summary

Introduction
This report looks at the special measures for agriculture within the field of taxation and social security. Chapter 1 and 2 deal with general overview of taxes and taxation principles. Chapter 3 give more detailed information of the tax system in the selected countries, US, Canada, Australia, Germany, UK, France, Ireland, Italy and Switzerland. Chapter four deals with notifications to the Committee on Agriculture in the World Trade Organisation (WTO) concerning tax measures. In chapter 5 we have tried to systematize the different tax schemes in the selected countries.

Overview
In the federal countries there are a minimum of three levels of taxation, the federal, the state and the local level. In the unitary countries there are only two main levels, the government and the local level. The local level can both in federal and unitary countries, consist of sublevels such as the county level and the municipal level.

A topic relevant for the efficiency of taxation is that of tax expenditures. Tax expenditure occurs when a fiscal advantage is conferred on a group of individuals, or a particular activity, by reducing tax liability rather than by direct cash subsidy. Subsidies through a tax expenditure program are relatively hidden as opposed to direct subsidies, which are open to review, debate and alteration at regular intervals. Several countries have a tradition of providing farmers with tax benefits by special treatment of agriculture and forestry.

Yearly income as basis for the taxation in the way we measure it today, is of relative recent date. The taxation of the real income depends on one or another form of record for the enterprise. The alternative and old form of taxation is the cadastral system, i.e. taxation based on a stipulated value of some selected items which in the agriculture sector can be land area, soil quality, the size and composition of the livestock etc. In some countries the tax of small private enterprises is computed as a certain percentage of the annual turnover.

Some countries allow averaging the income for a fixed number of years to determine the basis for the income tax. Whereas this method is reserved the agriculture and forestry sectors in some countries it may also be available for all small enterprises. The average method can provide tax benefits if there are fluctuations in the income from one year to another and the tax system is strongly progressive.

Social security contributions are a mixture of a tax, a duty and insurance. The system for social security is quite different from country to country. Since the late 1980's we can, however, see a trend toward an increase of the public liability for the social security for all inhabitants followed by increased social security contributions.

The property tax is a tax on gross value of real property (real estate) with no deduction for debts. It is often a local tax. For agricultural and forest properties it is common to use a form of agricultural or forestry value instead of the real or market value. In some countries agricultural and forest properties are completely exempted from the property tax.

In all countries transfers of estates and gifts are in principle taxable in accordance with the system of *inheritance, estate or gift tax*. It is quite usual with special relieves for transfers of certain categories of properties such as agriculture.
In almost all OECD countries the trade of goods and services is charged with *value added tax*. There are different statutory provisions in each country concerning which goods and services are exempted from VAT. The different VAT rates also vary from one country to another. Some important OECD countries in particular US, Canada and Australia use different kinds of general *sales taxes* instead of VAT.

Country reports

United States (US)

The farmers can opt for *federal corporation tax* or *federal income tax*, however they are bounded by their choices for five years.

Incomes from farm and forestry do not represent separate kind of incomes. These incomes are determined and taxed like incomes from other businesses of a comparable size. There are, however, some detail regulations regarding farm income.

Both enterprises and individuals that are paying corporation tax or income tax are obliged to keep a kind of balance, but the law does not prescribe any special record keeping method. Profit accounting allows the following three methods: cash method, accrual method and crop method. In general the cash method is preferred as most farmers find it easier to keep cash method records.

Sole farmers and partnerships may also form three years average income. The rule of income averaging is now only available for farmers and only on farm income.

The system of depreciation is very flexible and allows different depreciation methods with both geometric and linear depreciations. There are also separate rules for immediate depreciation of livestock, pasture fences, stables in livestock and greenhouses in horticultural enterprises.

Profits and losses from sale of fortune articles are (depending upon classification) treated as normal income or in accordance with the special rules for *capital gains* and losses.

Self-employed and farmers can in special cases deduct a *business tax credit* and an *investment tax credit* from the computed tax.

For the determination of the *state income taxes* the assessment basis is taken over by the individual state. However, since no clear regulations of the income exist on the level of individual federal states, it can lead to delimitation problems and double taxation on that level. A comparison of some of the most important agricultural states in the US reveals substantial differences in personal and other deductions as well as income intervals and tax rates in the states.

On the federal level no real estate taxes are raised, however in most of the states there are either *real estate taxes* or similar *property taxes*. The value in use of agricultural properties is 40 to 70 percent lower than the market value and the tax preferential treatment of agricultural properties is further strengthened by the lower rates of assessment.

The Federal tax system includes also *taxes for Social Security* both for employees and self-employed. The rules for social security taxes are the same to farmers as to other self-employed.

Federal estate and gift tax is a very special system that applies a unified tax rate structure and a cumulative lifetime credit to gifts and transfers of money and other property at death. There are three factors that in addition reduce gift and estate tax in small family business: special valuation of farmland, deduction for family-owned business and installment payment of estate tax. For all these three factors there are attached special terms.

Sales tax is a state and local consumption tax. Rules and rates are different in the different states and the total sales tax including both state and local tax is between 4.0 and 9.75 percent. In this report it is only refereed to rules for the state sales tax in Minnesota. A lot of goods and services used in agricultural production are not taxable such as animals, feed for animals, veterinarian services, plants and seed, machinery and equipment, building materials and different services.

Petroleum tax is not a federal tax but a state tax and it is different rules in the different states concerning state tax on petroleum products. In many states use of petroleum in agricultural or industrial production is exempt from both petroleum tax and sales or use tax.

About 80 percent of the farmers in US have an income of less than US$ 60,000 and they have an income tax rate less than 10 percent. As in a lot of other countries the social security taxes in US are rapidly growing and on average, farmers earning less than US$ 60,000 paid more in social security tax than in Federal income tax.

Since 1997, the tax system has given both farmers and other self-employed tradesmen different benefits as increased self-employed health insurance deduction, income averaging (only farmers), expanded capital expensing and reduced tax rates for capital gains.

In the US the most important tax advantage for agriculture are cash accounting and deductibility of certain capital expenditure. The main advantage of using cash instead of accrual method is caused by the mismatch of incomes and expenses in different tax years since it is always beneficial to receive a benefit sooner rather than later.

Canada

The federal government claims income tax, corporate tax, purchase tax as well as capital tax on corporations, consumption tax and customs. The provinces claim purchase tax, land and property taxes and also income tax.

There are four sources of income, business, property, employment and office. In addition come incomes from pensions, social security or scholarships etc. Taxable income is in general the sum of income from different sources or gross income reduced by deductions. From the calculated net income personal deductions like pension contributions, old age provisions, extraordinary strains as well as different kinds of losses are deducted. Capital gains are calculated separately.

Farmers' incomes from farm and forest operations are taxed as business income although there are some tax advantages for farmers. The farmer is the owner or tenant of the farm and he may be a sole proprietor, a partnership or a company. Income from hiring out land, agricultural tenancy or lease is otherwise considered as property income.

No method of book keeping is prescribed, however the Generally Accepted Accounting Principles are to be considered as directive without any legal obligations. Sole proprietors or partnerships can choose between both book-keeping (accrual method) and cash method whereas a combination of the two is not possible. In general the sole traders prefer the cash method whereas agricultural companies are imposed to make use the accrual basis of accounting and keep records.

In 1987 the possibility to calculate taxable income as average over several years was abolished. Instead the farmers were offered a governmental program to stabilize their income. Through the Farm Income Protection Act it is possible for the farmers to open a Net Income Stabilization Account (NISA).

The Income Tax Act has no rule for limits to *capital gains*, however the Canadian Consolidated Revenue Act has developed some rules of thumb. Especially for farm capital equipment there is a free amount over the life period of CA$ 500,000 for sale profit and capital gains. Investment items are qualified farm property when they have been the property of the farmer or his family for at least 24 months.
The local government or municipalities claim the *real estate taxes*. The character of these taxes is very different from province to province. Since the property concept is very wide the property taxes are high in international comparisons.

There are large provincial differences in valuation of farmland and farm residences with a view to property tax, but in all provinces the property taxation of agriculture is much lower than taxation of other properties.

In Canada provisions in the Excise Tax Act (the Act) regulate *the Goods and Services Tax (GST)* and *the Harmonized Sales Tax (HST)*. The tax rates are either 0 and 7.0 percent (GST) or 15.0 percent (HST including GST)). The HST applies to the same base of goods as GST at a rate of 15 percent. Of this 7 percent is the federal part and 8 percent is the provincial part. Businesses or farms with total sales above CA$ 30,000 per year have to register for GST/HST.

The supplies of most agricultural and fishing products are zero-rated, however several agricultural products not for human consumption like plants, hides, firewood etc. are taxable to a higher rate. However supplies of both raw tobacco and wool not processed further than washing, is zero-rated. Supplies of inputs like fertilizer, feed, pesticides and some agricultural equipment are zero-rated too.

Australia

Both the federal government as well as the local authorities in the states imposes taxes in different ways. About three quarters of the total taxes are paid to the federal tax collector. In Australia the tax-year runs from July 1 to June 30 for all taxpayers, both individuals and companies.

Income tax is a federal tax and represents about 75 percent of the total federal taxes. Many of the tax benefits for primary producers in Australia, are so-called conditional tax exemptions, i.e. the taxation is partial put off to a later period. The tax benefit can thus be composed of a mix of improvement of liquidity, lower tax progression and inflationary profit.

The main income tax system for primary producers aims at averaging taxable income over a maximum of five years. The primary producers can chose to withdraw permanently from the averaging system and pay tax at ordinary rates. However, once the taxpayer has made this choice, it will affect all his assessments for subsequent years and cannot be revoked.

The Farm Management Deposits (FMD) is part of the income tax averaging system and the scheme make farmers possible to set aside incomes in good years and take them back in more difficult years. Only taxable income from primary production can be invested in a FMD. Farmers earning more than AU$ 50,000 off-farm taxable income in the year of deposit cannot obtain the tax benefits of FMDs. The minimum period of a FMD is twelve months, and the maximum amount to hold in a FMD account at any given time is AU$ 300,000.

The Dairy Exit Program (DEP) is a part of the Government's Dairy Adjustment Package. If dairy farmers choose to exit agriculture, they can obtain an exit payment of up to AU$ 45,000 tax-free. The Dairy Exit Program was introduced in 1999 and was available until June 30 2002.

The general *Land tax* is a state and territory tax on land in all the states. The rules are somewhat different in the different states, and only the rules of the state of Victoria are described in this report. Land tax is an annual tax on all land in Victoria with a total unimproved value of AU$125,000 or more. There are several exemptions from this principal rule. The two most important exemptions are concerning land used for residence and the greater part of land used for primary production.

Stamp duty is a State and Territory tax on certain documents and transactions, and the rules vary between the states. As a support to younger family members to taking up ownership of family farms, transfer of family farms were in 1993 exempt from stamp duty in Victoria. Since June 1 1999, the exemption also include the transfer of land used for primary production from a company to natural persons if they are relatives of each other and own all the shares.

In Australia there is a mixture of public and private social security systems. *Medicare* is the public system, which provides access to health care for Australian residents. It is no special rules for farmers in the Medicare system.

The *pay-roll tax* is exclusively a state and territory tax. All Australian states and territories charge the pay-roll tax, but each state has its own legislation, with differing provisions and exemption. Employers are liable for paying pay-roll tax on wages, salaries etc. paid to the employees when their total wages exceeds a certain level. This level is called the exemption threshold and varies between the states. In Victoria the threshold is AU$ 515,000 and most small businesses, including primary producers, are therefore more or less exempt from the pay-roll tax.

The *Goods and services tax (GST)* constitute about 22 percent of the federal taxes. In principle GST is a Value Added Tax (VAT) so that companies, farmers, tradesmen etc. can deduct the greater part of GST paid on inputs. The base of the tax is very wide and includes most goods, services and activities. The rate for GST is 10 percent, however in addition several groups of goods and services are zero-rated.

Food for human consumption is normally zero-rated, but not prepared meals. Farmer's delivery of some products is not classified as food for human consumption before the products have passed through further treatment.

Sole traders or companies with an annual turnover of AU$ 50,000 or more; have to be registered for GST. If the annual turnover is less than the threshold it is access to voluntary registration for GST. It is allowed to use cash accounting for GST if the annual turnover is AU$ 1 million or less or if the accounting for income tax purpose is on a cash basis.

There are no special GST rules for primary producers except the zero rating of several products from the primary industries.

There are two Australian schemes for *rebates and grants for diesel fuels* used in agriculture and certain other categories of business activity. On of the two schemes provides a grant per liter diesel and alternative fuels for certain on-road uses. It is also possible for farmers to use this scheme for transport of farm products on public roads. Farmers eligible for rebate under both schemes have to keep separate records for each scheme.

Each year the Department of Treasury publishes information of the volume of *tax expenditures*. Tax expenditures are defined as tax concessions designed to provide a benefit to a specified activity or class of taxpayers. The value of the tax expenditures has increased over the last years. The total tax expenditures to farmers are small weighed up with several other groups of taxpayers.

Germany

It has long been known that the federal state of Germany provides its farmers with generous support through the tax system including social security. The main source of support comes from a special valuation of agricultural income and property together with a special social security system for the German farm sector.

The *income tax* is a personal and federal tax. The structure of income taxation is based on seven categories of income one of which is income from agriculture and forestry.

Agricultural and forestry taxation have several benefits in relation to business taxation. These include special rules for book keeping, special exemptions and tax rate reductions, a fixed arrangement on VAT taxation, a special valuation base for heritage taxation and a lower property tax on arable land. Agricultural income is calculated according to four different methods: (a) book keeping, (b) keeping an inventory, (c) flat method ('unit valuation'), and (d) income valuation by the financial administration. Farms are obliged to keep records if they exceed a certain size.

Around 30% of all German farms keep records. Farms that are not required to keep records, but exceed the limits for the flat method keep an inventory. The agricultural income on half of all German farms is calculated according to the flat method. The income calculation is based on the economic value of the land. The estimated profit per hectare is directly linked to the so-called 'hectare value' which is a measure of the potential land quality. The 'flat method' implies that taxable agricultural income is usually lower than under book keeping.

Agricultural income is subject to an income allowance, independent of the method of income calculation. All individuals with agricultural income are eligible to the allowance as long as gross income is below EURO 32,250 (single) or 64,500 (married) and gross agricultural income is higher than the income allowance. The income allowance was EURO 700 (single) or EURO 1,400 (married) in 2001.

Regard to *property tax* is agricultural property and non-agricultural property treated in the same way. The farm sector has certain benefits, however, since the calculation of agricultural property is based on the economic value of the farm with its key date from 1964.

German farmers have their own *social security system* covering an old age pension scheme, a health insurance scheme and an accident insurance scheme. This system is open for farmers, their families and agricultural workers. This special system for social security is strongly subsidized by the federal government.

Tractors and other agricultural machinery are exempt from *car tax*. In addition, there is an allowance on the *diesel oil tax*. There are also some allowances on diesel and gas used for greenhouses.

The budgetary effect of tax measures (incl. social security) target agriculture in Germany is around EURO 7,400 per man-year or around EURO 270 per hectare. Almost 85 percent of this tax measures is related to the special social security for the agricultural sector. The budgetary effect of tax measures exclusive social security shows a downward trend from 2000 to 2001, while it is just the opposite if one includes social security. This indicates that Germany is engaged in reducing special tax measures for its agriculture, while social security contributions are rapidly growing due to the age distribution of the German population.

United Kingdom

The agricultural industry in UK is taxed in almost the same way as other industries and the farmers are obliged to keep accounts as other tradesmen for the tax computations. The tax year is twelve months and it runs from April 6 one year to April 5 next year.

The *income tax* system is built up with different schedules for different items of profits or incomes. The two most important schedules are Schedule E, which covers income from employment, and Schedule D, which includes income from trades, professions, business, property and other annual profits. Incomes from farming and market gardening are chargeable under case I in the schedule D in the same way as incomes from other trades.

Small and medium sized businesses including agriculture can write down machinery and equipment by 40 percent in the year of purchase. After this reduction with the Writing Down Allowance, the recently acquired item is put in a common pool for all machinery and equipment in the enterprise. The pool is written off over the following years at 25% on the reducing balance each year.

In principle, there are no special rules for the *capital gains tax* in connection with agriculture. The farmhouse is a private asset and therefore exempt from Capital Gains tax.

Council tax is a local charge on dwellings. Farm houses, farm cottages, croft houses and houses connected with fish farms are placed in a lower valuation band then they would otherwise be placed. Non-domestic property is liable to *business rates*, but agricultural land and buildings are exempt from business rates.

Most people who work have to pay *National Insurance contributions*. There are six classes of contributions and farmers and other self-employed persons are placed in Class 2.

Registration limit for *Value added tax* is £ 55,000 per annum in dutiable turnover. There are three different rates for VAT: Standard rate at 17.5 %, reduced rate at 5,0% and zero rate at 0,0 %. For agriculture there are four main groups of zero-rated products: Food for human consumption, animal food, live animals and seeds and plants to provide food for human or animal consumption.

The flat rate scheme is an alternative to VAT registration for farmers. A farmer registered as a flat rate farmer, do not account for VAT and can therefore not reclaim input tax. A flat rate farmer can, however, charge and keep a flat rate "addition" (FRA) when he sell goods or services to VAT registered customers. FRA is not VAT, but compensation for losing input tax on purchases. The flat rate in UK is 4,0% and it is not intended as reimbursement of all the VAT incurred on purchases.

Transfers of gifts and estates are in principle taxable on the system of *inheritance tax*, but in addition to different tax-free basic deductions there are a lot of limitation and exceptions from the liability to pay inheritance tax. Transfers of business assets are separately privileged in the British rules for inheritance tax. There are inheritance tax relieves available for business and business assets, for agricultural property and for woodlands. The relieves depend on different terms as a minimum period for ownership and use of the property. Both the business relief and agriculture relief is 100% or 50% depending on what sort of assets are transferred.

Ireland

The income tax year is twelve months and will from the year 2002 follow the calendar year. If the farmer is a sole trader, profits and capital gains are assessable to income tax and capital gains tax. If the trade of farming is in a company, the profits and gains are assessable to corporation tax. Only about 40,000 farmers of 101,000 farmers in total were actually liable to pay tax on farming profits for 2001.

There are four schedules for *taxation of income,* and profits from farming and market gardening are taxable under Case I of Schedule D in the same way as profits from other trades. Individual full-time farmers may choose to be assessed in the ordinary way with an accounting period of one year or on the basis of three years average income.

Farmers may claim a farm buildings allowance for capital expenditure on the construction of farm buildings except building used as a dwelling. The rate is 15 percent of the capital expenditure in each of the first six years with the remaining 10 percent in year seven.

The Irish government gives different advantages to farmers who reduce the pollutions from the farms. The Irish government in different ways also prioritizes the *transfer of land to young, trained farmers* and gives both the young farmer and the retired farmer different tax benefits.

Residential property tax is an annual tax chargeable on the net market value of residential property. Net market value is the market value of the residential property reduced with a basic amount. It is no exemption for farmhouse as residential building.

Stamp duty is tax on certain documents,—for example legal and commercial documents which are necessary to transfer ownership of real property (house and land). There are a couple of exemptions or relieves from the stamp duty. For example the transfer of land to a young trained farmer is exempted from the stamp duty.

It is no special rules for farmers in the *social security system*.

Individual and legal persons are liable for *Value added tax (VAT)* if the annual turnover exceeds limits of EURO 51,000 for goods or EURO 25,500 for services. The standard VAT rate is 21%. In addition to the standard rate, it is three reduced rates: Zero-rate, 4.3% and 12.5%. Food used for human consumption, certain fertilizers, seeds and plants used to produce food, certain animal feeding stuffs, supply and sowing of crops for food production are zero-rated. Live animals are rated at 4.3% and different agricultural services are rated at 12.5%. Hire of machinery, leasing of milk quota (without land), transport and storage are rated at standard rate.

Ireland applies the EU system of flat-rate farmers. In order to compensate for VAT paid on supplies, the farmer is entitled to a flat rate additional of 4.3% to the selling price for the agricultural products or services. The farmer can only use the flat rate additional with sales to individual or legal persons who are registered for VAT.

Inheritance and gift tax is charged on the market value of the property comprised in the inheritance. The rate is 20% in all classes after a threshold. However, there are various exemptions from gift and heritance tax, for example Agricultural relief and Business relief. If the agricultural property is sold (or compulsorily acquired) within six years of the date of the gift or inheritance and is not replaced within one year by other agricultural property; the relief is withdrawn.

Farmers pay a reduced rate of *motor tax* for tractors, which only or chiefly are used in the agricultural production. It is relative strong restrictions for use of reduced rate tractors outside the farm.

France

French farmers face in principle the same rules for taxation and are subject to the same taxes as other self-employed tradesmen. There are, however, some special rules that only concern agriculture. In addition, there is a special social security system for French farmers, their families and farm workers.

The individual *income tax* is a household tax; this means that the family is taxed as a unit. Income from agriculture is one of several income sources subject to the income tax. Agricultural income can be calculated according to four different modes: Ordinary book keeping, simplified book keeping, simplified income calculation and a transition scheme. If a farmer keeps accounts he is entitled to a 20%

reduction in the taxable agricultural income. Young farmers that start farming are allowed to reduce their taxable agricultural income for five consecutive years by 50%. This special rule is also applied to tradesmen and craftsmen who start their own business.

Real estate is subject to a *property tax* that is collected by local communities. There is also a *land tax*, but its significance is decreasing.

France has its own *social security system* for farmers, their families and farm workers. Around 42% of all public support to French agriculture was provided through the special social security system for French agriculture in 1999 and 2000. The social security contributions of a farmer depend on his/her own income and an average national annual income.

It is difficult to quantify the value of the special tax measures directed to French farmers. It appears that there are only few measures that are solely applied to agriculture. It has been suggests that income from agriculture calculated by the simplified income calculation scheme may be 50 % lower than the income would be if farmers had been keeping accounts.

Switzerland

There are only a few tax related measures to Swiss agriculture. It is, however, difficult to quantify their financial impact.

The structure of Switzerland being a confederation with three administrative levels, *Bund*, *Kanton* and *Gemeinde*, implies that each level has the right to collect certain taxes and fees. Due to the partially strong sovereignty of the cantons, there might be different rules how to treat farmers and farm families between the cantons.

It is not any special measures in connection with the *income taxation* of Swiss agriculture. The Swiss farmers are obliged to keep accounts like other self-employed tradesmen.

The *property tax* belongs to the regions. The valuation of agricultural land for property tax purposes is based on the method of economic valuation. This method gives values that are significantly lower than those values that could be obtained through sale in real estate market.

Farmers are like other persons insured through the Federal Office for *Social Security*. A peculiarity concerns the family allowances for small farmers, which is given to small farmers below a certain income level. If the 'pure' income is below CHF 32,000 per farm family, then farm families are given a monthly payment for each child. The amount is regionally differentiated (valleys and mountain areas). The total amount of this support will probably be around 120 million CHF in 2002. The family allowance for small farmers is mentioned in the Swiss notifications on domestic support to the WTO as a 'green box'-measure.

Swiss agriculture is eligible to a partial refund of the *mineral oil tax* in the same way as other sectors like forestry, fisheries and transport.

Italy

The Italian structure of *personal income tax* is based on six categories of income. In each category, the taxable income is determined to own rules. The tax basis, however, is the aggregate income from the six categories of income. The Italian system for taxation in agriculture is special as it is a composition of normal and special regimes.

Income from agriculture and forestry is defined as income from real estate properties and placed in category one. Real estate properties in Italy are registered either in the property land registers or in the urban building land registers. If income from properties in these registers is registered with an assigned yield, the income is taxable in income category one as income from real estate properties. Income from agriculture and forestry is taxable in this way as an assigned yield from the particular estate (the cadastral system).

The taxation of income from i.a. agriculture and forestry differs in this way essential from the taxation of the other categories of income. The taxable income from agriculture and forestry is determined after the land register yield and not on the basis of the actual yield. The yields in the land register are estimated as average values of land and building with input of usual work and capital. The registered values in the land registers are stipulated very low and this result in a preference of agriculture and forestry when it comes to taxation.

Taxation on basis of certain standards instead of total net income has long tradition in Italy also outside agriculture and forestry. Until 1998 the standard system included 45 business-sectors but in 2001 the system increased to include about 120 business-sectors.

The communal tax on immovable property is a local tax to the municipality where immovable property is situated. There are different exceptions and deduction for the agricultural sector regarding this tax, for example for agriculture properties in the mountain areas and for full-times farmers.

Stamp duty is payable on the deeds, documents and records listed in an official tariff. It is some exemptions from the tax liability; for instance deeds and documents relating to the granting of agricultural loans and of Community and national aids to the agricultural sector.

As in Germany and France the government supports farmers in the *social security* system. There are also several specific benefits for farmers in the mountain region.

There are three important *taxes on goods and services*: the tax on mineral oils, the value added tax and the regional tax on production. The *tax on mineral oil* is reduced with 22% for use of a certain quantity of fuel in agriculture, horticulture, forestry and fish farming. The reducing of the tax on motor fuels is of big importance for the farmers.

Value added tax (VAT) is a state tax and the threshold for VAT registration is EURO 8,263. The standard rate for VAT is 20% and the reduced rates are 4 and 10%. Beside the main scheme there are special schemes for some categories of business, smaller trades and farmers.

Regional tax on productive activities–IRAP is charged on the net value from the businesses purposed within each region. Agricultural producers, which have a turnover less than EURO 2,582, are among others exempted from the liable to pay IRAP. For farms situated in the municipalities in the mountain areas is the limit EURO 7,746.

The two most important causes of the low tax burden in the agricultural sector are the lower rate of social security contributions and the taxation on the basis of the cadastral register

The WTO and Taxation of Agriculture

Chapter four deals with notifications to the Committee on Agriculture in the World Trade Organisation (the WTO) concerning tax measures. We have also briefly looked at discussions and disputes on tax measures between WTO members represented in the same committee.

In principle, the WTO regulations do not cover national tax policies. Nevertheless, systems of taxation can be relevant under the WTO law insofar as such systems come into conflict with basic principles like non-discrimination and/or affect other countries' rights under specific the WTO agreements like the Agriculture Agreement and the Agreement on Subsidies and Countervailing Measures. Thus, the decisive criteria for assessing whether or not member countries violate their WTO obligations through systems of taxation, is the way these systems is designed–not the level or size of the taxes themselves.

The term "tax" is not included in the text of the Agriculture Agreement of the WTO, but we have nevertheless identified taxation systems that are relevant for the provisions of the agreement. Still, since tax policies in principle are exempt from member states' WTO obligations, it is difficult to know with certainty how specific tax policies would be affected by the rules of the WTO in a potential dispute.

Our search shows that tax measures to a little extent have been notified to the WTO as such. In some notifications agricultural tax measures are "built into" other measures in a way that makes them difficult to identify. In others, tax measures are explicitly listed, but not quantified. Four of the countries being accounted for in chapter three of this report are represented. The notifications from these four countries are listed in appendix 2.

Two types of tax measures have been notified under AMS (Aggregate Measure of Support). One is about taxes and fees that are subtracted from total AMS. The other is about support for certain input factors–like tax exemptions for fuel–used in agricultural production.

Since 1995 tax measures have been discussed in 21 meetings of the Committee on Agriculture. We have focused on two topics that are of particular interest, both because they involve some of the major actors of the WTO and because they highlight different state views. The first topic is tax exemptions on fuel used in agriculture. The second topic is the question of tax measures being used as export subsidies.

The presentation in chapter four shows that the *way* national taxation systems are *designed* can bring them in conflict with the provisions of the Agriculture Agreement of the WTO (and other WTO agreements). But many tax measures specially intended for agriculture purposes may still be used as legitimate instruments without breaching the WTO regulations. Tax exemptions and tax refunding for fuel are examples of this.

1 Introduction

This report looks at the special measures for agriculture within the field of taxation and social security. Several countries have a tradition of providing farmers with tax benefits by special treatment of agriculture and forestry. The most common ways are i) the cadastral system, i.e. the use of stipulated agricultural values instead of real values for assessment of agricultural properties, ii) the income averaging taxation schemes, iii) the use of the cash method instead of the accrual method of accounting and iv) the special schemes for taxes on agricultural goods and services, either Value Added Taxes (VAT) or General Sales Taxes (GST).

It has been necessary to limit the report to some selected countries. The US, Canada and Australia have a large agricultural production and are important countries in the world trade with agriculture products. Germany, UK, France, Ireland and Italy are all members of the European Union (EU), but in spite of that have quite different ways to assess agriculture and forestry. We have also looked at Switzerland, one of the few countries outside the EU in Western Europe.

We have had some problems to stipulate the volume of the farmer's tax benefits due to different reasons. Primarily, the volume of the benefits is not determined in a majority of the countries (or we have not found them). Secondly, some of the tax benefits are also available to several other businesses and thirdly somewhat different ways of defining agriculture prevail in the different countries.

Chapter four of the report deals with notifications to the Committee on Agriculture in the World Trade Organisation (the WTO) concerning tax measures. We have also briefly looked at discussions and disputes on tax measures between the WTO members represented in the same committee.

In this report we have used the local currency for each country. For the EU countries we have changed old local currency to EURO with exempt for the UK.

2 General overview of taxes and taxation principles

2.1 Tax definition and some general tax requirements

According to James & Nobes (1992, p. 8):

> *"A tax is a compulsory levy made by public authorities for which nothing is received directly in return…….Taxes are, therefore, transfers of money to the public sector, but they exclude loan transactions and direct payments for publicly produced goods and services"*.

In reality, however, it is not always possible to distinguish between taxes and payments for publicly produced goods and services. An example of this is the stamp duty, which is a mixture of a payment for a public service and a tax on property transaction. Linguistic, however, a confusing use of the words tax and duty exists in some countries as some special taxes are sometimes denominated as duties.

There are, however, some general and important requirements relevant to a functional tax system. James & Nobes (1992, p. 13) emphasize four criteria: efficiency, incentives, equity and macroeconomic considerations. These criteria are based on the old four canons of taxation, dating back to Adam Smith (1776):

- Equity, i.e. fairness with respect to the tax contributions of different individuals
- Certainty, i.e. a lack of arbitrariness or uncertainty about tax liabilities
- Convenience, with respect to the timing and manner of payment
- Efficiency, i.e. small cost of collection as a proportion of revenue raised, and the avoidance of distortionary effects on the behavior of taxpayers (i.e. the principle of neutrality).

The public authority's principal intention of taxing the inhabitants and their business activities in a country is to confiscate personal means to finance the activity of the government. However, several other concerns are also considered when the authorities decide upon the actual tax structure.

One common requirement is that the system should be simple both for taxpayers and the taxation authorities. In addition the tax system should satisfy the people's own "sense of fairness". One problem in this respect is that different people may have a different understanding of the phrase "sense of fairness". The most common understanding of a fair tax system is that the burden of taxation has to be equally distributed among the physical and legal taxpayers depending on the capacity of each one to bear the burden. However, is it fair that a hard working person with a relative high income should pay more tax than a lazy person with a low income? Another question is in what way should a taxpayer's wealth be assessed and taxed compared to his or her income?

The tax level and structure can be changed or manipulated to control the financial politics and the inflation problems in a country. In the examined countries the tax structure is usually constructed so as to level out the after tax income or costs of living between poor and rich people. To achieve this the authorities use different kinds of measures such as reducing the taxable income with tax-exempt basic deductions and to use progressive tax rates. Tax credits are also common. The authorities in each country will have their own priority of what they want to achieve with the current tax structure.

2.2 Taxation authorities

All forms of taxation must have a legal foundation and thus only public authorities can have taxation rights in a country. This right is normally divided between the central and the local government. Although the political regime is quite similar, one can distinguish between unitary and federal countries. The central government has naturally a lower share of the total tax receipts in federal countries than in unitary countries (table 2.1). In Norway the share of the central government is relatively low (70 percent) in spite of being a unitary country.

Table 2.1 Government Centralization in Federal and Unitary Regimes, Measured by the Central Government's Share of total Tax Receipts, 1970s

Country	Central government's Tax share (%)
Federal countries	
Australia	80
Austria	70
Canada	50
Germany	51
Switzerland	41
United States	57
Unitary countries	
France	88
Ireland	92
Italy	96
United Kingdom	87
Norway	70

Note: For most countries, the years covered is 1972–1979

Source: Arend Lijphart 1984, p. 178

In the federal countries there are a minimum of three levels of taxation, the federal, the state and the local level. In unitary countries there are only two main levels, the government and the local level. The local level can both in federal and unitary countries, consist of sublevels such as the county level and the municipal level.

2.3 Tax expenditures and other tax instruments

A topic relevant for the efficiency of taxation is that of tax expenditures. According to James & Nobes (1992, p. 36) tax expenditure occurs when a fiscal advantage is conferred on a group of individuals, or a particular activity, by reducing tax liability rather than by direct cash subsidy. James & Nobes (1992, p. 36–37) call attention to the fact that subsidies through a tax expenditure program are relatively hidden as opposed to direct subsidies which are open to review, debate and alteration at regular intervals:

> *"Although deductions against tax liabilities are costs to government in the same way as cash payments or provisions in kind, they remain comparatively hidden and secure from scrutiny. Hence, it is even more likely than with outright subsidies that tax deductions may remain even when the case for them has diminished or even disappeared."*

The Commonwealth Department of The Treasury in Australia compares tax expenditure and direct expenditure from the fixed position of the Government, and concludes that a direct expenditure usually will have a smaller net budgetary impact than a tax expenditure of equivalent nominal value:

"Comparisons between tax expenditures and direct expenditures are informative in broad terms, although the costing are not strictly comparable for the following reasons:

A tax expenditure tends to provide a higher benefit than a direct expenditure of the same magnitude. This is because direct expenditures are often taxable, whereas tax expenditures are not. Therefore, a direct expenditure will, in some circumstances, have a smaller net budgetary impact than a tax expenditure of equivalent nominal value.

The removal of a tax expenditure or a direct expenditure of the same magnitude may have different effects on the underlying fiscal balance for reasons discussed in chapter 1.4."

(Commonwealth Department of The Treasury, Australia 2002.)

Also James & Nobes (2000, p. 38) oppose an extensive use of tax expenditures:

"A fourth difficulty is that tax expenditures complicate the tax system itself. Increased complexity inevitably increases administrative and compliance costs and, given the other problems, it seems reasonable to suggest that a convincing case ought to be made before aid for a particular cause is given through tax expenditure rather than by explicit subsidy.

The question why tax expenditure rather than direct subsidy is used to dispense aid is interesting. Apart from any historical reasons, it might be that politicians would prefer not to be seen spending public money, and so they hide behind the veil of taxation. For the same sorts of reasons, those in receipt of benefits from the state may well prefer a tax concession to a cash handout. It might be that the pervasiveness of the modern tax system is such that tax expenditure is a convenient tool for those wishing to manipulate the economy. Whatever the reason, it is clear that the subject of tax expenditure deserves more attention than it has received to date."

Tax expenditures are most common for shipping companies, ship owners and in agriculture. Several countries also tax selected employees more lenient than employees in general, for example sailors and foreign experts.

It is also common to have special tax rules for the first and latest life-years of an enterprise. These rules can be quite similar for all kinds of enterprises or different for selected enterprises such as in agriculture and forestry. The authorities use different instruments in taxation of trades and industries. The instruments may be different for big and small enterprises or for companies and individual enterprises. The instruments and rules can also be different for selected kind of industries, for example agriculture and forestry. We will limit this report to only deal with individual enterprises in the agricultural sector.

2.4 Different kinds of taxes

OECD (1993) apply the following classification for the main groups of taxes:

- Taxes on income, profits and capital gains
- Social security contributions
- Taxes on payroll and workforce
- Taxes on property

- Taxes on goods and services
- Other taxes.

2.4.1 Tax on income, profits and capital gains

Yearly income as basis for the taxation in the way we measure it today, is of relative recent date. The taxation of the real income depends on one or another form of record for the enterprise. The alternative and old form of taxation is the cadastral system i.e. taxation based on a stipulated value of some selected items which in the agriculture sector can be land area, soil quality, the size and composition of the livestock etc. In some countries the tax of small private enterprises is computed as a certain percentage of the annual turnover.

The taxation records are in various ways different from the financial records and the differences will vary from one country to another. In some countries small enterprises can file the tax return on the cash basis instead of the accrual basis.

All countries use a period of twelve months for the tax year but the period may be different from the calendar year. Some countries also allow averaging the income for a fixed number of years to determine the basis for the income tax. Whereas this method is reserved the agriculture and forestry sectors in some countries it may also be available for all small enterprises in other countries. The average method can provide tax benefits if there are fluctuations in the income from one year to another and the tax system is strongly progressive.

The tax rates are often progressive for income tax for natural persons and non-progressive for legal persons paying corporate tax. The effects of a system of progressive tax rates are discussed among economists. In accordance with the income-expenditure or Keynesian approach, taxes are "merely a transfer of money" and increased government spending will lead to increased growth, and thus the tax rates can be varied with little effect on production. The supply side school of thought in contrast stresses the disincentive effects of taxes, which work in several ways. First, the opportunity costs of leisure decreases, leading to people substitute leisure for work. Second, high tax rates cause people to work on jobs where they are less productive, for instance leading to induce a lawyer or a teacher to start painting the house, repair the car or perform other tasks where they are less productive. Third, high tax rates increase the incentive of individuals to evade taxes, and forth high marginal tax rates mean that more and more valuable resources are devoted to the tax shelter industry (Pascour 1990).

The main trends in most countries the last 10–15 years have been to reduce the progressive rates and instead extend the tax basis. In all countries there are different tax relieves to selected groups of taxpayers, for instance old people, single parents and persons with disability or serious illness.

In most countries taxable income from miscellaneous sources are added and the tax is then computed on the total taxable income. In a few countries one or more of the income sources are taxable separately.

2.4.2 Social security contributions

Social security contributions are a mixture of a tax, a duty and insurance. In principle a part of the social security contributions are paid directly in order to receive future pension benefits. Such payment is not considered to be a tax as long as there is a real relationship between the contribution and the pension. However, the contributions from high-income taxpayers are often bigger than their pension and this part is clearly to be perceived as a tax. A second part of the social security is payment for illness, medicines, hospital treatment etc. and for this part no direct connection exists between the contribution and the payback. This part is therefore characterized as a tax or an insurance premium.

The system for social security is quite different from country to country. Since the late 1980s we can, however, see a trend towards an increase of the public liability for the social security for all inhabitants followed by increased social security contributions.

2.4.3 Payroll and other taxes on workforce

In this report payrolls or other taxes on the workforces will not be described in greater details. In the examined countries we have not any special rules for farmers in this field.

2.4.4 Taxes on property

In most countries *the net-wealth tax*, as we know it in Norway is phased out.

The property tax is a tax on gross value of real property (real estate) with no deduction for debts. It is often a local tax. For agricultural and forest properties it is common to use a form of agricultural or forestry value (i.e. value when used in agriculture or forestry) instead of the real or market value. In some countries agricultural and forest properties are completely exempted from the property tax.

In all countries transfers of estates and gifts are in principle taxable in accordance with the system of *inheritance, estate or gift tax*, however several limitation and exceptions from the liability to pay the tax exist. The actual tax to be paid depends on different factors such as the valuation of the inherited property and the relationship between the deceased/donor and the heir/recipient.

It is quite usual with special relieves for transfers of certain categories of properties such as in agriculture. In this way there are more easy tax terms of transfer of business property or of private property.

Stamp duties are taxes charged on certain documents,—legal and commercial—that are necessary to transfer ownership of real property. The rules vary from one country to another, however as a main rule there are a couple of exemptions or relieves from the stamp duty.

2.4.5 Taxes on goods and services

In almost all OECD countries the trade of goods and services is charged with *value added tax*. There are different statutory provisions in each country concerning which goods and services are exempted from VAT and the tax-rates for different goods and services.

In the EU the VAT-system is mandatory in all member states and the common main rules are laid down in the Sixth Directive 77/388/EEC on the harmonization of the laws of the member states relating to turnover taxes. Article 24 in the Directive allows member states under certain conditions and within fixed limits of applying to use simplified procedures such as flat-rate schemes for charging and collecting the tax provided they do not lead to a reduction thereof. Article 25 in the Sixth Directive deals with farmers and the common flat-rate scheme for farmers.

VAT is mainly of liquidity significance for agriculture and other businesses as it is a tax on consumption. Therefore the VAT is passed over to the consumers.

Some important OECD countries in particular US, Canada and Australia use different kinds of general *sales taxes* instead of VAT. In these federal countries the sales tax is a state and local consumption tax.

2.5 Burden of taxation and taxable capacity

Measuring the burden of taxation is the most common way to undertake quantitative comparisons of taxation between different countries. The burden of taxation reflects the general transfer of money from the private to the public sector. (Olsen 1992, p. 27). The burden of taxation as a percentage of GDP is shown for the examined countries in table 2.2.

Table 2.2 Total tax revenues as a percentage of GDP

Country	1970	1980	1990	2000
US	29.2	29.3	29.5	28.9
Canada	31.3	31.6	37.0	37.5
Australia	24.2	28.4	30.8	30.6
Germany	32.9	41.7	36.8	37.8
United Kingdom	36.9	35.3	36.7	37.7
Ireland	31.2	34.0	36.8	31.5
France	35.1	41.7	43.8	45.5
Switzerland	23.8	30.8	31.5	35.9
Italy	26.1	30.2	39.1	42.3
Norway [1)]	39.3	47.1	46.3	40.2
OECD total	30.0	35.1	38.6	37.5

Source: OECD Revenue Statistics of OECD Member Countries, Various editions.

1) For Norway the tax revenues include tax from the oil sector. Excluding the oil sector the tax revenues in 2000 were 45.4 % of GDP.

Perry et al. (1992) maintain that farmers in countries with high levels of subsidies as well as high taxes may be in the same after-tax financial situation as farmers in countries with lower subsidies and considerably lower tax commitments. He compares the situation on two same size farms in the US and Canada. Due to different farm programs the farm income in the US is about US$ 3,800 higher than it would be under the Canadian farm programs. However, taxes and social programs of Canadian farmers increase the after tax farm incomes there by about US$ 5,150. The Canadian tax policy is especially advantageous to farmers with a low income; however also for farms of low or moderate size taxation policy and social programs are more important than differences in farm support programs. With increasing farm size differences in farm support programs will become more important.

The study also indicates that farmers in the two countries to a large extent are taxed as other self-employed. However, the Canadian government places a larger proportion of the taxation burden on wage earners and a smaller proportion on self-employed than the US. For 1991 the overall level of taxation was 29.8 percent of GNP in the US and 37.3 percent in Canada (Andersen et al. 1994). Generally speaking there will be less room for special tax concessions for farmers in countries with a low level of taxation.

3 Country reports

3.1 The United States (US)

3.1.1 Introduction

The US tax system is characterized by a pronounced federalism. In the US the original financial autonomy is incumbent on the federal state, taxes on the federal level may only be raised if they serve the common welfare. On the local level the counties, municipalities and townships, school districts as well as special purpose authorities, are allowed to claim taxes. The federation levies federal income tax on individuals, which is a uniform tax on gross income. Some states do not have an own income tax; others raise it in a quite different form. Municipalities raise own income and corporation taxes. All the states as well as most municipalities raise land and real estate property taxes. The Internal Revenue Code (IRC) of October 22 1986 (including later changes) is decisive for all federal taxes whereas the legal validity of the remaining taxes are the tax laws and the constitution of the respective Federal States or municipalities (Parsche et al. 2000, p. 196).

3.1.2 Income taxation

US citizens are unrestricted taxable with their worldwide income, if necessary also up to 10 years after giving up their citizenship. Likewise taxable are foreigners with a lasting residence permit or green card as well as other foreigners with an annual stay of more than 183 days in the US. As far as allocation of enterprises regarding income or corporation tax concerns, no precise rules exists, as they may be taxed as a corporate enterprise on the state level and as an unincorporated enterprise on the federal level. The following forms of businesses are distinguished:

- C corporations are larger enterprises with stocks traded on stock exchange markets, which are subject to corporation tax. The dividends are subject to the corporation tax of the personal income tax.
- S corporations are smaller capital enterprises as well as taxexempt organizations if they meet certain criteria. They may also opt for taxation as unincorporated enterprises.
- Under partnerships fall i.a. unincorporated firms and other profit intended associations. They normally have to pay income tax, however they can opt to pay corporation tax. Public traded partnerships always have to pay corporation tax. Limited liable companies are in some states treated as corporations and as partnerships on the federal level.
- Sole proprietorships are subject to the income tax. They can however, opt for taxation as a corporation if they are regarded as a one-person company.

The farmers (except C corporations) can opt for corporation tax or income tax, however they are bounded by their choices for five years. There is no legal definition or enumeration of the different kinds of incomes in the IRC. All kinds of income less their costs are regarded as taxable income, including capital gains, which are connected with it. These are however, separately determined and taxed (Parsche et al. 2000, p. 197).

Income from farming and forestry does not represent a separate kind of income. They are determined and taxed like income from other businesses of a comparable size apart from some detailed regulations regarding farm income. National subsidies for soil, groundwater or environmental protection, care for wild animals or forests is sometimes tax-free for the farmers. Consumption of farm products by the farm family is tax-free, however, connected costs are not deductible.

As for profit accounting both enterprises and individuals paying corporation tax or income tax are obliged to keep a kind of balance, but the law does not prescribe any special record keeping method. Profit accounting allows the following three methods: i) cash method, ii) accrual method and iii) crop method. The C corporations with more than US$ 1 million in annual turnover are compelled to use the accrual method. S and C corporations with less than US$ 1 million in controllable gross receipts can use the cash method. So-called family-farm corporations with yearly taxable gross incomes less than US$ 25 million can also use the cash method. Also a combination of methods is possible with certain restrictions. In general the cash method is preferred as most farmers find it easier to keep cash method records.

With reference to The Taxpayer Relief Act of 1997 sole farmers and partnerships may also form three years average income whereas C and S corporations, unincorporated firms and other self-employed persons are excluded from it. The rule of income averaging is only available for farmers and only on farm income. If a farmer elects to use the averaging rules, he has to use the rules for minimum three years before he can return to assessment on a yearly basic. Before 1986 income averaging was available to both farmers and all other taxpayers who satisfied certain basic requirement. This legal right balancing the income over several years was totally repealed in the period 1986–1997, also for the farmers (Durst & Monke 2001, p. 21).

By the *accrual method* the gross income from farming is computed by adding a) income from sale of cattle and agricultural products, b) year end balance of slaughter cattle and agricultural products if desirable also animals for breeding, work or milk, c) different irregular farm incomes such as payment for breed services letting out agricultural machinery and land, d) taxable subsidies and governmental help and e) gross income from other sources such as oil tax refunding, payment for work at cooperatives or sale of fire wood etc.
From the gross income is subtracted the balance at the beginning of the tax year as well as initial cost of cattle and agricultural products purchased during the tax year, if they were intended for resale. With the accrual method an inventory is mandatory comprising all semi-finished or finished products in particular grain, silage, hay, cotton, tobacco etc. whether meant for sale, feeding or for seed. The balance is assessed on the cost basis or if it is lower, the market price less the direct marketing or sales cost i.e. the so-called farm price method. Living cattle may also be assessed at a unit livestock price. Special rules apply for a combination of evaluation methods. Standing arable crops fruit or fiber plants are not assessed if their ripening time is less than two years and independent of evaluation method the writing up must follow the attributed manufacturing or raising cost.

The deductions comprise the most common costs such as wages and salaries for employees, seasonal workers and contractors, including different employer contributions but mandatory and voluntarily life or accident insurance of the employees. The expenditure for family members are considered if a genuine employer–employee relationship exists. Expenditures to be partly assigned to income achievement and personal costs such as electricity, gas, water, telephone are proportionally reduced. Expenditures for repairs are deductible if they do not represent activation acquiring improvements or extensions. Soil improvement due to fertilizing may be directly deducted or activated. Taxes for fortune, land as well as road taxes for agricultural vehicles are fully deductible and so are usual agricultural contributions for insurance against fires, storm and theft. Rents paid off in agricultural products are not deductible. For cars used in agricultural production a lump sum of 31 cents per mile (1999) can be deducted. All sorts of transportation costs, accommodation, food supply, laundry, telephone etc. are considered, for business meals and food supply on journeys usually 50 percent are deductible.

Generally the farmers can charge as an expense or activate expenditures for measures against soil erosion and ground water protection reduced by governmental subsidy payments. Ditching of humid areas or building of wells or water systems must be activated. As for not depreciable assets only expenditures for land and soil can be directly deducted. Assets with a production period of more than two years, i.e. buildings for agriculture or forestry and expenditures for production of Christmas threes have to be activated.

The following depreciation methods apply: Accelerated Cost Recovery System (ACRS) (start-up 1981–1987), Modified Accelerated Cost Recovery System (MACRS) (after 1986), both of which concerns procedures for accelerated writing-off. In MACRS the depreciation period is set somewhat shorter than economic (useful) lifetime for instance 5 years depreciation period for items with 4–10 years economic life. The MACRS further differentiates between the General Depreciation System (GDS) with geometric degressive depreciation and the Alternative Depreciation System (ADS) with linear depreciation. In some cases ADS is mandatory, in others is it voluntarily. There are specific depreciation periods for different items under each system and the period for agricultural property are shown in table 3.1.

Generally it is possible to change between geometric and linear depreciation (Parsche et al. 2000, p. 206). The depreciation in each tax period depends upon the original acquisition or manufacturing costs on an unadjusted basis. Improvements are considered as separate property assets. The so-called half-year convention subordinates the assets to be acquired exactly in the middle of the year, in the acquisition as well as in the expiration year half the depreciation rate is employed.

There are also separate rules for immediate depreciation of livestock, pasture fences, stables in livestock and greenhouses in horticultural enterprises. If the articles are not more than 50 percent agriculturally used or not for that purpose acquired, immediate depreciation is not possible. In 2000 the total amount of immediate depreciation was US$ 20,000 a year. If the total sum exceeds US$ 200,000 the maximum limit is reduced by US$ 200,000. The size of immediate depreciation may not exceed certain limits of the net income of self-employed, however it is possible to postpone not used depreciations to the nest tax year.

Table 3.1 Depreciation for agricultural property items in the USA

Property item	Depreciation period in years	
	GDS	ADS
Commercially used buildings	39	40
Agricultural buildings	20	25
Drainage, wells	15	20
Agricultural and garden plants (stables, greenhouses)	10	15
Truck (unloaded weight over 13,000 lbs.), airplanes	5	6
Cars, trucks (unloaded weight below 13.000 lbs.)	5	5
Tractors	3	4
Cotton harvesting machine	7	12
Agricultural devices and machines, pasture fences etc.	7	10
Wood harvesting machines	5	6
Goats and sheep (breed)	5	5
Pigs	3	3
Breed and workhorses (12 years or less)	7	10
Breed and workhorses (older than 12 years)	3	10
Racing horses (older than 2 years)	3	12
Cattle (breed and milk)	5	7
Fruit and nut trees, vines	10	20
Office equipment and furniture	7	10
Computers	5	5

If the requirements for immediate depreciation are not met the property item is depreciated according to the rules. For a truck acquired in 1999 and used to a 100 percent in the enterprise US$ 3,060 can be taken off the first year followed by US$ 5,000 the second year and US$ 2,950 for the third year and US$ 1,775 for all later years. This upper limit is multiplied by the degree of operational use. For certain low pollution vehicles acquired between 1997 and 2005 the limits are three times higher. The cost of gas, electricity, hydrogen or alcohol for driving are not subject to the depreciation limits and associated service or loading stations can be immediately depreciated up to US$ 100,000.

If profit accounting takes place in accordance with the *cash method* the gross income as different from the accrual method arises as sum of the following positions: a) income from sale of own agricultural products, b) profit (income less initial costs) from sale of livestock or other commodities purchased for resale (sale of breed animals or workhorses not held for the purpose of resale are possibly capital gains) and the positions c), d) and e) of the accrual method. Farmers reporting income in accordance with the cash method do not have to make an inventory and cannot make an inventory change valid for taxation without an appropriate payment. Prepayment for feeds, seeds, fertilizers or similar consumer goods typical for an agricultural enterprise is possible, if they are real payments and not deposit of security. Generally prepayments may not exceed 50 percent of all for taxation operating expenditures in the tax year. Special rules apply for surplus feed not used due to an epidemic illness. Whereas initial costs of livestock or other articles for resale can be deducted there are some exceptions for poultry, seeds and young plants.

Taxable income may also be determined on the basis of the *crop method* whereas determination in accordance with *overall values* (cadastral system) does not apply.

Profits and losses from sale of fortune articles are (depending upon classification) treated as normal income or in accordance with the special rules for *capital gains* and losses. For capital assets there are gains or losses independent of the duration of the ownership. With depreciable assets, operationally used real estates and not harvested agricultural products kept for more than a year, there will be capital gains. The resulting losses are, however, considered in the context of the regular income tax. As for breed and workhorses, cattle and milk cows the time limit is two years, in case of shorter ownership the profits are considered as regular income.

In principle inheritances are regarded as capital gains even when it is sold within a year after the transaction. Donations and other live transfers are treated as either normal income or as capital gains in accordance with special rules. It is taken into consideration the time of ownership before the transfer. First short term capital gains are settled against short-term capital losses, the same applies for long-term capital gains and losses. Afterwards the two are balanced, and if short term outweighs the surplus is considered as normal income, if long term outweighs the gain is separately treated. If losses are larger than gains a yearly total of US$ 3,000 can be settled against other income and further losses can be brought forward to the following years.

By sale of wood long term capital gains or losses are only possible if the wood sale does not belong to the usual farm business. The relevant profit/loss is the difference between the proceeds of the sale and the book value of the wood. For farmers using the cash method there are no duty to activate animals and for plants activation is required only when the ripening time is more than two years. On request it is possible not to activate plants as well (apart from i.e. citrus-trees). The costs are thus deductible directly and the profit from sale will be the selling price less the sales costs.

Already taken deductions (except for buildings) must be retrieved in case of a sale. If the sales costs lie over the acquisition or manufacturing costs the difference is taxed as long run capital gains and the deductions are taxed as normal income. If the sale price lies over the book value and under the acquisition costs, the difference between sales value and book value is taxed as regular income. If the sales costs are below the book value there is a long-term capital loss that can be settled against long-run capital gains.

To *determine the total income* for a taxpayer the income from all different sources are added. The adjusted gross income, resulting from the deduction of costs of income achievements and other deductions, results in taxable income after further deducting for standard or itemized deductions. There are certain restrictions to even losses between tax periods; losses on passive activities cannot be reconsolidated against gains from active ones. An operating net loss can generally be balanced with positive income two years back and 20 years forward. Losses from agriculture can be reconsolidated backwards as far as five years whereas property losses due to natural catastrophes and losses of small agricultural and commercial enterprises in distressed areas may be reconsolidated three years backwards.

To reach the adjusted gross income, maintenance payments to spouse or to divorce are deducted, however not to children. For self-employed and thus for farmers, contributions for nationally promoted old age pension (self-employed retirement plan) for up to 25 percent of the profit or a maximum of US$ 30,000 may be deducted. Up to 50 percent of the compulsory contributions of self-employed (including farmers) to the national social security (self-employment tax) can also be set off. As for the contributions to private health insurance (also for family members) or national insurance Medicare B, 60 percent (1999–2001), 70 percent (2002) and 100 percent (from 2003) can be subtracted. In addition can cost of relocation be deducted, however travel costs are not considered.

To reach taxable income a *standard deduction* at the value of (1999 conditions) is set off:

- US$ 4,300 for individuals
- US$ 6,350 for individuals with households
- US$ 7,200 for married with common assessment and widows/widowers.

An additional deduction of US$ 3,600 for couples during separation or for covering certain individual situations (itemized deductions like interest, extraordinary losses, disease costs, donations to charitable purposes, wealth taxes on real estate and other fortune to the state or the municipality, state and local income taxes and environmental taxes).

Married couples may be assessed separate or together. Children under the age of 14 are assessed separately with their own income and fortune. Fortune incomes of children 13 ages or younger are reduced by expenses (at least US$ 650) and the first US$ 650 is taxed at an own rate, the surplus with the marginal rate of the parents. There are also separate tariffs for spouses, individuals and individuals with a household with dependent persons. If the corrected gross income is less than certain limits (US$ 126,633 for individuals, US$ 189,950 for married with common assessment and widows/widowers, US$ 158,291 for individuals with households and US$ 94,977 for married with separate assessment) the tax person as well as spouse, children below 19 years and other dependent family members obtain a personal free allowance of US$ 2,750. For each US$ 2,500 that the income exceeds these amounts the personal free allowance is reduced by around 2 percent (all amounts refer to the 1999 tax year). (Parsche et al. 2000, p. 214–215).

The *income tax rate* for different intervals is shown in table 3.2. Since 1989 the intervals have been regulated in accordance with the consumer price index.

Table 3.2 Tax rate 1999 of the federal income tax in the US

Income 1999 in US$				Marginal tax rate
Individuals	Married, common assessment or widows/widowers	Married, separate assessment	Individuals with households	
25,750	43,050	21,525	34,550	15.0%
62,450	104,050	52,025	89,150	28.0%
130,250	158,550	79,275	144,400	31.0%
283,150	283,150	141,575	283,150	36.0%
Over 283,150	Over 283,150	Over 141,575	Over 283,150	39,6%

If the controllable income (including capital gains) lies in the lowest interval, capital gains are taxed by 10 percent. If the whole taxable income lies in the second interval and the regular income (exclusive capital gains) in the first interval, the capital gains of the difference between the regular income and the interval limit is taxed at 10 percent and the remaining capital gains at 20 percent. If the regular income (i.e. without capital gains) lies in the second interval or above, capital gains are taxed at 20 percent. The total income tax is the sum of taxes on capital gains and on regular income.

Self-employed and farmers can deduct a business *tax credit* from the computed tax. The credit is composed of deductions for the production of fuel from alcohol, for acquisition, production and renovation of subsidized low-rent housings, the production of electricity from renewable sources, measures for the more intensive use of domestic sources of oil, for employment of employees from structure-weak areas, handicapped and Indians.

As *investment tax credit* the following are accepted:

- 10 percent of the activate able costs for reforestation of used forest areas, yearly a maximum of US$ 10,000, surplus costs can, however, not be charged to the preceding or following years. The credit is independent of whether the costs were activated or depreciated immediately.
- 10 percent (20 percent if built before 1936) of the renovation or restoration costs of architectural monuments.
- 10 percent of certain investments to extract energy from sun or geothermal or other unconventional sources, acquisition of electric vehicles and the expenses for federal consumer tax on mineral oil for agriculture.

Private persons can further deduct the following tax credits:

- child and dependent care credit, 30 percent of the cost of care within a maximum of US$ 2,400 for one child and US$ 4,800 for two or more children; if the income exceeds US$ 10,000 only 20 percent of the cost of the care are deductible.
- deduction of tax for persons over 65 years and handicapped, depending on the assessment status and the received social security benefits.
- deduction of tax for independent and non-independent with small income.

- mortgage interests on residential property for borrowers with low incomes.
- retained taxes at source for wage tax and capital income tax.

In general persons must pay a minimum tax (alternative minimum tax), if this exceeds the regularly determined income tax debt.

To determine the *state income taxes* the assessment basis is taken over by the individual state. However, since no clear regulations of the income exist on the level of individual federal states, it can lead to delimitation problems and double taxation on that level (Parsche et al. 2000, p. 217–218). A comparison of some of the most important agricultural states in the US, (California, Iowa, Kentucky, Minnesota, Missouri, Ohio and Oklahoma) reveals substantial differences in personal and other deductions as well as income intervals and tax rates in the states. In addition some states also impose surtaxes. (Parsche et al. 2000, p. 217–218). Most states use a federal adjusted income as basis; however, Minnesota uses the federal taxable income unadjusted. Tennessee on the other hand levies income tax on interest and dividends only while Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming do not levy income tax at all. In larger cities use is also made of local income and corporation taxes, in rural areas they are not important.

3.1.3 Property taxation

On the federal level no real estate taxes are raised, however, in most of the states there are either real estate taxes or similar property taxes. The municipalities or the federal state specifies the basis of assessment and the tax rate, but since there are 48 states and around 87,000 municipalities in the US it is impossible to examine all the regulations (Parsche et al. 2000, p. 220).

In for example South Carolina the property tax is the primary source of tax revenue for the municipalities, the tax objects are agriculturally used fortunes, means of production for commercially or industrial enterprises, supply systems, railway lines, airlines, pipelines, other real estates and mobile property (table 3.3). The rates of assessment are specified by the federal state.

Table 3.3 Rates of assessment property tax in South Carolina

Fortune class	Assessment basis	Assessment basis
Agriculturally used real estates of single farmers,	Value in use	4.0%
unincorporated firm, finance companies		6.0%
Residential buildings	Market value	4.0%
Production fortune (Real estate)	Market value	10.5%
Other real estates	Market value	6.0%
Mobile fortune (commercially and privately used)	Book value	10.5%
Supply systems (Water and power supply)	Market value	10.5%

The value in use of agricultural properties is computed from expected yield of agriculturally used properties. This value will generally be lower than the market value and the tax preferential treatment of agricultural properties is further strengthened by the lower rates of assessment. The evaluation of production fortune, supply systems, railroad lines etc. take place by the Ministry of finance whereas the responsible county assessor assesses all other fortune articles. For agricultural enterprises all agricultural products, livestock, agricultural machinery and greenhouses, exempted thus only the land and the associated buildings, are subject to the tax.

There are, however, tax exemptions for other industrial concerns, new production plants and extensions of existing plants in the value of at least US$ 50,000 are free for five years likewise inventories of producers and dealers as well as plants for reduction of noise, water and air pollution. Companies in South Carolina can receive a lasting reduction of the property tax if they invest a certain minimum amount and create a certain number of full time jobs.

Computations of property taxes in 1994 for agricultural real estates in the different states (Parsche et al. 2000, p. 221) reveals that they range from US$ 0.14 (Alabama) to US$ 2.00 (Wisconsin) per US$ 100 in market value of the property. Measured per acre the property taxes range from US$ 0.40 (New Mexico) to US$ 56.75 in Rhode Island.

3.1.4 Social security system

The Federal tax system also includes *taxes for Social Security* both for employees and self-employed. The rules for social security taxes are the same for farmers and other self-employed. Social security taxes include two components:

- Pension (the old age, survivor and disability) (OASIS)
- Medicare hospital insurance (HI).

Social security tax burdens have risen dramatically over the last decades because of increases in both the tax rate and the amount of income subject to taxation (Durst & Monke, 2001, p. 28). The rate increase started in 1983 and the rate has been 15.3 percent since 1990. The rate is comprised of 12.4 percent OASIS and 2.9 percent HI. All incomes from self-employment are subject to the MI portion, but only the first US$ 84,900 of earned income is subject to OASIS.

In spite of the sharp increase in tax rates and in the maximum taxable earnings, total self-employment taxes paid by farmers have not increased nearly as fast. In 1996, farmers paid a total of US$ 1.8 billion in self-employment taxes. Durst & Monke (2001, p. 29) explain the relative weak increase in farmers' self-employment taxes in this way:

> *"The primary reason that total self-employment taxes have not kept pace with the increase in tax rates is the drop in the number of farms reporting a farm profit. IRS data indicate that each year since 1980 farmers in the aggregate have reported negative net farm income for taxes. The total amount of net farm losses increased annually from 1990 through 1996, reversing a recovery in farm income that started in 1984. The proportion of farm sole-proprietors reporting a net farm profit on schedule F has been declining with only 33 percent of farms reporting profits in 1996, compared with 44 percent in 1989.The reporting of losses for tax purposes varies by type of farm. While about 80 percent of farms with sales*

over $100,000 report a profit, only about 25 percent of retirement and lifestyle/other farms report a profit and pay self-employment taxes."

3.1.5 Other taxes and fees

The current *Federal Estate and Gift Tax* (FEET) was enacted in 1916. The tax laws have changed several times, last in connection with the Taxpayers Relief Act of 1997. The system for the Federal estate and gift tax is a somewhat special system applying a unified tax rate structure and a cumulative lifetime credit to gifts and transfers of money and other property at death (Durst & Monke 2001, p. 31).

According to Durst et al. (2002) farmers and owners of other small businesses hold significant amounts of wealth in the form of business assets and are thus likely to be subject to the FEET. For transferring an estate valued at US$ 1 million or more, an estate tax return have to be filed in, however, only once in a while federal estate taxes are paid because large amounts are exempted.

In the Taxpayers Relief Act of 1997 several important changes to the estate and gift tax were made:

- the unified credit was increased,
- the deduction for qualified family-owned was enacted,
- interests rate on the installment payment was reduced.

Because of these changes the farmers are expected to save more than US$ 150 million of the estimated US$ 500 million in annual payments. A drawback with the changes is that the new system has become more complex.

The unified credit applies to both the gift tax and the estate tax. The donor has to subtract the credit from any gift she or he forwards. Any unified credit the donor uses against hers or his gift tax one year reduces the amount of credit that can be used against the tax in later years. The total amount of credit used against a donors gift taxes alive reduces the credit available to use against her or his estate tax.

From 1987 the credit was unchanged at US$ 192,800 until it rose to US$ 345,800 in 1998. This amount will be unchanged for some years ahead (table 3.4). The credit amount of US$ 345,800 eliminates taxes on a total of US$ 1 million of taxable gifts and taxable estates (table 3.4).

The rate of estate and gift tax starts at 18 percent for taxable estates over US$ 11,000, but the effective rate starts at a rate of 41 percent. The tax rate for 2002 rises to 50 percent on taxable estates above US$ 2.5 million.

Table 3.4 shows the unified credit and the applicable exclusion amount for the calendar year in which a gift is made or a decedent dies.

Table 3.4 Gift and estate tax. Unified Credit and Applicable Exclusion Amount in US$

Year	For Gift tax purposes		For Estate tax purposes	
	Unified credit	Applicable Exclusion amount	Unified credit	Applicable Exclusion amount
2002 and 2003	345,800	1,000,000	345,800	1,000,000
2004 and 2005	345,800	1,000,000	555,800	1,500,000
2006–2008	345,800	1,000,000	780,800	2,000,000
2009	345,800	1,000,000	1,455,800	3,500,000

Source: IRS 2002 Publication 950

A separate annual exclusion applies to each person to whom the donor makes a gift. For 2002 the annual exclusion is US$ 11,000. Married persons can both of them give this amount to the same recipient. There are no limits as to how many individuals a donor can give such tax-free gifts; and such gifts are not to be included in the applicable exclusion amount. From 2002, the US$ 11,000 annual exclusion will be inflation adjusted.

As maintained in this quotation by Durst et al. (2002, p. 31), there are three additional rules that reduce gift and estate tax in small family business; special valuation of farmland, deduction for family-owned businesses and installment payment of estate taxes:

"The impact of Federal estate and gift taxes on the farm sector was an important issue during the late 1970's. During that period, the appreciation in land values, the increase in average farm size, and the rising investment in farm machinery and equipment increased farm estate values and taxes. Over the years, congressional concern that the farm sector's increasing estate and gift tax liability might cause the break-up of some family farms and other small businesses led to the enactment of a number of targeted provisions to provide tax relief to farmers and other small business owners. Targeted provisions include the special use-valuation of farmland, the installment payment of estate taxes, and a new deduction for family-owned business interests."

Generally the value of a property for estate tax purposes is the fair market value at the date of death. For real property devoted to farming or other closely held business, special rules apply. The value of the farm is set to the farm's use value as a farm.

To qualify for this use value, the property must:

- be transferred to a qualified heir,
- must have been used as a farm for five years during the last eight years,
- the decedent or a member of the decedent's family must have participated in the farm business,
- the value of the qualified real property must equal at least 25 percent of the estate, and
- the combined value of real and other business property must be at least 50 percent of the gross estate.

For most farms the special use value is 40 to 70 percent lower than the fair market value. The maximum reduction of the fair value is for 2002 determined to US$ 820,000.

The reduction in the estate tax due to farm use value can be considered as a conditional tax exemption. A new computing of the estate tax is necessary if the whole or a part of the property is sold to a non-family person or to a company within 10 years of the decedent's death. A new computing is also necessary if the property ceases to be used for farming within the 10 years limit.

In amendment to any benefits from the special farm use value and the unified credit, the estate tax can be reduced or discontinued because of a special rule for family-owned businesses. Different rules decide whether a family-owned business is qualified to the deduction or not. From the beginning of 1998, the value in a qualified family-owned business interest can be reduced by US$ 675,000. The total amount of this provision and the unified credit increases is limited to US$ 1.3 million. Durst et al. (2002) claims that a great many farms and closely held business property can be transferred free of estate tax because of the unified credit, the special value for farm property and the deduction for family-owned business.

Farmers and other small business owners often have a large portion of the property in land and other relatively illiquid business assets. This can be a problem for the payment of the estate and gift tax. While the tax generally must be paid within nine months of the date of death a special provision for farmers and other small business owners allows installment payment of the tax. When at least 35 percent of an estate's value is a farm or a closely held business, the additional payment period is fourteen years. The last nine years are interest free whereas the rate for the first five years is two percent (four percent before 1998) on the first US$ 1 million in taxable value (i.e. above amounts exempted by the unified credit).

> *"The amount of estate tax eligible for the 2-percent interest rate is scheduled to increase from US$ 153,000 in 1997 to US$ 435,000 for 2002. This provision, combined with the increase in the amount of property that can be transferred tax free, has greatly reduced the liquidity problem that some farmer heirs might otherwise experience as a result of Federal estate taxes." (Durst et al. 2002)*

The Federal Estate Tax will gradually be reduced and completely repealed in 2010 (Durst et al. 2002). The increase of the unified credit to US$ 1 million and the lowering of the top rate from 55 to 50 percent start the reducing in 2002. In 2002 the farmers are expected to save more than US$ 150 million of the estimated US$ 500 million paid annually. The gift tax will likely be in existence in a more moderate form with a US$ 1 million exemption amount and a tax rate equal to the top individual income tax rate (about 35 percent).

Sales tax is a state and local consumption tax. Both the rules and the rates vary between the states, but the rate varies between 4.0 and 7.0 percent in all states except Alaska (table 3.5). In Alaska the rate is 0 and the sales tax is thus a local tax. In the other states total sales tax, including both state and local tax, is between 4.0 and 9.75 percent.

In this report only the rules for the sales tax in Minnesota (Minnesota Department of Revenue, 2001) will be referred to in more detail. The rate of the state sales tax is 6.5 percent and no county or city in Minnesota has local rates of sales tax exceeding 1 percent. The maximum total sales tax rate in Minnesota is thus 7.5 percent. The local tax applies to the same items as those taxed by Minnesota state sales and use tax law. The Minnesota Department of Revenue currently administers and collects the local sales and use taxes.

Table 3.5 Comparison of State and Local Retail Sales Taxes in the US. July 2001

	Food Items [1] Taxable (T) Exempt (E)	State Rate	Maximum Local Rate [2]	Maximum State/Local Rate [2]
Alabama	T	4.00	5.00	9.00
Alaska	T	---	6.00 [4]	6.00
Arizona	E	5.60	3.00	8.60
Arkansas	T	5.125	3.00	8.125
California	E	5.75	2.50	8.25
Colorado	E	2.90	4.50	7.40
Connecticut	E	6.00	---	6.00
District of Columbia	E	5.75	---	5.75
Florida	E	6.00	2.50	8.50
Georgia	E	4.00	3.00	7.00
Hawaii	T*	4.00	---	4.00
Idaho	T*	5.00	2.00	7.00
Illinois	T**	6.25	2.50	8.75
Indiana	E	5.00	---	5.00
Iowa	E	5.00	2.00	7.00
Kansas	T*	4.90	3.00	7.90
Kentucky	E	6.00	---	6.00
Louisiana	T [3]	4.00	5.50	9.50
Maine	E	5.00	---	5.00
Maryland	E	5.00	---	5.00
Massachusetts	E	5.00	---	5.00
Michigan	E	6.00	---	6.00
Minnesota	E	6.50	1.00	7.50
Mississippi	T	7.00	---	7.00
Missouri	T	4.225	4.00	8.225
Nebraska	E	5.00	1.50	6.50
Nevada	E	6.50	0.75	7.25
New Jersey	E	6.00	---	6.00
New Mexico	T	5.00	2.1875	7.1875
New York	E	4.00	4.50	8.50
North Carolina	E [5]	4.00	2.00	6.00
North Dakota	E	5.00	2.00	7.00
Ohio	E	5.00	2.00	7.00
Oklahoma	T	4.50	5.25	9.75
Pennsylvania	E	6.00	1.00	7.00
Rhode Island	E	7.00	---	7.00
South Carolina	T**	5.00	1.00	6.00
South Dakota	T*	4.00	2.00	6.00
Tennessee	T	6.00	2.75	8.75
Texas	E	6.25	2.00	8.25
Utah	T	4.75	2.00	6.75
Vermont	E	5.00	---	5.00
Virginia	T**	3.50	1.00	4.50
WASHINGTON	E	6.50	2.30	8.80
West Virginia	T	6.00	---	6.00
Wisconsin	E	5.00	0.60	5.60
Wyoming	T*	4.00	2.00	6.00

[1] Food purchased for consumption off-premises.
[2] Highest local rate known to be actually levied by at least one jurisdiction. Includes local taxes for general purposes and those earmarked for specific purposes (e.g. transit). Taxes applying only to specified sales (e.g. lodging or meals) are excluded.
[3] Exemption has been temporarily suspended for the state tax; food remains subject to local taxes.
[4] Alaskan cities and boroughs may levy local sales taxes from 1% to 6%.
[5] Food except from state tax, but subject to local taxes.
* Income tax credit allowed to offset sales tax on food.
** Food taxed at lower rate.

Source: "State Tax Guide," Commerce Clearing House, Inc.; Federation of Tax Administrators. The table was compiled by the Washington Dept. of Revenue. Updated 10/18/2001, from state websites and input from state revenue/tax agency responses.

Several goods and services used in agricultural production are not subject to sales tax:

- Animals; including also fur-bearing animals
- Horses; including also pet-horses
- Feed for animals (not feed for pets)
- Veterinarian services (not for pets)
- Chemicals
- Fuel and electricity (not including fuel and electricity used for heating or lighting farm buildings or to operate a yard light)
- Petroleum products
- Packing materials (including not returnable containers used to package non-food items)
- Plants and seed used in agricultural production, but not in home vegetable gardens, lawns or flowers
- Machinery and equipment
- Building materials. Material and supplies used to construct, repair or maintain farm buildings, residences, greenhouses etc., are taxed at 6.5 percent.
- Different services.

Farm machinery is exempted from the sales tax. New farm machinery has been exempted since July 1, 2000 whereas used farm machinery has been exempted since 1994. Most repair and replacement parts (except tires) have been exempted since 1985. Hobby farms, including horse hobby farms, must pay sales tax for farm machinery unless the farm is producing products for sale.

The *use tax* for business complements and is quite similar to the sales tax. Use tax and sales tax rates are identical. Use tax applies at business purchase, lease or rent, taxable items or services used in the business without paying sales tax to the vendor. Use tax may be due when items are taken into the State or when items are taken out of inventory for a taxable use. As for the sales tax it can be collected locally in different cities and counties.

The Petroleum tax is a state tax and different rules apply in the different states. The rules reported here have reference to Minnesota. Motor fuels and other petroleum products are subject to either petroleum tax or sales and use tax (never both).[1] Diesel fuel (not gasoline) to be used for non-highway purposes is dyed red at the terminal to show that no federal petroleum tax has been levied on the fuel. The fuel is also sold without the state petroleum tax, since it is not intended for use on highways, except for government use.

Ordinary sales and use tax is due on petroleum used both on highways and elsewhere. Petroleum used in agricultural or industrial production is exempted from both petroleum tax and sales or use tax.

The exemption applies to fuel used among others:

[1] Effective July 1, 1997, sales of gasoline for farm use, delivered to on-farm bulk storage, may be sold tax-free.

- To operate farm equipment
- To operate manufacturing equipment
- To operate logging equipment
- To improve agricultural land.

3.1.6 Evaluation and significance

According to Pascour (1990) the federal tax laws in the US have historically extended special treatment to individuals engaged in agricultural production. The taxation in the US is on three levels:

- Federal
- State
- Local.

The federal system of taxation has gone through different changes during the last decades. In principle we can divide the period into three parts:

- The time before the middle of the 1980's,
- The time between the middle of the 1980's and the middle of the 1990's,
- The time after the middle of the 1990's.

Different research examining the first period concluded that: "*special agricultural tax preferences reduced the tax burden on farm income*" (Davenport et al. 1982). Individuals with a substantial farm income had a substantially lower tax burden than other taxpayers without farm income. A weakness with the study is that the comparison was between farmers and all other taxpayers and not between farmers and other business owners.

The tax benefits were prior to 1986 also available to non-farm investors who qualified as farmers for income tax purpose. Non-farmers and farm losses for tax purposes exceeded farm profits often used consequently farming as a tax shelter for several years prior to the Tax Reform Act (TRA) of 1986. However, the TRA curtailed the tax shelters and significantly reduced the attractiveness of investment in agriculture for non-farm investors (Pascure, 1990).

In 1981 the trend towards lower marginal tax rates started, over the following years making the income tax less progressive. In the second period the differences in tax rates for farmers and non-farm taxpayers *"were also reduced by the elimination of income averaging, the capital gains exclusion, the investment tax credit, and other important farm tax provisions"* (Durst & Monke 2001, p. 36). The trend starting in 1981 was reversed in 1993 increasing the maximum marginal tax rate from 31 to the current 39.6 percent.

The 1986 TRA generally increased the depreciation period for capital assets, but increased depreciation in the first years by changing the method of depreciation. The amount of newly acquired depreciable property was increased from US$ 5,000 to US$ 10,000. The depreciation period for larger items continue to be quite short compared to the expected lifetime of farm property, i.e. farm machinery seven years, and single-purpose agricultural buildings have a 10 years recovery period.

Some expenses can be fully deducted in the year of purchase like cost of lime and fertilizer enriching the land for more than one year, soil and water conservation expenditure on USDA–approved conservation projects.

A change in the value of a capital asset is not treated as income for tax purpose until the asset is sold. Before the TRA of 1986 capital gains were taxed at lower rates than ordinary income (a maximum of 20 percent). Since 1986 capital gains are taxed as other income, which significantly reduces the benefits of agriculture as a tax shelter. The federal estate tax is computed on the basis of agricultural use value instead of market value and farmers and small businesses are given an extended time to pay the tax in which the interest rate is well below the market rates. As for corporate farming there are some tax advantages and some disadvantages. Profits can be accumulated and not paid out at lower tax rates than if earned by individuals because corporate tax rates are lower than individual rates at lower income levels.

Farm transfers can be made more easily as shares of stocks can be traded without dividing the farm. Some fringe benefits can be deducted by the corporations and need not be included in the gross income of the shareholders. The main disadvantage of corporate farming is that income is taxed twice and the expense of keeping records which is mandatory.

Table 3.6 show that totally farmers paid US$ 39.8 billion in the direct taxes in 1996[2]: These taxes are levied on nearly US$ 122 billion in farm and non farm income reported by farm households for Federal tax purposes.

Table 3.6 Federal, state and local direct tax for farm households in the US 1996

Federal, state and local direct tax	Tax in billion US$
Federal income taxes:	19.2
Social Security and self-employment taxes[1)]	10.2
State and local property taxes	5.2
State and local income tax	4.7
Federal estate taxes	0.5
Total direct taxes	39.8

1) The social security tax includes US$ 1.8 billion in self-employment taxes on farm income and US$ 8.4 billion for both the employer's and employee's share of the payroll tax on wages.

Source: ERS (2001).

Since 1996 the changes in the tax rules indicate that farmer's Federal income tax has decreased by about 10 percent on a constant income basis. Also the estate tax has been reduced as a result from the changes in the rules[3].

Durst & Monke (1998) claims that for about 80 percent of the farmers the reported income is less than US$ 60,000 and the average effective federal income tax rate is less than 10 percent. As in several other countries the social security taxes in US are rapidly growing and according to Durst & Monke (1998) farmers earning less than US$ 60,000 actually paid more in social security taxes than in Federal income taxes.

[2] 1996 is the last year for which complete tax data are available.

[3] The Federal Estate Tax will completely be repealed in 2010.

Since 1997, the tax system has given both farmers and other self-employed and tradesmen different benefits such as increased self-employed health insurance deduction, income averaging (only farmers), expanded capital expensing and reduced tax rates for capital gains (Durst & Monke 2001, p. 36).

In the US the most important tax advantages for agriculture are cash accounting and deductibility of certain capital expenditure. The main advantage of using cash accounting is caused by the mismatch of incomes and expenses in different tax years since it is always beneficial to receive a benefit sooner rather than later. The use of cash accounting by farmers is limited to those with gross receipt below US$ 1,000,000, however, corporations engaged in certain types of farming are exempted from this restriction.

In their study of federal tax policies in general and for the agriculture sector in particular Durst & Monke (2001, p. 48) concludes:

"Tax legislation enacted during the decades of the 1980's and 1990's has resulted in a significant shift in Federal tax policies. Despite increase in marginal income tax rates and targeted relief in recent years, the Federal income tax system contains a broader base and lower marginal income tax rates with fewer opportunities to shelter income through exclusions, deductions, and credits compared with the system that existed two decades ago. Federal estate and gift taxes are of continuing concern, despite large increases in the amount of property that can be transferred free of tax. Social security and self-employment taxes impose a much greater burden and play a greater role in investment and management decisions due to sharp increases in tax rates and the amount of income subject to such taxes.

Although the implications of this new structure are less clear and research regarding the impact of these policies is somewhat limited, a number of implications of such policies for the agriculture sector have been established:

- *The Federal income tax system has become more progressive as a result of an expanded earned income tax credit, increased marginal tax rates, and other changes, while overall progressivity continues to be reduced by Federal payroll taxes, primarily social security and self-employment taxes.*
- *Federal income and payroll tax policies continue to favor capital investment over labor especially for those able to currently expense a large portion of their capital investment, but the availability of investments with negative effective tax rates is limited.*
- *Federal tax policies affecting land use, conservation, and preservation are environmentally friendlier due to reduced tax benefits for certain harmful practices and target incentives in support of farmland conservation and preservation efforts.*
- *Federal income, estate, and gift tax policies that provide favorable treatment to farmland relative to other assets continue to reduce the supply and increase the demand for farmland, exerting upward pressure on values.*
- *Federal tax policies continue to result in increased resource use in agriculture contributing to grater farm output and lower prices.*
- *Federal income, estate, and gift tax policies continue to support trends in an increase in the number of very small and very large farms.*
- *Proposals to increase opportunities for beginning farmers should increase the availability of land but are not expected to have a significant effect on affordability."*

3.2 Canada

3.2.1 Introduction

In Canada the federal government cover all areas of taxation unless they are not distinctly referred to the provinces in the 1981 constitution. The federal government claims income tax, corporate tax, purchase tax as well as capital tax on corporations, consumption tax and customs. The provinces claim purchase tax, land and property taxes and also income tax. By this task the provinces also provide the basis for the federal taxation and determine the different allowances. The province of Quebec represents a special case allowing the local authorities to claim an independent income tax. In the same way the municipalities, local school authorities and some special purpose authorities are allowed to claim taxes, however this is normally limited to property taxes (Parsche et al. 2000, p.173).

3.2.2 Income taxation

The residence of a person is in general decisive for his income tax liability, which normally passes for worldwide income of the resident. Natural persons with a normal stay at the residence of less than 183 days a year as well as decedent estate and guardianships, have tax liability for their inland income only. There are four sources of income, business, property, employment and office. Incomes from pensions, social security or scholarships etc. are included additionally. Some incomes such as income from lower land taxes for farmers and free barracks, free board or transport for workers to their workplace etc. are not taxable (Parsche et al. 2000, p.174–175).

Taxable income is in general the sum of income from different sources or gross income, reduced by deductions. Capital gains are calculated separately and only partly allowed for, deducted for cost of marketing. From the calculated net income personal deductions like pension contributions, old age provisions, extraordinary strains as well as different kinds of losses are deducted (Parsche et al. 2000, p. 175).

Farmers' incomes from farming and forestry operations are taxed as business income although there are some tax advantages for farmers. The farmer is the owner or tenant of the farm. The farmer may be a sole proprietor, a partnership or a company. Different kinds of enterprises (cattle, milk, fur etc.) may be operated on the farm, however pure forestry or fish farms companies are not regarded as farms. As farm income counts all agricultural products, forest products, slaughter or feeding animals sold. Further counts all hiring out of machinery or animals as well as governmental help and damage compensation payments. Own consumption of farm products by the farm family is not considered as income and connected cost cannot be deducted. Income from hiring out land, agricultural tenancy or lease is otherwise considered as property income. In case the lessor has a declared activity in managing the property the income can be considered as active income. Profit from sale of agricultural buildings or land, sale of animals kept for sport or work is not considered as income, however they are eligible to capital gains tax (Parsche et al. 2000, p. 175–177).

Sole proprietors or partnerships can choose between either book-keeping (accrual method) or the cash method whereas a combination of the two is not possible. In general the cash method is preferred of the sole proprietors whereas agricultural companies have an obligation to keep records. No special method of book keeping is prescribed, however recently the Supreme Court ruled out that the Generally Accepted Accounting Principles are to be considered as directive without any legal obligations. Although income from agriculture is considered as business income there are some differences in reporting capital gains.

In 1987 the possibility to calculate taxable income as average over several years to reduce the progressive effect of fluctuating incomes, was abolished. Instead the farmers were offered a governmental program to stabilize their income. Through the Farm Income Protection Act it is possible for the farmers to open a Net Income Stabilization Account (NISA). The NISA-account can be used for separate farm deposits (Funds 1) or deposits with support from Canada Consolidated Revenue Funds (Funds 2) as well as interests from the two. The farmer may deposit up to 3 percent of his income and are entitled to a similar amount in support from Funds 2. He can further deposit up to 20 percent of his income without support from Funds 2, however not more than CA$ 250,000 and the NISA-account may never be higher than 1,5 times the average income over the last 5 years. For partnerships as well as capital companies there are different rules in accordance with the number of part owners, activity and responsibility. The owner may withdraw money from his account when needed, however there are certain limits on the size of the withdrawals. (For more details see Parsche et al. 2000, p. 177–178).

When the farmer is filing the recorded income there are no particularities for taxation of farmers. The taxable income is income in the tax period plus or minus changes in the balance. In principle all running cost (within a reasonable size) can be deducted.

Interest costs for farm business loans (not personal loans) are in general deductible and also interest for loans on assets that are no longer part of the business assets. Taxes on wealth and land used for the income-earning activity (land, municipal and property taxes) are deductible. Assets are valued at either acquisition cost or a low market price; it can thus be the replacement value or the sales value. For capital cost allowances (CCA) the capital items are placed in certain groups with different rates ranging from four percent for stone fences, dams, greenhouses, and grain storage to 30 percent for farm tractors and machinery. Airplanes acquired before 1976 could be written off at 40 percent, the current capital allowance is 25 percent. For buildings in wood it is generally 10 percent depreciation. The terminal value can be written off if an item is no more placed in the group. By sale of items above recorded value the profit is treated as capital gains.

When the farmer is taxed according to the cash method attention should be paid to some special rules. Cost of acquiring animals for later sale can only be deducted in the same period. Income is entered with sale of the animals. By forced sale of animals for instance in a period of drought some of the income may be postponed to later periods under certain conditions. Normal subvention and different governmental programs like subvention for milk and dairy products, crop insurance, Western Grain Stabilization Act, Farm Income Protection Act or Farm Income Disaster Program can only be ascribed to the same tax year. Compensation payments from Health of Animals Act can; however, be postponed to the next year.

Farmers taxed according to the cash method have to make a mandatory inventory adjustment. If the farmer during the tax year has acquired different inventory items he has to value it at yearend, adjusted for losses. The lower of acquisition cost and fair market value (FMV) of the acquired items must be used (Canada Customs and Revenue Agency, 2002a, p. 24). For specified animals, horses or cattle as declared in provisions of the Animal Pedigree Act, there are special rules–between 70 and 100 percent of the acquisition costs. Independent of the profit or loss situation a chosen part of the products (not harvested field fruits) and acquired items are subject to optional inventory adjustment. The correcting amount from the two adjustments (mandatory or optional) is subtracted from the income in the following year thus allowing for a strong equalization of income between different tax periods.

Capital gains can arise from all material or immaterial property of operation whether private or business, yearly (rotational) as well as investment property. A certain period of owning the item is not necessary. There are no gains in case the profit is reinvested in a similar item within a certain time (roll over). The Income Tax Act has no rule for limits to capital gains, however the Canadian Consolidated Revenue Act has developed some rules of thumb. Capital gains can only be taken into consideration in connection with arrangements concerning capital items, realizing gains or losses in order to obtain income. An indication of an existing capital gain is that the item was not purchased for resale. For depreciable capital equipment capital gains surely exists, the main rule is that if the sales price is higher than the book value as well as the price of acquisition, the difference between the acquisition price and book value is taxed as income (depreciation recapture) and the difference between acquisition price and sale price is taxed as capital gains. If the sales price is somewhere between book value and the cost of acquisition, the difference between book value and sales price is regularly taxed. If the item is sold below the book value there is a terminal loss.

For farm capital equipment there is a special free amount of CA$ 500,000 over the life period for sale profit and capital gains (effectively CA$ 375,000). It must however, deal with qualified farm property from family farm corporations, family farm partnerships, agricultural land or buildings or immaterial items like milk or egg quotas. Investment items are qualified farm property when they have been the property of the farmer or his family for at least 24 months. Profits from sale of farm property according to a statement, are taxed as capital gains. By transfer of capital items to children (or widows or widowers or children-in-law), a capital gain or a lasting depreciation is not taxed before sale. Profits from sale of the farm house (inclusive one acre) are also tax-free (Parsche 2000, p. 187).

Like capital gains, capital losses also consist in property losses and the difference compared to losses on the running business activity is often difficult to spot. Capital losses can only be deducted from capital gains. Remaining capital losses can be deducted for up to three years backwards and unlimited on future capital gains (Parsche 2000, p. 187).

Losses on the running business activity can also be deducted from other positive incomes the same year or when that is not possible, for up to three years on earlier incomes or up to seven years on future incomes. For capital losses there are special rules as they cannot without more ado be deducted from other incomes. Losses from other incomes like employment can in principle be deducted, but will seldom become effective due to different limitations on the allowances. On certain other losses like hobby farming, such limitations may also become effective.

The personal allowances consists in contributions to registered pension plans or registered retirement savings plans with up to 18 percent of last years income or a maximum of CA$ 13,500. Cost of tax advisory service and interest on loans on capital for income earning are also deductible. Further are costs of nursing of children deductible if they are necessary for income earning. Completely deductible are costs for support for a divorced spouse whereas costs for support of children are considered neither by the provider nor by the receiver. Child allowances are depending on the number of children and their age as well as the net family income. For parents with a low income National Child Benefit Supplement is paid out depending on family income as well as the number of children.

The taxation rate of the basic federal income tax of the year 2000 was 17 percent up to CA$ 25,590, 26 percent between CA$ 25,590 and 59,180. Above that the rate was 29 percent. There is an individual surtax of 1.5 percent if the paid basic tax is above CA$ 8,333, however this is reduced if the tax paid is between CA$ 8,333 and CA$ 12,500. Above CA$ 12,500 there is a further increase of 5 percent.

There are several tax credits. At first is a basic personal amount (CA$ 1,147) or CA$ 592 higher for persons above 65 with taxable income below CA$ 49,134. There is further a spousal amount for couples or equivalent to spouse amount for people of equal status. From the cost of mandatory employment insurance and Canada (or Quebec) Pension Plan (CPP) 7 percent may be a tax credit. For farmers and other self-employed there is only contributions to retirement plans and the tax credit amounts to CA$ 3500 at a maximum (Parsche 2000, p. 190).

There is a tax credit (amounting to 17 percent of CA$ 4233) in case of handicaps affecting the income. In case of support of a handicapped household member can be deducted 17 percent of CA$ 2,353 plus the deductions not used by the handicapped household member. Also 17 percent of the costs for study can be deducted in the income of the partner, the parents, the parents in law or the grandparents. As for medical treatment as well as contributions to health insurance of the partner 17 percent may be deducted, however only the minimum of 3 percent of net income and what is over CA$ 1,614. Not used deductions can be transferred to the spouse or partner. If the sum of expenditure mentioned corresponds to the controllable net income and this is less than CA$ 29,591 there is no income tax to be paid (Parsche 2000, p. 191).

Natural persons have to pay a minimum tax if this is higher than the regularly determined basic tax. The difference can, however, be postponed over a period of up to seven years (Parsche 2000, p. 191).

Still further allowances can be made such as contributions to political parties (CA$ 500), deductions for investment tax (investment tax credit) such as 20 percent (within certain limits 35 percent) for specially qualified Canadian controlled private corporations) for expenditure for scientific research and experimental development (Canada Customs and Revenue Agency, 2002a), 10 percent of investment in new buildings, machinery and production plants, processing, mining industry as well as land, forestry and fishery in the structure weak areas of Canada. The deductions refer to the year to which the expenditures can be attributed. With the deductions also the basis for depreciation is reduced for the respective investment. In general unused deductions may be used on income three years backwards and up to ten years on future income. The Canadian Consolidated Revenue Agency refunds if necessary up to 40 percent of not used deductions for investment credit. Taxpayers with a certain income from self-employment and independent work as well as wages may in accordance with more detailed regulations, deduct up to CA$ 500 in health related expenditures.

The income tax for the provinces and the territories is limited to income that can be attributed to the provinces or territories. The municipalities do not claim income taxes. The income tax to the provinces or territories is computed as an increased rate on the basic rate of the federation. The maximum income tax rate (marginal rate) is thus relatively high, ranging from 43.5 percent in the Northwest-Territories to 52.5 percent in Newfoundland (Müssner 2000, p. 22–23).

3.2.3 Property taxation

Only the local government or municipalities claim real estate taxes. Generally the provinces determine the assessment basis and the control system whereas the municipalities determine the rates of taxation. In some provinces (i.e. Ontario) the municipalities are free to determine both the assessment basis and the control system. The character of the tax is quite different in the different provinces. In some provinces it has the character of a real estate tax while in others it covers other property as well and is thus a real estate property tax. Among the real estate taxes is also the school tax, raised by the school districts, the assessment basis of which is the real estate value. Since the property concept is very wide the property taxes are high in international comparisons (Parsche et al. 2000, p. 193–194).

An overview of agricultural property tax concessions and government transfer to agriculture is given in a report to Agriculture and Agri-Food Canada (AAFC), (Agriculture and Agri-Food Canada, 2000). The property tax is one of the few revenue sources used by local governments and provinces in some cases, to funding local services. It is also used to fund education in most provinces. The revenue depends on four variables:

- The tax base—what properties are subject to tax and not exempt from the tax,
- The assessment ratio—assessment value relative to the market (or current) value,
- The nominal tax rate applied to the assessed property values and
- The rebates and deferrals on property taxes.

Each province uses a different approach to providing agricultural property tax programs and concessions. An overview indicate that:

- British Columbia uses exemptions on buildings and farm residences in rural areas and has assessment values on land substantially lower than agricultural market values.
- Alberta exempts most farm residences and buildings and its assessment program results in land being assessed significantly below the agricultural market value.
- Saskatchewan excludes farm residences and buildings from property taxation, and the assessment value is ranging from 50 (rangeland) to 70 percent (cropland) of the agricultural market value.
- Manitoba assesses farm property at 30 percent of the market value and farm residence at 45 percent and excludes farmland from the school tax.
- Ontario has a maximum tax rate for eligible farmland and buildings, which is 25 percent of the residential rate.
- Quebec provides a rebate on farm property taxes which is around 50 percent on farm property taxes paid across all farms and around 77 percent for eligible farms with over CA$ 10,000 in gross sales. Quebec also has a maximum assessment value on farmland for school taxation.
- In New Brunswick farm property taxes assessed by the province are deferred through a deferral program. If the use of the property changes then the last 15 years of property tax are due. There is a maximum local government tax rate that farmers pay on farm property.
- Nova Scotia exempts farmland from taxation whereas farm residences and buildings are subject to the property tax.
- In Prince Edward Island, farmland is assessed at less than 50 percent of the agricultural market value.
- In Newfoundland farmland and buildings are exempt from paying real property taxes, however the local government in some areas assesses a business tax on farm property.

As an example the Ontario Province (according to the Fair Municipalities Finance Act of 1997) differentiates between seven classes of real estate properties: residential buildings and properties as well as agricultural (farm) buildings including associated property either residential or farm, multi-family houses (residential/farm), commercially used property, industrial used property, pipelines, agricultural effective areas and managed forests. The municipalities are free to define and tax new property classes. The municipality itself can determine the rates of the municipal property tax while the provincial government determines the rate of the education property tax. The value of the different tax objects is relatively accurately determined by the Ontario Property Assessment Corporation, the median assessment-to-sale ratio for a certain group of properties was about 0.98 in 1996. Agricultural areas and forests are thus appraised with their use value or discounted values of their yields. However, since 1998 these areas are taxed with 25 percent of the tax rate for residential buildings or agricultural usable buildings (Parsche et al. 2000, p. 194–195).

3.2.4 Social security system

Contributions to certain private disease insurance plans so-called private health service plans (PHSP), are deductible in the taxable income, however the net income from the farm business must be more than 50 percent of the total income of the farmer and other income must not be higher than CA$ 10,000. If there are no employed persons at the farm, the farmer can subtract CA$ 1,500 for himself, wife and children above 18 years and half of that for children below that age. For employed special rules apply (see Parsche et al. 2000 p. 179–180, Canada Customs and Revenue Agency 2002a).

3.2.5 Other taxes and fees

In Canada provisions in the Excise Tax Act (the Act) (Canada Customs and Revenue Agency 2000) regulate the Goods and Services Tax (GST) and the Harmonized Sales Tax (HST). Only three provinces (Nova Scotia, New Brunswick and Newfoundland) have harmonized their provincial sales tax with GST to create the harmonized sales tax (HST). The tax rates are either 0 and 7.0 percent (GST) or 15.0 percent (HST including GST)). The HST applies to the same base of goods as GST at a rate of 15 percent. Of this 7 percent is the federal part and 8 percent is the provincial part (Canada Customs and Revenue Agency 2002b). Businesses or farms with total sales in the three categories above CA$ 30,000 per year have to register for GST/HST.

The supply of basic groceries, which includes the majority of supplies of food and beverages for human consumption, is zero-rated and remain their tax status regardless of their form (e.g. milk powder or fluid milk). Thus the supplies of most agricultural and fishing products are zero-rated, however several agricultural products not for human consumption like plants, hides, firewood etc. are taxable. However, supplies of both raw tobacco and wool not processed further than washing, are zero-rated (Canada Customs and Revenue Agency, 2000). Most farm livestock raised for human consumption are zero-rated, however supplies of pet animals are taxable at 7 or 15 percent.

Supplies of inputs like fertilizer, feed, pesticides and some pre-described agricultural property (equipment) are zero-rated under the Agriculture and Fishing Property Regulations. Substandard food or waste from manufacturing of food for humans, which is not suitable for human consumption is taxable at 7 or 15 percent, however when such products qualify under the Agriculture and Fishing Property Regulations as ingredients for zero-rated farm livestock they are zero-rated.

Raw mineral salt is taxed throughout the production chain and becomes zero-rated at the point where it is packed for human consumption. Vitamins and minerals in pills or tonics (such as cod liver oil) are not considered as food and taxable at 7 or 15 percent. Certain categories (i.e. carbonated or alcoholic beverages) are taxable at either 7 or 15 percent. Several foodstuffs are excluded from zero-rating in accordance with special or detailed rules. The rules apply to fruit juice and some other products as well as cakes, muffins, pastries, tarts, cookies, doughnuts and some similar products.

Some important exceptions include food and beverages heated for consumption, including food and beverages heated at the area of purchase. Also salads, except when they are canned or vacuum sealed, and sandwiches or similar products (e.g. hot dogs, hamburgers), platters of cheese and cold cuts etc. other than when frozen, are taxable at 7 or 15 percent. The main distinction is between products suitable or not suitable for immediate consumption and so special rules applies for different combinations of products.

In addition to basic groceries and most farm livestock also medical devises such as hearing aids and artificial teeth as well as prescription drugs are zero-rated. Exports are also zero-rated as most goods and services taxable at 7 or 15 percent are zero-rated when exported (Canada Customs and Revenue Agency 2002b). Apart from zero-rated goods and services some goods and services are tax-exempt. This include sales of previously owned residential housing, most health, medical and dental services, day care services, legal aid service, tolls (for bridge, roads or ferries), financial services, charity services and some goods and services provided by non-profit organizations (Canada Customs and Revenue Agency 2002b).

Although the GST/HST is not a Value Added Tax it is still possible to obtain the GST/HST you paid or owed on some goods and services such as merchandise to resell, advertising services, some capital property such as office furniture, vehicles or general operating expenses such as office rent or rent of office equipment. However, on several expenses it is not possible to obtain an input tax credit. There are two simplified methods available to calculate the GST/HST, either the Quick Method or the Simplified Input Tax Credit Method.

3.2.6 Evaluation and significance

In concert with the provinces, Agriculture and Agri-Food Canada (AAFC) provides annual measurement of the level of financial transfers from government programs to the farm sector (as well as to the agri-food sector) (Agriculture and Agri-Food Canada 2002). The source of transfer is either federal, provincial or a combination of the two and the programs are classified into four groups:

1. Revenue enhancing such as direct output payments (e.g. stabilization, drought or special adjustment payments), programs related to market development activities and regulatory measures (e.g. supply management regulations, tariffs and duties).
2. Cost reducing, i.e. programs that reduce cost to producers such as subsidized credit, fuel subsidies and transportation subsidies.
3. Productivity enhancement such as funding for the development, transfer or adoption of new technologies, crop varieties and livestock breeds, research, extension and incentive grants. It further covers funding for human resource development e.g. training programs and funding for sustainable agriculture, e.g. Green Plan.

4. Quality Control, i.e. programs aimed to enhance or maintain product quality, food safety and health of animals such as different inspection programs and animal health improvement programs.

The measures above amounted to about CA$ 4,860 million or CA$ 15.2 per 100 CA$ of product value (i.e. Adjusted Value Of Production, AVOP) for the year 2000–01. Most of this relates to the four provinces Quebec (CA$ 1,258 or CA$ 23.8/100 CA$ AVOP), Ontario (CA$ 1,146), Saskatchewan (CA$ 837) and Alberta (CA$ 798). The value of tax measures cannot easily be isolated. They would most likely be included in 1 and 2 which in total amounts to CA$ 4,085 million. Most of them are likely also indirect transfers (from taxpayers to agriculture but not directly to producers). Such measures amounts to about CA$ 923 million or 19 percent of the total Government Transfers 2000–01.

The value of *property tax concessions* has been studied separately by Agriculture and Agri-Food Canada (2000). Total Net Farm (property) Taxes paid amounted to CA$ 436 million. Several methods have been used to measure taxes given up in a province, the results ranging from CA$ 70 million to CA$ 1,061 million in the grand total. The calculation method recommended in the report is the so-called "benefit based principle" since it is based on the principle that farm property (excluding the residence) should be taxed based on the services used by the farm operation. They adjust the provincial (rural) residential tax rate to remove the education tax and the proportion of local expenditure spent on services not used by the farm sector and reach a net result of CA$ 80 million. The largest estimated concession is in Ontario (CA$ 37.4) whereas also concessions in British Columbia (CA$ 21.5) and Quebec (CA$ 20.9) are significant. By these method farmers in Saskatchewan on the other hand seems to pay about CA$ 17.5 million too much.

3.3 Australia

3.3.1 Introduction

In Australia the tax-year runs from July 1 to June 30 for all taxpayers, both individuals and companies. The tax authorities can in some special situations allow the adoption of an alternative start and end of the tax-year, but the tax-year must have duration of twelve months.

The Commonwealth of Australia is a federal state and consists of six states and two territories. Both the federal government as well as the local authorities in the states imposes taxes in different ways. About three quarters of the total taxes are paid to the federal tax collector. The federal taxes are mostly (75 percent) taxes on income. The tax on goods and services (general sales tax or GST) constitute about 22 percent of the federal taxes. In principle GST is a Value Added Tax (VAT) since companies, farmers, tradesmen etc. can deduct the greater part of GST paid on inputs. Although collected by the federation the general sales tax is transferred directly to the states.

Table 3.7 gives an overview of the taxes in Australia[4]. The local taxes are employer's payroll taxes, taxes on property and taxes on goods and services. The tax on immovable property is a state tax, popularly said to be used on the three r-s (rates, roads and rubbish).

Table.3.7 Distribution of taxes on the federal and the local level in Australia 1999–2000

COMMONWEALTH TAXES	Million AU$	Percent of federal taxes	Percent of total taxes
Taxes on income	114,503	75.0	58.3
Individual	(83,710)	(54.8)	(42.7)
Enterprises	(29,517)	(19.4)	(15.0)
Non-residents	(1,276)	(0.8)	(0.6)
Employer's payroll taxes	3,434	2.3	1.7
Taxes on property	10	0.0	0.0
Taxes on goods and services	34,091	22.3	17.5
Other Taxes	538	0.4	0.2
Total Commonwealth Taxes	152,576	100.0	77.7
STATE AND LOCAL GOVERNMENT	Million AU$	Percent of state and local taxes	Percent of total taxes
Employer's payroll taxes	8.937	20.4	4.5
Taxes on property	18,084	41.3	9.2
Taxes on immovable property	(8,427)	(19.2)	(4.3)
Taxes on financial and capital transactions	(9,657)	(22.1)	(4.9)
Taxes on goods and services	6,577	15.0	3.4
Taxes on goods and activities [1)]	10,215	23.3	5.2
Total State and Local Taxes	43,813	100.0	22.3

Source: Commonwealth Department of the Treasury 2001

1) Tax on Goods (Wholesale Sales Tax) in 2000

3.3.2 Income taxation

Ordinary federal income tax is the most important tax in Australia and constitutes 75 percent of the federal taxation revenue. The *federal tax rates* are shown in table 3.8.

[4] In table 3.7 the tax on goods and services is shared between the federal and the local level. Before the tax reform in 2000, tax on goods (Wholesale Sales Tax) was a local tax administered by the states and territories (chapter 3.3.5).

Table 3.8 Australian income tax rates 2001–2002 and 2002–2003

Taxable income. AU$	Tax on the income
0 – 6,000	Nil
6,001 – 20,000	17c for each AU$ 1 over AU$ 6,000
20,001 – 50,000	AU$ 2,380 plus 30c for each AU$ 1 over AU$ 20,000
50,001 – 60,000	AU$ 11,380 plus 42c for each AU$ 1 over AU$ 50,000
60,001 and over	AU$ 15,580 plus 47c for each AU$ 1 over AU$ 60,000

Source: ATO 2002

The above rates *do not* include the Medicare levy of 1.5–2.5 percent; the highest marginal tax rate can thus be 49.5 percent.

A lot of the tax benefits or *special schemes for primary producers* in Australia, are so-called conditional tax exemptions, i.e. the taxation is partial put off to a later period. The tax benefit can thus be composed of a mix of improvement of liquidity, lower tax progression and inflationary profit.

D10 Income tax averaging system for primary producers

The main income tax system for primary producers aims at averaging taxable income over a maximum of five years in order to reduce the difference between good and bad years. Tax averaging is of most importance if the income is unstable and the tax progression is strong.

The primary producers can chose to withdraw permanently from the averaging system and pay tax at ordinary rates. However, once the taxpayer has made this choice, it will affect all his assessments for subsequent years and cannot be revoked. This means that the primary producer will be taxed on the same basis as taxpayers not eligible for averaging provisions.

D94 Farm Management Deposits (FMD)

Farm Management Deposits (FMD) are part of the income tax averaging system. The FMD scheme replaces the Income Equalisation Deposits (IED, D93) and Farm Management Bonds (FMB) schemes and is part of the Agriculture Advancing Australia (AAA) package of programs. The Department of Agriculture, Fisheries & Forestry, Australia (AFFA) describes the Farm Management Deposits scheme in this way:

> *"The Farm Management Deposit scheme provides farmers with an effective tax linked savings mechanism to allow them to set aside pre-tax income from the good years to help them better manage their businesses during the more difficult years."*

In this way the deposits reduce the taxable income in the period of deposit and the amount withdrawn is taxable in the period of withdrawal.

FMD is only available to individual primary producers who satisfy the eligibility conditions of the scheme. Only taxable income from primary production can be invested in a FMD. Farmers earning more than AU$ 50,000 off-farm taxable income in the year of deposit cannot obtain the tax benefits of FMDs. The minimum period of a FMD is twelve months. The minimum amount to deposit is AU$ 1,000 a year and the minimum withdrawal is also AU$ 1,000. The maximum amount to hold in a FMD account at any given time is AU$ 300,000. FMD accounts can only be opened in authorized financial institutions.

The FMD scheme is very popular among the Australian farmers. As of March 31, 2001, there were 15,844 holders and the total deposit amounted to AU$ 641,800,000 (AFFA 2002).

D11 Deferment of income from a double wool clip

It can occasionally be necessary with an advanced shearing of wool due to drought, fire or flood. Under these circumstances the woolgrowers can elect to put off the profit on the sale of the extraordinary wool to the succeeding year.

D12 Spreading insurance recoveries for loss, timber or livestock

It is access; by election, to spread insurance recoveries from loss of livestock and net income arising from forced disposal of livestock in equal installments over five income years. An analogous access is in force if timber is lost in a forest fire. If the disposal of livestock is compulsory due to the Brucellosis and Tuberculosis Eradication Campaign, the deferral period is extended to ten years.

D13 Valuation of livestock from natural increase

Primary producers can elect a specific system to assess natural increase in livestock value. The values are lower than the actual cost of production.

D14 New trading stock rules for oyster farmers

The scheme allows oysters farmers to use a special method to value the trading stock.

D15 Income tax exemption for Dairy Exit Program payments

The Dairy Exit Program (DEP) is a part of the Government's Dairy Adjustment Package. If dairy farmers choose to exit agriculture, they can obtain an exit payment of up to AU$ 45,000 tax-free. The Dairy Exit Program was introduced in 1999 and was available until June 30 2002.

D52–59 Different schemes to claim deductions

There are several schemes allowing primary producers to claim deductions in different capital expenditures such as:

- Accelerated depreciation for water management costs

- Land care deduction
- Land care offset
- Deduction for horse breeding stock
- Depreciation of the capital cost of telephone lines for primary producers
- Tax write-off for horticultural plants
- Accelerated depreciation for grapevine plantings
- Drought investments allowance.

3.3.3 Property taxation

The general *Land Tax* is a state and territory tax on land in all the states. It also applies in the Australian Capital Territory (Canberra), but not in Northern Territory. In all the states it is a tax levied on landowners, however in the Australian Capital Territory it is levied on lessees under a Crown lease. The rules are somewhat different in the different states, and only the rules of the state of Victoria will be dealt with in this report.

Land tax is an annual tax on all land in Victoria with a total unimproved value of AU$ 125,000 or more. The rate is progressive ranging from 0.1 to 5.0 percent for land with a total unimproved value of at least AU$ 2,700,000 (SRO.VIC 2002a).

There are several exemptions from the duty to pay land tax in addition to the general exemption for land with a lower total unimproved value than AU$ 125,000. The two most important exemptions concern land used for residence and the greater part of land used for primary production. The exemption for residence is (since 1998) available for properties owned and occupied as the principal residence of a natural person; i.e. not a legal person. There are three situations in which land used for primary production will be exempt from land tax in Victoria:

1. Land wholly outside the metropolitan area
2. Land wholly or partly within the metropolitan area, but not in an urban zone
3. Land wholly or partly within the metropolitan area, and wholly or partly in an urban zone.

As for point 3 there are several sub-conditions, which have to be fulfilled to satisfy the requirement for exemption of land tax such as requirements regarding time of ownership and whether or not it is a full-time farm (SRO.VIC 1995a).

In Victoria there is also a separate land tax with rate 5.0 percent. This special land tax is applicable only to land, which ceases to be exempt from the general land tax and only imposed the year the land ceases to be exempt. The tax is thus a tax on real estate or industrial development imposed when the land is sold or otherwise regulated for such purposes. However, if land for primary production wholly outside the metropolitan area ceases to be exempt, it will not become liable to the special land tax (SRO.VIC 1995b).

Stamp duty is a State and Territory tax on certain documents and transactions, and the rules vary between the states. Some changes in regulations of stamp duty took place after the introduction of the GST 1 July 2000; i.e. stamp duty on listed marketable securities was abolished. Several different rates apply for the stamp duty. Stamp duty is charged at either a flat rate or at a fluctuating rate based on the value of the transaction depending on the particular document or transaction. Stamp duty is charged on a value generally including the GST, depending on nature of the transaction.

When cattle are sold, stamp duty is charged on the value of the sale price. Sales of living cattle are liable to the duty at the rate of AU$ 0.05 for every AU$ 20 or part thereof of the total purchases money for cattle sold in one lot, provided that duty for any one head of cattle does not exceed AU$ 5.00. Calves are dutiable at a flat rate of AU$ 0.15. Sales of live sheep and goats are dutiable at a flat rate of AU$ 0.12 each (SRO.VIC 2002a). Table 3.9 show the stamp duty for transfer or conveyance of real property.

Table.3.9 Stamp duty for transfer or conveyance of real property. Victoria, Australia

Value of real property	Stamp duty
Where the value is between AU$ 0 and AU$ 20,000 inclusive	1.4 percent of the value
Where the value is between AU$ 20,001 and AU$ 115,000 inclusive	AU$ 280, plus 2.4 percent of the value in excess of AU$ 20,000
Where the value is between AU$ 115,000 and AU$ 870,000 inclusive	AU$ 2,560 plus 6.0 percent of the value in excess of AU$ 115,000
Where the value exceeds AU$ 870 000	5.5 percent of the value

Source: SRO.VIC 2002

As a support to younger family members to taking up ownership of family farms, transfer of family farms were in 1993 exempt from stamp duty in Victoria. By this way of promoting younger farmers, the authorities also wanted to encourage the use of more efficient and innovative farming methods. In 1993 only a narrow circle of family members were exempted from the tax, but the circle has now been widened. Since June 1 1999, the exemption also include the transfer of land used for primary production from a company to natural persons if they are relatives of each other and own all the shares. However several other conditions also have to be fulfilled if the transfer of the family farm shall be exempt from stamp duty (SRO.VIC 2000).

3.3.4 Social security system

In Australia there is a mixture of public and private social security systems. *Medicare* is the public system, which provides access to health care for Australian residents. Normally the Medicare levy is calculated as 1.5 % of the taxable income. The Medicare levy is not payable below certain income thresholds depending on family situation, taxable income and whether the taxpayer has pension or not.

From July 1 1997, high-income individuals and families without adequate private patient hospital cover pay an extra one percent of their taxable income as the Medicare levy surcharge. For single persons the lower limit to pay the surcharge is AU$ 50,000. Alternatively private patient hospital cover is a voluntarily health insurance policy formed by a registered fund. The insurance covers at least some of the fees and charges for treatment in Australian hospitals.

The *pay-roll tax* is exclusively a state and territory tax. All Australian states and territories charge the pay-roll tax, but each state has its own legislation, with differing provisions and exemption. Employers are liable for paying pay-roll tax on wages, salaries etc. paid to the employees when their total Australian wage exceeds a certain level. This level is called the exemption threshold and varies between the states. Groups of businesses are entitled to only one exemption threshold for the group.

In Victoria the threshold is AU$ 515,000 over a full financial year and the pay-roll tax is payable at a rate of 5.45 percent. Most small businesses, including primary producers, are more or less exempt from the pay-roll tax because their paid wages in the year are lower than the threshold (SRO.VIC 2002b).

3.3.5 Other taxes and fees

From July 1 2000*, the goods and services tax GST* replaced the Wholesale Sales Tax (WST) and some state and territory taxes. WST was imposed on the wholesale selling price of the goods. WST was invoiced at different rates, but the general rate was 22 percent. The GST on the other hand is based on the value added tax (VAT) model that is the most common consumption tax in the OECD countries.

Salesmen are liable to pay 10 percent GST for the delivery value of goods and services. The base of the tax is very wide and includes most goods, services and activities. However, it is a lot of exemptions, among other things medical treatment and books. In addition a lot of the goods and services are zero-rated; i.e. the tradesman claims no GST but still obtains deduction for GST paid on inputs. Zero-rating include most kinds of food for human consumption as well as goods and services which are to be exported. By deducting input GST it is possible to reduce the level of costs without increasing the price level for the customers.

Food for human consumption is normally zero-rated, but not prepared meals. Farmer's delivery of some products is not classified as food for human consumption before the products have passed through further treatment. The exclusions from the food concept are:

- Live animal (other than crustaceans or mollusks)
- Unprocessed cow's milk
- Any grain, cereal or sugarcane that has not been subject to any process or treatment resulting in an alteration of its form, nature or condition
- Plants under cultivation.

Sole traders or companies with an annual turnover of AU$ 50,000 or more; have to be registered for GST. If the annual turnover is less than the threshold it is access to voluntary register for GST. Voluntary registered enterprises must stay registered for at least 12 months. It is allowed to use cash accounting for GST if the annual turnover is AU$ 1 million or less or if the accounting for income tax purpose is on a cash basis.

If the annual turnover is less than AU$ 20 million, the tax period for GST is generally quarterly unless the taxpayer choose to report monthly. The tax period will be one month if the annual turnover is AU$ 20 million or more.

There are no special rules for primary producers as far as GST concerns apart from the zero rating of several products from the primary industries.

There are two Australian schemes for rebates and grants for use of fuel by businesses and certain other:

- *The Diesel Fuel Rebate Scheme (DFRS)* provides a rebate for the *off-road* use of fuel
- *The Diesel and Alternative Fuels Grants Scheme (DAFGS)* provides a grant for the *on-road* use of fuel.

From July 1 2002, both the off-road and the on-road schemes should have been replaced by the Energy Grants (Credits) Scheme. The new scheme intends both to retain the benefits for special use of fuel by some users, and to give preference to using cleaner fuels. In fact the introduction of the energy grants (credits) scheme has been delayed and both the on-road and the off-road schemes have so far been extended to June 30, 2003.

The Diesel Fuel Rebate Scheme for the off-road use of fuel (DFRS) provides a rebate for excise duty paid on diesel or similar fuels, but not on gasoline. The rebate is AU$ 0,38143 per l diesel. The rebate is paid out for fuel used in carrying out certain categories of business activity,—among others agriculture, forestry and fishing. In agriculture the following activities are eligible to the rebate:

- Growing crops
- Harvesting and storing crops (on the property on which they were grown)
- Rearing livestock
- Viticulture, horticulture, pasturage or apiculture.

The following activities are also eligible, provided they are carried out on an agricultural property:

- Drilling bores
- Building firebreaks
- Irrigation
- Fencing
- Weeding
- Controlling pests or disease
- Hunting and trapping
- Meeting general domestic residential requirements (for example by providing lighting)
- Building or maintaining sheds, pens, silos, water tanks, troughs, channels and irrigation systems
- Constructing earthworks (this includes building dams, levy banks and leveling or grading land to make farm tracks)
- Shearing

- Mustering
- Baling hay that has been produced on the same property.

These activities are not eligible:
- Distributing, manufacturing or marketing produce
- Doing contract work for councils, telecommunications providers, public utilities or any similar organization
- Breeding horses for show or racing
- Aquaculture.

In forestry there are also several eligible activities.

Farmers claiming the off-road rebate for diesel must keep records of the fuel purchased and used. The records have to be kept for five years.

The Diesel and Alternative Fuels Grants Scheme for the *on-road* use of fuel (DAFGS) provides a grant of about AU$ 0,18 per liter diesel and alternative fuels for certain on-road uses. It is also possible for farmers to use this scheme for transport of farm products on public roads. Farmers eligible for rebate under both schemes have to keep separate records for each scheme.

3.3.6 Evaluation and significance

Each year the Department of Treasury publishes a Tax Expenditures Statement. The publication contains different information; among other the volume of tax expenditures as reproduced in table 3.10. Tax expenditures are defined as tax concessions designed to provide a benefit to a specified activity or class of taxpayers.

Table 3.10 Total measured tax expenditures in Australia

Year	Superannuation Million AU$	Other tax expenditures Million AU$	Total Million AU$	Tax expenditures as a proportion of GDP (%)
1997–98 (est)	9,920	15,565	25,485	4.5
1998–99 (est)	9,510	16,243	25,753	4.4
1999–00 (est)	10,210	17,572	27,782	4.4
2000–01 (est)	9,065	20,520	29,585	4.4
2001–02 (proj)	9,485	19,787	29,272	4.2
2002–03 (proj)	10,305	19,500	29,805	4.0
2003–04 (proj)	11,225	19,537	30,762	3.9
2004–05 (proj)	11,875	20,260	32,135	3.9

Source: Department of the Treasury (2002)

The actual value of the tax expenditures has increased over the last years. However, a slight decrease in tax expenditures as a proportion of GDP is expected due to assumed stronger increase in GDP in the future.

The share of the tax expenditure of the primary producers (i.e. producers in agriculture, fisheries and forestry) and other businesses are shown in table 3.11.

The tax expenditures to farmers are small by comparison, for the last years the tax expenditures for the primary producers have been about 4.5% of the tax expenditures of other businesses. For the next years this ratio is expected to increase to about 8.5%.

Table 3.11 Tax expenditures by primary producers, businesses and others in Australia

	Estimates (million AU$)			Projections (million AU$)			
Year	1998–99	1999–00	2000–01	2001–02	2002–03	2003–04	2004–05
Primary producers	206	219	213	214	245	256	282
Businesses	4,667	5,071	6,081	4,605	3,766	3,121	3,211
Others	20,880	22,492	23,291	25,453	25,794	27,385	29,742
Total	25,753	27,782	29,585	29,272	29,805	30,762	32,135

Source: Department of the Treasury (2002)

In the Tax Expenditures Statement 2001, the expenditures have been estimated for the specific ordinances affecting the primary producers. This comprise the following schemes:

INCOME TAX BENCHMARKS:
D10 Income tax averaging for primary producers
D11 Deferment of income from a double wool clip
D12 Spreading insurance recoveries for loss timber or livestock
D13 Valuation of livestock from natural increase
D14 Introduction of new trading stock rules for oyster farmers
D15 Income tax exemption for Dairy Exit Program payments

DEDUCTIONS BENCHMARKS:
D52 Accelerated depreciation for water management costs
D53 Land care deduction
D54 Land care offset
D55 Deduction for horse breeding stock
D56 Depreciation of the capital cost of telephone lines for primary producers
D57 Tax write-off for horticultural plants
D58 Accelerated depreciation for grapevine plantings
D59 Drought investments allowance

OTHER BENCHMARKS:
D93 Income Equalisation Deposits (IED) scheme (phased out in 2000)
D94 Farm Management Deposit scheme

Table 3.12 Tax Expenditure Reference Table (Australia)

	Estimates (million AU$)				Projections (million AU$)			
	1997–98	1998–99	1999–00	2000–01	2001–02	2002–03	2203–04	2004–05
D10	100	75	70	75	80	95	100	110
D11	na	na	na	na	na	na	na	Na
D12	na	na	na	na	na	na	na	Na
D13	60	60	70	70	75	85	90	100
D14	-	-	-	-	..	..	..	..
D15	-	-	-	-	1	1	1	-
D52	25	20	20	20	22	20	20	25
D53	Included in D52							
D54	-	1	1	<1	<1	<1	<1	<1
D55	na	na	na	na	na	na	na	Na
D56	1	1	1	1	1	1	1	1
D57	1	3	4	5	5	6	7	8
D58	4	4	4	4	4	4	4	5
D59	14	12	10	5	-	-	-	-
D93	25	25	9	-	-	-	-	-
D94	-	-	25	30	25	30	30	30

Source: Department of the Treasury (2002)

The main tax expenditures due to primary production are the income tax averaging scheme (D10), which together with the Income Equalisation scheme (D93) and the Farm Management Deposit scheme (D94) constitute close to half of the total tax expenditures to primary producers. As for the deduction schemes the D52 (water management) and the D59 (drought investment) seems most significant.

3.4 Germany

3.4.1 Introduction

It has long been known that the federal state of Germany provides its farmers with generous support through the tax system including social security (Knerr 1991). As will be explained below, the main source of support comes from a special valuation of agricultural income and property together with a special social security system for the German farm sector.

3.4.2 Income taxation

The income tax is a personal and federal tax. The structure of income taxation is based on seven categories of income one of which is income from agriculture and forestry. In 1998, the tax rate was based on a progressive rate between 25,9% and 53%. Due to a ongoing tax reform in Germany, the tax rate will be reduced in several steps down to 15% and 42% in 2005.

Agricultural and forestry taxation have several benefits in relation to business taxation (EFAC 2000, p. 110). These include special rules for book keeping, special exemptions and tax rate reductions, a fixed arrangement on VAT taxation, a special valuation base for heritage taxation and a lower property tax on arable land. Agricultural income is calculated according to four different methods: (a) book keeping, (b) keeping an inventory, (c) flat method ('unit valuation'), and (d) income valuation by the financial administration. Farms are obliged to keep records if they exceed a certain size. In the first case, income is defined as the difference between the business assets at the end of the tax year and the end of the preceding tax year, plus withdrawals and minus contributions (EFAC 2000, p. 38). Around 30% of all German farms keep records (Andersen et al. 1994, p.187). Farms that are not required to keep records, but exceed the limits for the flat method keep an inventory (also called 'simplified book keeping'). Around 15% of all German farms calculate their agricultural income according to that method (Andersen et al. 1994, p. 188). The agricultural income on half of all German farms is calculated according to the flat method. The income calculation is based on the economic value of the land. Until 1999, this economic value was stipulated on the basis of its value in 1964. As part of the tax reform, the calculation was simplified in 1999. Now, the estimated profit per hectare is directly linked to the so-called 'hectare value' which is a measure of the potential land quality. The 'flat method' implies that taxable agricultural income is usually lower than under book keeping (Andersen et al., 1995). If a farm does not calculate income according to one of the methods (a) – (c); then the financial administration will undertake an income valuation by itself.

The middle size of all German agricultural enterprises is 32.1 hectares as contrasted with 70.4 hectares arable land for farms with book keeping.

Agricultural income is subject to an income allowance, independent of the method of income calculation. All individuals with agricultural income are eligible to the allowance as long as gross income is below EURO 32,250 (single individuals) or EURO 64,500 (married individuals) and gross agricultural income is higher than the income allowance. The income allowance was EURO 700 (single individuals) or EURO 1,400 (married individuals) in 2001.

In addition, there was an income tax reduction for all farmers who calculated income according to the flat method. The tax reduction scheme was abolished in 2001.

It is important to mention that income earned from agricultural activity by companies (such as stock companies, limited partnerships with shares or limited liability companies) is always defined as income from trade or business, and not as income from agriculture. Therefore, the various methods of calculating agricultural income do not apply for companies. Instead, they are usually obliged to do book keeping.

3.4.3 Property taxation

There exist different kinds of property taxation. Land including agricultural land is subject to a land tax. The rate of the land tax is higher for agricultural land than for other land. The total amount of the tax, however, is quite low (Andersen et al.

1994, p. 197). Agricultural property and non-agricultural property are treated in the same way. The farm sector has certain benefits, however, since the calculation of agricultural property is based on the economic value of the farm with its key date from 1964. This calculation method is special for agriculture.

3.4.4 Social security system

German farmers have their own social security system covering an old age pension scheme, a health insurance scheme and an accident insurance scheme. This system is open for farmers, their families and agricultural workers. The original intention was to have the system self-financed, i.e., the contributions of active farmers should match the pensions for retired farmers on a yearly basis. The decrease of labor force in agriculture, partly as a result of agricultural policies, would have implied a drastic increase in social security contributions for the remaining (active) farmers. In order to keep the increase at a level comparable to that of other employees, the federal government subsidizes social security contributions of active farmers.

3.4.5 Other taxes and fees

Tractors and other agricultural machinery are exempt from car tax. In addition, there is a allowance on the diesel oil tax. There are also some allowances on diesel and gas used for greenhouses.

3.4.6 Evaluation and significance

Table 3.13 shows the most important tax measures (incl. social security) targeted towards the German agricultural sector and measured by their budgetary effect from 1999 to 2002.

It appears that the federal grants to the agricultural old age pension scheme is the most important single measure amounting to around one half of the total amount of all tax-related measures. Moreover, all special social security measures together stand for ca. 85% of all tax-related measures.

Table 3.13 Budgetary effect of tax measures (incl. social security) for the agricultural sector in Germany 1999–2002 (million EURO)

	1999	2000	2001	2002
Agricultural income allowance	87.0	87.0	76.4	76.4
Income tax reduction under the simplified income calculation scheme	38.2	38.2	0.0	0.0
Simplified calculation of gross agricultural income	31.8	28.6	21.2	21.2
Exemption from car tax	92.3	92.3	92.3	92.3
Allowance on diesel oil tax	459.2	475.9	452.9	315.2
Agricultural old age pension scheme	2,368.8	2,298.5	2,311.6	n.a.
Agricultural health insurance scheme	1,187.5	1,078.1	1,261.6	n.a.
Agricultural accidence insurance scheme	298.4	271.3	271.3	n.a.
Additional insurance scheme for agricultural workers	12.3	12.6	13.0	n.a.
Sum	4,563.4	1,078.1	4,665.6	n.a.

Source: BMVEL (2000), BMVEL (2002a), BMVEL (2002b)

The budgetary effect of tax measures (incl. social security) per ha of land and per man-year in agriculture is shown in table 3.14. It turns out that the amount per ha land is around EURO 270 per hectare. Calculated per man-year in agriculture, the value of tax measures targeted towards agriculture in Germany is around EURO 7,360 per man-year. The sharp increase from 2000 to 2001 is mainly due to a reduction in the total agricultural labor force by almost 7%.

Table 3.14 Budgetary effect of tax measures (inclusive social security) in Germany (EURO)

	1999	2000	2001
Per hectare land	264.8	254.8	261.6
Per man-year	7,401.8	7,212.0	7,946.8

The amount becomes significantly lower if one excludes social security from the calculations (table 3.15). The value of tax measures alone is reduced to around EURO 40 per hectare of land and 1,138 per man-year. It is also interesting to see that the budgetary effect of tax measures (exclusive social security) shows a downward trend from 2000 to 2001, while it is just the opposite if one includes social security. This indicates that Germany is engaged in reducing special tax measures for its agriculture, while social security contributions are rapidly growing due to the age distribution of the German population.

Table 3.15 Budgetary effect of tax measures (exclusive social security) in Germany (EURO)

	1999	2000	2001
Per hectare land	41.0	42.0	37.4
Per man-year	1,146.3	1,188.3	1,135.1

3.5 United Kingdom

3.5.1 Introduction

75% of the total land area in the UK is farmland. UK farms are big compared with the rest of EU. Table 3.16 shows the distribution of the farmland in size groups.

Table 3.16 Farm holdings distribution in size groups. UK

Size groups	No. holdings	Total farmland in hectare
< 20 hectare	101,900	821,000
20–50 hectare	55,500	1,836,000
50–100 hectare	40,500	2,847,000
> 100 hectare	40,400	11,391,000

Source: EFAC 2000

In UK a big part of the farmland has been owned by landlords and rented to the tenants. Still the landlords own about 33% of the farmland, but the part of tenant farms is decreasing. There are two mains types of tenancy (EFAC 2000, p. 11):

"a. Agricultural Holdings Act tenancies (AHA tenancies) were granted until 1995 and gave the tenant right to occupy the farm for lifetime. Tenancies granted before 1984 also gave rights to successive generations.

b. Farm Business Tenancies (FTBs) have been in effect since 1995 and do not give any rights beyond those agreed in the contract. There is much greater freedom of contract between the landowner and the farmer."

The most common business form in agriculture in UK is partnership, but an appreciable part of these partnerships are partnerships between spouses. A not unimportant part of the agriculture compose of different business forms as share farming, contract farming, Private Limited Companies or trusts.

All farmers in UK as other tradesmen have to keep accounts that form the basis of the tax computations. The British accounting system follows the Anglo-Saxon tradition rules for accounting such that British accounts are highly commercially oriented, tailored for the investor as end-user and regulated by private authorities. The basic principles are a true and fair view, strict consistency over time and relevance (Hogg 1998).

The Inland Revenue is responsible for collection and administration the taxes on government level. Local taxes are paid to the local authorities. From 1998 most of direct taxes are "self assessed" by the taxpayer so the taxpayer himself has the responsibility for calculating the tax payable. Each natural person over the age of 18 is separate legal responsible for tax on his or her own income.

The tax year is twelve months and it runs from April 6 one year to April 5 next year.

3.5.2 Income taxation

The tax legislation has not a precise definition of the word "income". The income tax system is therefore build up with different schedules for different sorts of profits or incomes. The schedules for income tax are a classification of income tax according to the nature of the source from which the income is received.

The system of schedules is a very old tax system introduced in 1803. With some modifications, the system of schedules has survived to this day as one of the particular characteristics of the British income tax (James & Nobes 1992, p. 127).

The two most important schedules are Schedule E, which covers income from employment, and Schedule D, which includes income from trades, professions, businesses, property and other annual profits (James & Nobes 1992, p. 127).

- Schedule A Rents and other receipts from land and buildings
- Schedule B Repealed
- Schedule C Interest on government securities
- Schedule D Income from trades and professions; interest and other income, classified again into various Cases
  - Case I Profits of a trade
  - Case II Profits of a profession or a vocation
  - Case III Interest not taxed at source
  - Case IV Income from foreign securities
  - Case V Income from foreign possession
  - Case VI Miscellaneous profits not falling under any other Case or any other Schedule
- Schedule E Income from offices and employments, pensions and social security benefits, often taxed under PAYE
- Schedule F Dividends received from resident companies.

Income from a trade or a part of a trade is chargeable under *Case I of Schedule D*. Incomes from farming and market gardening managed on a commercial basis and with a view to the realization of profits, are therefore chargeable under this schedule and this case in the same way as incomes from other trades.

Since March 1988 it is either income tax or corporation tax attached to income or profits from the ownership of commercial woodlands. On the other side, there is no tax relief for expenses or for interest paid on loans for the purchase or development of woodlands. Up to March 1988 the occupier of woodlands managed of a commercial basis, was normally charged income tax under Schedule B, unless the taxpayer elected to be assessed under Schedule D Case I.

Farms and other enterprises have to adjusting their business accounts to tax accounts. The most important items of cost not allowed in the tax accounts, are the business depreciation of machinery, equipment, buildings and other permanent improvements. All private expenditure and expenditure linked to capital transactions, are also excluded.

Instead of the business depreciation, capital allowances connected the fixed assets are calculated and deducted in the taxable income.

Machinery and equipment is entitled to Writing Down Allowance of 40% in the year of purchase. This high first year allowance is limited to small and medium sized businesses. All family farms have a size that qualifies them for this allowance. After reducing with the Writing Down Allowance, the recently acquired item is put in a common pool for all machinery and equipment in the enterprise. The pool is written off over the following years at 25% on the reducing balance each year.

Rent and other income from property is chargeable to income tax under *Schedule A*. The landlord's rental income from a tenant is therefore chargeable under this schedule. The income chargeable is that to which the landlord become entitled, but does not necessarily receive, in the year for assessment.

Deduction may be made from the rent or other income for expenditure, including the following (SAC 1992):

- Normal repairs, upkeep and maintenance
- Cost of rent collecting
- Legal and accountancy costs of preparing tax statements relating to the property
- Premiums for property insurance
- Rates and rent paid by the landlord
- Upkeep of estate offices
- Cost of valuation for insurance, but not for purchase, sale or probate.

Wages, salaries, fringe benefits etc are chargeable under Schedule E. Farm employees' wages are e.g. taxed under Schedule E. Most of the accrued taxes under Schedule E are collected through the *PAYE (Pay As You Earn)* system. The normal basis of assessment is the amount received in the tax year.

Profits on disposing of assets are potentially liable to *Capital Gains Tax (CGT)*. Capital Gains Tax is only current if the disposing assets are chargeable. If a gain will be taxable, a corresponding loss will be allowable. The taxable part of the gains will be put to the top of the taxpayer's income for taxation.

In the principle, there are no special rules for the capital gains tax in connection with agriculture. As incomes or profits from the ownership of commercial woodlands are except from income tax, the increase in the value of timber through the physical growth of trees and timber price also is except from capital gains tax, but any increase in the value of the land is taxable.

The capital gains tax was introduced in 1965. It has been different corrections in the rules after that time. 1982 is an important year in this relation. As a main rule, the cost of an asset acquired before 31 March 1982 is set to its value on that date. An indexation allowance adjusts gains for the inflation from March 1982 up to April 1998. No indexation allowance is due for the period after 1998.

Because the value of farmland in 1982 was comparatively high when indexation is added to this value in arriving at the base value there are unlikely to be material gains to tax on sale of most UK farms at present (EFAC 2000, p. 195).

The farmhouse is a private asset and therefore exempt from Capital Gains tax.

3.5.3 Property taxation

Local authorities levy taxes on real property. This is the main tax income for the local authorities from the inhabitants. All income tax, inheritance tax and value added tax are government taxes, and the government transfers a lot of the tax income to the local authorities according to special regulations.

Council tax is a local charge on domestic property and is stipulated annually by local charging authorities. There is a single bill for each dwelling, i.e. a house, flat, holiday house, mobile house or houseboat. The tax is based on the value of the dwelling and the number of residents. In each authority area the dwellings are valuated and placed in one of eight valuation bands, A to H. The band determines the amount of tax to be paid for each dwelling. Band D is the main band and the other bands are stipulated relative to the Band D.

The council tax replaced the community charge ”poll tax” from April 1 1993. A council tax bill is regarded as having a 50% property element and a 50% personal element. Therefore the tax bill is reduced by 25% if the dwelling is occupied by only one adult person, and by 50% if the dwelling is empty or a second home. There are a lot of different causes to reduce the bill;—it is discounts for full-time students, nurses, patients resident in hospital etc. Some special dwellings are exempt from council tax at all.

Farm houses, farm cottages, croft houses and houses connected with fish farms, are all subject to special provisions. If they are occupied in connection with the farm, croft or fish farm they will be valued on the basis that their availability is restricted to being used in that way. The intention of these provisions is to recognize that the market for such houses will be restricted, and for that reason they often are moved to a lower valuation band that in which they otherwise would be placed (Andersen et al. 1994).

From April 1 1990, businesses pay a uniform *business rate* (also called the national non-domestic rate) on their ratable properties. Non-domestic property is liable to business rates, but agricultural land and buildings are exempt from business rates. If part of a dwelling house is let for business rather than as living accommodation, business rates will be payable on that part.

The regulations of business rate are somewhat different for Scotland, Wales, North-Ireland and England. Individual local councils collect the business rate but the rate is paid into a national pool and then distributed on a formula basis to the local authorities.

3.5.4 Social security system

The intention of The National Insurance Contributions (NIC) was to fund the National Health Service, Unemployment Benefits and the State Pensions. The legal authority for the social security system is the Social Security Contributions and Benefits Act 1992. The direct link between the input and the output has now, however, been lost and the contributions are now emerged into the general Treasury funds (EFAC 2000, p.211).

Most people who work have to pay National Insurance contributions and there are six classes of contributions:

- Class 1 paid by people who work as employed earners and their employers
  - Class 1A paid only by employers who provide directors and employees with certain benefits in kind which are available for private use, for example cars and fuel
  - Class 1B paid only by employers who enter into a Pay as You Earn Settlement Agreement with the Inland Revenue for tax purposes
- Class 2 paid by people who are self-employed
- Class 3 voluntary contributions paid by people who wish to protect their entitlement to State Pension, and who do not pay enough National Insurance contributions in another class
- Class 4 paid by those whose profits and gains are chargeable to income tax under cases I and II of Schedule D of the Income and Corporation Taxes Act 1988. Theses are normally paid be self-employed people in addition to Class 2 contributions. Class 4 contributions do not count towards benefits.

3.5.5 Other taxes and fees

Value added tax (VAT) was introduced in 1973. After April 25 2002 the registration limit is £ 55,000 per annum in dutiable turnover. There are three different rates for VAT:

- Standard rate 17.5%
- Reduced rate 5.0%
- Zero rate 0.0%.

For agriculture there are four main groups of zero-rated products:

- Food for human consumption
- Animals to be slaughtered and animal food
- Live animals
- Seeds and plants.

Both supply of plants grown to provide food for human or animal consumption and the seeds or other means of propagation (spores, rhizomes etc) used to produce such plants, are zero-rated (HM Customs and Excise 1999). Most live animals except pets are zero-rated and the zero-rating include sale, hire or loan of animals. Horses, racing pigeons, ornamental fish and ornamental poultry are standard-rated (HM Customs and Excise 1994). Most food that is to be fed to animals, are zero-rated but these foodstuffs are standard-rated:

- Canned, packaged or prepared pet food
- Packaged food for wild birds
- Biscuits and meal for cats and dogs
  (HM Customs and Excise 2002a).

Supplies of basic unprocessed foodstuffs for human consumption are zero-rated:

- Raw meat and fish

- Milk, egg and honey
- Vegetables and fruit
- Cereals, nuts and pulses
- Culinary herbs
  (HM Customs and Excise 2002b).

Farming businesses can reclaim 70% of the input tax on the repair and maintenance costs of a farmhouse provided the following conditions are met:
- The house must be a "typical working farmhouse"
- Farming must be the occupier's full-time activity
- The occupier must be a sole proprietor or partner
- The expenditure must be on general repair, maintenance or renovation, including some improvements such as replacement windows.

For other farmhouse expenses (e.g. fuel and power) the farmer will have a reclaim remains the proportion of actual business use (Homer & Burrows 1996, p 435).

The flat rate scheme is an alternative to VAT registration for farmers. A farmer registered as a flat rate farmer, do not account for VAT and can therefore not reclaim input tax. A flat rate farmer can, however, charge and keep a flat rate "addition" (FRA) when he sell goods or services to customers who are registered for VAT. FRA is not VAT, but compensation for losing input tax on purchases. The flat rate in UK is 4.0% and it is not intended as reimbursement of all the VAT incurred on purchases.

In the flat rate scheme a farmer is defined as someone who carries on almost all agricultural production including horticulture and forestry. The flat rate scheme includes also a lot of services in combination with agricultural production. Such services can among others, be field work, packing and preparing of agricultural products for market, storage of agricultural products, forestry services, hiring out equipment for use in agriculture, horticulture or forestry.

A farmer cannot join the flat-rate scheme if the value of his non-farming activities is above the VAT registration threshold (HM Customs and Excise 2002c).

Transfers of gifts and estates are in principle taxable on the system of *inheritance tax*, but it is several limitations and exceptions from the liability to pay inheritance tax.

Inheritance tax is calculated for the total value of the estate and not for the specific share to each heir/heiress. The value of the estate is reduced with a threshold amount of £250,000 (March 2002), and the rate is 40% for the exceeding amount. Since liability to pay inheritance tax is calculated for the estate, the tax rates don't differentiate because of kinship between deceased/donator and heir/heiress.

Gifts (lifetime transfers) given the latest seven years before the point of death are also liable to tax. The amount of tax will be reduced if the gift is made more than three years before the transferor's death. Certain gifts are completely free from inheritance tax even if they are made in the period of seven years before the death of the transferor. Such gifts are called exempt transfers and include gifts to husband or wife, wedding gifts and other gifts in the tax year up to different limit values etc.

The executor or administrator has to calculate the tax and is liable to pay any inheritance tax due on the estate in the course of 13 months after the deaths. Inheritance tax has to be paid before the estate is at the heir/heiress disposal.

Transfer of business assets is getting privileged in the British rules for inheritance tax. There are inheritance tax relieves available for business and business assets, for agricultural property and for woodlands.

Relief is available for transfers of certain categories of business and of business assets if they qualify as "relevant business property" and the transferor has owned them for minimum two years immediately before the transfer. The relief is available for transfers in life and on death. It is also available when relevant business property is chargeable as settled property. The relief is 100% or 50% depending on what sorts of assets are transferred (Inland Revenue UK 2002).

Agricultural property relief is available if the transfer is attributable to the agricultural value of property, owner-occupied or let. Relief is only available if the transferor has

- occupied the agricultural property for agricultural purposes for minimum two years immediately before the transfer, or
- owned the property throughout the seven years immediately before the transfer and the transferor or another has occupied the property throughout the period for agricultural purposes.

The agricultural property relief is available for transfers in both life and on death and when agricultural property is chargeable as settled property. The term agricultural property includes also:

- Farmhouses, cottages or buildings which are proportionate in size and nature to the requirements of the farming activities conducted on the agricultural land or pasture
- Buildings used for intensive rearing of livestock (or fish), if those buildings are occupied with agricultural land or pasture and the occupation is ancillary to that of the agricultural land or pasture
- Growing crops, when transferred with the land
- Stud farms engaged in the breeding and rearing of horses and to land used for grazing associated with those activities
- Land and building used in the cultivation of short rotation coppice.

If the valuation of the land reflects the benefit of a milk quota, agricultural relief is given on that overall value.

The basis for the agricultural relief is the agricultural value of agricultural property. The relief does not include agricultural property estimated as development value. In this case, it can be an opportunity to use the business relief. Neither the additional value of a farmhouse as a desirable county residence is included in the base for the relief. The agricultural relief is 100 or 50% dependent on the specific case.

There is also a specific relief for transfers of woodland on death. This relief has become less important since the introducing of 100% relief for businesses that qualify as relevant business property.

3.5.6 Evaluation and Significance

In UK the taxation of farmers is mostly like the taxation of other tradesmen. An important exception is that commercial woodlands since 1988 are exempt from taxation. There are special relieves in the inheritance tax for agricultural property but these are approximately at about the same levels as for other business property.

The VAT system is different from the ordinary VAT system and corresponding with the EU special VAT system for agriculture.

3.6 Ireland

3.6.1 Introduction

The land area of Ireland is 6.9 million hectares, of which almost 5 million hectares is used for agriculture and forestry.

Table 3.17 Role of Agriculture and the Food Industry in the Irish Economy, 1999/2000

	Primary Agriculture	Agri-Food Sector
Percent of GDP	3.5%	10.5%
Percent of employment	7.3%	10.5%
Percent of export	5.6%	9.6%

Source: DAFF (2001a)

There are 143,900 farm holdings in Ireland and almost all of them are family farms. The average farm size is 29.3 hectares. 47% of the farms have less than 20 hectares land. 11 percent of the farmers are under 35 years old and 45% are over 55.

The income tax year is twelve months and has so far commenced on April 6, but will from the year 2002 follow the calendar year. Most individuals in employment have tax deducted from their wages under the *Pay-As-You-Earn (PAYE) scheme*.

If the farmer is a sole trader, profits from farming and capital gains on the disposal of certain assets, are assessable to *income tax* and *capital gains tax*. If the trade of farming is in a company, the profits and gains are assessable to *corporation tax*. Partnerships itself is not chargeable to income tax. Each of the partners is, however, chargeable to her/his share of the partnership income.

3.6.2 Income taxation

Income after deductions is taxable either with a standard rate of 20% or with a marginal rate of 42%. For 2002 incomes up to EURO 28,000 are standard rated with 20% for single persons. Incomes over this basic level are assessed with marginal rate of 42%. There are other limits for the basic level for spouses and single parents.

There are several deductions both in the taxable income and directly in the tax amount. Most of these deductions are related to low income, standard of health, family responsibilities and the age of the taxpayer.

Income tax on salaries, wages and pensions is deducted under PAYE on a current year basic. On other personal income, income tax is also charged on a current year basic.

Taxable incomes are divided in four Schedules:

- Schedule C: Interest etc., payable out of any public revenue
- Schedule D: Profits or income from property, trades, professions or vocations and all other annual profits or gains not charged under any other schedule and not specially exempted from tax. Schedule D is divide up into five separate Cases
- Schedule E: Income from employment, including pensions
- Schedule F: Income from distributions.

Profits from farming and market gardening are taxable under Case I of Schedule D in the same way as profits from other trades.

Individual full-time farmers may elect to be assessed in the normal way with an accounting period of 12 month for the year of assessment, or on the basis of the averaging farming profits and losses of three years of assessment.

If the farmer or the spouse also has another trade or profession (except income from farmhouse holidays), they cannot elect the average way of taxation, but has to use the ordinary way. If the election for averaging is made, the farmer must remain on averaging for a minimum of tree years.

Farmers may claim a farm buildings allowance for capital expenditure on the construction of farm buildings except building used as a dwelling. The rate is 15 percent of the capital expenditure in each of the first six years with the remaining 10 percent in year seven.

The Irish government gives different advantages to farmers who reduce the pollutions from the farms. Earlier these advantages were regulated in the Control of Farm Pollution Scheme. The Farm Pollution Scheme was replaced with *the Waste Scheme* in 1999. It is expected that some 20,000 farmers will participate in this scheme in the period up to 2006. Until now, some 2,500 farmers have participated the scheme (DAFF 2002, p. 97).

In accordance with the Waste Scheme tax allowances are given to farmers who have nutrient management plans and incur necessary capital expenditure for pollution control facilities. The first year the farmer can use a special allowance of 50 percent of the expenditure, limited to a maximum of EURO 31,743. The remaining balance of the expenditure is written off as normal over the following seven years. The relief covers waste storage facilities (water, slurry and effluent tanks) and certain types of winter housing for cattle and sheep (DAFF 2002, p. 97).

There is several tax concessions aimed to encouraging *the transfer of land to young, trained farmers* (DAFF 2002, p. 101):

- 100% stamp duty relief on transfers of agricultural land and buildings to young trained farmers
- 90% agricultural relief from capital acquisitions tax
- 100% stock relief for young trained farmers for four years after transfer
- Income tax exemptions for land leased by farmers over 55 years to non-connected persons
- Retirement relief on capital gains tax for farmers over 55 years.

If an individual person aged 55 years or over, or an individual who is permanently incapacitated by mental or physical infirmity from carrying on a trade of farming, leases the farm to another person, she or he is entitled to have a deduction exempted from tax in the rental income. The deduction is EURO 5,080 if the durability of the leasing contract is five or six years, and EURO 7,620 if the durability is seven years or more.

Capital gains arising on the disposal of assets are chargeable to capital gains tax. A loss of a disposal will normally be allowable if a gain on the same transaction would have been chargeable. Disposal of an asset includes any transfer of ownership of the asset by way of sale, exchange or gift. Disposals of assets between spouses who are living together are not chargeable to capital gains tax. The first EURO 1,270 of a natural person's net gains is exempt from capital gains tax. Selected assets are exempt from tax liability, e.g. private assets as private residences (in certain circumstances) and private cars. Companies don't pay capital gains tax, as capital gains are chargeable to Corporation Tax. The standard rate for capital gains tax is 20 percent.

There are special rules for disposal of a business or farm if the seller is 55 years or more. The rules are the same for farms as for other businesses, but the rules are somewhat different for disposal out of the family and disposal within the family. If the disposal is out of the family and the seller is 55 years or more, it is full relief for capital gains tax if the compensation for the whole or part of the business assets or farm does not exceed EURO 476,250. The business assets must have been owned and used in the business throughout minimum the last ten years before the disposal. The rules are the same for farms as for the business assets.

For disposal to the seller's child it is no limit for the compensation. Therefore it is full relief also when the compensation is more than EURO 476,250. The same rules applies also for disposal to a niece or a nephew who has worked full-time on the farm or in the business for the previous five years.

3.6.3 Property taxation

Residential property tax is an annual tax chargeable on the net market value of residential property. Net market value is the market value of the resident property reduced with a basic amount. For 2002 the basic amount is determined to EURO 43,250. There are different relieves for old people, dependent child and families with low household income. The tax rate is 1.5 percent.

It is no exemption for farmhouse as residential building. A residential farm building will include the dwelling house with any garden, but will not include out-houses, sheds or lands apart from the garden.

Stamp duty is a tax chargeable on certain documents, for instance legal and commercial documents which are necessary to transfer ownership of real property (house and land). The amount of stamp duty payable depends of the purpose of the document.

Table.3.18 Rates of Stamp Duty. Ireland

	Aggregate consideration EURO	First Time Buyer Rate EURO	Full rate %
Residential property	Less than 127,000	Exempt	Exempt
	127,001 – 190,500	Exempt	3.00%
	190,501 – 254,000	3.00%	4.00%
	254,001 – 371,500	3.75%	5.00%
	371,501 – 381,000	4.50%	6.00%
	381,001 – 635,000	7.50%	7.50%
	Over 635,000	9.00%	9.00%
Non-Residential property	Less than 6,350		Exempt
	6,351 – 12,700		1.00%
	12,701 – 19,050		2.00%
	19,501 – 31,750		3.00%
	31,751 – 63,500		4.00%
	63,501 – 76,200		5.00%
	Over 76,200		6.00%

Source: Inland Revenue, Ireland 2002a: SD1 Stamp Duty

For mixed property, for instance a farm with a farmhouse, the residential rate of duty will only apply to the farmhouse. This is shown in the example in table 3.19.

Table 3.19 Stamp duty in EURO when buying a farm. Ireland

Purchase of a farm for EURO 500,000		
The farm without the farmhouse:	EURO 300,000 at 6%	EURO 18,000
The farmhouse	EURO 200 000 at 4%	8,000
Stamp Duty		EURO 26,000

Stamp duty is payable only at half the normal rate with transfer of real property to parents, child, brothers, sisters or other certain relatives. Stamp duty is not chargeable on transfers of any property between spouses.

Where property is purchases with the aid of a mortgage, stamp duty is chargeable on both the purchase deed and the mortgage deed. If the amount of the mortgage does not exceed EURO 254,000, no stamp duty is chargeable. If the amount of mortgage exceeds EURO 254,000, stamp duty is chargeable at the rate of 0.1%.

However, the maximum duty is EURO 630. For the cash amount of the purchase the rate is as shown in table 3.18.

Stamp duty is charged on the market value of the property where the property is transferred as a gift or for less than its full value.

There are a couple of exemptions or relieves from the stamp duty. For example the transfer of land to a Young Trained Farmer is exempted from the stamp duty (Inland Revenue, Ireland 2000). The purpose of the relief is to accelerate the transfer of farms to the younger and more trained generation. The relief was first introduced in 1994 with a reduction of two-thirds of the stamp duty. After January 1 2000 such transfer is quite exempt from stamp duty.

The relief is given when land is transferred as gift or sale to a farmer under 35 years of age on the date of execution of the deed of transfer. The demands and qualifications to be trained, are listen in the Inland Revenue's leaflet SD2 *Stamp Duty Relief on Transfer of Land to Young Trained Farmers*.

The transferee have to make a declaration that she or he for a period of five years will not sell or give away the land, and that she or he will spend not less than 50% of her or his normal working time to farming the land.

If the land is transferred into joint ownership, all of the joint owners have to be young trained farmers, and all of them have to obey the rules in the previous sentence. If the joint persons are husband and wife, only one of them has to satisfy the rules.

The amount of relief will be clawed back if the land is disposed of within five years from the date of execution of the deed of transfer with the exception of replacement by other land within one year of disposal.

3.6.4 Social security system

Pay Related Social Insurance (PRSI) is charged on all earnings from employment excluding non-pecuniary income (benefit-in-kind). The only allowable deductions are contributions paid to approved employee superannuating scheme, and certain permanent health insurance policies.

The rates for employees and self-employed persons includes 2.0% rate for health contribution. National Training Levy of 0.7% is included in the rates in table 3.20.

Self-employed natural persons who have earned EURO 3,175 or more in the tax year are liable to PRSI at Class S on all earnings. From January 1 2002 the Class S contributions are 3 percent PRSI, 2 percent health contribution, in total 5,0 percent.

In regard to PRSI there are no special rules for farmers; either as self-employed persons or as employers.

Table 3.20 PRSI rates 2002. Ireland

	Employer	Employee
Class A1 – most employed persons		
First EURO 38,740	10.75%	6.0 % (including 2% Health Contribution)
Balance (no ceiling)	10.75 %	2.0 % (Health Contribution)
Class S – Self-employed persons		
All income		5.0%(including 2% Health Contribution)

Source: Inland Revenue, Ireland 2002c: Budget 2002

3.6.5 Other taxed and files

Individual and legal persons are liable for *Value added tax (VAT)* if the annual turnover exceeds the following limits:

- EURO 51,000 where goods are supplied; or
- EURO 25,500 where services are supplied.

Taxable persons are obliged to be registered for VAT and to submit a return on the appropriate form, normally every two months, of their supplies and taxable purchases together with a remittance for any tax due. If the turnover for a taxable person doesn't reach the appropriate threshold, the person can elect to be registered.

The standard rate of VAT is 21% (20% before March 1 2002). In addition to the standard rate, it is three reduced rates: Zero rate, 4.3% and 12.5%. VAT rates for some relevant agricultural topics are shown in table 3.21.

Table 3.21 VAT rates for different goods and services in agriculture. Ireland

VAT rates	Goods and services
Zero rate	Food used for human consumption, certain fertilizers, seeds and plants used to produce food, certain animal feeding stuffs, supply and sowing of crops for food production
4.3%	Live cattle, sheep, pigs, horses, deer, greyhounds, goats
12.5%	Building work, land draining and reclamation
	Agricultural services consisting of field work, reaping, mowing, threshing, bailing, harvesting, sowing and planting (not for food production), livestock semen and animal insemination services, flower, flower seeds
21.0%	Hire of machinery, leasing of milk quota (without land), transport and storage

Source: Inland Revenue 1999: Guide to Value-Added Tax and other publications from Inland Revenue

A *flat-rate farmer* is a farmer who is not registered for VAT for the farming activities. In order to compensate for VAT paid on supplies, the farmer is entitled to a flat rate additional of 4.3% to the selling price for the agricultural products or services. The farmer can only use the flat rate additional with sales to individual or legal persons who are registered for VAT.

The flat rate additional is not VAT but part of the farming income. The farmer cannot use the flat rate additional for sale to unregistered customers. A flat-rate farmer is entitled to reclaim VAT incurred in respect of the construction, extension, alteration or reconstruction of farm buildings and land drainage.

Capital acquisitions tax (CAT) comprises both gift and inheritance taxes. Gift tax is charged on taxable gifts and inheritance tax is charged on taxable inheritances. An inheritance is a cost-free benefit taken on a death and a gift is a cost-free benefit taken otherwise than on death. The tax is charged on the taxable value of the gift or inheritance (Inland revenue, Ireland 2002b).

Inheritance tax (IHT) is charged on the market value of the property comprised in the inheritance. The rate is 20% in all classes after the threshold as shown in table 3.22, but there are various exemptions from gift and heritance tax, for example Agricultural relief and Business relief (Inland Revenue, Ireland 2002d).

Table 3.22 Inheritance tax. Classes for threshold limit 2002. Ireland

	Classes		
	A	B	C
Threshold limit	EURO 422,148	EURO 42,215	EURO 21,108
Relationship to the person who gave the inheritance	Parents, children or grandchildren under the age of 18	Brothers, sisters, nephews and nieces	Successors who does not come under Class A or B

Source: Inland Revenue, Ireland CAT 2 Inheritance tax.

Agricultural Relief (Inland Revenue, Ireland 2002e) has been available for gift and inheritance tax since the introduction of Capital Acquisitions Tax in 1976. Ordinary gift and inheritance tax is calculated of the market value, but for agricultural property the agricultural relief reduce this value to "agricultural value". "Agricultural property" means:

- Agricultural land, pasture and woodland
- Growing crops, trees and underwood
- Houses and other farm buildings appropriate to the property
- Livestock, bloodstock and farm machinery appropriate to the property.

The agricultural relief reduces the market value of the agricultural property by a flat rate of 90%. If agricultural assets don't qualify for agricultural relief, they may qualify for business relief (Inland Revenue, Ireland 2002b). Business relief was introduces in the Finance Act, 1994, nearly 20 years after the agricultural relief. The business relief reduces the market value of business property by a flat rate of 90% in the same way as the agriculture relief. Only farmers can use the agricultural relief. For the purpose of the relief, a farmer is defined as:

- an individual
- who is domiciled in Ireland; and

- at least 80% of the gross market value of whose assets represented on the valuation date by agricultural property—*after* taking the gift or inheritance.

If the agricultural property is sold (or compulsorily acquired) within six years of the date of the gift or inheritance, the relief is withdrawn if the released capital not is replaced within one year by other agricultural property. The withdrawal of the relief does not apply in relation to the sale of crops or timber. The withdrawal of the relief does also not apply if the beneficiary dies before the sale or compulsory acquisition.

If the individual in receipt of the benefit is not resident in Ireland for all of the three tax years after the Valuation Date, the relief is withdrawn.

Gift tax is charged on gifts reduced with the same threshold as inheritance tax. The tax is payable by the donee (the person receiving the gift). The tax rate for gift tax is also the same as the tax rate for inheritance tax (Inland Revenue, Ireland 2002f).

The standard rate of *motor taxation* for a general haulage tractor is EURO 162.52 per annum. A farmer only pays a reduced rate of EURO 62.23 per annum for tractors that only or chiefly are used in the agricultural production (DAFF 2001b, p. 132). It is relative strong restrictions for use of reduced rate tractors outside the farm.

3.6.6 Evaluation and significance

In the annual publication about the agricultural policies in OECD countries (OECD 2002), OECD describes the latest changes in taxation of agriculture in this way:

> *"In 2000 some adjustments were made to existing tax measures that benefit farmers. The accelerated capital allowance scheme for necessary expenditure on pollution control from activities was extended up until April 2003. The allowance is subject to a maximum that was increased from IEP 15 000 (euro 19 000) to IEP 25 000 (euro 32 000) (for 50% of the expenditure of which the relief is claimed, whichever is lower). The period over which it can be claimed was reduced from eight to seven years. However farmers will be able for claim relief in any of the seven years and not only the year in which the expenditure took place.*
>
> *As in previous years, all farmers who were not registered for VAT were entitled to a flat VAT refund on their purchases of inputs. The refund rate was increased from 4% in 1999 to 4.2% in 2000.*
>
> *Schemes where farmers are totally or partially exempted from income tax or increases in stock values were continued. These relieves allows for a general 25% exemption while the rate applicable to young trained farmers is 100%. Stamp duty relies on gifts and sales of land to young trained farmers were increased from two-thirds to 100%."*

Table 3.23 Farm households' income and direct taxation in EURO. 2000. Ireland

	Farm households	Non-farm rural households	Urban households	State average household
Farming income	13,445	306	17	1,070
Non-farm employment	14,339	21,026	29,650	26,075
Other direct income	1,809	2,779	3,816	3,375
State transfers	3,518	4,559	4,178	4,240
Gross income	33,111	28,670	37,661	34,760
Less total direct taxation	3,454	4,136	7,123	6,003
Disposable income	29,657	24,534	30,538	28,757
Persons per household	3.56	3.16	3.00	3.08
Gross income per household member	9,301	9,073	12,554	11,286
Disposable income Per household member	8,331	7,764	10,179	9,337

Source: DAFF (2002)

In the tax year of 2001 approximately 101,000 farmers (full-time farmers and "Trader Farmers") were assessed for tax. In addition, there are about 14,000 farmers who are assessed periodically, so the total numbers on records to the Revenue Commissioners were 115,000. However, only 40,100 farmers (provisional estimates) were actually liable to pay tax on farming profits (DAFF 2002, p 107). These 40,100 farmers are expected to pay EURO 97 million in tax and EURO 33 million in PRSI contributions as shown in table 3.24.

Table 3.24 Farmers Income Tax and PRSI, 1995 to 2001. Ireland. Million EURO

Year	Tax paid on farm profits	Paye on other earned income	PRSI	Total
1995	89	99	38	226
1996	99	117	32	248
1997	108	132	33	273
1998	99	146	30	276
1999	105	160	34	300
2000	103	N/A	36	N/A
2001	97	N/A	33	N/A

Source: DAFF (2002)

The greater part of the taxpayers is placed in the PAYE sector. This sector contributed 82.6% of the total income tax in 2001.This compares to only 1.1% from the farmers and 16.3% from other self-employed. The average individual tax payment from each of these sectors in 2001 is estimated at EURO 7,103 for PAYE, EURO 1,173 for farmers on farm profits and EURO 7,856 for other self-employed (DAFF 2002, p. 108). The average income tax paid by sectors in the period 1995–2001 is shown in table 3.25.

Table 3.25 Average Income Tax Paid by Sector in EURO, 1995 to 2001. Ireland

Year	Workers PAYE	Farmers	Other self-employed
1995	5,054	1,183	4,593
1996	5,386	1,281	4,906
1997	5,655	1,362	5,870
1998	5,817	1,220	6,415
1999	6,392	1,319	6,728
2000	6,672	1,359	7,792
2001	7,103	1,173	7,850

Source: DAFF (2002)

The last available data on PAYE tax paid by farmers and/or their spouses on other earned income is for 1998/99. These show that EURO 160 million was paid by some 32,200 individuals or couples involved in farming (DAFF 2002, p 107).

3.7 France

3.7.1 Introduction

French farmers face in principle the same rules for taxation and are subject to the same taxes as other self-employed tradesmen. There are, however, some special rules that only concern agriculture. In addition, there is a special social security system for French farmers, their families and farm workers.

3.7.2 Income taxation

The individual income tax is a household tax, by which a household is normally comprised by the spouses and their unmarried children less than 18 years of age (EFAC 2000 p 36).

Income from agriculture is one of several income sources subject to the income tax. Agricultural income can be calculated according to four different modes (Parsche et al. 2000, Andersen *et al.* 1994): Ordinary book keeping (*régime du bénéfice réel normal*), simplified book keeping (*régime du bénéfice réel simplifié*), simplified income calculation (*régime du forfait* and *bénéfice forfaitaire agricole*) and a transition scheme (*régime transitoire*). The amount of annual sales determines the mode according to which agricultural income has to be calculated. The simplified income calculation scheme is applicable to farmers whose annual turnover as two years average is less than EURO 76,224 (EFAC 2000, p. 104). The estimation of the farm income under the simplified income calculation scheme has two stages of which the first is collective and the next personal.

A farmer has always the possibility, the option to do book keeping, although the amount of annual sales would allow the calculation of agricultural income under the simplified income calculation scheme.

The forest income is always taxed under the simplified income calculation scheme, and the income is only dependent on the fixed annual value of the ground, a value that is very low.

About 510,000 farms use the simplified income calculation scheme and about 240,000 farms have to keep records, 50% in the ordinary way and 50 % in the simplified way. However, farms under the simplified income calculation scheme only cover 20 to 30% of the French agricultural production.

Whether taxable agricultural income is lower under the simplified income calculation scheme than under book keeping is an empirical question. The study of Wolffram *et al.* (1990) demonstrates that it can go both ways. Depending on the type of farm, the farm size and the share of rented land, agricultural income calculated under the simplified income calculation scheme can be lower or higher than under book keeping.

The total household income is divided by a coefficient in order to obtain the net taxable income for each part of the household (EFAC 2000:36). The tax rate is then applied to that result. The tax rate is a progressive rate between 0% and 54% in 2000 (Parsche et al. 2000, p. 65).

There are some special rules for farmers. Firstly, young farmers that start farming are allowed to reduce their taxable agricultural income for five consecutive years by 50% (Parsche *et al.* 2000). This special rule is also applied to tradesmen and craftsmen who start their own business. Secondly, there is a 20% reduction of taxable agricultural income if the farmer keeps records.

3.7.3 Property taxation

Real estate is subject to a property tax that is collected by local communities (region, department). There is also a land tax, but its significance is decreasing (EFAC 2000, p. 36).

3.7.4 Social security system

France has its own social security system for farmers, their families and farm workers. Around 42% of all public support to French agriculture was provided through the special social security system for French agriculture in 1999 and 2000 (MAP 2001).

Its aim is to provide a level of social security contributions for active farmers that are comparable with general social security contributions. The special social security system for French agriculture covers foremost health insurance and an old age pension scheme. The share of total expenses going to health insurance and the old age pension scheme was 39% and 56%, respectively, amounting to a total of 95% of the total expenses within the social security system for French agriculture. The remaining 5% of the total expenses are used for family welfare measures, holiday support etc. The farmers' social security contributions were around 18% of the total expenses of the social security system. The remaining part is covered by the State through the state budget and other sources (e.g., product fees on tobacco, sugar, and alcoholic beverages).

The social security contributions of a farmer depend on his/her own income and a average national annual income (the so-called social security ceiling (EFAC 2000, p. 204). For example, the rate of the agricultural health insurance is 10.84% with a base up to 6 times the social security contribution (EFAC 2000, p. 204).

3.7.5 Other taxes and fees

There exist taxes and fees on energy, insurance schemes and residences (Andersen *et al.* 1994:221f). In addition, French farmers pay a fee collected by the agricultural administration based on the economic valuation of the farm (Andersen *et al.* 1994, p. 221).

3.7.6 Evaluation and significance

It is difficult to quantify the value of the special tax measures directed to French farmers. It appears that there are only few measures that are solely applied to agriculture. Parsche *et al.* (2000 p. 17) suggest that income from agriculture calculated by the simplified income calculation scheme may be 50% lower than incomes using book keeping. Parsche *et al.* (2000 p. 17) argue, however, that simplified income calculation scheme must foremost be viewed as a means to ease income calculation, and not as a measure to provide support (although it has that effect). This statement is supported by the fact that there exists an incentive for farmers to switch from simplified income calculation to book keeping.

3.8 Switzerland

3.8.1 Introduction

The structure of Switzerland being a confederation with three administrative levels, *Bund*, *Kanton* and *Gemeinde*, implies that each level has the right to collect certain taxes and fees. Due to the partially strong sovereignty of the c*antons*, there might be different rules how to treat farmers and farm families between the c*antons*.

In general, agriculture in Switzerland appears to be treated only slightly different from the countries' other sectors in matters of taxation.

3.8.2 Income taxation

The income tax is collected by the regions (c*antons*), but split between the regions and the federal state. There is no special treatment for agricultural income, which is calculated according to book keeping records. One exception concerns the sale of agricultural land. Usually, taxable income from sale of land is calculated based on the difference between the sales price and the book keeping value. Since depreciation of land is quite seldom, taxable income corresponds to the added value of the land since the purchase. The taxable income from the sale of agricultural land, however, is often zero, because it is calculated as the difference between the price at which the land was purchased and its book keeping value (which often will be the same).

3.8.3 Property taxation

The property tax belongs to the regions. The valuation of agricultural land for property tax purposes is based on the method of economic valuation (*Ertragswert*). This method gives values that are significantly lower than those values that could be obtained through sale in real estate markets (Gerber 2002).

3.8.4 Social security system

The main result of equal treatment in taxation matters holds true in principal for social security contributions and welfare measures. Farmers are like other persons insured through the Federal Office for Social Security (BLW 2000). A peculiarity concerns the family allowances for small farmers (so-called *Familienzulage*), which is given to small farmers below a certain income level. If the 'pure' income is below CHF 32,000 per farm family[5], then farm families are given a monthly payment for each child. The amount is regionally differentiated (valleys and mountain areas). There is also a higher amount from the third child onwards. The yearly payments vary between CHF 1,980 and CHF 2,280 per child per year (BSV 2001). The total amounts of this support measure were 102 million CHF in 1997 (EFV 1999). Due to an increase of the payments in January 2002, own calculations suggest that the total amount of the *Familienzulage* will probably be around 120 million CHF in 2002. The family allowance for small farmers is mentioned in the Swiss notifications on domestic support to the WTO as a 'green box'-measure.

3.8.5 Other taxes and fees

Swiss agriculture is eligible to a partial refund of the mineral oil tax. Other sectors like forestry, fisheries and transport are, however, also eligible to this refund (SSK 2002).

3.8.6 Evaluation and significance

It appears that there are only a few tax related measures to Swiss agriculture. It is, however, difficult to quantify their financial impact.

3.9 Italy

3.9.1 Introduction

In 1997 there were about 2.3 million farms in Italy with more then 20 million hectares of land overall. About 14.8 million hectares was used as agricultural area

[5] The border increases by CHF 5,000 pr child.

(UAA). 75 % of the farms possessed less than 5 hectares of UAA. Average UAA per farm was 6.4 hectares. The trend in Italia is as in most other countries that the number of farms is decreasing while the average land per farm is increasing.

About 96% of the Italian farms are managed directly by the farmer and the farmer with the help of family labor operates nearly 80% of these farms (INEA 1999).

In Italy the tax revenue is distributed among the State, Regions, Provinces and Communes.

3.9.2 Income taxation

Natural persons resided in Italy have to pay *Personal income tax* (Imposta sul reddito depression persone fisiche–IRPEF) of both regular and occasionally income. The Italian structure of personal income tax is based on six categories of income:

1. Income from real estate properties (income from agriculture, forestry and other estate property including income from buildings)
2. Income from capital investments
3. Income from wages and salaries
4. Income from professional and independent personal services
5. Income from trade and industry
6. Income from other sources.

In each category, the taxable income is determined to own rules. The tax basis is the aggregate income from the six categories of income.

Income from agriculture and forestry is defined as income from real estate properties and placed in category one. Real estate properties in Italy are registered either in the property land registers or in the urban building land registers. If income from properties in these registers is registered with an assigned yield, the income is taxable in income category one as income from real estate properties. Income from agriculture and forestry is taxable in this way as an assigned yield from the particular estate (the cadastral system). Yields from other real estate properties in the land register which is not determined as an assigned value, are taxable in income category six as income from other sources (e.g. income from mines, salt works, lakes, ponds etc.) (Parsche et al. 2000, p. 72).

The taxation of agriculture and forestry income differs in this way essential from the taxation of the other categories of income. The taxable agriculture and forestry income is determined after the land register yield and not on the basis of the actual yield. The yields in the land register are estimated as average values of land and building with input of usual work and capital. The registered values in the land registers are stipulated very low and this result in a preference of agriculture and forestry when it comes to taxation (Parsche et al. 2000, p. 72).

The income from real estate properties is in principle added to that person who has the beneficial right to use the estate and not to the owner if these are different persons.

Taxation on basis of certain standards instead of total net income has long tradition in Italy also outside agriculture and forestry. Until 1998 the standard system included 45 business sectors but in 2001 the system expanded to include about 120 business sectors. Originally the standard system was a system for small enterprises, but in some business sectors as the restaurant sector, the upper limit for turnover is about EURO 35 million.

IRPEF is basically a state tax but since 1998 a part of IRPEF is used in the favor of the regions and the municipalities. IRPEF is progressive by income bracket according to table 3.26.

Table 3.26 The rate 2000 of the Personal income tax (IRPEF) in Italy

Income in EURO	Rate in percent
Up to 7,747	18.5
from 7,747 to 15, 494	25.5
from 15,494 to 30,988	33.5
from 30,987 to 69,722	39.5
from 69,722	45.5

Tax on incomes of legal persons (Imposta sul reddito delle persone giuridiche) is a State tax and the basis of assessment is total net income from companies and other legal persons. There is some exception from the tax liability, i.a. for incomes of agricultural cooperatives, small-scale fisheries cooperatives, or labor and production cooperatives under certain conditions. The tax rate is flat 37% on total taxable income.

3.9.3 Property taxation

In 1992 *the communal tax on immovable property* (imposta comunale immobiliare–ICI) replaced the two previous taxes: the communal tax on appreciation of immovable property (Imposta communale sull'incremento de valore degli immobili–INVIM) and the local income tax on real estates (Imposta communale sui redditi–ILOR)[6].

This tax is a local tax to the municipality where immovable property is situated. The tax is estimated for a calendar year but is payable on a proportional monthly basis for the period during which the immovable property, building land or agricultural land was in possession of the taxpayer. Whether the property was in use in the period or not, has no consequence for the tax computation. The rate is fixed by the municipality and may not be less than 0.4% or more than 0.7%.

Some kind of immovable properties are exempt for this communal tax. In accordance with Parsche et al. (2000, p. 86) the exemption from property tax includes i.a.:

- agricultural properties in mountain areas (over 700 meters as well as particularly selected municipalities, e.g. all 116 municipalities of South Tyrol) and hill situations,
- cultivatable properties of agricultural family businesses or agricultural enterprises;

[6] It was given a transitional period of 10 years.

- agricultural residential buildings.

The tax base of ICI for agricultural properties and buildings are cadastral estimated of values in the land registers or in the urban building land registers. The cadastral values are then multiplied with different factors (75 for agricultural properties, 34 for retail businesses, 50 for offices and industrial buildings and 100 for private dwellings.

For agricultural properties it is a tax-free basic deduction of EURO 25,823. Since 1998 the tax-free basic deduction is only estimated for full-time farmers.

Since 1997 the taxpayers obtain a deduction in the ICI-tax at a value from EURO 103 to maximum EURO 258 for the main dwelling (Parsche 2000, p. 87).

Stamp duty (Imposta de bollo) is payable on the deeds, documents and records listed in an official tariff. It is some exemptions from the tax liability; for instance deeds and documents relating to the granting of agricultural loans and of Community and national aids to the agricultural sector. The rates for stamp duty are a combination of fixed and proportional rates.

3.9.4 Social security system

We have only old information from 1988 of the social security system in Italy. The description of the Italian social security system is based on CEA (1993).

The public social security system in Italy is composed of sickness insurance, child benefit, accident insurance and old-age pension. The benefits from the sickness insurance are about at the same level as in other countries and the farmers' contribution is 6,5 percent of the income tax last year. The tax rates for farmers in the mountain areas are reduced to 5.5 percent. In addition to the payment from the taxpayer, the government supports the social security system. In 1987 the payment from the government was about EURO 650. Farmers can after a time for payments of 15 year, claim pension from the age of 65 for men and 60 for women. The benefit of pension was about EURO 350 per month in 1987 and there are special additional for spouses and children. The payment to the pension fond for farmers in the mountain area is about 40 percent lower than in other areas. The Government transfers to the pension fond correspond with about 59 percent. The basis for the payment to the accident insurance is the cadastral value. The Government gives no contribution to the accident insurance.

3.9.5 Other taxes and fees

Succession and gift duty (Imposta sulle successioni e donazion) is as State tax and the tax is payable jointly of the heirs, donors and donees. Tax is applied on the basis of two scales of progressive rates. The first is applied to the overall value of the assets on net inheritance, and the second is applied to each share and to gifts, and corresponds to the degree of relationship between the deceased and the heirs. The first scale ranges from 3 to 27%; the second ranges from 3 to 33%. Under the second scale there are certain amounts exempted to tax for relatives in direct line.

There are three important *taxes on goods and services*: the tax on mineral oils, the value added tax and the regional tax on production.

Motor fuels and other petroleum products are generally subjects for *tax on mineral oils* (Imposta di fabbricazione sugli oil minerali). This is a state tax. However it is a lot of exemption and use of reduced rates; for instance the reduction is 22% of the full tax for use of a certain quantity of fuel in agriculture, horticulture, forestry and fish farming.

The reducing of the tax on motor fuels is of big importance for the farmers:

> *"From a purely quantitative point of view, this measure is the most important "tax saving" attributable to the agricultural sector: in accounting terms alone, it cuts the cost of intermediate inputs by about 13–14 percent."*
> (INEA 2002, p 56).

Value added tax (VAT) (Imposta sul valore aggiunto) was introduced in Italy by the Presidential Decree October 26 1972 and took effect on January 1 1973. VAT is a state tax. The main rule is that anyone who wishes to set up a business (including handicraft) or a profession must be VAT-registered. The threshold for VAT registration is EURO 8,263. The standard rate for VAT is 20% and the reduced rates are 4 and 10%. Beside the main scheme there are special schemes for some categories of business, smaller trades and farmers.

Regional tax on productive activities (IRAP) (Imposta Regionale sulle atticità produttive) from 1997 is charged on the value of net production resulting from the business purposed within the region. The normal rate of tax is 4.25% but may be increased by up to one percentage point by individual regions. IRAP is charged on the value of net production resulting from the business activity within the region. The tax revenue is distributed among the State, Regions, Provinces and Communes

Agricultural producers, which have a turnover less than EURO 2,582, are among other selected natural and legal taxpayers exempted from the liability to pay IRAP. For farms situated in the municipalities in the mountain areas the limit is EURO 7,746. Those limits for turnover come into force only if the farmer has claimed the special arrangement for exemption from compliance with the legal framework of VAT.

3.9.6 Evaluation and significance

As described in INEA (2000, p. 55) the Italian system for taxation in agriculture is special as it is a composition system in which normal and special regimes co-exist. INEA (2000 p. 56) points out that the Italian agriculture sector has great tax advantages in relation to other industries:

> *"The agricultural sector displays enormous disparities with respect to the rest of the economic system for other parameters characterising the structure of public taxation. First, its composition is dominated by social contributions as compared with revenue from taxes, although this phenomenon has decreased since 1994 with the introduction first of ICI and then of IRAP; secondly, as regards wage labour, the lower rates for social security contributions, together with a smaller share of IRPEF, due to a lower level of taxable income and the presence of casual workers, means that the difference between the overall cost of labour for the enterprise and the net income received by the worker is far less in the agricultural sector than elsewhere, and the difference is considerable. Lastly, an equally*

significant gap is apparent for tax pressure on profits, another element of the primary division of value added, and an index of the ability of the firm to generate profits from its style of management. In the agricultural sector this changed from 13.9% in 1990 to 12.2% in 2000, whilst in the other sectors there was a strong increase from 9.1% to 21.4%. This difference is largely due to the influence of forms of taxation determined on the basis of the cadastral register."

The two most important causes of the low tax burden in the agricultural sector are the lower rate of social security contributions and the taxation on the basis of the cadastral register. INEA (2000, p 57) draw this conclusion in the chapter of fiscal policy and agriculture:

"The conclusion to be drawn from this analysis is that the system of confessions has in most cases only a support function, through considerable savings in taxes for weaker enterprises and those which may be more inefficient from the point of view of the capacity to generate profits. The absolute value of concessions indicates how much costs would rise if the ordinary norms applied; the trend which has been analysed, seems to indicate that the impact would be much greater for the farms with low profitability."

4 The WTO and Taxation of Agriculture

4.1 Introduction

In principle, the WTO rules do not cover national tax policies. Nevertheless, systems of taxation can be relevant under the WTO law insofar as such systems come into conflict with basic principles like non-discrimination and/or affect other countries' rights under specific The WTO agreements like the Agriculture Agreement and the Agreement on Subsidies and Countervailing Measures. Thus, the decisive criteria for assessing whether or not member countries violate their the WTO obligations through systems of taxation, is the way these systems are designed–not the level or size of the taxes themselves.

The term "tax" is not included in the text of the Agriculture Agreement of the WTO, but we have nevertheless identified taxation systems that are relevant for the provisions of the agreement. Still, since tax policies in principle are exempt from member states' WTO obligations, it is difficult to know with certainty how specific tax policies would be affected by the rules of the WTO in a potential dispute. These questions are matters of (legal) interpretations. There is thus a need to look more closely on how these questions have been discussed and handled in WTO meetings and in concluded disputes.

In this chapter we focus on two elements regarding WTO rules and member states' systems of taxation. First, we look at notifications to the Committee on Agriculture that contain tax measures. Second, we look at discussions and disputes on tax measures between WTO members represented in the same committee.

4.2 The WTO notifications containing agricultural tax measures

By searching the WTO website for documents online, we managed to put up a list of the notifications where agricultural tax measures are included. The search was made using the document symbol *G/AG/N*[7] and the entry words *tax, taxes, levy* and *fee*. The first two of these entry words returned the most relevant hits. The period searched for was January 1995 to March 2002.

Our search shows that tax measures to a little extent have been notified to the WTO as such. In some notifications agricultural tax measures are "built into" other measures in a way that makes them difficult to identify. In others, tax measures are explicitly listed, but not quantified. We also identified notifications that included tax measures, but where none of the entry words were mentioned. Consequently, such notifications are not included in our list.

One example of a tax measure being "camouflaged" under other labels is the notification from the Czech Republic dated 21 August 2000 (WTO 2000b). This notification includes the following program: "Support of sale of diesel for farmers 'green diesel' ". On a meeting in the Committee on Agriculture in September 2000 Japan and New Zealand asked for clarifications regarding this program (WTO 2000c). The Czech Republic responded by stating that the program referred to "tax reductions applied on fuel".

Our list includes 37 relevant notifications containing agricultural tax measures (see appendix 1 to this chapter). Four of the countries being accounted for in the country reports of this report are represented. The notifications from these four countries are listed in appendix 2.

From our list of notifications we have identified nine different types of notified tax measures. In table 4.1 these measures are placed into four separate categories of support as described in the Agricultural Agreement.

Table 4.1 Types of tax measures included in the WTO notifications January 1995–March 2002

Domestic support—Amber box (AMS)	Domestic support—Green box	Export subsidies	Special and differential treatment
Taxes which are subtracted from total product-specific or non-product specific AMS (i.e. tax on fertilizers, pesticides or levies/fees paid on milk)	Tax linked savings tool, which allows primary producers to set aside income in high-income years without paying tax until income is withdrawn.	Tax Credit Certificate	Tax exemption for producers for net gains from primary agricultural activities
Individual taxes on surplus production, which are subtracted from total product specific AMS	Marketing levy refunds to farmers		Tax refund
Transport cost subsidy (taxes on fuel)	Fees and taxes paid for various services (United States: state programs for agriculture)		

[7] This symbol stands for notifications ("N) being made to the Committee on Agriculture ("AG").

Table 4.2 on next page shows examples of the WTO notifications containing tax measures. Only notifications relating to "Domestic support" and "Export subsidies" are included in this table.

Table 4.2 Examples of the WTO notifications containing tax measures

Description of measure	Monetary value of measure	Reported—date/year	Reporting period	Country	Document symbol
Domestic support – Amber box (AMS)					
MILK. Support delivered through increases in the price of manufactured dairy products to domestic consumers by the levy paid on milk used in the manufacture of dairy products. Associated fees/levies are subtracted from other product specific support.	$A million 35.9	9 March 2000	1998/99	Australia	G/AG/N/AUS/30
Individual tax on surplus production. Milk and dairy products. Subtracted from total product-specific AMS.	3.2 million Swiss F	25 June 1998	1997	Switzerland/ Liechtenstein	G/AG/N/CHE/15
Non-Product-Specific AMS: Provincial Programs. Fuel tax concessions to the agriculture sector are part of this support.	Canadian $ 146.9 mill	14 June 2001	1998	Canada	G/AG/N/CAN/43
Domestic support – Green box					
Tax linked savings tool, which allows primary producers to set aside income in high-income years without paying tax until income is withdrawn.	$A mill. 20.00	21 March 2002	2000/ 2001	Australia	G/AG/N/AUS/41
Measures exempt from the reduction commitment—"green box". Repayments. Marketing levy refunds to farmers.	36.5 million ISK	23 July 1999	1998	Iceland	G/AG/N/ISL/14
State programs for agriculture. Fees and taxes paid for various services.	US $ 3,334 Million	26 June 2001	1998	United States	G/AG/N/USA/36
Export subsidies					
Export incentive system, basically consisting of Tax Credit Certificate	US$19.98 million	26 February 2001	1999	Costa Rica	G/AG/N/CRI/13

Two types of tax measures have been notified under AMS.[8] One is about taxes and fees that are subtracted from total AMS. The other is about support for certain input factors—like tax exemptions for fuel—used in agricultural production. Notified tax measures under "Green box" include tax concessions or repayments of taxes, fees or levies, for measures that are not directly coupled to agricultural production. Costa Rica is the only country that has notified tax measures under "Export subsidies". The purpose of the "Tax Credit Certificate" was to stimulate exports through credits on tax for exported agricultural products. The summary reports of the meetings of the Committee on Agriculture show that similar systems exist in other countries, but these have not been notified. Costa Rica totally eliminated its "Tax Credit Certificate" system by 30 September 1999. Thus, the system will not be further commented upon.

[8] AMS: Aggregate Measure of Support.

As will be shown later, other tax measures have also been discussed under ”Export subsidies”, but these did not show up in our search findings, either because they have been notified under other labels or simply because they haven't been notified at all. One example of a tax measure not being notified to the WTO is United States' rules on “Foreign Sales Corporation”, which later became subject of a WTO dispute. We'll come back to this later.

The member states of the WTO do not agree on the kind of tax measures that should be notified. There is also disagreement on what measures should be subject to reduction commitments under the Agriculture Agreement. We will explore these disagreements further by looking at the discussions on agricultural tax in the Committee on Agriculture.

4.3 Discussions on tax in the Committee on Agriculture of the WTO

Our search through the WTO website was performed by combining two search criteria: the document symbol *G/AG/*R and the entry words *tax, taxes, levy* and *fee*. The period searched for was January 1995 to March 2002.

Since 1995 tax measures have been discussed in 21 meetings of the Committee on Agriculture.[9] In this chapter we focus on two topics that are of particular interest, both because they involve some of the major actors of the WTO and because they highlight different state views. The first topic is tax exemptions on fuel used in agriculture. The second topic is the question of tax measures being used as export subsidies.

As shown in table 4.2, Canada has notified tax exemptions on fuel as part of the ”Non-Product-Specific AMS”. Slovenia notified a similar measure in 2001.[10] As mentioned earlier, the Czech Republic made a similar notification to the WTO, but without stating explicitly that it included a tax measure.[11] Still, member countries do not agree whether such measures should be notified to the WTO. Canada raised a question regarding this question to the United States on a meeting in the Committee on Agriculture 29–30 September 1999:[12]

“Clarification sought on the treatment of revenue foregone (e.g. fuel tax exemptions for agricultural producers) since under the Agreement on Agriculture, domestic support includes

[9] See summary report of the following meetings: 27 September 2001 (G/AG/R/28), 28–29 June 2001 (G/AG/R/27), 29–30 March 2001 (G/AG/R/26), 14 November 2000 (G/AG/R/25), 27 September 2000 (G/AG/R/24), 28 June 2000 (G/AG/R/23), 22–23 March 2000 (G/AG/R/22), 29–30 September 1999 (G/AG/R/20), 24–25 June 1999 (G/AG/R/19), 24–25 June 1999 (G/AG/R/19), 25–26 March 1999 (G/AG/R/18), 17–18 November 1998 (G/AG/R/17), 30 September–1 October 1998 (G/AG/R/16), 25–26 June 1998 (G/AG/R/15), 19–20 March 1998 (G/AG/R/14), 20–21 November 1997 (G/AG/R/13), 25–26 September 1997 (G/AG/R/12), 13–14 March 1997 (G/AG/R/10), 28 November 1996 (G/AG/R/9), 28–29 October 1996 (G/AG/R/7), 28–29 March 1996 (G/AG/R/5).

[10] See WTO Document: G/AG/N/SVN/18, Dated 14 September 2001.

[11] See summary report of the meeting 27 September 2000 (G/AG/R/24).

[12] See summary report of the meeting 29–30 September 1999 (G/AG/R/20).

both budgetary outlays and revenue foregone by governments at national and sub-national levels."

The response from United States was as follows:

"State level fuel tax exemptions are not included in this notification and have never been included in any of the United States notifications. The United States does not consider that tax exemptions fall within the scope of domestic support programmes covered by the Agreement on Agriculture."

No further clarification on this topic was sought at the September meeting.

Three years later Canada once more drew attention to this topic[13]:

"Elaboration sought regarding the US comment at the September 1999 meeting that it does not consider tax exemptions, particularly fuel tax exemptions, to fall within the scope of domestic support programmes covered by the Agreement?"

This time Japan also raised a question concerning US tax concessions on fuel:

"The US Federal Government has implemented bio-energy programmes, such as tax concessions, which are aimed at the promotion of ethanol usage for fuel. Could the US clarify its position on how these programmes should be treated in the Table DS: 1 notification?"

United States responded by stating that it did not believe that fuel tax exemptions belong in the AMS. In a follow-up comment Canada pointed out that the Annex 3 of the Agriculture Agreement seem to cover tax concessions. Annex 3, point 2, reads:

"2. Subsidies under paragraph 1 shall include both budgetary outlays and revenue foregone by governments or their agents."

The US reply to Canada's comment was as follows:

"US fuel tax exemptions are not necessarily specific to agricultural uses. For example, off-road use exemptions are tax differentials based on user fee concepts of equity. There is no subsidy involved for any off-road users, whether they are farmers or not."

This statement is worthwhile commenting upon. United States claims that its tax exemptions are not specific for agriculture and thus should not be notified as an agriculture measure. If, as United States claims, the measure is a *general* tax concession, the question is whether it falls under "subsidies" as defined in the Agreement on Subsidies and Countervailing Measures.[14] Article 1.1 of this agreement reads:

"1.1 For the purposes of this Agreement, a subsidy shall be deemed to exist if:

(a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:

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[13] See summary report of the meeting 27 September 2001 (G/AG/R/28).

[14] The Agreement on Subsidies and Countervailing Measures do not apply to subsidies maintained on agricultural products (see Article 3, Article 5, Article 6, Article 7, Article 10, Article 15). The provisions of the Agriculture Agreement thus cover agricultural subsidies.

(ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits)"

Here, we need to have in mind that in order to determine whether a subsidy shall be subject to the provisions of the Subsidies Agreement, one has to read article 1 in accordance with article 2 on "specificity". To be relevant for the Agreement the subsidy must be specific to an enterprise or industry or group of industries within the jurisdiction of the granting authority.

In any case, the definition of a subsidy as formulated in Article 1.1 (a)(1)(ii) could be interpreted as covering tax concessions. However, United States claims that its measure is not a subsidy and thus is not a breach of the Subsidies Agreement. Further attempts at interpretations were not pursued by any of the parties.

The exchanges of views taking place in the Committee on Agriculture indicate that probably more countries use tax exemptions on fuel as an agricultural policy measure, than what the few WTO notifications containing this measure imply. Nevertheless, although such tax concessions primarily may be intended for agricultural purposes, often they are *not exclusively* accessible for farmers. Thus, the measures may be relevant for the Agreement on Subsidies and Countervailing Measures. However, insofar as they do not contain subsidy components the measures are not in conflict with neither the Subsidies Agreement nor the Agriculture Agreement.

A powerful actor as United States categorically refuses to notify tax concessions, and apparently no more discussions on the subject has taken place in the Agriculture Committee–i.e. no discussions that match our search criteria. Hence, there are good reasons to believe that such measures do not have to be part of the AMS calculations. So far, state measures containing tax exemptions on fuel have not been seriously challenged under the WTO rules. Thus, the question of whether tax concessions are part of member states' obligations according to the Agriculture Agreement is not finally settled. States do therefore seem to have some leeway to implement such measures without notifying them to the WTO.

Some countries have referred to other tax exemptions that in their view should not be part of the calculations of "Domestic support". For example, at the meeting in September 1999, Australia, Canada, Japan, New Zealand and Thailand asked the EU to clarify the contents of its notification on so-called "Income insurance and income safety-net programs". EU's response was as follows:[15]

"The notified amount concerns insurance subsidies and should therefore be notified in ST/DS: 9. The remaining corresponds to tax exemptions, which should not have been notified."

Thus, EU in its response stressed that the tax exemption measure in question should not be notified under "Domestic support".

We have not been able to identify any detailed or concrete discussions on this topic being carried out in the WTO meetings. Thus, we may have to wait for dispute settlements and/or negotiated interpretations/understandings for further

[15] See summary report of the meeting 29–30 September 1999 (G/AG/R/20).

clarifications on the question of how tax exemptions relates to the calculation of domestic support under the Agriculture Agreement. The same goes for the question of what kind of tax measures contain subsidy components. Moreover, in practice these questions have to be considered on a case-to-case basis.

Tax measures related to agricultural exports are also controversial in the WTO. In 1997 Switzerland questioned the legality of New Zealand's system of exemption on Value-Added Tax for fuel being used on international flights.[16] Switzerland seemed to be of the opinion that this system was in conflict with the Agriculture Agreement, in particular the provisions regarding export subsidies:

> *"It appears that, in New Zealand, aircraft fuel is subject to a Value-Added Tax of 12.5 percent for domestic flights, but that such fuel is VAT-exempt when used on international flights. How does New Zealand view this difference in taxation in the light of Article 9.1 (e) of the Agreement on Agriculture?"*

New Zealand rejected the claim that the system was a breach of the WTO rules:

> *"New Zealand considered that the question is based on a misinterpretation of Article 9.1(e) of the Agreement on Agriculture and of the relevance of New Zealand's practise of zero-rating exports for the purposes of the goods and services tax (GST). According to Article 9.1(e), export subsidies that are subject to reduction commitments include "internal transport and freight charges on export shipments, provided or mandated by Governments, on terms more favourable than for domestic shipments". In New Zealand's view exports subsidies include the subsidized costs of international transport and freight and the subsidized costs of internal transport and freight for exported products. New Zealand's goods and services tax is a broadly based consumption tax, or value-added tax (VAT), imposed on consumption of goods and services by either residents or visitors in New Zealand. There is no differential in the taxing of aircraft fuel for freight within New Zealand. A GST of 12.5 percent is applied on the fuel used for domestic flight and fuel for international flight is tax-free."*

According to New Zealand the system of VAT exemption was neither discriminating nor exclusively designed for the export of agricultural products. Thus, New Zealand argued that this system was not a breach of neither the Agriculture Agreement or of other WTO rules.

Questions concerning tax exemptions and export subsidies have also been raised in connection with Colombia's notifications on its so-called "Tax Reimbursement Certificate" (CERT).[17] CERT is an instrument that allows for the refunding of the equivalent of all or some of the indirect taxes (tariff duty, the VAT, and "industry tax") paid by the exporter of agricultural products. On a meeting in March 2000 Argentina, Australia, Canada and the EU asked for clarifications regarding this system, in particular concerning the potential export subsidy component of the measure. Colombia's response was as follows:[18]

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[16] See summary report of the meeting 20–21 November 1997 (G/AG/R/13).

[17] See summary report of the meeting 22–23 March 2000 (G/AG/R/22).

[18] There were no references to tax or CERT in Colombia's notifications. Thus, these notifications were not included in our list of tax related notification to the WTO.

"The average effective CERT for agricultural products was 2.8% of the f.o.b. value of exports. In turn, studies indicate that, for agricultural activities, indirect taxes represent on average 4.4% of the national value added, a figure that is higher than the equivalent CERT refund granted to agricultural products since 1996. Because of this differential, Colombia considers that the CERT programme does not carry with it a subsidy component."

Thus, according to Columbia its system of refunding indirect taxes to exporters did not contain a subsidy component. Nevertheless, tax systems that contain elements of refunding or exemption of tax for exports of agricultural products, are controversial in the WTO. Controversies on this topic were highlighted in the dispute between the EU and the United States on "Foreign Sales Corporation" (WTO 1999a, 2000a). We look closer at this dispute in the following sections.

4.4 WTO disputes on agricultural tax

Taxation systems have been discussed for a long time in the WTO and in the GATT before 1995. In the 1970s, under GATT, there were four important disputes regarding national taxation systems. EC and others challenged parts of the taxation system of the United States–related to the so-called "Domestic International Sales Corporation" (DISC). United States on its part challenged the so-called "territorial tax systems" of France, Belgium and the Netherlands (Hufbauer 2000). The disputes resulted in four panel reports, which collectively have been named the "Tax Legislation Reports". The reports all concluded, but on different grounds, that the national taxation systems contained elements of export subsidies (GATT 1976a, 1976b, 1976c, 1976d). Both the United States and the EC considered the panels to be too critical, and much time was therefore spent on clarifying the conclusions of the "Tax Legislation Reports" during the Tokyo-round of the GATT (1973–79). The panel reports where accepted for adoption by the parties in 1981. Before 1995, under the GATT, the panel reports had to be approved by all parties in order to be legally binding. The clarifications made during the Tokyo-round were important for the subsequent Subsidies Agreement and the Agriculture Agreement, which were both negotiated during the Uruguay Round of GATT (1986–93).

We will not explore further the considerations made by the panels and the GATT member states regarding the "Tax Legislation Cases" of the 1970's since these cases were not specifically about agriculture. These cases are nevertheless important as backgrounders for the later the WTO dispute between the United States and the EU on "Foreign Sales Corporation" (FSC) in the 1990's (WTO 1999a). Moreover, the four disputes were all referred to in the 1990's dispute. In our account of the "Foreign Sales Corporation" dispute we focus exclusively on issues concerning the Agriculture Agreement of the WTO.

A "Foreign Sales Corporation" is a corporation created, organized, and maintained in a qualified foreign country or US possession outside the customs territory of the United States (WTO 1999a: 1). Under US tax legislation these companies obtain a tax exemption on a portion of its earnings ("foreign trade income"). The earnings in question must be generated by certain qualifying transactions, which generally involve the sale or lease of a so-called "export property". Among the elements covered by the term "export property" are agricultural products manufactured, produced, grown, or extracted in the United States. Moreover, special rules apply for agricultural cooperatives. Under certain circumstances, all of the foreign trade income that a "Foreign Sales Corporation" owned by a related qualified cooperative earns form the sale of agricultural or horticultural products will be treated as exempt foreign trade income (WTO 1999a: 1). The special tax treatment for "Foreign Sales Corporations depart from the general US tax laws which imply that the United States asserts the right to tax all income earned "worldwide" by its citizens and residents.

EU claimed that US tax treatment for "Foreign Sales Corporations" had the effect of subsidizing US exports. Thus, EU initiated the dispute settlement procedure of the WTO. According to the EU the US tax law was a breach of the Agriculture Agreement Article 3.3, Article 8, Article 9.1 (d), and Article 10.1 and 10.3 (see WTO 1999b):

Article 3

Incorporation of Concessions and Commitments

3. Subject to the provisions of paragraphs 2(b) and 4 of Article 9, a Member shall not provide export subsidies listed in paragraph 1 of Article 9 in respect of the agricultural products or groups of products specified in Section II of Part IV of its Schedule in excess of the budgetary outlay and quantity commitment levels specified therein and shall not provide such subsidies in respect of any agricultural product not specified in that Section of its Schedule.

Article 8

Export Competition Commitments

Each Member undertakes not to provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member's Schedule.

Article 9

Export Subsidy Commitments

1. The following export subsidies are subject to reduction commitments under this Agreement:

(d) the provision of subsidies to reduce the costs of marketing exports of agricultural products (other than widely available export promotion and advisory services) including handling, upgrading and other processing costs, and the costs of international transport and freight;

Article 10

Prevention of Circumvention of Export Subsidy Commitments

1. Export subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments.

3. Any Member which claims that any quantity exported in excess of a reduction commitment level is not subsidized must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question.

All of these provisions are related to export subsidies.

In September 1998, a panel was established to consider the complaint from the EU regarding the US special tax treatment for "Foreign Sales Corporations". The Panel Report was published in October 1999. The Panel supported the claim put forward by the EU that United States' tax treatment was a breach of several of the provisions of the Agricultural Agreement (WTO 1999a: 293):

"(b) the United States has acted inconsistently with its obligations under Article 3.3 of the Agreement on Agriculture (and consequently with its obligations under Article 8 of that Agreement):

- *by providing export subsidies listed in Article 9.1(d) of the Agreement on Agriculture in excess of the quantity commitment levels specified in the United States' Schedule in respect of wheat;*
- *by providing export subsidies listed in Article 9.1(d) of the Agreement on Agriculture in respect of all unscheduled products."*

United States appealed certain issues of law covered in the Panel Report, among them the Panel's conclusions regarding the Agreement on Agriculture. The report from the Appellate Body was published in February 2000 (WTO 2000a). Even though the Appellate Body departed from the Panel on certain issues, the main conclusions were upheld, namely that United States' special tax treatment for "Foreign Sales Corporations" was a breach of the WTO rules. With respect to the Agriculture Agreement, the Appellate Body concluded as follows (WTO 2000a: 59):

" (d) finds that the United States acts inconsistently with its obligations under Articles 10.1 and 8 of the Agreement on Agriculture by applying export subsidies, through the FSC measure, in a manner which results in, or which threatens to lead to, circumvention of its export subsidy commitments with respect to both scheduled and unscheduled agricultural products;"

Thus, United States was asked to bring the "Foreign Sales Corporations" measure into conformity with its obligations under the Agriculture Agreement. The Dispute Settlement Body specified that the FSC subsidies had to be withdrawn "at the latest with effect from 1 October 2000 (WTO 2001). The United States and the EU thereafter started consultations with the intention of finding a bilateral solution to the problems.

On 15 November 2000, the President of the United States signed into law an Act of the United States Congress entitled the "*FSC Repeal and Extraterritorial Income Exclusion Act of 2000*" (the "Act"). With the enactment of this legislation, the United States considered that the legislation was consistent with the United States' WTO obligations. However, the EU alleged that the Act "appears to replicate the violations of the WTO Agreement found in the original dispute rather than remove them" (WTO 2001: 2). Consequently, the EU requested the establishment of a panel to consider whether or not the new US measures where in compliance with the recommendations and rulings of the Dispute Settlement Body. The new Panel Report was published in August 2001 and concluded that the new US measures did not bring the United States in compliance with its WTO obligations. The Appellate Body upheld these conclusions.

Thus, arbitration was carried out by the original panel with the intention of determining the appropriate amount of countermeasures from the EU (WTO 2002). The Arbitrator concluded that the amount of countermeasures proposed by the European Communities (US$ 4,043 million) was an appropriate level. Thus, WTO allowed for trade sanctions that were 20 times the amount levied in any previous WTO ruling. This raised considerable concern in the WTO system and made the Director-General Mike Moore to urge the parties to resolve the differences between them:

"*The arbitration ruling marks a further stage of WTO involvement in this long-running and difficult dispute. I have been following the FSC case closely and I commend both parties for working in a constructive manner throughout the duration of this dispute. I urge both parties to continue to cooperate and work toward resolving this dispute and the others between them in an amicable and constructive fashion. The European Union and the United States are among the most important members of this organization and both hold a special responsibility to ensure the continued health and soundness of WTO and global trading system.*"[19]

4.5 Summary

This short presentation has shown that the *way* national taxation systems are *designed* can bring them in conflict with the provisions of the Agriculture Agreement of the WTO (and other WTO agreements). But many tax measures specially intended for agriculture purposes may still be used as legitimate instruments without breaching WTO rules. Tax exemptions and tax refunding for fuel are examples of this.

Nevertheless, controversies do arise with respect to tax measures under the Agriculture Agreement. Our search through WTO documents shows that there are uncertainties with respect to both the question of which measures should be included in the calculation of AMS and to the question of whether a measure containing tax exemptions and/or tax refunding for exporters is a breach of the provisions of the Agriculture Agreement on export subsidies. Tax measures *may* fall under the definition of subsidies according to both the Agriculture Agreement[20] (agriculture specific measures) and the Subsidies Agreement (general tax concessions).[21] However, national tax measures have to a little extent been challenged under WTO rules. Consequently, not many legal interpretations of these issues have been carried out.

As the dispute between the US special tax treatments for "Foreign Sales Corporations" illustrates, there is nevertheless a potential in the Agricultural Agreement that can be exploited. Thus, every member state of the WTO run the risk of their systems of agriculture taxation being challenged by other member states.

One noteworthy observation is that there apparently haven't been any controversies regarding taxation systems that contain measures of reduced income tax for farmers–despite the fact that reduced income tax can have the same effect as direct budgetary support. One reason for the lack of attention towards such measures may be that member states of the WTO do not consider these measures to be of much relevance for the provisions of the Agriculture Agreement. Alternatively, no member states have *so far* considered reduced income tax as a problematic trade distorting measure.

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[19] Press release from the WTO (Press/311, 30 August 2002). See WTO web site: http://www.wto.org/english/news_e

[20] See Annex 3 and the provisions on export subsidies.

[21] See Article 1 and the provisions on export subsidies.

5 Overall evaluation and outlook

5.1 Income tax basis

The selected countries have different principles to determine the taxable income. We can simplify these principles in this way:

- The Cadastral and similar principles
- The book keeping principle (accounting principle)
  - The accrual method
  - The cash method.

If accounts form the basis of the tax computations the tax base may be the income of the specific year that is to be taxed or the average of the income of this year and a fixed number of the previous years. Both the accrual and the cash account methods can form the basis for the average.

The main rule for industrial or business enterprises is to determine the taxable income on basis of book keeping according to the accrual method. In some countries individual enterprises and partnerships have opportunity to use both the cash method and the average principle.

In *the US* both farmers, other self-employed and relative big corporations can choose between the accrual and the cash method, but in general most farmers prefer the cash method as they find it easier to keep cash method records. Sole farmers and partnerships may also form three years average income as basis for the assessment. If a farmer elects to use the averaging rules, ha has to use the rules for minimum three years before he can return to assessment of a yearly basis.

The opportunity to choose income averaging is now only available for farmers and only on farm income.

No method of bookkeeping is prescribed for *Canada*, however the Generally Accepted Accounting Principles are to be considered as directive without any legal obligations. Sole proprietors or partnerships can choose between either accrual method or cash method. In general the cash method is preferred whereas agricultural companies have an obligation to keep records.

In 1987 the possibility to calculate taxable income as average over several years was abolished. Instead the farmers were offered a governmental program to stabilize their income. Through the Farm Income Protection Act it is possible for the farmers to open a Net Income Stabilization Account (NISA).

In *Australia* small business taxpayers can use a cash accounting system and primary producers also are imposed to average the taxable income over a maximum of five years. The primary producers can chose to withdraw permanently from the averaging system and pay tax at ordinary rates. However, once the farmer has made this choice, it will affect all his assessments for subsequent years and cannot be revoked.

In addition to the average system Australia also have a government program to even the incomes of primary producers. The Farm Management Deposits (FMD) is only available to individual primary producers who satisfy the eligibility conditions of the scheme. Only taxable income from primary production can be invested in a FMD. Farmers earning more than AU$ 50,000 off-farm taxable income in the year of deposit cannot obtain the tax benefits of FMD.

There are four different methods in *Germany* to calculate the agricultural income: (a) book keeping, (b) keeping an inventory (simplified book keeping), (c) flat method ('unit valuation'), and (d) income valuation by the financial administration. Farms are obliged to keep records if they exceed a certain size. Around 30% of all German farms keep records, 15% use simplified book keeping and 50% of the farms calculate according to the flat method. The income calculation in the flat method is based on the economic value of the land. The estimated profit per hectare is directly linked to the so-called 'hectare value' which is a measure of the potential land quality.

If a farm does not calculate income according to one of these three methods; then the financial administration will undertake an income valuation by itself.

Income earned from agricultural activity by companies is always defined as income from trade and business and agricultural companies are therefore obliged to ordinary book keeping.

All farmers in *United Kingdom* have to keep accounts as basis of the tax computations.

The British accounting systems follow the Anglo-Saxon tradition and are less regulated in the legislation. For farmers and market gardeners there are a special election available to average out the profits of two years. There are some limitations in connection with this right.

In *Ireland* individual full-time farmers may elect to be assessed in the normal way on annual basis or on the basis of the averaging farming profits and losses of three years. If the farmer or the spouse also has another trade or profession (except income from farmhouse holidays), they cannot elect the averaged way for taxation.

If the election for averaging is made, the farmer must remain on averaging for a minimum of tree years.

In *France* agricultural income can be calculated according to three different main modes: Ordinary book keeping, simplified book keeping and simplified income calculation. The amount of annual sales determines the mode according to which agricultural income has to be calculated. The simplified income calculation scheme is applicable to farmers whose annual turnover as two years average is less than EURO 76 224. A farmer has always the possibility, the option to do book keeping, although the amount of annual sales would allow the calculation of agricultural income under the simplified income calculation scheme.

More than 50% of the French farms use the simplified income calculation scheme but these farms only cover 20 to 30 of the French agricultural production.

In *Switzerland* are the farmers obliged to keep accounts like other self-employed tradesmen.

Incomes from agriculture and forestry are in *Italy* defined as incomes from real estate. Real estate properties are registered either in the property land registers or in the urban building land registers. Income from agriculture and forestry is taxable as an assigned yield from the particular estate (the cadastral system). The yields in the land register are estimated as average values of land and building with input of usual work and capital. The registered values in the land registers are stipulated very low and this result in a preference of agriculture and forestry when it comes to taxation.

Taxation on basis of certain standards instead of total net income has long tradition in Italy also outside agriculture and forestry. Until 1998 the standard system include 45 business-sectors but in 2001 the system rise to include about 120 business-sectors.

In most of the selected countries income from agriculture does not represent a separate kind of income even though there are some detail regulations regarding farm income. The taxable income from agriculture is put together the farmer's other taxable incomes in the tax assessment. Incomes from farms are, to put in briefly, taxed like income from other businesses of a comparable size.

In *Italy* and *France* farms income is taxed independent of other incomes.

5.2 Capital Gain

The exact definition of Capital Gain varies from country to country. Shortly capital gain is the net increasing of a property's value from the point of time for acquisition to the point for disposal.

In *the US* profits and losses from sale of fortune articles are (depending upon classification) treated as normal income or in accordance with the special rules for *capital gains* and losses. Self-employed and farmers can in special cases deduct a *business tax credit* and an *investment tax credit* from the computed tax.

The Income Tax Act in *Canada* has no rule for limits to *capital gains*, however the Canadian Consolidated Revenue Act has developed some rules of thumb. Especially for farm capital equipment there is a free amount over the life period of

CA $ 500,000 for sale profit and capital gains. Investment items are qualified farm property when they have been the property of the farmer or his family for at least 24 months.

In principle, there are no special rules for the capital gains tax in connection with agriculture in *the United Kingdom*. The farmhouse is a private asset and therefore exempt from Capital Gains tax.

In *Ireland* there are special rules for disposal of a business or farm if the seller is 55 years or more. The rules are the same for farms as for other businesses, but the rules are some different for disposal outside of family and disposal within the family. If the disposal is outside of family and the seller is 55 year or more, it is full relief for capital gains tax if the compensation for the whole or part of the business assets or farm not exceeds EURO 476,250. The business assets must have been owned and used in the business throughout minimum the last ten years before the disposal. For farms the rules are the same as for the business assets.

For disposal to the seller's child it is no limit for the compensation. Therefore it is full relief also when the compensation is more than EURO 476,250. The same rules applies also for disposal to a niece or a nephew who has worked full-time on the farm or in the business for the previous five years.

5.3 Special allowance in agricultural income

Of the selected countries only *Germany* and *France* have special agricultural income allowance in the calculation of income tax. In Germany all individuals with agricultural income are eligible to income allowance as long as gross income is below EURO 32,250 (single people) or 64,500 (married people) and gross agricultural income is higher than the income allowance. The income allowance was EURO 700 (single people) or EURO 1,400 (married people) in 2001. The income allowance is independent of the method of income calculation.

In *France* the government work for increasing the part of farmers who keep account. A farmer that keeps accounts is therefore entitled to a 20% reduction in the taxable agricultural income.

In *Switzerland* it is a specific family allowance for small farmers below a certain income level. If the 'pure' income is below CHF 32,000 per farm family[22], then farm families are given a monthly payment for each child. The amount is regionally differentiated (valleys and mountain areas). There is also a higher amount from the third child onwards. The yearly payments vary between CHF 1,980 and CHF 2,280 per child per year. The total amounts of this support measure were 102 million CHF in 1997. Due to an increase of the payments in January 2002, own calculations suggest that the total amount of the Familienzulage will probably be around 120 million CHF in 2002. The family allowance for small farmers is mentioned in the Swiss notifications on domestic support to the WTO as a 'green box' measure.

[22] The border increases by CHF 5,000 pr child.

5.4 Depreciation and valuation of stocks and livestock

The systems of depreciation for tax purposes vary from country to country. The depreciation methods can be different, in the main degressive or linear method. The rates for the specific items are different and in some countries they allow an extraordinary allowance in the year or purchase.

In the same way there can be large variation between the countries regarding tax valuation of stocks and livestock. In this report we have not focused on depreciations and valuation of stocks or livestock because this is an extensive area, however this is of big importance to the tax level.

5.5 Taxes on property

Net wealth tax is a historic tax in more and more countries. Of the selected countries for this report, only *France* has net wealth tax today.

Land tax or *property tax* is in most countries a local gross tax. What types of property that is taxed by property tax and how the property is valued varies between the countries. In federal countries as the US, Canada and Australia it also varies between the states. The value of agriculture and forestry properties is usually set to the use value as agriculture or forestry and not to the market value.

In *the US* it is no property tax on federal level. However, in most of the states there are either real estate taxes or similar property taxes. The value used for property tax of agricultural properties is 40 to 70 per cent lower than the market value. In some states the property tax rates also are put lower for agricultural properties than other properties.

Also in *Canada* it is the provinces or municipalities that claim the real estate taxes. The character of the tax is very different in the different provinces. Among the real estate taxes is also the school tax, raised by the school districts, the assessment basis of which is the real estate value. Since the property concept is very wide the property taxes are high in international comparisons. There are large differences in valuation of farmland and farm residences for property tax, but in all provinces the property taxation of agriculture is much lower than taxation of other properties.

The general Land tax in *Australia* is a state and territory tax on land in all the states. The rules are somewhat different in the different states, and only the rules of the state of Victoria are described in this report. Land tax is an annual tax on all land in Victoria with a total unimproved value of AU$125,000 or more. There are several exemptions from this principal rule. The two most important exemptions are concerning land used for residence and the greater part of land used for primary production.

Regarding property tax agricultural property and non-agricultural property is treated in the same way in *Germany*. The farm sector has certain benefits, however, since the calculation of agricultural property is based on the economic value of the farm with its key date from 1964.

The United Kingdom council tax for dwelling houses is partial payment for several local services as water, sewage and rubbish and partial a direct tax to the municipal and the district. Farm houses, farm cottages, croft houses and houses connected with fish farms are placed in a lower valuation band then in which they otherwise would be placed. Instead of council tax, non-domestic properties are liable to business rates, but agricultural land and buildings are exempt from business rates.

The Residential property tax in *Ireland* is an annual tax chargeable on the net market value of residential property. It is no exemption for farmhouse as residential building.

In *France* real estate is subject to a property tax that is collected by local communities. There is also a land tax, but its significance is decreasing.

Also in S*witzerland* is the *property tax* a local tax. The valuation of agricultural land for property tax purposes is based on the use value as agriculture and not on the value that could be obtained through sale in real estate market.

In *Italy* it is a communal tax on immovable property. There are different exceptions and deduction for the agriculture sector respecting this tax, for example for agricultural properties in the mountain areas and for full-times farmers. This tax is also lower for agricultural and forestry properties since the calculation of such properties is based on the cadastral value and not on the farm real value.

Stamp duties are taxes on documents that are necessary to transfer ownership of real property. It is no stamp duty to pay for transfer of movable property as plant, machinery, stock, livestock etc. The stamp duty regulations vary from one country to another, however as a main rule there are a couple of exemptions or relieves from the stamp duty.

Stamp duty is a State and Territory tax in *Australia* and the rules vary between the states. As a support to younger family members for taking up ownership of family farms, transfer of family farms were in 1993 exempt from stamp duty in Victoria. In 1993 only a narrow circle of family members were exempted from the tax, but this circle has now been widened. Since June 1 1999, the exemption also include the transfer of land used for primary production from a company to natural persons if they are relatives of each other and own all the shares.

In *Ireland* the amount of stamp duty depends of the purpose of the document. There are a couple of exemptions or relieves from the stamp duty. For example the transfer of land to a Young Trained Farmer is exempted from the stamp duty.

In *Italy stamp duty* is payable on the deeds, documents and records listed in an official tariff. It is some exemptions from the tax liability; for instance deeds and documents relating to the granting of agricultural loans and of Community and national aids.

5.6 Gift and inheritance tax

It is quite different rules for gift and inheritance tax in the selected countries. We have only concentrated on special rules for agriculture or forestry enterprises. On the whole however, in several countries there are different tax benefits with transfer of business properties compared with private properties (except dwellings).

However, the basis for gift and heritance tax is often the use value for agriculture and forestry properties instead of a real value.

In *the US* the system for Federal estate and gift *tax* is a very special system that applies a unified tax rate structure and a cumulative lifetime credit to gifts and transfers of money and other property at death. There are three factors that in addition reduce gift and estate tax in small family businesses; special valuation of farmland, deduction for family-owned business and installment payment of estate tax. For all these three factors special terms are attached.

Transfers of gifts and estates in *United Kingdom* are in principle taxable on the system of inheritance tax, but in addition to different tax-free basic deductions there are several limitation and exceptions from the liability to pay inheritance tax. Transfers of business assets are separately privileged in the British rules for inheritance tax. There are inheritance tax relieves available for business and business assets, for agricultural property and for woodlands. The relieves depend on different terms as a minimum period for ownership and use of the property. Both the business relief and agriculture relief is 100% or 50% depending on what sort of assets are transferred.

In *Ireland* Inheritance and gift tax is charged on the market value of the property comprised in the inheritance. The rate is 20% in all classes after a threshold. However, there are various exemptions from gift and heritance tax, for example Agricultural relief and Business relief. Only farmers can use the agricultural relief. If the agricultural property is sold (or compulsorily acquired) within six years of the date of the gift or inheritance and the compensation is not replaced within one year by other agricultural property; the relief is withdrawn.

5.7 Social security contributions

Germany, France and Italy have special social system for farmers. *German* farmers have their own social security system covering an old age pension scheme, a health insurance scheme and an accident insurance scheme. This system is open for farmers, their families and agricultural workers. This special system for social security is strongly subsidized by the federal government.

France has its own *social security system* for farmers, their families and farm workers. Around 42 % of all public support to French agriculture was provided through the special social security system for French agriculture in 1999 and 2000. The social security contributions of a farmer depend on his/her own income and an average national annual income.

As in Germany and France the *Italian* government supports farmers in the *social security* system. There are also several specific benefits for farmers in the mountain regions.

In the other countries, *US, Canada, Australia, UK, Ireland* and *Switzerland* there are no special social system for farmers.

5.8 Taxes on goods and services

In *the US* sales tax is a state and local consumption tax. Rules and rates are different in the different states and the total sales tax including both state and local tax is between 4.0 and 9.75 per cent. In this report it is only referred to rules for the state sales tax in Minnesota. A lot of goods and services used in agricultural production are not taxable such as animals, feed for animals, veterinarian services, plants and seed, machinery and equipment, building materials and different services.

In *Canada* there are both Goods and Services Tax (GST) and Harmonized Sales Tax (HST). GST is a federal tax and HST is a provincial tax. Only three provinces (Nova Scotia, New Brunswick and Newfoundland) have harmonized their provincial sales tax with GST to create the harmonized sales tax (HST). The tax rates are either 0 and 7.0 percent (GST) or 15.0 percent (HST including GST)). The HST applies to the same base of goods as GST at a rate of 15 percent. Of this 7 percent is the federal part and 8 percent is the provincial part. Businesses or farms with total sales above CA $ 30,000 have to register for GST/HST.

The supplies of most agricultural and fishing products are zero-rated, however several agricultural products not for human consumption like plants, hides, firewood etc. are taxable to a higher rate. However, supplies of both raw tobacco and wool not processed further than washing, is zero-rated. Supplies of inputs like fertilizer, feed, pesticides and some agricultural equipment are zero-rated too.

The Goods and services tax (GST) in *Australia* is in principle a Value Added Tax (VAT). Therefore companies, farmers, tradesmen etc. can deduct the greater part of GST paid on inputs. The base of the tax is very wide and includes most goods, services and activities. The rate for GST is 10 per cent, however in addition several groups of goods and services are zero-rated.

Food for human consumption is normally zero-rated. Farmer's delivery of some products is not classified as food for human consumption before the products have passed through further treatment.

Sole traders or companies with an annual turnover of AU$ 50,000 or more; have to be registered for GST. If the annual turnover is less than the threshold it is access to voluntary registration for GST. It is allowed to use cash accounting for GST if the annual turnover is AU$ 1 million or less or if the accounting for income tax purpose is on a cash basis.

There are no special GST-rules for primary producers except the zero rating of several products from the primary farm industries.

Registration limit for Value added tax in *United Kingdom* is £ 55,000 per annum in dutiable turnover. There are three different rates for VAT: Standard rate at 17.5 %, reduced rate at 5,0 % and zero rate at 0,0 %. For agriculture there are four main groups of zero-rated products: Food for human consumption, animal food, live animals and seeds and plants to provide food for human or animal consumption.

The flat rate scheme is an alternative to VAT registration for farmers. A farmer registered as a flat rate farmer, do not account for VAT and can therefore not reclaim input tax. A flat rate farmer can, however, charge and keep a flat rate "addition" (FRA) when he sell goods or goods and services to VAT registered customers. FRA is not VAT, but compensation for losing input tax on purchases.

The flat rate in UK is 4,0% and it is not intended as reimbursement of all the VAT incurred on purchases.

In *Ireland* individual and legal persons are liable for Value added tax (VAT) if the annual turnover exceeds limits of EURO 51,000 for goods or EURO 25,500 for services. The standard VAT rate is 21%. In addition to the standard rate, it is three reduced rates: Zero-rate, 4.3% and 12.5%. Food used for human consumption, certain fertilizers, seeds and plants used to produce food, certain animal feeding stuffs, supply and sowing of crops for food production are zero-rated.

Live animals are rated at 4.3 % and different agricultural services are rated at 12.5 %. Hire of machinery, leasing of milk quota (without land), transport and storage are rated at standard rate.

Ireland applies the EU system of flat-rate farmers. In order to compensate for VAT paid on supplies, the farmer is entitled to a flat rate additional of 4.3% to the selling price for the agricultural products or services. The farmer can only use the flat rate additional with sales to individual or legal persons who are registered for VAT.

The Value added tax (VAT) in Italy is a state tax and the threshold for VAT registration is EURO 8,263. The standard rate for VAT is 20% and the reduced rates are 4 and 10%. Beside the main scheme there are special schemes for some categories of business, smaller trades and farmers.

In Italy it is also a local tax on goods and services Regional tax on productive activities–IRAP–is charged on the net value from the businesses purposed within each region. Agricultural producers, which have a turnover less than EURO 2,582, are among others exempted from the liability to pay IRAP. For farms situated in the municipalities in the mountain areas the limit is EURO 7,746.

Germany, France and *Switzerland* also have Value added tax, but we have not described these in this report.

5.9 Other taxes

This is only partly dealt with in this rapport. We have only focused on different form for tax on fuels. It is quite usual to give tax concessions in the fuel tax for off-roads users. There have been several discussions between the OECD countries how far such tax concessions should be notified to the WTO. The US writes in a reply to Canada:

> *«US fuel tax exemptions are not necessarily specific to agricultural uses. For example, off-road use exemptions are tax differentials based on user fee concepts of equity. There is no subsidy involved for any off-roads users, whether they are farmers or not.»*[23]

In *the US* petroleum tax is not a federal tax but a state tax and it is different rules in the different states concerning state tax on petroleum products. In many states use of petroleum in agricultural or industrial production is exempt from both petroleum tax and sales or use tax.

[23] See chapter 4.3 in this report.

Today there are two *Australian* schemes for rebates and grants for diesel fuels used in agriculture and certain other categories of business activity. On of the two schemes provides a grant per liter diesel and alternative fuels for certain on-road uses. It is also possible for farmers to use this scheme for transport of farm products on public roads. The other scheme comprises off-road use of petroleum products. Farmers eligible for rebate under both schemes have to keep separate records for each scheme.

German farmers have a rebate on the diesel oil tax for off-road use. There are also some allowances on diesel and gas used for greenhouses. Tractors and other agricultural machinery are exempt from car tax.

Irish farmers pay a reduced rate of motor tax for tractors, which only or chiefly are used in the agricultural production. It is relative strong restrictions for use of reduced rate tractors outside the farm.

Swiss agriculture is eligible to a partial refund of the mineral oil tax in the same way as other sectors like forestry, fisheries and transport.

In *Italy* the tax on mineral oil is reduced with 22% for use of a certain quantity of fuel in agriculture, horticulture, forestry and fish farming. The reduction of the tax on motor fuels is of big importance for the farmers.

5.10 Special tax benefits in connection with establishment of a business or for changing the ownership of an enterprise

In several countries it is special tax benefits in connection with establishment of a business or for changing the ownership of a going enterprise. The benefit schemes are usually general for small enterprises and therefore independent of what industry or business the taxpayer carry on.

Young farmers in *France* that start farming are allowed to reduce their taxable agricultural income for five consecutive years by 50%. This special rule is also applied to tradesmen and craftsmen who start their own business.

The *Irish* government prioritizes in different ways the *transfer of land to young, trained farmers* as i) 100% stamp duty relief, ii) 90% agricultural relief from capital acquisitions tax, iii) 100% stock relief for four years after transfer, iv) income tax exemptions for land leased by farmers over 55 years to non-connected persons and v) retirement relief on capital gains tax for farmers over 55 years.

5.11 Tax distribution between central and local authorities

The right to impose a tax is normally divided between central and local authorities. The local part of the taxes is of course bigger in a federal country or in a unitary country (se chapter 2.2 in this report). In federal countries there also can be big differences from one state or province to another.

As a main rule income, value added tax and heritance tax will be determined by the central government while property tax and sales taxes are local taxes.

5.12 The volume of tax expenditure

Tax expenditure is described in chapter two in this report. For most countries it is difficult to measure the tax expenditure both generally and for agriculture and forestry.

Each year the Department of Treasury in *Australia* publishes information of the volume of tax expenditures. Tax expenditures are defined as tax concessions designed to provide a benefit to a specified activity or class of taxpayers. The value of the tax expenditures has increased over the last years. The total tax expenditures to farmers are small weighed up with several other groups of taxpayers.

The budgetary effect of tax measures (incl. social security) target in agriculture in *Germany* is around EURO 7,400 per man-year or around EURO 270 per hectare. Almost 85 per cent of these tax measures is related to the special social security for the agricultural sector. The budgetary effect of tax measures exclusive social security shows a downward trend from 2000 to 2001, while it is just the opposite if one includes social security. This indicates that Germany is engaged in reducing special tax measures for its agriculture, while social security contributions are rapidly growing due to the age distribution of the German farmers.

It has long been known that the federal state of Germany provides its farmers with generous support through the tax system including social security. The main source of support comes from a special valuation of agricultural income and property together with a special social security system for the German farm sector.

In *UK* the taxation of farmers is mostly like the taxation of other self-employed persons There are special relives in the inheritance tax for farms but it is about corresponding relieves for other business properties.

In *Ireland* only about 40,000 farmers of 101,000 farmers in total were actually liable to pay tax on farming profits for 2001. These 40,100 farmers are expected to pay EURO 97 million in tax and EURO 33 million in social security contributions.

It is difficult to quantify the value of the special tax measures directed to *French* farmers. It appears that there are only few measures that are solely applied to agriculture. It has been suggested that income from agriculture calculated by the simplified income calculation scheme may be 50 % lower than the income would be if the farmers had been keeping accounts.

There are only a few tax related measures to *Swiss* agriculture. It is, however, difficult to quantify their financial impact.

The two most important causes of the low tax burden in the agricultural sector in *Italy* are the lower rate of social security contributions and the taxation on the basis of the cadastral register.

5.13 Conclusion

In all the investigated countries there are some tax expenditures connected to farmers. The volume and the shaping of the tax expenditures is different from country to country, however we can list the most usual way the farmers get tax expenditure:

- Special system for valuation and foundation for income tax (cadastral system, "unit valuation", Germany, France, Italy)
- The average method to calculate the taxable income
- Special system for social security contribution (Germany, France and Italy)
- Special valuation for property tax (use value instead of market value)
- Property tax exception
- Special schemes for petrol tax
- Inheritance tax reduction
- Special regulations connected to establishing a business or changing the ownership of an enterprise
- Special VAT scheme for i.a. farmers (flat rate scheme) in the EU countries
- Some of these tax expenditures are also available to other industries.

We have found only few examples of directly allowances in the income from agriculture.

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Appendix

Appendix 1: List of notifications on tax to the Committee on Agriculture of the WTO

Entry words: tax, taxes, levy, fee
Document symbol: G/AG/N/
Total reporting period: January 1995–March 2002

	Reported to the WTO: date/year	Reported period	Country
Document			
G/AG/N/AUS/41	21 March 2002	2000/2001	Australia
G/AG/N/AUS/30	9 March 2000	1998/99	Australia
G/AG/N/AUS/20	5 November 1998	1997/98	Australia
G/AG/N/AUS/14	31 October 1997	1996/97	Australia
G/AG/N/AUS/7/Rev.1	12 November 1996	1995/96	Australia
G/AG/N/AUS/36	20 June 2001	1999/2000	Australia
G/AG/N/ARG/16	8 October 2001		Argentina
G/AG/N/CAN/37/Rev.1	14 June 2001	1997	Canada
G/AG/N/CAN/43	14 June 2001	1998	Canada
G/AG/N/CAN/35	21 March 2000	1996	Canada
G/AG/N/CAN/17	6 November 1997	1995	Canada
G/AG/N/CRI/13	26 February 2001	1999	Costa Rica
G/AG/N/CRI/10	20 July 2000	1998	Costa Rica
G/AG/N/CRI/4/Add.1	26 February 2001	1997	Costa Rica
G/AG/N/CRI/4	10 March 1998	1995, 1996	Costa Rica
G/AG/N/EST/3	20 November 2001	2000	Estonia
G/AG/N/ISL/14	23 July 1999	1998	Iceland
G/AG/N/NOR/30	7 March 2001	1999	Norway
G/AG/N/NOR/25	8 March 2000	1998	Norway
G/AG/N/NOR/22	29 April 1999	1997	Norway
G/AG/N/NOR/11	19 September 1997	1996	Norway
G/AG/N/NOR/5	30 September 1996	1995	Norway
G/AG/N/NOR/36	27 February 2002	2000	Norway
G/AG/N/PER/3	25 November 1999	1995, 1996, 1997	Peru
G/AG/N/SVN/18	14 September 2001	2000	Slovenia
G/AG/N/CHE/22	29 June 1999	1998	Switzerland/Liechtenstein
G/AG/N/CHE/15	25 June 1998	1997	Switzerland/Liechtenstein
G/AG/N/CHE/11	24 July 1997	1996	Switzerland/Liechtenstein
G/AG/N/CHE/6	1 August 1996	1995	Switzerland/Liechtenstein
G/AG/N/USA/36	26 June 2001	1998	United States
G/AG/N/USA/27	28 June 1999	1996, 1997	United States
G/AG/N/USA/17	15 June 1998	1995, 1996	United States
G/AG/N/VEN/19	14 March 2001	1998	Venezuela
G/AG/N/VEN/16	9 March 2000	1997	Venezuela
G/AG/N/VEN/8	15 October 1997	1996	Venezuela
G/AG/N/VEN/4/Rev.1	25 September 1997	1995	Venezuela
G/AG/N/TUR/4	12 May 1997	1996	Turkey

Appendix 2: Notifications on tax to the Committee on Agriculture of the WTO: Selected countries

Countries represented: Australia, Canada, United States and Switzerland
Entry words: Tax, taxes, levy, fee
Document symbol: G/AG/N/
Total reporting period: January 1995–March 2002

	Measure Type	Name and description of measure	Monetary value of measure in year in question	Data Sources	Reported to the WTO: date/year	Report. period	Country
Document							
G/AG/N/ AUS/41	Domestic support. Measures exempt from the reduction commitment—"Green Box". "Income Insurance and Income Safety-net Programs": Farm Management Deposits Scheme.	A tax linked savings tool, which allows primary producers to set aside income in high-income years without paying tax until income is withdrawn, so that a lower marginal tax rate may be paid. The programme is commercially delivered by approved deposit taking institutions—market based interest rates apply.	$A mill. 20.00	AFFA	21 March 2002	2000/ 2001	Australia
	Domestic support. Product-Specific Aggregate Measurements of Support: Other Product-Specific Support and Total Product-Specific AMS	Dairy Structural Adjustment Program Support is provided to producers to assist adjustment to deregulation of the industry. The payments are funded by an 11 cents per litre levy on retail sales of milk.	$A million 200.67	Dairy Adjustment Authority	21 March 2002	2000/ 2001	Australia

G/AG/N/ AUS/30	Domestic support. Product-Specific Aggregate Measurements of Support: Other Product-Specific Support and Total Product-Specific AMS	MILK. Support delivered through increases in the price of manufactured dairy products to domestic consumers by the levy paid on milk used in the manufacture of dairy products. *(The increase in the price of manufactured dairy products (consumer transfer) is calculated on a per litre of manufacturing milk produced and multiplied by total milk production less the market milk levy which is paid by producers.)*	Other product specific support (include calculation details) $A million 155.61 Associated fees/levies $A million 35.9 Total other product-specific support $A million 119.71 **Total AMS** ***$A million 119.71***	Milk production —ABARE Levy administrati on data—Australian Dairy Corporation	9 March 2000	1998/99	Australia
G/AG/N/ AUS/20	Domestic support. Product-Specific Aggregate Measurements of Support: Other Product-Specific Support and Total Product-Specific AMS	MILK. Support delivered through increases in the price of manufactured dairy products to domestic consumers by the levy paid on milk used in the manufacture of dairy products.	Other product specific support (include calculation details) $A million 167.62 Associated fees/levies $A million 36.0 Total other product-specific support $A million 131.62 **Total AMS** ***$A million 131.62***	Milk production —ABARE Levy administrati on data—Australian Dairy Corporation	5 November 1998	1997/98	Australia

G/AG/N/ AUS/14	Domestic support. Product-Specific Aggregate Measurements of Support: Other Product-Specific Support and Total Product-Specific AMS	MILK. Support delivered through increases in the price of manufactured dairy products to domestic consumers by the levy paid on milk used in the manufacture of dairy products.	Other product specific support (include calculation details) $A million 180.29 Associated fees/levies $A million 36.1 Total other product-specific support $A million 144.19 **Total AMS** ***$A million* 144.19**	Milk production —ABARE Levy administrati on data— Australian Dairy Corporation	31 October 1997	1996/97	Australia
G/AG/N/ AUS/7/Rev. 1	Domestic support. Product-Specific Aggregate Measurements of Support: Other Product-Specific Support and Total Product-Specific AMS	MILK. Support delivered through increases in the price of manufactured dairy products to domestic consumers by the levy paid on milk used in the manufacture of dairy products.	Other product specific support (include calculation details) $A million 187.532 Associated fees/levies $A million 35.815 Total other product-specific support $A million 151.717 ***Total AMS*** ***$A mill 151.717***	Milk production —ABARE Levy administrati on data— Australian Dairy Corporation	12 November 1996	1995/96	Australia
G/AG/N/ AUS/36	"Income Insurance and Income Safety-net Programs": Farm Management Deposits Scheme	A tax linked savings tool, which allows primary producers to set aside income in high-income years without paying tax until income is withdrawn, so that a lower marginal tax rate may be paid. The programme is commercially delivered by approved deposit taking institutions—market based interest rates apply.	$A 20.00 mill.	AFFA	20 June 2001	1999/ 2000	Australia

G/AG/N/USA/36	Domestic support. Product- Specific aggregate measurements of support: other product-specific support and total product-specific support	Fees/levies *(Fees/levies now include loan origination and related fees for most loan commodities, in addition to marketing assessments for sugar, peanuts, and tobacco. Although applicable every year, this is the first year the loan related fees have been evaluated.)*	Million $ 112.268		26 June 2001	1998	United States
	Domestic support. Measures exempt from the reduction commitment—"Green Box"	State programs for agriculture (FY outlays, net of fees and taxes). State governments provide a number of generally available services. Includes extension, marketing, and research. Excludes state credit programs. Amount reported is net of producer fees and taxes paid for various services.	Million $ 3,334		26 June 2001	1998	United States
G/AG/N/USA/27	Domestic support: Product-specific aggregate measurements of support: other product-specific support and total product-specific support	Fees/levies	Million $ 84.335		28 June 1999	1997	United States
	Domestic support. Measures exempt from the reduction commitment—"Green Box"	State programs for agriculture (FY outlays, net of fees and taxes). State governments provide a number of generally available services. Includes extension, marketing, and research. Excludes state credit programmes. Amount reported is net of producer fees and taxes paid for various services.	Million $ 3,067		28 June 1999	1997	United States
	Domestic support. Measures exempt from the reduction commitment—"Green Box"	State programs for agriculture (FY outlays, net of fees and taxes). State governments provide a number of generally available services. Includes extension, marketing, and research. Excludes state credit programmes. Amount reported is net of producer fees and taxes paid for various services.	Million $ 2,948		28 June 1999	1996	United States

G/AG/N/ USA/17	Domestic support. Measures exempt from the reduction commitment—"Green Box"	State programs for agriculture (FY outlays, net of fees and taxes). State governments provide a number of generally available services. Includes extension, marketing, and research. Excludes state credit programmes. Amount reported is net of producer fees and taxes paid for various services.	Million $ 2, 785		15 June 1998	1995	United States
	Domestic support: Product-specific aggregate measurements of support: other product-specific support and total product-specific support	Fees/levies	Million $ 66.607		15 June 1998	1996	United States
G/AG/N/ CAN/37/R ev.1	Non-Product-Specific AMS: Provincial Programs	Fuel tax concessions to the agriculture sector are part of this support.	Canadian $ 155.3 mill.	Provincial Ministries of Agriculture (FY).	14 June 2001	1997	Canada
G/AG/N/ CAN/43	Non-Product-Specific AMS: Provincial Programs	Fuel tax concessions to the agriculture sector are part of this support.	Canadian $ 146.9 mill	Provincial Ministries of Agriculture (FY).	14 June 2001	1998	Canada
G/AG/N/ CAN/35	Non-Product-Specific AMS: Provincial Programs	Fuel tax concessions to the agriculture sector are part of this support.	Canadian $ 142.00 mill	Provincial Ministries of Agriculture (FY).	21 March 2000	1996	Canada
G/AG/N/ CAN/17	Non-product-specific AMS. Provincial programs	Fuel tax concessions to the agriculture sector are part of this support.	Canadian $140.3	Provincial Ministries of Agriculture (FY).	6 November 1997	1995	Canada
G/AG/N/ CHE/22	Domestic support. Product-specific aggregate measurements of support: Other product-specific support and total product-specific AMS	Individual tax on surplus production. Milk and dairy products	5.4 Swiss F million *(subtracted from total product-specific AMS)*	OFAG: Federal Office for Agriculture, Bern	29 June 1999	1998	Switzerland–Liechtenstein
G/AG/N/ CHE/15	Domestic support. Product-specific aggregate measurements of support: Other product-specific support and total product-specific AMS	Individual tax on surplus production. Milk and dairy products.	3.2 Swiss F million *(subtracted from total product-specific AMS)*	OFAG: Federal Office for Agriculture, Bern	25 June 1998	1997	Switzerland–Liechtenstein

G/AG/N/ CHE/11	Domestic support. Product-specific aggregate measurements of support: Other product-specific support and total product-specific AMS	Individual tax on surplus production. Milk and dairy products	4.4 Swiss F million *(subtracted from total product-specific AMS)*	OFAG: Federal Office for Agriculture, Bern	24 July 1997	1996	Switzerland–Liechtenstein
G/AG/N/ CHE/6	Domestic support. Product-specific aggregate measurements of support: Other product-specific support and total product-specific AMS	Individual tax on surplus production. Milk and dairy products	3.1 Swiss F million *(subtracted from total product-specific AMS)*	OFAG: Federal Office for Agriculture, Bern	1 August 1996	1995	Switzerland–Liechtenstein