Date Introduced: 2 May 1984
House: House of Representatives
Presented by: Hon. Chris Hurford, M.P., Acting Treasurer

Short Digest of Bill

Purpose

To change the basis of the incentive to primary producers to set aside income in high income years for use in lower income years from an income tax deferral to a concessionary interest rate applying on deposits.

Background

The Income Equalization Deposits (IED) scheme was introduced by the Loan (Income Equalization Deposits) Act 1976, replacing the Drought Bonds Scheme. Both schemes provided a form of drought assistance.

Tax measures were inserted into the Income Tax Assessment Act 1936 (ITAA) (sections 159GA-159GD) to complement the IED scheme. As a consequence, a primary producer could use the scheme as a form of "forward tax averaging" and so even out the effects of fluctuating income on his tax liabilities over a number of years. The provisions allow a primary producer to claim a deduction for moneys deposited with the Commissioner of Taxation and to include in assessable income the proceeds received on withdrawal of deposits. Thus a primary producer may defer income from a "good" year in which his marginal rate of tax is high, to a "poor" year in which his marginal rate of tax is lower. For example (note the new IED scheme applies from 1 September 1983) -

Suppose a primary producer lodges an income equalization deposit of $5000 on 10 August 1982, the deposit being deductible against income of the 1981/82 income year. In February, he redeems the full amount of the deposit as a result of serious financial difficulties. Also, say, his taxable income derived solely from primary production was $25,000 in 1981/82 and $11,500 in 1982/83.
### 1981/82

<table>
<thead>
<tr>
<th>Description</th>
<th>1981/82</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxable income before IED deduction</td>
<td>$25,000</td>
</tr>
<tr>
<td>Less IED deduction</td>
<td>$5,000</td>
</tr>
<tr>
<td>Taxable Income</td>
<td>$20,000</td>
</tr>
<tr>
<td>Tax saved</td>
<td>$2,300.00</td>
</tr>
</tbody>
</table>

### 1982/83

<table>
<thead>
<tr>
<th>Description</th>
<th>1982/83</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxable income</td>
<td>$11,500</td>
</tr>
<tr>
<td>Add deduction (IED redeemed)</td>
<td>$5,000</td>
</tr>
<tr>
<td>Taxable Income</td>
<td>$16,500</td>
</tr>
<tr>
<td>Increase in tax</td>
<td>$1,533.50</td>
</tr>
<tr>
<td>Net tax saved ($2,300 - $1,533.50)</td>
<td>$766.50</td>
</tr>
</tbody>
</table>

**Notes:**

1. If the deposit had been lodged for more than 12 months it could have been redeemed irrespective of hardship, etc.

2. The deposit would also earn *assessable* interest at the rate of 9.5 per cent.

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On 19 May 1983, the Treasurer announced, in his Ministerial Statement, the Government's decision to introduce a new income equalization deposit scheme which would "provide an incentive for farmers to set aside in good years money for use in poor years."[1] The new arrangements would apply to deposits made on or after 1 September 1983. Such deposits would no longer qualify for a tax deduction when made, nor would they be included in assessable income when redeemed. Instead, a tax credit would be allowed on eligible deposits at the standard rate of tax while a surtax...
at the standard rate would apply on withdrawals. Under such arrangements a uniform tax saving to all depositors regardless of income levels would apply.

The interest rate would be varied so as to provide an effective interest rate on the investment component of the deposit (i.e., 70 per cent of the gross amount deposited) at a margin of 2 percentage points over the two year bond rate.

Transitional arrangements would be available to depositors to transfer deposits into the new scheme. Deposits remaining in the old scheme after 1 September 1983 would attract an interest rate of 7.5 per cent, reducing at yearly intervals by 2 percentage points.

"The (new) measure is expected to cost less than $1 million in 1983-84; the budgetary effect in later years will depend on the response to the new scheme".[2]

On 16 June 1983,[3] the Treasurer announced that the Government had decided to dispense with the tax credit and surtax so that deposits lodged with the Commissioner of Taxation on or after 1 September, 1983 would have no tax consequences. Thus, under the new scheme, the incentive to set aside money in high income years would take the form of a uniform loading in the rate of interest paid on deposits. An interest rate at a margin of 2 per cent above the 2 year bond rate would be paid on the entire face value of the deposit that remained invested. Transitional arrangements remained unaltered.

A Statement of Terms and Conditions under which deposits may be lodged after 1 September 1983 was issued in conjunction with the Treasurer's press release dated 30 August 1983.

Outline

The eligibility criteria and provisions relating to withdrawal and making of deposits have generally remained the same under both old and new schemes. However, under the proposed new arrangements, primary producers must provide a self-assessment of their expected income from primary production and their expected taxable income (excluding income from property) to determine their eligibility to earn the concessionary rate of interest on deposits. Alternatively, "a depositor investing in the two months following an income year may elect to have his or her eligibility assessed on the basis of the income year just ended".[4] On this basis of determination a depositor must confirm his eligibility to the concessionary rate upon
receiving an income tax assessment for the year. Gross over-estimates of income may be subject to a penalty of $2000 or imprisonment for 12 months or both.

Deposits under the new scheme will be classified as Class A, Class B or Class C, each attracting a different interest component. Class A deposits include those deposits, subject to specified limits, made in the new scheme by an eligible primary producer on or after 1 September 1983 and converted deposits from the old scheme. Such deposits will attract an interest rate of 2 percentage points above the short term bond rate in relation to the quarter.

Class B deposits include non-primary producer deposits and primary producer deposits which fall outside the Class A interest deposit limit. An interest rate of 3 percentage points below the short term bond rate will be payable on this category.

Those deposits made before 1 September, 1983 and not converted into Class A or Class B deposits are to be classified as Class C deposits. The interest rate payable on Class C deposits will be 7.5 per cent until 1 September, 1984 decreasing 2 percentage points on 1 September each year until it reaches zero on 1 September 1987.

The following table compares the old scheme with that of the new scheme.

<table>
<thead>
<tr>
<th>Income Equalization Deposits Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>OLD SCHEME</strong></td>
</tr>
<tr>
<td>(expired 31 August 1983)</td>
</tr>
<tr>
<td><strong>NEW SCHEME</strong></td>
</tr>
<tr>
<td>(effective 1 September 1983)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ELIGIBILITY</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Taxpayers. However, main benefits accrue to a taxpayer carrying on business of primary production (includes fishing and forestry operations).</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>DEPOSITS</th>
</tr>
</thead>
<tbody>
<tr>
<td>who may lodge:</td>
</tr>
<tr>
<td>An individual, company, and partner in a partnership, (sec. 159GC ITAA). Trustees are entitled to lodge deposits in limited cases (sec. 159GB ITAA).</td>
</tr>
</tbody>
</table>
Deposit must be made during the 12 months period ending 2 months after the end of that income year.

no upper limit

not to result in a loss

The deposit must be greater than $100 and in multiples of $100. The deposit must be accompanied with the prescribed application form and lodged with the Commissioner of Taxation.

Deposit deductible (for primary producers only) from assessable income. A deduction is not allowable for deposits repayable during 12 month period (sub-sec. 159GC(3) ITAA).

Naturally, no amount would be included in assessable income.

Deduction cannot exceed -

(i) amount of deposit;

(ii)(a) 60 per cent of taxpayers' gross receipts from primary production or

(b) the amount that, during that year, would be the primary producer's taxable income other than income from property whichever is the lesser and

Class A deposits (new deposits and primary producer converted deposits, subject to specified limits).

Class B deposits (non-primary producer deposits or primary producer deposits not included in Class A above).

Class A deposit cannot exceed -

(i) (a) 60 per cent of taxpayers' gross receipts from primary production or

(b) the amount that, during that year, would be the primary producers' taxable income other than income from property whichever is the lesser and
(iii) $250,000 at any one time.

(ii) $250,000 at any one time.

WITHDRAWALS

Repayable in amounts of $100 and multiples of $100.

Applications must be made on repayment application forms and lodged with Commissioner of Taxation.

Proceeds included in assessable income in year in which application to withdraw is made but only to the extent of deductions allowed.

Deposits repayable upon request after 12 months from the date of lodgment; for shorter periods deposits repayable -

(i) where depositor experiences serious financial difficulties;

(ii) where the depositor has died or become bankrupt, or in the case of a company, that company has been, or is being, wound up;

(iii) to the extent to which it was not deductible.

Interest paid to actual date of repayment.
INTEREST RATE

Established by Regulations under Loan (Income Equalization Deposits) Act 1976

23 October 1981 - 31 August 1983

9.5 per cent

1 September 1983 - 31 December 1983

Class C 7.5 per cent

Class A 16.792 per cent
Class B 11.792 per cent

1 January 1984 - 31 March 1984

Class C 7.5 per cent

Class A 13.394 per cent
Class B 8.394 per cent

1 April 1984 - 30 June 1984

Class C 7.5 per cent

Class A 15.39 per cent
Class B 10.39 per cent

This rate will reduce to 5.5 per cent on 1 September 1984 and be further reduced by 2.0 percentage points each subsequent 1 September until it reaches zero on 1 September 1987.

Variations will apply to all deposits at the time the variations occur as well as new deposits made after that time.

Interest from IEDs will be subject to income tax.

Right of Objection

Deposits redeemed on grounds of financial difficulties.

Where depositor was dissatisfied with Commissioner of Taxation's decision to refuse to pay, the decision was referred to the Taxation Board of Review

Where depositor is dissatisfied with the Secretary of Department's decision to refuse to pay, that decision may be referred to Administrative Appeals Tribunal
Provisional Tax

No automatic adjustment to be made to primary producers income tax assessment.

Penalties

If applicants overstate their eligibility to earn concessionary rate of interest,
or fail to notify cessation of primary production business -

Then, $2000 fine or imprisonment for 12 months or both.

TRANSITIONAL ARRANGEMENTS

Existing IEDs and drought bonds may be invested in new scheme even though the amount was deposited in old scheme for less than 12 months (Class A or B). However, the conversion will form part of assessable income of the year in which the transfer was sought.

The time the amount was on deposit under the former scheme will count towards the 12 month minimum period necessary before a deposit can be withdrawn under the replacement scheme.

Main Provisions

Clause 2 provides definitions for a number of words and expressions used in the Bill.
A primary producer deposit is defined as a deposit made by an eligible primary producer on or after 1 September 1983 or that part of a primary producer's Class C deposits or Drought Bonds which are converted and in respect of which an unrecouped income tax deduction exists. Partial conversions are pro-rated by the proportion of the total deposits in respect of which an unrecouped income tax deduction exists.

An eligible primary producer includes a natural person, company, partner in a partnership, and a beneficiary of a trust estate, the trustee of which carries on in Australia a business of primary production.

'Short term bond rate' refers to the weighted average yield of successful bids for the shortest Treasury Bond series (with maturity of less than 5 years) offered at tender in any calendar quarter.

Clause 4 inserts a number of new sections into the Principal Act to deal with the proposed deposit arrangements. Proposed section 4A specifies the interest rates to apply to the different categories of deposits. The concessional Class A interest rate will apply to primary producer -

(i) deposits less than the Class A interest deposit limit;

(ii) converted deposits less than the $250,000 maximum limit;

(iii) deposits in (i) and (ii) above where primary producer business does not cease for more than 120 days.

The Class B rate will apply to -

(i) non-primary producer deposits; and

(ii) new deposits which fall outside the Class A interest deposit limit.

The Class C rate applies to deposits made before 1 September, 1983 and which are not converted.

Proposed section 4B outlines the Class A interest deposit limit which determines the amount of new deposits in any income year which a depositor can make in order to attract the Class A interest rate. The Class A interest deposit limit in respect of a depositor for an income year, is the lesser of:
(i) taxable income, other than taxable income from property, or

(ii) 60 per cent of gross receipts from primary production of the income year.

Proposed section 4C requires depositors, in their application to the Secretary of the Department of Primary Industry, to estimate the amount of income which the initial interest payments are based and to which the depositor may refer when deciding upon the level of his new deposits. Some basis of assessment is necessary until the Commissioner of taxation's determination of relevant income amounts are made (proposed section 4D) so that the appropriate interest payment in respect of recent deposits can be made.

The Commissioner of Taxation is required under proposed section 4D to determine on request from the Secretary of the Department, the relevant income amounts in respect of depositors. The Department is required to communicate such determinations to depositors.

Clause 7 replaces section 12 of the Principal Act and allows for the conversion of Drought Bonds and deposits under the old IED scheme into Class A or B deposits. Where an application for conversion of Class C deposits is made within 60 days of commencement of the amending legislation the conversion will be deemed to have taken place on 1 September, 1983. Whereas applications made after 60 days from commencement, or for conversions of stock, will be Class A or B deposits from the date of receipt of the application. Appropriate interest will be payable.

Any part of a Class C deposit or stock that has been converted into a non-Class C deposit will be deemed to have become repayable (clauses 10 and 11).

Clause 12 provides that the excess of new or converted Class A deposits above $250,000 in any income year is repayable on request. Deposits which, when deposited, were eligible only for the Class B rate may not be withdrawn under this clause.

In addition where a depositor ceases to be a primary producer, all deposits become repayable on the date of receipt of a withdrawal application irrespective of whether the deposits have been held for 12 months.

Clauses 14 and 15 allow a depositor to refer an Authorized Person's decision to refuse to repay a deposit on grounds of financial difficulties to the Administrative Appeals Tribunal.
Non-notification by the depositor or trustee of the cessation of primary production business will cause the depositor or trustee to be liable to a fine of $2,000 or imprisonment for 12 months or both. A similar penalty will be enforced (clause 17) in circumstances where the depositor provides a false estimate of his income i.e. the depositor does not believe or has no reasonable grounds for believing it to be correct or to be a fair estimate.

Clause 18 amends the Loan (Drought Bonds) Act 1969 to prevent payment of interest in respect of a converted Drought Bond while interest is being earned on the IED which resulted from the Drought Bond conversion.

Remarks

Drought Assistance

The tax-related IED scheme has provided drought affected farmers with an appropriate means of alleviating the problems experienced following drought. Two further drought assistance measures in the form of a subsidy to aid farmers to service their debt and to retain valuable breeding stock was introduced in the Drought Assistance (Primary Producers) Act 1982. However, primary producers who participated in the IED scheme were ineligible for the subsidy. The drought relief fodder subsidy scheme ceased operations from 30 June 1983.

Currently adjustment assistance measures of a general nature are provided through the Rural Adjustment Scheme, unemployment benefits and taxation relief. The taxation relief takes the form of accelerated taxation allowances for expenditure on fodder and water storage facilities.

Equity

Previously, the IED scheme acted as a tax equity measure by allowing farmers to transfer pre-tax income form high income years to low-income years in order to avoid the inequitable effects of a progressive tax rate on unstable incomes. The scheme has now reverted to being purely an instrument to facilitate stabilisation of post-tax income.

According to the Second Reading Speech to the Bill removal from the taxation system should permit the benefits accruing from the scheme to be more evenly available to all primary producers. Only primary producers on the highest marginal tax rate benefitted the most under the old arrangements.
Tax Avoidance

The scheme has been removed from the taxation system to prevent the possibility of it being used for tax avoidance.

Interest Rate

The rationale underlying the introduction of an income equalization deposit scheme is to provide primary producers with the incentive to set aside money in high income years for use in poor years. Under the new scheme, the incentive takes the form of a uniform loading (2 per cent above the short-term bond rate) in the rate of interest paid on deposits.

However, high rates of return offered from such investment opportunities as property trusts, may capture more of the surplus funds of primary producers than was envisaged.

IED Balance

Funds held on deposit in the Scheme as at 7 May 1984 are represented as follows -

<table>
<thead>
<tr>
<th></th>
<th>Old Scheme</th>
<th>New Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>Class A</td>
<td>$3,455,740</td>
<td>Class A</td>
</tr>
<tr>
<td>Class B</td>
<td>$558,160</td>
<td>Class B</td>
</tr>
<tr>
<td></td>
<td>$129,606,850</td>
<td>$4,013,900</td>
</tr>
<tr>
<td></td>
<td>$133,620,750</td>
<td></td>
</tr>
</tbody>
</table>

On the balance date there were 238 separate deposits in Class A and 36 separate deposits in Class B. Since 1 September 1983, 5 deposits with a total value of $49,000 have been withdrawn from the Class A category; no withdrawals from the Class B category.

For further information, if required, contact:

16 May 1984
Economics and Commerce Group
LEGISLATIVE RESEARCH SERVICE
References


2. Ibid, page 32.

