National
Farmers
Federation

12 April 2023

Director
Tax and Transfers Branch
Retirement, Advice, and Investment Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: superannuation@treasury.gov.au

RE: NFF submission to the better targeted superannuation concessions consultation

The National Farmers' Federation (NFF) welcomes the opportunity to provide a submission to Treasury's consultation on the proposed changes to superannuation taxation.

The NFF was established in 1979 as the national peak body representing farmers and more broadly, agriculture across Australia. The NFF's membership comprises all of Australia's major agricultural commodities across the breadth and the length of the supply chain. The NFF represents Australian agriculture on national and foreign policy issues including taxation, economic policy, workplace relations, trade and natural resource management.

<u>Current arrangements in Australian agriculture</u>

Self-managed superannuation funds (SMSFs) are a common tool in Australian agriculture to manage assets and use agricultural land to provide retirement income. While exact figures are unavailable, anecdotal evidence suggests that this could exceed 30 per cent of Australian farm businesses.

The use of SMSFs to hold agricultural land stems from the nature of farmers long-term superannuation contributions. Unlike salaried employees, farmers do not make regular superannuation contributions throughout their working life. Instead, their land asset is effectively their superannuation.

As part of the succession planning process, land assets are commonly transferred into a SMSF. The next generation then takes on the running of the business and makes a lease payment to the retiring farmer. This lease payment becomes their retirement income.

While this process provides stability in retirement income it creates a situation where many farmers will be materially worse off as a result of the proposed increased taxation. There is a distinction between the value of an agricultural land asset and its return. On average, the return on agricultural land assets is relatively modest around 2 per cent. Put simply, this makes a typical farmer 'asset rich' but 'cash poor'.

Impact of proposed changes to superannuation taxation

The government's proposal will introduce an additional tax of 15 per cent on balances exceeding $3 million. This additional tax will apply to 'unrealised capital gains' within a fund, meaning the additional tax burden will be levied annually on any increase in land values above this threshold.

This taxation of unrealised gains will mean some farmers will struggle to meet the annual tax bill on their land assets without selling the land itself. Given high land values and modest cash income, this new tax could represent a significant share of a farmers' annual retirement income, or even exceed it.

Given the highly cyclical nature of Australian agriculture, the impact of the proposed changes will have an outsized impact on farmers who have agricultural assets within their SMSF. The value of Australian agricultural land can experience rapid increases based on seasonal conditions. For example, in 2021 the median price per hectare of Australian farmland increased by 20 per cent.[1] This was most pronounced in Queensland, Victoria and Western Australia where median price per hectare grew at more than 30 per cent.[2]

However, the growth in lease value for agricultural assets does not grow at the same rate. This exposes farmers to a significant potential tax liability despite no substantial change in their overall wealth position. Given the proposal to not index the superannuation concessional cap, overtime an increased number of farming assets will be captured by the increased tax rate.

Attachment A outlines four key examples of the increased burden on farmers with modest superannuation balances. These examples demonstrate the significant impact the proposed additional tax will have.

Calculation of Total Superannuation Balance

The NFF appreciates Treasury's desire for a simplified method to calculate the total superannuation balance. While a simplified method will reduce compliance costs, it will increase the tax liability on farmers who have witnessed an increase in land values but have not realised that gain through sale of the land.

To this end, the NFF strongly recommends the exclusion of agricultural land assets from the calculation of total superannuation balance. Exclusion of these assets would allow farmers to continue to use lease payments from agricultural land assets as a clear and consistent form of retirement income without undue tax burden or other market distortions.

The NFF recommends Treasury consider a clear definition of an agricultural land asset through existing definitions of the primary production assets as provided by the Australian Tax Office (ATO). This could include a clear definition founded on land used by or leased to primary production businesses[3] or land eligible for primary production land care operations[4]. This would provide clarity and simplicity in the determination agricultural land assets and compliance and reporting activities.

[1] Rural Bank, Australian Farmland Values 2022
[2] Rural Bank, Australian Farmland Values 2022
[3] TR 97/11 - Income tax: am I carrying on a business of primary production?
[4] https://www.ato.gov.au/Business/Primary-producers/In-detail/Capital-expenditure/Landcare-operations/

Additionally, the NFF recommends the exclusion of unrealised capital gains on the calculation of total superannuation balance. As it currently stands, capital gains on land assets are calculated when assets within the fund are sold. On the sale of an asset, the following tax rules apply:

- For a fund in 'accumulation phase' – gains are taxed at the current concessional rate of 15%, reducing by 1/3 to 10% if the asset has been owned for more than 12 months.
- For a fund in 'pension phase' – capital gains are received tax free.

Under Treasury's current proposal, farmers will pay tax on these unrealised gains through the application of the additional tax on earnings on funds over $3 million. The NFF recommends Treasury not tax unrealised gains and instead remain committed to the principle that tax is payable on assets only on disposal.

If the taxation of unrealised capital gains is included under the proposed model, the NFF strongly recommends the introduction of back-carry provisions for loses incurred in superannuation accounts. This would allow farmers who have had a decrease in earnings to receive a refund for tax paid in previous years.

The NFF also recommends Treasury consider stamp duty and Capital Gains tax roll over relief for farmers as part of any transition process associated with the implementation of the Australian Government's additional taxation arrangements. This will facilitate farmers to adjust to the new taxation conditions in a way that supports effective decision making and does not disadvantage farmers who have invested in good faith within the existing rules.

<u>Indexation of cap on concessional taxation</u>

The NFF is concerned about the proposal not to index the cap on concessional taxation arrangements for superannuation balances. Given the long-term nature of superannuation and rising inflation, the $3 million value will increasingly capture a greater share of Australian farming assets. As such, the NFF recommends indexing the cap to inflation or the Consumer Price Index.

<u>Unintended consequences of the proposed reform</u>

There are a number of unintended consequences from this proposed reform that the NFF believes Treasury and the Australian Government has not considered. Each of these unintended consequences and their negative impact on Australian farmers must be considered as part of the proposed reform.

Reduced investment in agricultural land

The NFF is concerned about the impact of the proposed changes on agricultural land. Removing a well-established approach holding agricultural land risks reducing the appetite and long-term investment in agricultural land in Australia. Australian agriculture already faces a significant capital gap, with an additional $7.5 billion in net capital investment needed each year if agriculture is to reach industry's goal of $100 billion in farm-gate output by 2030.[5]

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[5] AgriFutures Australia 2021, Capital requirements of Australia's agriculture, fisheries and forestry sector, AgriFutures Australia Publication No. 20-140

At the same time, the proposed changes will disadvantage family farmers with agricultural land assets in SMSFs competing with corporate investors. The Australian Government's past changes to superannuation to allow SMSF investment in real estate and land assets opened up additional capital into agriculture. However, this proposal not only reverses existing support for agriculture but puts family farms at a significant disadvantage. This is because corporate investors will have preferable taxation of land capital gains than individual farmers with SMSFs in accumulation phase.

Barriers to entry into agriculture

The proposed changes will reduce the options available to agricultural businesses to conduct succession planning between generations. The NFF is concerned that this will increase barriers to entry into agriculture for new small and medium sized firms. As previously discussed, under current arrangements younger farmers are able to take over the operational elements of an agricultural business with ongoing lease payments to the older generations through their SMSF. This reduces the immediate and upfront capital requirements of new entrants to agriculture. This is because they do not need to immediately purchase land assets and instead can build up capital within the operational business overtime and progressively purchase the underlying land asset.

Without this pathway, new small and medium sized firms may be required to directly purchase the full underlying asset. This presents a significant barrier to entry where new firms may not be able to access loans and financing to purchase the large asset. The new business may also face a significant debt burden that reduces its viability.

Market distortions

The NFF is concerned that in its current form, the proposed changes to superannuation taxation will introduce market distortions through a direct disconnect between agricultural land sale and seasonal conditions. The proposed changes to concessional taxation may result in many SMSFs unable to service the new tax burden. This may see agricultural land assets sold in order to service the tax burden.

A significant influx of large agricultural land assets may distort the market and not allow an effective functioning of price signals. Agricultural land assets play a significant role in the overall capital and debt of a farm business. As such, market distortions through the unexpected sale of agricultural land assets may have a negative impact on the viability of many small and medium sized agricultural businesses across the country.

The NFF believes that these unintended consequences have not been properly considered by Treasury and the Australian Government. However, these unintended consequences can be avoided or reduced if the NFF's proposed recommendations are adopted into Treasury's proposed model.

<u>Consultation period</u>

Finally, the NFF is concerned about the short period of time Treasury has allowed for this consultation. Given the nature of the proposed reforms and the potential impact on Australians, Treasury and the Australian Government more broadly should have allowed more time to effectively engage with the detail of this issue. The NFF believes there is now a substantial risk that the full impact of these changes will not be considered due to the insufficient opportunity to consult with affected stakeholders.

Thank you again for the ability to contribute to this consultation process. The NFF looks forward to continuing its constructive relationship with Treasury and the Australian Government.

Yours sincerely

TONY MAHAR
Chief Executive Officer

Attachment A – Examples of the impact of proposed changes on farmers

EXAMPLE 1
Typical farmer with land assets in superannuation

Graham is a 68-year-old mixed farmer. His son has returned to the farm and they have negotiated a succession plan allowing Graham to retire and his son to take over the business. In 2018, they transferred land assets valued at $1.6 million into Graham's self-managed super fund. The SMSF receives an annual lease payment of $65,000 from his son, enabling him to fund his retirement.

As at 30 June 2025 that land has now increased in value to $4 million and the annual lease payments are $100,000. Only 50% of Graham's fund is in pension phase due to the liquidity of the fund. Graham is now 75.

Current Tax Outcomes (FY22)
Because Graham's SMSF is in pension phase, he does not pay any tax on income. Under current tax principles unrealised increases in land values are not taxed. He draws down 100% of the lease income he receives, which is not taxed as he is over 60.

Total FY22 tax liability = **$0**

Proposed Tax Outcomes (FY26)
Assume that the value of Graham's land assets increases by 12% over the course of FY26, from $4 million to $4.48 million. He also draws down 100% of the lease income he receives to satisfy his minimum pension requirement.

Tax liability SMSF = 15% x Earnings (100,000) x share in accumulation (50%)
Tax liability within SMSF = $7,500
Additional tax liability = 15% x Earnings ($480,000 + $100,000) x share over $3 million (33%)
Additional tax liability = $28,710
Total tax liability = **$36,210**

Asset transfer out of super
Assume Graham decides to transfer asset from his SMSF to reduce his balance below the $3 million threshold. Transfer occurs June 2025

Tax liability SMSF = 15% x Earnings ($100K) x share in accumulation (50%)
Plus capital gains on property sale ($4 mil - $1.6 mil x 10% x share in accumulation (50%)
Tax liability within SMSF = $7,500 + $120,000
Total tax liability with SMSF = $127,000

Graham's tax in future years based on $100K pa = $24,967

EXAMPLE 2
Typical farming couple with land assets in superannuation

Matthew (67) & Judy (64) are mixed farmers. Their son has returned to the farm and they have negotiated a succession plan allowing Matthew and Judy to retire and their son to take over the business. In 2018, Matthew transferred land assets valued at $1.6 million into their self-managed super fund and Judy makes cash contributions of $300,000. The SMSF receives an annual lease payment of $65,000 from their son, enabling them to fund their retirement.

As at 30 June 2025 that land has now increased in value to $4 million and the annual lease payments are $100,000.

Current Tax Outcomes (FY22)
Because Matthew and Judy's SMSF is in pension phase, they do not pay any tax on income within the SMSF. Under current tax principles unrealised increases in land values are not taxed. They draw down their minimum pension which includes 100% of the lease income received, which is not taxed as they are over 60.

Total FY22 tax liability = **$0**

Proposed Tax Outcomes (FY26)
Assume that the value of land assets increases by 12% over the course of FY26, from $4 million to $4.48 million.

Member balances:

	30 June 2025	Min pension 2025	30 June 2026
Matthew (75) (100% pension)	$4,000,000	$200,000	$4.480,000
Judy (72) (100% pension)	$500,000	$20,000	$550,000

They draw down their minimum pension which includes 100% of the lease income received, which is not taxed as they are over 60.

Tax liability SMSF = 0% x Earnings
Tax liability within SMSF = $0
Additional tax liability = 15% x Earnings ($480,000 + $200,000) x share over $3 million (33%)
Additional tax liability = $33,660
Total tax liability (inc. existing 15% concessional rate) = **$33,660**

Asset transfer out of super
Assume Matthew decides to transfer the land asset from the SMSF to reduce his balance below the $3 million threshold. Transfer occurs June 2025 and is transferred 50/50 to Matthew and Judy.

Tax liability SMSF = 0% x Earnings
Plus capital gains on property sale ($4 million - $1.6 million x 0%)
Tax liability within SMSF = $0

Matthew and Judy's tax in future years based on $50,000 each pa = $7,717

EXAMPLE 3
Typical farming couple with land assets in superannuation

William (67) & Jane (64) are mixed farmers. Their son has returned to the farm and they have negotiated a succession plan allowing William and Jane to retire and their son to take over the business. In 2018, William and Jane transferred land assets valued at $3 million into their self-managed super. The SMSF receives an annual lease payment of $130,000 from their son, enabling them to fund their retirement.

As at 30 June 2025 that land has now increased in value to $6.5 million.

Current Tax Outcomes (FY22)
Because William and Jane's SMSF is in pension phase, they do not pay any tax on income within the SMSF. Under current tax principles unrealised increases in land values are not taxed. They draw down their minimum pension which includes 100% of the lease income received, which is not taxed as they are over 60.

Total FY22 tax liability = **$0**

Proposed Tax Outcomes (FY26)
Assume that the value of land assets increases by 12% over the course of FY26, from $6.5 million to $7.2 million.

Member balances as at:

	30 June 2025	30 June 2026
William (75) (100% pension)	$3.25 million	$3.6 million
Jane (72) (50% pension)	$3.25 million	$3.6 million

They draw down their minimum pension which includes 100% of the lease income received, which is not taxed as they are over 60.

Additional tax liability = 15% x Earnings ($350,000*) x share over $3 million (7%)
Additional tax liability = $3,675 per member
Total additional tax liability = $7,350

*Ignores the impact of pension withdrawal this calculation

EXAMPLE 4
LRBA to purchase land assets in superannuation.

David (45) has a superannuation balance of $1.5 million. In August 2022 he enters into a Limited Recourse Borrowing arrangement (LRBA) to purchase land worth $3 million. The loan is interest only and with one of the Big 4 banks.

As at 30 June 2025 the value of the land has increased to $4 million. David now has a total superannuation balance (TSB) of $2.5 million (Land value - outstanding balance LRBA). In May 2026 David is involved in a farm accident and is permanently disabled and as a result he meets a condition of release. Because the outstanding balance of the LRBA is now included in his TSB, his TSB has increased to $4 million. The proposed additional tax will now apply to David in the 2027 financial year even though his actual superannuation balance is below $3 million.

Proposed Tax Outcomes (FY27)
Assume that the value of land assets increases over the course of FY27, from $4 million to $4.5 million.

Additional tax liability = 15% x Earnings ($500,000) x share over $3 million (33%)
Additional tax liability = **$24,750**