

**Submission  
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## **INQUIRY INTO ZONAL TAXATION**

**Organisation:** NSW Farmers  
**Name:** Ms Jaimie Lovell  
**Position:** Policy Director - Rural Affairs and Business, Economics and Trade  
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## **Submission: Parliamentary Inquiry into zonal Taxation**

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**NSW Farmers' Association  
35 Chandos St  
St Leonards NSW 2065**

[REDACTED]

### **NSW Farmers' Association Background**

The NSW Farmers' Association (the Association) is Australia's largest State farmer organisation representing the interests of its farmer members – ranging from broad acre, livestock, wool and grain producers, to more specialised producers in the horticulture, dairy, egg, poultry, pork, oyster and goat industries.

## **Executive Summary**

The NSW Farmers' Association is Australia's largest state based farming organisation and represents the interests of numerous agribusiness enterprises located within rural and regional NSW. The organisation provides its farming members the opportunity for representation to Government through non-party political lobbying.

The Association supports reform of the Australian Commonwealth, State and Local Government revenue collection provided the reform improves the fairness, efficiency and simplicity of the overall tax system; balances tax efficiency (marginal economic burden) with fairness across asset and income classes; provides the various levels of government with more consistent and manageable long-term revenue streams without increasing the overall tax burden; and supports and encourages a vibrant rural Australia, a productive and efficient agricultural sector, and fairly reflects the highly variable returns that farmers receive as a result of risk factors beyond their control.

### *Payroll Tax, Stamp Duty and Land Tax*

We are opposed to stamp duty and payroll tax. In the current taxation debate, we urge the NSW Government to play their part in meaningful taxation reform to provide a platform for future economic growth. Removal of payroll tax from all small business in rural and regional areas would drive employment growth in these areas.

The current land tax exemptions for primary production businesses must be retained.

### *Utility Charges*

We further suggest that policy makers must turn their attention to programs that drive water-efficient irrigation practices and increased electrification of pumping, thereby reducing diesel consumption and increasing the energy productivity of Australian agriculture. Advancing renewable energy will require ensuring that there are efficient feed-in tariffs for farmers.

In addition, it is vital that there are changes to the way that electricity is regulated so that the asset base is transparent and efficiently calculated. Equally solar energy needs to be appropriated incentivised following the cessation of the Solar Bonus Scheme.

### *Fuel Levies*

It is critical that those living in rural areas are not disadvantaged by the introduction of new taxes or winding back of subsidies designed to compensate them for the lower level of government services or infrastructure that they have access to. In this respect, telecommunications are no different to other utilities and are one of the most commonly cited deficits in service to the bush. In fact, farmers say this is one of the greatest inhibitors of productivity growth on farm.

The Association welcomes the opportunity to outline recommendations which support greater productivity in the farming sector to the NSW Parliament.

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## **i. Exemptions from, or concessions in relation to, payroll tax, stamp duty, and land tax.**

### Payroll tax

The burden of payroll tax is borne by employers, creating an immediate disincentive to businesses taking on new employees. This disincentive is would be most keenly felt by employers that are approaching or just above the \$0.75 million threshold where the additional cost of compliance is comparatively more significant.

Administration of payroll tax obligations is particularly complex for employers operating in multiple states. Different rules apply in certain jurisdictions in relation to the grouping of related businesses, the determination of which State the employment relates to, the definition of wages in each State, and what activities are eligible for an exemption. This complexity creates considerable compliance risk and administration cost to affected businesses.

Further, payroll tax is calculated monthly and, if you start or stop employing in NSW within a financial year, you are not entitled to the full threshold. Instead, you receive a proportion of the threshold equal to the ratio of the number of days you employ to the number of days in a year. This system penalises those who require seasonal workers – this is particularly relevant to the agricultural sector. Horticulturalists, for instance, require large workforces seasonally and are penalised for producing fresh produce for households across the state and beyond.

#### ***Recommendation 1: Remove payroll tax, which is a tax on productivity and growth.***

Whilst only a small percentage of our membership pay payroll tax, it does affect the larger businesses some of our big horticulture members may also need to pay payroll tax due to the high level of casual employees they employ for harvesting.

The time involved in processing payroll tax is a drain on businesses and a cost in accountancy or in time and red tape for smaller businesses where bookkeeping work is typically done by the partner.

In addition, certain contractors (e.g. shearing contractors) are liable for payroll tax. In the agricultural sector, where there is increasing level of contracting occurring, the costs of red tape like payroll tax are increasingly being passed to the farmer.

### Stamp duty

Stamp duty should be abolished, particularly on all non-residential property conveyances, in accordance with the 1999 Intergovernmental Agreement.<sup>1</sup>

The Henry Review identified stamp duty on property conveyances as an inefficient tax. It can be avoided by simply not taking part in dutiable transactions, making it volatile. It also leads to inefficient economic decision making as it discourages moving capital that could potentially be invested in more productive locations and assets.

<sup>1</sup> Stamp duty on non-residential property conveyances was the final tax that was to be abolished under the Intergovernmental Agreement however the States and Territories have only agreed in part to this by committing to the removal of stamp duty on non-real non-residential property (e.g. transfer of shares in a Company or goodwill of a business). In New South Wales the abolition of stamp duty on non-real non-residential property has been deferred multiple times and is currently scheduled to occur on 1 July 2016

In NSW the stamp duty rate on land and business transfers is 5.5% over \$1m – a considerable cost. Further, as the subsequent purchaser also needs to pay duty, this impost does not add to the value of the assets and can often mean it takes some years before values increase sufficiently in order for the owner to recover their cost of the asset in a sale let alone make a profit. This conceptually can lead to taxpayers retaining assets that would otherwise have been sold merely to try and recover their original investment and potentially distorting the market.

When dutiable property is also a taxable supply for GST purposes, stamp duty is calculated on the total GST inclusive price of the property. This results in the purchaser paying tax on a tax as the GST component increases the stamp duty payable.

In NSW, intergenerational transfers of rural land used for primary production between generations (and between siblings) are exempt from 'Transfer Duty' to facilitate younger family members taking over family farms. In the 2014-15 budget this was worth \$35 million to the sector. It is critical that this exemption is retained.

Additionally, young farmers who want to start their own farm or those who cannot inherit property from family find stamp duty is also one of the impediments to getting established. The Government should consider an exemption for all young farmers purchasing their first farming enterprise.

***Recommendation 2: Remove stamp duty, which is a tax on farms agglomerating to build more efficient and competitive businesses and one of the impediments to young farmers getting established.***

### Land Tax

The current land tax exemptions for primary production businesses must be retained. Whilst Recommendations 51-54 of the Henry Review suggested that the inefficiencies of stamp duty be addressed by replacing stamp duty with a broad based land tax, by definition, any alternative land based tax would increase the tax burden upon farmers.

An extension of Land Tax to include agricultural land would have a severe impact on farmers' income. Income from farming is seasonal and volatile. During drought and natural disasters the revenue that can be generated from the land can be very seriously disrupted. The ability to pass on extra costs to consumers is limited, and therefore any additional Land tax would considerably reduce profitability.

Because Australian property owners are potentially subject to three different taxes (stamp duty, land tax and council rates), taxes on property make up around 9% of taxation which is almost double the OECD average of 5%.<sup>2</sup>

Land is the most significant asset in a primary production business<sup>3</sup>, particularly the family farm, and as a result, this high rate of tax falls heavily upon the industry and reduces competitiveness (see example in the box below, from an internal paper from RIRDC).

In NSW, the Land Tax Exemption was worth \$500 million to the agricultural sector in 2014-15.

<sup>2</sup> Australian Government 2015, *Re:think – Tax Discussion Paper*, [http://bettertax.gov.au/files/2015/03/TWP\\_combined-online.pdf](http://bettertax.gov.au/files/2015/03/TWP_combined-online.pdf)

<sup>3</sup> Australian Bureau of Agricultural Resource Economics (ABARE), 2014 figures state that total farm business assets on average comprise 83% property value, 2% current assets, 15% non-current assets.

**Recommendation 3: Maintain current exemptions for primary production businesses from land tax**

Take the example of, say, a 4th generation dairy farmer on the South Coast of NSW - just 5 minutes from the beach and 90 minutes from Sydney. Due to the low farm gate milk prices, it has been difficult to make a good return for the risk and effort, however the fertile soils and good milk production has meant the family have maintained a successful farming.

In recent years, there has been an increase in residential development down the coast and neighbouring farms have been subdivided into 5 acre lifestyle blocks. However more than half remain unsold and, in this example, it could be 10 to 20 years before the population will increase to the point where further development of the farming land would be feasible. Land values have risen to such an extent that this member's land has increased in value to above a level where Land Tax would be imposed if the Henry recommendation was implemented.

The additional cost to the business would place at risk the family farm. For example a farm with land worth \$2 million in NSW would attract land tax of \$24,388 per annum and this would be in addition to other costs of land ownership including Shire Council rates, stamp duty on purchase, and Local Land Services rates). Further, if the member and his/her family decided to sell, developers would need to take into account this cost in their investment decision, especially given it could take 10 to 20 years before it was feasible to develop.

## **ii. Concessions in relation to utility charges**

Energy continues to be a major cost for primary producers. Agriculture is the fourth most energy intensive industry in Australia, behind manufacturing, transport and mining.<sup>4</sup>

Distance also has a huge negative affect on the cost of energy for farmers. There are currently tax concession, loans and reduced interest loans in place for farmers to implement technology to reduce energy costs. For example, the NSW Rural Assistance Authority has the Farm Innovation Fund, while the Clean Energy Finance Corporation provides loan at reduced interest rates.

The NSW Farm Innovation Fund provides low interest loans of amounts per project ranging from \$250,000 and a maximum of \$500,000 to be borrowed at once. These loans can be used towards the costs of carrying out permanent capital works that will have a significant beneficial impact on the land, long term profitability and address adverse seasonal conditions, such as drought preparedness, environment, farm infrastructure and natural resources. Currently there are available funds of \$250 million with \$69 million worth of loans approved.<sup>5</sup> In addition, the accelerated small business write offs and the current depreciation regime are also applicable to energy-related capital works.

### Electricity pricing

Electrification is a key to innovation and total productivity in agriculture and NSW Farmers requests that the Committee considers the potential of zonal taxation measures to address the structural problems created by current regional electricity pricing policy.

Increased electrification is a priority for most sectors of agriculture and fundamental to general productivity as well as energy productivity. Electricity is the optimal energy source for smart systems, automated vehicles, robotics and advanced manufacturing plants. In the longer term, we predict significant increases in agricultural electricity demand as the industry innovates.

<sup>4</sup> Australian Bureau of Statistics, 4604.0 Energy Account Australia

<sup>5</sup> We note that the Treasurer has recently announced that \$30million will be brought forward to next year (total of \$80million for 2016/17), due to high demand for this program.

Today, however, we are moving in the wrong direction as exorbitant network charges drive farmers to substitute electricity for diesel and to disconnect from the grid.

We are calling for reform to electricity market policy to:

- reduce the cost of network electricity for irrigators and other intensive sectors
- stem the loss of regional electricity customers from the national electricity market
- drive demand management collaboration in regional networks
- drive strategic deployment of renewable generation where is most needed to provide energy at least cost to industry and society

National electricity policy has to date largely neglected the opportunities that exist to drive innovation in regional electricity supply and demand management.

An international comparison of Australia's key agricultural trading partners conducted in 2012<sup>6</sup>, showed that Australia's average electricity costs had grown by 40 percent since 2007. In 2011/12 average household electricity prices in Australia were 12% higher than average prices in Japan, 33% higher than the EU, 122% higher than the U.S. and 194% higher than Canada.

Typically government regulated network costs account for 60% of a farmers' electricity bill while the actual cost of electricity makes up just one-quarter of the electricity bill. Exorbitant network charges are forcing irrigators to go off grid, typically turning to diesel powered generators rather than renewables. Something is seriously wrong when switching to on-farm diesel generation has become a better option than continuing to use an existing investment in network connection (establishing a grid connection can cost upwards of \$100,000). Farmers want to use network electricity but increasingly they cannot afford to.

Machinery and equipment, including irrigation pumps, can operate more efficiently and flexibly using electricity. Electrification is thus a pathway to improved performance and opens the door to use sophisticated efficiency technologies (solar, VSDs, automated control *etc*). Currently, however, rising costs of the fixed electricity network are pushing farmers away from electrifying and onto diesel.

#### Food & fibre tariffs or compensating taxation measures

Farmers, and especially irrigators, have electricity demands profiles that are considerably inelastic compared to other industries. Production is strongly tied to weather and water availability, as well as the role energy plays to provide water at critical times. A bespoke tariff is therefore necessary to enable farmers to operate effectively and not abandon a crop (resulting in several months of productivity loss) if energy costs are considerable.

Such a tariff should also explore the role that farmers may play in demand management through load shifting measures. For example, the most effective energy storage solution in irrigation is transfer pumping to elevated storages. Irrigators are well positioned to utilise this dynamic if a tariff structure or demand management solution is put in place to enable it.

The AER through its draft pricing determinations in Queensland, New South Wales and South Australia sought to deliver significant cost reductions to regional users. However, due to the electricity networks vigorously challenging the AER determinations and the

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<sup>6</sup> *'Electricity Prices in Australia: An International Comparison': A report to the Energy Users Association of Australia by Carbon + Energy Markets, 2012.*



constraints within the Australian Energy Markets Commission (AEMC) rules that govern the regulatory process, the sector is back where it started, facing unacceptable costs across those states.

A well constructed food and fibre tariff or taxation measure could:

- Provide energy security to irrigators by providing for inelastic demand at a financially sustainable price
- Drive demand management collaborations at the ends of regional networks, reducing operational expenses and future capital expenditure for distributors.
- Facilitate a more orderly deployment of local scale renewable generation.
- Arrest the present flight from grid electricity by irrigators
- Drive electrification of irrigation and thus help ameliorate the 'death spiral'. Analyses have shown that a 30% reduction in electricity prices could result in a greater increase in electricity consumption and farm productivity and thus be a revenue-neutral proposition for the networks.

***Recommendation 4: Electricity pricing, policy and programs that drive water-efficient irrigation practices and increased electrification of pumping, thereby reducing diesel consumption and increasing the energy productivity of Australian agriculture, including:***

- a. a national food and fibre tariff model tailored to the unique needs of producers***
- b. a regional electricity policy framework that drives efficient demand management at the ends of networks and avoids large electricity users moving off the grid (leaving stranded network assets)***

***Recommendation 5: Policy and R&D that advances farm-scale renewable energy as part of integrated region energy supply and demand management solutions, thereby leveraging existing distribution assets.***

***Recommendation 6: Electricity Examination of a rule change at the Australian Energy Market Commission (AEMC) to change the way the regulated asset base (RAB) of network companies is calculated.***

A scoping study is needed to explore policy options in detail. Research commissioned by National Irrigators Council found that key features of an effective policy would include:

- A supply charge of approximately \$50-\$200 per annum (customer specific but invariant to electricity consumption)
- A shortened 'peak' demand window (to approx 3 hours) to incentivise irrigators to shift electricity use.
- Different electricity rates for:
  - Seasonal use
  - Days of week
  - Time of Day

Further notes on restructuring charges and tariffs are laid out in Appendix 1.

#### Solar Bonus Scheme (SBS)

The Association supports farmers who are seeking a reasonable price (parity pricing) for solar power produced once the SBS finishes. The tariffs provided under the SBS are set to expire on 1 January 2017. A replacement or transitional tariff solution for systems still under this scheme has not been proposed and many voluntary feed-in-tariffs (from electricity retailers) that may replace the SBS tariff are often lower than IPART's recommended "fair value" of 4.4-5.8 c/kWh. Participants in the scheme

could find themselves buying that electricity back at normal (and much higher) retail rates.

Whilst some participants can change over to new meters to be eligible for the Net power pricing, this is an added expense and does not address the underlying structural problem, i.e. that farmers both produce and use a lot of energy and need to be supported to continue to provide clean energy to the grid.

**Recommendation 7 – That adequate incentives are provided to farmers and irrigation corporations to install or continue to operate renewable electricity generation infrastructure with the aim of:**

- **Assisting in the management of regional peak load**
- **Reducing maintenance costs and future capital costs of regional and remote distribution infrastructure**
- **Reducing farmer electricity supply costs for pumping and other intensive energy use**
- **Accelerating electrification of farm machinery and reducing dependence on fossil fuels**
- **Enable smart demand management (eg load shifting)**

**To support this process, require distributors to fund provision of smart meters which are required both for net power pricing and strategic demand management.**

### **iii. The impact of fuel levies on regional growth**

The Association is firmly of the view that the Fuel Tax Credit scheme must remain.

The purpose of the fuel tax credits scheme is to remove the effect of fuel tax on business inputs; the same tax policy principle that underpins the GST. Fuel tax credits also recognise that excise is an implicit road-user charge originally introduced to fund public roads. Farmers operate vehicles and machinery on farms not public roads.

Fuel tax credits further recognise that excise should not apply to the use of fuel in electricity generation because excise is targeted at transport use of fuels - not electricity generation, heating or other applications.

Fuel tax credits are claimed by a range of industries and by households. They are vital to the competitiveness of industries operating in regional Australia. Agriculture makes up 45 per cent of the claims for the credit.

Large export earning industries such as mining, agriculture, fishing, forestry and tourism rely on diesel to operate heavy machinery off-road and to operate in remote areas off the electricity grid.

Any changes to existing fuel tax credit arrangements would amount to a new tax on regional and rural Australia. In fact, as Treasury staff have noted, it would amount to double taxation.<sup>7</sup>

<sup>7</sup> A senior Treasury official told a Senate hearing in June 2014: ‘... the principal rationale behind the fuel tax credit system ... was to ensure that a number of industries that used fuel off road were not subject to double tax.’ (quoted in *Powering Regional Australia: Fuel Tax Credits*, April 2016 available at: <http://www.nff.org.au/read/5263/importance-of-fuel-tax-credits-for.html> )

**Recommendation 8: Maintain the fuel tax credits scheme**

#### **iv. Any other related matters**

##### Tax zone rebates

Tax zone rebates were introduced in 1945 to compensate recipients for the disadvantages of living in remote areas, including distance, climate and the higher cost of living. These rebates apply to people living in two designated Zones (Zone A and Zone B), as well as 'special areas' (particularly isolated areas). The Western Division of NSW falls into Zone B which means that residents<sup>8</sup> receive a base rebate per year of \$57 as well as a 20 per cent loading.

The rebate amounts have remained unchanged since 1993. The effects of inflation have rendered the dollar amounts of rebates ineffective in meeting the disadvantages of living in the remote areas. At today's rates Zone B should rise to \$221.

**Recommendation 8 – Increase the zonal rebate to keep pace with CPI**

The Association believes that the rebate amount should be increased to an amount in line with CPI, that would be more closely aligned with the original policy intent of the tax zone rebate when it was introduced in 1945, *i.e.* to compensate recipients for the disadvantages of living in remote areas. Centres with populations greater than a certain level (say 25,000) could be removed from the zoning.

##### Distance and telecommunications

Farmers want a telecommunications service that is comparable to that in the city. They also want broadband pricing that reflects how much you use, not where you live. Whilst the National Broadband Network (NBN) is now being rolled out, the issue of mobile coverage continues to be a major impediment to efficient and productive businesses in the bush.

Expanding the footprint of mobile phone coverage (and concurrently NBN fixed wireless coverage) is critical to encouraging the next leap in agricultural productivity. A 2014 NSW Farmers survey of over 600 members showed that the overwhelming majority of NSW farmers believe that mobile service is 'essential' but less than 20% have reliable access on farm for mobile or mobile internet coverage.

The NSW Coalition Government has taken a leadership role in partnering with the Federal Government to fix the black spot issues in NSW. It is critical that there is an ongoing budget allocation for the elimination of mobile black spots. This funding should be provided with similar conditions to those that existed under Round One of the program, which required that mobile towers funded by the NSW government be made available to any telecommunications company that wished to site equipment on them. In addition to this, NSW Government funding should be prioritised towards mobile towers that will also be used to extend the National Broadband Network, particularly the Fixed

<sup>8</sup> Section 78A of the ITAA 1936 states that to receive the rebate a person must reside or work in a specified remote area for more than 182 days in an income year.

Wireless network. Finally, the NSW Government should coordinate with the Commonwealth to ensure this is a recurring budget item.

In October 2015, the Federal Government's Regional Telecommunication Review Committee released the latest Regional Telecommunications Review, which identified ongoing and systemic issues in provision of regional telecommunications. Among other items, the review recommended that a long term fund be established to support loss-making regional infrastructure and services with scope to include subsidy arrangements for the non-commercial NBN services (Satellite and Fixed Wireless) as well as social equity elements that merit funding.

The Mobile Black Spot Program Round 2 has the ability to further leverage significant private funding and make a meaningful improvement to mobile coverage in regional areas. It also has the potential to facilitate the roll out of mobile broadband or fixed wireless broadband services using the NBN. Provision of these services drives increased business and social connectivity (overcoming isolation), allows innovation and productivity improvements in business practice and also improves the communication in case of emergencies. As agriculture moves towards the greater use of mass produced sensor technology and the use of 'big data' to drive productivity, reliable on farm mobile and internet service will become increasingly vital. Without reliable mobile and internet coverage, farm businesses will not seek out the technological improvements that will allow them to significantly improve business management.

Noting that the Federal Government has contributed \$60 million nationally to Round 2 of the Mobile Black Spot Program, NSW Farmers seeks that the NSW Government provide between \$15-20 million in the 2016/17 budget, which is commensurate with the proportion of funding that it provided under Round 1 of the program. Allocation of this funding can then be used to secure co-contributions from telecommunications companies.

## **Conclusion**

In conclusion, the Association supports fairness, efficiency and simplicity of the overall tax system with consistent and manageable settings which supports and encourage a vibrant rural Australia, a productive and efficient agricultural sector, and fairly reflects the highly variable returns and services that farmers receive as a result of factors beyond their control.

## **Appendix 1: Details on restructuring charges and tariffs**

**Supply charges:** These charges are connection-specific and do not vary with consumption. They should be set at a level high enough to recover individual customer specific costs – such as for reading and supplying meters – (i.e. costs that are not shared with other consumers and which do not vary with the customers' level of consumption or demand)

**Consumption charges:** These charges are levied per kWh consumed. They should be set to cover costs that are variable in the short term and also to make a contribution to the recovery of sunk costs. The design of consumption charges should also reflect the following considerations:

- It may be sensible to have consumption charges that vary by time of day: such as peak and off-peak or peak, standard and off-peak and where applicable should reflect seasonal variations.
- The difference between peak, off-peak and if applicable standard rates should reflect the existence of temporally defined capacity constraints and customers' temporally varying elasticity of demand.
- If there are to be significant differences between the peak and off-peak rates (peak rates greater than, say, twice off-peak rates) then it is important that the peak rates apply for limited intervals so that irrigators can respond to those prices by reducing their consumption.

**Demand charges:** Charges for peak demand in addition to, or as an alternative to consumption charges, introduce additional complexity in metering and billing: specifically the requirement for half-hourly remotely read meters. Demand charges are plausible for higher consumption customers (those that are likely to consistently consume more than 100 MWh per year). An economically sound specification of demand changes should reflect the following:

- Demand charges should not be subject to minimum chargeable demand levels. Such minimum thresholds simply turn demand charges into fixed charges, which defeats the rationale for their inclusion.
- It is plausible to differentiate demand charges by voltage of supply (in recognition of the greater amount of infrastructure required to supply lower voltage customers relative to higher voltage customers).
- It is not plausible to differentiate demand charges on the basis of subscribed or minimum maximum demands.
- Demand charges should signal expected future network capacity shortfalls that may arise (depending on the network) during periods of simultaneous peak demands. The applicable period should be short (no more than three hours). This is adequate to capture the time periods when peak demands are most likely to arise. Sufficiently short peak demand charge periods are also necessary to provide irrigators with an opportunity to reduce their bills by reducing demand in those periods.

## **Acknowledgements**

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