Department of Agriculture and Water Resources

Background Paper 17

This paper was prepared by the Department of Agriculture and Water Resources in response to a request made by the Royal Commission.

Australian Government
Department of Agriculture and Water Resources

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Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

28 June 2018

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Executive summary

Debt is an important source of funding for farm investment and ongoing working capital, particularly for the family owned and operated farm businesses dominating most sectors of Australian agriculture.

The Department of Agriculture and Water Resources (the department) delivers a number of measures on behalf of the Australian Government to assist farmers with debt financing, including a $2.5 billion commitment over 10 years for concessional loans. The Regional Investment Corporation (RIC) will deliver farm business concessional loans and the National Water Infrastructure Loan Facility (NWILF) from 1 July 2018.

The government is also continuing to work in a number of other farm debt and finance related areas, including discussing a nationally consistent farm debt mediation scheme with state and territory governments, and commencing the annual collection of detailed information on agricultural debt.

This background paper summarises a range of existing information from the Australian Bureau of Agricultural and Resource Economics and Sciences (ABARES), including data from the farm surveys it conducts, and other public resources.

This data indicates:

- Nationally, total indebtedness of the agriculture, forestry and fishing industries[1] to institutional lenders was $71.7 billion at 30 June 2017.
- Bank lending accounts for 96 per cent of total institutional lending[2] to agriculture, forestry and fishing industries, with bank lending accounting for $68.6 billion at 30 June 2017.
- Debt to fund land purchases accounts for the largest share of debt on farms, accounting for an estimated 44 per cent of average broadacre debt at 30 June 2017. Working capital debt accounted for 37 per cent of average broadacre debt at 30 June 2017.
- Much of the aggregate agriculture sector debt is held by a relatively small proportion of mostly larger farms. At 30 June 2017, around 70 per cent of aggregate broadacre debt was held by just 12 per cent of farms.

[1] Defined by the Reserve Bank of Australia (RBA) as 'rural debt'.
[2] Defined by the RBA as lending from banks (Authorised Deposit-taking Institutions), other government agencies (such as the Queensland Rural and Industry Development Authority), and pastoral and other financial companies (e.g. those providing finance leases).

This background paper also provides some information from the first annual (2017) Agricultural Lending Data collection undertaken by the Australian Prudential Regulation Authority (APRA). While this data is not yet finalised, it indicates (at 30 June 2017):

- The average debt (total credit outstanding) per business entity (effectively 'borrowers') was $481,428 as at 30 June 2017.
- The average credit limit per business entity was $579,055 as at 30 June 2017.
- Of farm business entities with borrowings, 0.65 per cent had loans more than 90 days past due.
- Of the total value of loans, 0.90 per cent was more than 90 days past due.

This data also indicates (over the 1 July 2016 to 30 June 2017 period):

- Nationally, there were 96 farm debt mediations and 33 foreclosures.
- The average credit outstanding per business entity for new foreclosures was $1.9 million.
- Total credit outstanding on new foreclosures was $62 million, or 0.09 per cent of aggregate credit at 30 June 2017.

Introduction

The Department of Agriculture and Water Resources (the department) welcomes the opportunity to provide a background paper for the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

The requested focus of this background paper is on key reforms (legislative, regulatory or policy developments) over the past 10 years, and any anticipated reforms, relevant to farm finance issues. The department notes, however, its activity in farm finance issues needs to be considered in the broader context of Treasury portfolio activities and responsibilities, as it has limited legislative and regulatory responsibility for financial and economic matters.

The department continues to maintain an active interest in farm debt matters, having contributed to a number of past inquiries and government reports/responses, including the:

- Parliamentary Joint Committee on Corporations and Financial Services' *Inquiry into the Impairment of Customer Loans* (2016)
- Australian Small Business and Family Enterprise Ombudsman report on its *Inquiry into Small Business Loans* (2017)
- Senate Select Committee Inquiry on *Lending to Primary Production Customers* (2017)
- Senate Inquiry on *Foreign Investment and the National Interest* (2013), and
- Senate Inquiry on the *Reserve Bank Amendment (Australian Reconstruction and Development Board) Bill 2013* (2015).

The department currently delivers a number of measures to assist farmers with debt financing issues. These are outlined below in detail, but range from those aimed at supporting farm businesses through a crisis or shorter-term financial difficulties, to those with the objective of increasing the longer-term preparedness and financial resilience of farmers.

The department is also involved in a number of other debt related projects, also summarised below, including the collection of more robust and regular data on debt in the agriculture sector and supporting developing a nationally consistent farm debt mediation scheme.

Recent financial performance of Australian farms

There is substantial variability in the income and debt servicing capacity of Australian farms across years. In any year, it is common for a proportion of farms in some industries and regions to be under financial pressure as a result of seasonal or other production conditions and commodity prices.

The Australian farm sector recorded strong financial performance in 2016-17. The gross value of farm production was a record $62.3 billion – 15 per cent above the average of $54.4 billion for the five years to 2015-16, in real terms.

Record production values in 2016-17 mainly reflected an increase of 6 per cent in the volume of farm production as record winter crop yields in southern Australia resulted from favourable seasonal conditions throughout winter and spring.

In 2016-17, farm cash[3] incomes for grains, sheep and beef industry farms were the highest recorded in more than 20 years. Grains, sheep and beef industry farms (broadacre farms) in aggregate account for 70 per cent of Australian farm businesses. Average farm cash income increased for grains, sheep and beef farms in all states in 2016-17.

For irrigated agriculture, widespread early season rainfall resulted in national storages increasing from 50 per cent of capacity at the start of 2016-17 to 79 per cent at the end of the year, allowing high water allocations around Australia. High allocations resulted in increased irrigated agricultural production in 2016-17, particularly rice, cotton and horticulture.

While most Australian farms experienced high farm cash incomes in 2016-17, farm cash incomes declined for dairy farms in southern New South Wales, Victoria, Tasmania and South Australia. Prices received by many dairy farmers in these regions were reduced in 2016-17 as a result of lower export returns and difficulties with Australia's largest dairy processor, Murray Goulburn. Milk production declined in response to lower prices and wet seasonal conditions in Victoria, the state with the largest share of production.

Cyclone Debbie and associated flooding disrupted production on sugar cane, vegetable and horticultural farms along the Queensland coast from Proserpine to Bundaberg and damaged farm infrastructure. Farms on the North Coast of New South Wales were also affected by the flooding.

[3] Farm cash income is a measure of cash funds generated by farm businesses for farm investment and consumption after paying all costs incurred in production.

Record farm cash incomes for broadacre in 2016-17 followed two years of high incomes in 2014-15 and 2015-16. This income provided many farm businesses with an opportunity to reduce existing farm business debt as well as the opportunity to undertake new farm investment, partly funded by new borrowing. Investment in farm land and machinery and infrastructure increased in 2015-16 and land values increased in many regions boosting farm equity.

Farm debt levels

Debt is an important source of funds for the Australian agriculture sector. Without debt financing, the family owned and operated farm businesses dominating most areas of Australia's agricultural industries would not be able to fund on-farm investments and maintain their working capital.

Funding by family owned and operated farms (which make up more than 95 per cent of broadacre and dairy farms) would otherwise be limited to the funds the family has in reserve and the profits the business can generate.

ABARES data show:

- Debt to fund land purchases accounts for the largest share of debt on farms, accounting for an estimated 44 per cent of average broadacre debt at 30 June 2017.
- Working capital debt accounted for 37 per cent of average broadacre debt at 30 June 2017.

Farm equity

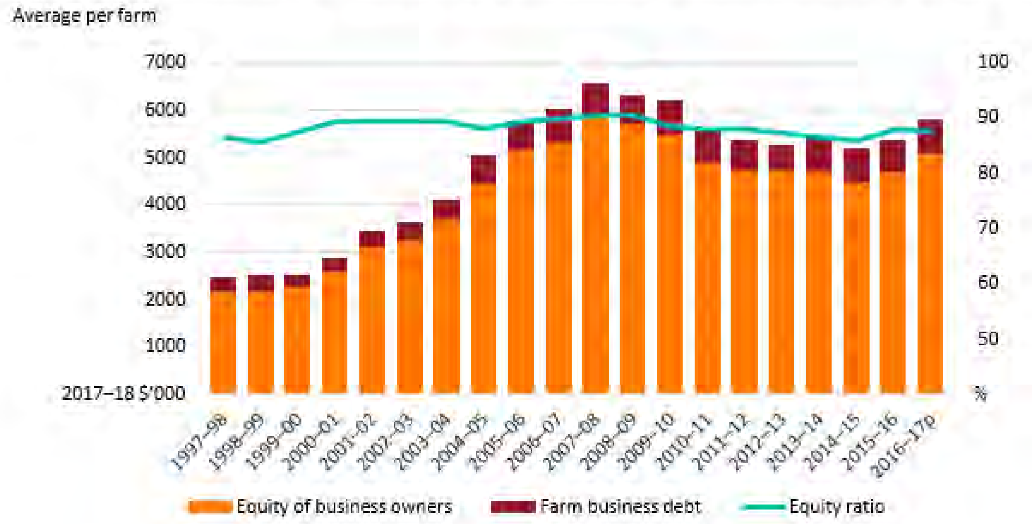
Family farms in Australia rely on maintaining high farm equity to provide the capacity to borrow to meet cash flow needs during periods of reduced farm income as well as for new investment. Despite increases in farm debt over the long-term, average farm equity for broadacre and dairy farms remains strong because of increases in the value of agricultural land (Figure 1).

The average equity ratio at 30 June 2017 is estimated at 87 per cent for broadacre farms and 80 per cent for dairy farms. Around 83 per cent of broadacre farms and 51 per cent of dairy farms had equity ratios exceeding 80 per cent at 30 June 2017.

Decline in land values in some regions between 2007-08 and 2013-14 reduced farm equity in those regions. Together with the onset of the global financial crisis in 2008, these declines prompted banks to review and tighten lending to the agriculture sector.

Farm equity strengthened for the majority of broadacre farms since 2014-15 with the general rise in prices for beef cattle and sheep, higher land values and reductions in debt as a result of high farm cash incomes. Higher farm cash incomes for broadacre farms from 2014-15 to 2016-17 led to an increase in the proportion of broadacre farms buying land.

Figure 1: Farm business debt, owner equity and equity ratio, Australian broadacre farms, 1997-98 to 2016-17.



p Preliminary estimate. All financial estimates are in 2017-18 dollars.
Source: ABARES Australian Agricultural and Grazing Industries Survey

National rural indebtedness

Data collected by the Australian Prudential Regulation Authority (APRA) and reported by the Reserve Bank of Australia (RBA) provides an indicator of trends in debt since 1964. This data indicates nationally, total indebtedness of the agriculture, forestry and fishing industries[4] to institutional lenders[5] increased by 77 per cent from $42.7 billion at 30 June 2001 to $75.5 billion at 30 June 2009, in real terms (Figure 2).

Several factors contributed to the growth in debt over this period, including:

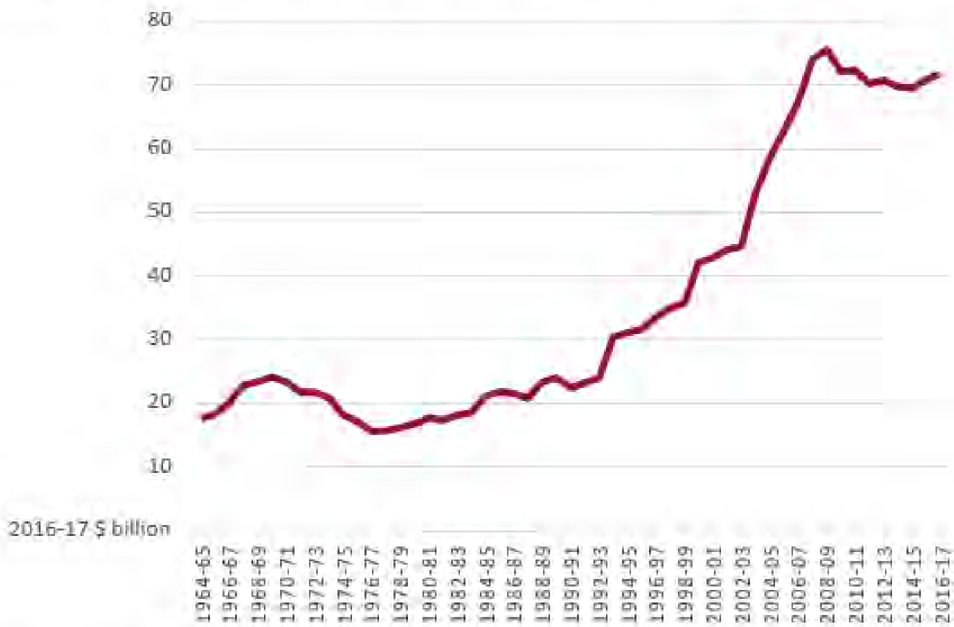
- lower interest rates
- large increases in land values, which raised borrowing capacities
- increases in farm size and intensity of production
- changes in commodities produced
- reduced farm cash incomes because of widespread and extended drought conditions
- provision of interest subsidies to farmers in drought through Exceptional Circumstances arrangements[6], and
- increased use of interest-only lending.

[4] Defined by the RBA as 'rural debt'.
[5] Institutional lenders are defined as Authorised Deposit-taking Institutions (ADIs), other government agencies (such as the Queensland Rural and Industry Development Authority) and pastoral and other financial companies.
[6] Exceptional Circumstances Interest Rate Subsidies ceased on 30 June 2012.

Total rural debt subsequently declined in real terms to $69.4 billion at 30 June 2015 before rising to $71.7 billion at 30 June 2017.

Bank lending accounts for 95 per cent of total institutional lending, with bank lending declining from $68.5 billion at 31 December 2009 to $63.2 billion at 31 March 2014 before rising to $68.6 billion at 30 June 2017.

Figure 2: Total institutional debt, agriculture, forestry and fishing industries



Source: Reserve Bank of Australia money and credit statistics, Rural Debt by Lender (table D9)

Agricultural indebtedness

APRA has recently commenced collection of data for the department[7] to improve the information available on lending to the agriculture sector. This will build on the quantitative information available from the farm surveys conducted by ABARES, and the anecdotal and other qualitative evidence available from those delivering services on behalf of the department, such as the Rural Financial Counselling Service (RFCS).

The first mandatory annual collection of data was for 30 June 2017, with the collection to be repeated at 30 June for each subsequent year. An interim voluntary collection was completed for 30 June 2016, as part of the consultation process with financial institutions, comprising Authorised Deposit-Taking Institutions (ADIs) and Registered Financial Corporations (RFCs) with lending facilities exceeding $50 million.[8]

[7] Reporting Standard ARS 750.0.

[8] Further information on this collection process is provided in Attachment A.

Data from the 2016 and 2017 collections has not as yet been publicly released. The interim voluntary data collection for 30 June 2016 resulted in under-representation of ADIs and RFCs, making comparison with the 30 June 2017 data problematic. Tabulation of data for ADIs and RFCs reporting in both periods is therefore yet to be finalised, however, there are some conclusions to be drawn about agricultural indebtedness as a whole:

- As at 30 June 2017, there was $70.123 billion of agricultural debt.
  - This was spread across 145,656 business entities (effectively 'borrowers').
- Average debt (total credit outstanding) per business entity was $481,428 as at 30 June 2017.
- Total credit limits equated to $84.343 billion as at 30 June 2017.
  - The average credit limit per business entity was $579,055 as at 30 June 2017.

It is important to note this data is not directly comparable with the RBA rural debt data as it does not include fishery and forestry businesses.

Distribution of farm debt

Much of the aggregate agriculture sector debt is held by a relatively small proportion of mostly larger farms. At 30 June 2017, around 70 per cent of aggregate broadacre debt was held by just 12 per cent of farms. On average, these were large farm businesses and, in aggregate, they produced around 50 per cent of the total value of broadacre farm production in 2016-17.

Around 44 per cent of grains industry farms and 32 per cent of dairy industry farms nationally carried more than $1 million in debt at 30 June 2017. In contrast, 71 per cent of beef farms and 56 per cent of sheep and sheep–beef farms nationally were recorded as having debt of less than $100,000 at 30 June 2017. Many of these businesses are small.

Aggregate debt is slightly less concentrated among larger farms in the dairy industry. Nevertheless, around 70 per cent of aggregate dairy sector debt at 30 June 2017 was held by 30 per cent of farms.

Debt serviceability

Paying off debt

Declines in interest rates over the past 25 years, reduced bank lending following the global financial crisis in 2008 and, more recently, the strong increase in farm income, have reduced the burden of servicing debt and increased the rate of debt repayment.

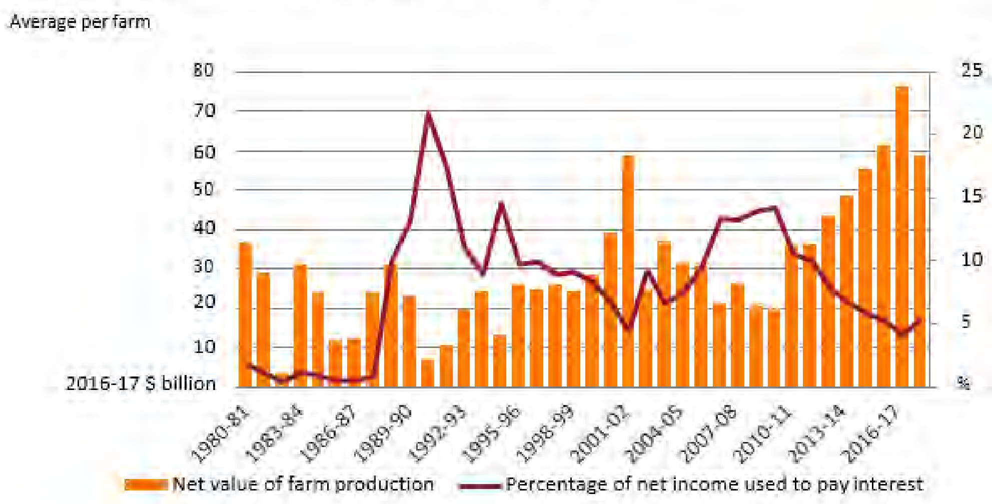
For the agriculture sector as a whole, the proportion of the net value of farm production needed to fund interest payments rose substantially between 2001-02 and 2008-09. This resulted from a large increase in farm debt and reduced farm receipts through extended drought conditions. Higher net farm income since 2010-11 and reductions in interest rates resulted in a decline in the average proportion of net income needed to fund interest payments (Figure 3).

Large increases in borrowing through the 2000s and a reduction in net income between 2007-08 and 2013-14 resulted in the proportion of net income needed to fund interest payments being high for the beef industry (Figure 4). The proportion of net income needed to fund interest payments peaked at just over 60 per cent in 2007-08 as northern beef industry farms commenced rebuilding herds after the end of the 2000s drought. The proportion trended downwards to 16 per cent in 2015-16 and is projected to be around 20 per cent in 2017-18. This is similar to the proportion recorded in 2000-01, when beef cattle prices were also historically high.

In 2017-18, the proportion of net income needed to fund interest payments is also projected to be historically low in the sheep industry at around 10 per cent. Farm cash incomes for sheep industry farms in 2017-18 are projected to be the highest recorded in more than 20 years.

For the dairy industry, the proportion of net farm income needed to fund interest payments increased very sharply in 2002-03, 2006-07 and 2012-13. Dry seasonal conditions and low milk prices resulted in very low net farm incomes in those years. In 2016-17, the proportion of net farm income needed to meet interest payments increased to 37 per cent for the dairy industry nationally. This is projected to decline to around 28 per cent in 2017-18 as a result of higher milk prices and increased milk production.

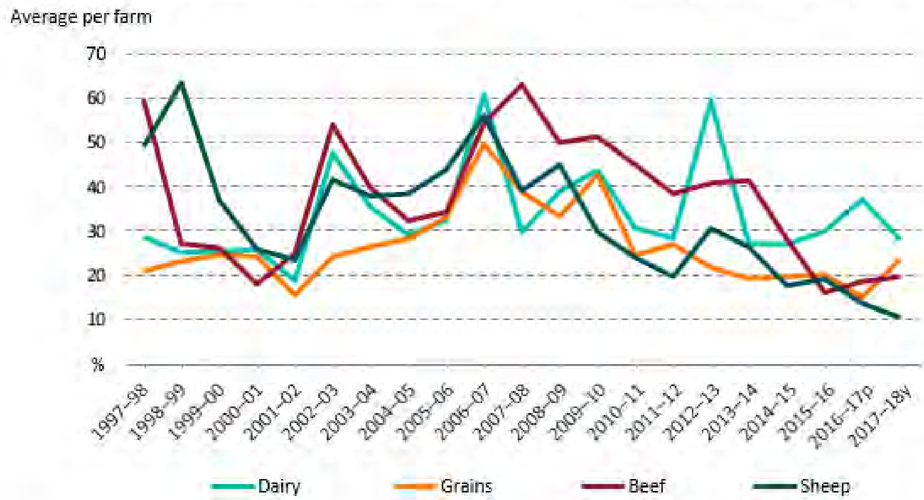
Figure 3: Ratio of interest payments to net income, Australian agriculture



Source: ABARES Agricultural Commodities March quarter 2018.

[7512488: 21721765_1]

Figure 4: Ratio of interest payments to net farm income for farms with debt, by industry, Australia



p Preliminary estimate. y Provisional estimate.
Source: ABARES Australian Agricultural and Grazing Industries Survey and Australian Dairy Industry Survey.

Loans and leases in arrears

APRA data collected for the department, while not yet finalised, provides some useful information on loans and leases in arrears in the agriculture sector:

- 945 farm business entities[9] across Australia had loans more than 90 days past due at 30 June 2017.
  - This was 0.65 per cent of farm business entities with borrowings.
- The total value of loans more than 90 days past due at 30 June 2017 was $630 million.
  - This was 0.90 per cent of the total value of loans.
- By industry, the proportion of the total value of loans more than 90 days past due at 30 June 2017 was highest for grape growing (4.7 per cent nationally), vegetable growing (2.9 per cent nationally) and dairy farming (1.5 per cent nationally).
- Of the total value of loans to grape growers in New South Wales and South Australia, 7.8 per cent and 7.1 per cent (respectively) was more than 90 days past due.
- Of the total value of loans to vegetable growers in Western Australia, New South Wales and Tasmania, 6.9 per cent, 6.5 per cent and 6.0 per cent (respectively) was more than 90 days past due.

[9] Effectively 'borrowers'

- Of the total value of loans to dairy farmers in South Australia, Tasmania and Queensland, 4.6 per cent, 3.5 per cent, and 3.3 per cent (respectively) was more than 90 days past due.
- By state, the proportion of the total value of loans more than 90 days past due at 30 June 2017 was lowest in the Northern Territory (zero) and highest in Tasmania at 3.1 per cent, followed by Western Australia and South Australia at 1.1 per cent.
- For Tasmania, 5.6 per cent the total value of loans to grain growing and mixed livestock- grains farms was more than 90 days past due at 30 June 2017.

While detailed time-series data is not available on arrears, previous ABARES publications[10] indicate nationwide, as at 30 June 2013, 3 per cent of the total value of agriculture, fisheries and forestry sector debt was more than 90 days in arrears. This compared to approximately 2 per cent of the total value of all other business sector debt.

Farm debt mediations and foreclosures

APRA data collected for the department, while not yet finalised, also provides some useful information on farm debt mediations and foreclosures in the agriculture sector:

- Nationally, there were 96 farm debt mediations and 33 foreclosures in the 2016-17 financial year.
- New foreclosures in 2016-17 accounted for 0.06 per cent of business entities with borrowings in Tasmania, 0.40 per cent in Western Australia, 0.03 per cent in New South Wales, 0.02 per cent in Victoria and Queensland, and 0.01 per cent in South Australia. There were no new foreclosures in the Northern Territory.
- Average credit outstanding per business entity for new foreclosures in 2016-17 was $1.9 million.
- Total credit outstanding on new foreclosures in 2016-17 was $62 million, or 0.09 per cent of aggregate ADIs and RFCs credit at 30 June 2017.
- New foreclosures in 2016-17 accounted for 0.27 per cent of total ADIs and RFCs credit in Tasmania, 0.16 per cent in Victoria, 0.13 per cent in Queensland, 0.10 per cent in Western Australia and 0.01 per cent in New South Wales and South Australia.
- New South Wales and Victoria had the highest proportion of business entities entering farm debt mediation in 2016-17. In both states, 0.09 per cent of business entities with borrowing entered farm debt mediation.

[10] ABARES 2014, *Regional farm debt: northern Queensland gulf, south west Queensland and north west New South Wales,* Canberra, December 2014. Available at: www.agriculture.gov.au/abares/display?url=http://143.188.17.20/anrdl/DAFFService/display.php?fid=pb_rfmd td9aasf20141203.xml

While detailed time-series data is not available on foreclosures and farm debt mediations, previous ABARES publications[11] provide some relevant statistics for drought-affected areas of Queensland and New South Wales. Further statistics are also available from those state and territory governments operating either mandatory (Victoria, New South Wales and Queensland) or voluntary (Western Australia and South Australia) farm debt mediation schemes.

<u>Rural Financial Counselling Service (RFCS) data</u>

The Rural Financial Counselling Service (RFCS), discussed further below, is another useful source of qualitative and quantitative information on debt-related matters.[12] The department understands a number of RFCS service providers have already provided information to the Royal Commission.

The RFCS is funded by the Australian, state and Northern Territory Governments, and provides free financial counselling to farmers, fishing enterprises, forestry growers and harvesters, and small, related businesses across Australia who are suffering financial hardship.[13]

RFCS service providers give information to the department on the main activities they undertake when meeting with a client, which can include support with asset management processes and farm debt mediations.

Rural financial counsellors provided some anecdotal information about their farm debt mediation work with clients as part of the feedback provided to the New South Wales Government for the review of its *Farm Debt Mediation Act 1994 (NSW)*. This feedback indicated:

- The process of farm debt mediation, particularly through legislated processes, is valuable and preferable to rapid foreclosure decisions.
- Financial institutions operate within the intent of existing farm debt mediation legislation.

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[11] ABARES 2014, Regional farm debt: northern Queensland gulf, south west Queensland and north west New South Wales, Canberra, December 2014. Available at: <u>www.agriculture.gov.au/abares/display?url=http://143.188.17.20/anrdl/DAFFService/display.php?fid=pb_rfmd td9aasf20141203.xml</u>

[12] It should be noted the RFCS program is only available to farmers, fishing enterprises, forestry growers and harvesters, and small, related businesses in hardship; this means RFCS information may not reflect the situation for the broader population of these business types.

[13] A rural financial counsellor is not permitted to provide family, emotional or social counselling or financial advice, rather it can provide a referral service, allowing clients to obtain professional information and service.

- There could be improvements to the farm debt mediation process, particularly when considering legal aspects:
  - The days of farmers negotiating 'in good faith' with their local bank representative have lapsed. In some instances, banks appear to outsource their credit/control and direct recovery to their legal representatives much earlier than previously.
  - While it is anticipated banks attend mediation with their legal representatives, there have been instances where the bank's legal representative has attended as their sole agent. This often places the farmer at a disadvantage, as they have to decide whether to get their own legal representation; this may be a difficult decision when they are already in severe financial difficulty.
  - Legal costs incurred by banks through the farm debt mediation process should, in the spirit of the legislated process, be borne by the banks, just as the farmer would be expected to meet any legal costs they incur in supporting themselves through farm debt mediation.

Current Australian Government programs

A number of frameworks govern the provision of assistance measures, including the Intergovernmental Agreement on National Drought Program Reform (IGA) and the Agricultural Competitiveness White Paper.

The IGA was agreed by Australian, state and territory ministers in May 2013, in recognition of Australia's history of drought events and the increasing likelihood of such conditions. The IGA implemented a new approach to drought policy, replacing Exceptional Circumstances arrangements, which relied on drought declarations and were only available in times of crisis. It has encouraged a shift away from providing reactive assistance based on climatic conditions, towards support available at all times to encourage preparedness and risk management. Australian Government measures under the IGA include a farm household support payment – the Farm Household Allowance (FHA) – and continued access to Farm Management Deposits (FMDs) and taxation measures, which are each discussed in further detail below.

Recently, the Australian, state and territory governments conducted a review of the IGA to assess its effectiveness. The review found there is broad support for the current IGA, and noted the shift away from in-drought assistance based on emergency circumstances, towards measures encouraging farm businesses to manage risk and prepare for future challenges, including drought. In response to the review, all primary industries ministers, at the 27 April 2018 Agriculture Ministers' Forum (AGMIN), agreed to an extension of the current IGA, which was due to expire on 30 June 2018, until a new agreement is finalised.

The Australian Government had also previously affirmed and strengthened its commitment to the IGA in the Agricultural Competitiveness White Paper. The Agricultural Competitiveness White Paper, released in 2015, had the aim of improving farm gate profitability, including through improved risk management. While improved farm gate profitability has positive flow-on effects on the ability of farmers to service their debts, the terms of reference for the White Paper specifically included an investigation into farm debt and access to finance.

A number of initiatives from the Agricultural Competitiveness White Paper have since been implemented to assist farmers with aspects of debt financing. These include the delivery of $2.5 billion over 10 years for concessional loans to help farmers access finances, and the removal of legislative impediments to FMDs being used as farm business loan offset accounts.

Concessional loans – to 30 June 2018

The department, through arrangements with the relevant state and territory governments, has delivered six different concessional loans products to date, which have provided farm businesses with temporary assistance through financial difficulty: Farm Finance, Drought, Drought Recovery, Dairy Recovery, Drought Assistance and Business Improvement loans.

Loans are administered on behalf of the Australian Government by state and Northern Territory government delivery agencies. The interest rate for these concessional loans products is reviewed every six months, with changes effective on 1 February and 1 August if applicable. The state and territory delivery agencies are made aware of any interest rates changes 30 business days prior to them taking effect so loan recipients can be provided with sufficient notice of these changes.

In applying for these loans, farm businesses must be able to demonstrate a capacity to repay the loan and return to commercial viability in the longer-term. Loan amounts are capped at 50 per cent of the farm business' eligible debt (up to a maximum of $1 million) to maintain the farm business' relationship with its commercial lender(s). At the end of the loan term, the total loan amount must be either repaid in full or refinanced with a commercial lender.

Loan recipients will be able to apply to refinance their existing loan(s) through the Regional Investment Corporation (RIC) (discussed further below), however the parameters and eligibility criteria for loans delivered by the RIC may differ.

Farm Finance Concessional Loans

The Farm Finance Concessional Loans (available under the Farm Finance Concessional Loans Scheme) closed for applications on 30 June 2015. Loans were available for five-year terms to farm businesses experiencing debt servicing difficulties but were assessed as commercially viable in the longer-term.

Eligibility for the loans was not contingent on a particular reason for hardship. The type of loans available (debt restructuring and/or productivity enhancement activities), value and terms were tailored to meet the farm business needs in each participating jurisdiction.

The interest rate is currently 3.51 per cent (effective 1 February 2018).

As at 30 April 2018, 409 farm businesses had been approved for Farm Finance Concessional Loans valued at $196.175 million.

Eligible farm businesses experiencing hardship due to drought could apply to transfer their Farm Finance Concessional Loan to a Drought Concessional Loan.

The five-year loan term for the first of the Farm Finance Concessional Loans will expire during the 2018-19 financial year.

Drought Concessional Loans

The Drought Concessional Loans (available under the Drought Concessional Loans Scheme) closed for applications (in all jurisdictions except Western Australia) on 31 October 2016. The scheme was extended in Western Australia and closed for applications on 30 June 2017. The loans were available to farm businesses in need of financial assistance due to the impacts of drought.

- For the purposes of the scheme, a drought was defined as a rainfall deficiency equivalent to, or worse than, either a 1 in 10 or a 1 in 20 year or worse rainfall event for at least 12 months in the previous 24 months.
- Applicants could assess their eligibility to apply for a loan by using the Bureau of Meteorology's Australian Rainfall Deficiency Analyser[14], to confirm whether they fell within an area covered by a 1 in 10 or a 1 in 20 year or worse rainfall event.

Applicants were required to demonstrate they had taken reasonable steps to prepare for the effects of drought; their farm business had sound prospects for a return to commercial viability; they had the ability to service the loan; they could provide adequate security; and their commercial lender agreed to the proposed arrangements for the concessional loan.

Loans were available for debt restructuring; operating expenses; and drought recovery and preparedness activities.

The interest rate is currently 3.01 per cent (effective 1 February 2018).

As at 30 April 2018, 508 farm businesses had been approved for Drought Concessional Loans valued at $296.669 million.

Drought Recovery Concessional Loans

Drought Recovery Concessional Loans (available under the Drought Recovery Concessional Loans Scheme and the Drought Recovery and Dairy Recovery Concessional Loans Scheme) closed for applications on 31 October 2016. The Drought Recovery Concessional Loans assisted farmers to, where seasonal conditions allowed, commence eligible replanting and/or restocking activities.

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[14] The Analyser was developed specifically to support the delivery of drought-specific concessional loans schemes and is available at www.bom.gov.au/climate/ada.

Loans were available to farm businesses experiencing equivalent or worse than a 1 in 50 year or 1 in 100 year rainfall event.

- Applicants could assess their eligibility to apply for a loan by using the Bureau of Meteorology's Australian Rainfall Deficiency Analyser to confirm whether they fell within an area covered by a 1 in 50 or a 1 in 100 year or worse rainfall event.
- In Queensland, farm businesses involved in the direct consignment of live cattle to the export trade to Indonesia experiencing a 1 in 10 or a 1 in 20 year rainfall event were also eligible to apply.

Applicants also had to demonstrate their farm business had taken reasonable steps to prepare for the effects of drought and they had the support of their current commercial lender(s).

The interest rate is currently 2.69 per cent (effective 1 February 2018).

As at 30 April 2018, 101 farm businesses had been approved for Drought Recovery Concessional Loans valued at $43.525 million.

Dairy Recovery Concessional Loans

Dairy Recovery Concessional Loans were initially made available through the 2015-16 Dairy Recovery Concessional Loans Scheme and have continued to be made available through the 2016-17 and 2017- 18 Farm Business Concessional Loans Scheme. They are currently open for applications until 30 June 2018.

Dairy Recovery Concessional Loans are available to eligible suppliers of Murray Goulburn, Fonterra and National Dairy Products, in Victoria, New South Wales, South Australia and Tasmania. These loans recognise the May 2016 decisions by Murray Goulburn, Fonterra and National Dairy Products to reduce the farm gate price of milk had a severe impact on some dairy farm businesses.

Loans are available for a maximum of $1 million, with conditions applying, for the purposes of debt restructuring, new debt for operating expenses or productivity enhancement activities, or a combination of these.

The interest rate is 2.69 per cent for loans approved under the 2015-16 application period (as at 1 February 2018) and 3.09 per cent for loans approved under the 2016-17 and 2017-18 application periods.

As at 30 April 2018, 310 farm businesses had been approved for Dairy Recovery Concessional Loans valued at $178.618 million.

Drought Assistance Concessional Loans

Drought Assistance Concessional Loans are offered under the Farm Business Concessional Loans Scheme, which is currently open for applications until 30 June 2018. These loans assist eligible farm businesses in need of financial assistance to manage, recover from and prepare for droughts and maintain prospects for long-term commercial viability.

Loans are for a maximum of $1 million, with conditions applying, for the purposes of debt restructuring, new debt for operating expenses, drought preparedness activities or drought recovery activities, or a combination of these.

The interest rate is currently 3.09 per cent (effective 1 February 2018).

As at 30 April 2018, 187 farm businesses have been approved for Drought Assistance Concessional Loans valued at $113.517 million.

Business Improvement Concessional Loans

Business Improvement Concessional Loans are offered under the 2017-18 Farm Business Concessional Loans Scheme, which is currently open for applications until 30 June 2018. These loans are available to commercially viable farm businesses that have exhausted their full 1,095-day FHA entitlement (discussed below), on or before 30 June 2018. These loans recognise that, while a current or ex-FHA recipient was by definition in financial hardship, if a farmer has improved their financial circumstances, then the farm business may benefit from being able to reduce its interest payments by restructuring and refinancing existing loans.

Loans are for a maximum of $1 million, with conditions applying, for the purposes of debt restructuring only.

The interest rate is currently 3.09 per cent (effective 1 February 2018).

As at 30 April 2018, 12 farm businesses have been approved for Business Improvement Concessional Loans valued at $5.89 million.

Farm Management Deposits (FMD) Scheme

The FMD Scheme is a financial risk management tool for primary producers to help smooth the uneven income streams common in agriculture due to climatic and market variability.

The scheme commenced in 1999, replacing the earlier Income Equalisation Deposits Scheme, which commenced in 1976, and the Farm Management Bond Scheme, which commenced in 1992 and operated in parallel with the Income Equalisation Deposits Scheme until the introduction of the FMD Scheme.

The scheme encourages individual primary producers to set aside pre-tax income in good years to build up cash reserves for use in low-income years.

Deposits are tax deductible in the financial year they are made, and form part of the primary producer's taxable income in the financial year they are withdrawn.

To hold an FMD a person must:

- be an individual[15] carrying on a primary production business in Australia at the time of making a deposit
- not earn more than $100,000 in non-primary production income in the year of deposit

[15] Companies and trusts are not eligible to hold FMDs. However, individuals who are trust beneficiaries may be able to access the scheme.

- deposit only primary production income in their FMDs[16]
- not hold more than $800,000 as FMDs at any given time
- make a minimum deposit of at least $1,000
- generally hold the deposit for at least 12 months to receive the tax benefit, and
- claim a tax deduction in a financial year not exceeding their taxable income from the primary production business for that financial year.

As at 30 April 2017, $5.17 billion was in held in more than 49,330 FMD accounts across the country.[17]

The department and the Treasury continue to co-manage the FMD scheme and assess what changes are needed to improve it on an ongoing basis.

- The department has policy ownership of the scheme, while the Treasury has legislative responsibility. The scheme is delivered by the Australian Taxation Office through the tax system.

The Agricultural Competitiveness White Paper brought about the most recent changes to the scheme, which were implemented from 1 July 2016:

- The deposit limit was increased from $400,000 to $800,000. This allows more flexibility for farming enterprises to manage income fluctuations by setting aside funds for low income years.
- An 'early access in drought' provision was reintroduced, allowing farmers in drought to withdraw their FMDs within 12 months of deposit without losing their claimed taxation benefits.
  - This is similar to a provision previously available under the Exceptional Circumstances arrangements that ceased on 30 June 2014, which was used to trigger the availability of early access.
  - A similar provision also exists for primary producers who receive primary production Category C assistance under the Natural Disaster Relief and Recovery Arrangements following a natural disaster.[18]
- Allowing FMDs to be used to offset the costs of their primary production business borrowings, reducing the interest payable on business debt and improving primary producers' net cash positions.

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[16] This can include income a beneficiary receives from a primary production trust.
[17] Detailed statistics, including holdings by state/territory and industry are available at www.agriculture.gov.au/ag-farm-food/drought/assistance/fmd/statistics.
[18] Primary producers who withdraw their FMDs early under either the drought or natural disaster exemptions cannot deposit any more FMDs in the same financial year.

Other taxation measures

The government provides a range of other taxation concessions, rebates and offsets to assist with farmers' bottom lines, which has flow-on effects to their ability to access and service debts.

The 2018-19 Federal Budget extended access to the $20,000 instant asset write-off for small businesses with turnovers up to $10 million for a further 12 months until 30 June 2019. As the majority of farms operate as small businesses, this will allow more opportunities for investment and replacing or upgrading assets.

This is in addition to the instant write-off on water infrastructure and fences and the three-year write-off of fodder storage, which help farmers to build their drought resilience and profitability.

Rural Financial Counselling Service (RFCS)

The RFCS program has been in existence in several forms since 1986. It was originally created in response to increased financial difficulties across the farming sector due to high interest rates, the deregulation of the financial sector, drought and depressed commodity prices.

It was initially intended as a short-term measure, however, it is now an ongoing service, forming part of the Australian Government's overall assistance measures for regional Australia, particularly those facing prolonged drought.

The RFCS is delivered as a grants program, with some co-funding from states and the Northern Territory. Grants are awarded to incorporated entities to deliver the services and they employ boards of directors, executive officers, administrative staff and rural financial counsellors.

While the delivery model has changed over time, the main objective has been to provide free financial counselling services to farmers, fishing enterprise operators and small, related businesses suffering financial hardship who have no alternative sources of impartial assistance to manage the challenges of change and adjustment.

Services include:

- building an accurate view of at least three years of business financials
- guiding clients to build a sound business planning framework into their operations
- immediate help with preparing for meetings with lenders, succession planners, accountants, and farm debt mediators
- Assisting eligible clients to apply for FHA and other forms of assistance, and
- Providing referrals to agricultural advisors and social and emotional support networks.

Around 4,500 clients across the country seek assistance from the RFCS each year, and around 3,000 Australians are using the service at any point in time. Of clients that have left the program, 75 per cent said the RFCS had helped improve their business skills and/or financial situation.

The Farm Household Allowance (FHA)

The FHA is a time-limited income support program helping farmers in hardship make decisions about the future of their farm businesses and to take action to support themselves. It was introduced on 1 July 2014 and provides up to three cumulative years of assistance per recipient.

Applicants must meet income and asset tests to be eligible for payment. Net farm assets must be under $2.55 million, and off-farm assets (including cash) must be below $380,500 (for homeowners who are partnered – around 80 per cent of recipients). The same supplementary allowances applying to other social security allowances are also paid where applicable: pharmaceutical allowance, rent assistance, remote area allowance, and telephone allowance. A health care card is automatically issued, and recipients over 60 years of age with nine months of continuous payment receive a pension concession card.

Unlike other social security payments, recipients estimate their business income for the coming 12 months and this is taken into account when their fortnightly payments are made. Other
non-business income is declared each fortnight and is combined with the estimated business income. Recipients can change their estimate at any time and as frequently as needed. At the end of the financial year, in line with the lodgement of their income tax return, their actual income is reconciled against the estimate.

While the FHA is limited to three cumulative years for each recipient, support is given to help recipients make business decisions and plan and implement changes for their future. These plans are captured in a Financial Improvement Agreement, which recipients develop and report against through at least 13 one-on-one meetings with a Farm Household Case Officer from the Department of Human Services. In addition, recipients can access up to $4,000 in activity supplements for planning and training ($3,000 on claim and $1,000 for the third year).

Since the program commenced, as at 29 April 2018, over 7,900 farmers and farmers' partners have benefited from the FHA.

Clean Energy Finance Corporation (CEFC)

In supporting a government election commitment, the department works with the Clean Energy Finance Corporation (CEFC) to enhance the agriculture sector's access to CEFC finance. In particular, the department is encouraging further investment of CEFC finance in the agriculture sector for energy efficiency, renewable energy and low emissions projects.

The CEFC provides finance for energy efficiency, renewable energy and low emissions projects. CEFC investment provides an opportunity for farmers and agribusinesses to reduce their energy costs and improve their productivity through the use of discounted and tailored finance, to invest in energy efficient equipment and renewable energy upgrades.

The CEFC directly invests in large projects (typically loans larger than $5 million) and, for smaller projects (loans up to $5 million), it partners with Australia's major banks to allow eligible farmers to access discounted and tailored finance arrangements.

The CEFC, through the ANZ, Commonwealth Bank, NAB and Westpac, provides loans to undertake on-farm projects such as purchasing new farm vehicles, production equipment, irrigation pumps and systems, and solar power and/or other renewable power generation.

The department works with the CEFC and encourages agribusinesses to either talk to the CEFC directly for large (greater than $5 million) projects, or to work through their existing banks for smaller (less than $5 million) projects. The department does not interact directly with the banks in supporting this election commitment.

Emissions Reduction Fund (ERF)

The department maintains an active interest in the Emissions Reduction Fund (ERF) (within the portfolio responsibilities of the Department of the Environment and Energy) as it provides farms with alternative or additional income streams.

The ERF is a voluntary scheme providing ongoing opportunities for farmers and land managers to participate in emissions reduction and carbon sequestration (capture and storage of carbon) projects. Under the scheme, landowners and farmers who adopt approved ERF methods can earn Australian Carbon Credit Units, which can be sold to provide alternative or additional income streams while benefitting the environment.

Other portfolio involvement in recent debt and banking issues

Farm Debt Mediation (FDM)

The government continues to work with the states and territories on implementing nationally consistent and transparent FDM processes to resolve farm debt disputes between creditors and farmers before enforcement actions are undertaken.

At a meeting of the Agricultural Finance Forum on 26 September 2014, the former Minister for Agriculture, the Hon. Barnaby Joyce MP, confirmed his commitment to the development of a nationally consistent FDM scheme.

The need for a nationally consistent FDM scheme was considered by the Parliamentary Joint Committee on Corporations and Financial Services' May 2016 report on its *Inquiry into the Impairment of Customer Loans.*

The 3 February 2017 release of the Australian Small Business and Family Enterprise Ombudsman report on its *Inquiry into Small Business Loans*, which was produced as a result of the Parliamentary Joint Committee on Corporations and Financial Services' *Inquiry into the Impairment of Customer Loans*, also recommended a nationally consistent approach to FDM.

State/territory government methods of providing FDM vary, from providing no formal FDM processes, to voluntary or compulsory FDM, with either subsidised or non-subsidised approaches.

Currently, New South Wales and Queensland offer legislated non-subsidised FDM approaches, while Victoria provides a legislated subsidised FDM scheme. ABARES data indicates the combined legislation of these three states covers approximately 77 per cent of Australia's farm businesses.

New South Wales recently completed a review of its legislation. Amendments to the New South Wales Government *Farm Debt Mediation Act 1994 (*Farm Debt Mediation Amendment Bill 2018) passed both houses of Parliament on 3 May 2018.[19]

The Victorian Government is currently finalising a broader review of its legislation and the operation of its scheme.

South Australia has a voluntary scheme, used in conjunction with the Fair Trading (Farming Industry Dispute Resolution Code) Regulations 2013. The Marshall Government, appointed on 19 March 2018, committed to introduce an FDM Bill into Parliament within its first 100 days of governing. This would bring the total number of farm businesses covered by a legislated scheme to 87 per cent.

In July 2017, the Western Australian Government completed a 2-year voluntary pilot FDM scheme. A recent review of the scheme found a voluntary system (covering 9 per cent of Australian farm businesses) was preferred.

Tasmania (3 per cent of farm businesses), the Northern Territory and the Australian Capital Territory (both less than 1 per cent) have no formal FMD mechanisms in place. The Australian Capital Territory has not committed to legislated FDM due to its low number of primary producers, however, it does not consider this should prevent other jurisdictions from implementing legislated schemes.

The Australian Government's preferred model for achieving a nationally consistent approach to FDM is through the harmonisation of legislation across the country and its implementation at the state/territory level. Having the states/territories implement their own legislation has advantages, including flexibility to select delivery agencies and whether it is appropriate to subsidise mediations.

At the April 2018 Agriculture Senior Officials' (AGSOC) meeting, officials from the majority of jurisdictions indicated they were continuing to work towards a harmonised approach to FDM.

At the latest Agricultural Ministers' Forum (AGMIN) meeting on 27 April 2018, Ministers agreed to continue working towards nationally harmonised FDM by re-committing to a set of standard principles and exploring how to best implement these, such as through an intergovernmental agreement, noting this facilitates both voluntary and legislated approaches.

Ministers also noted recent developments at the Commonwealth level in banking and dispute resolution, including the establishment of the Australian Financial Complaints Authority (AFCA) and this Royal Commission.

At the same meeting, the Western Australian Minister advised a set of principles for a harmonised approach was supported. The New South Wales Minister noted changes to the New South Wales legislation had been finalised and the amended act could be used as a model by other jurisdictions to implement new, or amend existing, FDM schemes.

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[19] Details on the amendments are available at www.raa.nsw.gov.au/fdm/2018-amendments.

Forthcoming Australian Government Initiatives

Regional Investment Corporation (RIC) – from 1 July 2018

In June 2016, the Australian Government committed to establish the Regional Investment Corporation (RIC) to be the national administrator for up to $2 billion in Commonwealth farm business concessional loans and the $2 billion National Water Infrastructure Loan Facility (NWILF).

The RIC will consolidate loans expertise within the portfolio and streamline the administration of farm business loan arrangements to ensure they are delivered in a nationally consistent and efficient manner, as well as providing loans to state and territory governments for the construction of nationally significant water infrastructure.

A new farm business concessional loans program will be available through the RIC. Under the new arrangement, more Australian farm businesses will be eligible for a concessional loan and they will have more flexibility on how they use their loan. The new loans will support farm businesses solely or mainly supplying, or intending to solely or mainly supply, products into interstate or international supply chains. The RIC will also continue to provide concessional loans to help farm businesses prepare for, manage through and recover from periods of drought.

The RIC will also administer the NWILF. State and territory governments can apply for concessional loans to co-fund the construction of water infrastructure. This funding will accelerate the construction of major water infrastructure projects such as dams, weirs, pipelines and manage aquifer recharge projects.

Legislation to establish the RIC (as a corporate Commonwealth entity within the Agriculture and Water Resources portfolio), its functions and governance arrangements, passed through Parliament on 6 February 2018. The RIC is not a deposit-taking institution and therefore is not subject to banking regulations.

The RIC will be operational from 1 July 2018. An independent Board has already been appointed for the RIC. It is responsible for finalising establishment of the RIC, including the program guidelines for the RIC's new farm business concessional loans. The experienced Board includes Mr David Foster as Chair, Ms Lucia Cade, Mr Mark Lewis and Ms Prue Bondfield. They have combined backgrounds covering the financial sector, water infrastructure and agribusiness.

The RIC Board will be engaging with stakeholders as soon as practical, to discuss the RIC's functions and loan offerings.

Attachment A

Agricultural Lending Data Collection - History

At the Agricultural Finance Forum meeting in September 2014, the Australian Bankers' Association (ABA), on behalf of its member banks, agreed to investigate the more systematic collection of agribusiness lending and debt data. As part of this commitment, the ABA, in conjunction with the National Farmers' Federation, the Northern Gulf Cattlemen's Association and ABARES, undertook a trial data collection process on debt levels and serviceability for specific regions of Queensland and New South Wales. This information was published by ABARES on 4 December 2014.[20]

On 28 March 2017, APRA released a formal consultation package to ADIs, RFCs and other agricultural and financial stakeholders, proposing APRA would collect the following data from ADIs and RFCs on behalf of the department:

- total loan facilities and outstandings by state/territory and agricultural activity
- number of, and outstanding balances on, loans more than 90-days in arrears by state/territory and agricultural activity
- number of instances of FDM and foreclosures.

As part of the consultation process, ADIs and RFCs were asked to voluntarily provide the data outlined above for the 30 June 2016 reporting period.

The government, through the Treasury portfolio, has made amendments to the *Financial Sector (Collection of Data) Regulations 2008* and the *Australian Prudential Regulation Authority Regulations 1998* to list the department as an agency with which APRA can share the data it has collected on its behalf.

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[20] ABARES 2014, Regional farm debt: northern Queensland gulf, south west Queensland and north west New South Wales, Canberra, December 2014. Available at: www.agriculture.gov.au/abares/display?url=http://143.188.17.20/anrdl/DAFFService/display.php?fid=pb_rfmd td9aasf20141203.xml