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Forum

Country Towns and Fluctuating Rural Fortunes - Is There a Case For Assistance ?

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This paper provides a review of some commonly held arguments for extending government assistance to the non-farm rural business sector as a means of maintaining the infrastructure of agriculture through periods of rural downturn. Recent literature on the nature of linkages between the farm sector and small business is reviewed to identify the scale of exposure of the various types of small business. Assistance measures available to the farm sector are compared to those available to small business and differences between the two groups are discussed. It is concluded that the disparity in tax treatment between the farm and non-farm rural business sector is an important focus for policy reform and that assistance to the non-farm rural business sector should encourage the development of appropriate small business structures and risk management techniques.

1. Agricultural Adjustment and Assistance Considerations

Rural downturns, whether the result of drought or market collapse, bring into focus the vulnerability of small businesses in country towns to the fluctuating fortunes of the farm sector. They highlight the often close linkages that exist between farms and businesses that supply their inputs and those that handle and process their outputs. Although fluctuating farm incomes translate to small business in varying degrees, this linkage has often been the basis of arguments for government assistance to be extended to the small business sector. This was recognised by the Drought Policy Review Taskforce (McInnes 1990, Vol.2, p.181), where it was stated that "non-farm rural businesses face many of the difficulties experienced by primary producers when periods of climate stress or other economic downturns affect rural communities."

In recent decades Australian agriculture has adjusted to its declining terms of trade in various ways. One of the key trends has been a steady increase in the productivity of farm capital and studies suggest that technological advance in Australian agriculture has tended to save both labour

and capital, but the effect has been much greater on labour (Lewis, Martin and Savage 1988). In relation to farm adjustment in Australia, Bain (1987, p.8) said "there have been major economic and structural changes, with increases in the size of farms, sharply falling employment and a centralisation of activities into major rural towns and a decline over time of the relative importance in the economy of communities dependent on agricultural industries."

He went on to say (p.9),

"a consequence of a long term decline in the importance of agriculture is that the economies of regional communities providing services to agricultural industries will not only diminish in relative importance but will also change in nature. There will be some growth in the provision of inputs as farmers substitute these for labour. Also, there is likely to be a change in the provision of consumption goods. Existence of substantial economies of size in the provision of many services and progressively fewer people employed in rural agriculture imply that there will be a secular reduction in the number of rural centres servicing agriculture."

The relevance of these trends is that they need to be kept in mind in any consideration of new policy measures that may effect resource adjustment in rural areas. Policies, that through the use of short term incentives, attempt to artificially slow the movement of resources from rural towns and regions, or attempt to attract resources to a region, run

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the risk of producing only short term localised benefits at the expense of the broader community. They may also exacerbate structural adjustment problems in future periods.

Alternatively, policies that facilitate adjustment within rural communities, such as programs designed to improve small business skills and the removal of regulatory impediments to adjustment, are more likely to result in longer term efficiency gains being realised.

1.1 Arguments for extending assistance to non-farm rural businesses

Two arguments are often put forward as grounds for government assistance to be extended to non-farm rural businesses. The first is that small business incomes fluctuate in parallel with those in the farm sector, due to the close linkages that exist between the two groups, yet assistance made available to farmers on the basis of their fluctuating incomes is not also made available to small business. Some relevant measures here include financial assistance available through the Rural Adjustment Scheme and State drought relief arrangements and income smoothing assistance provided through the income equalisation deposits scheme (IED's) and tax averaging. On this point, the Planning Research Centre (1989) surmised that as a generalisation, the farming community had more stabilising strategies available to them to offset income variability than did non-farm rural businesses. These include the ability to change enterprises and to earn off-farm income to reduce risk associated with variable farm incomes. For service industries, changes in enterprise will require learning new skills, establishing a new client base and reputation and new capital investment.

In response to the alleged disparity in assistance between the two groups, an important point to note is that intuitively it would be expected that assistance to the farm sector should, through the multiplier effect, flow on to the relevant sections of the small business community. A difficulty for non-farm rural businesses and an uncertainty of the argument is the length of time it takes for this flow-on to occur. The lags involved are likely to vary in line with the nature of assistance. Direct grants and

concessional finance, for example, might flow more quickly from the farm sector to small business than the effect of income smoothing. A result of this flow-on effect is that additional financial assistance targeted at non-farm rural businesses could represent a duplication of assistance at the small business level.

In recognition of the 'assistance multiplier effect', the Drought Policy Review Taskforce (McInnes 1990, Vol.2, p.181) noted that "the traditional approach to maintaining the economic health of small business in rural communities has been to attend to the needs of primary producers", however, the report concluded that the approach was likely to be insufficient in meeting the needs of non-farm rural businesses.

The Task Force recommended that the feasibility of extending tax averaging and income smoothing to non-farm rural businesses through the IED scheme be reviewed and that state and territory governments determine the benefits and feasibility of regionally based industry adjustment arrangements. The former recommendation was also an outcome of the recent Beddall Inquiry into small business (Beddall 1990).

A second point in relation to the 'equal treatment' argument, is that much assistance to agriculture has been based on political expediency, rather than economic rationality, and various forms of assistance to farmers owe their presence to agricultural fundamentalist attitudes and distorted views about when government assistance is justified. For example, McInnes (1990, Vol.2, p.86) states that producers "interpret uncertainty and the risks involved in managing market and climatic conditions as a sign of market failure".

The extension to small business of some forms of financial assistance will, therefore, to varying degrees, duplicate assistance already provided to farmers which flows on to the non-farm rural business sector. In addition, such measures would further compound existing inefficiencies associated with farm assistance. In particular, extension of grants, concessional finance and interest rate subsidies in times of hardship would stifle greater self-reliance by the non-farm rural business sector. There may,

however, be a case for better targeted assistance in the form of government sponsored programs aimed at improving small business management skills and business structures. This form of assistance would facilitate adjustment and encourage greater emphasis on a contingency approach to small business management. There may also be a case for extending income smoothing assistance to non-farm rural businesses. The difficulty with this option would be the definitional problem of determining when a business can be defined as being rural. These points are expanded upon in the following sections.

A second argument put forward for extending assistance to non-farm rural businesses recognises the long term adjustment trends of agriculture, but proposes there is a case for short term government assistance in times of rural downturn. The basis of the argument is that the cost of resources adjusting out of a regional community will be greater than the cost of government assistance required to retain these resources. The often cited example is the adverse impact that declining populations have on the provision of community services such as health care and education.

The argument implies imperfections in the capital market and fails to recognise additional costs in the form of resource use distortions that are likely to be associated with any short term assistance measures targeted at retaining non-farm rural businesses. In the absence of such assistance, for example, resources would be expected to flow to the more prosperous towns as a result of their natural comparative advantage, consistent with long term structural adjustment trends. Short term assistance would impede this process, as a cost would be imposed on the more prosperous centres in the form of reduced economic growth. Lower economic growth will in turn result in a reduced overall capacity to provide community services, thus undermining any welfare arguments put forward in support of short term assistance measures.

Calls for assistance to avoid diminution of public services in country areas also implies that resource planning by service authorities is in some way flawed. For example, the view that public authorities see short term downturns as opportunities to

contract services in a manner inconsistent with longer term population trends, is a common one. The problem, if it exists, is one of poorly based government intervention with the solution lying in improved community service planning and achieving greater transparency and reform of community service planning policies and processes. The introduction of an additional tier of government intervention, in the form of assistance to non-farm rural businesses to address this issue, would simply compound existing regulatory inefficiencies within rural communities.

Much of the regional demographics literature details the effects of long term structural change on the provision of services in rural communities (see Phillips 1974, Davidson 1976, Smailes 1979, Holmes 1984, Webb 1984, Bowie and Smailes 1988, Sorensen 1990), however there has been less research into the effects of exogenous shocks, such as drought or market collapse. The proposition that significant population reductions are associated with, or initiated by, short term rural downturns (see Walmsely and Sorensen 1988) is at odds with the conclusions of Bowie and Smailes (1988), that rural communities have become accustomed to periods of downturn and in many cases have maintained or increased their populations. They also point out that reduced asset values dampen the rate of adjustment during rural downturns. Another point worthy of mention is that there has been a significant uncoupling of local regional economies from the fortunes of agriculture (Stayner and Reeve 1990).

An overriding difficulty with any argument to expand assistance to the non-farm rural business sector is the problem of determining what small businesses should qualify for assistance given their varying levels of exposure to the farm sector. As revealed in the following section, our understanding of the linkages between the farm and non-farm rural business sectors of rural communities is not extensively developed. Existing studies have shown that the impact of drought and low agricultural commodity prices on small business varies, both spatially and intertemporally, depending on the mix of rural industries in a region and the presence of other activities such as tourism and mining.

Little is known about the impact of the farm sector's changed purchasing patterns during periods of rural downturn on suppliers of farm inputs and little is reported about the strategies adopted by the more dedicated farm input suppliers to offset their reduced incomes during these periods. The extent to which suppliers of farm inputs have developed their own strategies to cope with the fluctuating fortunes of the farm sector is an area worthy of closer scrutiny.

Extension of assistance to non-farm rural businesses for the purpose of surviving periods of short term rural downturn and avoiding any subsequent reduction in community services is therefore also difficult to justify. Such measures fail to recognise possible inefficiencies associated with existing community service arrangements and if implemented, would represent government intervention to overcome inefficiencies of government intervention elsewhere in rural communities. Furthermore, our understanding of the effects of short term rural downturns on non-farm rural businesses and the service infrastructure of rural communities, provides an insufficient basis for targeting assistance.

It may be the case that calls for assistance from the non-farm rural business sector during periods of rural downturn, source from businesses with more tenuous links to the farm sector and whose problems are more a function of longer term structural adjustment trends within these communities. The 'organic view' of country towns (see Sorensen 1990, p.46) may also be an important factor underpinning the more general calls for assistance.

2. The Rural Economy

2.1 Characteristics of small business in rural areas

Definitions of small business, though varied, agree that small businesses are normally independently owned and managed, they are closely controlled by owners/managers who also contribute most, if not all of the operating capital and owner/managers have principal decision making functions (Beddall 1990, p.9). Many definitions of small business, therefore, centre around management characteris-

tics. A more concise definition provided by Stayner (1985), is that small businesses are those where all management decisions are taken by one or two people without the assistance of internal specialists.

Johns, Dunlop and Sheehan (1989) highlight characteristics of small business, apart from ownership and management structure, that differentiate it from a large scale business such as type of employment, lower qualification requirements, less unionisation and lower pay rates. They also propose that the competitive advantage of most small businesses lies not in economies of scale but in the provision of good quality and design, prompt delivery, flexibility in meeting customer requirements and good after sales service.

Definitions such as these, however, fail to capture the dynamic dimension of small business and highlight our limited insight of key aspects of small business such as the extent of speculative market entry and exit, the extent to which profit levels in good times compensate those in bad times, keeping in mind that higher returns are usually associated with high risk businesses, and their degree of diversification. Consistent with this point the Beddall Inquiry found there was a lack of reliable and comprehensive data about small business which hampers investigation and research into problems specific to the sector.

2.2 Links between agriculture and non-farm rural businesses

Regional economies consist of both farm and non-farm activities (Planning Research Centre 1989). Powell (1978, p.74) summarised the main characteristics of rural economies in Australia, drawing on the work of Mandeville and Powell (1976), Jensen (1976) and Dickinson (1977). They were:

"Agriculture is the most important sector in the rural regional economy. This varies between regions, but dependence on the rural sector is far higher than is indicated by agricultures' 4 to 5 percent contribution to national GDP.

Within the rural regional economy the market for agricultural products is small and most agricultural production is exported from the region.

For most agricultural products produced in Australia, there is relatively little processing undertaken within the rural economies themselves.

Manufacturing industries, including the manufacture of agricultural inputs, is heavily concentrated in the main metropolitan centres. Thus, farm inputs are imported into the region with local firms providing the importing, distribution and service functions, only.

Apart from the higher rainfall coastal fringe and irrigation areas, there is a narrow range of agricultural production possibilities. Diversification is limited, so that the rural economy is dependent on the markets for a narrow range of commodities."

According to Powell (1978, p.75), implications that can be drawn from this type of rural economy are that "the exposure of a key sector to unstable world markets generates instability in the region which is added to the high risk of unfavourable growing conditions" and that "most non-agricultural activities are directed to servicing agriculture and because the agricultural sector imports most of the required material inputs and exports most of the output unprocessed, this instability in the agricultural sector is passed on to the rest of the economy."

Given these characteristics of the rural economy, country towns are likely to play a diminishing role in the agricultural production process and associated value adding activities. An important dimension of many country centres will therefore be a growing emphasis on supplying non-farm consumables, such as food, clothing, entertainment and other relatively low cost items.

The Planning Research Centre (1989) identified four major linkages between agriculture and the rural regional economy. They were the purchase of farm sector inputs from input suppliers, the processing and marketing of farm sector output, the purchase of consumer goods by the farm sector and the farm sector's contribution to the population of the region and its demand for population dependent activities. Stayner (1990) added that the farm sector provides labour to other employers in the region.

A number of factors have reduced the relative importance of the smaller, traditional agricultural service centres according to Stayner (1990). First,

there has been a long term trend in Australian agriculture for the substitution of capital inputs for labour inputs. In many cases, local value added has been limited to retail margins and a service component. Second, the increased complexity of capital goods has meant that local firms are less likely to be able to carry out servicing. This factor increases the importance of larger regional towns as agricultural service centres. Third, there has been a trend towards employing contract rather than permanent labour. Contract labour forces tend to be more transient, so a smaller share of the income they earn tends to be spent locally.

2.3 Factors influencing the reliance of non-farm rural businesses on agriculture

The economic downturn in agriculture has not occurred evenly throughout Australia as a result of differences between regions. Harrold and Powell (1987) concluded that the nature of the resource base of the region for other activities such as manufacturing, mining and tourism and the existence of government policies that influence the location of activities, particularly government services, were important in influencing the regional impact of rural downturns.

Powell and Saeed (1984, p.20) said that "variation in the ability of regions to cope with rural downturns arises due to enterprise differences in the agricultural sector among regions, from differences in the structure of the regional economy and from other factors such as location relative to major metropolitan centres". A study of small towns in Victoria by Henshall Hansen Associates (1988) cited rationalisation of Government services as a major factor contributing to increased reliance by country centres on agriculture.

3. Case Studies

A few case studies have been conducted which have shed some light on the effects of drought, rural recession and industry rationalisation on the prosperity of country towns.

Gregory (1984) reported on the experience of businesses in 20 Australian country towns from 1979 to 1983 to evaluate the impact of drought on town

prosperity. Surveys were conducted in 1983 in eight towns in New South Wales, four in Victoria, five in Queensland and three in Western Australia. Between 20 and 30 businesses were interviewed in towns with more than 4500 inhabitants and between 10 and 15 in smaller towns.

Results of the surveys showed that businesses that experienced the highest growth over this period were accountants, furniture stores, paint suppliers, solicitors and registered clubs. Least growth was experienced by white goods and electrical retailers, machinery and farm suppliers, corner stores, clothing retailers and garages.

A further result of the study was that 20 per cent of business proprietors interviewed were opposed to government assistance for non-farm rural businesses and 13 per cent were opposed to such support for farmers. The most common suggestion was that government should provide lower interest rates to drought affected businesses.

While noting that the effects of drought are felt differently by various business types within a town, Gregory suggested that the impacts of decreased demand for farm inputs on the manufacturer of these inputs needs to be examined further, as it may be these firms, rather than retailers, which merit assistance. This again brings into question the multiplier effect of assistance and the appropriate point in the production or supply chain at which it is best provided. It would seem that if assistance is to be provided, targeting it at the base level of the production process, or supply chain, would avoid duplication and extension of assistance to businesses not dependent on agriculture.

Stayner (1990) examined the effect increasing wool prices had on small towns, using Guyra as a case study. A survey was conducted of local graziers in November 1988. Farmers were questioned about recent expenditure patterns on a range of farm inputs. Information on reductions in farm debt and their amount of off-farm income was also obtained. Results showed that less than 30 per cent of the extra spending by graziers, resulting from high wool prices, flowed back to the local economy.

Stayner observed that for larger items of expendi-

ture, such as fencing, building materials and vehicles, farmers were more likely to shop around for the best price available. For more regular domestic purchases, they appeared to be less price conscious and shopped locally. This is consistent with the observation that the local farming community maintains a loyalty to the local town, but in the case of smaller towns, that loyalty is limited to regularly purchased convenience items. Expenditure on these items is less affected by fluctuations in farm incomes.

In drawing conclusions from the case study, Stayner stated that the mix, structure and prosperity of many non-farm businesses are heavily influenced by factors related to the non-local and non-agricultural economy and that changes in the terms of trade for agriculture have become less important determinants of their prosperity. The study highlights that only a minor proportion of expenditure by grazing properties is retained as value-added in small towns, and therefore, they are unlikely to be drastically effected by low commodity prices.

4. A Comparison of Assistance Measures Available to Farmers and Non-farm Rural Businesses in New South Wales

Government assistance measures available to farmers and non-farm rural businesses in New South Wales are summarised in Table 1 and expanded upon in Appendices A and B. While the differences in assistance arrangements that exist between the two groups are often highlighted by the non-farm rural business sector, these differences are not a sufficient basis for making additional assistance available to this group. Instead, they may highlight areas where assistance to farmers requires rationalisation, or they may simply reflect fundamental differences between the two groups which warrant different policy measures.

4.1 Differences in assistance between the two groups

From Table 1 it can be seen that the main differences in assistance between the farm sector and non-farm rural businesses are: non-farm rural busi-

nesses are excluded from much of the financial assistance available to farmers under the Rural Adjustment Scheme and State drought relief arrangements and non-farm rural businesses are excluded from the income equalisation deposit scheme and income averaging for tax purposes.

As already discussed, access to broad financial assistance measures such as those available under Parts A and B of the Rural Adjustment Scheme is difficult to justify due to the distortions to incentive structures that would result. Assistance for training, as is available under Part A, may be less distortionary. A problem with this provision, where farmers having long term viability are eligible for up to \$1000 a year for three years, is the difficulty of assessing viability and the associated administrative cost of doing so.

To the extent that welfare assistance, similar to that available to the farm sector under Part C (non-viables exiting the industry), is unavailable elsewhere to non-farm rural businesses, then there is an inconsistency in assistance arrangements.

Lack of access by non-farm rural businesses to income smoothing measures such as the IED Scheme and tax averaging is also difficult to justify. Although they were set up for primary producers, the basis of their introduction is equally valid for many small rural businesses with fluctuating rural incomes. Income averaging represents one of the main forms of assistance to agriculture (see Table 2) and in terms of potential benefits to non-farm rural businesses, this inconsistency is one of the most significant. The benefits to primary producers from income averaging and IED's are discussed further in the following section. In Appendix C various tax elections available to primary producers, that also have an income smoothing effect, are detailed.

4.2 Income smoothing

4.2.1 Income averaging for tax purposes

The tax system provides primary producers with various income smoothing measures that are not available to non-farm rural businesses. Averaging of incomes has been justified on the grounds that

with a progressive taxation system, taxpayers with fluctuating incomes will pay more tax over time than those with more stable incomes. If a fluctuating income represents sufficient basis for the introduction of averaging, then there seems little reason other than the administrative difficulties that might be involved, for not extending access to non-farm rural businesses.

Primary producers using the averaging system pay tax on their taxable income at the average tax rate applicable to their average income. If the averaging system results in a taxpayer paying less tax than is prescribed at the scheduled rates, the difference is called an average rebate. If more tax is paid than is prescribed, it is called complementary tax.

Typical marginal tax rates for primary producers in 1989 are shown in Table 3. These rates can be compared with the scheduled rates which apply in the absence of averaging, shown in Table 4. The rates in Table 4 are the same for non-farm rural businesses and are substantially higher.

From Table 5 it can be seen that averaging favours those on higher incomes, with a positive relationship existing between the amount of taxable income and the amount of the average rebate. This bias suggests that significant inequities may be present in the averaging system.

4.2.2 Income Equalisation Deposit Scheme

Income equalisation deposits are a tax linked scheme allowing primary producers to reduce fluctuations in farm incomes by depositing money with the Federal Government. The deposits are tax deductible. Withdrawals are included in assessable income. The Government pays interest on 61 per cent (the non-tax component) of the deposit at the short term bond rate. The 39 per cent of the deposit upon which interest is not paid is called the 'tax component', with 39 per cent being claimed to be a typical marginal rate of a depositor to the scheme. The reason why interest is not paid on the non-tax component is that it is claimed that this would have been paid in tax if the deposit had not been made.

Deposits in a year are restricted to the taxpayer's net primary production income for the year. The

Table 1. State and Federal Government Assistance to Agriculture and Small Business

Assistance to Agriculture	Assistance to Small Business
Rural Assistance Authority	
Provides assistance in the form of advances (under the special conservation scheme), low interest loans (under the disaster relief scheme), interest subsidy grants (under the rural adjustment scheme).	Can apply only under the disaster relief scheme.
Rural Counsellors	
Provide free financial advice to farm families. Prepare RAA application forms and loan applications. Present clients with a range of feasible options for the farm. Also funded by local communities.	Do not provide assistance to agribusiness.
Commonwealth Development Bank (CDB)	
Loans assessed on the likelihood of the success of the venture rather than the security offered.	Similar conditions apply to small and medium sized business as apply to agriculture.
Taxation	
Income Averaging, IED's and taxation concessions.	No special provisions.
Austrade	
Export Market Development Grants Scheme and the Innovative Agricultural Marketing Program provide taxable cash grants to eligible applicants.	Similar provisions apply.
NSW Agriculture	
Extensive advisory service dealing with livestock, crop, horticulture and farm management. Ongoing research programs in the above areas. Financial services provided by Farm Cheque. Administers drought relief measures.	Make use of forecasting information relating to demand for input supplies.
Consumer Affairs	
Provide information on licences and registration requirements.	Services available include: - advisory - financial - mediation - education and training - regional business development scheme. Provide information on licences and regulations.
Conservation and Land Management	
Provide advice on planning design and construction of farm water supplies, comment and advice on environmental impact statements and assistance to landholders in the formation of Landcare groups.	Not applicable.

Table 2. Assistance to Agriculture by Form: 1984-85 to 1987-88 (\$ millions)

	1984-85	1985-86	1986-87	1987-88
Assistance to outputs				
Domestic pricing arrangements	514.6	558.8	618.7	522.2
Export incentives	3.2	1.0	1.0	9.0
Export inspection services	29.2	40.2	47.8	27.0
Local content schemes	17.1	14.6	8.5	18.8
Marketing support	26.8	32.8	36.7	35.4
Underwriting arrangements	12.8	2.6	164.4	1.8
Tariffs	55.8	50.8	56.3	48.0
TOTAL	659.5	700.8	936.4	662.2
Assistance to value-adding factors				
Adjustment assistance	33.0	48.9	65.5	66.8
Agricultural research	95.1	101.3	120.2	127.8
Concessional credit	7.2	-	-	-
Income taxation concessions*	125.7	100.0	180.0	280.0
Natural disaster relief	42.9	37.7	38.7	41.8
TOTAL	303.9	287.9	404.4	516.4
Assistance to inputs				
Disease control	18.3	13.5	18.1	13.4
Fertiliser subsidies	52.0	51.7	-	-
Tariffs on materials	-185.1	-157.7	-136.8	-162.4
Tariffs on plant and machinery	-207.7	-197.1	-214.4	-255.7
TOTAL	-321.7	-289.6	-333.1	-404.7

*This is the amount of saving given by the income averaging scheme. Statistics are not kept on the value of other tax concessions available to farmers.

Source: Industries Assistance Commission (1989)

maximum deposit that an individual may have at one time is \$250,000. Over \$50 million was lodged with the scheme in the 1990 tax year.

4.2.3 Other tax considerations

Anecdotal evidence suggests that the influence of taxation on farmers' purchase decisions may exacerbate the impact of downturns on agricultural suppliers. This arises from a tendency by farmers to purchase and store tax deductible supplies during years of high income. Such supplies may include

fertilisers, chemicals, drenches, wool packs, etc. Farmers entering a downturn may not have to purchase such supplies for periods of up to a year. The result is to cause fluctuations in sales of inputs despite them being used on a regular basis.

In summary, there are a range of measures available to primary producers through the tax system, that are not available to non-farm rural businesses, that have an income smoothing effect. The tax system also exacerbates rural downturns by distorting expenditure patterns.

Table 3. Marginal Tax Rates for Primary Producers in 1989

Income group	No. of taxpayers	Mean taxable income (\$)	Mean average income (\$)	Marginal tax rate (%)
Non-tax group	1,720	6,383	6,895	9.54
<7,500	10,658	5,301	8,548	11.46
7,500 - 12,599	25,583	10,253	9,284	13.73
12,600 - 19,499	40,301	16,017	12,059	16.55
19,500 - 27,999	39,484	23,475	16,305	20.90
28,000 - 34,999	21,869	31,320	20,638	26.50
35,000 - 49,999	23,621	41,202	25,696	29.43
>50,000	20,044	83,821	45,323	39.06

Source: Number of taxpayers, mean taxable income and mean average income calculated from Tables 1.18 and 1.19 Australian Taxation Office (1990). Marginal rates calculated by applying Bates (1968) formula to mean taxable income and mean average income.

Table 4. Marginal Tax Rates in the Absence of Averaging-1989

Income bracket	Marginal tax rate (%)
0 - 5,100	Nil
5,101 - 12,600	24
12,601 - 19,500	29
19,501 - 35,000	40
>35,000	49

Table 5. Mean Average Rebate Received by Income Group

Income group	No. of taxpayers	Mean average rebate (\$)	Percent of total average rebate (%)
Non-taxable	1,720	159	0.00
<7,500	10,658	-219	-0.87
7,500 - 12,599	25,583	240	2.30
12,600 - 19,499	40,301	601	9.07
19,500 - 27,999	39,484	1,121	16.58
28,000 - 34,999	21,869	1,705	13.97
35,000 - 49,999	23,621	2,627	23.24
>50,000	20,044	4,745	35.62

Source: Calculated from Tables 1.18 and 1.19 of Australian Tax Office (1990).

5. Conclusions

There is a commonly held belief within the rural community that non-farm rural businesses should be afforded similar assistance to that provided to the farm sector, particularly in times of rural downturn. Assistance available to farmers that is not available to non-farm rural businesses includes financial assistance through the Rural Adjustment Scheme and State drought relief arrangements as well as income smoothing assistance provided through the IED Scheme and tax averaging.

The extension of broad based financial adjustment assistance to the non-farm rural business sector would lead to poor resource use outcomes and would impede the development of small business self-reliance and small business structures most suited to a fluctuating income environment.

Income averaging for tax purposes, income equalisation deposits and various tax concessions provide significant benefits to the farm sector that are not available to other small rural businesses. This disparity in tax treatment is an important focus for policy reform. Arguments for extending these tax benefits to non-farm rural businesses on the basis of their fluctuating incomes, however, can equally be extended to others in the broader community with variable income streams. An IED scheme for small business would encourage self reliance and warrants further examination.

Most forms of assistance that could be offered to non-farm rural businesses are likely to be administratively difficult due to definitional problems associated with non-farm rural businesses and the varying degree to which small businesses are reliant upon agriculture. This latter characteristic is a result of the variable environments, both across regions and over time, in which non-farm rural businesses operate.

The key to a viable non-farm rural business sector and to ensuring an appropriate level of support from the sector to agriculture, is to ensure the sector retains the capacity to adapt to changing circumstances. To this end, existing and future Government programs aimed at improving small business skills must adequately recognise the degree and range of risks faced by non-farm rural businesses.

This point is also relevant to new entrants to the non-farm rural business sector, in that information available to them is unlikely to reflect the range of risks involved. Greater emphasis needs to be placed on encouraging the development of appropriate small business structures and risk management techniques.

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Appendix A: Assistance Available to Primary Producers in New South Wales

A.1 Rural Assistance Authority

Primary producers have access to the Rural Assistance Authority under the following three schemes.

Special conservation scheme

This scheme provides assistance in the form of advances for capital programs that have a beneficial impact on the land, community and environment. These include soil conservation, stock and domestic water supply, irrigation, tile drainage and the control and eradication of serrated tussock. Advances are provided by way of a loan at an interest rate of 8 per cent. The amount of advance available is limited to 90 per cent of the reasonable cost of the works. The advances may be for a maximum term of up to 15 years. To be eligible, the farming enterprise must provide the majority of total income for the applicants and net assets must not exceed \$800 000.

Relief scheme

This scheme is for the provision of carry-on requirements following production losses caused by natural disasters including bushfires, floods and other seasonal factors. Assistance is available by way of a loan up to \$80 000 at an interest rate of 6 per cent. Advances are for a maximum period of ten years, which may be preceded by interest only payments for an initial two years.

Rural adjustment scheme

Assistance is available to any farmer, grazier, horticulturist, agriculturist or oyster farmer, but does not extend to forestry or fishing. The scheme is divided into parts A, B and C.

Part A

Under part A, assistance is given in the form of an interest subsidy on commercial borrowings. The subsidies are payable for a maximum term of seven

years, and are limited to a maximum of half the total interest costs, and a ceiling of \$20 000 in each year. Funds are available to farmers who are suffering financial difficulties but who have long term viability for the following measures: capital restructuring; increasing farm size; increasing capital intensity; changing farm programs; adopting improved technologies; training (up to \$1000 p.a. for three years); and assisting eligible farmers to purchase the assets of other farmers who have no prospects in the industry.

Part B

Primary producers in industries that have been deemed to be suffering a severe market downturn are eligible to apply for "carry-on" finance.

Part C

This scheme assists non-viable farmers exit the industry through household support and re-establishment assistance. Household support is a cash payment equivalent to unemployment benefits and is payable for up to two years where an effort is being made to sell the property. Re-establishment is a means tested grant where farmers have sold their productive assets and will exit from farming in a hardship situation. The maximum amount available as at 30 June 1990 is \$31,928, which is indexed quarterly.

A.2 Commonwealth Development Bank

The Commonwealth Development Bank's (CDB) function is to supplement loans made through normal commercial sources to primary producers where credit is not available on reasonable and suitable terms and conditions. The non-availability of credit may be due to a lack of security and the need for extended repayment terms by the borrower. Loans proposals are assessed primarily on the likelihood of success and ability to repay borrowings, rather than the security offered. The CDB also provides hire purchase or similar financing arrangements for new and second hand equipment.

A.3 NSW Agriculture

Drought relief

Financial assistance is available in the form of road and rail freight subsidies and assistance with water cartage.

Farmcheque

Farmcheque is a whole-farm monitoring and management program run by NSW Agriculture. The aim of the project is to help producers: improve their record keeping skills; gain experience in assessing the physical and financial performance of their farms; use comparative analysis to improve their overall farm management; and use information and advice provided by bankers, accountants and other professionals.

Advisory services

NSW Agriculture provides extensive advisory services throughout the State. Advice can be obtained on production aspects relating to livestock, crops and horticultural enterprises. Advice on farm and financial management is also available.

A.4 Rural Counsellors

The Rural Counselling service is funded by Federal and State Governments and by local community advisory groups. Counsellors are trained to help the farm family identify and assess available options. Rural counsellors provide assistance with: assessment of a farmer's current financial position; cash flow budgeting; reviews of contracts with lending institutions; loan applications; communication with lenders; information on government assistance schemes, including the Rural Adjustment Scheme; information on Social Security and other welfare benefits; assistance with family decision making; personal or family counselling when required or referral to an appropriate service.

A.5 Department of Conservation and Land Management

The Department provides resources, advice and assistance to protect, repair and maintain the land

resource base of the State. Services include assistance in property planning and the design and construction of farm water supplies and soil conservation works. Under appropriate circumstances loans are available at reduced rates of interest for approved soil conservation and farm water supply programs. It also provides advice and assistance in the formation of landcare groups.

Appendix B: Assistance Available To Non-farm Rural Business in New South Wales

B.1 Department of Consumer Affairs

Advisory

A confidential counselling service exists for small business owners. Advisers can help clients to establish a business, develop a plan and assess business opportunities. The Department of Consumer Affairs also provides advice on marketing services, financial management, planning and performance review, financial restructuring and applying for a loan. Some of the major regional centres such as Dubbo, Tamworth and Wagga Wagga have computer and audio visual services available to clients. Programs available include self assessment, costing and break-even analysis.

Financial

Financial assistance, in the form of a subsidy, is available to be put towards the cost of a specialist consultant's study into activities of business where benefits to New South Wales can be demonstrated. The maximum amount payable, on a dollar for dollar basis, is \$5000 to existing businesses and \$3000 to new businesses.

Mediation

A free mediation service exists to assist small business people to overcome or minimise difficulties relating to: delayed responses from government departments, instrumentalities or local government; landlord/tenant disagreements; problems with suppliers; arranging appointments with and/or identifying the correct government department to

deal with; and facilitating payment of outstanding accounts between small businesses and government departments.

Education and training

The Department of Consumer Affairs conducts training, education and skill development programs for intending and existing small business operators. A new venture workshop is held regularly for persons intending to go into business. Other workshops available are business planning, financial management, franchising, marketing, import/export. All workshops are available in country areas by arrangement with appropriate groups or bodies.

National Information Awareness Program (NIAP)

This program is run in conjunction with the Commonwealth Government and is designed to increase the use of external advisers by small business people. The program aims to create a network between accountants, solicitors, bankers, government, business advisers and the small business sector and aims to raise awareness of small business clients.

Regional Business Development Scheme

This scheme was established as part of a program to encourage regional economic growth and is being funded by savings from the Payroll Tax Rebate Scheme. The main aims of the scheme are: to enhance the viability of industry and commerce in non-metropolitan areas of New South Wales; to assist business relocate to country New South Wales; and to promote expanded employment opportunities in non-metropolitan areas, both directly and indirectly.

The scheme may provide subsidisation of costs incurred by firms in the following areas: business planning; plant and removal costs; skills training; key personnel removal costs; contribution towards infrastructure; offsetting local government charges; technology development; export development; identification of business opportunities; and contribution to payroll tax, land tax, and stamp duty obligations.

B.2 Commonwealth Employment Service (CES)

CES has the facilities to act as a recruiting and training service for small businesses seeking employees. Training can be provided through TAFE colleges.

B.3 Commonwealth Development Bank (CDB)

The CDB's function is to supplement loans made through normal commercial sources to small and medium sized businesses where credit is not available on suitable and reasonable terms and conditions. Loan proposals are assessed primarily on the likelihood of success and ability to repay borrowings, rather than the security offered. The CDB also provides hire purchase or similar financing arrangements for new and second hand equipment.

Appendix C: Tax Elections With An Income Smoothing Effect

C.1 Valuation of livestock

Livestock are trading stock for primary producers. As such they are required to be brought to account as closing stock at either 'cost' or 'market valuation', with the cost method being the most common. Because of difficulties in identifying specific animals, most primary producers determine the value of closing stock using the "average cost" method.

When the cost method is used, difficulties arise in establishing the cost of natural increase. Therefore a series of arbitrary values are set by the Tax Office for natural increase. There is no provision for these minimum values to be increased as the animal ages.

The combination of the average cost method of valuation and the prescribed values, results in livestock being brought to account at low values. In an enterprise with a self replacing herd, the average cost trends towards the prescribed value over time. This results in a significant deferral of tax until the livestock is sold or dies. The effect is to defer the payment of tax on inventories until they are actually sold, this being at the discretion of the producer.

C.2 Livestock insurance recoveries

Insurance recoveries following the loss of livestock are taxable income. Primary producers can elect not to pay tax on the entire recovery in the year of receipt, but instead can include only 20 per cent of the recovery in their income in the year of receipt and each of the four succeeding years. This concession is not available for other forms of trading stock, and does not apply to small business.

C.3 Forced sales of livestock

Where primary producers sell livestock as a result of loss of pastures following fire, flood or drought, they may elect not to pay tax on the entire profit in the year of sale. One option they face is to pay tax on 20 per cent of the profit in the current year and each of the succeeding four years. Alternatively, profit from the forced disposal can be used to reduce the cost, for taxation purposes, of replacement livestock. This effectively defers the tax liability until the replacement livestock are sold. If primary producers decide to breed replacement livestock, they are required to include such part of the profit on the sale as they think is appropriate. The entire profit must be allocated either to replacement livestock, or included in assessable income within five years.

C.4 Double wool clips

Where primary producers shear early as a result of fire, flood or drought and they receive income from two wool clips in one year, they may elect to defer tax on the profit from the second clip to the following year. In the case of drought, however, it is not necessary that an area be drought declared before the farmer is entitled to make the election. Anecdotal evidence suggests that a seasonal dry spell may be considered sufficient justification for some primary producers to invoke these elections.

C.5 Grain and fodder

Grain and fodder on-hand at the end of the year and intended for use as feed or seed does not have to be bought to account as trading stock.

C.6 Land degradation and water conservation

Primary producers qualify for a 100 per cent tax deduction for capital expenditure to prevent land degradation. If the property is then sold, there is no requirement that the deduction be repaid. They also qualify for a deduction on capital expenditure for conveying and conserving water. The expenditure is claimed in three equal annual instalments. Again, if the property is then sold, there is no requirement that this deduction be repaid.