PRIMARY PRODUCTION & FMD

Who can be a primary producer?

A primary producing business includes businesses involved in:

- Cultivating land
- Maintaining animals for sale or their produce
- Fishing or pearling
- Tree farming or forestry
- Planting and tending trees for felling

These activities generally involve producing raw products from natural resources.

Primary Production Activity	Examples / Activities	Products
1. Agriculture	Wheat farming, Rice farming, Cotton farming, Vegetable farming, Fruit orchards	Grain, Fruits, Vegetables, Sugar cane
2. Livestock Farming	Dairy farming, Sheep farming, Cattle farming, Goat farming, Pig farming, Poultry farming	Milk, Wool, Meat, Eggs
3. Fishing	Commercial fishing, Aquaculture, Fish breeding, Oyster farming	Fish, Crabs, Lobsters, Oysters
4. Pearling	Pearl oyster farming, Pearl harvesting	Pearls
5. Forestry	Growing trees, Managing forests, Harvesting timber	Timber, Wood pulp, Logs

Businesses That Are NOT Primary Producing Businesses

Business	Reason
Grocery stores	Sell products rather than produce them directly
Supermarkets	Retail products instead of producing them
Food processors	Process raw materials into finished products
Restaurants	Prepare and sell food rather than produce raw materials
Bakeries	Process ingredients into baked goods
Butchers buying animals from others	Process and sell meat without raising the animals
Furniture manufacturers using purchased timber	Manufacture products using timber produced by others

Income Averaging

Definition

Income averaging is a tax concession that helps eligible primary producers reduce the impact of fluctuating incomes by spreading taxable income over several years for tax calculation purposes.

Important:

- Income averaging **does not change your taxable income.**
- Instead, it changes **how much tax you pay** on that income.

Purpose of Income Averaging

The purpose is to:

- Reduce tax when income suddenly increases.
- Balance tax across good and bad years.
- Support farmers with unpredictable income.
- Encourage long-term sustainability.

Why Does ATO Provide Income Averaging?

Primary production depends heavily on nature.

Example:

A wheat farmer may experience

Year	Income
Year 1	$25,000
Year 2	$32,000
Year 3	$210,000
Year 4	$18,000

Without income averaging:

- Year 3 attracts very high tax.
- Year 4 provides little benefit despite low income.
- Income averaging smooths the tax burden over time.

How Does Income Averaging Work?

The ATO compares:

- Current year's taxable primary production income
- Average of previous eligible years

If current income is:

Higher than the average

➞ Less tax may be payable than under ordinary tax rates.

Lower than the average

➞ More tax may be payable than would otherwise apply, reflecting the averaging system over time.

The averaging system aims to smooth tax outcomes over multiple years rather than maximize savings every year.

Case Study

James grows cotton.

Year	Income
Year 1	$35,000
Year 2	$42,000
Year 3	$48,000
Year 4	$250,000

Question:

Would income averaging help?

Answer:

Yes. The significant increase in Year 4 income may result in a lower tax liability than ordinary tax rates alone because the averaging system reduces the impact of that one unusually profitable year.

Income Averaging if individual has both primary production income and non-primary production income

An individual can have both primary production income and non-primary production income and still be eligible for income averaging. However, income averaging does not automatically apply to all of their income.

The ATO uses a concept called the **"averaging component"** to determine how much of the individual's taxable income is subject to the averaging calculation

Treatment of non-primary production income

Non-primary production income	Treatment in the averaging component
Less than $5,000	Included in full.
Between $5,000 and $10,000	Only a reduced ("shade-out")* amount is included.
More than $10,000	Not included in the averaging component. Only the primary production income forms the averaging component.

***Shade-out**

- If your taxable non-primary production income is between $5,000 and $10,000:
- Non-primary production shade-out amount = $10,000 − Taxable non-primary production income
- This shade-out amount is then added to your taxable primary production income to determine the averaging component.

Case Study:

- Primary production income = $50,000
- Salary income = $6,000

Since the salary is between $5,000 and $10,000:

Shade-out amount = $10,000 − $6,000 = $4,000

So, the averaging component is:

Primary production income + Shade-out amount

= $50,000 + $4,000 = $54,000

Notice that the full $6,000 salary is not included—only $4,000 is included through the shade-out rule.

LIVESTOCK

Livestock in the context of a primary production business refers to animals that are maintained for sale or for the sale of their produce as part of carrying on a business. Livestock farming is one form of animal cultivation, which is a primary production activity.

Examples of livestock (ATO context

- Cattle
- Dairy cows
- Sheep
- Goats
- Pigs
- Poultry (chickens, ducks, turkeys)
- Farmed deer
- Farmed alpacas and llamas

Valuation of Livestock

- You can choose to value livestock at cost, market-selling value or replacement value. An additional option is available for certain horse breeding stock.
- You may change the basis of valuation year by year. You may also use different valuation methods for different stock in the same year.
- However, the value of your opening livestock (at 1 July) each year must be the same as the value of your closing stock (at 30 June) for the previous year.
- That is, you must use the same valuation method at the beginning of the new income year as you used at the end of the previous income year.

Draft Livestock Trading Statement

Dr						**Cr**
Particulars	**Units**	**Amount**		**Particulars**	**Units**	**Amount**
Opening Stock	XX	XXX		Sales	XX	XXX
Purchase	XX	XXX		Death	XX	??
Natural Increase	XX	??		Killed for Rations	XX	??
Gross Profit/Loss		XXX		Closing Stock	XX	XXX
Total	XX	XXX			XX	XXX

What is Natural Increase?

Natural increase means animals that are born and raised on your farm, rather than being purchased from someone else.

How is the Cost of Natural Increase Determined?

Instead of calculating the actual cost, you may use the ATO prescribed cost.

Animal	Prescribed Cost
Cattle	$20 each
Horses	$20 each
Deer	$20 each
Pigs	$12 each
Emus	$8 each
Goats	$4 each
Sheep	$4 each

What is Killed for Rations?

Killed for Rations means livestock from the farm that is not sold, but is instead:

- Consumed by the farmer or their family (private use).
- Provided as food to employees, shearers, farm workers, etc.

The animal is removed from trading stock, so a value must be assigned to it.

How to value this Killed for Rations stock

There are 2 ways you can value this stock. You can either:

- keep records of the value of goods you take from your trading stock for your own private use and report that amount
- use the amounts we provide (and update annually) as estimates of the value of goods you have taken.

Journal Entry (Simple)

If livestock is used privately:

Drawings A/c ..... Dr

Killed for Rations A/c .... Cr

Valuation of Closing Stock

The ATO allows livestock held as trading stock to be valued using one of the following methods:

- Cost (Average cost)
- Market Selling Value or Replacement Value

The method chosen should comply with the ATO trading stock rules and be applied appropriately.

Formula to Calculate Average Cost per Livestock Unit

Before calculating the **Closing Stock Value** under the **Average Cost Method**, first calculate the **Average Cost per Livestock Unit**.

Formula

$$\text{Average Cost per Unit} = \frac{\text{Opening Stock Value} + \text{Purchases Value} + \text{Natural Increase Value}}{\text{Opening Stock Units} + \text{Purchased Units} + \text{Natural Increase Units}}$$

Formula to Calculate Closing Stock Value

Once the **Average Cost per Unit** is calculated, determine the **Closing Stock Value** using the following formula:

Formula

$$\text{Closing Stock Value} = \text{Closing Stock Units} \times \text{Average Cost per Unit}$$

FMD (FARM MANAGEMENT DEPOSIT)

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Primary producers often experience fluctuating income because of factors such as:

- Drought
- Floods
- Bushfires
- Cyclones
- Market price fluctuations
- Seasonal conditions

A farmer may earn:

- Very high income in one year.
- Very low income in the following year.

To help farmers manage these income fluctuations, the Australian Government introduced the Farm Management Deposits (FMD) Scheme.

What is a Farm Management Deposit (FMD)?

A Farm Management Deposit (FMD) is a special bank deposit available to eligible primary producers.

It allows a farmer to:

- Deposit money during a profitable year.
- Claim a tax deduction for the deposit (if all eligibility conditions are met).
- Withdraw the money in a later year when income is lower.
- Include the withdrawn amount in assessable income in the year of withdrawal.

Simple Definition

Farm Management Deposit (FMD) is a tax planning tool that helps eligible primary producers move taxable income from a high-income year to a lower-income year.

Who Can Open an FMD?

To use the FMD scheme, a taxpayer must generally:

- Be an **individual** carrying on a primary production business.
- Have **taxable non-primary production income of $100,000 or less** for the income year in which the deduction is claimed.
- Hold the deposit with an **approved FMD provider**.

Note: Companies and most trusts are generally not eligible to claim FMD deductions in their own right.

Key Points

- **Minimum Deposit** - The minimum amount for each Farm Management Deposit is **$1,000**
- **Maximum Total FMD Balance -** The maximum total balance a person can hold in Farm Management Deposits is **$800,000**
  This is the combined balance across all FMD accounts.
- **12-Month Rule –** Generally the deposit must remain in the FMD account for **at least 12 months** before it is withdrawn to retain the deduction.

Case Study 1 – Good Year and Poor Year

Mr. David is a wheat farmer carrying on a primary production business in Australia.

In the **2024–25 income year**, he had an excellent harvest due to favourable weather conditions.

His financial details are:

- Primary Production Income: **$350,000**
- Non-Primary Production Income (Bank Interest): **$8,000**
- Total Taxable Income (before FMD): **$358,000**

David is concerned that he will pay a large amount of tax this year. He also knows that farming income can fluctuate because of drought and unpredictable weather.

His accountant advises him to use the **Farm Management Deposit (FMD) Scheme**.

David deposits **$100,000** into an approved FMD account before the end of the financial year.

Question 1

Is David eligible to claim an FMD deduction?

Answer

Yes, provided he satisfies all the ATO eligibility conditions, including:

- He is an **individual** carrying on a primary production business.
- His **non-primary production income is $100,000 or less** (his bank interest is only $8,000).
- The deposit is made with an **approved FMD provider**.
- The minimum deposit requirement is met.

- **Question 2**
- What deduction can David claim?
- **Answer**
- FMD Deposit = **$100,000**
- David can claim an **FMD deduction of $100,000**.

Question 3

What will be David's taxable income after claiming the deduction?

Before FMD

Total Taxable Income = **$358,000**

Less: FMD Deduction = $100,000

Taxable Income = $258,000

David has reduced his taxable income for the current year.

Two Years Later

Unfortunately, a severe drought affects David's farm.

His income for the **2026–27 income year** is:

- Primary Production Income = **$70,000**

To meet his farming expenses, David withdraws the **$100,000** from his FMD account.

Question 4

Is the withdrawal taxable?

Answer

Yes.

The **$100,000 withdrawn** must be included in David's assessable income in the year of withdrawal.

Assessable Income:

Primary Production Income = **$70,000**

Add: FMD Withdrawal = **$100,000**

Assessable Income = $170,000

Learning Outcome

David:

✓ Paid less tax during a profitable year.

✓ Had savings available during a drought.

✓ Paid tax on the withdrawn amount in a year when his farming income was much lower.

This demonstrates the main purpose of the **Farm Management Deposit Scheme**—to help primary producers manage fluctuating income and improve cash flow.

Drought and Forced Disposal of Livestock

Australia frequently experiences droughts, which can have a major impact on primary producers.

During a drought, farmers may face:

- Shortage of feed.
- Lack of water.
- Poor pasture growth.
- Financial difficulties.
- Reduced livestock productivity.

In many cases, farmers are forced to sell livestock earlier than planned because they cannot maintain their animals.

What is Forced Disposal of Livestock?

Forced disposal means selling livestock because of circumstances beyond the farmer's control.

These circumstances may include:

- Drought
- Flood
- Bushfire
- Cyclone
- Other natural disasters

The livestock are sold earlier than they normally would have been due to these events.

Why Does the ATO Provide Relief?

- Normally, selling a large number of livestock in one year can result in a significant increase in taxable income.
- To reduce this tax impact, the ATO allows eligible farmers to defer part of the profit from the forced disposal to a later income year, subject to the relevant conditions.

Conditions for the Concession

To be eligible:

- The livestock must be sold because of an eligible natural event (such as drought).
- The disposal must be **forced**, not voluntary.
- The taxpayer must satisfy the conditions set out in the tax law.
- Appropriate records and evidence should be maintained.

What is Income Deferral?

Income deferral means postponing the recognition of part of the profit from the forced sale until a future income year.

This helps reduce the tax payable in the year the livestock are sold.

Scenario – Drought Sale

David normally sells **100 cattle** each year.

Due to severe drought, he is forced to sell **300 cattle**.

As a result:

- His income for the year increases significantly.
- The sale was not part of his normal business operations.

David may be eligible for the ATO's drought-related concessions if all conditions are satisfied.

Case Study 1 – Forced Disposal Due to Drought

Mr. James owns a cattle farm in Queensland. Under normal conditions, he sells around **150 cattle each year** as part of his regular farming operations.

During the **2025–26 financial year**, the area experienced a severe drought. Due to the shortage of water and pasture, James could no longer maintain all of his cattle.

As a result, he was forced to sell **450 cattle**, which was **300 more cattle than he would normally sell**.

- The details are:

Particulars	Number
Normal annual sales	150 cattle
Actual sales due to drought	450 cattle
Additional cattle sold because of drought	300 cattle

The sale generated a much higher income than usual, increasing James's taxable income.

Question 1

Why did James sell more cattle than usual?

Answer

James was **forced to dispose of the additional 300 cattle because of drought**. The sale was not voluntary; it was necessary because there was insufficient feed and water.

Question 2

Can James claim the drought concession?

Answer

Yes, provided he satisfies the ATO eligibility conditions.

The additional cattle were sold because of drought, so James may be eligible for the **forced disposal of livestock concession**.

Question 3

What is the benefit of the concession?

Answer

Instead of paying tax on all the additional profit in one year, James may be able to **defer part of the profit** from the forced disposal to a later income year, subject to the ATO rules.

This reduces the immediate tax burden and helps with cash flow during the drought.

Question 4

What records should James keep?

- **Answer**

James should keep:

- Livestock sale invoices.
- Livestock registers.
- Farm records showing the number of cattle sold.
- Evidence that the area was affected by drought (for example, government drought declarations or other supporting evidence where relevant).
- Financial records.

Accelerated Depreciation

Accelerated depreciation allows eligible primary producers to claim tax deductions for certain depreciating assets **earlier than under the normal depreciation rules**.

Instead of claiming deductions over many years, the taxpayer may be able to claim:

- The **full cost immediately**, or
- A **faster deduction** than the standard depreciation method.

Primary producers often invest significant amounts in farm infrastructure such as:

- Dams
- Irrigation systems
- Fencing
- Hay sheds
- Silos
- Water tanks

- Normally, these assets are depreciated over several years.
- However, the ATO provides special accelerated depreciation rules for certain assets used in primary production, allowing eligible taxpayers to claim deductions more quickly, and in some cases immediately.

Immediate Deduction

Some eligible assets can be claimed 100% in the year they are first installed and ready for use.

Asset Type	Examples	Key Point
Water Facilities	Dams, Water tanks, Bores, Irrigation channels, Pumps, Pipes, Windmills	Used primarily to conserve or convey water
Fencing Assets	Boundary fences, Internal paddock fences, Gates, Fence posts, Wire, Rails	Eligible fencing assets may qualify for an immediate deduction
Fodder Storage Assets	Hay sheds, Silos, Grain storage sheds, Feed storage tanks, Above-ground bunkers	Eligible fodder storage assets may also qualify for an immediate deduction