Pre-Budget Consultation Submission

NATIONAL
CATTLE FEEDERS'
ASSOCIATION

ASSOCIATION
NATIONALE DES
ENGRAISSEURS DE BOVINS

Submitted to the House of Commons
Standing Committee on Finance

August 6, 2020

RECOMMENDATIONS

Recommendation 1

Pursue meaningful improvements to *Agri-Stability* by removing the $3 million cap on payments or increasing it to at least $20 million, eliminating “reference margin limiting” and increasing the payout from 70% to 85%.

Recommendation 2

Take a measured and informed response to labour challenges in the agriculture sector that have been exacerbated by the pandemic to ensure that positive employers of federal labour programming are not unfairly impacted.

Recommendation 3

Establish a dedicated line item in the budget for investments in rural infrastructure, particularly rural roads and bridges.

Recommendation 4

Carefully consider the consequences on agriculture of any proposed action to change the business tax regime or close so-called corporate tax “loopholes.”

Pre-Budget Consultation Submission

Overview

The National Cattle Feeders' Association (NCFA) is the voice of Canada's cattle feeders. NCFA strives to improve the growth, economic and environmental sustainability, and competitiveness of the fed cattle sector.

Cattle feeding is the critical lynchpin of the Canadian beef industry, connecting the breeding and ranching sectors to the beef processing, wholesale, and retail sectors.

COVID-19 Impact

COVID-19 has presented multiple and severe challenges:

1) A slow-down in beef processing caused cattle to back-up in feedlots. This back-up peaked at 130,000 head in May and currently sits at 113,000 head. These cattle are costing feedlots $450,000 each day.

2) Prices for finished cattle fell dramatically. Live market-ready fed cattle usually price between $155 to $175 per hundred-weight (cwt) during the first six months of the year. In 2020, prices started at $165 and then plummeted to $110. Prices have yet to recover and currently sit at $135. This $20 to $30 drop from the average translates into a loss of $300 to $450 per head.

3) From mid-March to the end of July, cumulative losses for ranchers and cattle feeders are $300 million.

Looking Ahead

Prior to COVID-19, agriculture in Canada was poised for growth. Like many sectors, the pandemic has created great financial strain and an uncertain future. NCFA believes that a return to growth is within reach for the beef industry, but only with the right policies, programs, and supports.

Recommendation 1

Pursue meaningful improvements to *Agri-Stability* by removing the $3 million cap on payments or increasing it to at least $20 million, eliminating "reference margin limiting" and increasing the payout from 70% to 85%.

Government support to manage agricultural risk is comprised of four programs:

- *Agri-Insurance*
- *Agri-Invest*
- *Agri-Recovery*
- *Agri-Stability*

Together, these programs provide about $1.6 billion annually to producers. However, very little of this can be accessed by ranchers and cattle feeders.

About $1 billion (63%) is paid through *Agri-Insurance* for crop failures. This has little relevance for cattle. About $250 million (15%) is a government match for producers who make deposits into their *Agri-Invest* accounts. The average size of a cattle account is $13,000. This does very little for a feedlot with thousands of cattle. About $350 million is paid annually through *Agri-Stability*, one of the most important risk management tools. But again, a number of challenges work against participation by ranchers and cattle feeders.

This explains why the beef industry appealed for special COVID-19 support under the fourth program, *Agri-Recovery*. While the government response under *Agri-Recovery* is appreciated, it may not be enough. Producers will be looking towards *Agri-Stability.*

Currently, only 31% of producers are enrolled in *Agri-Stability.* In 2012, that figure stood at almost 45%. The lower participation rate is a consequence of two factors:

1) A number of changes were made to the program in 2013. For example, payments used to be triggered after farm net income fell by 15%. Today, payments are triggered only after net income falls by 30%. This has made the program less attractive.

2) A number of structural issues work against participation, particularly for beef producers. For cattle feeders, the $3 million "cap" is a key impediment.

A recent study commissioned by the Alberta Cattle Feeders' Association (ACFA) estimates that a feedlot of 25,000 head will likely sustain a loss of $6.5 million this year, assuming that current market dynamics hold to the end of 2020. A second COVID wave could push losses upwards of $25 million. In the very best case scenario, less than half the anticipated loss is covered by *Agri-Stability,* which caps out at $3 million very quickly and leaves feedlots exposed to losses in the tens of millions of dollars.

The Cap on Agri-Stability

The current $3 million cap on *Agri-Stability* payments has not changed in 20 years. However, there has been a 47% increase in the consumer price index, a 50% increase in the average annual price for finished cattle, and a 70% increase in feedlot input costs.

There has also been growth in the scope and scale of individual feedlot operations. Because of continued concentration and consolidation in the cattle feeding sector, the scale of operations is larger. This has also diminished the relevance of a $3 million cap.

Between 2011 and 2020, the number of beef feedlots in Alberta and Saskatchewan fell from 201 to 165. However, the size of the remaining feedlots grew considerably. Some of the largest gains have been seen in operations with 10,000 head or more. These feedlots have increased, on average, by over 3,300 head. This represents an additional $8 million in gross sales per operation (assuming each 1,500 pound steer sells at $1.60 per pound).

To make Agri-Stability work better for cattle feeders, NCFA is asking for the $3 million cap on Agri-Stability to be removed entirely, or increased to at least $20 million to reflect the effects of inflation and the growing scale of today's modern cattle feeding operations.

Recommendation 2

Take a measured and informed response to labour challenges in the agriculture sector that have been exacerbated by the pandemic to ensure that positive employers of federal labour programming are not unfairly impacted.

A chronic shortage of labour is the single largest challenge facing Canadian agriculture. Each year, labour shortages cost the beef industry $435 million in lost sales. Lost sales across all of agriculture are some $2.9 billion annually.

Throughout the pandemic, temporary foreign workers (TFWs) became even more critical to the sector. NCFA acknowledges and appreciates the steps government has taken to ensure that TFWs can continue their important contribution in securing Canada's food supply.

It is important to recognize the different ways that foreign workers participate in agriculture. There are TFWs who supply temporary and seasonal labour for fruit and vegetable operations, and TFWs with specific skills who work full-time, year-round, and long-term for livestock sectors such as beef. Many of these TFWs will eventually become permanent residents and Canadian citizens.

As we witness the pandemic challenges confronting seasonal workers in Ontario, NCFA calls upon government to understand how changes to the TFW Program in one sector (seasonal) has the potential to harm another sector (livestock).

A knee-jerk reaction to the challenge must be avoided. Rather, a measured response that acknowledges the distinction between "temporary and seasonal" versus "full-time and year-round" is critical.

Recommendation 3

Establish a dedicated line item in the budget for investments in rural infrastructure, particularly rural roads and bridges.

The lack of a strong rural infrastructure foundation is a significant barrier to growth for the beef sector. Most agriculture operations are located in small rural municipalities with a limited tax base to support the infrastructure needed to get agriculture products to market. In the post-COVID recovery phase, these same municipalities are even further financially strained.

The federal government is already considering economic stimulus programs to boost the Canadian economy, and infrastructure investments are one of the most immediate and effective means of economic stimulus. However, this stimulus must address the needs of all communities and not just urban municipalities.

As such, NCFA calls upon the government to boldly prioritize the transportation infrastructure needs of rural communities so already strained municipalities can provide the infrastructure required to deliver on the first portion of the trip to market.

Our challenge to the government is to implement a dedicated line item in the federal budget for critical investments in rural and agriculture infrastructure. A separate budget line item highlights the importance of that item, demonstrates a commitment, and enhances accountability.

Recommendation 4

Carefully consider the consequences on agriculture of any proposed action to change the business tax regime or close so-called corporate tax "loopholes."

Documents from the Office of the Parliamentary Budget Officer outline a proposal that would disallow business from deducting the full amount of interest paid on debt when calculating taxable income (deductibility would be reduced from 100% to 30% of "earnings before the deduction of interest, taxes, depreciation and amortization or EBITDA).

This proposal will generate unintended consequences, particularly for capital intensive businesses that are highly leveraged. Cattle feeding is exactly that kind of business.

Feedlots are capital intensive and require a large land base, significant heavy equipment, and multiple structures. On top of that, thousands of cattle are purchased continually through various financing mechanisms. Feedlots also operate on a narrow margin that is subject to huge volatility. Thus, the EBITDA for a cattle feeding operation can fluctuate wildly from year to year, magnifying the impact of any reduction in interest deductibility.

Impact on a Typical Feedlot

Assume a feedlot with $60 million in debt at an interest rate of 2.25%. Annual interest costs will be $1.35 million. Further, assume that capital depreciation is $1.5 million and that the net income before tax (EBITDA) is $4 million.

Under the current rules, the tax owed by the feedlot is $310,500. This is calculated by taking the $4 million in income and subtracting the $1.5 million in depreciation and $1.35 million in interest. This yields a taxable income of $1.15 million. At a combined corporate tax rate of 27%, the amount of tax is $310,500.

Under the proposed rules, the tax owed increases to $351,000. This is derived by taking the same $4 million in income less the $1.5 million in depreciation and a smaller amount of $1.2 million for the interest. Taxable income rises to $1.3 million, and tax paid at 27% is $351,000.

Under this scenario, the amount of tax rises by 13%. In all likelihood, this will be replicated on farms right across Canada, many of which carry high debt loads—even more so given the COVID-19 pandemic.

It is important to understand that this proposal comes on the heels of recent tax increases at all levels of government from the federal carbon tax and increased provincial fuel taxes (with no corresponding increase in the farm fuel exemption) to strange levies such as the livestock "Head Tax" in Lethbridge County, Alberta.

This "piling on" of taxes is undermining competitiveness. NCFA believes government must proactively consult with stakeholders to ensure no unintended consequences of this proposal, or any other tax proposal.

(Word Count=1,818)