



TRUST *for* NATURE

INFORMATION SHEET

TAXATION, PRIVATE LAND CONSERVATION AND PARTICIPATION IN LAND-BASED ENVIRONMENTAL MARKET SCHEMES

This information sheet addresses taxation issues relating to the interests of owners of land being managed for conservation purposes as well as those wishing to enter into environmental market schemes and arrangements. It is not intended as legal advice or an alternative to obtaining independent taxation advice, but may assist in guiding decisions and identifying what advice you may need to seek.

How does tax law affect me if I get paid for looking after the natural environment on my land or for carrying out particular conservation works?

The laws relevant to participation in schemes providing payments for ecosystem services include Commonwealth income tax legislation as well as Victorian land tax laws and municipal rating schemes.

The Australian Taxation Office ('ATO') has produced information on these issues including:

- a number of 'class rulings' providing guidance on matters such as treatment of payments and rights under offset schemes and public tender schemes. (Those rulings have been used in the preparation of this information sheet); and
- helpful plain English information on the ATO website.

Commonwealth income tax laws

Commonwealth income tax law covers areas such as income tax, capital gains tax, fringe benefits, tax offsets, tax deductions, capital allowances (akin to depreciation), and the Carbon Farming Initiative (CFI).

What is likely to be treated as ordinary income for tax purposes?

Any payments you receive under an agreement for managing land (for example, for identified conservation purposes) will be treated as ordinary income. These may be received in periodic payments, such as annual payments, or periodically in performance of parts of an agreement.

Will I be liable to capital gains tax if I participate in an environmental scheme and receive payments?

The right to receive payments under an environmental market scheme (whether accompanied by an obligation to undertake on-title protection or not) is likely to have capital gains implications, notably as payments are received. However, capital gains tax exemptions may apply where payments are subject to income tax assessment as ordinary income.

Can I receive any income tax deductions from my participation in an environmental market scheme?

- Income tax deductions may be available to you for expenses associated with entering into an environmental market agreement.
- Deductions may also be available to you for expenses associated with performing management actions.
- Whether or not losses can be claimed in a particular income tax year will depend upon a number of factors, including whether you are regarded as carrying on a commercial business under the tax law.
- Individuals with losses from carrying on non-commercial business activities as a result of conservation activities and/or participation in a environmental scheme may need to defer those losses to future income tax years depending on your particular circumstances.

Preparing annual profit and loss statements for your land-based activities regardless of whether or not you are a primary producer, or carrying on a commercial business, may be helpful to you in dealing with these issues now and into the future.

Can I receive an income tax deduction for agreeing to permanent protection of my land registered on title as a result of participating in an environmental market scheme?

Income tax deductions are currently available for a period of no more than 5 years under the *Income Tax Assessment Act 1997* for any capital losses arising from entering into conservation covenants, regardless of source of assessable income. However, access to these income tax deductions is limited to circumstances where the landholder does not receive a 'material benefit' in relation to the application of the covenant, as well as experiencing a decrease in market value of the land (greater than \$5000 as assessed by a ATO valuer) resulting from the covenant. This means that establishing on-title protection by way of covenant as a result of participating in an environmental market or incentive scheme could only entitle you to an income tax deduction if you could demonstrate that you receive no material benefit or reward for this aspect of the contract and at the same time a loss in market value of your land occurred.

The ATO has helpful information and case studies on its website about the application of conservation covenants and capital gains treatment that may assist you, depending on your particular circumstances and the nature of any reduction in market value of your land as a result of establishing a conservation covenant.

Can I receive deductions for expenditure on landcare operations?

'Landcare operations' are activities that combat land degradation, which include the types of activities frequently funded under environmental market programs. This may include fencing, control of invasive species, and revegetation used to combat salinity or erosion. There are provisions under Commonwealth income tax law for tax deductions of capital expenditure for 'landcare operations'. These deductions are available to landowners involved in primary production, as well as taxpayers managing rural land for the purposes of producing assessable income (except the business of mining or quarrying). If you are in one of these categories you may be eligible to claim deductions relating to 'landcare operations'. To do so, you need an 'approved land management plan' prepared by an authorised consultant registered with the Commonwealth Department of Agriculture, Fisheries and Forestry ('DAFF'). A list of authorised consultants can be found on the DAFF website: links to which are provided under Useful Resources.

'Primary production' is defined in the *Income Tax Assessment Act 1997* and the ATO has useful information for primary producers: please refer to list below in 'Useful resources'.

Are there ATO rulings relevant to environmental market and incentive schemes?

The ATO has produced a number of class rulings at the request of public authorities administering ecosystem service regulations and payment schemes. These are particularly helpful in understanding how payments received may be treated as either ordinary income or a capital gain or loss under the tax rules. For Taxation Rulings and other guidance relevant to native vegetation offset agreements and other environmental schemes please refer to the list below in 'Useful resources'.

Carbon Farming

Division 420 of the *Income Tax and Assessment Act 1997* forms a code covering the tax treatment of registered Australian Carbon Credit Units (ACCU) created under the Carbon Farming Initiative (CFI) regulatory framework by undertaking land-based emissions reduction or sequestration activities. The complexities that may arise with other environmental market and payment schemes in distinguishing income from capital are avoided by the tax law deeming the value of ACCUs to be income in the year of receipt. Expenses that relate to the issue of the ACCU are deductible under Division 420. Other expenses incurred in developing and generating the offset that leads to the issue of the ACCU are covered under the general rules for deductibility.

Apart from the CFI framework, under Subdivision 40-J of the *Income Tax Assessment Act 1997* you may be able to claim deductions for capital expenditure on trees established as a 'carbon sink forest', if you are carrying out a business. The deduction encourages the establishment of carbon sink forests for the dedicated purpose of carbon sequestration. To make deduction claims, certain conditions must be met including that you are carrying on a business and you are not establishing the trees with the intention of felling them or using them for commercial horticulture. Other conditions apply, including that the trees occupy more than 0.2 hectares and that they are likely to grow to at least 2m in height.

The ATO provides information about what constitutes carrying on a business and can provide private rulings tailored to individuals' circumstances.

Victorian land tax and municipal rating laws

What implications are there under Victoria Land Tax law if I participate in an environmental market scheme?

Land tax in Victoria applies to land valued at \$250,000 or more.

Land used for primary production in Victoria attracts an exemption from land tax. If land is withdrawn from primary production as a result of entering into a conservation covenant and/or environmental market arrangement (meaning it is no longer used for the cultivation of plants or produce, or maintenance of animals, for sale), it is possible that the land may no longer be regarded as in primary production and may no longer attract the exemption.

The Australian Valuation Property Classification Code applied by municipal valuers to land that has an on-title covenant permanently protecting it will influence how your land may be classified for rating and other land-based taxation purposes.

What municipal rates implications are there in environmental market participation?

Where an environmental market or incentive scheme arrangement involves placing a conservation covenant over land, in some instances Councils will provide rate rebates or discounts to landowners. This does not presently apply to all Councils in peri-urban, rural and regional areas. Check with your local Council to see whether a rebate is provided in your municipality.

Check Trust for Nature's website for updated information about land-based taxation in Victoria as this is a changing area of the law.

Useful resources

Consult a tax advisor to make sure your particular circumstances are taken into account to guide your particular arrangements.

ATO and tax rulings on biodiversity offsets, tender programs and eligibility in relation to landcare operations and water facility concessions:

<https://www.ato.gov.au>

Land Management Plan authorised consultants for the purposes of 'Landcare operations' <http://www.daff.gov.au/natural-resources/landcare/tax>

For primary producers, <https://www.ato.gov.au/Forms/Information-for-primary-producers-2014/>

Carbon Sink Forests, <https://www.ato.gov.au/Business/Deductions-for-business/In-detail/Other-deductions/Carbon-sink-forests/>

Class Ruling 2013/28 Native vegetation offsets – *Victorian Department of Sustainability and Environment* – Bushbroker Scheme Method 1 (sale of native vegetation offset credits to private sector permit holder), <http://law.ato.gov.au/pdf/pbr/cr2013-028.pdf>

Class Ruling CR 2013/29 *Income Tax: Victorian Department of Sustainability and Environment – Bushbroker Scheme (Method 2)* [concerning the transfer of land to the Crown as a result of a native vegetation offset arrangement], <http://law.ato.gov.au/pdf/pbr/cr2013-029.pdf>

Class Ruling 2010/76 EcoTender payments – Murrumbidgee CMA (NSW), <http://law.ato.gov.au/pdf/pbr/cr2010-076.pdf>

Taxation Ruling TR 97/11 *Income tax: am I carrying on a business of primary production?*, <http://law.ato.gov.au/atolaw/view.htm?DocID=TXR/TR9711//ATO/00001>

More information and help with arranging a valuation is available from the ATO by phoning 1300 130 248 or visiting <https://www.ato.gov.au/Non-profit/Guides/In-detail/Fact-sheets/Other/Conservation-covenant-concessions/>

Department of the Environment *Gifts that keep on giving: a landholder's guide to land protection and conservation options*, <http://www.environment.gov.au/resource/gifts-keep-giving>

Norton Rose Fulbright *CFI Legal and Contracts Guide* (2013), see <http://www.daff.gov.au/climatechange/cfi>

Trust for Nature information sheets *Additionality in environmental markets* and *Legal issues for participants in environmental markets* <http://www.trustfornature.org.au>

Trust for Nature *Land-based environmental markets and the law: The evolving legal landscape underpinning ecosystem services markets in Victoria* (2014), <http://www.trustfornature.org.au/data/media/00002011/Web2-Land-based-environmental-markets-and-the-law.pdf>

Trust for Nature *Shining a Light on law and markets in private land conservation: insights and issues from Victorian landowners* (2014), <http://www.trustfornature.org.au/data/media/00002093/Shining-a-light.pdf>

Victorian State Revenue Office & land tax <http://www.sro.vic.gov.au>