

Tax implications of land conservation payments and activities

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 arrangements.

Trust for Nature is grateful to all Victorians who conserve the natural habitat on their land, in particular those who make the significant commitment to protect their land forever with a conservation covenant. We appreciate that the taxation implications of conservation payments and activities can be complex, and we hope that this information sheet will help Victorians navigate this area a little more easily.

This information sheet 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 tax laws relevant to participation in schemes providing payments for conservation services include Commonwealth income tax and goods and services tax (GST) 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 conservation management schemes, 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 tax laws

Commonwealth tax laws cover areas such as income tax, capital gains tax (**CGT**), GST, fringe benefits tax, 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 CGT if I participate in an environmental scheme and receive payments?

The entry into a conservation covenant under an environmental scheme where you receive payments (whether accompanied by an obligation to undertake on-title protection or not) is likely to have CGT implications.

The entry into an offset scheme, where you receive and sell vegetation or biodiversity credits, is also likely to have CGT implications. Notably, these consequences arise at the time you enter into the agreement.

The formula for working out your capital gain from entering into a conservation covenant allows you to take into account the effect of the conservation covenant on the value of the land, so you will need a valuation to work out your CGT. However, you may be entitled to certain CGT concessions which reduce the amount of the capital gain, such as:

- a pre-CGT exemption, if the land was acquired before 20 September 1985;
- the CGT discount, if the land was owned for at least 12 months before the grant of the conservation covenant; and/or
- the small business CGT concessions, where the relevant criteria are met, including that the land is an 'active asset'.

A CGT exemption 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.
- Income tax deductions may not be available if the amount derived by you is a capital gain and not ordinary income, and you are not carrying on business on the land. However, in an offset scheme you may be able to include your expenses in the cost base of your credits for CGT purposes.
- 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 an environmental scheme may need to defer those losses to future income tax years depending on their 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 entering into perpetual conservation covenants. However, access to these income tax deductions is limited to circumstances where the landholder does not receive any money, property or other material benefit for entering into the covenant, as well as experiencing a decrease in market value of the land of greater than \$5,000 (as assessed by an ATO valuer) resulting from the covenant (if you have held the land for at least 12 months). This means that a permanent conservation covenant on land you have held for more than 12 months could only entitle you to an income tax deduction if you could demonstrate that you receive no material benefit from entering into the contract and at the same time a greater than \$5,000 loss in market value of your land occurred. Also, the deduction cannot add to or create a tax loss, but can be spread over up to 5 years.

The ATO has helpful information and case studies on its website about conservation covenant concessions and their CGT treatment that may assist you, depending on your particular circumstances.

Can I receive deductions for expenditure on landcare operations?

If you are carrying on a business of primary production or other business activities on your land, you may be entitled to tax deductions for capital expenditure on landcare operations.

'Landcare operations' are generally activities that combat land degradation, which include the types of activities frequently funded under environmental market programs. This may include erecting a fence to separate different land classes in accordance with an 'approved land management plan', control of invasive species, and revegetation used to combat salinity or erosion. The deductions are only 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'.

The 'approved land management plan' for erecting a fence to separate different land classes must be prepared by an authorised officer of an Australian government agency responsible for land conservation or an approved farm consultant (contact the Commonwealth Department of Agriculture, Water and Environment for more information).

'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 payment schemes and offset 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 current ATO public rulings and other guidance relevant to conservation covenants, native vegetation and biodiversity 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 deals with the tax treatment of registered Australian Carbon Credit Units (**ACCU**) created under the Carbon Farming Initiative (**CFI**) regulatory framework. These rules apply if you acquire, hold or dispose of ACCUs. Broadly, they treat the cost of acquiring the ACCUs as generally deductible (with some exclusions), the proceeds of disposing of the ACCUs as assessable, and any increase or decrease in the value of ACCUs in an income year as assessable or deductible.

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 for establishing trees as a 'carbon sink forest', if you are carrying on a business. The deduction encourages the establishment of carbon sink forests for the dedicated purpose of carbon sequestration. To 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 (\$300,000 from the 2022 land tax year) for individuals and companies or \$25,000 or more for trusts.

Land used primarily for primary production in Victoria may be exempt from land tax. If land is no longer used for 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 used for primary production and may no longer be exempt from land tax.

The Australian Valuation Property Classification Code applied by municipal valuers to land that has an on-title covenant permanently protecting it may 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. Check with your local Council to see whether a rebate is provided in your municipality.

Goods and Services Tax (GST)

You may need to register for GST as a result of entering into an environmental market or incentive scheme arrangement. The creation of offset or biodiversity credits on entering into the agreement, the sale of credits and the receipt of annual payments may involve a GST liability for landowners who are registered for GST. Landowners who are registered for GST may also be able to claim input tax credits on the acquisition of goods or services when performing management activities.

Useful resources

Your tax consequences will depend greatly upon the specific arrangements you are entering into. As this is a complex area of taxation law, please consult your regular tax advisor for assistance.

ATO publications and tax rulings on conservation covenant concessions, vegetation and biodiversity offsets and eligibility for landcare operation deductions:

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

For claiming conservation covenant concessions: https://www.ato.gov.au/non-profit/gifts-and-fundraising/in-detail/fundraising/claiming-conservation-covenant-concessions/?page=1#CGT_concessions

For primary producers: <https://www.ato.gov.au/Forms/Information-for-primary-producers-2021/>

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

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

Class Ruling 2010/76 EcoTender payments – Murrumbidgee CMA (NSW) (concerning conservation management payments received by landowners), <https://www.ato.gov.au/law/view/pdf/pbr/cr2010-076.pdf>

Class Ruling 2009/77 Income tax: NSW Department of Environment, Climate Change and Water - Biodiversity Banking and Offsets Scheme (concerning the issue and sale of biodiversity credits and management payments received by landowners), <https://www.ato.gov.au/law/view/pdf/pbr/cr2009-077.pdf>

Class Ruling 2007/87 Income tax: treatment of payments received under the Lower Murray Darling Catchment Management Authority Rangelands Incentive Strategy – Conservation Reserves and Sustainable Grazing Schemes (concerning on-ground establishment works payments and stewardship payments for permanent conservation management to landholders), <https://www.ato.gov.au/law/view/pdf/pbr/cr2007-087.pdf>

Class Ruling 2007/92 Income tax: assessable income: treatment of payments received under the Western Catchment Management Authority Enterprise Based Conservation Program (concerning on-ground establishment works payments and ongoing conservation management payments to landholders), <https://www.ato.gov.au/law/view/pdf/pbr/cr2007-092.pdf>

ATO Interpretative Decision 2004/714 Capital Allowances: landcare operation – revegetation expenditure – carbon sequestration rights, <https://www.ato.gov.au/law/view/document?DocID=AID/AID2004714/00001&PiT=99991231235958>

ATO Interpretative Decision 2002/678 Income Tax Can a taxpayer, a landowner who enters into a conservation covenant, be entitled to an income tax deduction under Division 31 of the Income Tax Assessment Act 1997 (ITAA 1997) where it benefits because of the covenant? <https://www.ato.gov.au/law/view/document?DocID=AID/AID2002678/00001&PiT=99991231235958>

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

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

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