Submission by

The Nature Conservancy, Australia

to the review process for

"Australia's future tax system"

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The Nature Conservancy, Australia

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The Nature Conservancy

The Nature Conservancy is a leading conservation organization working around the world to protect ecologically important lands and waters for nature and people. Founded in 1951, TNC now works in more than 30 countries.

The Mission of The Nature Conservancy

The Nature Conservancy's mission is to preserve the plants, animals and natural communities that represent the diversity of life on Earth by protecting the lands and waters they need to survive.

How We Work

Science-Driven

The Conservancy uses a strategic, science-based approach to conservation, identifying and protecting the highest-priority places— landscapes that, if conserved, ensure the diversity of life on Earth over the long term.

Tools & Tactics

Private Lands Conservation and Restoration
Funding for Conservation
Conservation-Friendly Public Policies

Collaboration

We work closely with partners, corporations, government agencies, indigenous people and traditional communities. Our non-confrontational, collaborative approach yields balanced results that benefit the environment and local communities.

Australia Priorities

- Northern Australia Grasslands
- Central Australia Aridlands
- Mediterranean Woodlands: Gondwanalink Project
- Freshwater Systems: Murray-Darling Basin

Achievements

- Protected 47 million hectares of habitat worldwide
- Named as a U.S. top 15 charitable institution
- Support from millions of individuals, foundations, and corporations
- More than 400 offices worldwide
- More than 1,500 volunteer trustees
- Pioneered land protection techniques such as debt-for-nature swaps and covenants

Request for Direct Consultation

The timing of a wholesale tax review, coinciding with the strong commitment of the Rudd government to expanding the national conservation estate, offers a unique opportunity to design and implement good incentives for biodiversity conservation.

The Nature Conservancy’s Australia Program is currently working with the Department of Environment, Water, Heritage and the Arts to accelerate the establishment of private protected areas in Australia and as part of this work intends to examine the financial incentives, including tax and transfer instruments, for land conservation. Accordingly, we would appreciate a discussion with the tax review panel to ensure there is adequate alignment between the two processes.

Introduction

The Nature Conservancy Australia welcomes the review of Australia's tax system and the potential for designing a system that will "position Australia to deal with the demographic, social, economic and environmental challenges of the 21st century."

We applaud the inclusion of environmental considerations in this review, however, we note with concern the extremely limited discussion of the environment in the architecture report (released on August 6, 2008) except with reference to assistance for households in the transition period to higher-priced carbon under the Carbon Pollution Reduction Scheme (CPRS).

From our reading of the architecture report, we see the limited references to "environmental taxes" being those typically conceived as a tax on pollution—a mechanism for raising the price of pollution and correcting a negative externality. We wish to see a far more sophisticated discussion of the environment in the tax-transfer review, particularly in relation to biodiversity. This submission intends to offer some suggestions for this discussion, and therefore contribute to the agenda for the tax review.

We would like to point out that the issue of taxes and transfers with regard to the environment is a discussion that covers all uses of natural resources and all types of pollution. It is a discussion that cuts across cultural, social and welfare issues and, since the environment is our natural resource base, it is a discussion about the basis of our economy. We acknowledge that the tax-transfer system can play many roles in raising revenue, correcting market failures, providing public goods and influencing behaviour through incentives.

We note that the review of the tax-transfer system also occurs at a time when there is great interest and hope in market-based instruments (MBIs) to correct market failures around the environment and we support the ongoing development of these instruments. We also note, however, that the development and application of markets for biodiversity conservation and ecosystem services may be slow, incomplete and, as we have seen in the burgeoning carbon offsets market, difficult to regulate. The application of MBI's for biodiversity in particular has been inadequately funded, and ad hoc in approach. Therefore the establishment of markets for biodiversity offsets and water allocations will not be sufficient to achieve the policy goals. In all likelihood, environmental policy will remain a mix of MBIs, regulation, education and financial incentives provided through the tax-transfer system.

All Australian governments recognize biodiversity conservation and ecosystem services as high-value, essential public goods, and in this submission we will argue for the use of the tax-transfer system as a mechanism for enhancing the provision of those public goods. In particular, this submission will address the need for effective tax treatment of environmental philanthropy, ensuring that the establishment and management of protected areas on private land are encouraged and supported by the tax system.

In accepting this premise, the goals of the tax-transfer system should then include:

a) Sharing the costs of conservation equitably using tax revenue, and
b) Using transfers (direct payments or tax concessions) as incentives to encourage positive externalities (i.e. environmental philanthropy).

We acknowledge that environmental taxes may be used to correct negative externalities/ change negative behaviours (i.e. taxes on pollution), but, given that this is already on the agenda for the tax review we will not discuss this here.

Conservation and ecosystem services are a high-value essential public good.

Aside from cultural and recreational amenity, conservation of our environmental assets—our lands and waters—allows for the ongoing functioning of broad-scale ecological processes. These ecological processes provide critical ecosystem services including: carbon sequestration, prevention of carbon release from vegetation clearing, regulation of surface and underground waters, provision of clean water, maintenance of fertile soil, climate regulation, crop pollination and, not least, the very oxygen we breathe. Furthermore, the economic activities that depend on natural areas and natural processes —including agriculture, tourism and fisheries— will be significantly impacted if natural areas are allowed to continually decline.

More conservation is needed: Private provision of a public good.

Some conservation is provided in Australia by the government directly in the form of national parks and similar protected areas. However, it is now widely recognised that much, much more is needed if conservation of biodiversity is to be effective. Our climate change safety net must take the form of conservation and environmental management across entire landscapes to ensure that a viable amount of the systems are conserved, in a connected way that allows the migration and evolution of flora and fauna, and are managed in such a way that the condition of these systems is maintained or improved. Only this can give some assurance of a natural system that will be able to adapt to climate change impacts.

All Australian governments have committed to establishing a comprehensive, adequate and representative (CAR) reserve system, in line with Australia's commitments under the Convention on Biological Diversity. However, it is recognized that land purchase is expensive and many high priority areas for protection occur on private land. The expansion of Australia's conservation estate, and associated sustainable land management practices, is not possible without large-scale private contributions of land, time and money.

Of a total of 8,800 protected areas in Australia, almost 2,000 are private protected areas. These are either covenants placed on the title of the land by landholder, or properties acquired and managed by an NGO or community group. (note: this does not include indigenous protected areas). It can be seen that Australians are already generous environmental philanthropists, but the level of activity is still insufficient.

When the tax system was created in 1937, the value of these ecosystem services was poorly understood, and conservation was conceived as the setting-aside of pockets of wilderness for amenity, recreation and spiritual well-being. Over subsequent decades, taxes and transfers were designed according to the social objectives of sustaining rural communities and increasing national productivity. Society's understanding of the role of conservation has shifted enormously in the decades since the initial design of Australia's tax system: we now understand that ecological processes are our life support systems, and that their decline will be more costly than we can imagine.

> *"Australia is now facing a different set of challenges. The breadth of this review provides an opportunity to step back from the day-to-day processes and historical events that have shaped the tax-transfer system. It is an opportunity to consider how the system might best be shaped to complement, and even facilitate, the reforms needed to address the challenges facing Australia as we move through the 21st century."*

We need to fundamentally rethink the role of conservation as a high-value public good and economic service, and consider how best to use the taxation system to share the burden of this cost amongst the wider community. Private conservation lands must be actively encouraged as a critical contribution to our "safety net" in the face of climate change and rapid biodiversity loss. Again, it is fundamental to achieving our international obligations under signed treaties such as the Convention on Biological Diversity. The new tax-transfer system for Australia must provide a consistent set of incentives that recognise the value of biodiversity to our society, and the contribution that private conservation makes to the broad public good.

Tax-transfer system as a mechanism for sharing the cost of conservation

The tax-transfer system provides a mechanism for sharing the cost burden of environmental management and conservation amongst the beneficiaries. In many cases, private individuals are contributing environmental goods which benefit the wider community (such as carbon storage, water cycle regulation and endangered species protection), but the cost is borne entirely by the individual.

As the social value of conservation increases, so does the minimum duty-of-care of landholders. As we more clearly understand the services that ecosystems provide, we are better able to distinguish public goods and private goods that result from conservation, and to apportion a share of the costs of conservation equitably amongst the beneficiaries.

Tax-transfer instruments for enhancing environmental philanthropy

> *"Rather than depend upon public acquisitions of sites of high conservation value, which is expensive, there is an important opportunity to use tax incentives to encourage philanthropic investment in conservation. Philanthropic investment offers the opportunity to achieve the same outcome at much less cost to government."* (Binning and Young 1999.)

Tax-transfer instruments provide a means for creating incentives for private philanthropy of a public good and to achieve government objectives in a cost efficient manner. As has been acknowledged above, private individuals and organisations provide conservation in ways government cannot. It is highly desirable for the government to provide signals and support for environmental philanthropy, and an efficient means to do this is through tax concessions. Tax support for environmental philanthropy is important for a couple of reasons:

- It reduces the cost of giving a gift, so that donors give more.
- It provides a tangible signal that altruistic giving is socially valuable. (Allen Consulting Group 2002.)

Further to these reasons, government support for environmental philanthropy, when effectively targeted to achieve policy goals, leverages government expenditure and ensures the provision of the public good.

Australia's future tax-transfer system should work to encourage environmental philanthropy, including the following activities:

1. **Establishment of conservation covenants or conservation management agreements on private land:** a key mechanism for private land conservation is the establishment of a perpetual conservation covenant on the title of land, or an agreement to manage the land for biodiversity conservation.
2. **Donation of land to conservation organisations:** Landholders often donate parcels of land to an environmental organization or state/territory government for addition to the public protected area estate. Provisions should allow for the following types of gifts:
   a. **Outright donation:** land is donated outright as a property gift to the recipient organisation.
   b. **Part gifts:** A bargain sale is made when a donor sells property to an eligible organization or government at a discount. This discount is recognized as a gift for tax purposes, allowing for situations where the property is strategically important, and when the donor cannot afford to make an outright donation.
   c. **Living bequests:** A living bequest is when the donor wishes to see the property under the management of a conservation group or government and donates the property, but retains some rights over the property until their death.

3. **Ongoing conservation management works:** Maintaining and improving the condition of biodiversity in an area, and promoting the functioning of ecosystems often requires substantial outlay for expenses such as: preparation of management plans, biodiversity surveys, fencing, weed and feral animal control, and re-vegetation works.

Problems with the current system

The existing tax-transfer system was the result of decades of policies clearly designed to promote productive land use. The result for conservation has been very poor: private conservation activities are the least tax-favoured land-use, (Douglas 2002; Binning and Young 1999) and the current tax-transfer system creates perverse incentives that prevent the achievement of conservation outcomes.

In August 2001 the Australian Government announced changes that addressed a number of impediments to private conservation in Australia with an amendment to the *Income Tax Assessment Act*. (Commonwealth Taxation Laws Amendment Act (No.2) 2001.) However, these changes fall well short of the mark in providing adequate incentives for conservation, and both substantive and technical barriers remain.

1. **Differential incentives on low-income individuals:** The tax treatment of gifts of property, and the establishment of conservation covenants was substantially improved in the last decade, with recognition of the value of the donation allowable as a tax deduction, apportionable over up to 5 years. However, this mechanism along with the changes in income tax marginal rates has resulted in lower incentives for a group of donors who own land, but who may have a low income. Land-rich, cash-poor landholders will not realise the full value of the tax deductibility as will a more affluent landholder. Anecdotal evidence suggests the low uptake of landowners seeking a tax concession for any of loss in value on their property as a result of the covenant[1] was in part due to the costly and bureaucratic nature of the valuation with little guarantee of a real loss in property value. This provision is also inconsistent with the broad message given by covenanting programs that a covenant does not usually result in a loss in property value (see Fitzsimons and Carr 2007).

2. **No recognition or support for conservation works:** Under the current tax system these expenses are not tax deductible unless they are directly related to the commercial use of that land (such as an eco-tourism resort). The incentive effect clearly means landholders will be encouraged to put or keep land in production rather than conserve it.

3. **Lack of clarity around part-gifts, living bequests and flexible approaches to environmental philanthropy**. Currently in the tax system there is a lack of clarity around the more flexible approaches to environmental philanthropy which include living bequests and part-gifts or bargain sales, thus providing a barrier to participation in these activities. Further, tax deductions are not available to people donating land to governments for the addition to the public protected area estate when, in many situations, this is more desirable than donating to an environmental group under the Register of Environment Organisations (e.g. where land adjoins a national park).

What reforms are needed to address those problems?

These recommendations are made within the context of the current tax-transfer architecture as minimum steps that must be taken to provide acknowledgement and incentives for environmental philanthropy and private conservation.

1. Ensure tax treatment of conservation land is *at least* on a par with productive land use.

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[1] See http://www.environment.gov.au/biodiversity/incentives/covenants-tax.html

- Expenditure on conservation works in accordance with a management plan should be fully tax deductible against income (not capital). This can be conceived on the basis of conservation works being a philanthropic public good, and thus should be treated in the same way as a philanthropic donation OR it can be conceived as essential works for maintaining the economic productivity of ecosystems and land. Either way, it should be fully tax deductible.

2. Ensure equity of tax benefits and recognize everyone's contribution.
- Remove the differential disincentive on donors in a lower marginal tax bracket by considering tax rebates or tax credits, rather than direct deductibility for gifts and conservation management expenses.
- Allow apportionment of deductions or rebates on gifts of property (covenants or land) over a longer time frame, for example 10 or 15 years rather than 5 years.

3. Allow flexibility in "gifts" of environmental philanthropy.
- Clarify the tax treatment of living bequests.
- Recognise 'bargain sales' or 'part gifts' as tax deductible.

4. Improve the unwieldiness of current tax concessions for covenants and consider alternatives
- Recognise the unwieldiness of the current provision for applying for a tax concession for any loss in value on a covenanted property, and that even if this process were made easier it may not act as an incentive as a loss in value may not be realized.
- More direct financial incentives such as subsidizing local governments to provide exclusions from rate payments for covenanted properties may be a more direct and tangible incentive.

The issue of tax treatment of private conservation and environmental philanthropy has been repeatedly investigated over the last 10 years in policy research in Australia, resulting in a substantial body of work. In addition, the experience of over 40 years of private conservation and the development of a strong civic philanthropy culture in the United States can usefully inform this process. Key references are listed here in the Appendix. These references have been compiled and are available from The Nature Conservancy.

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