Income tax and environmental provisions – green gold or lead weight?
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Abstract
The mine site rehabilitation, land degradation and environmental protection activities income tax provisions are three tax expenditures that are able to assist environmental management. While environmental policy may not have necessarily been the impetus for their introduction, it has been a factor in their development over time. Using the policy behind each tax expenditure, derived from its history, this paper attempts to analyse their effectiveness with respect to environmental consequences and in meeting the associated costs of mitigation and/or rectification. However, a lack of quality data is an impediment. A conclusion that is drawn is that Australian tax policy is subject to the influence of various groups at any point in time resulting in a lack of clear direction and restrictive appeal. This then raises the question: income tax and environmental provisions – green gold or lead weight?

1. Introduction
The primary function of the income tax system is to raise revenue to fund the general functions of government. Equally, the taxation system can be used to assist environmental management.

As a rule expenditure on the environment is not deductible from income tax unless it is related to the earning or production of income or a specific tax expenditure applies. The term ‘tax expenditure’ refers to any provision of the tax law which provides a financial benefit to a particular class of taxpayer or a particular activity in the form of a tax preference or concession, most commonly as an exemption, deduction or offset1.

Income tax provisions that are able to assist environmental management are characterised by being expenditure that is not incurred in gaining or producing assessable income and not necessarily incurred in a business for such purpose. This paper discusses three specific provisions in terms of policy and environmental outcomes. These are mine site rehabilitation, land degradation and environmental protection activities. The former attempts to integrate tax and environmental concerns into policy that is industry specific, the latter is activity specific while the second has evolved into a hybrid of industry and activity specificity. After an introduction to each tax expenditure, their history is outlined drawing particular reference to community and governmental discussion prevalent at each stage of evolution. From this, the policy behind the tax expenditure is determined and/or inferred. This is followed by an analysis of the environmental consequences including cost versus benefit. The paper concludes with a comparative analysis and conclusion.

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2. Income tax and environmental policy

The Australian federal government uses taxation policy to encourage environmental responsibility. This is consistent with numerous Organisation for Economic Cooperation and Development (OECD), United Nations (UN) and World Bank reports that advocate the use of ‘economic incentives to correct market failure in the management of natural resources and the control of pollution’.2 Indeed, the arguably preeminent report on sustainable development, Our Common Future (also referred to as the Brundtland Report), espoused that, in order to implement ecological sustainable development, public policy should make use of incentives to encourage the business sector to refrain from polluting where ‘[p]ollution is a form of waste, and a symptom of inefficiency in industrial production’.3 The term ‘polluting’ is not restricted to carbon emissions but also incorporates land degradation and other environmental damage.4

Similarly, it is recognised that ‘the sound management of private land may have to be encouraged by law’ such as through the provision of taxation incentives5 and that tax policy should be used to encourage sustainable land use.6

The use of tax policy to encourage investment in natural resources is a contentious issue as some taxpayers obtain a benefit not available to all. Yet the tax system has also been described as an appropriate tool for governments to implement policies requiring the expenditure of funds to achieve specified policy goals.7 A tax expenditure is a form of government spending. It is also contentious from an environmental perspective: those who abstain from polluting or damaging the environment are not rewarded whereas those who have polluted receive a reward through the tax expenditure.

Historically, the literature has tended to focus on stand-alone environmental taxes and charges, generally referred to as ‘green taxes’. These have generally been premised upon the ‘polluter pays’ principle and have attempted to allocate a market price to the environmental activity or item being taxed. The use of tax expenditures is an alternative policy tool that utilises the income tax system to deliver environmental goals. As such they are the result of selective tax legislation that benefits particular taxpayers. Since the government foregoes revenue that would have been collected in

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6 Hatfield-Dodds S, Address to the Fourth Annual Global conference on Environmental Taxation, Sydney, June 2003.
the absence of the special legislation, these policies have real costs, hence the term ‘tax expenditures’.

The financial impact to the government depends on three factors: the size of the eligible industry or activity, the magnitude of the allowable benefit and the rigour in which eligibility is interpreted and enforced. The benefit is more difficult to quantify as it concerns the provision of public goods which generally do not have attributed market values.

The advantage of taxation-based measures is that they provide support for environmental projects where the private benefits are less than the overall cost of the project. Without such support, these projects may not be undertaken. They also encourage innovation, whether in technology or business practices, in order to achieve the government’s policy goals. The alternative is for the government to impose a system of command and control that is generally difficult to establish and expensive to maintain.

Providing a tax expenditure for an activity has the dual impact of reducing the net benefits received from the activity and the net costs incurred in undertaking the activity. In effect, the tax system results in the community sharing financially both the costs and benefits of taxed activities. If it is assumed that all benefits and costs of an activity are financial and there are no externalities, including an activity within the tax system will reduce the private net return from the activity if it is profitable, and increase the private net return if the costs exceed the benefits (that is, reduce the private loss). Thus, the community will not only share in the gains from profitable activities but also share in the losses from unprofitable activities.

Tax expenditures are, however, generally difficult to target to environmental projects with public benefits. Indeed, they have been criticised as being ‘generally poorly targeted, always too difficult to cost, diametrically opposed to usual distributional goals, difficult to administer, structurally almost invisible and unaccountable”. Being ‘hidden’ in the tax system means that there can be an escalation of the tax expenditure without any explicit budgetary decision being made. The costs of tax expenditures are also more difficult to predict and monitor. These characteristics are evident in the discussion of the tax expenditures to follow.

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10 Ibid.
There is a public cost associated with using tax expenditures as policy tools. The question is whether the cost is worth the public benefit.

3. Mining site rehabilitation

3.1 Introduction

The rehabilitation of mining sites is now widely accepted by the industry as an integral and expected part of mining.\(^\text{14}\) It is also mandated through the requirement to lodge and maintain bonds or similar financial security as a condition for state licensing.\(^\text{15}\)

To be effective, a regulatory system for mine site rehabilitation should provide incentives to minimise damage, ensure sufficient funds are available to finance the rehabilitation, develop clear standards for rehabilitation and ‘ensure that mining companies receive equitable tax treatment with respect to the costs incurred’.\(^\text{16}\)

Contained in subdivision 40-H of the Income Tax Assessment Act 1997 (ITAA97), section 40-735 provides an immediate deduction for capital and non-capital expenditure incurred rehabilitating a mining site, subject to certain conditions. This provision is replicated in Appendix 1.

3.2 History

Mining companies are considered special taxpayers with income tax provisions expressly and exclusively for the industry. Section 40-735 is one such provision. To illustrate: A comparable expense to mining site rehabilitation is repairs, the tax treatment for which does not differentiate between taxpayers whether by industry or activity. While the distinction between capital and non-capital expenditure is irrelevant for the purposes of section 40-735, it is a major consideration in relation to repairs.

Referring to the mining industry as a special taxpayer, the 1975 Asprey Report said that the ‘nature of the taxation treatment of anti-pollution and ecological expenditure should be no different in relation to mining from that accorded to other industries’.\(^\text{17}\) Nevertheless, the Committee recommended that a provision for the estimated total costs of site rehabilitation should be available as a deduction from assessable income. It was suggested that this be subject to the Commissioner of Taxation being satisfied that such amount was a reasonable sum to meet the obligations of the mining


\(^{15}\) See, for example, Mineral Resources (Sustainable Development) Act 1990 (Vic) Part 7.


enterprise. It also recognised the difficulty of the tax system to allow deductions for expenses typically incurred once income-earning operations had ceased.

Deductibility for mine site rehabilitation expenditure was inserted into the Income Tax Assessment Act 1936 (ITAA36) as division 10AB with effect 1 July 1991\(^{18}\) (but without the Commissioner of Taxation being de facto \textit{auditor}). This had been announced in the 1990-91 Budget\(^{19}\) on 21 August 1990.

The Budget announcement was followed by the release of a three-volume report by the Industry Commission in February 1991: The Industry Commission Inquiry into Mining and Minerals Processing (Inquiry).\(^{20}\) Commissioned by the then Treasurer, Paul Keating, on 18 October 1989, the Inquiry into the mining industry was broad, covering factors affecting minerals exploration and development, operating costs and access to technology while having regard to social and environmental objectives, the commonwealth/state arrangements and taxation structures and efficiencies. The Inquiry recommended that mining site rehabilitation expenditure be tax deductible, including the demolition of old plant. It also recommended the carry-back of such expenditure in financial years where there was insufficient income available. Only the first recommendation was adopted.

As part of the 1997 Tax Law Improvement Program (TLIP), division 10AB ITAA36 was rewritten into ITAA97 as subdivision 330-I.\(^{21}\) It was subsequently rewritten (in 2001) as subdivision 40-H ITAA97 as part of the uniform system of capital allowances post the 1999 Ralph Review of Business Taxes.\(^{22}\)

Five years after its introduction and reflecting increasing societal concern, the Minerals Council of Australia, as the industry peak body, developed the Australian Minerals Industry Code for Environmental Management as a self-regulatory tool.\(^{23}\) By 1998 41 companies had signed the code and were producing publically available environmental performance reports.\(^{24}\) The Australian Minerals and Energy Environmental Foundation went on to establish an award system for environmental reporting within the mining and energy industries.\(^{25}\) Mandatory environmental reporting for eligible entities was also introduced in 1998 under what was then the Corporations Law.\(^{26}\)

At an international level and in line with increasing community and societal environmental concerns on a meaningful scale, there were three major areas of

\(^{18}\) As part of Taxation Laws Amendment Act (No 2) 1991 comprising ss 124BA to 124BF.


\(^{20}\) Industry Commission, above n 14.

\(^{21}\) Comprising ss 330-435 to 330-455 ITAA97.


\(^{24}\) Ibid.


\(^{26}\) Corporations Act 2001 s 299(1)(f).
development within the mining industry with respect to sustainability and the environment.

In 1991, the UN and the German Foundation for International Development organised the International Round Table on Mining and the Environment in Berlin. This resulted in the ‘Berlin Guidelines’, published in 1994 and revised in 1999. While the original guidelines focused on the technical and physical aspects of environmental management, the revised version reflected a greater understanding of, and concern for, social and community issues that had developed internationally over that decade. Item 13 of the Berlin Guidelines states that governments should ‘[e]valuate and adopt, wherever appropriate, economic and administrative instruments such as tax incentive policies to encourage the reduction of pollutant emissions and the introduction of innovative technology’.

In June 1994 the World Bank and two UN agencies organised the International Conference on Development, Environment and Mining. A key point noted was that the ‘objective of rehabilitation of mine sites should be to restore them to a self-sustaining ecosystem that is as close as practical to its original state prior to mining activity.’ The need for mechanisms to ensure the available of funds to finance rehabilitation was also stressed. A number of international conferences and workshops are now run regularly.

The Global Mining Initiative was launched in 1998 by the chief executive officers of nine of the largest mining and metals companies. This was perhaps the earliest large-scale industry-based effort to establish sustainability practices in the sector. Out of this came the Mining, Minerals and Sustainable Development project in 2000 (a fact-finding mission) and the International Council on Mining and Metals in 2001.

3.3 Policy

Towards the end of the last century, and in particular from the early 1990s, there has been increasing societal concern over environmental issues. These community
concerns have influenced policy from both the company and government perspectives and have led to increasingly stringent regulations governing activities that have an impact on the environment.\textsuperscript{34} In its submission to the Inquiry, Coal & Allied Operations Pty Ltd acknowledged that many of the constraints imposed on the industry resulted from community concerns with respect to environmental management and rehabilitation of mining sites.\textsuperscript{35}

The Explanatory Memorandum (1991 EM) accompanying the introduction of the provisions notes that ‘rehabilitation expenditure should form part of the overall costs of the mining operation’ [emphasis added].\textsuperscript{36} The reasoning is that a right to quarry or mine is dependent on agreement to rehabilitate the site after operations have ceased. Rehabilitation requirements for mining projects are written into the laws of state and territory governments as a prerequisite for the issuance of exploration permits or mining leases. Environmental bonds ensure that funds are available for rehabilitation in the event of non-compliance. Yet no tax deduction is available for these.

The reasons as to why a special deduction was warranted were provided by in the 1991 EM. It acknowledged that the majority of rehabilitation expenditure is capital in nature and therefore does not qualify for deduction under the general deduction provision. For capital expenditure to be deductible, it is restricted to expenditure incurred in the process of extracting minerals. This clearly excludes rehabilitation expenditure. And, in any event, such expenditure is generally incurred once the income earning operations have ceased and therefore excluded from deductibility as not being incurred for the purpose of producing assessable income.

But then again, certain expenditure may be non-deductible, not because of government policy but simply because the importance of the expenditure was not previously realised.\textsuperscript{37} That is, there is a time lag between business practice and legislation.

The deduction is restricted to the restoration of the site to its pre-mining condition or to a reasonable approximation thereof. The only latitude is to use the condition of the surrounding land (also at the time the operations or activity commenced) as a guide and only if the original condition of the site is unknown – not in place of or as a substitute for. It is also worth noting that partial site rehabilitation is deductible expenditure, even if there is no intention that the work be completed.\textsuperscript{38}

\textsuperscript{34} Allen et al, above n 33.


\textsuperscript{36} EM 1991, above n 19, ch 13, cl 2.


\textsuperscript{38} Subsection 40-735(5) ITAA97.
The concept of ‘site’ is also restrictive. The deduction is limited to expenditure incurred in rehabilitating only that area where the exploration and/or mining operations were conducted, that is, the ‘mine site’. Although not specifically stated, it is probably fair to state that the area considered to be the ‘mine site’ is that area covered by the exploration permit or mining lease. Expenditure spent rectifying any other area, although damaged by the mining operations, does not qualify for the deduction.39

Rehabilitation expenditure is not, however, limited to mining sites. Typical examples are the removal of plant, equipment and facilities from ‘off-site’ areas that are, in other contexts, considered to be part of mining operations.40 Examples include trunk lines, access roads, storage facilities, wharves, conveyors and railways.

Then there are areas even more removed from the actual ‘site’ but nevertheless impacted by the mining operations. An example is the Ok Tedi copper and gold mine in Papua New Guinea. The seventy-kilometre corridor of the Ok Tedi River has been declared ‘biologically dead’ and 150 square kilometres of Fly River floodplains downstream potentially affected by acid mine drainage.41 Australian examples include Queensland’s Mount Morgan gold and copper mine which has devastated the aquatic ecosystem of the Dee River42 and Tasmania’s Mt Bischoff tin mine which has created a ‘Dead Zone’ in the upper 30 kilometres of the Arthur River.43 These outlying areas cannot be considered to be with the mine ‘site’.

It was noted above that the mining site rehabilitation provision has been rewritten twice since its introduction. TLIP introduced a minor policy change by widening the deduction to include the cost of constructing dams and levees as part of the rehabilitation process.44 When explaining subdivision 330-I, the Explanatory Memorandum (1997 EM) stated that the dams and levees must be ‘essential for rehabilitation’.45 The justification is that they are an essential part of the rehabilitation process and have little or no residual value to the rehabilitator and, as a result, should not be treated as an enhancement or redevelopment. The 1997 EM gave dams as a means of securing a water supply for revegetation as an example of a dam ‘necessary for proper rehabilitation’.46 As such, tailings dams and dams for recreational purposes would not be deductible.

40 Birch C, ‘Rehabilitation Expenditures – does the law need cleaning up’ (1999) (Nov-Dec) *Journal of Australian Taxation* 401-418. See also FCT v Reynold Australian Alumina 90 ATC 5018 which concerned a bauxite conveyor and Robe River Mining Co Pty Ltd v FCT 90 ATC 5028 which concerned an iron ore railway.
46 Ibid, 102
Not all issues relating to defining a mining site and what constitutes rehabilitation expenditure have been presented. Nevertheless, it is submitted that the above discussion demonstrates that rehabilitation expenditure incurred by mining operators is treated preferentially within the income tax legislation. It is also limited in its environmental features.

The policy behind legislative provisions is not always specifically stated. In such cases it can usually be gleaned from the history leading up to the legislation, from the explanatory memorandum accompanying the legislation and from the wording of the provision itself. With respect to the mining site rehabilitation provision, it would appear that the policy behind section 40-735 is more commercial than environmental. It has even been suggested that its purpose was to ‘[correct] an anomaly of the tax system as it applies to the natural resources industry’.47

3.4 Analysis

Rehabilitating a mining site serves an environmental purpose. However, section 40-735, as currently drafted, fails to deliver.

The provision does not achieve full deductibility for rehabilitation expenditure. There are two aspects to this: the specified exclusions and the result of the restrictive interpretation of terms such as ‘rehabilitation’ and ‘site’ are defined. What qualifies as deductible expenditure is defined narrowly; the majority of major environmental disasters arise off-site. Further, permitting partial rehabilitation with no penalty for non-completion, especially intentional non-completion, is clearly contrary to environmental principles.

Tailings dams are often the most significant environmental liability yet these are specifically excluded. Tailings dams store waste material from mineral processing at mine sites.48 A lack of tailings dams resulted in the Ok Tedi disaster, damaging agricultural land and displacing entire communities. The Los Frailes disaster in Spain in April 1998 caused approximately €152 million in socio-economic losses and approximately €147 million was spent correcting the environmental and agricultural impacts, including restoration of the area’s natural resources.49 This does not include the subsequent impacts on communities and local industries. Closer to home is Mount Todd. The company went into receivership leaving behind a tailings dam of acid water and heavy metals. The environmental bond of $900,000 was forfeited but, even with the additional $5 million spent by the Northern Territory government, financing remediation has hardly begun.50

The actual cost of section 40-735 cannot be accurately ascertained as it is not included in Treasury’s Tax Expenditure Statements. While there is little detailed information,

47Stolianoff et al, above n 23.
49Ibid.
the estimates vary substantially. This may be because rehabilitation expenditure is mine-specific. As examples, it is estimated that rehabilitating March Mining at Moliagul would cost $1 million, Denehurst at Benambra $7 million and Mount Todd in the Northern Territory in excess of $100 million.  

In the Mine Closure and Rehabilitation Plan of the Wonarah Phosphate Project it is stated that ‘[i]t is not economically viable to backfill all open pits’ with costs ‘in excess of $250 M’. Estimated closure costs are $43.5 million, but, as outlined in table 1, not all items would qualify for a deduction under section 40-735.

<table>
<thead>
<tr>
<th>Domain</th>
<th>Estimated cost ($AUD)</th>
</tr>
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<tbody>
<tr>
<td>Site infrastructure</td>
<td>$2,436,231</td>
</tr>
<tr>
<td>Extractive workings</td>
<td>$368,890</td>
</tr>
<tr>
<td>Hard rock pits</td>
<td>$28,303,722</td>
</tr>
<tr>
<td>Water dams and ponds</td>
<td>$12,540</td>
</tr>
<tr>
<td>Waste rock storages</td>
<td>$2,367,500</td>
</tr>
<tr>
<td>Exploration</td>
<td>$2,183,800</td>
</tr>
<tr>
<td>Access and haul road</td>
<td>$1,851,120</td>
</tr>
<tr>
<td>Sub total</td>
<td>$37,523,803</td>
</tr>
<tr>
<td>Post closure monitoring</td>
<td>$187,495</td>
</tr>
<tr>
<td>Contingency (5%)</td>
<td>$5,656,695</td>
</tr>
<tr>
<td>Total (nearest $500,000)</td>
<td>$43,500,000</td>
</tr>
</tbody>
</table>

Table 1: Summary of estimated closure costs for Wonarah Phosphate Project

State governments have developed rehabilitation cost calculators to provide a consistent methodology for estimating rehabilitation costs. However, there is no requirement that they be adhered to and the calculations are only randomly audited. An example is the White Dam Gold Project in South Australia where the miner has adopted a rehabilitation rate of $800 per hectare and an ongoing maintenance rate of $140 per hectare against the calculator’s rate of $4,070 per hectare and $715 per hectare respectively.

53 Ibid, 59.
There is limited publicly available statistics on mine site rehabilitation costs from the Australian Bureau of Statistics. The most recent relates to the 2000-2001 financial year where current expenditure amounted to $97.7 million or 0.3 per cent of total current expenses, and capital expenditure amounted to $7.4 million being 0.2 per cent of total capital expenditure. On a per hectare basis this is approximately $2,050 (current) and $145 (capital). For these purposes, ‘rehabilitation’ includes landscaping, re-vegetation and removal of buildings, fixtures and equipment to a reasonable approximation of its pre-mining condition. The only other information relates to capital rehabilitation expenditure of $22.7 million (1994-1995) and $15.7 million (1995-1996). It would appear that there is a year-on-year decline in capital rehabilitation expenditure which may be the result of more rehabilitation work being done while the mine is still operative, that is, more current than capital expenditure. Further research is required to test this hypothesis.

When section 40-735 was introduced, the cost to the revenue was expected to be $10 million per annum from the 1992-1993 income year. Taking into account the removal of the Bass Strait oil platforms, the cost was expected to increase to around $40 million a year from early 2000s. However, the actual or estimated expenditure far exceeds the original projections. Being specific to mining, the mining industry is being subsidised to help it meet the costs of mining site rehabilitation.

It is also informative to examine the relationship between mining earnings and expected rehabilitation expenditure. In a 2001 report prepared for the Department of Industry, Science and Resources, the Australian Bureau of Agricultural and Resource Economics (ABARE) stated that annual provisions for rehabilitation expenditure (as determined by the value of rehabilitation bonds) had risen from around $160 million to $285 million in the decade while gross value of mine production for the 1998-99 income year equated to $34,566 million. Expected rehabilitation expenditure represented only 3.3 per cent of the gross value of production. By 2011 the expected expenditure was $420.7 million with 2009-10 industry operating profit before tax exceeding $50,000 million.

Two specific examples: the White Dam Gold Project’s forecasted rehabilitation expenditure represents a mere 0.02 per cent of its 2012 profit margin on production.

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59 Explanatory Memorandum, Taxation Laws Amendment Bill (No 2) 1991 (Cth) 5
61 Allen et al, above n 33.
The Wonarah Phosphate Project, on the other hand, has apportioned 0.0009 per cent of its projected net revenue from mining operations for the rehabilitation of the site.\textsuperscript{65}

From this it can be deduced that, generally and on average, expenditure incurred by the mining industry on rehabilitation costs is a small percentage of their profits. This, in turn, appears disproportionately low when compared to the cost incurred by governments in stabilising and/or rehabilitating abandoned mine sites. As previously mentioned, Mount Todd is expected to cost in excess of $100 million to rehabilitate. This seeming disparity and the insignificance in respect of total earnings raises questions of whether the industry needs government, and hence taxpayer, support.

\section*{4. Land degradation}

\subsection*{4.1 Introduction}

Over half of Australian agricultural land is considered degraded.\textsuperscript{66} A significant contribution to this has been the clearing of over 80 per cent of native vegetation.\textsuperscript{67} Environmental issues associated with land degradation include soil erosion, siltation and salinity. By definition, land degradation threatens the quality and quantity of soil resources\textsuperscript{68} which, in turn, threatens productivity yields and hence income.

While technological developments have compensated for reduced yields resulting from land degradation, studies have identified yield declines due to land degradation as high as 30 per cent.\textsuperscript{69} Gross output on farm production in 2009-2010 was $48.7 billion,\textsuperscript{70} nearly double the $25 billion in 2003-2004.\textsuperscript{71} Yield declines of even one or two per cent on adversely affected farmland would result in significant lost revenue even apart from the environmental consequences of poor land management. The threat to the viability of Australia’s agricultural industries resulting from land degradation can be put another way: degradation costs $1.5 billion annually in lost production or around six per cent of agricultural production.\textsuperscript{72}

The importance of native vegetation, food security and pristine landscapes to future generations cannot be evaluated in monetary terms. Yet the benefits are increasing as the adverse affects of excessive clearing become more defined.\textsuperscript{73} As a result, there are clear arguments in favour of public intervention in private rural and farmland management.

\begin{flushright}
\begin{itemize}
  \item \textsuperscript{66} Thomson N J, ‘Fiscal Incentives for Australian Bushland’ (1986) 10(5) \textit{Environmental Management} 591-597.
  \item \textsuperscript{67} Ibid.
  \item \textsuperscript{68} Such as top soil, embedded nutrients and moisture as well as soil biology.
  \item \textsuperscript{69} Junor R S, Marston D and Donaldson S G, ‘A situation statement of soil erosion in the Lower Namoi area’ (Soil Conservation Service of New South Wales, 1979).
  \item \textsuperscript{70} National Farmers Federation, ‘NFF Farm Facts: 2012’ (National Farmers Federation, 2012).
  \item \textsuperscript{71} Productivity Commission, \textit{Trends in Australian Agriculture} (Research paper, 2005).
  \item \textsuperscript{73} Thomson, above n 66.
\end{itemize}
\end{flushright}
Contained in subdivision 40-G of ITAA97, section 40-630 provides an immediate deduction for capital expenditure incurred, subject to certain conditions. This provision is replicated in Appendix 2 together with section 40-635 which defines the activities covered by the tax concession.

4.2 History

It would appear that, from the onset of the income tax legislation, primary producers were able to deduct certain capital expenditure expended on rural land. Even the first taxation Royal Commission, established on 24 September 1920 and chaired by Warren Kerr, inquired into, inter alia, special rules for primary producers, ‘particularly in relation to losses resulting from adverse weather conditions’.74

In reviewing available extrinsic legislative material, the first reference to deductions for capital expenditure for ‘improvements to pastoral properties’ was made in 1941 by the then Treasurer Chifley when discussing the ‘war tax’.75 The next reference, in 1958, specifically referred to section 75 ITAA36 as allowing a tax deduction to primary producers for the capital cost of ‘developing rural lands’ in Australia.76 That is, for the clearing, draining and otherwise preparing land for agriculture or pasture. It was made in the context of extending the boundary of ‘Australia’, for income tax purposes, to include the Territory of New Guinea in addition to the Territory of Papua.

In 1963 the definition of ‘primary production’ was extended to include ‘forest operations’.77 That forestry operations should be treated as primary production was an outcome of the Commonwealth Committee on Taxation (Ligertwood Committee). The amending legislation also extended the section 76 deduction for expenditure on fences to cover constructing or altering a fence to prevent animals pests entering land used in primary production and to mitigate the effects of deposits of mineral salts. Previously expenditure was only deductible if it was incurred on acquiring wire or wire netting and placing it in position on a fence.78

From 21 August 1973, it was no longer possible to obtain a section 75 deduction unless there was a pre-existing contract between the primary producer and a supplier of relevant goods and services. The expenditure would only be deductible either by way of depreciation under the general depreciation provisions or in equal annual instalments over 10 years in accordance with new section 75A.79 Within the scope of section 75A(1) was

(a) the eradication or extermination of animal or vegetable pests from the land;

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75 Treasurer Chifley, Second Reading Speech, Income Tax Assessment Bill (No 2) 1941.
76 Explanatory Memorandum, Income Tax and Social Services Contribution Assessment Bill 1958 (Cth) 1.
77 Explanatory Memorandum, Income Tax and Social Services Contribution Assessment Bill (No. 2) 1963 (Cth) cl 4.
78 Ibid cl 24.
79 Explanatory Memorandum, Income Tax Assessment Bill (No 5) 1973 (Cth) cl 17, 18.
(b) the destruction and removal of timber, scrub or undergrowth indigenous to the land;
(c) the destruction of weed or plant growth detrimental to the land;
(d) the preparation of the land for agriculture;
(e) ploughing and grassing the land for grazing purposes;
(f) the draining of swamp or low-lying lands where that operation improves the agricultural or grazing value of the land;
(g) preventing or combating soil erosion or flooding of the land; or
(h) conserving or conveying water for use in carrying on primary production on the land.

Section 76 was also terminated under the same terms as section 75 with the ordinary depreciation provisions applying to post 20 August 1973 expenditure.\(^80\)

These amendments were only to last seven years. In his policy speech leading up to the 1980 election, then Prime Minister Malcolm Fraser announced full tax deductibility for capital expenditure on soil conservation by a primary producer.\(^81\) This was costed at $1 million and became effective from 1 October 1980. The kinds of expenditure to benefit from this measure were those that were then deductible by way of equal instalments over 10 years and, for fencing, deductible under the depreciation provisions. Specifically, subsection 75A(1)(a), (c), and part of (g) relating to soil erosion were transferred to new section 75D as subsection (1)(a), (b) and (c).\(^82\) Section 76 became new subsection 75D(1)(d)\(^83\) while (e) and (f) related to capital expenditure incurred in the construction of levee banks or similar improvements having like uses and construction of measures to control salinity or assist in drainage control but not extending to the draining of swamp or low-lying land, respectively. Anti-flooding expenditure would remain in section 75A. Section 75D therefore became the ‘soil conservation’ measures.

Effective 23 August 1983, the land clearing provisions of section 75A were abolished.\(^84\) These were the initial clearing of land by the destruction and removal of timber, scrub or undergrowth indigenous to the land, the initial preparation of the land for agriculture, the ploughing and grassing of land to be used for grazing purposes and the draining of swamp land. The then Treasury Keating specifically stated that, while having no impact on deductions for capital expenditure on soil and water conservation, the amendment will ‘remove the encouragement through the tax system of environmentally and economically unsound activities’ and estimated to save $3 million a year.\(^85\)

The availability of the immediate deduction was tightened in 1985 by inserting a ‘primarily and principally’ test.\(^86\) Expenditure on all the subsection 75D(1) operations,

\(^{80}\)Ibid cl 19.
\(^{82}\)Explanatory Memorandum, Income Tax Assessment Amendment Act (No. 6) 1980 (Cth) cl 8, 9.
\(^{83}\)Ibid cl 4, 9.
\(^{84}\)Explanatory Memorandum, Income Tax Assessment Amendment Act (No. 4) 1983 (Cth) cl 7.
\(^{85}\)Keating P J, Second Reading Speech, Explanatory Memorandum, Income Tax Assessment Amendment Act (No. 4) 1983 (Cth) 5.
\(^{86}\)Explanatory Memorandum, Taxation Laws Amendment Bill (No. 4) 1985 (Cth) cl 12.
except for (e) being the construction of levee banks or similar improvements, now were required to be incurred primarily and principally for that purpose. This was to differentiate between expenditure that was deductible immediately (under section 75D) and that which was deductible over five years (under section 75B). Subsection 75A(h), dealing with conserving or carrying water had been enacted as its own section 75B in 1980 permitting full deductibility in the year the expenditure was incurred. Full deductibility was later withdrawn and replaced with deductions in equal instalments over five years.

At the same time as the introduction of the primarily and principally test, the scope of section 75D was broadened: references to ‘soil erosion’ and ‘salinity’ was replaced with ‘land degradation’. The Explanatory Memorandum explains that this term was intended to include the ‘decline of soil fertility or structure, degradation of natural vegetation, the effects of deposits of eroded material and salinisation’.

Significant amendments were again made in 1991 following the review of the Landcare objectives. They gave effect to the undertaking of the Government announced in the July 1989 Statement of the Environment and in the 1990-91 Budget. In the first place, section 75D was extended to all taxpayers who carried on a business on and from rural land, excluding mining and quarrying operations. Secondly, the deduction for the cost of fences was no longer limited to fencing already degraded land. Examples given were fencing off an area where the soil is lighter or where there is valuable native vegetation in order to prevent degradation through overgrazing. The only requirement being that the fences were erected in accordance with an ‘approved whole farm plan’, now referred to as a ‘land management plan’. The prevention of land degradation became the qualifying criterion.

As part of TLIP, the landcare provisions (as they were now referred to) were rewritten into ITAA97 as subdivision 387-A. While it was not intended to change its meaning, the rewrite did change the sentence structure and ordering. As with the mining site rehabilitation provision, the introduction of the Uniform Capital Allowance regime in 2001 applied to the landcare provisions. Contained in subdivision 40-G, this renumbering also did not change the effect of the special primary producer provisions.

The most recent significant amendments to the landcare provisions came in 2005. In the first instance, access to the tax concession was extended to rural land irrigation

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87 Six months prior to the enactment of section 75D.
88 Explanatory Memorandum, Income Tax Assessment Amendment Act (No. 3) 1980 (Cth) cl 4.5.
89 Explanatory Memorandum, Taxation Laws Amendment Bill (No. 4) 1985 (Cth) cl 11.
90 Ibid 52.
91 Originally a grassroots movement established in 1985, Landcare became a national program in July 1989 when the Australian Government, with bipartisan support, announced its ‘Decade of Landcare Plan’ and committed $320 million to fund the National Landcare Program.
92 Explanatory Memorandum, Taxation Laws Amendment Bill (No 2) 1991 (Cth) 127-128.
93 Ibid 128-129.
94 Explanatory Memorandum, Tax Law Improvement Act 1997, Ch 11. The corresponding provisions are sections 387-55 and 387-60.
96 Explanatory Memorandum, Tax Laws Amendment (2004 Measures No. 6) Act 2005, cl 6.7, 6.24. Other minor amendments are been made such as to some definitions to ensure consistency.
water providers. Secondly, the definition of ‘landcare operation’, used to determine eligible capital expenditures for the landcare tax concession, was amended to include repairs of a capital nature (in addition to alternations, additions and extensions already legislated for). This was further broadened to include a structural improvement, repairs of a capital nature, or alteration, addition or extension that is ‘reasonably incidental’ to the assets already deductible under a landcare operation associated with a levee or similar, or drainage works. The examples given by the Explanatory Memorandum are that of a bridge constructed over a drain that was constructed to control salinity or a fence constructed to prevent livestock entering a drain that was constructed to control salinity but not the bulldozer that was used to construct the drain.

As with all tax deductions, the largest benefit is received by those with the highest taxable incomes. Anticipated to benefit approximately 60 per cent of primary producers, a tax rebate for landcare expenditure was introduced in 1998 effective 1 July 1997. Projected to cost $80 million, the rebate was available for the same type of expenditures and over the same timeframe as the corresponding tax deduction. Targeted at low-income primary producers, the rebate was capped at $5,000 a year but, if unused, could be carried forward to future years. Its purpose was environmental in that it would ‘help reinforce landcare activities as an important and regular part of farm management …and continue the cultural change to sustainable natural resource management’ as well as to encourage ‘[investment] in landcare as a normal part of farm business’. However, in order to utilise tax offsets, one has to have surplus funds or a reasonable cash flow. As many low-income primary producers had neither, the offset was not used and subsequently repealed from 1 July 2001.

4.3 Policy

At an international level, the ratification of the UN Convention to Combat Desertification by 193 countries, including Australia, reflects a global consensus about the need to prevent and reverse land degradation. The land degradation between income tax law and the minerals resource rent tax. See Explanatory Memorandum, Minerals Resource Rent Tax Act 2012 cl 19.6.

provision was already well established when the federal and state governments endorsed the National Strategy for Ecologically Sustainable Development in 1992.\textsuperscript{103} This Strategy resulted in the establishment of the National Landcare Program, now the Caring for our Country initiative.\textsuperscript{104}

Section 40-630 ITAA\textsuperscript{97}, and its forerunner section 75D ITAA\textsuperscript{36}, provide a 100 per cent deduction in the year of expenditure for capital works that are primarily for the control or prevention of land degradation. This provision is designed to provide an incentive ‘to confront the problems associated with erosion, salinity and other forms of land degradation’\textsuperscript{105} and to encourage primary producers and users of rural land to undertake capital expenditure that assists in the long-term sustainable use of the land.\textsuperscript{106} The land degradation measures, also referred to as the Landcare provisions, provide an incentive for farmers and other businesses conducted on rural land to undertake capital works to combat land degradation. Being capital, they are explicitly designed to provide investment incentives.

The relationship between the land and the environment has always been a factor of Australian public policy. Determining the extent of land degradation and devising mitigation solutions has been on policy agendas for many decades and certainly predates the increasing societal concern over environmental issues from the early 1990s.

Throughout the progression from section 75 ITAA\textsuperscript{36} to section 40-630 ITAA\textsuperscript{97} there have been numerous government-initiated reports and inquiries regarding issues of land degradation and the articulation of policy agendas for sustainable resource management in the primary production sector, addressing key questions such as how to cost and treat land degradation.\textsuperscript{107} These included the development of land use policy,\textsuperscript{108} soil conservation policy,\textsuperscript{109} and public good conservation.\textsuperscript{110} The interrelationship between the economy and the environment was also prominent in these reports. For example, one government standing committee, when reviewing the impact of taxes on land degradation (among other areas), noted the lack of integration between economic and environmental policy making.\textsuperscript{111}

While concern about land degradation problems amongst Australian landholders is now well established, many do not recognise the multiplicity of subtle or insidious

\begin{thebibliography}{9}
\bibitem{105} Parliamentary Research Service, Taxation Laws Amendment Bill (No. 2) 1991, 2.
\bibitem{107} Examples include the 1971 Australian Standing Committee on Soil Conservation, the 1978 Commonwealth and State Government Collaborative Soil Conservation Study and the 1984 Department of Environment Conference on Conservation and the Economy.
\bibitem{108} Senate Standing Committee on Science, Technology and the Environment, \textit{Land Use Policy} (AGPS, 1984).
\bibitem{109} Department of Environment, Housing and Community Development, \textit{A basis for soil conservation policy in Australia} (Report No 1, AGPS, 1978).
\bibitem{111} House of Representatives Standing Committee on Environment and Conservation, ‘Fiscal Measures and the Achievement of Environmental Objectives’ (AGPS, 1987).
\end{thebibliography}
manifestations.\textsuperscript{112} In 1997 ABARE conducted an inquiry into the land degradation tax concession and its effect on the undertaking of landcare works.\textsuperscript{113} It found that the tax deduction was probably the most efficient tool available to provide broad-based incentives for landcare works with an uptake rate of around 60 per cent. Another study found that some form of landcare work is undertaken on more than one third of all farms.\textsuperscript{114} However, such landcare work may or may not be significant in terms of ameliorating land degradation.\textsuperscript{115} It is also important to note that reviews of landcare tax provisions acknowledge the argument that tax deductions provide greater benefit to primary producers with high taxable incomes.\textsuperscript{116} The regressive distribution of benefits under a system of tax deductions has also been recognised in other studies.\textsuperscript{117}

It is clearly evident that environmental policy played a major role in shaping the land degradation provisions not only in respect of the operative provision of section 40-630 but also in regard to the eligible activities listed in section 40-635.

\subsection*{4.4 Analysis}

From an environmental sustainability perspective, ‘landcare operations’ are defined narrowly as they do not cover expenditure, for example, in nature conservation areas.\textsuperscript{118} Further, it is unclear whether fencing off areas of bushland is included. While this was an example given by the explanatory memorandum introducing the 1991 amendments, the latter was qualified as being in order to prevent degradation through overgrazing.\textsuperscript{119} Areas of bushland have ecological importance even apart from their soil and water conservation values.\textsuperscript{120} In addition, without a definition of ‘pest’, the provision may provide tax deductions for eradicating or exterminating native animals as well as introduced species and for the clearing of native vegetation and regrowth.\textsuperscript{121}

Three activities most commonly cited by primary producers as deserving greater government assistance are soil and pasture improvements that cannot be claimed as operating expenses, catchment planning and protection of river corridors.\textsuperscript{122}

\begin{footnotesize}
\textsuperscript{113} ABARE, ‘Landcare Taxation Arrangements’ (Evaluation Report, Department of Primary Industries and Energy February 1997).
\textsuperscript{115} Cary and Thompson, above n 112.
\textsuperscript{116} Department of Primary Industries and Energy, ‘Review of taxation arrangements relating to the prevention and treatment of land degradation’ (Paper prepared for the Minister of Resources, March 1990).
\textsuperscript{118} Douglas, above n 9.
\textsuperscript{119} Explanatory Memorandum, Taxation Laws Amendment Bill (No 2) 1991 (Cth) 128-129.
\textsuperscript{120} Thomson, above n 19.
\textsuperscript{121} Douglas, above n 9.
\textsuperscript{122} Mues et al, above n 72.
\end{footnotesize}
Environmentalists, on the other hand, are more concerned that environmental issues, such as biodiversity loss, may not be sufficiently addressed.\textsuperscript{123}

A criticism that has been levied is that only activities conducted for profit-making purposes can be considered primary production; a non-profit organisation can never be a primary producer.\textsuperscript{124} This result is inevitable when using the income tax legislation to deliver environmental outcomes – taxable income is required in order to benefit from a tax deduction. A similar argument can be presented for hobby farmers. However land degradation does not discriminate between landholders. It is acknowledged that landholders who are not taxpayers only as a result of their land holdings\textsuperscript{125} need incentives to invest in natural resource management.\textsuperscript{126}

Arguable, the most acute problems associated with land degradation are sedimentation and salinisation.\textsuperscript{127} These are referred to as problems on non-point pollution, that is, it is either impossible or excessively costly to determine the contributions made by individual landholdings.\textsuperscript{128} It is therefore not feasible to penalise the primary producers individually for imposing external costs in direct proportion to the size of the costs. In one study it was estimated that 96 per cent of the external costs associated with dryland salinity are borne by the general community.\textsuperscript{129}

Problems such as these generate the largest off-farm costs. Incentives to landholders to invest in addressing landcare works would result in the greatest benefits to society, especially if these works would not be undertaken without the incentive. The impacts from land degradation extend beyond their geographical location and include issues related to food security and environmental health. However, it is difficult to accurately quantify the off-farm (or off-site) costs of degradation and hence equally difficult to match the level of incentive to the level of societal benefit.\textsuperscript{130}

As stated in the 1991 Digest, section 75D was designed to provide an incentive ‘to confront the problems associated with erosion, salinity and other forms of land degradation’.\textsuperscript{131} As noted above, the original insertion of section 75D providing full tax deductibility for capital expenditure on soil conservation was costed at $1 million

\textsuperscript{124} Douglas, above n 9.
\textsuperscript{125} Although they may be taxpayers for other reasons such as salary and wage earners.
\textsuperscript{126} Ashby and Polkinghorne, above n 123.
\textsuperscript{129} Wilson S, ‘Formulating cost efficient salinity management plans: a case study in the Kyeamba Valley’ (Paper presented to the National Conference of Land Management for Dryland Salinity Control Conference, Bendigo, 28 September – 1 October 1993).
\textsuperscript{130} Mues et al, above n 72.
\textsuperscript{131} Parliamentary Research Service, Taxation Laws Amendment Bill (No. 2) 1991, 2.
per annum. While the amendments are peppered with anticipated costs and savings, none of these amount to more than $5 million.\textsuperscript{132}

There is limited data on annual expenditure on land degradation available from the Australian Bureau of Statistics. This is shown in table 2 and illustrated in figure 1. This includes both capital and non-capital expenditure whereas the tax expenditure is restricted to capital expenditure only. ‘Control and prevention of land degradation’ includes the establishment of trees or shrubs, earthworks to control, treat or prevent erosion or salinity and fencing to exclude livestock from sensitive areas.

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Table 2: Expenditure on land degradation\textsuperscript{133}

Figure 1: Expenditure on land degradation (capital and non-capital)

Treasury’s Tax Expenditures Statements generally show the combined landcare deduction for primary producers, the three-year write-off expenditure on water facilities for primary producers and, in later years, the water facilities and the land

\textsuperscript{132} See, for example, Button J N, Second Reading Speech, Taxation Laws Amendment Bill (No. 2) 1991, 3; Keating P J, Second Reading Speech, Explanatory Memorandum, Income Tax Assessment Amendment Act (No. 4) 1983 (Cth) 5.
care concession for irrigation water providers, ranging between $20 million and $30 million.\textsuperscript{134} The only exception was 2007 where the landcare deduction for both primary producers and irrigation water providers where shown individually as nil.\textsuperscript{135} It is therefore not possible to determine, nor even estimate, what the land degradation tax concession is likely to be costing taxpayers.

It is submitted that the landcare and the water facilities are not comparable for two reasons. Firstly, landcare expenditure is written off immediately while expenditures on water facilities are written off over three years. Secondly, qualifying rural businesses are able to claim the deduction for landcare expenditure but not for water facilities.

In a survey conducted for the 1993-94 income year, the average size of landcare expenditures claimed amounted to $2,800 with a total cost to the revenue of around $10.9 million.\textsuperscript{136} The most common activities were tree establishment and weed control, although the expenditure per farm was relatively small. The largest individual landcare investments were in earthworks to control erosion or treat salinity. Further, the more profitable farms were more likely to undertake landcare expenditures and also spent more, on average, on landcare works. Expenditure to control salinity or fencing to separate land classes were more likely to be claimed under the landcare provision in order to take advantage of the accelerated rate of depreciation offered by the tax concession. Expenditure on pest management, however, was more likely to be claimed as normal operating expenses due to there being no timing or other advantage to counteract the increased compliance costs involved in separating the expenditure.

The survey also concluded that only about half of the $10.9 million cost was directly attributable to the land degradation provision, the other being claimed as normal operating expenditure. No mention was made of the capital/non-capital differential. The survey also found that, if the capital items could otherwise have been depreciated, then the present value of tax revenue foregone as a result of claims may be less than $2 million. For those with a landcare issue but not making any landcare investment, the reason was inadequate cash available. This is highlighted by an analysis covering the 2000-01 income year that found that 26 per cent of all farms made no farm cash income while 23 per cent made less than $25,000, totalling 49 per cent.\textsuperscript{137}

The 1997 ABARE inquiry also raised concern about the low level of uptake of the provisions. This resulted in the introduction of the tax offset which, as noted above, was short-lived. In a survey of primary producers it was suggested that a tax deduction of 150 per cent to 200 per cent would be a greater incentive to invest in measures to combat land degradation.\textsuperscript{138} The current deduction was considered inadequate considering the time spent on the landcare work and the fact that direct tax


\textsuperscript{136} Mues et al, above n 72.

\textsuperscript{137} Ashby and Polkinghorne, above n 123.

deductions could be gained from other activities that more directly increased farm income. In recommending a deduction of 120 per cent, a report for the Rural Industries Research and Development Corporation it was held that the ‘extra deduction must be high enough to encourage and identify natural resource management expenditure … [but] be viewed against the cost to tax revenue’. It was considered that this would have a dual benefit: additional expenditure on landcare activities and, being separately disclosed, easier for policy-makers to measure.

Estimates of the impact on land degradation vary widely. During the 1970s and 1980s there were four large-scale studies that focused of the extent and impacts of land degradation. These provided a perspective of the extent of the financial problem posed by land degradation. The first, organised by the Australian Standing Committee on Soil Conservation in 1971, estimated that the cost of controlling soil erosion with structural measures in non-arid regions was $350 million. This was followed by a three-year study (1975-78) known as the Commonwealth and State Government Collaborative Soil Conservation Study. Published in 1978 by the Department of Environment, Housing and Community Development, it consisted of 12 separate reports. It was estimated that the cost of treating all the degraded land in Australia was $675 million.

The other two large-scale studies focused on measuring the costs of salinity degradation. In 1982 The Working Party on Dryland Salting in Australia reported that scalding (the major form of dryland salting in Australia) affected 3.78 million hectares, resulting in $5.4 million in annual productivity losses to agriculture and would cost $18.1 million to repair. A consultant’s report, however, put productivity losses at $22 million per year with abatement costs of land salinisation at $10 million per year.

What the above discussion shows is that there is little semblance between estimated costs of abatement and the costs incurred by primary producers, whether or not the tax deduction is taken.

Land degradation is a complex problem and demands a comprehensive approach. The problems of land degradation, the divergence between private and social objectives in land use and the lack of private resources makes some intervention by.

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139 Ashby and Polkinghorne, above n 123, 47.
143 Working Party on Dryland Salting in Australia (Report on salting of non-irrigated land in Australia, Soil Conservation Authority, Victoria for Standing Committee on Soil Conservation, 1982).
the government inevitable. Nevertheless, it is thought that the environment is increasingly being used as a justification to financially support farmers.\footnote{Bignal E M, ‘Using an ecological understanding of farmland to reconcile nature conservation requirements, EU agricultural policy and world trade agreements’ (1998) 35(6) Journal of Applied Ecology 949-954.}

Notwithstanding the tax concession as an incentive, over the period 1990 to 2000, Australia had the sixth highest annual rate of land clearing in the world.\footnote{Lindenmayer D and Burgman M, Practical Conservation Biology (CSIRO, 2005).} It is also the only developed nation in the top 20 land-clearing nations.\footnote{Ibid.} This raises questions over the effectiveness of the tax exemption, at least as it is currently drafted. A broader application and/or an increased rate should be considered.

5. Environmental protection

5.1 Introduction

The concept of ‘environmental protection’ is very broad. Under the Australian Constitution, many of the roles that relate to the protection of the environment reside with state government.\footnote{Department of Sustainability, Environment, Water, Population and Communities, ‘Environment Protection and Biodiversity Conservation Act 1999 (EPBC Act) Frequently asked questions’ <http://www.environment.gov.au/epbc/publications/epbc-act-fact-sheet.html>.} At a federal level, the environmental minister’s role is limited to the protection of eight areas of national environmental significance.\footnote{The eight matters of national environmental significance are world heritage sites, national heritage places, wetlands of international importance, nationally threatened species and ecological communities, migratory species, Commonwealth marine areas, the Great Barrier Reef Marine Park and nuclear actions: Environmental Protection and Biodiversity Conservation Act 1999.} This does not, however, prevent the Commonwealth government from providing incentives via the income tax system.

Contained in subdivision 40-H ITAA97, sections 40-755 to 40-765 provide an immediate deduction for capital and non-capital expenditure incurred in environmental protection activities, subject to certain qualifications. These provisions are replicated in Appendix 3.

5.2 History

Announced in the 1992-93 Budget, new subdivision CA ITAA36, comprising sections 82BH to 82BR, took effect from 19 August 1992.\footnote{Explanatory Memorandum, Taxation Laws Amendment Act (No. 5) 1992 cl 25.} These provisions allowed a deduction for certain environmental protection expenditure and allowed depreciation of plant and equipment and amortisation of the capital costs of structures, structural improvements and buildings used for environmental protection purposes. The deduction was available for certain environmental expenditure in relation to pollution or waste resulting from an activity or site connected to the taxpayer’s business. A sole
or dominant purpose test applied. It was acknowledged in the explanatory memorandum that a reliable costing could not be made.\textsuperscript{152}

The explanatory memorandum accompanying its introduction was specific as to the reasons for its introduction.\textsuperscript{153} It acknowledged that environmental protection expenditure incurred by a business may not qualify for deduction as it may be incurred before commencement or after cessation of the income-producing activity or business, or it may be of a capital nature. It also recognised that there may be a legal requirement to carry out such work or that businesses may undertake such work of their own volition.

The introduction of the environmental protection provisions coincided with the endorsement of the National Strategy for Ecologically Sustainable Development.\textsuperscript{154} However, there is no obvious record of discussions or debates linking these tax provisions with broader community environmental concerns.

Except for the omission of some definitions which did ‘not clarify or extend the ordinary meaning of the word’,\textsuperscript{155} neither the TLIP\textsuperscript{156} nor the UCA\textsuperscript{157} rewrote altered or amended the original meaning of the environmental protection provisions. With no amendments been made since its inception, this must be one of the few tax provisions that has retained its original concept.

### 5.3 Policy

From the wording of the explanatory memorandum, the environmental protection provisions have a commercial purpose. However, from the timing, nature and wording of the provisions, they also appear to have an environmental purpose albeit restricted to ‘preventing, fighting or remedying pollution’ or ‘treating, cleaning up, removing or storing waste’. Terms such as ‘preventing’ have a clear environmental connotation. The explanatory memorandum provides an example of the removal of underground storage tanks because they may leak and cause loss or injury to a future owner or user of the site.\textsuperscript{158}

By not defining terms such as ‘pollution’ and ‘waste’ they take on their ordinary meaning.\textsuperscript{159} When originally enacted, the term ‘environment’ was defined as including ‘all aspects of the surroundings of humans, whether affecting them as individuals or

\textsuperscript{152} Ibid.
\textsuperscript{153} Ibid cl 25.
\textsuperscript{155} Previously section 82BJ ITAA36. Explanatory Memorandum to the Tax Law Improvement Act (No. 1) 1998, 164.
\textsuperscript{156} Explanatory Memorandum, Tax Law Improvement Act (No. 1) 1998: subdivision 400-B ITAA97 comprising sections 400-55 to 400-65.
\textsuperscript{158} Explanatory Memorandum to the Taxation Laws Amendment Act (No. 5) 1992 (Cth).
\textsuperscript{159} ATO, \textit{Petroleum resource rent tax and income tax: treatment of geosequestration expenditure and receipts}, Taxation Ruling TR 2008/6, [23].
in social groupings’. It was not limited to the natural environment but included all aspects of the environment including the demographics of a community. Thus ‘pollution’ and ‘waste’ are not confined to their effect solely on the natural environment but rather to the totality of the surrounding conditions and influences, physical and social, of a particular area. This broadens the scope to encompass, for example, the built environment. The treatment, clean up, removal or storage of waste, for example, includes any operation that leads to resource recovery, recycling, reclamation, direct re-use or alternative uses of waste at any stage of an industrial process. It also includes any means of disposal such as landfill, storage, chemical conversion and incineration.

On 4 September 2012 the Australian Government announced the establishment of an Office of Asbestos Safety, tasked with developing a national strategic plan to phase out the presence of hazardous building material. This followed the release of a report that recommended tax deductibility should be extended to all property owners ‘to assist in the take-up of the scheme’ to remove asbestos. Previously associated with direct contact, either through mining or working with asbestos in manufacturing processes, asbestos-related diseases are now becoming more prevalent among the general population of home renovators and their families. As a result of the establishment of this Office and increased awareness of the extent of the issue, it is possible that the environmental protection provisions may get more policy attention.

5.4 Analysis

Only two activities constitute an ‘environmental protection activity’. These are preventing, fighting orremedying pollution and treating, cleaning up, removing or storing waste. Even within these confines, the provision does not achieve full deductibility. For example, the provisions do not apply more broadly to general pollution, as is already the case with carbon capture and storage, or geological sequestration.

Statutory definitions of ‘pollution’ often include categories such as erosion. Indeed, the Commissioner accepts that, for the purposes of environmental protection legislations, the ‘deposition of sediment into waterways as a result of erosion would constitute pollution’. Nevertheless, the Commissioner contends that the statutory definition of non-tax related legislation should not ‘be preferred over the clear

160 ITAA 1936 s 82BJ (as it then was).
161 Explanatory Memorandum to the Taxation Laws Amendment Act (No. 5) 1992 (Cth).
162 Ibid.
163 Shorten B, 'A national approach to asbestos management' (Media Release, Minister for Employment and Workplace Relations, Financial Services and Superannuation, 4 September 2012).
167 See, for example, Clean Waters Act 1970 (NSW); Environment Protection Act 1986 (WA).
explanation of the term in the EM’, referring to the explanatory memorandum of 1992. However, it is submitted that the explanatory memorandum does not provide a ‘clear explanation’ of the term pollution – it merely states pollution includes both known and currently unknown harmful and potentially dangerous contaminates and noise. It is the Commissioner’s contention that erosion does not cause pollution. Erosion is a significant problem in Australia affecting, amongst other things, salinity and water quality. If Australia is serious about tackling these issues, consideration should be given to extending the concept of ‘pollution’ to more categories and thereby making them available to more taxpayers.

No guidance has been given to the concept of ‘waste’ in section 40-755 as has been done for ‘pollution’. As there is no requirement that it be hazardous waste it could equally apply to household waste. Many campaigns designed to get people thinking about environmentally friendly living have focused on household waste as something which can be easily manipulated to make a difference in the environment. This raises the question of whether, at least theoretically, a tax deduction is available under s 40-755 for all household waste of rental properties. This is obviously incongruous but serves to illustrate how widely a provision can be applied when it rests on a word with a broad ordinary meaning.

On a positive environmental note, preventative measures will qualify. In addition it is not site specific but extends to cleaning up other sites impacted by the pollution and/or waste. However, that there is no requirement that the activity be completed, or that there be complete disposal, is contrary to environmental principles.

Commencing the 2004-05 income year, Treasury’s Tax Expenditures Statements combines the deductions for environmental protection activities (EPA) and environmental impact studies (EIS), the latter being outside the scope of this paper. The tax expenditures only cover the combined mining, manufacturing and construction sectors which may understate the claims as the provision has wider taxpayer application. These are shown in figure 2. As a provision of last resort, most qualifying non-capital expenditure would be deductible as an ordinary business expense negating the need (and compliance costs) to separate the expenditure.

168 Explanatory Memorandum to the Taxation Laws Amendment Act (No. 5) 1992 (Cth).
171 Rental properties meet the requirement of being an ‘earning activity’: subsection 40-755(3) and (4).
173 Contained in subdivision 40-1 ITAA97.
175 Subsection 40-760(1)(e) ITAA97.
Australian Bureau of Statistics data on ‘environmental protection activities’ encompasses waste management, waste water and water protection, ambient air and climate protection, protection of biodiversity and landscape, protection of soil and groundwater and other environmental protection activities. As this is broader than the tax expenditure for ‘environmental protection activities’ a comparison cannot be made. While attempts have been made to cost pollution and waste in the broader Australian environment, this has focused predominantly on carbon emissions which too are outside the scope of the tax expenditure. It is therefore not possible to ascertain exactly how effective the tax expenditure is on a cost-benefit basis.

6. Comparative analysis

Capital expenditure is not normally deductible unless a particular provision makes it so. Those that do usually allow deductions to be claimed over a period approximately corresponding to the consumption of the benefit from the expenditure. However, a few provisions allow for capital expenditure to be fully deducted in a single income year notwithstanding that the benefits will be consumed over a longer period. These provisions serve particular policy objectives, usually to encourage certain activities. Three such provisions are mine site rehabilitation, land degradation (or landcare) and environmental protection. A comparison of their features is contained in table 3.

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178 Explanatory Memorandum, New Business Tax System (Consolidated and Other Measures) Act (No. 1) 2002.
Table 3: Comparative analysis

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7. Conclusion

The income tax system influences the way taxpayers invest in environmental projects. Using the tax system to encourage investment into natural resource management is both wise and desirable. While policy makers are generally loathe to use the tax system to encourage one form of investment over another, encouraging private investment in natural resource management is desirable if it provides both a public and private benefit and links the environmental project work to the direct investment made by governments. In this case the government investment is the revenue foregone.

As evident from the discussion on the introduction of the mine rehabilitation and land degradation tax expenditures, any expected cost has been severely underestimated. Indeed, determining the cost of tax deductions for environmental protection activities was not even attempted. This is often an outcome of the tax legislative process as there is no outlay of funds (as with direct payments or grants) and the real cost will only be incurred at some future date in the form of reduced tax collections.

Once established, the tax expenditure is administered as part of the tax system and therefore not monitored to the same extent as spending programs. A report by the National Commission of Audit also noted that tax expenditures were not accurately costed nor within direct ministerial control of spending in relevant portfolios and concluded that ‘tax concessions are a largely non-transparent form of assistance’

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179 Ashby and Polkinghorne, above n 123.
180 Ibid.
181 Gumley, above n 127.
which ‘reduces accountability’ and ‘increases the likelihood that poorly targeted concessions will remain on offer’.\textsuperscript{183}

Nevertheless, once implemented tax expenditures become entrenched and difficult to abolish. From an environmental perspective, this is an advantage especially as taxation-based measures provide additional support for environmental management projects where the private benefits are less than the overall cost of the project.\textsuperscript{184}

What emanates from the above discussion is that Australian tax policy is subject to the influence of various groups at any point in time and that influence is dependent, to some extent, on which political party is in government. A criticism of Australian tax policy is that it ‘is subject to frequent change, is very complex and is lacking in clear direction. Much publicised policy announcements tend to be watered down at the implementation stage and their availability and appeal is severely restricted.’\textsuperscript{185}

This then raises the question: income tax and environmental provisions – green gold or lead weight?

Further research is required to ascertain the effect these tax expenditures have had on encouraging rehabilitation of mine sites and the prevention and rectification of land degradation and of environmental protection activities and whether the environmental benefits justify subsidisation by taxpayers. A good starting point would be reliable data with respect to anticipated costs, actual expenditure and tax expenditure claims.

\textsuperscript{183} National Commission of Audit, \textit{Report to the Commonwealth Government} (June 1996) 11.2.

\textsuperscript{184} Douglas, above n 9.

\textsuperscript{185} McKerchar and Coleman, above n 101.
Appendix 1

40-735 Deduction for expenditure on mining site rehabilitation

40-735(1)
You can deduct for an income year expenditure you incur in that year to the extent it is on *mining site rehabilitation of:

(a) a site on which you:
   (i) carried on *mining and quarrying operations; or
   (ii) conducted *exploration or prospecting; or
   (iii) conducted *ancillary mining activities; or

(b) a *mining building site.

Note 1: If an amount of the expenditure is recouped, the amount may be included in your assessable income: see Subdivision 20-A.

Note 2: If Division 250 applies to you and an asset that is land:
   (a) if section 250-150 applies – you can deduct expenditure you incur in relation to the land to the extent specified in a determination made under subsection 250-150(3); or
   (b) otherwise – you cannot deduct such expenditure.

40-735(2)
However, a provision of this Act (except Division 8 (which is about deductions)) that expressly prevents or restricts the operation of that Division applies in the same way to this section.

40-735(3)
However, you cannot deduct expenditure under subsection (1) to the extent that it forms part of the *cost of a *depreciating asset.

40-735(4)
*Mining site rehabilitation* is an act of restoring or rehabilitating a site or part of a site to, or to a reasonable approximation of, the condition it was in before *mining and quarrying operations, *exploration or prospecting or *ancillary mining activities were first started on the site, whether by you or by someone else.

40-735(5)
Partly restoring or rehabilitating such a site counts as *mining site rehabilitation* (even if you had no intention of completing the work).

40-735(6)
For a *mining building site, the time when *ancillary mining activities were first started on the site is the earliest time when the buildings, improvements or *depreciating assets concerned were located on the site.
Appendix 2

40-630 Landcare operations

40-630(1)
You can deduct capital expenditure you incur at a time in an income year on a ‘landcare operation’ for:

(a) land in Australia you use at the time for carrying on a ‘primary production business’; or

(b) rural land in Australia you use at the time for carrying on a ‘business for a ‘taxable purpose from the use of that land (except a business of ‘mining and quarrying operations).

Note: If Division 250 applies to you and an asset that is land:

(a) if section 250-150 applies – you are taken to be using the land for the purpose of carrying on a primary production business, or a business for the purpose of producing assessable income from the use of rural land (except a business of ‘mining and quarrying operations), to the extent specified in a determination made under subsection 250-150(3); or

(b) otherwise – you cannot deduct such expenditure.

40-630(1A)
A ‘rural land irrigation water provider’ can deduct capital expenditure it incurs at a time in an income year on a ‘landcare operation’ for:

(a) land in Australia that other entities use at the time for carrying on ‘primary production businesses; or

(b) rural land in Australia that other entities use at the time for carrying on ‘businesses for a ‘taxable purpose from the use of that land (except a business of ‘mining and quarrying operations); being entities supplied with water by the rural land irrigation water provider.

40-630(1B)
A rural land irrigation water provider is:

(a) an ‘irrigation water provider; or

(b) an entity whose ‘business is primarily and principally the supply (otherwise than by using a ‘motor vehicle) of water to entities for use in carrying on ‘businesses (except businesses of ‘mining and quarrying operations) using rural land in Australia.

Exception: plant
40-630(2)
However, you cannot deduct an amount under this Subdivision for capital expenditure on ‘plant, except:

(a) a fence erected for a purpose described in paragraph 40-635(1)(a) or (b); or

(b) a dam or structural improvement (except a fence) covered by paragraph (1)(c), (d), (e) or (f) of the definition of plant in section 45-40.

40-630(2A)
In applying paragraph (2)(b) to capital expenditure incurred by a ‘rural land irrigation water provider on a dam or structural improvement, the requirement in paragraph 45-40(1)(c) that the land on which the dam or structural improvement is situated be used for agricultural or pastoral operations is to be disregarded.

Exception: deduction available under Subdivision 40-F
40-630(2B)
A 'rural land irrigation water provider cannot deduct an amount under this Subdivision for capital expenditure if the entity can deduct an amount for that expenditure under Subdivision 40-F.

Exception: deduction available under Subdivision 40-J
40-630(2C)
You cannot deduct an amount under this Subdivision for capital expenditure if any entity can deduct an amount for that expenditure for any income year under Subdivision 40-J.

Reduction of deduction
40-630(3)
You must reduce your deduction by a reasonable amount to reflect your use of the land in the income year after the time when you incurred the expenditure for a purpose other than the purpose of carrying on:
(a) a 'primary production business; or
(b) a 'business for the 'purpose of producing assessable income from the use of rural land (except a business of 'mining and quarrying operations).

40-630(4)
Subsection (3) does not apply to expenditure incurred by a 'rural land irrigation water provider. Instead, a rural land irrigation water provider must reduce its deduction in relation to particular land by a reasonable amount to reflect an entity's use of the land in the income year after the rural land irrigation water provider incurred the expenditure for a purpose other than a 'taxable purpose.

40-635 Meaning of landcare operation
40-635(1)
Landcare operation for land means:
(a) erecting a fence to separate different land classes on the land in accordance with an approved management plan for the land; or
(b) erecting a fence on the land primarily and principally for the purpose of excluding animals from an area affected by land degradation:
   (i) to prevent or limit extension or worsening of land degradation in the area; and
   (ii) to help reclaim the area; or
(c) constructing a levee or a similar improvement on the land; or
(d) constructing drainage works on the land primarily and principally for the purpose of controlling salinity or assisting in drainage control; or
(e) an operation primarily and principally for the purpose of:
   (i) eradicating or exterminating from the land animals that are pests; or
   (ii) eradicating, exterminating or destroying plant growth detrimental to the land; or
   (iii) preventing or fighting land degradation (except by erecting fences on the land); or
(f) a repair of a capital nature, or an alteration, addition or extension, to an asset described in paragraph (a), (b), (c) or (d) or an extension of an operation described in paragraph (e); or
(g) constructing a structural improvement, or a repair of a capital nature, or an alteration, addition or extension, to a structural improvement, that is reasonably incidental to an asset described in paragraph (c) or (d).
Note: A depreciating asset and a repair of a capital nature or an alteration, addition or extension to that asset are not the same asset for the purposes of section 40-50 and this Subdivision: see section 40-53.

40-635(2)
Paragraph (1)(d) does not apply to an operation draining swamp or low-lying land.
Appendix 3

40-755 Environmental protection activities

40-755(1)
You can deduct expenditure you incur in an income year for the sole or dominant purpose of carrying on *environmental protection activities.

Note: If Division 250 applies to you and an asset that is land:
(a) if section 250-150 applies - you can deduct expenditure you incur in relation to the land to the extent specified in a determination made under subsection 250-150(3); or
(b) otherwise – you cannot deduct such expenditure.

40-755(2)
Environmental protection activities are any of the following activities that are carried on by or for you:
(a) preventing, fighting or remedying:
   (i) pollution resulting, or likely to result, from *your earning activity; or
   (ii) pollution of or from the site of your earning activity; or
   (iii) pollution of or from a site where an entity was carrying on any *business that you have acquired and carry on substantially unchanged as your earning activity;
(b) treating, cleaning up, removing or storing:
   (i) waste resulting, or likely to result, from your earning activity; or
   (ii) waste that is on or from the site of your earning activity; or
   (iii) waste that is on or from a site where an entity was carrying on any business that you have acquired and carry on substantially unchanged as your earning activity.

No other activities are environmental protection activities.

40-755(3)
Your earning activity is an activity you carried on, carry on, or propose to carry on:
(a) for the *purpose of producing assessable income for an income year (except a *net capital gain); or
(b) for the purpose of *exploration or prospecting; or
(c) for the purpose of *mining site rehabilitation; or
(d) for purposes that include one or more of those purposes.

40-755(4)
If *your earning activity is:
(a) leasing a site you own; or
(b) granting a *right to use a site you own or control; or
(c) a similar activity involving a site;
that site is taken to be the site of your earning activity.

Note: This means you can deduct your expenditure on environmental protection activities relating to the site, even if the pollution or waste is caused by another entity that uses the site.

40-760 Limits on deductions from environmental protection activities
Expenditure you cannot deduct

40-760(1)
You cannot deduct an amount under section 40-755 for an income year for:
(a) expenditure for acquiring land; or
(b) capital expenditure for constructing a building, structure or structural improvement; or
(c) capital expenditure for constructing an extension, alteration or improvement to a building, structure or structural improvement; or
(d) a bond or security (however described) for performing environmental protection activities; or
(e) expenditure to the extent that you can deduct an amount for it under a provision of this Act outside this Subdivision.

Note: You may be able to deduct expenditure described in paragraph (1)(b) or (c) under Division 43 (which deals with capital works).

40-760(2)
In particular, you cannot deduct under section 40-755 expenditure to the extent that you incur it on carrying out an activity for environmental impact assessment of your project.

40-760(3)
However, a provision of this Act (except Division 8 (which is about deductions)) that expressly prevents or restricts the operation of that Division applies in the same way to section 40-755.

40-765 Non-arm’s length transactions
If you incurred arm’s expenditure under an arrangement and:
(a) there is at least one other party to the arrangement with whom you did not deal at arm’s length; and
(b) apart from this section, the amount of the expenditure would be more than the market value of what it was for;
the amount of expenditure you take into account under this Subdivision is that market value.