

EXPLANATORY STATEMENT

Issued by the Authority of the Minister for the Environment

Income Tax Assessment Act 1997

Income Tax Assessment (Environmental and Natural Resource Management in relation to the Establishment of Trees for the purposes of Carbon Sequestration) Guidelines 2018

Purpose

Subdivision 40-J of the Income Tax Assessment Act 1997 (the Act) provides a deduction for capital expenditure for the establishment of trees in carbon sink forests.

Subparagraph 40-1010(1)(h)(i) of the Act provides that expenditure on establishing trees in carbon sink forests is covered if a taxpayer gives the Commissioner of Taxation a statement that sets out all information necessary to determine whether all of the conditions in subsection 40-1010(2) of the Act are satisfied. The conditions set out in subsection 40-1010(2) include a condition that the establishment of the trees meets the requirements of the guidelines in subsection 40-1010(3).

Subsection 40-1010(3) of the Act provides that the Minister must, by legislative instrument, make guidelines about environmental and natural resource management in relation to the establishment of trees for the purposes of carbon sequestration (the guidelines).

The purpose of this instrument is to make the guidelines for the purposes of subsection 40-1010(3) of the Act.

This instrument is a legislative instrument for the purposes of the *Legislation Act 2003*.

This legislative instrument repeals the previous guidelines made on 1 December 2008, but maintains the intent of those guidelines. Under this instrument eligible offset projects already declared eligible under the *Carbon Credits (Carbon Farming Initiative) Act 2011* will automatically meet the requirements. This is because the issue of adverse environmental and natural resource management impacts is already addressed in the approval of such projects, including that the project is not an excluded offsets project within the meaning of that Act. Where the activity is not part of an eligible offsets projects, the criteria under the earlier guidelines will be applied as the relevant conditions set out in Schedule 1.

Public consultation

The amendment incorporates the recommendation of an Agency Review conducted into the legislative instrument by the Department of the Environment and Energy in 2018 to streamline eligibility and reduce regulatory burden for Emissions Reduction Fund projects (Attachment A). Consultation on this amendment included a public consultation period inviting comment on a revised draft instrument, as well as direct invitations to comment to stakeholders. The first guidelines made in December 2008 were developed after extensive consultation with stakeholders and the arrangements in Schedule 1 for projects that are not under the Emissions Reductions Fund reflect those existing arrangements.

Commencement

This instrument commenced the day after it was registered on the Federal Register of Legislation.

Detailed description of the Amendment Rule

Attachment B outlines and describes the sections in the Amendment Rule.

Regulatory impact

The Office of Best Practice Regulation has agreed that these amendments have a minor regulatory impact, and a Regulatory Impact Statement is not required.

Statement of compatibility with human rights

A statement of compatibility with human rights for the purposes of Part 3 of *the Human Rights (Parliamentary Scrutiny) Act 2011* is set out at Attachment C.



Australian Government

Department of the Environment and Energy

Agency Review

Environmental and Natural Resource Management Guidelines in Relation to the Establishment of Trees for the Purposes of Carbon Sequestration

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CONTENTS

Background3

Purpose and Scope3

Structure of the Review3

Objective of the Instrument4

Regulatory Impact4

Broader Legal and Policy Context5

Clearer Laws5

Consultation5

Conclusions and Recommendations6

BACKGROUND

Subdivision 40-J of the *Income Tax Assessment Act 1997* (ITAA) provides for tax deductions for the costs of establishing trees for the purpose of carbon sequestration (referred to in the ITAA as carbon sink forests).

One of the conditions of tax deductibility is that the establishment of the trees must meet *Environmental and Natural Resource Management Guidelines in relation to the establishment of trees for the purposes of carbon sequestration* (the Guidelines). The Guidelines are a legislative instrument. The ITAA provides that the Department of the Environment and Energy (DoEE) is responsible for assessing compliance with the Guidelines.

The Guidelines were made on 1 December 2008 and are scheduled to sunset on 1 April 2019. Sunsetting is a process of automatic repeal of legislative instruments that occurs approximately ten years after their registration on the Federal Register of Legislation. If an instrument sunsets, it ceases to have any effect.

PURPOSE AND SCOPE

This paper reviews the fitness for purpose of the Guidelines, in preparation for their scheduled sunsetting. It does not review subdivision 40-J of the ITAA, or associated taxation policies.

The review is an essential part of the sunsetting process. It informs the rule-maker's decision about whether the instrument should be left to sunset, remade with amendment, remade without amendment or rolled over by the Parliament.

This review conducts an assessment of the effectiveness and efficiency of the Guidelines by means of a fit for purpose test.

STRUCTURE OF THE REVIEW

This review follows the approaches recommended for conducting a fit for purpose test outlined in the Attorney General's Department's Guide to managing sunsetting instruments¹ and applies the principles outlined in the Office of Best Practice Regulation's guidance note on sunsetting instruments². This includes assessment of: the objective of the instrument; its regulatory impact; broader legal and policy context; compliance with clearer laws principles and outcomes from public consultation.

¹ Attorney General's Department. Guide to Managing Sunsetting of Legislative Instruments. 2016. Available online at: <https://www.ag.gov.au/LegalSystem/AdministrativeLaw/Documents/guide-to-managing-sunsetting-of-legislative-instruments-december-2016.pdf>

² Office of Best Practice Regulation. Sunsetting legislative instruments guidance note. 2016. Available online at: <https://www.pmc.gov.au/resource-centre/regulation/sunsetting-legislative-instruments-guidance-note>

OBJECTIVE OF THE INSTRUMENT

Subsection 40-1010(3) of the ITAA provides that the Minister administering the *National Greenhouse and Energy Reporting Act 2007* must, by legislative instrument, make guidelines about environmental and natural resource management in relation to the establishment of trees for the purposes of carbon sequestration.

Taxpayers seeking the tax deduction must ensure their planting projects comply with the Guidelines to be eligible (paragraph 40-1010(2)(d)). Subsection 40-1010(6) establishes the role of the Department to assess compliance with the Guidelines. Claims for the tax deduction also need to meet other conditions not covered in this review.

The Guidelines cover the following requirements that carbon sink forest plantings seeking the tax deduction must comply with: (1) adhering to best practice approaches for achieving water and land environmental benefits, (2) complying with applicable government regulatory requirements and being guided by regional natural resource management plans, and (3) registering legal rights concerning carbon sequestration in carbon sink forests on the land title.

If the instrument is allowed to sunset, taxpayers would not be able to meet one of the conditions for obtaining a tax deduction for the costs of establishing carbon sink forests, and therefore would not be able to claim a deduction. The Guidelines are required, to enable the tax deduction provision to continue to operate.

REGULATORY IMPACT

The primary regulatory impact of the Guidelines is the requirement for taxpayers to submit a carbon sink statement providing information and evidence of meeting each of the requirements in the Guidelines, when they submit a Notice of Assessment to the Australian Taxation Office (ATO).

If a taxpayer has not provided sufficient information demonstrating the current environmental and natural resource management guidelines have been addressed in the Notice of Assessment, DoEE advises the ATO that further evidence is required. The ATO then advises the taxpayer that further evidence is required. DoEE considers any further evidence obtained from the taxpayer to determine compliance with the guidelines. If further evidence is not provided, or if evidence is provided showing that all components of the guidelines have been considered but the Notice of Assessment does not demonstrate that all components of the Guidelines have been adhered to, the claim is assessed as non-compliant and a non-compliance Notice is issued to the Commissioner.

In 2010, the former Department of Climate Change and Energy Efficiency (DCCEE) and ATO identified that for most claims it was necessary to seek further information from the taxpayer, as insufficient information was being supplied with the Notice of Assessment to demonstrate compliance with the Guidelines and other conditions for eligibility for the tax deduction. The ATO and DCCEE amended the application form and accompanying instructions for taxpayers to expand on and clarify requirements around the information required. This additional guidance proved effective in reducing the regulatory burden of seeking a deduction, as all subsequent Notices of Assessment have provided sufficient information.

The Guidelines do not require any new regulatory arrangements at any level of government. They were developed to leverage existing state and regional frameworks for best practice land management, to avoid negative environmental outcomes, and provide realistic compliance and administration costs for government and taxpayers.

One area of potentially avoidable regulatory burden associated with the Guidelines is that there is some duplication of regulatory requirements in the case of projects participating in the Australian Government's Emissions Reduction Fund (ERF) under the *Carbon Credits (Carbon Farming Initiative) Act 2011*.

No concerns or complaints about regulatory burden or other aspects of the Guidelines have been raised with DoEE by taxpayers or the public since the Guidelines' inception. DoEE did not receive any indications of concerns during consultation conducted as part of this review.

BROADER LEGAL AND POLICY CONTEXT

The Guidelines form part of Australian taxation law. They do not touch on any legal or policy issues identified for consideration in the Office of Best Practice Regulation's guidance (Australia's obligations under international law, constitutional law, criminal law, administrative law, privacy law and deregulation).

The Guidelines are of relevance to the broader legal framework around carbon sink forest establishment in Australia. In particular, the ERF provides an incentive to establish forests for the purpose of sequestering carbon, to generate carbon credits. The ERF requires these projects to comply with rigorous eligibility requirements, several of which are similar to those specified in the Guidelines.

CLEARER LAWS

Reducing complexity of legislation including regulations is a core clearer laws principle³. This review finds the Guidelines are clear and concise. The level of specificity is appropriate to the objectives of the guidelines, and the terminology and references to other regulation can be readily understood by those intending to claim a tax deduction.

Minor reformatting of the Guidelines and updating would be required to be consistent with other instruments and current drafting standards.

CONSULTATION

DoEE conducted public consultation between 31 August and 14 September 2018 to inform this review. This included publication of a proposed amendment to the Guidelines to update them and reduce regulatory burden for ERF projects. The proposed amendment was in response to draft conclusions of this sunset review.

³Developing Clearer Laws. Attorney General's Quick Reference Guide. Available online at: <https://www.ag.gov.au/LegalSystem/ReducingTheComplexityOfLegislation/Documents/ClearerLawsQuickReferenceGuide.pdf>

DoEE published the proposed amendment on its website and forwarded it to stakeholders including carbon sink forest growers who have previously claimed the tax deduction and participated in the ERF, the Treasury, the Australian Taxation Office and NRM Regions Australia. DoEE did not receive any responses.

The Office of Best Practice Regulation reviewed the proposed amendment to the Guidelines, concluding that due to its minor nature a Regulatory Impact Statement is not required.

CONCLUSIONS AND RECOMMENDATIONS

A review of the Guidelines has found they have been operating effectively and efficiently.

This finding is supported by the Guidelines operating since inception without complaints or concerns being raised by taxpayers or the public, and a public consultation process concluding without any concerns being raised over the operation of Guidelines.

If the Guidelines instrument is allowed to sunset, taxpayers would not be able to meet one of the conditions for obtaining a tax deduction for the costs of establishing carbon sink forests, and therefore would not be able to claim a deduction. The Guidelines are thus required in order to enable the tax deduction provision to continue to operate.

The review identified some duplication between the requirements of the Guidelines and the requirements for ERF projects. The review recommends a minor amendment to respond to this issue and update the Guidelines for the current policy environment.

- The Guidelines could be amended to allow projects that seek a tax deduction and are already an ERF project to automatically qualify for the deduction without separate assessment against the Guidelines. This would streamline access to the tax deduction for eligible offsets projects involving establishing carbon sink forests under the ERF, reduce duplicative regulatory burden and ensure the instrument continues to operate effectively and efficiently.
- The Guidelines could be amended to be consistent with current drafting standards and support clearer laws.

Details of the sections in the *Income Tax Assessment (Environmental and Natural Resource Management in relation to the Establishment of Trees for the purposes of Carbon Sequestration) Guidelines 2018*

1. Name

Section 1 provides that the name of the instrument is the *Income Tax Assessment (Environmental and Natural Resource Management in relation to the Establishment of Trees for the purposes of Carbon Sequestration) Guidelines 2018*.

2. Commencement

Section 2 provides that the instrument would commence on the day after it is registered.

3. Authority

Section 3 provides that the instrument is made under subsection 40-1010(3) of the *Income Tax Assessment Act 1997*.

4. Requirements

Section 4 provides two pathways for the establishment of trees to meet the requirements of paragraph 40-1010(2)(d) of the *Income Tax Assessment Act 1997*.

The first pathway is if the trees are established as part of an eligible offsets project within the meaning of the *Carbon Credits (Carbon Farming Initiative) Act 2011*. That Act provides for the crediting and purchasing of carbon abatement, through projects such as the establishment of trees to sequester carbon. All eligible offsets projects must be assessed by the Clean Energy Regulator and meet a number of criteria in the Act, rules, regulations and methodology determinations. This includes a requirement that the project is not an ‘excluded offsets project’ which may have adverse environmental or natural resource management impacts. Having satisfied these criteria, further requirements are unnecessary.

The second pathway is that the establishment of the trees complies with the guidelines set out in Schedule 1. These reflect the requirements set out in the existing guidelines.

5. Repeal

Section 5 repeals the existing guidelines, the *Environmental and Natural Resource Management Guidelines in relation to the establishment of trees for the purposes of carbon sequestration* made under subsection 40-1010(3) of the *Income Tax Assessment Act 1997* on 1 December 2008.

Schedule 1–Guidelines

This Schedule sets out the guidelines for projects which are not eligible offsets projects under the *Carbon Credits (Carbon Farming Initiative) Act 2011*. There are four central requirements:

[1] Carbon sink forest establishment should be based on regionally applicable best practice approaches for achieving multiple land and water environmental benefits.

- [2] Carbon sink forest establishment activities should be guided by regional natural resource management plans and water sharing plans, and environmental impacts at a catchment scale should be considered.
- [3] Carbon sink forest establishment activities should recognise and adhere to all government regulatory requirements.
- [4] Legal rights concerning carbon sequestration in carbon sink forests should be registered on the land title in accordance with state and territory government legislation.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Income Tax Assessment (Environmental and Natural Resource Management in relation to the Establishment of Trees for the purposes of Carbon Sequestration) Guidelines 2018

The *Income Tax Assessment (Environmental and Natural Resource Management in relation to the Establishment of Trees for the purposes of Carbon Sequestration) Guidelines 2018* (the **Guidelines**) is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

Subdivision 40-J of the Income Tax Assessment Act 1997 (the Act) provides a deduction for capital expenditure for the establishment of trees in carbon sink forests.

Subparagraph 40-1010(1)(h)(i) of the Act provides that expenditure on establishing trees in carbon sink forests is covered if a taxpayer gives the Commissioner of Taxation a statement that sets out all information necessary to determine whether all of the conditions in subsection 40-1010(2) of the Act are satisfied. The conditions set out in subsection 40-1010(2) include a condition that the establishment of the trees meets the requirements of the guidelines in subsection 40-1010(3).

Subsection 40-1010(3) of the Act provides that the Minister must, by legislative instrument, make guidelines about environmental and natural resource management in relation to the establishment of trees for the purposes of carbon sequestration (the guidelines).

The Guidelines are the relevant legislative instrument for the purposes of subsection 40-1010(3) of the Act. The requirements are that such projects are either eligible offsets projects under the *Carbon Credits (Carbon Farming Initiative) Act 2011* or that the projects meet a number of criteria set out in the Schedule to the instrument.

Human rights implications

The Guidelines do not engage any of the applicable rights or freedoms.

Conclusion

The Guidelines are compatible with human rights because they do not limit any human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.