Nature: We're Taxing it to Death

By Bob Barnett

Nature brings us a whole suite of benefits. It cleans the air, the water, prevents floods, welcomes tourists and helps protect native species. Almost 10 years ago the Ontario government released a report, *Estimating Ecosystem Services in Southern Ontario,* which shows that nature provides us with $85 BILLION dollars worth of services every year.

How do we reward those landowners who understand this and protect it? First, we tax it every year for its property value. Then, when the landowner sells it, we tax it again for its capital gain.

I understand that 20 and 40 years ago when we decided to tax properties on their current value and we decided that rich people shouldn't pass on so much of their wealth that we didn't understand that nature had a value. Its benefits were ascribed to "externalities" or things we didn't count as having a real financial value. At that time, we didn't know that an acre of forest brings us "services" worth $1,800 an acre every year and wetlands are worth $6,140.

So why do we continue to tax nature? Municipalities need the money, they don't see the benefits flowing as cash into their economy and the province doesn't want to pay for it either. Here's an anomaly: Escarpment Biosphere Conservancy (EBC) has 48 conservation agreements which reduce the value of the property because the owner has agreed not to subdivide the property, not to build more houses, not to sell the aggregate and to use good forest management practices. Despite the value of the property being reduced by a federal government-approved $100-$200,000, the provincial government refuses to reduce the assessment.

The federal government doesn't distinguish between capital gains for good and bad things. They give exemptions for houses, which are of political advantage, but not nature which is actually helping the public and government save money while achieving community objectives like protecting increasingly rare species. Protecting farmland is good: it produces the food we eat, but it only protects a small fraction of the ecological services of forest or wetland. Farmland is exempted from capital gain.

Beating Property Taxes

My discussions with landowners tell me that they have to beat property taxes by harvesting their woodlot every seven to 15 years. Many argue this is good for the forest and good for the economy. Studies indicate that mature, or unharvested, woodlots sequester far more carbon than those with younger trees growing where the mature ones have been removed. Only 10 per cent of harvested wood lasts a century. Most of it ends up as fuel, in landfill or left as slash left in the forest. But yes, it helps the conventional economy as it adds to our manufacturing GDP. That's why most foresters and most economists prefer timber to leaves and fatter trees which sequester more carbon and slow climate change, which is just another externality. Note: EBC has sold $200,000 of carbon credits to companies which voluntarily agree to sequester carbon. We are allowed to sell and certify these credits because we use "enhanced" forestry management. That means sparing it from harvest and letting the trees grow instead. Despite EBC's success, few companies are willing to spend money to "do the right thing" and become carbon neutral.

What happens when capital gains or "estate" taxes rear their ugly head? Most often, the family can't afford to keep the forest or wetland in the family; they need to sell it off. The new purchaser often logs the mature timber or figures it's a good place for a new house. Often it both gets logged, then resold to a city slicker who doesn't notice the difference since they're looking for a place to live in the country.

Avoiding Other Taxes

What can YOU do to avoid crippling capital gains/estate taxes?

We suggest looking into adding covenants to your title if you are willing to avoid severances, new buildings, aggregate extraction, commercial tree harvesting etc. This exempts you from capital gains on the portion of the value covered by the use restrictions. It also gets you an income tax receipt for the value reduction which then offsets the capital gain. Then you CAN afford to pass the land along to your kids. See the example in the box in which a "normal" transfer of land to the kids costs $60,000 but one with a conservation agreement has no cost.

Others choose to donate some of their land outright to EBC which not only cancels out the gain on the ENTIRE portion donated but also gives you an income tax receipt which can be used against other parts of your estate.

For more detailed advice, call your investment advisor or Bob Barnett at EBC.

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CAPITAL GAIN EXAMPLE	NORMAL	WITH CONSERVATION AGREEMENT
Value of Recreational Property	$400,000	$400,000
Original Purchase Price	-$50,000	-$50,000
Value of Improvements	-$50,000	-$50,000
Value of Conservation Agmt.		$100,000
Capital Gain	$300,000	$200,000
Taxable Capital Gain	$150,000	$100,000
Tax on Gain	-$60,000	-$40,000
Value of Income Tax Receipt		$40,000
Net Cost of Transfer	-$60,000	$0

This table illustrates a sample project. The first column illustrates how much capital gain tax the government collects if the property is sold, or transferred to a family member. Each case is different, but a $400,000 recreational property could cost $60,000 to transfer, based on a $150,000 increase in value from the time of purchase. The second column illustrates how one can save that $60,000 tax by placing a conservation agreement on title. This means you decrease the value by agreeing not to sell gravel or build more houses on it. You get a capital gain exemption of $100,000 and an income tax receipt worth $40,000.