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# **BIODIVERSITY FISCAL INCENTIVES**

## **A FRAMEWORK ON FISCAL INCENTIVES FOR BIODIVERSITY**

**August 2009**

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## List of Acronyms

NEMA	National Environmental Management Act (107 of 1998)
NBF	National Biodiversity Framework
NPAES	National Protected Area Expansion Strategy
PES	Payments for Ecosystem Services
SARS	South African Revenue Service

## Executive Summary

This document provides an overview of the fiscal incentives that relate specifically to biodiversity conservation through custodianship of the land - generally referred to as 'biodiversity fiscal incentives'. Both the National Biodiversity Framework and the National Protected Area Expansion Strategy call for the development and use of fiscal incentives for the conservation of biodiversity on private and communal land.

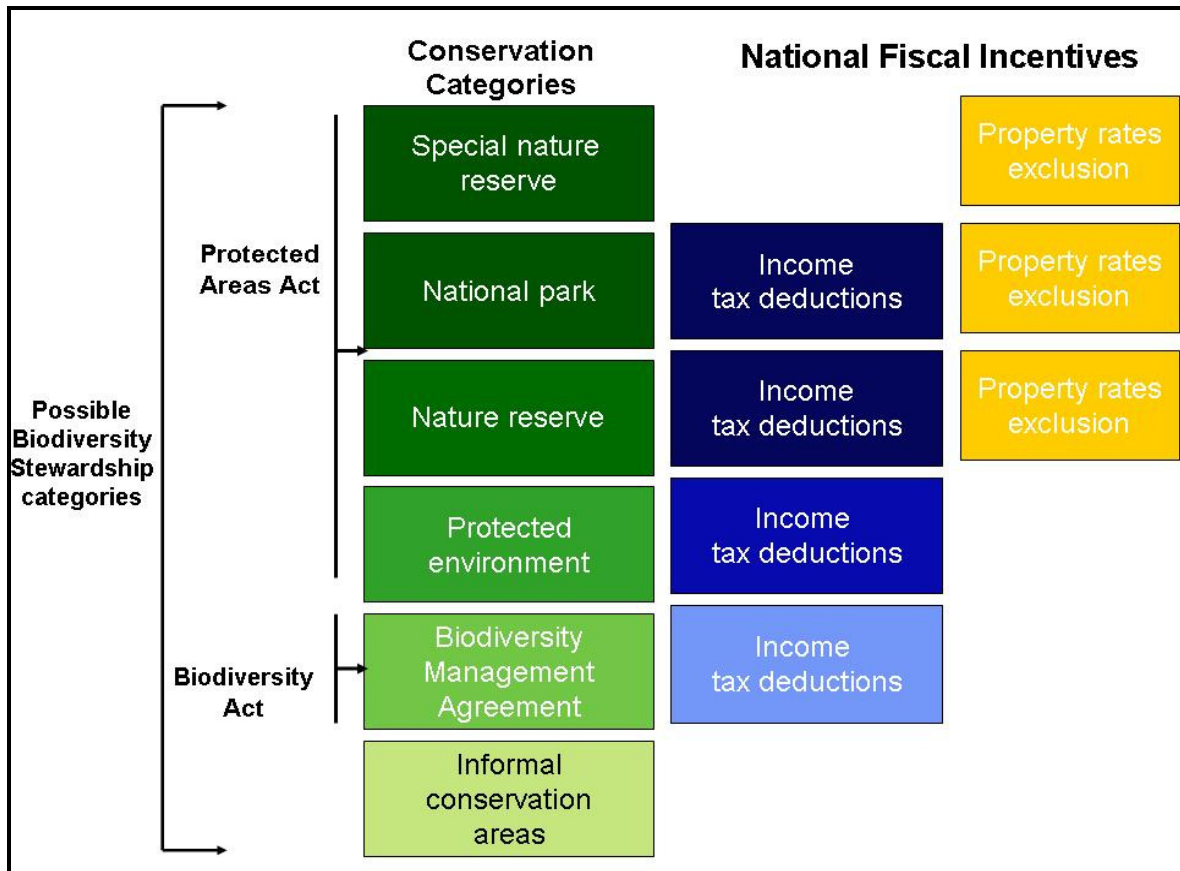
Biodiversity fiscal incentives fall into two categories: national and discretionary. National fiscal incentives are found in national legislation, and are automatically applicable across the country, provided certain criteria are met. Falling into this group are income tax based incentives, and property rates exclusions. These incentives are only available for certain of the statutory conservation categories which are recognised in national legislation and which include special nature reserves, national parks, nature reserves, protected environments and Biodiversity Management Agreements.

Discretionary fiscal incentives have the potential to be applied at the discretion of an implementing agent. They are not necessarily strictly for statutory conservation areas recognised in national legislation. Specifically, this document covers the role of local property rates policies to include property rates based fiscal incentives for biodiversity outcomes. It also touches briefly on emerging thinking around payments for ecosystem services (PES). An effective PES model could not only result in sound land management, but also address the major national challenge of poverty reduction, particularly in our marginalised rural areas.

Section 2 of the document explains the different conservation categories, from Special Nature Reserves through to informal conservation areas. Section 3 outlines the currently available biodiversity fiscal incentives. Section 4 explains how the available national fiscal incentives apply to the different conservation categories. The diagram below summarises the relationship between the conservation categories and available national fiscal incentives.

This document is intended for decision-makers and practitioners in the biodiversity sector, specifically those involved in the implementation of the National Protected Areas Expansion

Strategy and biodiversity stewardship programmes. It should also be of interest to biodiversity decision-makers and practitioners at the municipal level.



## 1 Introduction

The leading cause of biodiversity loss in South Africa is loss of natural habitat. In response to this, two main strategies exist: a) to expand the protected area network, and b) to manage threatened ecosystems sensitively and with production systems that are compatible with retaining biodiversity - in other words, encouraging sound stewardship of the land.

Outside of state-owned protected areas there is a hierarchy of conservation categories available to private and communal landowners who wish to conserve land of high biodiversity priority through entering agreements with conservation agencies.

In order to make stewardship by private and communal landowners more effective, the conservation sector has developed incentives to support landowners entering into these agreements. A range of incentives are needed, both to match different conservation categories and to meet the needs of the heterogeneous stakeholder base.

Different types of incentives include:

- Fiscal incentives - economic incentives based on government revenue or expenditure
- Technical and professional advice and support (for example, with developing management plans)
- Management assistance and support (for example, with clearing invasive alien plants, fire management, enforcement)
- Partnerships in nature-based commercial ventures and access to marketing resources
- Recognition

The focus of this document is on key fiscal incentives for biodiversity that have been developed and are starting to be implemented. The document does not cover non-fiscal incentives for biodiversity<sup>1</sup> or fiscal incentives for broader environmental outcomes (such as reducing carbon emissions or pollution, for example<sup>2</sup>).

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<sup>1</sup> For more on these see the Biodiversity Stewardship Guideline Document

<sup>2</sup> For more on the range of possible *environmental* fiscal incentives see National Treasury (2006) Draft Policy paper: A Framework for Considering Market Based Instruments to Support Environmental Fiscal Reform in South Africa. National Treasury, Pretoria

Intended users of this framework are decision-makers and practitioners in the biodiversity sector, especially those involved in the implementation of the National Protected Area Expansion Strategy and biodiversity stewardship programmes. It should also be of interest to biodiversity decision-makers and practitioners at the municipal level.

This framework is structured as follows:

- **Section 2** provides the context for the biodiversity fiscal incentives by outlining key aspects of relevant biodiversity legislation, policies and programmes which the incentives have been designed to serve. It includes an overview of the different conservation categories available to private landowners.
- **Section 3** describes existing biodiversity fiscal incentives for the purpose of providing an understanding of the spectrum of biodiversity fiscal incentives as they exist at present.
- **Section 4** links the conservation categories and the biodiversity fiscal incentives, explaining which incentives apply to which categories.

**Appendix 1** Provides an overview of the biodiversity fiscal incentives in tabular form.

## 2 Context for Biodiversity Fiscal Incentives

This section briefly outlines key aspects of relevant biodiversity legislation and policy: the Protected Areas Act, the Biodiversity Act, the National Protected Area Expansion Strategy, the National Biodiversity Framework. It also introduces biodiversity stewardship, the main implementing vehicle for conservation on private land.

### 2.1 *Relevant National Biodiversity Legislation*

The **National Environmental Management Act** (Act 107 of 1998) (NEMA) was created to provide the legal framework that aims to ensure that all people within South Africa have their constitutional environmental rights realised. NEMA, together with the Constitution, prepared the way for a suite of environmental legislation including the National Environmental Management: Protected Areas Act (Act 57 of 2003) and the National Environmental Management: Biodiversity Act (Act 10 of 2004). These two Acts provide the legal enabling environment for ensuring the sound management of biodiversity and biodiversity conservation.

#### 2.1.1 The National Environmental Management: Protected Areas Act

The National Environmental Management: Protected Areas Act 57 of 2003 (hereafter referred to as the Protected Areas Act) creates a framework for the declaration and management of protected areas. The Act further aims to provide a representative network of protected areas on state, private and communal land, while promoting the sustainable utilisation of protected areas for human benefit without losing the ecological character of the area. Additionally the Act encourages local community participation in the management of protected areas and aims to balance the relationships between biodiversity conservation, human settlement and economic development.

The Protected Areas Act provides for four categories of protected areas, namely:

- Special Nature Reserves (Section 18)
- National Parks (Section 20)
- Nature Reserves (Section 23)

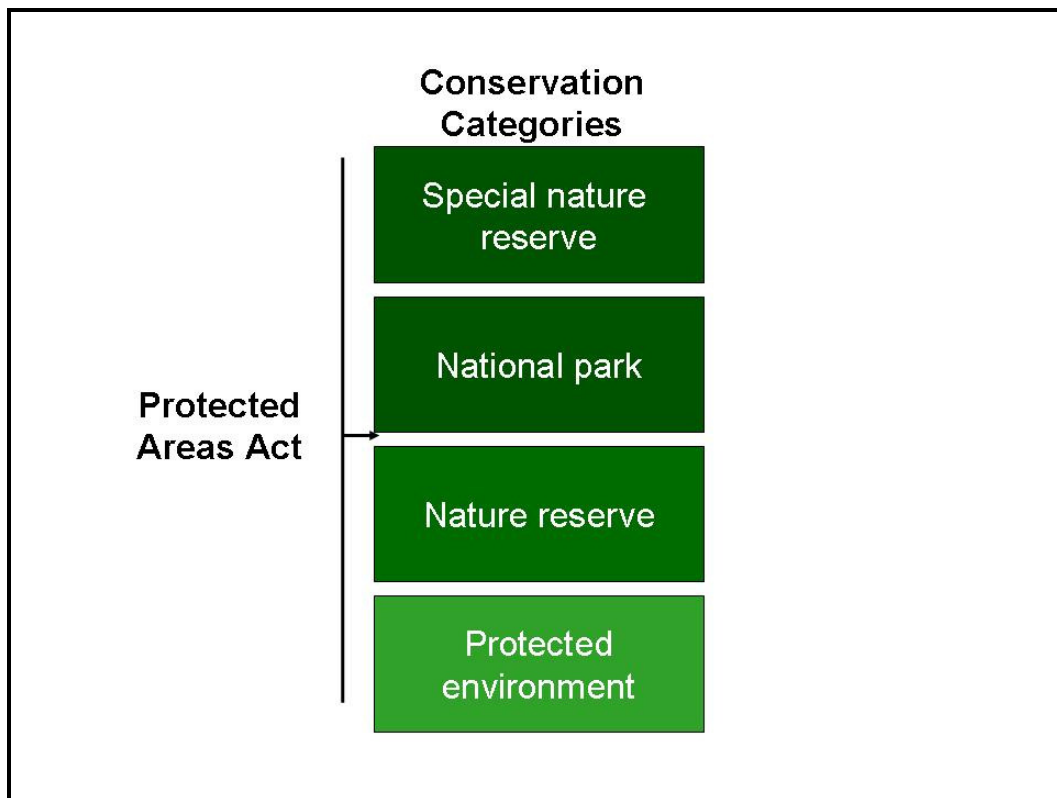


- Protected Environments (Section 28 )<sup>3</sup>

These categories all require:

- Formal declaration of the land either by the Minister or provincial MEC
- Restrictions placed on the land which are recorded in the title deed (optional for Protected Environments); and
- Adherence to a management plan

All four of these protected area categories can be declared on private or communal land with the consent of the landowner. Furthermore, the management authority of such land need not be an organ of state, and could be the landowner. These two provisions in the Protected Areas Act laid the basis for the development of contract protected areas through biodiversity stewardship programmes, explained in section 2.4.



**Figure 1: Conservation categories available in terms of the Protected Areas Act**

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<sup>3</sup> The Protected Areas Act also recognises Mountain Catchment Areas, Protected Forest Areas, World Heritage Sites, and Marine Protected Areas. However, these protected areas are also governed by other legislation and do not have promulgated regulations in terms of the Protected Areas Act outlining allowed and disallowed developments, nor do they have stipulated management obligations in terms of the Protected Areas Act.

### 2.1.2 National Environmental Management: Biodiversity Act

The National Environmental Management: Biodiversity Act 10 of 2004 (hereafter referred to as the Biodiversity Act) provides a range of tools for biodiversity planning and management. These include the National Biodiversity Framework (see section 2.2.1) and Biodiversity Management Agreements. Biodiversity Management Agreements are agreements entered into by the Minister and the responsible person, organisation or organ of state with regard to the sound management of land.

Biodiversity Management Agreements can be grouped with the protected area categories in the Protected Areas Act, to form the *statutory conservation categories*. These statutory conservation categories are being implemented through biodiversity stewardship programmes (see section 2.4).

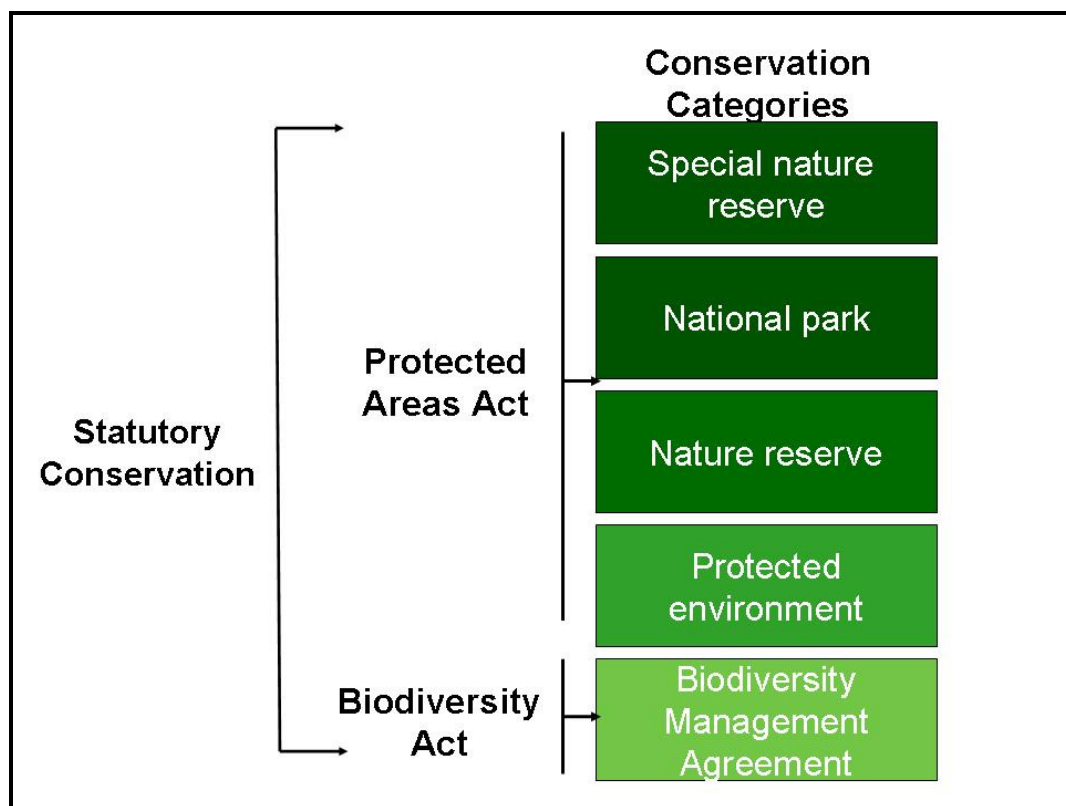


Figure 2: Conservation categories available in terms of the Protected Areas Act and the Biodiversity Act

## 2.2 Relevant National Policy

### 2.2.1 National Biodiversity Framework

The National Biodiversity Framework (NBF) is a five-year framework that aims to coordinate and align the efforts of organs of state in all spheres of government, nongovernmental organisations, the private sector and local communities, and other stakeholders as they relate to biodiversity management and related activities.

The NBF identifies thirty-three Priority Actions. Of particular relevance to this framework are:

- **Priority Action 2:** Integrate biodiversity considerations into fiscal policy through environmental fiscal reform, including the development of fiscal incentives for the conservation of biodiversity
- **Priority Action 30:** Implement the National Protected Area Expansion Strategy
- **Priority Action 31:** Establish and strengthen provincial stewardship programmes
- **Priority Action 32:** Strengthen programmes that support the informal conservation area system

### 2.2.2 National Protected Area Expansion Strategy

The National Protected Area Expansion Strategy (NPAES), developed in 2008, sets protected area targets for South Africa, provides maps of focus areas for protected area expansion, and makes recommendations on mechanisms for protected area expansion. The two main mechanisms identified for expanding the land-based protected area network are:

- acquisition of land,
- contract agreements with private and communal landowners/users, developed through biodiversity stewardship programmes.

It is neither desirable nor financially feasible for government to purchase all the land identified as high priority for meeting protected area targets. The NPAES recommends that contract agreements through biodiversity stewardship programmes should play an increasingly important role in protected area expansion. Furthermore, the NPAES advocates the use of fiscal incentives to support this.

### 2.3 *Informal Conservation Areas*

Beyond the expansion of the statutory conservation network, there remains a need to maintain the integrity of ecosystems across broader landscapes. This contributes not only to the sound functioning of proximate protected ecosystems and linkages between ecosystems, but also provides ecosystem services and supports livelihoods beyond protected areas.

Informal conservation areas include:

- the lowest (non-binding) level of biodiversity stewardship (see Figure 4),
- conservancies and game farms, if they are compatible with sound management of biodiversity, provide key ecosystem services or provide a buffer for protected areas.

South Africa is engaged in several international programmes that support the establishment of informal conservation areas, including the Man and the Biosphere Programme and the Ramsar Convention.

The NBF recognises both the distinction between statutory conservation and informal conservation, and the importance of supporting informal conservation areas, in Priority Action 32.

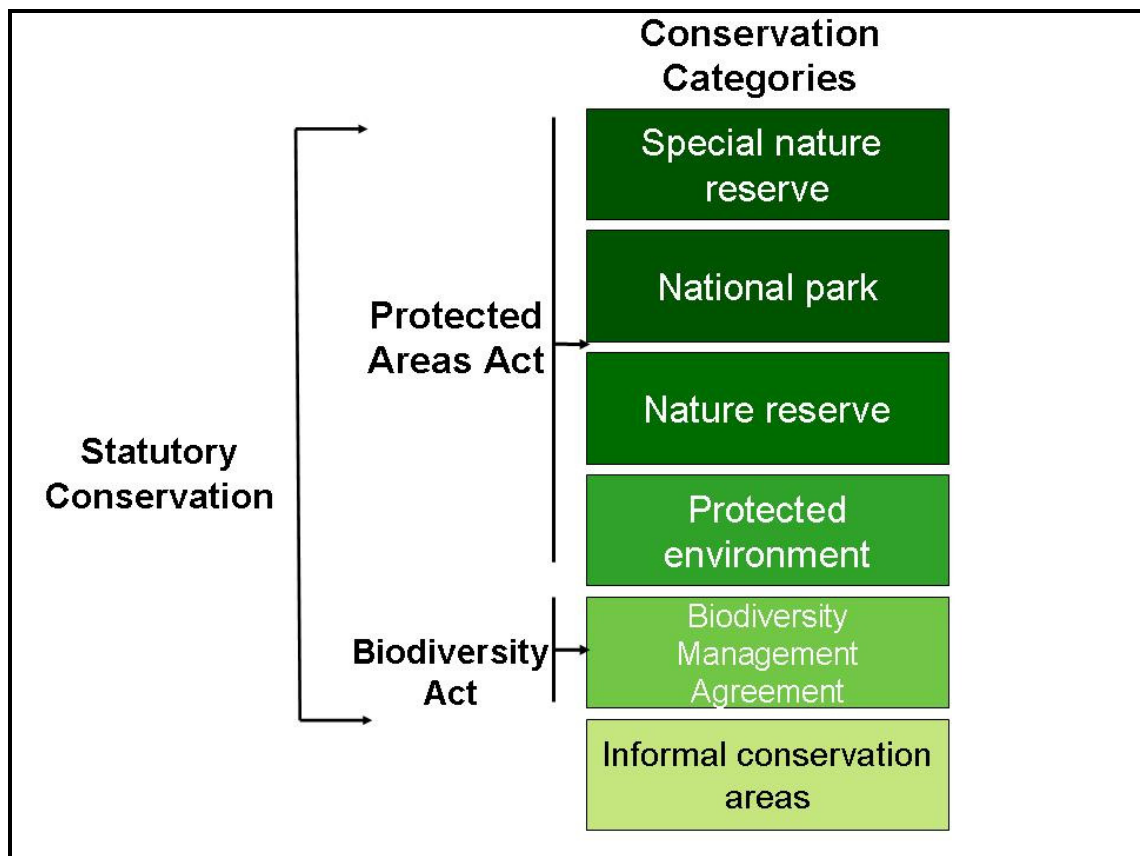


Figure 3: Statutory and informal conservation categories

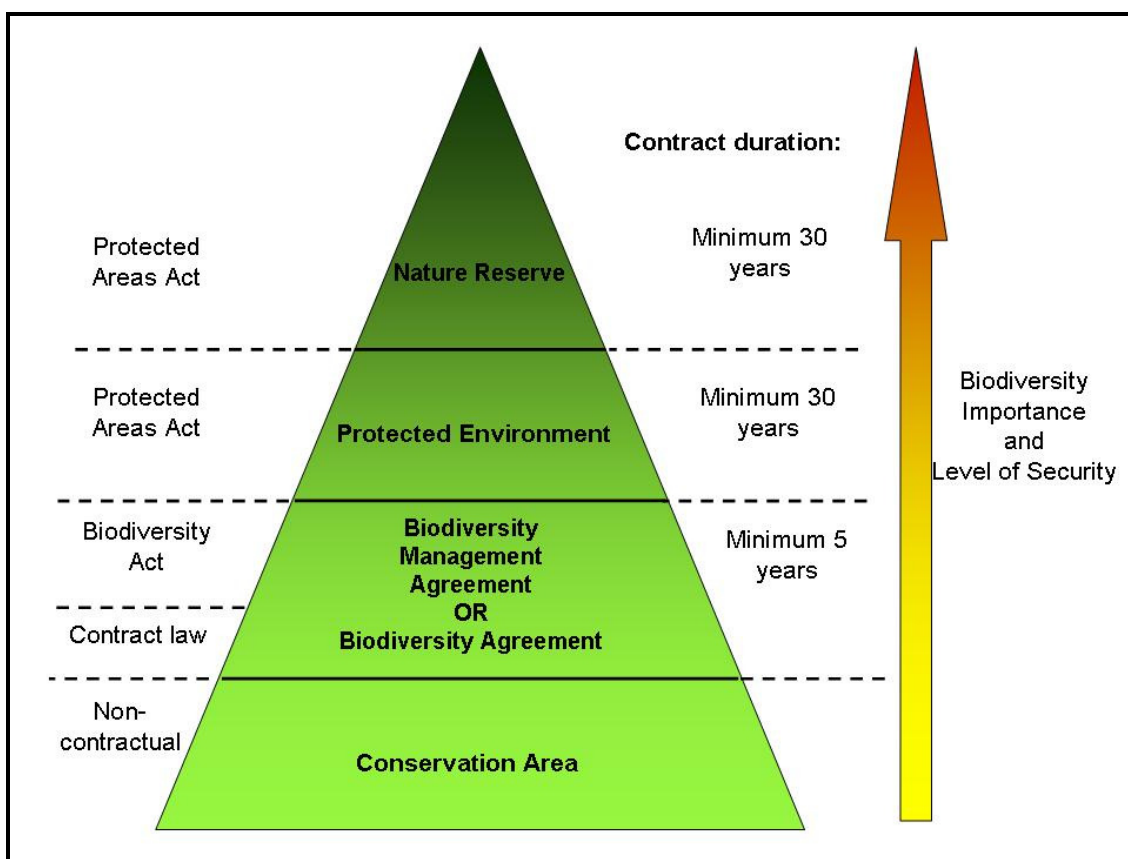
## 2.4 Biodiversity Stewardship Programmes

Biodiversity stewardship has been implemented in South Africa over the past several years and in that time has gained importance as a key mechanism to secure priority biodiversity on land outside of state-owned protected areas through contractual agreements with land owners. Some provinces have well-developed biodiversity stewardship programmes, others are in the process of initiating or establishing them.

Biodiversity stewardship plays a central role in the implementation of the NPAES and the achievement of South Africa's protected area targets. It can also play a critical role in securing threatened ecosystems, for which the establishment of large traditional state-owned protected areas is usually no longer feasible. Further, biodiversity stewardship contributes to broader socio-economic goals such as rural development and creation of green jobs, and has the potential to make significant contributions to land reform and livelihoods of land reform beneficiaries.

Biodiversity stewardship provides a cost-effective mechanism for government to carry out its conservation mandate and achieve protected area targets, at much lower cost to protected area agencies than acquisition of land. The lower cost is partly the result of savings from not having to purchase land, and partly the result of much of the ongoing cost of managing the land being borne by the landowner not the conservation agency.

Biodiversity stewardship programmes use a hierarchy of conservation categories provided for in the Protected Areas Act, the Biodiversity Act and contract law to secure land for conservation (see Figure 4). Each category has a minimum duration for the contractual agreement. The degree of biodiversity importance of the site and the degree of security associated with the contract increase as one moves up the hierarchy of conservation categories.



**Figure 4: A typical set of conservation categories used in a biodiversity stewardship programme**

(Note: Biodiversity stewardship could also include Special Nature Reserves and National Parks, but most biodiversity stewardship programmes tend not to focus on these two categories)

The biodiversity stewardship programmes:

- provide an extension service to participating landowners;
- draw up and manage contracts and management plans;
- facilitate the protected area declaration process; and
- audit the agreements.

A Biodiversity Stewardship Policy, and a Biodiversity Stewardship Guideline Document have been developed.

### 3 Outline of Available Biodiversity Fiscal Incentives

Incentive mechanisms can range from financial and tangible to non-financial and less tangible, such as social, cultural or moral incentives. As noted in section 1, fiscal incentives are one of many types of incentives that can be applied. Both the NBF and the NPAES call for the development and use of fiscal incentives for the conservation of biodiversity on private and communal land.

This section outlines biodiversity fiscal incentives available in terms of current legislation, and briefly discusses two related issues: perverse incentives discouraging game farms and payments for ecosystem services.

In developing biodiversity fiscal incentives the aim has been to develop a suite of fiscal tools that encourage conservation outcomes in different landowner situations, and that can be applied to different conservation categories.

#### **Box 1. Fiscal Incentives: Guiding Principles**

South Africa has three key principles of taxation: ease of implementation, certainty, and simplicity. Biodiversity fiscal incentives have been designed to adhere to these three principles. In addition, there are specific principles followed for biodiversity fiscal incentives:

- The incentives aim to ensure the conservation and sustainable use of biodiversity, through encouraging sound land management within South Africa's biodiversity priority areas.
- The Provider-Gets principle, which is embodied in numerous environmental fiscal policies across the globe, allows for fiscal incentives to accrue to the person(s) responsible for providing a public good.
- Biodiversity and other environmental taxes should be part of a tax shifting exercise, rather than increasing the overall tax burden of the country.
- In order for fiscal incentives to be effective, cohesion needs to be found within the tax and regulatory systems, and perverse incentives and anomalies currently found within these systems must be addressed.
- While some environmental taxes might aim to raise revenue, biodiversity taxes aim to encourage a behaviour change, thereby making the biodiversity outcomes more important than revenue raising.
- For biodiversity taxes that are aimed at incentivising behaviour, the neutrality principle no longer applies. The neutrality principle requires that the tax system should have a minimal influence on the economic decision-maker.



Two categories of biodiversity fiscal incentives exist: national fiscal incentives and discretionary fiscal incentives.

**National fiscal incentives** are provided for in national legislation, and apply automatically to any landowner who meets certain specified conditions. Currently, national fiscal incentives consist of biodiversity-based tax deductions and national property rates exclusions, and apply only to statutory conservation categories.

**Discretionary fiscal incentives** do not automatically apply to any scenario, but are rather implemented at the discretion of an agency. For example, a local municipality may *choose* to allow rate rebates to landowners in return for certain agreed upon management actions such as, for example, clearing invasive alien plants on their land.

One advantage of discretionary fiscal incentives is that they can be applied in a wider set of situations and can be tailored to meet specific biodiversity management needs in a particular region.

The fiscal incentives are described in more detail below.

### 3.1 *National Fiscal Incentives*

#### 3.1.1 Income Tax Deductions

Tax based biodiversity incentives were promulgated in the Revenue Laws Amendment Act 60 of 2008, and have been incorporated into the Income Tax Act 58 of 1962. The incentives are effective from the 2009/2010 tax year.

The incentives are designed to address only statutory conservation. Furthermore, they depend on the existence of a contract with a specified duration between the landowner and a conservation agency.

In response to the commitments of landowners to formally secure biodiversity on their land and thereby to contribute to the public good, National Treasury has recognised that:

- a) Landowners have forgone use rights to their land, which have inherent value, and

b) Landowners often incur substantial costs in managing their land under these agreements.

Tax deductions have therefore been offered to address these costs.

For some landowners, income tax deductions will provide a strong incentive to protect their land formally. In other circumstances, income tax deductions will at least provide landowners who are *already* willing to conserve their land with some form of compensation. It is important to note that the income tax mechanisms can only be effective incentives for landowners who are generating enough income to make the income tax deductions significant.

The income tax deductions currently available are explained in more detail below.

**Income Tax Deductions on Management Expenses:**

For Biodiversity Management Agreements with minimum 5 year contracts

All conservation and maintenance expenses incurred in terms of a Biodiversity Management Agreement are to be treated as expenditure incurred in the production of income and for purposes of trade. Examples of these expenses could be rehabilitation expenses, alien clearing or burning fire breaks. However, expenses are only deductible if the activity is reflected in the management plan linked to the Biodiversity Management Agreement.

Important factors:

- The taxpayer may only make these deductions from income generated from the land subject to the Biodiversity Management Agreement, or land in the immediate proximity. The Act does not define ‘immediate proximity’, but it is taken to mean neighbouring, or within a few kilometres of the land under the BMA.
- The deduction may not exceed the income of the taxpayer derived in the year of assessment. However, the amount by which the deduction exceeds the income will be deemed to be expenditure incurred by the taxpayer in the following year of assessment. In other words, a roll-over of deductions

**Farmers** entering into Biodiversity Management Agreements are subject to the same deductions, with the only difference being:

- The deductions are allowed for under paragraph 12(1A) of the First Schedule. This portion of the Income Tax Act deals specifically with all allowable deductions made by farmers.
- The deductions are limited to income derived by the taxpayer from farming activities on the land or within the immediate proximity of the land.

#### **Recoupment clause**

- If the taxpayer is in breach of the agreement, the amount of the deductions previously allowed in the five years preceding the contravention would be recouped<sup>4</sup>.

#### **18A Deductions from Income Tax on Management Expenses:**

For Protected Environments, National Parks, Nature Reserves, with minimum 30 year contract

All conservation and maintenance expenses are deemed to be Section 18A deductible donations. This means that expenses related to the management of the land, as required by the Management Plan, can be deducted from the taxpayer's taxable income<sup>5</sup>. Activities not required in the management plan are not deductible.

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<sup>4</sup> SARS would recover the money by including it in the amount owed to them in the tax year in which the breach arose

<sup>5</sup> Gross income - exemptions = Income

Income - Deductions + Taxable Capital Gains = Taxable Income

### **Box 2: 18A Deductions**

An '18A deduction' refers to deductions from taxable income allowable under Section 18A of the Income Tax Act 58 of 1962 (Chapter II, Part I, Section 18A).

This Section allows the taxpayer to deduct from their taxable income donations made in cash or of property made in kind to Public Benefit Organisations, which includes Government Departments.

**NB:** An 18A deduction may not exceed 10% of the taxpayer's taxable income.

### **Recoupment clause**

- If the taxpayer is in breach of the agreement, he/she will be subject to a recoupment of the deductions previously allowed in the five years preceding the contravention.

### **18A Deductions from Income Tax on Value of Land:**

For National Parks and Nature Reserves with minimum 99 year contract

The value of land is deemed to be a Section 18A deductible donation. This means that the taxpayer may deduct the value of the land from their taxable income. This deduction must follow some prescribed guidelines, outlined below.

- Taxpayers under this agreement are still entitled to deduct management expenses from their income, as outlined above.

### **Calculating the value:**

***If the land owner does not retain any right of use of the property under declaration (such as residential or commercial use)***

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:
  - the cost to purchase the land, or
  - the market value of the land

- In other words, each year, for ten years, the land owner may deduct:

$$10\% \times \text{Lesser of cost or market value of the land}$$

***If the land owner does retain some right of use over the property***

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:
  - the cost to purchase the land, or
  - the market value of the land
- This 10% amount must then be multiplied by the ratio of the market value of the land reduced by the right of use as that amount bears to the value of the land as if that land had been donated full, as depicted in the formula below:

$$10\% \times \text{Lesser of cost or market value declared} \times \frac{\text{Market value of land subject to the right of use}}{\text{Market value of land if there had been no right of use retained}}$$

**Duration of deduction**

- The taxpayer may deduct the amount in the year of declaration, and again in each of the following nine years. This means that by the end of the ten year period, the full base value (cost or market value as the case may be, reduced to take account of any right of use that was retained), may have been deducted.
- There is no allowance for a roll-over of deductions into the following year, should there be no or insufficient income from which to make the deduction in any given year.

**Recoupment clause**

- If the taxpayer is in breach of the agreement, he/she will be subject to a recoupment of the deductions previously allowed in the five years preceding the contravention.

### Implementation and Auditing of the Income Tax Deductions

The income tax deduction is claimed when the landowner completes his/her tax return. South African Revenue Service (SARS) has the right to audit this deduction, as they do with any other tax transaction. SARS will only audit:

- Whether the land is formally protected, with the relevant contract agreement and declaration;
- whether the management expenses claimed are real expenses (i.e. proof of payment must be kept); and
- whether the management activity is required in the management plan.

The landowner is audited separately on their meeting the requirements of their agreement with the conservation agency, and the requirements of the declaration on the land.

#### 3.1.2 Property Rates Exclusions

For Special Nature Reserves, National Parks and Nature Reserves

Property rates have the potential to significantly affect land use decisions. In the past, landowners outside of urban areas were not subject to property rates. Under the Municipal Property Rates Act 6 of 2004, municipalities are now able to rate rural properties within their jurisdiction. In some cases, landowners who were not required to pay rates before may be facing prohibitively high rates - high enough to stimulate a change in land use behaviour in order to lessen the rates burden. Often this change can result in the conversion of natural habitat to agriculture, even in marginal agricultural land, simply to take advantage of the agricultural rates rebate. However, property rates can also provide an opportunity to incentivise sound land use behaviour and biodiversity conservation.

Property rates can positively influence biodiversity at two levels - national and local. Local property rates fall under the category of discretionary fiscal incentives (see section

3.2.1). At the national level, the Municipal Property Rates Act provides national fiscal incentives in the form of property rates exclusions.<sup>6</sup>

Section 17 (1) (e) of the Municipal Property Rates Act states that special nature reserves, national parks and nature reserves are excluded from paying property rates. This exclusion applies only to those portions of the land that are not used for commercial, business, agricultural or residential purposes. It is important that municipalities apply this in line with the intention of the law, which is to rate only the actual improved areas. This is best illustrated with an example of nature reserve with a lodge and game drives. The lodge should be liable for property rates, but the remainder of the nature reserve, including the land over which game drives are taken, should not be rated.

### 3.1.3 Game farms and Property Rates: A Perverse Incentive?

Currently, the Municipal Property Rates Act, Section 1(b), defines game farming activities as commercial activities, and specifically excludes game farm activities from agricultural activities. As a result, game farms are liable for up to eight times greater property rates than what would be levied on the land if it was considered agricultural land. This may motivate landowners to convert game farms, which could be providing a corridor or maintaining biodiversity, to intensive agriculture.

## 3.2 Discretionary Fiscal Incentives

Discretionary fiscal incentives can be applied at the discretion of an implementing agent. This means that these incentives can be used in a range of circumstances, according to the needs of the implementing agency. Discretionary fiscal incentives should be applied in:

- those statutory conservation areas where existing national fiscal incentives will have little or no influence, usually because the levels of income being generated are too low for income tax deductions to provide a major incentive (e.g. in communal lands)
- informal conservation areas, where no national fiscal incentives apply

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<sup>6</sup> Property rates exclusions are different from property rates exemptions. Exclusions are determined nationally and apply automatically in all municipalities. Exemptions are determined by local property rates policies and apply only in the municipality concerned. See box on important property rates terms and definitions.

Currently, the only existing discretionary fiscal incentives are property rates exemptions (different from property rates exclusions), property rates rebates and property revaluations. However, there are a number of promising opportunities to develop additional discretionary fiscal incentives that can have a much wider reach. Arguably the most important is payments for ecosystem services (PES). For this reason, PES is outlined briefly in this section.

### **3.2.1 Local Property Rates Policies**

Municipal rates policies are governed by the Municipal Property Rates Act. Municipalities are responsible for developing their own rates policies in accordance with the Act. These policies are subject to annual review, and may be amended. They are also responsible for ensuring that all properties are valued. The valuation of a property has a direct impact on the rates the landowner is liable for, apart from those properties excluded from paying rates.

Municipalities have the opportunity to use the rates policy to achieve their own specific objectives related to natural ecosystems, for example, fire mitigation by encouraging the clearing of alien invasive plants, flood mitigation through maintaining natural ecosystems such as wetlands, or securing biodiversity priority sites on private land.

### **Property Rates Rebates and Exemptions**

Under the Municipal Property Rates Act, local municipalities are entitled to offer property rates rebates or exemptions for defined categories of properties within their jurisdiction. This would be done through a contractual agreement between the landowner and the municipality, requiring certain management actions on the land, and/or placing certain restrictions on the land. The capacity and objectives of the municipality should drive the complexity and degree of landowners' commitments in these agreements.

Certain metropolitan municipalities have used their rates policies to incentivise local biodiversity stewardship agreements. Nelson Mandela Bay Municipality, for example, offers rates rebates and exemptions to landowners within biodiversity priority sites who have signed a contract with the metropolitan municipality specifying land use restrictions and responsibilities.



Metropolitan municipalities are relatively well capacitated to use their rates policies to achieve a range of biodiversity conservation objectives. For less well resourced local municipalities, more discrete goals could be reached through contracts with landowners requiring more simplified actions. For instance, a single ecosystem service, such as water provisioning through maintaining natural grasslands, could be managed through a contract between the landowner and the municipality, with resulting rates rebates.

### **Property Valuation Reductions and Environmental Servitudes**

Property valuation reductions allow the municipality to reduce the rates paid by the land owner by reducing the valuation of the property on the valuation roll. This is done by declaring an 'environmental servitude' on a portion or all of the property. The servitude is written against the title deed of the property, and thereby becomes binding. The property is then devalued on the valuation roll to reflect the diminished development rights. As property rates are a function of the land value, the land owner will subsequently be charged a lower property rate. This mechanism has been applied in eThekweni Metropolitan Municipality.

Property valuation reductions can be used on properties or portions of properties that the municipality would like to remain undeveloped, or properties that should not be developed due to international agreements, such as Ramsar or Bonn sites.

While municipalities must record exemptions and rebates as expenditure in the municipal annual budgets, reduced valuations are not reflected in the budgets.

#### **Box 3: Property Rates: Important Terms and Definitions**

Exclusions: The Municipal Property Rates Act defines categories of land types that are excluded from paying property rates. These exclusions apply nationally.

Exemptions and Rebates: Determined by each municipality's property rates policy developed in accordance with the Municipal Property Rates Act. Applies to categories of properties or landowners.

Property Valuations: Conducted by municipalities in accordance with the Municipal

Property Rates Act, and can be applied to categories of land or individual properties.

### 3.2.2 Payments for Ecosystem Services (PES)

PES is in the very early stages of development in South Africa, and could play a significant role in both biodiversity management and development of impoverished rural economies.

The central principle of PES is that recipients of environmental services should pay for their provision, and providers of environmental services should be compensated for doing so. Application of PES often includes the additional benefit of providing an income source to poor and marginalised communities.

The ASGISA 2008 annual report<sup>7</sup> recognises that severe inequality in the economy remains a critical challenge for South Africa. Sometimes referred to as the ‘second economy’, these marginalised communities are spatially skewed towards rural areas, with little infrastructure and few development opportunities. However, these same rural poverty nodes often supply, or could supply through ecosystem restoration, critical ecosystem services to the more developed parts of the country. In particular, the ecosystem services of carbon sequestration, surface water supply, water flow regulation and soil retention are often concentrated in these areas.

Currently, there are few cases in which land users (private or communal) have engaged in efforts to conserve natural capital or rehabilitate degraded lands. This is largely because, while these landowners are providing key ecosystem services to broader society, they are not seeing the direct benefits of this. As a result, land is often mismanaged and ecosystem services deteriorate. A PES scheme is able to address this market failure directly, by channelling financial rewards to land users and owners in return for sound land management. As noted, this can provide critical income to impoverished land users, who would otherwise have little chance of entering the cash economy. PES can thus be a useful vehicle for national income redistribution.

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<sup>7</sup> The Presidency of South Africa. Annual Report 2008: Accelerated and Shared Growth Initiative for South Africa

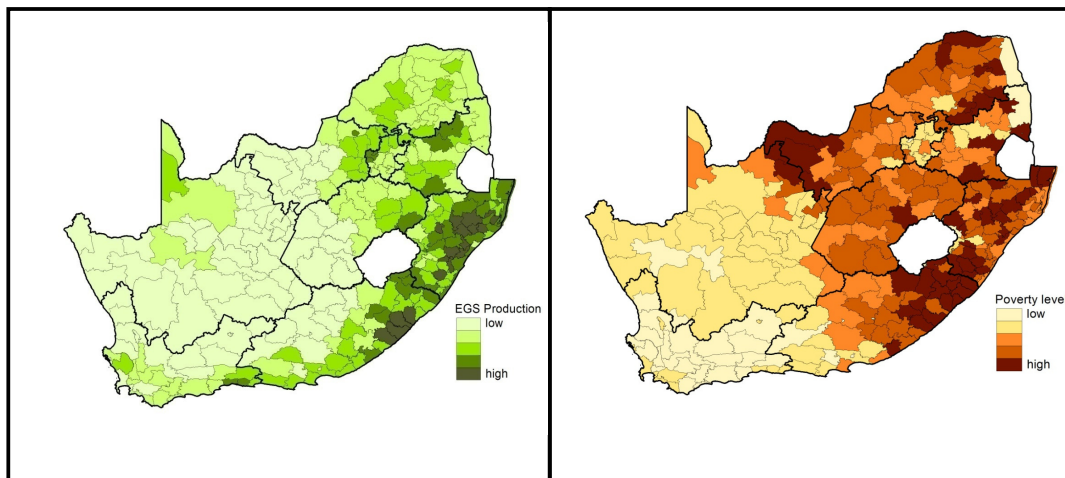
Emerging national strategies designed to address the economic marginalisation of rural communities include PES (TIPS 2009)<sup>8</sup>. PES could be a powerful tool for poverty reduction, particularly in communal areas and land reform sites where other fiscal incentives for conservation are likely to be ineffective. Given the important role PES can play, for biodiversity, ecosystem services and poverty reduction, it is imperative that key agencies support and participate in the emerging thinking and development around PES.

Blignaut *et al* (2008)<sup>9</sup> mapped areas of high ecosystem service productivity in South Africa. The ecosystem services considered were carbon sequestration, surface water supply, water flow regulation and soil retention, with a focus on intact ecosystems as well as degraded landscapes that could provide ecosystem services through the restoration process

Figure 5(a)).

This ecosystem service production map was then compared with South Africa's poverty nodes

Figure 5(b)), showing a strong geographic correlation between production of ecosystem services and poverty. An overlay of the two maps helps to identify priority areas for implementing PES projects (Figure 6).



**Figure 5: (a) Production of ecosystem goods and services; (b) Poverty levels by local municipality**

<sup>8</sup> TIPS (2009) The Second Economy Strategy: Addressing Inequality and Economic Marginalisation. An initiative of the Presidency

<sup>9</sup> Blignaut, J., Marias, C., Rouget, M., Mander, M., Turpie, J., Preston, G., Philip, K., du Plessis, L., Klassen, T., Tregurtha, N. (2008) Making Markets Work for People and the Environment. Research paper commissioned by The Second Economy Strategy Project, an initiative of the Presidency

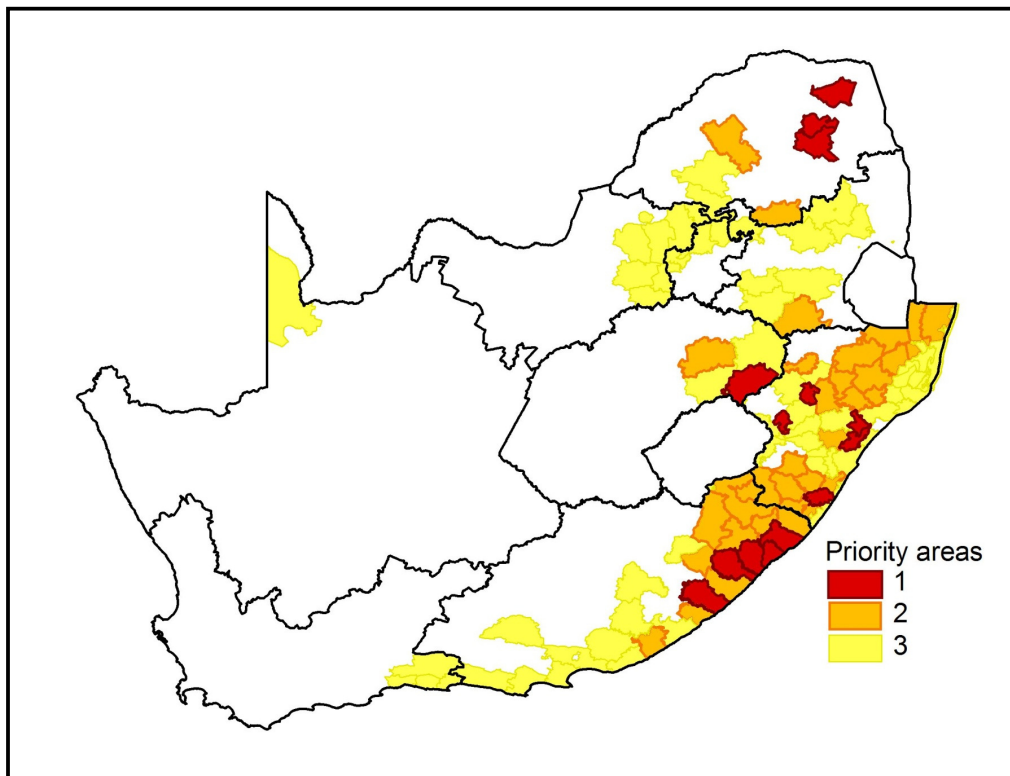


Figure 6: Overlap between areas of high production of ecosystem services and high poverty levels, to identify priority areas for implementing PES projects

## 4 Application of Biodiversity Fiscal Incentives to Conservation Categories

This section sets out how national fiscal incentives apply to the different statutory conservation categories in the Protected Areas Act and Biodiversity Act. It does not address discretionary fiscal incentives, as there is much more flexibility in how these are applied. Table 1 and Figure 7 summarise the relationship between the various national fiscal incentives explained in section 3.1 and the different conservation categories outlined in section 2.

Note: There is some repetition in the subsections that follow, as the same incentives often apply to more than one conservation category.

**Table 1: Summary of application of national biodiversity fiscal incentives to different conservation categories**

Conservation Category	Applicable National Fiscal Incentives
Special Nature Reserve	Property rates exclusion
National Park Min 99 year contract	Property rates exclusion
	18A Tax deduction: value of land
	18A Tax deduction: management expenses
National Park Min 30 year contract	Property rates exclusion
	18A Tax deduction: management expenses
Nature Reserve Min 99 year contract	Property rates exclusion
	18A Tax deduction: value of land
	18A Tax deduction: management expenses

Nature Reserve Min 30 year contract	Property rates exclusion
	18A Tax deduction: management expenses
Protected Environment Min 30 year contract	18A Tax deduction: management expenses
Biodiversity Management Agreement Min 5 year contract	Tax deduction: management expenses

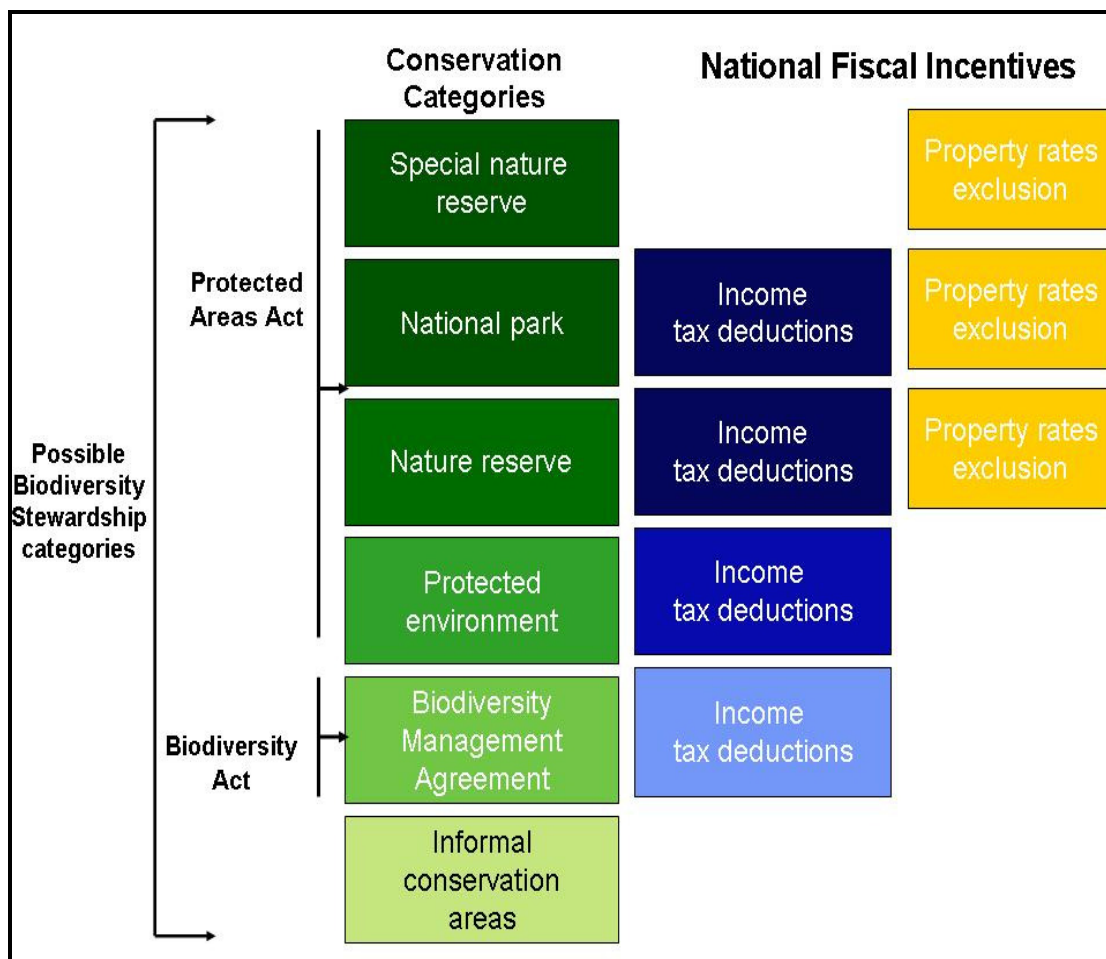


Figure 7: Summary of application of national biodiversity fiscal incentives to different conservation categories

## 4.1 *Special Nature Reserves*

### Special nature reserves

### Property rates exclusion

#### Property Rates Exclusion

The Municipal Property Rates Act Section 17 (1) (e), states that special nature reserves, national parks and nature reserves are excluded from paying property rates.

This exclusion applies only to those portions of the land that are not used for commercial, business, agricultural or residential purposes. It is important that municipalities administer this exclusion in line with the intention of the law, which is to rate only the actual improved areas of the activity. This is best illustrated with an example of nature reserve with a lodge, and game drives. The lodge should be liable for property rates, but the remainder of the nature reserve, including the land over which game drives are taken, should not be rated.

There are no income tax incentives for Special Nature Reserves.

## 4.2 National Parks

### National park 99 year agreement

#### Property rates exclusion

Income tax deduction: value of the land

Income tax deduction: land management expenses

### National park 30 year agreement

#### Property rates exclusion

Income tax deduction: land management expenses

### Property Rates Exclusion

The Municipal Property Rates Act Section 17 (1) (e), states that special nature reserves, national parks and nature reserves are excluded from paying property rates.

This exclusion applies only to those portions of the land that are not used for commercial, business, agricultural or residential purposes. It is important that municipalities administer this exclusion in line with the intention of the law, which is to rate only the actual improved areas of the activity. This is best illustrated with an example of nature reserve with a lodge, and game drives. The lodge should be liable for property rates, but the remainder of the nature reserve, including the land over which game drives are taken, should not be rated.

### Income tax deductions: For National Park with a minimum contract of 30 years

In terms of the Income Tax Act, all conservation and maintenance expenses are deemed to be Section 18A deductible donations. This means that expenses related to the management of the land, as required by the Management Plan, can be deducted from the taxpayer's taxable income<sup>10</sup>. Activities undertaken that are not required in the management plan are not deductible.

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<sup>10</sup>Gross income - exemptions = Income



This deduction is allowed for the duration of the declaration and contract (the contract may be renewed).

This deduction is subject to the 10% cap prescribed for all 18A deductions (see Section B Tax incentives)

If the taxpayer is in breach of the agreement, he/she will be subject to a recoupment of the deductions previously allowed in the five years preceding the contravention.

**Income tax deductions: For National Park with a minimum contract of 99 years**

In addition to the deduction described above, the value of the land that is declared is deemed to be a Section 18A deductible donation. This means that the taxpayer may deduct the value of the land from their taxable income.

Taxpayers under this agreement are still entitled to deduct management expenses from their income. However, both these deductions, combined, must fit under the 10% cap prescribed for all 18A deductions.

The taxpayer may deduct the amount in the year of declaration, and again in each of the following nine years. This means that by the end of the ten year period, the full base value may have been deducted. There is no allowance for a roll-over of deductions into the following year, should there be no or insufficient income from which to make the deduction in any given year.

If the land owner retains some right of use over all or a portion of the land, this must be taken into account in determining amount that is deductible (outlined in *calculating the value* below).

Calculating the value of the land follows prescribed guidelines, outlined below.

***Calculating the value:***

**If the land owner does not retain any right of use of the property under declaration (such as residential or commercial use)**

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Income - Deductions + Taxable Capital Gains = Taxable Income

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:
  - the cost to purchase the land, or
  - the market value of the land
- In other words, each year, for ten years, the land owner may deduct:

10%	x	Lesser of cost or market value of land
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**If the land owner does retain some right of use over the property**

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:
  - the cost to purchase the land, or
  - the market value of the land
- This 10% amount must then be multiplied by the ratio of the market value of the declared land reduced by the right of use as that amount bears to the value of the declared land as if that declared land had been donated full, as depicted in the formula below:

10%	x	Lesser of cost or market value of land	x	Market value of land subject to the right of use
				Market value of land if there had been no right of use retained

### 4.3 Nature Reserves

#### Nature reserve 99 year agreement

#### Property rates exclusion

Income tax deduction: value of the land

Income tax deduction: land management expenses

#### Nature reserve 30 year agreement

#### Property rates exclusion

Income tax deduction: land management expenses

#### Property Rates Exclusion

The Municipal Property Rates Act Section 17 (1) (e), states that special nature reserves, national parks and nature reserves are excluded from paying property rates.

This exclusion applies only to those portions of the land that are not used for commercial, business, agricultural or residential purposes. It is important that municipalities administer this exclusion in line with the intention of the law, which is to rate only the actual improved areas of the activity. This is best illustrated with an example of nature reserve with a lodge, and game drives. The lodge should be liable for property rates, but the remainder of the nature reserve, including the land over which game drives are taken, should not be rated.

#### Income tax deductions: For Nature Reserve with a minimum contract of 30 years

In terms of the Income Tax Act, all conservation and maintenance expenses are deemed to be Section 18A deductible donations. This means that expenses related to the management of the land, as required by the Management Plan, can be deducted from the taxpayer's taxable income<sup>11</sup>. Activities undertaken that are not required in the management plan are not deductible.

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<sup>11</sup>Gross income - exemptions = Income

Income - Deductions + Taxable Capital Gains = Taxable Income

This deduction is allowed for the duration of the declaration and contract (the contract may be renewed).

This deduction is subject to the 10% cap prescribed for all 18A deductions (see Section B Tax incentives).

If the taxpayer is in breach of the agreement, he/she will be subject to a recoupment of the deductions previously allowed in the five years preceding the contravention.

**Income tax deductions: For Nature Reserve with a minimum contract of 99 years**

In addition to the deduction described above, the value of the land that is declared is deemed to be a Section 18A deductible donation. This means that the taxpayer may deduct the value of the land from their taxable income.

Taxpayers under this agreement are still entitled to deduct management expenses from their income. However, both these deductions, combined, must fit under the 10% cap prescribed for all 18A deductions.

The taxpayer may deduct the amount in the year of declaration, and again in each of the following nine years. This means that by the end of the ten year period, the full base value may have been deducted. There is no allowance for a roll-over of deductions into the following year, should there be no or insufficient income from which to make the deduction in any given year.

If the land owner retains some right of use over all or a portion of the land, this must be taken into account in determining amount that is deductible (outlined in *calculating the value* below).

Calculating the value of the land follows prescribed guidelines, outlined below.

***Calculating the value:***

**If the land owner does not retain any right of use of the property under declaration (such as residential or commercial use)**

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:

- the cost to purchase the land, or
  - the market value of the land
- In other words, each year, for ten years, the land owner may deduct:

10%	x	Lesser of cost or market value of land
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**If the land owner does retain some right of use over the property**

- The landowner may deduct 10% p.a. of the value of the land over ten years, starting on the year of declaration.
- The deductible amount is initially equal to 10% of the lesser of:
  - the cost to purchase the land, or
  - the market value of the land
- This 10% amount must then be multiplied by the ratio of the market value of the declared land reduced by the right of use as that amount bears to the value of the declared land as if that declared land had been donated full, as depicted in the formula below:

			Market value of land subject to the right of use
10%	x	Lesser of cost or market value of land	x
			Market value of land if there had been no right of use retained

#### 4.4 Protected Environments

Protected environment 30 year agreement

Income tax deduction: land management expenses

Protected environments are the only Protected Areas that are not provided property rates exclusions in the Municipal Property Rates Act.

##### Income tax deductions: for Protected Environment with a minimum contract of 30 years

In terms of the Income Tax Act, all conservation and maintenance expenses are deemed to be Section 18A deductible donations. This means that expenses related to the management of the land, as required by the Management Plan, can be deducted from the taxpayer's taxable income<sup>12</sup>. Activities undertaken that are not required in the management plan are not deductible.

This deduction is allowed for the duration of the declaration and contract (the contract may be renewed).

This deduction is subject to the 10% cap prescribed for all 18A deductions (see Section B Tax incentives).

If the taxpayer is in breach of the agreement, he/she will be subject to a recoupment of the deductions previously allowed in the five years preceding the contravention.

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<sup>12</sup>Gross income - exemptions = Income

Income - Deductions + Taxable Capital Gains = Taxable Income

#### 4.5 Biodiversity Management Agreements

**Biodiversity Management Agreement:  
contract 5 years**

**Income tax deduction:  
land management  
expenses**

##### **Income tax deductions for Biodiversity Management Agreement, with a minimum contract of 5 years**

In terms of the Income Tax Act, all conservation and maintenance expenses incurred in terms of a Biodiversity Management Agreement are to be treated as expenditure incurred in the production of income and for purposes of trade. Examples of these expenses could be rehabilitation expenses, alien clearing or burning fire breaks. However, expenses are only deductible if the activity is reflected in the management plan connected to the Biodiversity Management Agreement.

The taxpayer may only make these deductions from income generated from the land subject to the Biodiversity Management Agreement, or land in the immediate proximity. The Act does not define ‘immediate proximity’, but it is taken to mean neighbouring, or within a few kilometres of the land under the BMA.

The deduction may not exceed the income of the taxpayer derived in the year of assessment. However, the amount by which the deduction exceeds the income will be deemed to be expenditure incurred by the taxpayer in the following year of assessment. In other words, a roll-over of deductions into the next tax year is allowed.

**Farmers** entering into Biodiversity Management Agreements are subject to the same deductions, with the only difference being the deductions are allowed for under paragraph 12(1A) of the First Schedule. This portion of the Income Tax Act deals specifically with all allowable deductions made by farmers.

The deductions are limited to income derived by the taxpayer from farming activities on the land or within the immediate proximity of the land.

##### *Recoupment Clause*

If the taxpayer is in breach of the agreement, the amount of the deductions previously allowed in the five years preceding the contravention would be recouped<sup>13</sup>.

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<sup>13</sup> SARS would recover the money by including it in the amount owed to them in the tax year in which the breach arose



#### 4.6 *Informal Conservation Areas*

The national fiscal incentives (property rates exclusions and biodiversity income tax deductions) do not apply to informal conservation.

Other incentives may be designed to support this type of informal conservation. Local property rates based incentives are one such tool that could be used by a municipality to support conservancies or game farms.

## Appendix I: Biodiversity Fiscal Incentives Overview

Conservation Category	Fiscal Incentive	Suggested Biodiversity Geographic Focus	Landowner Beneficiary Type
	<b>Income Tax Based Incentives</b>		
Biodiversity Management Agreements in terms of the Biodiversity Act, minimum contract duration 5 years	Deductibility of management expenses for Biodiversity Management Agreements	Threatened Ecosystems	The tax mechanisms preferentially benefit individuals and other legal entities generating income
Protected Environment, minimum contract of 30 years	Deductibility of management expenses for Protected Environments	NPAES focus areas, biodiversity priority areas identified in a provincial or fine-scale systematic biodiversity plan, Threatened Ecosystems, important catchments	
Nature Reserve, minimum contract of 30 years National Park, minimum contract of 30 years	Deductibility of management expenses for Nature Reserves and National Parks	NPAES focus areas, biodiversity priority areas identified in a provincial or fine-scale systematic biodiversity plan, Threatened Ecosystems, important catchments, and other biodiversity priority areas	
Nature Reserve, minimum contract of 99 years National Park, minimum contract of 99 years	Deductibility of land value for Nature Reserves and National Parks	NPAES focus areas, biodiversity priority areas identified in a provincial or fine-scale systematic biodiversity plan, Threatened Ecosystems, important catchments	

	<b>Property Rates: National</b>		
<b>National parks and nature reserves in terms of the Protected Areas Act</b>  Aimed at portions of PA's not used for commercial, residential or industrial purposes.	<b>Municipal Property Rates Act: Rates exclusion for national parks and nature reserves</b>	NPAES focus areas, biodiversity priority areas identified in a provincial or fine-scale systematic biodiversity plan, Threatened Ecosystems, important catchments	Landowners paying property rates , including government agencies, private
<b>Informal conservation, e.g. non-contractual biodiversity stewardship arrangements and conservancies</b>	<b>National Property Rates Act: Removal of perverse incentives</b>	Corridors, important catchments, landscapes outside of Protected Areas.  The perverse incentives related to ecotourism and game farming, which provides an alternative land use to activities that would require land transformation	Land owners paying property rates  Predominantly aimed at removing perverse incentives on land used for ecotourism or game farming.
	<b>Local Property Rates Policies</b>		
<b>Statutory, and/or informal conservation</b>	<b>Local property rates policies and property valuations: conservation biodiversity and other ecosystem services</b>	Local biodiversity priority areas can be protected through agreements between land owner and municipalities  Could also apply to ecosystem services, such as water quality and quantity, fire	Land owners paying property rates

		mitigation, erosion, etc.	
<b>Statutory and/or informal conservation</b>	<b>Local property rates policies and valuations: Avoiding perverse incentives</b>	<p>Areas of local or national biodiversity significance with development restrictions placed upon them</p> <p>Land where specific threats to biodiversity have been addressed, e.g. invasive alien plant control</p> <p>Could also apply to ecosystem services, such as water quality and quantity, fire mitigation, erosion, etc.</p>	Land owners paying property rates
	<b>Payments for Ecosystem Services</b>		
<b>Statutory and/or informal conservation</b>	<b>PES</b>	Predominantly landscapes that offer carbon and/or water benefits combined with biodiversity benefits.	Any landowner, however, PES could significantly benefit impoverished communities and communities in communal areas, where other fiscal incentives would not be effective

