



NATIONAL ROUND TABLE ON THE ENVIRONMENT AND THE ECONOMY  
TABLE RONDE NATIONALE SUR L'ENVIRONNEMENT ET L'ÉCONOMIE

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# National Round Table on the Environment and the Economy

## Economic Instruments to Encourage Sustainability on Private Woodlots Workshop - Notes from Discussion

Ottawa, Wednesday, October 22, 1997

### Alternate Discussion Paper:

A request was made that an alternate paper be circulated. The group agreed to do so, provided that its content be blended into the proposed agenda.

Title of alternate paper: *Tax Incentives / Disincentives to Sustainable Forest Management: a Review of the Curtis Study Recommendations*. Author: Mr. Bruce Lunergan.

Some discussion between Mr. David Liston, co-author of the official NRTEE discussion paper, and Mr. Lunergan, developed at the beginning of the workshop. It centred, in part, on the relationship between the notions of woodlot management "business" and the tax criteria for "reasonable expectation of profit". Eventually, both the participants and the workshop agreed that this discussion should be left to Finance officials. Other aspects of the alternate paper were brought up as pertinent to the agenda during the balance of the day.

### Key Initiative

#### Create New Tax Class Based on Definitions of Woodlot Management and Woodlot Owner-Manager:

Participants had some difficulty focusing on this topic, as the proceedings were disrupted by the collapse of the simultaneous translators' box in the room and subsequent re-testing of the equipment. They did, however, unanimously agree with the need for a separate category or tax status for private woodlot owners and eventually agreed with the definitions contained in the May 1992 Curtis report (Incidentally, both Mr. deMarsh and Mr. Lunergan were members of the advisory committee for this report):

1. Curtis report's proposed definition of **woodlot management**, "*woodlot management*" includes the application of silvicultural techniques in accordance with a reasonable woodlot management plan on land owned or leased by a woodlot manager but does not include an office or employment under a person engaged in the business of woodlot management".

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2. Curtis report's proposed definition of **woodlot manager**, "*a person engaged in the business of woodlot management (excluding operators of timber limits as part of logging, lumbering or papermaking or other similar businesses and nurserymen)*".

A number of participants argued in favour of using 'woodlot owner-manager', rather than 'woodlot manager'; they also strongly supported, with regard to the Curtis definitions, the addition of references to relatively long timeframes and small size of private woodlot operations.

There was much discussion in reference to the woodlot management plan which would probably be required by tax officials to show woodlot owner-managers' seriousness in pursuing this kind of business. Some proposed that this plan involve forestry professionals in some direct or indirect capacity, while other participants argued for setting standards (to be met by such plans) in a manner that would allow owner-managers to prepare those plans without necessarily being forced to involve forestry professionals.

It was noted that failure to create a separate tax class would result in a negative impact on the economy, considering the relative importance of private woodlots in the industrial sector.

Overall, participants did not develop any further the concept of 'reasonable woodlot management plan' in terms of administration and qualifying criteria, other than mentioning that this kind of plan might include traditional business components such as marketing, implementation schedule, training.

Finally, some participants suggested that additional research be done on examining provincial definitions used in other tax contexts, including property taxes, as well as examining a broader definition of woodlots which would include easements and other forms of property interests.

## **Recommendations**

### **Recommendation 1**

#### **Deductibility of Expenses and Losses**

Participants suggested that identification of deductible items should be directly related to components of a reasonable management plan. They discussed how dollar amount limits on deductibility might be related to size of woodlot operations but shied away from venturing any specific numbers. The group concluded that simple mechanisms for relating deductible expenses to plan contents were preferable.

## **Recommendation 2**

### **Cash vs. Accrual Accounting Basis**

An example was offered to explain the difference between the two accounting methods: relating to shifting the timing of expenses on thinning operations, depending on which method is used.

Participants felt that the impact of this recommendation would be limited for woodlot owner-managers. They also unanimously agreed that silviculture costs were the most important aspect of this topic.

## **Recommendation 3**

### **Depletion Allowance for Timber**

Participants expressed mixed views as to whether this proposal was an incentive or a disincentive. They were also moderately perplexed about the relationship between this allowance and an associated proposal for a federally funded insurance program. Subsequently, it became clearer that an insurance program would make sense if this allowance was denied.

It was pointed out that such an insurance plan would reduce the business risks of owner-managers, induce more people into this line of business and eventually result in sustainability. The group saw a logical relationship amongst management plans, susceptibility to business risk and insurance plans.

At this point, participants were reminded that they should analyze each economic incentive in light of the industry's two biggest problems:

- overcutting and
- lack of proper silviculture methods.

One participant pointed out that this proposal dealt with the acquisition cost of standing timber and the timing of its harvesting. Others saw the proposal as an incentive to defer the early cutting of timber. although some scepticism was expressed about this position.

The group was warned against the potential for investors looking for a tax shelter, and concluded that the need for a balance between the interests of investors and woodlot owner-managers should be underlined.

#### **Recommendation 4**

##### **Income vs. Capital Treatment of Timber Sales**

Participants saw two aspects to this recommendation:

- inequity for owner-managers resulting from their inability to elect between either method; and
- inconsistencies in the application of rules in this tax domain, particularly with regard to infrequent harvesting of timber.

The discussion led to other areas (not discussed) such as income averaging, GST and use of woodlot for conservation easements.

#### **Recommendation 5**

##### **Old Age Supplement**

Up to 25% of woodlot owner-managers in New Brunswick were recipients of old age supplements.

Three participants suggested that this measure could be counterproductive, concerned many individual scenarios, and should be considered as a lower priority item.

#### **Recommendation 6**

##### **Capital Gains Treatment on Disposition**

It was agreed that two distinct aspects were contained in this recommendation:

- eligibility of woodlot owner-managers for the \$500,000 exemption (an incentive to build value in assets resulting in better sustainability, according to one participant); and
- the intergenerational transfer of assets — an item of particular interest due to the long timeframes associated with this kind of business.

It was strongly suggested that the discussion be broadened to include donation of woodlots to charities and conservation authorities; although it was acknowledged that changes were required to rules applying to a donor's control of the value of a donation.

Participants expressed strong consensus on the importance of this recommendation.

### **Recommendation 7**

#### **Investment Tax Credits**

Research in demographics would be useful in assessing the impact of this measure. An example was mentioned: the average age of woodlot owner-managers in P. E. I. was approximately 62 years.

The importance of woodlot management plans in identifying the range of tax items was pointed out. In this light, participants suggested the following items for consideration: plan preparation costs, plan implementation costs, education and training (broaden availability to operators), reforestation, pre-commercial thinning, certification fees, etc.

Participants were cautioned that investment tax credits were not necessarily the most tax effective instruments a careful analysis of impacts was suggested.

### **Recommendation 8**

#### **Registered Forest Management Fund**

This vehicle received wide support from the participants, especially in regards to the treatment of larger sums of money over longer timeframes.

### **Recommendation 9**

#### **Government Funding**

Participants supported these programs but did not offer specific suggestions as to what types of funding could be the most effective.

### **Summary**

- A. Participants produced strong consensus on creating a new tax class for woodlot owner-managers
- B. Participants agreed that the best move would be to combine recommendations 1, 4 and 6, while showing their direct impact on the business of managing private woodlots.

Participants also noted a need to receive better interpretation of income vs. capital treatment of timber sales from Revenue Canada.

- C. Participants agreed that strong and specific support should be offered for registered forest management funds, in a manner which already exists for environmental funds and provincial forest trust funds.