The natural capitalist

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How might drafting agreements for ecosystem services look? Asks Charles Cowap

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Clause one of the Agriculture Bill currently before Parliament sets out how the government will fund environmental work in the countryside in future. Financial assistance will be available for:

- managing land and water to protect or improve the environment;
- supporting public access to the countryside;
- managing land and water for improved cultural or natural heritage;
- climate change adaptation and mitigation;
- mitigation of environmental hazards; and
- activities for the health and welfare of livestock; and
- plant protection.

What might such measures look like? The box below shows 1 example of how this may work, although published details are still sketchy.

An environmental land management system

Hangery Farm covers 200ha crossed by two footpaths and a bridleway. The farm is predominantly arable, with some beef rearing and finishing to make use of the less accessible areas. There is a 10ha block of woodland, two public footpaths and one public bridleway. One of the footpaths skirts the farmyard.

Under the new vision for the countryside in the government's 25-year environment plan, the Department for Environment, Food & Rural Affairs? command paper*Health and Harmony*and the Agriculture Bill's new funding, we can expect rigorous but effective and efficient enforcement of minimum standards for public access; in other words, the footpaths and bridleway must be compliant with minimum legal requirements in all respects at all times. We can also anticipate funding to support access to the countryside, which will seek to add to the minimum amenities of the fully compliant access network. It will entail, for example:

- better surfacing standards;
- improved accessibility;
- other facilities including rest areas, observation points, interpretation material, parking areas, emergency contact information and medical assistance such as a defibrillator;
- added benefits including an environmental plan for the woodland, the treatment of watercourses and flows, and field boundaries? wider compliance issues, such as the management of farm waste and the attainment of minimum soil management standards; and
- payment based on simple formulae or menus for work that gives benefit over and above the attainment of minimum standards, for which the polluter ? who in this case would be the farmer ? pays.

But why rely on government funding when there are private commercial arrangements to be sought? Deals that, given the caprice of government funding, could be more sure-footed, secure and sustainable, as well as more private and confidential? What might these look like?

Utility companies might for instance pay for natural asset management to protect or enhance their operational assets. The most obvious examples of this would be water companies paying to secure decent supplies of good-quality water, by funding changes to farming practices or peatland restoration for instance. Stretches of railway line could also be made less vulnerable to weather and flooding by having developers contract with Network Rail to provide natural flood management and sustainable drainage systems. More broadly, the full adoption of the principle of environmental net gain in development planning could open a wide range of opportunities to work with developers. Carbon sequestration should also advance.

Proposals such as these will need careful appraisal, and will draw on all the traditional skills and knowledge that land agents and valuers have.

Appraisal and agreement

Financial appraisal will draw together the important elements. However, the final decision will depend on the answers to the following questions.

- What new revenue will be generated, over what period, and according to what cash flow pattern? How secure is this revenue?
- How will revenues be updated or reviewed?
- What extra costs will be incurred, both capital and operational? Again, how will these fluctuate in future?
- What existing revenue, if any, might be compromised or forgone?
- What existing costs, if any, might be saved?

If the total extra revenue plus costs saved exceeds extra costs plus revenue forgone, the deal might be worthwhile, but some more questions must be answered first.

- What will the tax consequences be?
- What will be the impact of the change on capital value?
- What other knock-on effects might arise in terms of future use and management, whether positive or negative?
- What happens if or when the agreement is terminated, and at what cost?

The exact form of legal agreement will then need to be settled. At one extreme this may be a lease or licence to enter or occupy land and carry out activities there, and in this case, the terms will have to be considered against the appropriate statutory background. Is this an agricultural lease for example, taking effect as a farm business tenancy? Or is it a commercial letting, falling under the scope of the Landlord and Tenant Act 1954 The answer will be crucial in determining many of the terms of the agreement ? for example, contracting out under the 1954 Act.

In many other cases, however, the contract will cover the provision of a service by the farmer or landowner and payment for this service by the beneficiary. The agreement may need to provide for the beneficiary to come on to the land to carry out certain works. Payment may need to be conditional on such works being carried out or outcomes achieved.

Questions will therefore arise over the duration of the agreement and the terms under which it can be reviewed or terminated. In the longer term, what will happen if the landowner dies or wishes to sell? Will the agreement be intended to bind future owners, and how will this be effected?

The inclusion of covenants to this effect may be another important consideration in negotiations. The government has accepted the Law Commission?s proposals for conservation covenants , but other parliamentary business has so far scuppered legislative progress on this. This legislation will allow for positive covenants for conservation purposes to be binding on future title-holders, and there will of course be subsequent registration requirements. Meanwhile, some purchasers may consider the use of estate contracts to protect their longer-term interests.

Existing land use

Some natural capital contracts may have few if any implications for the existing use and management of land. Others, however, could be significant. Stocking densities for example may need to be reduced, and machinery movement may become more difficult over ground that becomes waterlogged for longer periods. Other uses such as sporting activities may also need to be considered. The financial effects of these requirements will need to be reflected in the financial appraisal, but it will be equally important to look at the physical working implications.

This should also be broadened to consider the knock-on effects where the land is part of a larger working farm or estate. Some upland farmers in the North of England and Wales have for example reported problems with livestock arising from a greater prevalence of bog asphodel (*Narthecium ossifragum*). Veterinary research has suggested that an interaction between the plant and other microbes in the soil has, in some circumstances, led to the production of toxins that can be fatal to cattle and sheep, although the effect is by no means certain, universal or predictable.

Other interests in the same land will need to be identified and considered as well. Examples could include existing tenancies, joint owners, holders of sporting or mineral rights, beneficiaries of easements and restrictive covenants, mortgagees and other security-holders, and, where trust ownership is involved, the interests of beneficiaries. There may also be statutory agencies that have an interest; for example, where land is designated a Site of Special Scientific Interest, the appropriate authorities will need to be involved.

Risk assessments may need to be reviewed regarding new activities and the relationship with existing activities. Questions of occupier liability should also be considered, concerning both invited visitors under the Occupiers? Liability Act 1957 and others under the Occupiers Liability Act 1984 . Insurers should also be consulted to ensure that public liability and other cover is not compromised.

At the very least, most farmland is likely to be registered on the Rural Land Register and receiving funding under the Basic Payment Scheme . The same land may also be signed up to stewardship or other agreements. The rules will need to be reviewed to ensure continuing compliance, or reflect the cost of disengagement in the financial appraisal.

Many providers of the environmental services envisioned here will be farmers for tax purposes. Will their trading status be affected by the new arrangement? How will they stand for aspects of capital gains tax such as entrepreneurs?, holdover and rollover reliefs? Crucially, will the land continue to qualify as agricultural and business property for inheritance tax reliefs?

Compromise of these reliefs may be a reason not to proceed, but this question needs to be looked at fully in the round. For example, the loss of agricultural property relief may be less of an issue if business property relief takes its place; equally, the loss of both reliefs may be acceptable if expected revenue can more than make up the difference. Again, this will call for careful financial appraisal. A contractual arrangement that offers more than enough compensation for the loss of key reliefs may even be preferable to a reliance on the continuing availability of these reliefs.

The future

The interests and commitment of future generations will be an important issue for some. Contrast the farming family where at least 1 child is keen to carry on in agriculture with the situation where all the youngsters see their primary employment away from the farm. Might a scaling back of farming activities open other business opportunities, servicing the new contract itself or in other areas altogether? Might the release of capital from 1 part of the business ? by selling surplus stock for example ? allow for investment in other, potentially more profitable areas?

Finally, what impact will the new venture have on capital values? What are the key financial and other risks associated with the project? Careful evaluation of these will be crucial to determining the long-term security of the project. Potential changes in capital value may also be modelled through the financial appraisal, particularly where there is no certainty as to what these changes might be in future. In this situation the financial appraisal can be used to model different degrees of impact; in other words, how much change in value can be absorbed before the project falls over in financial terms?

There is plenty of work, then, that is an excellent fit with the traditional knowledge and skill set of land agents and valuers, especially those who can identify and develop new initiatives in this area: the land agent can become an eco-entrepreneur.

Charles Cowap , chartered surveyor, is the author of the RICS papers Challenges for international professional practice: From market value to natural value (2012) and Value of natural capital: The need for chartered surveyors (2017)

Further information

- Related competencies include: Agriculture , Landlord and tenant , Land use and diversification , Management of the natural environment and landscape
- This feature is taken from the RICS Land journal (March/April 2019)
- Related categories: Agricultural and rural property ; Ecological considerations ; Finance