

The future of forestry — A battle between economic theory and common sense

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Whether New Zealand foresters like it or not they are now forced to meet the challenge to their unquestioning faith in the concept that creating renewable assets is good business for investors, whether they are using their own money or the public purse. The Minister of Finance's Economic Statement of December 12, 1985 and the publication of the Consultative Document on Primary Sector Taxation of March 1986⁽¹⁾ were both clear indications of the present tax gatherer's appreciation of the business of forestry.

In simple terms, if an investor creates a capital asset which grows in value over a long period rather than depreciates, he can expect to pay full tax on most of the original investment plus the increase in value over the growing period, thereby effectively placing a tax on inflation and natural growth. That is, from a taxation point of view, plantation forestry is to be treated as a capital investment at the start and as full taxable income in the final year after 30 years' growth of value. The original intentions of the Treasury theorists were modified to a small extent by the Report of the Consultative Committee on Primary Sector Taxation, June 1986⁽²⁾. However, even this galaxy of four (including one woman) eminent neutral economists failed to bury the theoretical fallacies which gave rise to the original proposals. Given the proven ability of these people, one must question whether their hands were tied by the terms of reference under which they were forced to report. It surely must be a very simple exercise to conclude that investing capital in a crop (or trading stock) with a relatively short pay back period (e.g. kiwifruit growing) is a much more viable option than tying up the same capital for 25-30 years and therefore different tax regimes should apply?

It is however fruitless to merely criticise either the Treasury theorists or the Committee, which appears to have done an otherwise sterling job in sweetening the pill which the primary sector is being forced to swallow. The problem lies in the complexity of economic theory when applied to long-term investment, the evaluation of risk and returns by those who spend the money and those who collect the tax and, put bluntly, the blind faith of most foresters in the infallibility of their financial decisions. A harsh judgement of the latter could be that most of us won't be

around to face up to the consequences of the burden of accumulated expenditure, excessive extraction and transport costs or market supply and demand variations. This perhaps explains a predilection for using carefully calculated Internal Rates of Return when we are measuring the expected financial consequences of our actions rather than facing up to the more stringent discipline of Net Present Value calculations based on Discounted Cash Flow including the burden of taxation.

It has fallen to another economist, rather than a forester, to point out the errors in Treasury's original thinking. A paper published by Ed Vos of Waikato University entitled Net Present Value vs Internal Rates of Return — Another Misunderstanding, The Accountants' Journal, June 1986⁽³⁾ uses detailed theoretical arguments to effectively demolish the equally theoretical Treasury case published in the March White Paper. It behoves all foresters to read both if they wish to be responsible for investment decisions in the future or indeed if they expect to have any budgets with which to carry out such decisions! You may not follow completely the mathematics and theory but in both cases the messages are clear. It is important however that the conclusions are at such variance and that the tax gatherer's spokesmen have more power in the land than the academic defender of long-term investment. Vos's conclusions are important to the future of NZ forestry and should be studied and understood by anybody who plans to invest in forestry — with either his own or others' money. There are many passages in the paper which it would be useful to reproduce here but

one will suffice as a warning to both the Government and investors: —

"What motivation is required on the part of an investor to invest in a long-term project so that the tax collector gets a present value income and cannot sustain a loss, and the investor *may* get a present value income and must sustain all the risks and uncertainty over long-term investment?"

What motivation indeed? One can but conclude that the only people who will now invest in creating further forest assets in New Zealand are those who have a blind faith in the hope that common sense will at some time return to the Treasury benches.

It will be a tragedy if this only happens after serious disruption of the sustained build-up of a most valuable national asset and the diversion of hours of executive time to preparing and presenting submissions. An even greater loss will be the probable dispersal of both a professional corps of foresters to overseas positions and a skilled rural workforce to the stultifying dependence on social welfare in an alien urban environment.

References

- (1) Consultative Document on Primary Sector Taxation. Minister of Finance. March 1986.
- (2) Report of the Consultative Committee on Primary Sector Taxation. June 1986.
- (3) Vos, E. "Net Present Value vs Internal Rates of Return — Another misunderstanding" The Accountants' Journal. June 1986.

Whose forest when?

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"Property," wrote the 19th century anarchist Pierre-Joseph Proudhon, "is theft." Fifty years later, G. B. Shaw was to commend this as "the only perfect truism that has been uttered on the subject". Surprisingly, there is some recognition of this principle from an unexpected quarter — statute law; the concept of absolute ownership clarifies the Crown's ultimate power whilst the ownership in

"fee simple" (freehold) by which we "possess" our greater or lesser sections is legally a lower authority delegated from the Crown. This status is not only bluntly revealed by the non-ownership of water, minerals and oil on our land, the easements of public utilities, or the planning controls of district schemes, but even by the justification of estate duty in terms of a levy for the privilege of