

[Interpretation statement IS3970 issued by Adjudication & Rulings in April 1998]

## **“FORESTRY”: WHETHER OR NOT IT IS INCLUDED IN THE SECTION CD 1(7) DEFINITION OF “FARMING OR AGRICULTURAL BUSINESS”**

### **Summary**

This item states the Commissioner’s view on whether “forestry” falls within the definition of “farming or agricultural business” in section CD 1(7) of the Income Tax Act 1994. Under this interpretation, the Commissioner accepts that “forestry” falls within the definition of “farming or agricultural business” in section CD 1(7).

All legislative references are to the Income Tax Act 1994 unless otherwise stated.

### **Background**

The Commissioner’s previous policy, dated January 1993, sets out the activities Inland Revenue considers are carried on for agricultural or farming purposes. It specifically does not include the growing of trees for the production of timber in the definition of agriculture and farming. The following specified activities were considered to be carried on for farming and agricultural purposes: beekeeping, animal husbandry, dairy farming, grain and seed growing, market gardening, fruit growing, poultry farming, sharemilking, tobacco growing, and vegetable growing. The following activities specifically did not qualify: dealing in livestock, leasing or bailing livestock by the bailor, aerial topdressing, growing trees for the production of timber, and providing services to persons carrying on a farming or agricultural business, e.g. services provided by agricultural contractors and seed cleaners.

### **Legislation**

Section CD 1(2) includes in a taxpayer’s gross income, any amounts derived from the sale or other disposition of any land in some seven categorised circumstances. Section CD 1(7) excludes from the gross income of a taxpayer any amount derived from the sale or disposition of land resulting from the division into two or more lots of a larger area of land occupied or used by the taxpayer, or spouse, “or by both of them, primarily and principally for the purposes of a farming or agricultural business”.

The following requirements must **all** be satisfied before the exemption applies:

- The land sold must have resulted from the division into two or more lots of a larger area of land which, immediately before the division was occupied or used by the taxpayer, or spouse, or both, primarily or principally for the purpose of a farming or agricultural business that the relevant persons carried on.
- The Commissioner must be satisfied that the land sold is of such an area and nature that it is presently capable of being worked as an economic unit in a farming or agricultural business.

- The Commissioner must be satisfied, having regard to the circumstances in which the land was disposed of, that the land was disposed of primarily and principally for the purpose of it being utilised in a farming or agricultural business.

## **Application**

The question of whether forestry is included in the expression “farming or agricultural business” has been considered by the courts in relation to other sections of the Act that use similar wording, but not directly in relation to section CD 1(7).

Earlier cases tended towards the view that forestry was not included in the definition of “farming and agriculture”. In *Gilchrist v Lanarkshire Assessors* (1895) 35 Sc LR 663, the Court had to consider whether a greenhouse used for growing tomatoes was an erection or a structural improvement made or required for agricultural purposes. Lord Stormouth Darling said at page 665:

Now that question must be solved by considering the meaning of the phrase in its ordinary acceptation. The appellant considers that a market garden is an agricultural subject because it effects the culture of the ground. No doubt it does but there are three main methods of utilising the soil, which are expressed by the terms agriculture, horticulture and forestry. These three things are distinguishable, and any one of them is not to be held as including any other without special provision to that effect.

In *Horniblow v Napier* [1985] NZLR 105, the question was whether an orchardist was a farmer for the purposes of the Transport Act 1949. Barrowclough CJ referred to the *Gilchrist* case and said at page 105:

It might be very unsafe to accept as applicable to this country’s special type of husbandry (I deliberately use a new and comprehensive word), a classification that was applicable in Scotland over fifty years ago. But it appears to me that that classification is adaptable to New Zealand conditions, and is a classification which is commonly accepted here. Agriculture is essentially the business of the farmer. That is recognised in the interpretation clause of the Transport Act 1949, where the phrase ‘agriculture purpose’ is defined ‘as a purpose concerned directly with the management of a farm’. I would conclude that a farmer is one engaged in the first of the three methods of utilizing the soil referred to by Lord Stormouth Darling, and consequently that a person engaged in either of the two other methods is not a farmer. The viticulturist is in the second group comprising those who utilize the soil of a garden; and so also, is the fruitgrower or an orchardist. They are not properly referred to as farmers. The silviculturist is in the third group; and he too, is not properly referred to as a farmer.

In 1994, in the Court of Appeal decision of *Hill v CIR* (1994) 16 NZTC 11,037, Richardson J concluded that agriculture and farming might include forestry. The Court of Appeal considered whether forestry was included within the expression “farming or agricultural business” in terms of section 126 and 127 of the Income Tax Act 1976. In this case, Richardson J who delivered the judgment of the Court stated at page 11,046:

“Farming” and “agricultural” are broad flexible words and the use of both expressions in the phrase on its face suggests that a broad approach casting a wide net was intended. But the particular meaning to be accorded to the words depends on the context in which they are used. In order to determine the intended application of the phrase in ss 126 and 127 it is also necessary to set the sections in context in the Income Tax Act as a whole.

After briefly considering the earlier cases, Richardson J stated at page 11,047:

*Horniblow v Napier* and *Hill v Rothwell* were decided 40 years ago and *Gilchrist* is even more remote in time. But the classification in *Gilchrist* and the approach in *Re Walker and Township of Uxbridge* perhaps indicate that variable meanings and shades of meaning may attach to such expressions. At the same time it is apparent from any reference to standard dictionaries that in their ordinary sense the words have wide meanings. Thus the *Shorter Oxford English Dictionary* definitions are indicative of the potential breadth of the expression. Agriculture is defined as “the science and art of cultivating the soil; including the gathering in of the crops and the rearing of livestock; farming (in the widest sense)”. Farming is “the business of cultivating land, raising stock etc” and a farm is “a tract of land held...for the purpose of cultivation; sometimes specialised as dairy-, grass-, poultry-farm. Also a tract of water used as a preserve, eg fish, oyster, etc.” Interestingly forestry is defined as “the science and art of forming and cultivating forests, management of growing timber”. Closer to home the two Australian dictionaries, *The Macquarie Dictionary* and *Tasman Dictionary*, both define agriculture as “the cultivation of land, including crop-raising, forestry, stock raising, etc; farming.

Richardson J concluded that:

Sufficient has been said to show that in New Zealand usage agricultural and farming may include forestry. But in determining the intended scope of the expression “farming or agricultural business on land in New Zealand” and so in deciding the intended reach of ss 126 and 127 it is necessary to consider the context...In our view it is a necessary implication from ss 126 and 127 considered in their statutory setting that they did not apply to taxpayers engaged in the business of forestry.

Richardson J considered by way of necessary implication that sections 126 and 127 when they were considered in their statutory setting did not apply to taxpayers engaged in the business of forestry, because Parliament subsequently legislated specifically (in section 127A) to provide a similar deductibility regime for any taxpayer who carried on any forestry business. In doing so it allowed for the same range of expenses and followed the model of sections 126 and 127, which would, of course, have been unnecessary had those two provisions already applied to forestry. This did not, however, detract from his initial conclusion that the phrase “farming or agriculture” might include forestry on an ordinary meaning of the words.

Whilst not all dictionaries give a consistent indication, several other dictionary meanings also indicate that farming and agriculture include forestry: *Webster’s International Dictionary*, Second Edition, gives a wide meaning to the word “agriculture”:

The art or science of cultivating the ground, and raising and harvesting crops, often including also feeding, breeding, and management of livestock; tillage, husbandry; farming; in a broader sense, the science and art of the production of plants and animals useful to man, including to a variable extent the preparation of these products for man’s use and their disposal by marketing or otherwise. In this broad use it includes farming, horticulture, forestry, dairying, sugar making, etc.

Funk and Wagnall’s *New Standard Dictionary* gives this definition of “agriculture”:

1. The cultivation of the soil for food-products or any other useful or valuable growths of the field or garden; tillage; husbandry; also by extension, farming, including any industry practised by a cultivator of the soil in connection with such cultivation, as forestry, fruit-raising, breeding and rearing of stock, dairying, market-gardening, etc.

There is also overseas authority to support the approach that the phrase “farming or agriculture” includes forestry.

In Canada, forestry is considered to be a farming activity. “Farming” is defined in section 248 of the Canadian Income Tax Act 1994 to include the various activities of

a person who is engaged in the business of earning income from the tillage of soil, the raising or exhibiting of livestock, the maintenance of horses for racing or exhibiting, the raising of poultry, the keeping of bees, fur farming, dairy farming, and fruit growing.

The definition is not exhaustive and it has been decided by the courts that farming also includes tree farming: *Her Majesty the Queen v Douglas C Matthews* 74 DTC 6193, [1974] CTC 230(FCTD).

Revenue Canada's *Interpretation Bulletin IT—373R March 14 1985* relating to farm woodlots and tree farms states that proceeds from the sale of logs, lumber, poles or Christmas trees are income from farming.

It also states that a taxpayer who is not otherwise engaged in a lumbering or logging business and who undertakes the reforestation of an area of land with the objective of producing mature trees at a date that may be 40 or 50 years in the future, or even longer, is considered to be farming.

### **Possible alternative interpretations**

Certain provisions in the Income Tax Act indicate that (for those provisions at least) Parliament had clearly intended "farming and agriculture" to not include forestry by having explicit separate treatments. The decision in *Hill* illustrates one such example, and others include the Income Equalisation provisions in sub-part EI of the Act, and sections DZ 2 and DZ 3. It could certainly be argued that this indicates it was Parliament's intention or understanding that forestry was not included in the phrase "farming and agriculture".

Whilst such an argument does have some merit, it is considered that the better approach is that expressed by Richardson J in *Hill*, that forestry does generally come within the phrase, unless the context of a particular provision indicates otherwise.

Accordingly, each provision needs to be examined separately, and whilst some (such as those discussed above) will result in a conclusion that forestry is not included, section CD 1 has no such contextual reasons to overturn the general proposition that forestry is included.

It might also be suggested that the use of the word "worked" in section CD 1(7) can be seen as suggesting a greater level of day to day activity than might be involved in small to medium scale forestry operations. However, the word "worked" is capable of a wide meaning ranging from the application of mental or physical effort for a purpose to cultivating land. The ordinary meaning of the word "worked" tends to suggest that there must be some form of physical activity, but does not necessarily require any particular activity level. Many activities that are clearly regarded as a "farming or agricultural business" do not demand day to day physical work on the part of the proprietor. The existing case law in New Zealand simply analyses as a whole the meaning of the phrase "worked as an economic unit as a farming or agricultural business" in section CD 1(7). It does not look at the meaning of each word in the phrase in isolation.

## **Conclusion**

The words “farming or agriculture” in their ordinary usage may include forestry. The wording and context of section CD 1(7) do not prevent this interpretation. The New Zealand Court of Appeal case of *Hill* supports the interpretation that agriculture and farming may include forestry.

Several dictionary meanings of these words indicate that farming and agriculture can include forestry. Case law and a revenue interpretation bulletin in Canada also indicate that farming and agriculture can include forestry

The phrase “farming and agriculture” has a wider meaning now than it did many years ago as technology has advanced, and agricultural practices have changed over time. In New Zealand and in the previously mentioned overseas jurisdictions, the ordinary meaning of “farming and agriculture” may include forestry. In determining whether forestry is included in any phrase of the Income Tax Act, the context of the section must be examined. For the purposes of section CD 1(7), forestry is included in the phrase “agriculture and farming”. There is nothing in the context of section CD 1(7) to indicate that forestry is not included.

It should also be noted that any claim for exemption under section CD 1(7) in respect of a forestry activity must not only satisfy paragraphs (a) and (c) (“farming or agricultural business”), but the land under consideration must also be “capable of being worked as an economic unit” as required by paragraph (b) of section CD 1(7).