

Taxation of woodlands and forestry

by Julie Butler

It has generally been considered that the tax regime for woodlands has been traditionally benevolent. This kindness dates back over 40 years to 1963. This changed in part in 1988 when it was considered that woodlands had become a tax shelter. The aim at that time was to try to take woodlands out of the tax system altogether.

The impact of this tax regime really began to have an impact in 1992–93 when the cost of managing woodlands was no longer allowed as an offset against the woodland owner's total income. This exemption from tax only applies to long-term woodland projects. Short rotation coppices, i.e. timber used in cycles of under ten years, are not 'exempt'. Now that Margaret Beckett has made her 12 February 2004 speech (to heated response) and it is confirmed that subsidies (direct farm payments) will be moved away from farm production and towards agri-environmental schemes and the development of rural initiatives, woodlands could be in the forefront of landowners' and farmers' minds as farming changes under the mid-term review of the common agricultural policy (CAP) reform. This direction could so easily interact with tourism and countryside access which should be favoured under the diversification initiatives.

As mentioned above, under the current tax regime it is considered that the Inland Revenue tries to extract from 'woodlands' the short term profitable activities and bring them into *Income and Corporation Taxes Act 1988*, Sch. D, Case I, e.g. Christmas trees,

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the production of planks and 'short rotation coppices' (the quick production of timber). The Revenue fought quite hard to have Christmas trees assessed as a timber trade – see *Jaggers (t/a Shide Trees) v Ellis*¹. In this case, there were claims by the taxpayer that they were carrying out a trade that constituted 'the occupation of land which comprised woodlands or is being prepared for use for forestry purposes'. The taxpayer's trade was the sale of

four-year-old coniferous trees to the public as Christmas trees. The commissioner's decision held that 'woodland' connoted a wood, a sizeable area of land to a significant extent covered by growing trees of some maturity, size and height. The special commissioner found that Christmas trees are not prepared for forestry – there was no evidence of past production, or future intention of timber production. In this case, there was Christmas tree production, not timber production. There has been a clear move by the Revenue to divide the long-term projects (woodland and forestry) and the short-term projects (Christmas trees, short rotation, planking etc.). So how far does the woodland discrimination by the Revenue go?

The commissioner's decision in *Jaggers* was upheld in the High Court². It was decided that the taxpayer's site had had the appearance of a nursery rather than a wood. This was followed up by the Inspector's Manual at IM2270C.

Inheritance tax

Woodlands are exempt for deferral relief under the *Inheritance Tax Act 1984*, s. 125, 127 and 128, but with the introduction of the business property relief (BPR) at 100% does this really present the most tax efficient alternative? Are planners thinking of the bigger (and possibly more valuable) 100% potential relief of the value of the land and the woodland (trading asset) of BPR? The tax planning question is: would the woodlands/forestry qualify for BPR?

Capital gains tax

The gain on the disposal of the asset of 'woodlands' is eligible for rollover relief if run on a commercial basis with a view to realising a profit, but this is where the largest potential area of discrimination occurs – business asset taper relief (BATR). From 6 April 2004, nearly all tenanted land and building used in a trade, profession or vocation are business assets. Land used for commercial forestry is not a 'business' asset, although this can qualify for rollover relief. During the standing committee debates on the *Finance Act 2003* (FA 2003) taper relief changes, the paymaster-general said that the lack of BATR for woodlands would: 'receive serious consideration from the Government in due course'.

Income tax position of short-term rotation coppice

As mentioned above, short-rotation coppices (harvested within ten years) are taxable as a trade. The farm building and short-rotation coppice land becomes land for agricultural property relief (APR) (FA 1995, s. 154) with obvious benefits for the farmhouse. Tax losses can be offset against income under ICTA 1988, s. 380 which can be preferable to exemption.

Forestry grants – farm woodland premium scheme

Grants receivable under the farm woodland premium scheme (FWPS) are taxable.

This form of 'income' is taxable whether or not the woodland is commercial or non-commercial, i.e. it is taxable whatever. Where there is an 'exempt' woodland, that qualifies for the deferral provisions of IHT it is taxable as income.

It could be argued that the above creates a contradiction in tax terms. The FWPS is a grant for plantings on agricultural land. The land must have been in agricultural use for the last three years. Where does that place the tax status of land for IHT? There is the beneficial 100% APR or inclusion into the 1988 woodland exemption from income and the deferral scheme.

So where is the benevolence towards the long-term woodlands?

As mentioned, short-term woodlands have been caught as taxable under Sch. DI and this could be most beneficial overall. Christmas trees, the trade of 'nursery' is also a trade for Sch. DI and qualifies for BPR for IHT. However, short-term rotation coppice is agriculture for tax purposes and therefore qualifies for APR for IHT. So what of long-term woodlands? What is the economic benefit of deferral tax relief? It is not taxable and does not enjoy BPR for IHT. There is no income tax loss relief under the woodland exemption. While we await the decision on BATR, what action should the tax planner take?

Land Registration Act – effective 13 October 2003

The above act has resulted in land registry title certificates being replaced by electronic titles which are live and viewed on screen with open access to the public including leases and charges. The advantage is that landowners can verify their title to all their landownership including woodlands.

Action plan for tax advisers regarding woodland

Review all woodlands owned with details:

- history of ownership and tax treatment;
- cost;
- value – current;
- potential;
- plans for the future;
- current tax treatment – income tax, capital gains tax and IHT; and
- diversification and grant potential.

Tax planners need to advise clients on the serious decisions that should be made as to the future tax treatment of woodlands and it is hoped that the above review is a starting point.

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¹ *Jaggers (t/a Shide Trees) v Ellis* [1996] STC (SCD) 440.

² *Jaggers (ta Shide Trees) v Ellis* [1997] STC 1417.



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