

The Joy of Woodland

It might be a sensible argument to ask why would anyone buy a wood or a forest?

They can be expensive to maintain, harvesting the timber can cost more than the sale proceeds and the public liability insurance is high. But what about the beauty?

There are obvious advantages of woodland such as game covert, wildlife habitat preservation, belts of amenity trees for farms providing firewood, fencing and timber. There is also a shelter from suburban and urban pressures and somewhere to observe wildlife – the list is endless and appreciating the beauty of woodlands can be at the top of the list.

But what of commerciality and investment? Many consider that with current world food and fuel shortages any wood or forest must have long term commercial advantages.

Into the melting pot of woodland advantages perhaps should be placed tax relief. However, is this fully understood by the current and potential owner of the woodlands and also those proposing new planting programmes? Some investors in woodlands consider that there is a tax shelter from Inheritance Tax and income tax exemption advantages, but these potential advantages should be handled with professional care.

Income from woodland held as an investment can be exempt from income tax. This may seem very attractive, but the exemption means that expenses cannot be claimed, and so the tax exemption 'flagship' for woodland might not be as beneficial or attractive as it first seems. But there are still various Inheritance Tax advantages that may be more beneficial.

Inheritance Tax Relief

So can an investment in woodland escape death duties?

There are essentially three types of

Inheritance Tax (death duty) relief available for holdings in woodland/forestry, as follows:

- Deferral Relief.
- Agricultural Property Relief (APR).
- Business Property Relief (BPR).

The deferral relief should be the last resort, as it is what it 'says on the tin', a deferral of Inheritance tax. In other words it does not remove the tax, and it does not leave the beneficiary free to start again. In contrast APR or BPR can remove the Inheritance Tax on the asset entirely through 100% relief.

In order to qualify for Business Property Relief (BPR) the wood has to be managed as a business, or be part of a business unit. To qualify as part of a business unit there should be a mixed Estate with the woodland or forestry properly integrated with the main business activity and agricultural activity. The integration should show real evidence of the woodland being part of the main business.

For the woodland to qualify for Agricultural Property Relief (APR) the wood must either qualify as agricultural property or it must be ancillary to agricultural property, e.g. ancillary to the main farming activity.

Let us look at the three reliefs in more detail.

Deferral relief for long term forestry

Many forests are purchased with the specific aim of shelter from Inheritance Tax. Instead of investing in say stocks and shares or bricks and mortar, the investor chooses woodland purely for the Inheritance Tax advantages, in the full understanding that the income is either low or negative. This can be done without any practical involvement in the woodland operation, since there are many woodland management companies throughout the UK who will take care of

every worry.

The deferral relief does provide, guess what, a deferment of Inheritance Tax, i.e. the Inheritance Tax is deferred until the timber is felled or otherwise sold. At this point, a 'tax penalty' is exacted as the proceeds from the felled timber are taxed as if they formed part of the deceased estate in respect of which the deferral relief is claimed, and taxed at 40%. The irony, it is argued, is that the relief was claimed on the woods and therefore what is taxed is the growth which has taken place after the death – which was not even part of the estate at death.

Obviously, it is far better for the owner of the wood to try and achieve a full 100% relief of APR or BPR. In addition, there are other advantages of BPR which will be shown below.

Agricultural Property Relief (APR) for woodlands

For the woodlands to qualify for APR, it must either qualify as agricultural property in accordance with the Taxes Act, or be occupied with agricultural land and be ancillary to that farmland.

Woodland used for the production of commercial timber is not agricultural property. The type of woodlands that qualifies as farming/agriculture in its own right are short rotation coppices, i.e. timber harvested every 10 years and woodlands grown as an energy crop.

By definition, new planting that was the subject of a grant to take land out of agricultural use and must not return to agricultural use within 20 to 30 years cannot qualify as agricultural property as it is not agriculture.

Alternatively woodland can qualify as agricultural property because it is ancillary to farmland, e.g. game coverts and coppices grown or used for farm timber.

It is considered by many that guidance is given by the recent Earl of Balfour case

(see the August and September issues) – before the Special Commissioners – concerning a mixed Estate in Scotland. In the statement of facts the forestry was deemed to be agriculture, therefore ancillary to a very substantial farming operation. Help is also found in the Tax Office Inheritance Tax Manual (Chapter 24) on the HMRC website as to the definition of agriculture.

Business Property Relief (BPR)

In order for woodland and forestry to qualify as business property and therefore BPR, the woods must be either commercial woodland or they must qualify as part of the farming business as a whole.

There are further tax advantages of BPR for the hidden value of the woodland. If the woodland is to be developed, any 'hope value' will qualify for Inheritance Tax relief under BPR through the fact that it is part of the business. APR

is restricted to the "agricultural value" (the value as if there was a perpetual covenant for the property to be used only for agricultural purposes; see the September issue for more detail on this), but in contrast BPR is available for the full market value, including any "hope" of development value. This is because the woods are part of the business.

If, for example, the woodlands contained wind turbines these would also qualify for BPR as part of the business. What about the shooting rights? If, for example, in the case of probate the District Valuer wants to inflate/increase the value of the woods for a well-run shoot, business property relief (BPR) can be claimed against the shooting rights.

Conclusion

The reality is that investment in woodland or forestry, whether a large forest for

investment and enjoyment or a small shooting covert to be added to a farm, does have the potential for superb tax reliefs. However these reliefs are not straightforward and a full professional review of the tax reliefs should be undertaken prior to purchase. □

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