

The joy of woodlands – but are they a tax-efficient investment?

Buying a wood or a forest may not be an obvious choice – they can be expensive to maintain; harvesting the timber can cost more than the sale proceeds; and the public liability insurance is high. Julie Butler examines the overall tax relief of woodlands; their commerciality and investment, and the interacted tax efficiency.

At the time of writing, timber prices are on the increase. Forestry is a long-term investment where the crop often takes 35 years to mature, which can reflect interesting accounting and tax disclosures.

With current world food and fuel shortages, it might seem that any wood or forest must have long-term commercial advantages. But are the full tax reliefs being considered? Is the tax obligation fully understood by the current and potential owner of the woodlands, as well as by those proposing new planting programmes? Let us look at the various tax scenarios.

Inheritance tax (IHT) relief

There are three types of IHT relief available for holdings in woodland/forestry. These are:

- deferral relief for the standard investment holding;
- agricultural property relief (APR); and
- business property relief (BPR).

Woodlands are exempt for deferral relief under s125, 127 and 128 Inheritance Tax Act 1984 (IHTA 1984), but with the alternatives of APR or BPR at 100%, is deferral really the most tax-efficient alternative? Deferral relief should really be the last choice of IHT relief. It is merely a deferral of IHT – it does not remove the tax, whereas APR or BPR can provide 100% IHT relief on the asset.

In order to qualify for BPR, the wood has to be managed as a business or be part of a business unit – ie, a mixed estate with the woodland or forestry integrated with the main business activity and agricultural activity. The following activities can be incorporated:

- shooting and stalking rights;
- ponds for fishing;
- coppicing;
- on-site sale of firewood and woodchips;
- interaction of ponds for fishing;
- timber holiday cabins with visits;
- equestrian with nature trails; and
- games such as paintballing.

For the woodland to qualify for APR, the wood must either qualify as agricultural property or it must be ancillary to agricultural property.

IHT deferral relief for long-term forestry

Forests are often purchased as an investment with the specific aim of shelter from IHT. An investor will choose woodland for its IHT advantages in the understanding that the income will be either low or negative (the expenses exceed the income).

However, the deferral relief does provide a deferment of IHT until the timber is felled or sold. At this point, a 'tax penalty' is exacted. 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%.

Income tax

Income from woodland held as an investment can be exempt from income tax, which seems very attractive. However, this exemption does mean that expenses cannot be claimed and the tax exemption 'flagship' for woodland might not be as attractive as it first seems.

If the land is predominantly occupied for farming and is not commercial woodland, the receipts from felled timber may fall outside the exemption and be taxed as farm income. Receipts from the sale of trees planted on farms should be included as part of farming profits.

Agricultural Property Relief (APR)

For the woodland to qualify for APR, it must qualify as agricultural property in accordance with IHTA 1984 or be occupied with agricultural land and be ancillary to that farmland.

Where new planting has been the subject of a grant to take land out of agricultural use for 20 to 30 years, it cannot qualify as agricultural property as it is not agriculture. Woodland such as game coverts and coppices grown or used for farm timber can qualify as agricultural property because it is ancillary to farmland. Woodland that is used for the production of commercial timber is not agricultural property.

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. If part of the

woodland is to be developed at a future time, any 'hope value' will qualify for IHT relief since it is part of the business.

Tax protection action plan

Investment in woodland or forestry therefore does have tax relief potential, but the relief is not straightforward and a full professional review of the tax reliefs should be undertaken prior to purchase.

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