



UK Forestry Taxation Summary August 2010

An investment in commercial growing timber in the UK is highly tax efficient. The return from the trade of commercial woodlands is free of both income tax and CGT. There are also considerable inheritance tax advantages.

The main provisions of relevance to Investors are summarised below. Prospective Investors are advised to consult their own professional advisers on the impact of these provisions in relation to their own particular circumstances.

Inheritance Tax

On Death

Timberland exploited commercially qualifies for 100% business property relief (BPR) once held for two years, (Inheritance Tax Act (IHTA) 1984, s105 and s106 as amended by Sch 14 Finance (No.2) Act 1992). If held at death, there is no inheritance tax payable on the total value of the land and trees. Any CGT liability on the asset which has been held over or rolled-over will be extinguished.

The ability to leave the value of growing timber out of the account when establishing the value of an estate at the date of death (under s125-130 and s208 IHTA 1984) is now usually irrelevant, due to these provisions.

In the event of death before the owner has completed the two year qualifying period for 100% BPR, the IHT due may be paid in ten annual instalments, interest free, (S227 IHTA 1984).

On Lifetime Transfers

There is now no particular benefit in making a lifetime transfer of assets which will qualify for 100% BPR, apart from safeguarding against a change of legislation in the future.

However, for the estate to benefit from 100% BPR in the event of a lifetime transfer becoming liable to tax due to the death of the donor within seven years of making the gift, the donee must still own the asset and it must still qualify for relief at the date of death; or, if the donee has sold the asset, he must have reinvested all the proceeds of sale in another qualifying business asset within 36 months of the sale (s113A and s113B IHTA 1984).

If this condition is not fulfilled, the donee and/or the donor's estate will be assessed for inheritance tax. However, provided the donee is due to pay the tax, this may be paid in instalments as above.

Investment Potential

Investors have considerable flexibility on the optimum investment to benefit from 100% business property relief.

Plantations

Investment in forest plantations fulfils the primary objective of mitigating inheritance tax within a tax-free environment.

Where maturity may be required in the shorter term, semi-mature plantations may be appropriate. For longer term investments, young plantations would be relevant if no income is required, or a development under the Farm Woodland Premium Scheme (FWPS) where income is important.



Capital Gains Tax

Tax Free Growth

The increase in the value of timber and plantations is exempt from Capital Gains Tax (CGT) (s250, Taxation of Capital Gains Act (TCGA) 1992).

Any increase in the value of the land from the date of acquisition will be taxed without indexation at the CGT rate, currently 28%. It should be noted that the land value currently only accounts for 10 to 15% of the overall value of a mature forest.

Entrepreneurs' Relief may be available on a chargeable gain on a disposal.

Roll-Over Relief

There is a clear opportunity for those who have a CGT liability arising from the sale of a business asset.

By rolling over into another qualifying asset - timberland, (under s158(1)(b) TCGA 1992) the CGT liability can be deferred. By holding the forest until death, the estate is assessed for inheritance tax (but see immediately below) and the CGT liability is extinguished.

Forestry provides 100% relief from inheritance tax if held for two years prior to a gift or death, hence the tax liability on this portion of the estate is generally nil.

Alternatively, the new forestry asset could at some stage be gifted. If held for two years prior to a gift and the donor survives for seven years there would be no liability to inheritance tax and any CGT liability could be held over by the donor and donee (subject to certain conditions, under s165(9) TCGA 1992). The CGT liability could then be further deferred long into the future. As the value of the growing timber is exempt from CGT, (s250 TCGA 1992), it is only the land element of the investment which can qualify for roll-over or hold-over relief.

Investment Potential

The optimum route to benefit from roll-over relief is to acquire a farm for development under the Farm Woodland Premium Scheme (FWPS). The total investment will qualify for roll-over relief. Indeed, with the surplus generated by the receipt of planting grants over development costs in the first two years, roll-over relief could in effect be obtained on 130% or more of the net capital actually employed in the project.

A development under the FWPS can provide:-

- 100% roll-over relief.
- Annual income.
- High compound return after CGT relief.
- 100% relief from inheritance tax.



Income Tax

Tax-Free Income

Income generated from the ownership of commercial woodlands is exempt from both income tax and corporation tax.

No tax relief is therefore available on development costs or interest payments, and no income tax is payable on income generated from a timber crop or on the sale of an entire plantation (Income Tax (Trading and Other Income) Act 2005, ss11, 768; Corporation Tax Act 2009, s37).

Investment Potential

Timberland offers investors seeking to build up a tax-free return considerable flexibility. Investments may be planned to provide income within a 5 to 10 year period, or up to 35 years, by either acquiring mid-rotation plantations or planting land.

It is possible to match investments to known future events, such as providing for school fees or as a pension, with considerably greater flexibility than can be obtained under a pension scheme.

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