

## **Forest Tax Primer**

**Linda Wang  
Forest Tax Specialist  
USDA Forest Service**

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### **A Tax Expert?**

***Who is the figure behind every great man, the individual who knows his ultimate secrets? A father confessor?... no, the tax expert.***

***Louis Auchincloss***

## **Tax** *Important to Private Forests*

- Tax is consistently listed as one of the top concerns for private forest owners

## **General Principles**

- Income: capital gains better than ordinary income
- Loss: ordinary loss better than capital loss

## Tax Rates

- **Ordinary Income:**  
**10% - 35%**
- ***Long-term* capital gains:**  
**0% - 15%**

## Tax Status Is Key

- **Timber property is taxed either as an investment or a business**
- **Business is taxed either as an active or passive one**

## Tax Term: Basis

- **Most useful**
  - at timber sale
  - when timber suffers loss
- **Basis relates to property**
- **It is the purchase cost of a property**

## Inherited Property: Basis

- **The basis is the fair market value of the property**
- **Measured on the date of the decedent's death**

## Timber Basis: An Example

Pine sawtimber:

$$200 \text{ tons} \times \$20/\text{ton} = \$4,000$$

Pine pulpwood:

$$100 \text{ tons} \times \$5/\text{ton} = \$500$$

Hardwood pulpwood:

$$2000 \text{ tons} \times \$1/\text{ton} = \$2,000$$

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$$\$6,500$$



### Quiz #1

Is “basis” intimidating? :-)

## Sale Income of Timber

- Sale of stumpage are capital gains
  - Investment: Sec. 1221
  - Business: Sec. 631(b)
- Sale of cut timber by business: two parts
  - Capital gain and ordinary income
  - Sec. 631(a)

## Forest Management Expenses

- For Investment tax status:
  - Currently deductible but subject to income limit
  - The expenses must be reduced by 2% of adjusted gross income

## Forest Management Expenses

- **Business:**
  - **Active Business: Fully deductible**
  - **Passive Business: Restricted**

## Property Taxes

- It is a **deductible** expense
  - Deduct it annually
  - Or put it into the timber basis (“capitalize”) and deduct it upon timber sale



## Quiz #2

- Is income from stumpage sale taxed as capital gains?

## Reforestation

- Reforestation costs may be expensed, up to \$10,000
- Excess over \$10,000 may be deducted over 8 years (“amortized”)

## Timber Loss

- Hurricane, tornado, fire, theft, ice, snow storms... (“casualty loss”)
- Loss is deductible
- The amount is: the *smaller of* FMV loss or timber basis.

## Form T

- A tax form not familiar to most tax professionals
- Filing is not always required



## Quiz #3

- Can landowner write off \$14,000 reforestation cost in one year?



## New Tax Incentives from Farm Bill

- The Farm Bill was passed in May 2008
- Contains tax incentives for timber



## Timber Corporation Receives Lower Tax Rate

- **15% rate is granted for C-corp**
- **Available only for 1 year**
- **Must have held for more than 15 years**



## Conservation Easement Donation

- **This donation deduction is: up to 50% of adjusted gross income**
  - **100% if a traditional forest owner**

## Presidential Tax Return

### *President George W. Bush 2004 Tax Return*

<b>Salary</b>	<b>\$397,065</b>
<b>Interests</b>	<b>\$363,483</b>
	<hr/>
	<b>\$672,788</b>

**Total Taxes:**           **\$207,307**

**Refund:**                   **\$38,534**



## Endangered Species Expenditure

- One of the first tax incentives for ecosystem service production
- Not applicable to forest land



## Cellulosic Biomass

- Brand new tax credit—\$1.01 per gallon
- For fuel producers, not landowners

## The Size of the IRS

*In fiscal year 2006, the IRS employed almost 100,000 people and had a total budget of about \$10 billions!*

## Proposed IRS Regulation

- For lump-sum timber sale
- Timber buyers file Form 1099-S with the IRS
- Effective after the reg. is adopted

## Cost Share Payment

- Must report in the tax return
- May be excluded from income if qualified

## “Forest Health Management” Cost Share

- **Examples: Southern Pine Beetle, Mountain Pine Beetle cost shares**
- **Still pending the IRS approval for income exclusion**
- **Landowner must report as income**
- **Expense may be deducted**

## Tax Return

### *Teresa Heinz 2003 Tax Return*

<i>Salary</i>	\$0
<i>Tax-Exempt Interests</i>	\$2,781,791
<i>Dividends</i>	\$2,216,280
<i>Taxable Income</i>	\$2,023,596
 <i>Total Taxes:</i>	 \$628,401
<i>Refund:</i>	\$247,933

## **Tax Resources** *by US Forest Service*

- Provide timber tax workshops
- National Timber Tax Website:  
[www.timbertax.org](http://www.timbertax.org)

## **Tax Publications** *by US Forest Service*

- Annual Timber Tax Tips
- The Forest Landowner's Guide to the Federal Income Tax
- Federal Income Tax on Timber: A Key to Your Most Frequently Asked Questions
- [2009 Edition: Estate Planning for Forest Landowners—available now](#)

## **Tax Freedom Day**

- **In 1944, Americans must work the first 90 days, until March 30, to pay all taxes**
- **By 2008, it was April 23**

Source: Tax Foundation