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Publications

*Forest Owners Guide to the Federal Income Tax*,

Badly out of date,
Covers developments through 2000


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Publications


Order at http://www.timbertaxadvice.com

Updated and expanded at least annually

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Websites

• National Timber Tax Website
  – http://www.timbertax.org
  – Maintained by USDA Forest Service

• Timber Tax, LLC
  – A work in progress
  – Focus is on tax professionals
  – Depletion software will be available
  – http://www.timbertaxadvice.com
Timber As An “Investment”

- Not a tax shelter in classical sense
  - Can’t write-off more than out-of-pocket investment.
- Major advantage is accumulation of value and pre-tax compounding.
Characteristics of timber activities and associated actions

- High initial cost with little possibility of immediate recovery
  - Maximize proportion of available basis allocated to recoverable assets
  - Deduct and amortize reforestation expenditures
Allocation of Basis

• Original basis
  – Acquisition cost for purchase
  – Date of death fair market value for inheritance
  – Donor’s basis on date of gift

• Allocate original basis among assets based on proportion of total fair market value each asset represents
  • Example
Characteristics of timber activities and associated actions

• Long pre-productive period
  – Structure activity to allow write-off of qualified expenses against other income
    • Business
    • Investment
    • Hobby

Pennsylvania Black cherry
Investment Expenses

- Take standard deduction
  - No benefit at all
  - Capitalize carrying charges

- Itemize
  - Property tax
    - Add to other deductible taxes on Form 1040, Schedule A, Line 6 – Real Estate Taxes
  - Operating expenses
    - Add to other Miscellaneous Itemized Deductions on Form 1040, Schedule A, line 27, with attachment
    - No benefit until Miscellaneous Itemized Deductions exceed 2% of Adjusted Gross Income

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Business Expenses

• Claim deductible expenses on business form
  – Sole proprietorship
  – Corporation, C or S
  – LLC
  – Partnership
  – Estate

• Operating loss has same affect as adjustment to gross income

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Hobby Loss Rule

• What it says
  – If an activity produces a “profit” for 3 years in a consecutive period of 5 years, the IRS presumes the activity is engaged in with an intent to make a profit

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Hobby Loss Rule

Owners of small timber tracts can’t meet this test because of inherent nature of timber production process

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Hobby Loss Rule - Hoover’s definition of profit

Amount by which income from timber and other outputs plus appreciation in value of land and growing stock exceeds expenses of operation over expected life of activity
Reforestation Expenses

- Deduct up to $10,000 per year per qualified timber property (QTP)
- Amortize amounts over $10,000 per QTP in a given year
- Details
Characteristics of timber activities and associated actions that should be taken

• **Investment horizon multi-generational**
  - Arrange affairs to minimize liability for estate and other death taxes
  - Transfer management before death

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Timber Revenue

- Always can qualify for capital gains treatment
- Only exception is timber broker
Capital Gains Advantage

- **Individuals**
  - No 15.3% self-employment tax
  - Capital gains rates
    - 0% for 10% and 15% ordinary income brackets
    - 15% otherwise
    - Applies to “net long-term capital gains”
Capital Gains in 2011 & Beyond

• Without congressional action
  – Capital gains rate will be 20% because of reversion to pre-EGTRRA tax law

• President’s current proposal
  – 20% rate for c.g. & qualified dividends of joint filers >$250,000 after std. deduction & 2 personal exemptions, and >$200,000 for single
  – Otherwise current 0% and 15% rates apply
Capital Gains Advantage

• Non-corporate business
  – Capital gains pass through to owners
  – Owners pay tax on their share of gain at their individual rate

• C corporations
  – No rate advantage, but
  – Gains and losses offset each other
Qualifying for capital gains

- Long-term capital gains available
  - Disposal on stump as capital asset (IRC Sec. 1221)
  - Disposal of stumpage held for use in trade or business (IRC 1231) or primarily for sale (631(b) & 1231), pay-as-cut contract no longer required
  - Sale of cut products with election to treat cutting as a sale (IRC 631(a) & 1231)
Recovering basis

- Reduce revenue from disposals by basis of timber disposed of,
  - No percentage depletion
  - “Depletion” applies only to party severing timber
  - Stumpage – recover “allowable basis”
Use Form T – Forest Activities Schedule

- Revised in December 2005
- Don’t file if you only make an occasional sale of timber, 1 or 2 every 3 or 4 years
- **Always complete and keep in your files**
- If make sales more often, file if
  - Claim a deduction for depletion
  - Elect under section 631(a)
  - Make an outright sale of timber under 631(b)
- **Form T**

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