

Financial Aspects of Owning Forestland

Information on various tax codes, record keeping and audits for private forestland owner by Larry Camp, RPF #1698

Relevant Internal Revenue Codes (IRC) for Forestland Owners

IRC § 126 - Cost-share payments

IRC § 162 - Deductible Expenses

IRC § 165 - Casualty losses, thefts, condemnations

IRC § 167 - Depreciation

IRC § 170(h) - Conservation Easements

IRC § 179 - Deduction for Capital Expenses

IRC § 183 Hobby Loss (operating a business or is it a hobby?)

IRC § 194 - Reforestation

IRC § 469 - Passive Loss rules

IRC § 611 Depletion (cost recovery for timber)

IRC § 631(a) & 631(b) - Gains or Losses from sale of Timber

IRC § 1031- Like-Kind Exchanges

IRC § 1033 - Involuntary Conversions

IRC § 2001 etc. - Estate Taxation and Legacy Planning

DISCLAIMER

The information in this handout is for educational purposes only. It is NOT legal or accounting advice. Each taxpayer's circumstances need to be considered for the appropriate application of tax law. Please consult a tax professional.



"What is a TPZ?" A Timberland Production or Timberland Preserve Zone (TPZ) allows County Boards of Supervisors to designate areas of timberland as preserves, restricting use to the production of timber for an initial 10-year term.

The land is subject to enforceable restrictions, meaning it is assessed for taxation based on the values of comparable lands subject to similar restrictions. Lower land value = lower taxes.

Rezoning land formerly identified as TPZ incurs tax recoupment fees and will change how the land is assessed. Please consult your tax professional for specifics.

IRC § 194 – Reforestation

DEFINITION: COSTS ASSOCIATED WITH REFORESTATION INCLUDE SITE PREPARATION COSTS, SEEDLING COSTS AND LABOR AND TOOL EXPENSE

Reforestation costs are capital in nature and are NOT deductible in the year that they are incurred. Establishing a reforestation account or sub-account can be established to help landowners account for reforestation costs. Additional reforestation expenditures generally amortize over 7 years (84 months).

A deduction of up to \$ 10,000 for reforestation expenses is allowed per Qualified Timber Property (QTP). The credit is available to individuals, partnerships, corporations, and estates although not to trusts. It can also be allocated to either single or multiple tracts

“What is a QTP?” A site that is at least one acre in size; planted in the normal manner used for reforestation; and held by the taxpayer for commercial production of timber. This does not apply to ornamental trees, including Christmas trees.

IRC §170(h) - Conservation Easements

A contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes, granted in perpetuity.

The term "conservation purpose" means -

- (i) the preservation of land areas for outdoor recreation by, or the education of, the general public;
- (ii) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem;
- (iii) the preservation of open space (including farmland and forest land) where such preservation is for the scenic enjoyment of the general public, or pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or the preservation of an historically important land area or a certified historic structure.

IRC § 1033 - Involuntary Conversion

Definition: When property is destroyed, stolen, or condemned for public use. Destruction is often synonymous with a casualty such as fire or windstorm but it need not be a sudden event. This can also include theft of timber by trespass or loss due to severe drought.

Claiming an Involuntary Conversion permits a taxpayer to avoid paying gain on the property. It allows for the reinvestment of income generally within a 2 year time period.

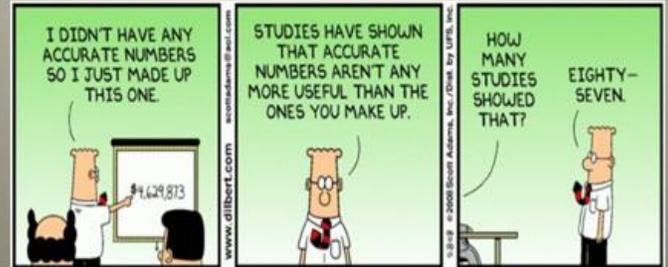
Replacement property must be similar in nature, such as:

- Reforestation on timberland owned by the taxpayer,
- Buying additional land for replanting,
- Acquisition of standing timber, or
- Acquisition of timberlands.

A Few Words on Record Keeping and Audits

1. Keep all receipts, management plans, and photos related to your forest land. Even gas receipts as you travel to your property can be used as a deduction!
2. Find a record keeping method that works for you. Shoebox, journal, excel spreadsheet, etc. Know that each of these methods will have limitations.
3. Form T: Forest Activities Schedule is the primary form for reporting activities related to timber growth and harvest. This does not need to be filed every year, but it is good practice to keep it up to date, especially if buying or selling land.
4. Records are important because they help you document your ownership activities and income and expenses. They will come in handy if audited....
5. Reply to document requests in case of an audit. Document all calls, meetings, actions and agreements. Request that your IRS agent verify this.
6. If you cannot reach an agreement with the IRS, request that an IRS Forester be assigned to review the issue.
7. You have an option of appealing decisions if you have a supportable position.

Do not use the following approach to your record keeping !



Dilbert cartoon by Scott Adams

TPZ, Timber Yield Tax References and other Resources

- Guide to the Calif. Timber Yield Tax pub. 87 <https://www.cdtfa.ca.gov/formspubs/pub87.pdf>
- TPZ land values <https://www.cdtfa.ca.gov/taxes-and-fees/2020-Timberland-Production-Zone-Values-signed.pdf>
- Harvest Value Schedules https://www.cdtfa.ca.gov/formspubs/cdtfa401hs_vi.pdf
- Allocation of purchase price worksheet example <https://ucanr.edu/sites/forestry/ForestStewardsHipWorkshops/Materials/>

Internet Web Resources

- www.irs.gov
- www.timbertax.org - a good non-government site sponsored by USFS, Univ. Georgia, American Tree Farm System
- www.fs.fed.us/spf/coop - USDA Forest Service tax publications