

# Forestry Income Tax Series

## Timber Tax Overview

*Are you a taxpayer? Do you own forestland?* If you answered “yes” to these questions, then you need to understand the unique tax rules that can affect your management decisions and the profitability of your forest. If one of your objectives is timber production, this publication will give you an overview of the tax laws that apply to you. It focuses mainly on federal taxes, but it also includes information on the Mississippi Reforestation Tax Credit. Mississippi has a “piggyback” tax code, meaning that state deductions are usually the same as federal deductions, so you can assume that deductions for federal tax purposes will also be deductions for state purposes, with the exception of reforestation costs treated with the Mississippi Reforestation Tax Credit.

Because the tax code is so complex and dynamic, you should consider this publication as an educational guide – not legal advice. However, it does provide useful information on timber taxation, with brief examples that will alert you to seek additional information as needed. To help you understand the topic better, important words that may be unfamiliar to you are defined within boxes (see next column). Each topic contains a reference to Agricultural Handbook 718 *Forest Landowners’ Guide to the Federal Income Tax*. This is the standard reference for forest landowners, and it can be obtained from your local Mississippi State University Extension Service (MSU-ES) office.

### IRS Categories for Forest Landowners

The IRS separates forest landowners into three taxpayer categories: *hobby owners*, *investors*, and *business owners*. Do you know which category best fits your situation? You should! Each category differs in how expenses are deducted and in how income is reported. Your category depends on your desire to produce income from growing timber and how involved you are in managing your timberland.

Fortunately, you are able to choose your preferred category based on your individual situation. Once you select a category, it cannot be changed without a very good reason. If your situation is already established, you may not have a choice. Following are the three categories with explanations of how they differ (Agricultural Handbook 718, pp. 17-19).

#### Hobby Owners or Personal Use Owners

Forestland held and managed for personal use is considered a hobby. A typical hobby owner owns land for personal hunting or recreation and does not intend to make a profit from growing and selling timber. If you are a hobby owner, you cannot deduct your yearly expenses except when you have income from your timber property that exceeds those expenses. However, you may capitalize your



expenses and deduct them from some future timber sales.

Hobby timber sales do qualify for capital gains treatment, which provides a lower rate of taxation than ordinary income rates. When you reforest your hobby acres with commercial timber species, you can use the special federal tax breaks for reforestation and the Mississippi Reforestation Tax Credit. To avoid being characterized as a hobby landowner, state your intention in writing to make a profit from your timber, either in your management plan or in your timber tax or tree farm journal, and manage your forest land accordingly (Agricultural Handbook 718, p. 17).

**Capitalization:** The process of writing costs in an account so they may be recovered (deducted) in the future when the property is sold (for example, timber) or as it is worn out (for example, machinery).

**Capital Gain:** The increase in value of a capital (long term or large value) asset – such as land and timber. Capital gains are taxed at lower rates (8, 10, 18, and 20%) than ordinary income rates (10, 15, 27, 30, 35, 38.6% for 2001-2002). Both rates are set by the U.S. Congress and are subject to change.

Generally, the asset must be owned for more than a year to qualify for capital gains treatment. Capital gains are not subject to self-employment taxes.

#### Investors

If you own forestland and intend to sell timber in the future for a profit or to grow timber for capital appreciation, but you are not an active manager, you may be an investor. If you are a typical investor, you probably hire a forestry consultant and perhaps others to plan and carry out most management activities. You may make only one or two timber sales in your lifetime. You are allowed to deduct most management expenses as miscellaneous itemized deductions on Schedule A of Form 1040. Some investors prefer to take the standard deduction and capital-

ize these expenses. As an investor, you qualify for both the federal and state tax programs for reforestation, so you can recover much of your site preparation and reforestation costs within 8 years through tax credits and amortization. You are eligible for capital gains treatment of timber sales income if you have owned the timber for the required amount of time. Landowners who make frequent timber sales cannot be categorized as investors and must be categorized as business owners. Unfortunately, the IRS has never issued specific rules on the definition of “frequent” (Agricultural Handbook 718, pp. 42-43).

**Amortization:** Recovery of capitalized expenses over a period of years before any sale of property. Reforestation expenses can qualify. Up to \$10,000 in annual reforestation expenses can be deducted in the 8 years following the expenditure.

## Business Owners

As a business owner, you intend to make a profit from growing and/or selling timber and are actively involved in managing your forest. Business owners are further subdivided according to Passive Loss Rules into two categories: *material participants* or *passive participants*. The difference between material and passive participation is the amount of time you spend on the business activity.

**Passive Loss Rules:** Rules from the Tax Reform Act of 1986 designed to eliminate tax shelters. They apply only to businesses, not to hobby owners or investors. The rules do not affect the deduction of expenses, but do affect your ability to offset operating losses against income from other sources. They also affect your ability to use the reforestation tax credit.

Material participants manage their property on a “regular, continuous, and substantial” level and may deduct expenses against any source of income. Passive participants consider themselves “in the business” but are inactive managers. Passive participants face special restrictions for deducting expenses and reporting losses. If you are a passive business owner, then you may use only the reforestation tax credit to offset taxes on passive income. If you are a materially participating business owner, you may use the reforestation tax credit against taxes owed from any income source.

To be considered as a material participant, you will need to pass one of seven tests in the Passive Loss Rules that determine how active you are in managing your forest. As a business owner, you need to keep records of the time spent managing your property to prove you can pass one of these tests (Agricultural Handbook 718, pp. 40-42).

Landowners who are “in the business” and are material participants may deduct forest management expenses on the front of IRS Form 1040. Business owners use Schedule C “Profit or Loss from Business” to itemize forest business expenses. Some landowners qualify as a “Farmer,” which is a special business category that uses Schedule F

“Profit or Loss from Farming.” Unlike investors, business owners cannot always qualify for capital gains treatment of timber sales income even if the timber was owned for the required amount of time. When business owners sell timber for a lump sum, their timber sales income is taxed at the ordinary income tax rate and social security and Medicare tax rules apply. When business owners sell timber by the cord, by the thousand board feet (MBF), or by some other unit, the timber sales income may qualify for capital gains treatment under IRS Section 631(b). As a business owner, you may use the special state and federal tax programs (tax credits and amortization) to recover site preparation and reforestation costs within 8 years.

**Lump Sum Sales:** Selling timber on a lump sum basis means you and the buyer agree on a total price for the standing timber before it is cut. The amount paid does not vary according to the volume of timber or the number of trees harvested. Ownership of the timber passes to the buyer when the contract is signed and money changes hands, not when the timber is cut.

**IRS Section 631:** IRS regulations on how business timber sales must be sold in order to qualify for capital gains treatment of income. 631(b) sales are eligible for capital gains treatment if the holding requirement is met and the owner “retains an economic interest.” The term “retains an economic interest” means the seller owns each tree until it is actually cut and measured, unlike in the lump sum sale as described above. In a 631(b) sale, timber is sold by the unit-cord, ton, cunit, thousand board feet, or tree – rather than for a single lump sum.

## Examples of IRS Categories

- Mrs. Lola Friendly has 60 acres of land she inherited from her grandfather. She and her family use the property as a retreat from their city life. Her husband is an avid birdwatcher and has planted sunflowers and other seed-bearing plants for the birds. Her children love to hunt deer, and they have the forested areas prescribe burned every 5 years. Mrs. Friendly doesn’t plan to harvest any timber except in case of insect infestation or other destructive event. She is a *hobby owner*.
- Mrs. Woody Brown has 160 acres of land she inherited from her parents. Mrs. Brown had the entire tract planted in trees 10 years ago. Every third year she has a neighbor plow fire lanes. Apart from property taxes, this is her only operating expense on the property. On the advice of her consulting forester, she plans to thin the trees twice during the next 10 years and harvest and replant in 25 years. Her consultant will manage all the sales activities. She is an absentee landowner and seldom visits her property. She is an *investor*.
- Mr. Cliff Robin, Mrs. Brown’s brother, owns 160 acres next to his sister. He lives 150 miles from his land and is actively involved in its management. Mr. Robin is practicing uneven-aged management and has a small

timber sale every year or two. His yearly expenses include a home office, travel to and from the property, tractor operation and maintenance (for fire lanes and road maintenance), herbicides, and property taxes. He is a *business owner*.

## Record Keeping

You must maintain good records in order to take maximum advantage of the special tax treatments available for timber. At a minimum, keep a tree farm journal that lists all activities, costs, and incomes from your forest. Ideally, maintain accounts for land, timber, other capital assets, and yearly operating expenses. Basically, your accounts need to be in a format that allows you to complete IRS Form T *Timber Activities Schedule*. Form T is an informational form that can be used as a guide to set up necessary accounts and records and to fill out the required tax forms (Agricultural Handbook 718, pp. 111-123).

Maintain accounts for land and timber, including reforestation and site preparation, for as long as you own the property so that you will have the information required to figure your basis. If you deed the property to someone as

a gift, pass on these records to the new owners because they will need this information to determine their timber basis. Operating expense records are normally kept for 3 years. Income records are kept for at least 6 years. If you want to determine the economic return on your various forestry enterprises, you must keep individual income and expense records for each separate parcel and/or timber stand. If you are a business owner, keep records of the time spent on your forest business to prove your material participation.

**Basis:** The amount of investment in a capital asset as recorded in a capital account such as land, timber, or equipment. The initial basis for a property depends on how it was acquired as described later. The basis increases as you capitalize costs into the account. The basis is reduced as you amortize, depreciate, deplete, or sell the asset.

**Timber Stand:** A group of trees in one location, usually similar in species mix, size, or age that will be treated as one unit for management purposes.

## Example of a Tree Farm Journal for a Business Owner

Date	Activity	Income/(Cost)
4/3/95	Attended Miss. State Forestry Extension Short Course: Marketing Your Timber, Rankin Co. Extension office, 10 hours. 64 miles of travel.	(\$25)
6/1/95	Hired Trees-R-Us Forestry Consultants to cruise Grandpa's Woods and establish timber basis for property inherited 3/1/90. 3 hours of walking landlines with consultant.	(\$250)
12/1/95	Miss. Forestry Commission prescribed burned Grandpa's Woods. 7 hours of burning time, 1 hour of walking landlines.	(\$300)
4/5-8/95	Marked Grandpa's Woods for pulpwood sale. 30 hours of work, purchased paint gun and paint from Forestry Suppliers	(\$200)
6/5-18/95	Sold marked wood to Cutter's Pulpwood Services for \$8/cord, 150 cords cut. Was on site 2 hours each day to ensure security of sale.	\$1,200

## Recovery of Forestry Expenses

Many of the costs you incur from managing your forestland can be recovered by reducing your taxes. How you recover these expenditures depends on whether the sum is an operating cost, a sales expense, or a capital cost. Categorizing forestry-related expenses can be confusing because the same practice can be a capital, operating, or sales expense, depending on why and when the expense was incurred. For example, a timber cruise (estimation of the amount of timber and its value) is a capital expense when done to acquire property, a management expense when done to write a management plan, or a sales expense when done to sell the timber. Timing, purpose, and amount of the expense determine its category and eventual recovery.

## Operating or Management Costs

Ordinary operating costs are the routine expenses you incur in managing your property on an ongoing basis. Ordinary operating or management costs are generally expensed in the year they occur. This means they are deducted as miscellaneous itemized deductions for investors, deducted as business expenses for business owners, or deducted as farming expenses for farmers. You may choose to capitalize all forest management costs instead of deducting them yearly, but once you make this choice, you must stick with it.

Examples of operating and management costs include the cost of small tools, travel expenses, timber cruises for management purposes, prescribed burning for hazard reduction, fire lane maintenance, road maintenance, herbicide release not associated with reforestation, equipment

operating expense, home office expense, and so on. Salaries and wages paid to hired help and not related to tree planting and other capital projects may also be expensed. However, you as the landowner cannot deduct the value of your own labor, as you will be paid by the eventual profits. Carrying charges such as property taxes and mortgage interest may be expensed or capitalized yearly. Wildlife habitat improvement expenses are not deductible unless they have a profit-related motive (for example, if you lease your property to hunters) or unless they are done for soil conservation (Agricultural Handbook 718, pp. 38-40).

## Timber Sales Expenses

Costs associated with making a timber sale can include forestry consulting fees, surveying, advertising, attorney's fees, timber sales monitoring, and security. You do not deduct these costs like other expenses. Instead, you subtract them directly from the timber sales proceeds, reducing the amount of taxable gain. After a timber sale, use Form T's Schedule F "Capital Returnable through Depletion" and Schedule C "Profit or Loss from Land and Timber Sales" to determine your profit or loss and fill out your tax return (Agricultural Handbook 718, pp. 45-49).

## Capitalized Costs

Capital costs are the costs of investment in long-term assets such as land or timber. Examples of these costs are the costs of acquiring land and timber, site preparation and reforestation, equipment, and buildings. These costs are not deducted as annual expenses. Capital costs are capitalized (recorded in an account to become your basis) and then recovered through amortization, depletion, or depreciation deductions, or when the asset is sold. How you recover the costs depends on standard accounting rules and the nature of the asset (Agricultural Handbook 718, pp. 21-22).

## Methods of Capital Cost Recovery

- **Amortization** - The money (up to \$10,000 a year) invested in establishing a new forest is recovered through amortization. This capital cost recovery method allows you to expense or deduct these costs over a period of 8 years according to the law. There is a limit of \$10,000 per year on reforestation expenditures eligible for amortization. Any costs above that maximum are capitalized in your timber account (as your timber basis) and are then recovered through depletion.
- **Depletion** - For natural resources such as timber, the cost or other basis is recovered as the timber is cut and sold or otherwise disposed of. You deplete the basis of the timber removed by (1) subtracting it from the timber account and (2) subtracting it from the timber sales proceeds to determine the net taxable gain. For a clearcut harvest, the entire basis of the timber is subtracted from the sales proceeds. When only part of the timber is cut, such as a thinning, a proportional amount of the basis is subtracted from the timber account and the sales proceeds.

- **Depreciation** - You use this method of recovery for material assets such as trucks, tractors, roads, culverts, and so on. Depreciation is the deduction of the cost or other basis of a material asset over its estimated useful life according to standard accounting rules. Here you are taking deductions as the asset is used up or wears out.

## Tax Credits

Under both the state and federal tax laws, you are allowed a tax credit for establishing a new forest. A tax credit is a dollar-for-dollar reduction in the amount of taxes you pay. The maximum federal tax credit for reforestation is \$1,000 per year.

## Acquisition Costs

The cost of acquiring forestland must be capitalized into the land and timber accounts when it is purchased. Such costs include attorney's fees, surveying costs, timber cruises for acquisition, title fees, and purchase price of the property. The acquisition cost is divided between land and timber on a proportional basis and is recorded in the appropriate land or timber account. These costs form the initial basis of the property and cannot be recovered until the land or timber is sold. (Agricultural Handbook 718, pp. 21-26).

The initial basis of inherited or gifted property is very different from the basis of purchased property. The initial basis of inherited property is the fair market value of the property at the time of the decedent's death. This is called a "stepped-up basis," as the basis is usually increased or stepped up to fair market value. Gifted property generally retains the basis of the giver. The IRS sets the rules on basis.

## Timber Basis

Timber basis is important because it helps determine your net taxable income on any timber sales. When you sell timber, the basis in that timber (along with sales expenses) is subtracted from sales income to determine the net taxable gain. It also is used to determine the amount of deductible loss in case of a casualty or other loss. Establish your timber basis when you acquire the property, and keep it up to date to significantly reduce taxes on the eventual sale of timber (Agricultural Handbook 718, pp. 21-26). Keeping the basis up to date involves adding in any capitalized costs as they occur, updating volumes before any timber is sold, and depleting or subtracting basis as timber is cut, sold, or destroyed. Use IRS Form T *Forest Activities Schedule* as a guide to set up your timber account with basis. See MSU-ES Publication 1983 *The Basics of Basis* for detailed information.

## Examples of Basis

Leif Oakman owns 180 acres of land acquired in 1955 for \$18,000. He did not set up separate land and timber accounts at that time. Mr. Oakman clearcut his property twice and allowed natural regeneration to reestablish the forest, so he has no basis in his timber account. He sells 60 acres to his neighbor Forest Green for \$87,000. He gives his nephew Hilton Glade 60 acres. He dies shortly afterwards, and his daughter Scarlet Oakman inherits the last

60 acres. Assume that each 60-acre tract had the same land and timber value, and the land and timber each made up 50 percent of the property value. What is the timber basis of each?

- Forest Green purchased 60 acres for \$87,000 and paid \$3,000 for legal fees and surveying costs. His total acquisition cost was \$90,000. Mr. Green's land basis is \$45,000, and his timber basis is \$45,000.
- Hilton Glade's basis is the same as the donor's (Mr. Oakman's) basis. His land basis is \$6,000 (one-third of Mr. Oakman's original \$18,000 acquisition cost). Mr. Glade has no timber basis because there were no capital costs involved in establishing or maintaining the current forest.
- Scarlet Oakman inherited the property at her father's death. At that time, the property was valued at \$800 per acre for land and \$55,000 for timber. Her land basis is \$48,000, and her timber basis is \$55,000.

Each new owner has a different basis because of the way each acquired the property.

### Equipment and Other Depreciable Costs

Equipment is a capital asset with an expected useful life of more than 1 year. You recover these costs by depreciating them over a specified period of years according to standard accounting rules such as the Modified Accelerated Cost Recovery System (MACRS) and IRS regulations. For example, the expected useful life of a light truck or automobile is 5 years. Bridges and culverts are expected to last 15 years. The IRS allows the cost of equipment to be recovered by depreciation over the estimated useful life of the asset. Business owners may choose to deduct certain depreciable costs under IRS Section 179, which speeds up the depreciation/deduction process. Temporary land improvements such as gates, bridges, and temporary logging roads are depreciated over the expected useful life of the asset or according to a units-of production method. Consult IRS Publication 946 *How to Depreciate Property* for details and see Agricultural Handbook 718, pp. 29-38.

### Example of Southfork Tree Farm's Reforestation Account

Date	Activity	Cost	Federal Credit/ Amortization Deduction	Adj. Basis	State Credit/ Amortization Deduction
2/9/00	Plant improved loblolly – 600 trees/acre McLeod Forestry Services	\$20,000		\$20,000	
1/15/01	Tax credit		\$1,000	19,500*	\$10,000
1/15/01	Amortization deduction for year 1		679	18,821	0
1/15/02	Amortization deduction for year 2		1,357	17,464	0
1/15/03	Amortization deduction for year 3		1,357	16,107	0
1/15/04	Amortization deduction for year 4		1,357	14,750	0
1/15/05	Amortization deduction for year 5		1,357	13,393	0
1/15/06	Amortization deduction for year 6		1,357	12,036	0
1/15/07	Amortization deduction for year 7		1,357	10,679	0
1/15/08	Amortization deduction for year 8		679	10,000	0

\*The basis used for amortization must be reduced by 1/2 of the tax credit claimed.

### Site Preparation and Reforestation Expenses

The cost of establishing a new forest, either by planting or by natural regeneration, is a capital expense. These costs include site preparation, planting, seeding, or other expenses necessary to enable the new forest to become established. You can recover up to \$10,000 of these expenses each year by using the federal reforestation tax credit and an accelerated amortization program. Any costs in excess of \$10,000 per year must be capitalized and recovered when the timber is sold. Consult MSU-ES Publication 2102 *Handling Reforestation Expenses* for details. Also, see Agricultural Handbook 718, pp. 26-29.

If you are a Mississippi taxpayer establishing a new forest on Mississippi land, you are also eligible for the Mississippi Reforestation Tax Credit. You may obtain a tax credit of up to \$10,000 on your Mississippi income tax return over your lifetime to offset reforestation expenses. To use this program, you must have a reforestation plan written by a professional forester. Consult MSU-ES "Forest Resources Management Technical Note 14C" for details.

### Example of a Tree Farm Reforestation Account

James and Dorothy Brown of Southfork Tree Farm are planting 320 acres of bare land. They are using the special tax treatment for reforestation costs for both federal and state taxes. An example of their reforestation subaccount is shown *below*. Their total costs are \$20,000. Their federal tax credit is \$1,000, the maximum allowable. The state tax credit is 50 percent of total costs, or \$10,000. Their amortizable basis is \$10,000 less one-half of the tax credit, or \$9,500. The amount above \$10,000 must be capitalized. The initial adjusted basis is \$19,500. Divided over 7 calendar years, each deduction is \$1,357. The first year's deduction and the eighth year's deduction are for one-half year, or \$679. There is no state amortization deduction, as the amortizable basis for Mississippi tax purposes is the federal amortizable basis (\$9,500) less the state tax credit (\$10,000), which is a negative number.

## Cost-Share Payments for Reforestation/Afforestation

You may use a variety of cost-share programs to cover part of the costs of forest management, including the Forestry Incentive Program (FIP), the Conservation Reserve Program (CRP), the Wetlands Reserve Program (WRP), and the Mississippi Forest Resources Development Program (FRDP). The 2002 Farm Bill merges the federal tree planting programs into a new program called the Forest Land Enhancement Program (FLEP). Please check with your county MSU-ES office or your local Natural Resource Conservation Service office to find out details on this program.

You may exclude cost-share payments for reforestation and site preparation from taxable income if you follow the IRS provisions. One exception is cost-share payments from CRP, which are taxed as ordinary income. If you exclude cost-share payments from income taxation, then you must exclude the cost-shared part of reforestation or site preparation costs from the amount used to figure the reforestation tax credit and amortization (Agricultural Handbook 718, pp. 58-61). Mississippi excludes all forestry cost-share programs from taxation.

## Tax Treatment of Forest Income

### Timber Sales Income

If you are an investor or a hobby owner, income from the sale of standing timber is eligible for long-term capital gains treatment if held for more than 1 year. Timber held for less than 12 months may be treated as a short-term capital gain. Capital gains are reported on Schedule D of IRS Form 1040. If you are in the timber business, sale income is reported as the sale of business property on IRS Form 4797. If your sale qualifies as a 631(b) sale (that is, it is sold on a per-unit basis), then the income is eligible for capital gains treatment as long as the holding requirements are met. You must remember to pay estimated taxes on timber sales income. Self-employment (Social Security and Medicare) taxes are due on timber sales receipts taxed as ordinary income, such as when business owners sell their timber on a lump sum basis. Taxes are paid on the net taxable gain, not the total sales proceeds. Subtract your timber sales expenses and the appropriate timber basis from the total sales proceeds to determine net taxable gain (Agricultural Handbook 718, pp. 45-57).

### Example of Timber Sales Income

Forest Green purchased 60 acres for \$87,000 and paid \$3,000 for legal fees and surveying costs. His total acquisition cost was \$90,000. The land and the timber each equalled 50 percent of the value of the property. His land basis is \$45,000 and his timber basis is \$45,000.

Mr. Green allows his timber to grow for 5 years. At that time, he hires a consultant to sell his timber on a lump sum basis and agrees to pay him 10 percent of the timber sales proceeds. The sale price for the timber is \$65,000.

*What is his net taxable gain?*

#### Formula:

$$\text{Sales Price} - \text{Timber Basis} - \text{Consultant's Fee} = \text{Net Taxable Gain}$$

#### Example:

$$\$65,000 - \$45,000 - \$6,500 = \$14,500$$

Mr. Green is eligible for capital gains treatment if he is an investor. At the 20 percent capital gains rate, his tax is \$2,900. If Mr. Green were “in the business,” he could not receive capital gains treatment for a lump sum sale. As a business owner in the 27 percent tax bracket, his income tax on the \$14,500 gain would be \$3,915. He must also pay any required self-employment taxes on that gain because it is considered as ordinary income rather than as a capital gain.

### Other Forest Income

Hunting leases, timber leases, CRP payments, grazing leases, and other recreational leases or fees generate ordinary income for the forest landowner. You may generate a variety of “other” products from your property. The income produced from products such as grapevine wreaths, pine straw, mushrooms, ginseng, or other products is considered ordinary income. Selling firewood or pulpwood bolts directly to customers is also considered as ordinary income although you can obtain capital gains on the stumpage value of these products under IRS Section 631(a). Ordinary income is subject to the ordinary tax rates and Social Security and Medicare taxes (Agricultural Handbook 718, p. 61).

### Losses

As a forest landowner, you may be shocked to learn how little you can deduct when timber is destroyed or damaged because of a casualty or other event. The reportable deduction for any type of loss is limited to the loss in fair market value or the timber basis, whichever is less. If you do not have a basis, the reportable loss is zero. The rules for claiming losses are complicated, so be careful in determining the type of loss and have documentation to support your claim. Some types of losses are deductible, some are not. Following are the types of losses:

- **Normal losses** are not deductible. Losses from poor planting practices, expected mortality, and low levels of insect or disease are considered part of the risk of growing timber. You cannot deduct these losses.
- **Casualty losses** are losses from sudden, unexpected, or unusual events. Examples include tornado, hurricane, and wildfire. Usually disease or insect infestations are not casualty losses. Use IRS Form 4684 *Casualties and Thefts* to report these losses.
- **Noncasualty business losses** result from abnormal events. As with casualty losses, they are unusual or unexpected losses. Unlike casualty losses, they are not sudden. Sometimes the death of seedlings from an extended, unusual drought is a noncasualty business loss. Epidemic losses from Southern Pine Beetles may

be noncasualty business losses. These losses are reported on IRS Form 4797.

- **Thefts and condemnations** may result in deductible losses. As with other losses, the actual loss is reduced by any compensation received. Use IRS Form 4684 *Casualties and Thefts* to report these losses.

You are also expected to try to salvage timber following a loss. If the salvage income is greater than the basis, you have a taxable gain. You may be able to postpone paying taxes on such a gain if you reinvest in qualified replacement property (buy more timber or timberland, reforest, or buy standing timber) within a specified period of time. The time allowed for purchase of replacement property also varies according to the type of loss. As you can see, tax treatment of losses is very complicated, so you should check with your tax advisor on how to handle specific losses (Agricultural Handbook 718, pp. 67-77).

## Timber Tax Information Sources

Many sources of information on timber taxation are available to you. The chief resource is Agriculture Handbook 718 *Forest Landowner's Guide to the Federal Income Tax*, referenced for each topic in this publication. Every aspect of timber taxation is covered in this handbook, with many detailed examples. You may obtain a copy from the U.S. government bookstore at <http://bookstore.gpo.gov/locations/index.html>, or on the World Wide Web at

[www.timbertax.org](http://www.timbertax.org), or at [www.fs.fed.us/spf/coop/](http://www.fs.fed.us/spf/coop/). You may also obtain a copy of the Agricultural Handbook 718 and MSU-ES tax publications from your county Extension office.

Extensive tax information can be found on the Web, starting with the National Timber Tax web site at [www.timbertax.org](http://www.timbertax.org). Every forest landowner needs to use IRS Form T *Forest Activities Schedule* as a guide for setting up timber accounts. The MSU-ES web site has timber tax publications available for downloading at [www.msucares.com/](http://www.msucares.com/). The IRS has an excellent web site at [www.irs.gov/](http://www.irs.gov/) containing all current forms (including Form T) and publications for downloading. IRS tax forms can also be requested from 1-800-TAX-FORM (1-800-829-3676). The Forest Landowners Tax Council maintains a web site with information about current legislation on timber taxation at [www.fltc.org](http://www.fltc.org).

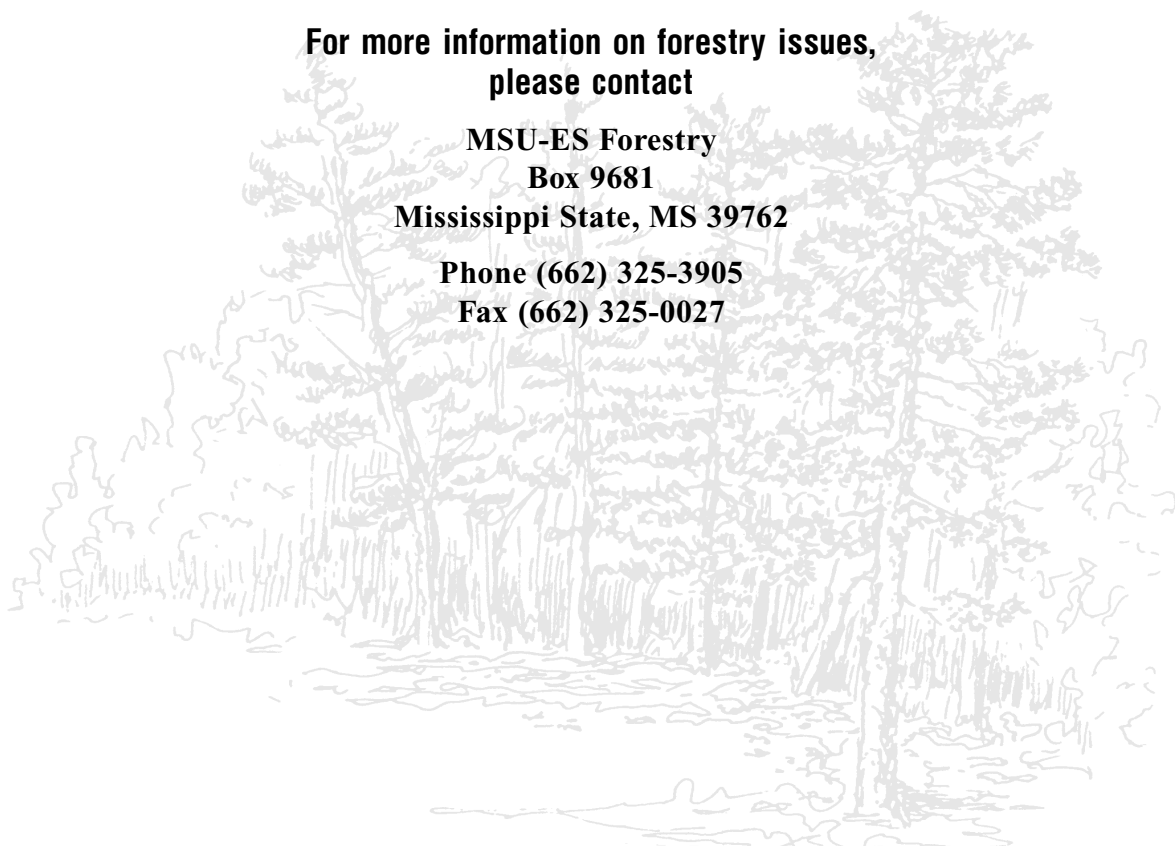
Forestry magazines are a good source of up-to-date information on timber taxation. *Forest Landowner*, *Tree Farmer*, and *National Woodlands Owner* magazines have regular columns on forestry and taxation, written by nationally recognized experts.

Extension Forestry in the MSU Department of Forestry teaches a Timber Tax Fundamentals Short Course at a variety of locations throughout Mississippi. Check with your county MSU Extension office to see when a course will be taught near you.

**For more information on forestry issues,  
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