

Webinar Portal for forestry and Natural Resources




Timber Tax Update for the 2014 Tax Year

01:00(Eastern Time)


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Webinar Portal
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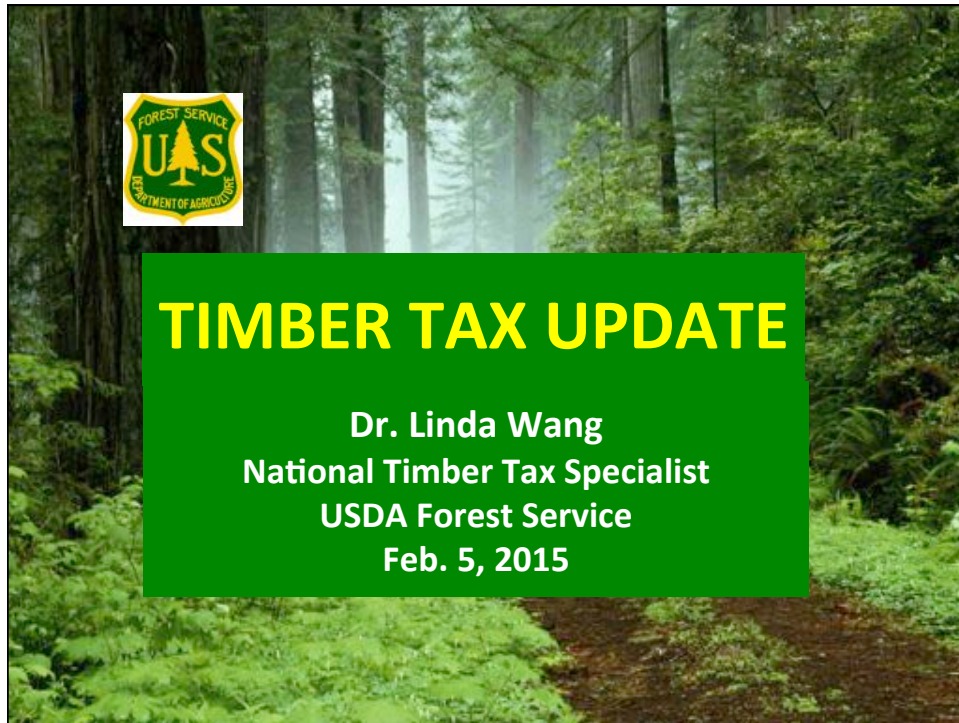
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- B. **Mountain**
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- E. **Other**





TIMBER TAX UPDATE

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Today's discussion is educational, NOT legal or accounting advice, since the facts and circumstances of each taxpayer's individual situation need to be taken into consideration for exact application of the tax law.

DISCLAIMER

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Tax Rates

- **Ordinary Income:**
10% - 39.6%
- **Long-term capital gains:**
0% - 20%

Tax Rates

- **0% long-term capital gains tax rate:**
 - ✓ If taxable income is up to \$73,800 (joint returns)
 - ✓ up to \$36,900 for single taxpayers
- **20% max. rate if taxable income is over \$457,600 (Joint) or \$406,750 (Single)**
- **Otherwise, 15% max. tax rate**

Tax Rates

- **3.8% Net Investment Income Tax**
- **The tax is imposed on the lesser of:**
 - Net investment income for the year or
 - The excess of modified adjusted gross income over \$200,000 (\$250,000 joint filers)

An Example

- **Husband and wife have \$270,000 adjusted gross income, including \$50,000 capital gains.**
- **The excess of \$270,000 over \$250,000 threshold is \$20,000. Thus, their net investment income tax is \$760, or 3.8% of \$20,000**

Net Investment Income

- ✓ interest, dividends
- ✓ annuities, royalties, rents
- ✓ net gain from sale of investment property
- ✓ net gain from sale of passive business property

Tax Status Is Key

- Personal property
- Investment property
- Business property



Quiz

- If your adjusted gross income is less than \$250,000, your capital gains are not subject to the 3.8% net investment income tax.

True or False?



TAX LAW CHANGE

Increased Depreciation

- A new tax law was enacted in December 2014 that increased the amount of tax deduction on depreciation

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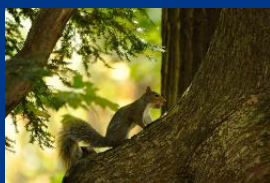
Increased Depreciation

- Expense up to \$500,000 spent on qualifying business property in 2014
- In addition, a 50-percent depreciation deduction is allowed in 2014

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TIMBER SALES



A Question

- Timber sales are not taxable because the current tax law allows special tax incentives to the timber resource.

True or False?

Sale of Investment Timber

- Sale of *standing* timber held as an investment is a capital gain

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Sale of Business Timber

- 1) Sale of *standing* timber held in a *business* is a capital gain if it's held for more than 1 year
- 2) Sale of *felled* timber: all gains are ordinary income unless a sec. 631(a) election is made
 - ✓ The timber must be held for more than 1 year before it is cut

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Investment Timber Sale: Tax Reporting

- Form 1040 Schedule D
- Form 8949, as applicable

Sale of Standing Timber by Business: Tax Reporting

- Report a capital gain (or loss) from the outright or pay-as-cut sale of standing timber on Form 4797
 - It will be combined with other sec. 1231 gains and losses, with a net gain treated as a capital gain and a net loss treated as ordinary income

Election to Treat Cutting as Sale: Tax Reporting

- Make a sec. 631(a) election by checking the YES box on Form T, Part II, line 18a
- Report capital gains (sec. 1231 gain) on Form 4797
- Report ordinary income on Form 1040, Schedule C

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TIMBER DEPLETION

Depletion

- Depletion is a deduction from the timber sale income.
- Depletion is calculated using the timber basis.

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What Is “Basis”?

- For purchased property, your timber basis is the cost you paid for the property
 - *Only* the timber portion, separate from that of the land

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An Example

Ten years ago you bought 40 acres of forestland for \$48,000. You also paid \$1,900 for various fees.

The timber at the time was worth \$29,000.

Q: What's your timber basis? Is it \$29,000?

Yes or No?

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An Example

- ✓ The land itself was worth \$15,000.
- ✓ The \$29,000 timber consisted of:
 - 72 MBF of sawtimber, worth \$19,000, and
 - 560 cords of pulpwood, worth \$10,000.

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Proportion of FMV

Asset	Fair Market Value (FMV)	Proportion of FMV
Land	\$15,000	34%
Sawtimber . . .	\$19,000	43%
Pulpwood	\$10,000	23%
	\$44,000	100%

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Timber and Land Basis

	Proportion of FMV	Original Basis
Land	34%	\$16,966
Sawtimber . . .	43%	\$21,457
Pulpwood	23%	\$11,477
	100.0%	\$49,900

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Timber Depletion

- Determine the depletion unit:
Adjusted Basis ÷ Pre-harvest volume
- *Depletion Unit x Number of Units Harvested*

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Timber Depletion

- You sold 50 MBF out of the 100 MBF sawtimber and 600 cords out of the 1,000 cords pulpwood in your property .

How much is your depletion deduction?

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Timber Depletion

- *Sawtimber:*
 $\$21,457 \div 100 \text{ MBF} \times 50 \text{ MBF} = \$10,728.50$
- *Pulpwood:*
 $\$11,477 \div 1000 \text{ cords} \times 600 \text{ cords} = \$6,886.20$

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What Is “Basis” for Inherited Property?

- It is the fair market value of the timber on the date of the decedent’s death.

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A Question

If I inherited the timber property 10 years ago, does this mean I have to go back 10 years to estimate the fair market value of my timber to set up my timber basis?

Yes or No?

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WHAT COST CAN I DEDUCT?

Deductible Items

- Tools of short useful life or small cost, e.g., axes, handsaws, etc.
- Hired labor
- Fees of consultant and accountant *
- Property taxes

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Deductible Items

- The costs of prescribed burning
- The expenses of fire, insect and disease control and protection; and
- road and firebreak maintenance costs
- Overnight travel

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Schedules for Reporting

- Deduct expenses for an investment property as “miscellaneous itemized deductions” on Form 1040, Schedule A
- Investment expenses are deductible only to the extent that – combined with other miscellaneous itemized deductions – they exceed 2 percent of your Adjusted Gross Income

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Schedules for Reporting

- Deduct business expenses on Form 1040, Schedule C if you materially participating in the business

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FORM T (TIMBER)

What Is Form T (Timber)?

Forest Activities Schedule

This tax form has five parts:

- Acquisition
- Timber Depletion
- Profit or Loss from Land and Timber Sale
- Reforestation and Timber Stand Activities
- Ownership

Who Must File Form T?

- It's prudent to file when you claim depletion deduction and if you sell business timber
- Occasional timber sellers are not required to file
 - Occasional: one or two sales every 3 or 4 years

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PAYMENT RECEIVED ("COST SHARE")

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Cost Share Payment

- Cost share payment must be included in your income unless it qualifies for income exclusion
- The excludable cost share payment must be:
 - From an approved program
 - For capital project (such as reforestation)

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FORM 1099

Form 1099-S Reporting

- **Who Must Issue 1099-S?**
 - (1) the person (including attorney or title company) responsible for closing the transaction,
 - (2) the mortgage lender,
 - (3) the seller's broker,
 - (4) the buyer's broker, or
 - (5) the buyer

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Deadlines

- **Due to the payees: at or after closing but by Feb. 17, 2015 ***
- **Due to the IRS:**
 - March 2, 2015 on paper
 - March 31, 2015 if filing electronically

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Deadline Extensions

- An automatic 30-day extension to furnish statement to the payee:
 - By letter or electronic request to the IRS
- An automatic 30-day extension of time to file 1099 with the IRS:
 - By filing Form 8809 by the due date of the return
 - No signature or explanation is required
 - Must file the extension by the due date of the return

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Penalty

- \$30 per form if correctly file within 30 days after the due date
- \$60 per form if more than 30 days but by August 1
- \$100 per form if after August 1 or not filing
- Max. penalty: \$1.5 million (\$500,000 for small businesses)

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FOREST PLANTING COST DEDUCTION

Reforestation Cost

- **Hired labor**
- **Seedling cost**
- **Site preparation costs**
- **Equipment**
- **Competition control to establish trees**

Reforestation Tax Deduction

- You can deduct outright the first \$10,000 per year of qualifying expenses per qualified property; and
- Deduct (“amortize”) *any* additional amounts over 8 tax years

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Reforestation Example

Total Cost of Reforestation: \$14,000

1. Take \$10,000 deduction (joint return)

2. Amortization:

1) $(\$14,000 - \$10,000) / 14 = \underline{\$286}$ (Year 1)

2) $(\$14,000 - \$10,000) / 7 = \underline{\$571}$ (Years 2-7)

3) $\underline{\$286}$ (Year 8)

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Reforestation by A Trust

- A trust can not take the \$10,000 deduction
- A trust is eligible only for the amortization deduction.

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Tax Forms for Reforestation

- Investors take the deduction on the front of Form 1040, as an adjustment to income
 - Write RFST and the amount on the dots for the adjustments to income line
- Participants in a trade or business take the deduction on:
 - Form 1040, Schedule C for a business or Schedule F for a farm; use the “Other expenses” line

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Tax Forms for Reforestation

- You must specifically elect to amortize reforestation expenses on a timely-filed return (including extensions)
 - ✓ Make the election on Form 4562, Part VI
 - ✓ Form T, if you are required to file

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Tax Forms for Reforestation

- ✓ Attach a statement to your return showing:
 - Unique stand identification number
 - Total acres reforested during the tax year
 - Nature of the reforestation treatment
 - Total qualified expenditures eligible to be amortized or deducted

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TIMBER LOSS

Casualty and Theft Loss

- The amount of your deduction the lesser of the fair market value loss or the adjusted basis of your timber
- If returns from a salvage harvest, court award, or insurance claim, exceed your basis, you will have a *gain*




Federal Income Tax on Timber A Quick Guide for Woodland Owners


Fourth Edition
2012

Dr. Linda Wang



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Questions?

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- Complete the satisfaction survey
- Take and pass the short quiz
- Complete the Continuing Education Unit Request Form (CEU Form)
- Certify that you have participated in the webinar in its entirety