

Branching Out: Maryland's Forest Stewardship Educator

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Editors: Jonathan Kays, Pam Townsend

Contributors: Anita Schipper Caplan, Arlyn Perkey, Robert Tjaden

We welcome your e-mail: jkays@umd.edu. Branching Out is published quarterly and distributed to 8,300 woodland owners, resource professionals, and others interested in forest stewardship. Calendar and news items are welcome. The sponsoring agencies' programs are open to all citizens without regard to race, color, sex, age, religion, national origin, or disability.

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Timber Sales: A Taxing Business?

Many forest owners find timber tax issues complex and confusing as most sell timber only once or twice during their lives. Knowing how to keep records and structure your sale in order to minimize your taxes can save dollars. This article is only a primer and expert tax advice should always be sought for your own situation.

Establish Your Basis

Woodland owners often overlook their basis deduction when selling timber. The basis refers to the owner's financial investment in the trees being sold. The original basis is the value of the trees only when the property was acquired, separate from the value of the land. Your basis can be determined in one of three ways: 1) purchase price; 2) inherited (your basis is the fair market value on the date of the death of the donor; this is called "stepped up basis."); or 3) gift (your basis is the original owner's basis plus the gift tax).

The basis for some forestland that was planted and managed is the establishment cost. The original basis of forestland can be increased based on improvements made.

A problem occurs when the landowner doesn't know the basis of the trees, because when most land changes hands, no allocation of the purchase price is made between land and timber. The basis of the timber must be established by a professional forester or appraiser. This is best done when the land is acquired but may also be done at a later date. The adjusted basis of the trees sold (on a per unit basis) can be deducted from the sale proceeds, thus lowering the amount of income subject to income tax.

Capital Gains vs. Ordinary Income

Make sure your income from a timber sale qualifies as capital gains and not ordinary income. Also, own the property at least one-year before harvesting to receive treatment as a long-term capital gain. The difference in total taxes can be substantial. The maximum federal income tax rate on non-corporate long-term capital gains (long-term means asset has been owned more than one year) is 28 percent. In contrast, income from timber held as a short-term capital gain will be treated as ordinary income, with a maximum possible rate of 39.6 percent. Most timber sales could easily put you into the higher tax

bracket.

The self-employment tax is another big difference between capital gains and ordinary income. Ordinary income may be subject to the self-employment tax (15.6 percent) if the owner's woodland is a business held in sole proprietorship or partnership form. In contrast, short- or long-term capital gains are not subject to this tax. If retired, capital gains do not count in reducing social security payments.

When considering a large timber harvest, it may be beneficial to structure the sale over two years or more to keep your income in a lower tax bracket. This is called an installment sale and should be detailed in your logging

Sale Expenses, Record Keeping and Reporting

Costs directly related to the sale of timber include, but are not limited to advertising, consultant fees, travel, and tree marking. Such expenditures can be deducted from the sale amount when computing gain or loss.

Keeping good records is essential and the shoe box method can lead to mistakes and confusion. It is best to record any receipts, expenditures, and time spent working on the property in an accounting journal. Good records are indispensable because the IRS puts the burden of proof on you to supply them if you're audited.

To report a timber sale on your income taxes, use the Federal Tax Form T, the Forest Industries Schedule. Schedules C and F of this form are used to record a timber sale if you are a small woodlot owner, whose only timber-related activity during the year was an isolated sale of timber.

Listed below and on page 4 of this publication are some good tax resources. *The Forest Owner's Guide to the Federal Income Tax* (Agric. Hndbk. 708) supersedes the older version (#681), updating changes made since the 1987 Revenue Act and expanding its contents. It costs \$10 and can help educate your accountant. To charge to MasterCard, call the U.S. Government Printing Office at (202) 512-1800. Send a check or money order to: Superintendent of Documents, PO Box 371954, Pittsburgh, PA, 15250-7954.

Golden Hard Hat Awarded

The American Tree Farm System has awarded Mike Kay, Frederick County Forest Service, its

Coveted Golden Hard Hat Award for certifying 100 Tree Farms. This is the first time a Maryland forester has received this award. More than 1,400 Tree Farms are certified in Maryland and collectively they account for 13 percent of Maryland's private woodlands.

The Tree Farm program is sponsored nationwide by private forest industries to encourage and recognize forest owners who manage their properties for forest products as well as for wildlife, watershed protection, recreation, and aesthetics. To become a Tree Farm, a forest management

plan is prepared by a forester and the property is inspected five years later to make sure the plan was implemented. If so, the property becomes a Certified Tree Farm and owners are given a sign to post proudly on their property.

Mike enjoys making on-site inspections because he "gets to know the landowners, see their needs and acknowledge their accomplishments." He feels the Tree Farm certification is important as it recognizes the landowner and encourages future involvement. If you are interested in the program, contact a state or private forester.

Viewing The Forest With Ease

Quadrangle maps produced-by the U.S. Geological Survey (USGS) provide woodland owners a two-dimensional look at features associated with their property: roads, streams, buildings, wetlands, houses, differences in elevation, and more. However, to truly appreciate different forest types and wildlife habitats on your property and the properties that surround it, you need aerial photos.

Aerial photos are a snapshot at a particular point in time. By viewing photos taken 10, 20, or 30 years apart, you can see how abandoned fields turn into forests, harvested areas regenerate, land is developed, and other changes occur in the landscape. A large majority of Maryland's forests are agricultural lands that have reverted back to forest cover.

When enhancing your property for wildlife, it is important to consider the features of neighboring properties which may provide habitat not found on your land. Wildlife habitat includes food, cover and water within the range of a species. Lack of any one of these elements throughout the year will limit wildlife populations.

Aerial photos will show you what habitat is available in the area bordering your property and aid you in planning your forest management activities to attract the types of species you desire. For example, if conifer trees for winter cover are not available in your area, you may decide to plant part of an old field with conifers to help attract wildlife to your property in the winter.

If you have a choice of photos, select those taken in the winter. With no leaves to hide the landscape, features such as the type of forest (hardwood or conifer), tree size, streams, ponds, wetlands, and other habitat features are more visible.

Forests are truly dynamic and do change regardless of human activity. Aerial photos are the basic tool used by natural resource professionals to develop forest management plans. They give you a real appreciation of why forests are truly a renewable natural resource.

Ordering Your Photos

Photos taken prior to 1950 are available from the National Archives. Those taken after 1950 can be obtained from the USDA-FSA (Farm Service Agency, previously known as ASCS). The addresses, phone numbers, and fax numbers of both agencies are listed below.

County FSA offices generally have current and older photos available to view. Your local FSA office (it may still be listed as ASCS) is listed in the blue pages of your phone book in the U.S. Government section.

When you decide which photo you want to order, record the dates, roll numbers and exposure numbers on form FSA-441, which is available at the county office. Two photo sizes are commonly used: a 10" x 10" black-and-white photo costs \$3 for older photos and \$6 for photos taken after 1990. However, the scale of this photo is too small to show much detail (1 inch = 3,333 feet). A better choice is a 24" X 24"

photo (1 inch = equals 660 feet) which costs \$14 for older photos and \$20 for shots taken after 1990. (Another option is to ask to borrow FSA photos from the local office and have them photocopied).

If you are unable to find the identifying number of the photos you want, send a photocopy of the USGS quadrangle map that has the property outlined. Make sure the longitude and latitude are visible and include the name of the map quadrangle, county, and state.

To obtain an older photo from the National Archives, call, mail, or fax them a map. If photos are available they will cost \$14 - \$20 each, and will be provided by an independent provider.

Post-1950 Photos: USDA-FSA, Aerial Photography Field Office, Customer Services, 2222 West 2300 South, P.O. Box 30010, Salt Lake City, Utah 84130-0010, Phone: (801) 975-3503, Fax (801) 975-3532.

Pre-1950 Photos: National Archives, Cartographic & Architectural Branch, 8601 Adelphi Rd., College Park, MD 20740-6001, Phone: (301) 713-7040, Fax: (301) 713-7488.

Take Note . . .

A Homeowner's Guide to Northeastern Bats and Bat Problems: This publication discusses characteristics of bats, how to attract them, bat box plans, and bat-proofing your home. Available free from: Publication Distribution Center, Penn State University, 112 Agric. Admin. Bldg., University Park, PA, 16802-2602. (814) 865-6713.

Enhancing Your Backyard Habitat for Wildlife: This 26-page, color publication explains how to develop a plan to provide backyard habitat. Included are lists of beneficial and invasive exotic plants, nest structures and how to guard them from predators. \$5, Contact: Conn. Dept. of Environ. Prot. Wildlife Division, PO Box 1550, Burlington, CT, 06013-1550. (203) 675-8130.

Both of the publications below are available free from your local Cooperative Extension Service office.

- **Keeping it in the Family: Estate Planning and Timber Tax Resource List for Woodland Owners. (FOR 1).** List of resources and ordering information.
- **Tax Tips for Forest Landowners for the 1995 Tax Year.** USDA Forest Service - Cooperative Forestry Mgt. Bull. R8MB74, Dec.'95. Update on cost-share payments, capital gains, casualty losses, etc.

Black Walnut.- The History, Use, and Unrealized Potential of a Unique American Renewable Natural Resource: Written by Bob Chenoweth, this hardcover, 300-page book, is interesting, informative and in-depth. \$28.95. Contact: Sagamore Publishing, PO Box 647, Champaign, IL. 61824-0647 (800) 327-5557.

Project Learning Tree (PLT) is sponsored by educational organizations. PLT workshops are offered throughout the state and are free to teachers, youth organizations, and the general public. The six-hour workshop focuses on increasing youth awareness by stimulating critical and creative thinking about environmental issues related to forests. The activity guide is designed for use in the classroom or home and offers curriculum formats that incorporates many subjects and can be used at many grade levels. For more information on a workshop near you, contact Dave Rinecke, Maryland Forest Service, 580 Taylor Ave., Annapolis, MD 21401 (410) 543-1950.

