



## Timber Taxes Cost Basis (Part I)

In the last article, we described the elements of a timber sale contract. Assuming completion of a successful sale, you received income that is probably subject to federal income tax. Income from the sale of timber is subject to special provisions in the IRS code and can receive favorable treatment resulting in limited tax liability for the timberland owner. However, some preparation prior to actually selling timber is usually necessary to qualify for these benefits.

Soon after obtaining ownership is the best time to begin this preparation. The first step is to determine the value of the asset (timber) you acquired. If you acquired the timber by inheritance, a current value is established as of the date of death of the person from whom you received it. If you purchased land with timber on it, the actual market value of the timber should be determined independent of the value of the land plus improvements such as structures, fences, roads, ponds, etc. In either case, a *timber inventory* may be necessary to determine the amount of timber present (board foot volume), size distribution (diameter), species, and the quality (grade) of the trees. This information is necessary to complete *IRS Form T* which becomes part of your permanent tax records. A timber inventory should be completed by a qualified forester. A list of consulting foresters is available at the website [www.missouriforesters.com](http://www.missouriforesters.com) or from offices of the Mo. Dept. of Conservation.

A word of caution is appropriate. A “farm appraisal” is rarely suitable for establishing timber value and may, in fact, significantly undervalue it. It is recommended that a timber inventory & appraisal be completed in conjunction with a farm appraisal and combined to assure appropriate tax benefits in the future.

Results of the timber inventory tell you *what* you acquired but must be combined with local price information applicable to the size, species and quality of trees to provide an estimate of the timber value. The value estimate is also recorded on *Form T* in your tax records. A reference of timber values is published quarterly by the Mo. Dept. of Conservation titled Missouri

Timber Price Trends. Copies are available through public libraries, MDC offices, or online at [www.mdc.mo.gov](http://www.mdc.mo.gov). Your local MDC or consulting forester is also a good source of local stumpage prices.

Timber is considered a *capital asset* and as such, owners of these assets are allowed to recover the total expenses involved in their acquisition. This total is known as *timber cost basis*. Recovery is achieved by deducting the appropriate *depletion allowance* from the amount received for the standing timber. Taxes are paid only on the difference which is known as a *capital gain*. Capital gains are taxed at lower rates than ordinary gains for even further savings for the landowner. In addition, income qualified as capital gains is not subject to *self employment tax* which saves an additional 15.3% of the total amount received for the timber.

Resulting tax savings are usually much greater than the cost of a timber inventory/appraisal and the savings continue for subsequent timber sales. Our next article in this series will explore specific details and information related to special timber tax laws. All of this information and more is available at the following web site [www.timbertax.org](http://www.timbertax.org).

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