



Timber and Taxes

William C. Siegel, J.D.

Forest Stewardship and the Federal Income Tax

Most woodland owners realize multiple benefits from owning their forest land. Some people may have a special interest in providing wildlife habitat, conserving soil and water, protecting endangered plants and animals, or other activities not related to the production of income. Generally in these cases, most income expectations are limited to an increase in market value of the property, that would be realized in the event it is sold.

Forest stewardship refers to the care and management of woodland in the best sense of conservation and wise use. The income tax law may be of benefit in some of these efforts. However, to the extent that nonmarket activities are involved, the tax law will apply little or not at all.

Tax Law Applicable To Income Production

The income tax law is keyed primarily to the production of income. Expenses incurred for an activity carried out to produce income as either a business, or as an investment, can generally be recovered (deducted) as discussed in previous "Timber and Taxes" articles. A critical consideration is that the expense incurred in connection with a particular activity be directly related to its potential to produce income. Even though a woodland owner may expect to sell timber sometime during his (her) life, timber production may not be the primary motivating factor at the present time.

As an example, in the recent Holmes case, the Tax Court held that a full-time insurance sales manager and his wife's activities on land adjacent to their home weren't engaged in for profit. Raising fish and planting garden crops overshadowed the possibility of harvesting timber sometime in the future.

Certain woodland owners may have a special interest in wildlife and manage their property to attract certain species. In some regions of the country, wildlife expenditures may be related to the production of income because the land is leased for hunting. These costs, for example, would in-



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clude those incurred for planting food plots and shrubs for food and cover, and maintaining a timber species and stocking mix to favor certain wildlife.

On the other hand, money spent for these purposes may be only for increasing enjoyment of the property. To deduct management costs on your tax return, the woodland must be managed so that the activities in question are directly related to eventually making a profit from the property.

In many cases, it is possible to carry out a wildlife habitat management program as part of the timber management operations and receive income from both activities. If the wildlife management expenses are incidental to the timber management activities, they could be treated as timber management costs. If, however, wildlife activities dominate the management program and you don't receive any income related to wildlife, the expenses probably won't qualify as deductions.

Many of the best opportunities to promote stewardship on your woodland are associated with forest estate

planning. These are outlined in the publication *Estate Planning for Forest Landowners: What Will Become of Your Timberland?*—General Technical Report SO97, USDA Forest Service, Southern Research Station, New Orleans, Louisiana, authored by Harry L. Haney, Jr. and William C. Siegel.

Conservation Easements

If a woodland owner is highly motivated to engage in activities to improve the ecological value of the property, it may be in his (her) best interest to sell, donate or otherwise transfer all or part of the ownership interest to an organization specializing in the management of forest and other lands for conservation purposes. It is not necessary that there be an outright transfer of all ownership interests. Less than the entire interest in forest land can be legally transferred.

For example, you can transfer a restriction on the use of property for purposes other than forest land such as commercial or industrial development. Such a restriction can be transferred

with the right retained to live on the land and continue to produce timber. These types of transactions (called creating a conservation easement) provide a way for the present owner to control the use of the land both during both and after his (her) lifetime.

If the easement is sold rather than donated, it would provide some income from the development rights. If the easement is donated in perpetuity to a qualifying organization, the transfer may qualify for a charitable deduction on your income tax return.

Charitable Deduction

The criteria necessary to qualify for a charitable deduction need to be carefully evaluated. Legal counsel should be retained to facilitate the process. Three basic criteria must be met.

Qualified Organization

The donation must be made to one of the following qualified organizations:

1. a unit of local, state or federal government.
2. a publicly supported charitable, religious, scientific or educational organization, or
3. an organization that is controlled by, and operated for the exclusive

benefit of, a governmental unit or a publicly supported charity.

Conservation Purpose

The donation must be made for only one of the following purposes:

1. preservation of land areas for outdoor recreation by, or for the education of, the general public.
2. protection of a relatively natural habitat for fish, wildlife, or plants, or a similar ecosystem.
3. preservation of open space, including farmland and forest land. The preservation must yield a significant public benefit. It must be either for the scenic enjoyment of the general public, or under a clearly defined federal, state or local governmental conservation policy.
4. preservation of a historically important land area or a certified historic structure.

Qualified Real Property Interest

All of the following interests in real property qualify. Forest land and timber are real property.

1. the entire interest in real estate other than a mineral interest.
2. a remainder interest, that is the in-

terest after an interest held for some designated time period, or a time period fixed by an identifiable event, such as a person's death.

3. a restriction on how the property may be used if the restriction is perpetual.

Valuation of the Donation

The value of a donation of a conservation easement generally is equal to the value of the entire property before the donation minus its value after the donation. The best evidence of this difference in value, if it exists, is reference to sales of similar properties in the same area that were bought and sold, some without any restrictions, and some with restrictions similar to those associated with the donation in question.

Example

You own 400 acres of forestland. Similar land in the same area has a fair market value of \$1,000 per acre. However, land in the general area that is restricted solely to forestry uses under the state's open-space program has a fair market value of \$500 per acre. The state, which wants to preserve green space in the vicinity of your woodland and prevent further development, is

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Tax Procedure

Because of the need for accuracy, a professional written appraisal should be used to determine the value of the donation. This is required for deductions of donated property if the deduction is more than \$5,000. A copy of the appraisal must be attached to the tax return. Generally, a deduction can be taken on the tax return for the year of the donation up to 30 percent of the adjusted gross income reported on the return. Any excess not able to be deducted on that return can be carried forward and deducted as necessary over the next five years, subject to the same 30 percent rule each year.

Conclusion

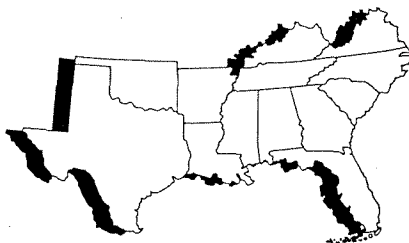
Many woodland owners utilize their property for purposes other than commercial timber production even if they do make occasional timber sales. The expenses associated with the other uses are generally not deductible. Granting a conservation easement and taking the associated income tax deduction is one method of recovering some of these otherwise non-recoverable costs.

It must be remembered, however, that if the value of an easement is to be deductible, the easement must be granted in perpetuity which precludes any future development of the property forever that is not compatible with its use as woodland.

William C. Siegel is an attorney and consultant in private practice specializing in timber tax law and forestry estate planning. He is retired from the US Forest Service where he served as Project Leader for Forest Resource Law and Economics Research with the Southern Forest Experiment Station, where he still serves as a volunteer. He provides this column as a regular service to *National Woodlands* readers. Mr. Siegel welcomes comments and questions. They may be directed to him at: 9110 Hermitage Place, River Ridge, LA 70123; tel. (504) 737-0583.



News from the Regions



SOUTH

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Landowner Education Programs Reach New Levels in the South

Two unique programs in the South are utilizing new technologies and heightened interest in forestland management to reach hundreds of landowners. These programs, the Forest Masters Program in Alabama and the Master Tree Farmer 2000 Program, Southwide, are providing opportunities for landowners and managers to better understand our forests and how they can be managed better.

In Alabama, the Forest Masters Program has signed up more than 200 landowners. This program is designed to motivate and recognize Alabama forest landowners and stakeholders for educational and service efforts.

Focus areas are identified that encompass a range of forest-related topics. Educational programs, including a technical presentation, are evaluated and "credits" assigned within a focus area to each presentation or portion of a field trip. This procedure is similar to continuing education utilized by many professions.

Landowners and others interested in participating in the program must make an application. A unique aspect of the Program is the Bronze, Silver and Gold status that landowners can attain following increased levels of participation and activity.

Forest Masters is a recognition program only, in that no exams are administered to evaluate competency. Examples of opportunities that can be utilized to fulfill the service requirement of the Silver and Gold levels of Forest Masters include (but are not limited to):

- Mentoring other forest landowners to help them better manage their forest;
- Participation in Adopt-A-School or similar programs;
- Participation in FAWN program;
- Serving as an officer in a forest landowner organization;
- Hosting a forest landowner field trip; etc.

For more information about this program visit the website at www.pfmt.org or contact Dr. Glenn Glover at glover@forestry.auburn.edu.

Master Tree Farmer 2000 Broadcast Program Complete

The Master Tree Farmer 2000 Program recently completed its seven-week live broadcast from Clemson University in South Carolina. More than 20 speakers delivered information on a variety of topics from pine and hardwood management, financial and taxation aspects, wildlife management, timber marketing and harvesting and forestry services for the landowner.

Sixty-two sites in ten states hosted close to 1,400 landowners and 200 county agents and foresters. These landowners completed 21 hours of classroom activity. Some sites and states will host field days.

The program was received very well and plans are being made to continue this effort in future years. For more information about the broadcast, or to learn how to obtain video tapes and other materials from the course, contact the website at www.mtf2000.net or Dr. George Kessler (864) 656-4836 email: gksslr@clemson.edu.

Forests at the Interface: Course for Nat. Res. Professionals

The Wildland-Urban Interface (WUI), the area where urban lands meet and interact with rural lands, presents many challenges and concerns for natural resource managers as well as its residents. Issues range from increased incidence of wildfires to economic development to forest management and conservation.

Natural resource managers working at the interface are directly involved with land management, but can also be



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Front Cover: Last spring the National Woodland Owners Association again teamed up with the America the Beautiful Fund (we did it once before in 1993) to distribute an amazing number of 25,000 daffodil bulbs nationwide. Our objective and agreement with the Fund was to make America's managed private woodland more diverse and attractive in the spring. The sun-loving bulbs are especially appropriate for restored landings and logging trails, even stumps, as in this case.

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