Forest Taxation Update

Recent Federal Income Tax Provisions
Affecting Nonindustrial Woodland Owners

All Forest Owners

- Bonus depreciation
  - ✓ESA: Economic Stimulus Act of 2008 (PL 110-185)
  - ✓ARRA: American Recovery & Reinvestment Act of 2009 (PL 111-5)
- Treasury Decision 9450
- Revenue Ruling 2009-23

Bonus Depreciation

- Depreciation allows taxpayers to recover their investment in income-producing property through annual deductions
  - ✓ To qualify, the property must have a useful life longer than 1 year and be something that wears out, deteriorates, or becomes obsolete over time

Bonus Depreciation

- ✓ All taxpayers can take depreciation deduction for property they purchase for the production of income, whether as an investment or part of a trade or business

Bonus Depreciation

- ESA permitted taxpayers to take a first-year depreciation deduction equal to 50 percent of the adjusted basis of qualifying property
  - ✓ Limited to property purchased and placed in service after Dec. 31, 2007, and before Jan. 1, 2009 (Jan. 1, 2010, for certain property with a long production period)
- ARRA extended provision an additional year

Bonus Depreciation

- To qualify, property must be:
  - ✓Tangible personal property depreciated under MACRS with a recovery period of less than 20 years, water utility property, off-the-shelf computer software, or qualified leasehold improvement property
  - ✓New property – not used – with the taxpayer the original purchaser

Bonus Depreciation

- Cannot be used for:
  - ✓ Property purchased under a binding agreement in place prior to Jan. 1, 2008,
  - ✓ Property purchased from a related person,
  - ✓ Self-constructed property for which construction began prior to …

Bonus Depreciation

… Jan. 1, 2008, or

- ✓ Ineligible property, such as property owned by a controlled foreign corporation

Bonus Depreciation

- Calculate your bonus depreciation AFTER you take any section 179 deduction
  - ✓It is not affected by short tax years
  - ✓It is allowed for both regular and AMT purposes
  - ✓Many states have decoupled from bonus depreciation

Treasury Decision 9450

- Requires purchasers of timber in a lump-sum sale to file a Form 1099-S, as a real estate transaction
  - ✓ Effective for timber harvested after May 28, 2009
  - ✓ Now every sale or disposal of standing timber requires a Form 1099, whether it is pay-as-cut or lump-sum

Revenue Ruling 2009-23

- Approves cost-share payments under the Forest Health Protection Program (FHPP) for exclusion from gross income
  - ✓ Program administered by US Forest Service to prevent, retard, control or suppress infestations by gypsy moth, Southern Pine Beetle, spruce budworm, other major insect pests

Material Participants

- Expanded Section 179 Deduction
  - ✓SBWOTA: Small Business and Work Opportunity Tax Act of 2007 (PL 110-28)
  - ✓ESA
  - ✓ARRA
- Family Business Tax Provision
  - ✓SBWOTA

Expanded Section 179 Deduction

- IRC section 179 permits material participants in a trade or business to deduct outright at least part of the cost of qualifying property acquired for the business, instead of having to depreciate it
  - ✓ In general, qualifying property is depreciable tangible personal property, defined to include single-purpose …

Expanded Section 179 Deduction

… agricultural or horticultural structures, but not most other buildings or components of buildings

- ✓ The deduction is not available to passive participants in a trade or business, investors, trusts, or estates

Expanded Section 179 Deduction

- SBWOTA raised maximum amount of the section 179 deduction to $125,000, indexed for inflation, through 2010
  - ✓ Also increased phase-out limit to $500,000, indexed for inflation, and
  - ✓ Extended section 179 deduction provisions for GO Zone businesses through 2008

Expanded Section 179 Deduction

- ESA increased maximum amount of the deduction to $250,000 and the phase-out limit to $800,000
  - ✓ Neither amount was indexed for inflation and both applied only to tax years beginning in 2008

Expanded Section 179 Deduction

- ARRA extended both provisions an additional year
  - ✓ For tax years beginning after 2009, will return to SBWOTA provisions

Family Business Tax Provision

- A husband and wife who both qualify as material participants in an unincorporated business ordinarily would be treated as a partnership for tax purposes
  - ✓ Under a provision of SBWOTA spouses who conduct a qualified joint venture and who file a joint Federal income tax return can elect to be treated as two sole proprietorships

Family Business Tax Provision

- A qualified joint venture is any joint activity involving the conduct of a trade or business, if:
  - ✓ The husband and wife are the only members of the joint venture
  - ✓ Each qualifies in their own right as a material participant in the trade or business according to the passive loss rules, and
  - ✓ Both elect for the provision to apply

Family Business Tax Provision

- If the spouses make the election, then:
  - ✓All items of income, gain, loss, deduction, and credit are divided between them according their interest in the venture
  - ✓Each files their own business and self-employment tax forms, and
  - ✓Each receives individual credit for paying Social Security and Medicare taxes