

What Are Involuntary Conversions of Timberland?

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If your standing timber is destroyed or stolen, or if your forestland is condemned for public use, you may be entitled to take a deduction on your income tax return. The above timber losses are called **involuntary conversions** (3). There are two types: **non-casualty losses** and **casualty losses**. Anyone who owns in timberland should be familiar with the basics of all involuntary conversions and aware of their legal and tax implications.

A **non-casualty** or business loss can occur from drought, insect or disease infestation, property condemnation, or timber theft. Under certain circumstances these losses are deductible from taxes by landowners who hold timber for sale as a trade or business or for landowners who hold the timber for profit but not in a trade or business. To be deductible the loss must result from an abnormal event that is unusual and unexpected but not necessarily sudden. A tax disadvantage may exist since non-casualty losses are deducted from capital gains that are normally taxed at lower rates than ordinary income (2).

One example of a non-casualty loss is the abnormal death of seedlings due to drought. However, the deduction is limited to the cost basis of the seedlings on the acreage that must be replanted. Financial loss from mortality due to insects may reach abnormal levels due to unusual and filled_unexpected infestations of insects such as the southern pine bark beetle and may be deductible. Theft losses are deducted in the year the theft

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Is discovered not when the theft occurred. A condemnation is the taking of private property for public use without consent of the owner but with award and payment of just compensation. The tax consequences are the same whether you sell the property under the threat of condemnation or the property is actually condemned. Use IRS Form 4797 – Sales of Business Property for reporting. The property must have been held for more than one year (2). Normal losses like tree death caused by competition, routine disease and insect infestations, or low rainfall are not deductible.

Timber **casualty losses** generally are caused by a sudden, unexpected, and unusual event. Examples are listed below:

- Hurricanes
- Tornadoes
- Wildfires
- Floods
- Wind damage
- Ice storms
- Shade tree losses (caused by pine beetle attack)
- Others like plane crashes, explosions, earthquakes and volcanic eruptions

Unlike for non-casualty losses, hobby owners also may claim a casualty loss. Hobby owners hold timber for personal use and not for profit. They report their losses on IRS Form 4684 Section A (1). Deductions are made from ordinary income not capital gains.

Subsequent articles in this series casualty losses address topics about including in your management plans the potential for losses plus the issue of establishing and maintaining an adjusted basis (investment value) for you timber. Loss appraisal and loss documentation requirements, salvage obligations and insurance considerations are covered as well.

Citations:

1. Gaddis, D. A. and S. G. Dicke. 2010. Frequently asked questions about timber casualty losses. Publication 2619. Mississippi State University, Extension Service. <http://msucares.com/pubs/publications/p2619.html>.
2. National Timber Tax Website. 2011. Section 1033 – Involuntary Conversions. <http://www.timbertax.org/research/irc/sub/sections/sec1033/>.
3. Siegel, W. C. 2001. Special involuntary conversion situation involving timberland. National Woodland, Vol 24(3):21-23 or http://www.srs.fs.usda.gov/pubs/ja/ja_siegel011.pdf.

Have Questions? Contact Ben Jackson at bjack@uga.edu or 706-542-9051

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