Federal Tax Treatment of Private Forest Land

A Position Statement of the Society of American Foresters

Initially adopted by the Society on April 21, 1986, subsequently revised and extended by the Council on December16, 1996, June 9, 2001, June 8, 2002, October 6, 2006 and October 31, 2011. It shall expire October 31, 2016 unless, after subsequent review, Council decides otherwise.

Position

The Society of American Foresters (SAF) believes federal tax policies based on equality and certainty are required to encourage the nation's private forest landowners to make sustained, long-term capital investments in forest management. Rather than distorting market forces, taxation should place private forest landowners on near-equal playing fields with other capital ventures, including agriculture, as this will encourage practices that retain forests as working, contributing assets to the nation. Tax policies need to recognize the unique and long-term characteristics associated with timber and forest management investments, including the intergeneration transfer of forest assets, to alleviate uncertainty in tax treatment. Ultimately, the nation should strive for sustainable forests, where the economic, environmental, and social values provided from forests are in balance. Sound tax policy will ensure the sustained environmental and social benefits within a predictable economic framework.

Issue

A shift in forest management has occurred over the past few decades as a result of reduced federal and state funding, combined with intervening litigation on federal forestlands. This has resulted in private forest landowners taking a leadership role in the practice of sustainable forestry, conservation, and best management practices. Private forests provide essential watershed protection, carbon sequestration, wildlife habitat, and many recreational opportunities, as well as the major share of forest products produced in the United States. At the same time, private forests are subject to a variety of pressures to convert to nonforestry uses. Federal tax policy can play an important role in counteracting pressures that reduce private forests' ability to provide these wide-ranging benefits. Well-crafted tax policy can further the public's interest in promoting adequate investment in, and sustainable management of, the nation's private forests.

Background

The Role of the Private Forest Landowner:

Private forestry investments significantly add to the ecological, economic, and social prosperity of the nation. Approximately 423 million acres (56%) of forestland in the United States is owned by private individuals, corporate entities, or other private groups. These lands accounted for 92 percent of the volume of timber harvested in 2006 (Smith et al. 2009). The nation's private forests represent an important pillar of job creation in rural areas where each 1,000 acres of privately owned forest is responsible for the creation of eight jobs. For example, Forest2Market's (2009) 29-state study found that more than 2.6 million people were employed either directly or indirectly in forest-related sectors. In addition to wood fiber, the sustained management of private forests provides wildlife habitat, recreation opportunities, and numerous environmental amenities such as clean water, carbon sequestration, and biodiversity protection.

Private forests face tremendous pressures from urban expansion, highway construction, utility rights-of-way, and the aforementioned reliance of society as the primary source of wood fiber. Increasing development pressure on private forests, combined with a lack of forest management incentives in the federal tax system, discourages private forest owners from managing for long-term sustainability and environmental quality (see SAF's Position Statement on Loss of Forest Land: http://www.safnet.org/policyandpress/psst/loss_of_forest_land.cfm).

The Abbreviated Tax Treatment of Private Forest Lands:

Three types of taxes affect private forest landowners: property, income, and estate taxes (Kimbell et al. 2009). The federal government levies income and estate taxes, while state and local municipal governments may collect all three. In the federal income tax system, forest landowners demonstrating material participation in management activities generally qualify for long-term capital gains treatment on profits generated from the sale of timber (Haney et al. 2001). Federal tax provisions take into account the long-term nature of forest investments: the treatment of reforestation which allows $10,000 to be deducted in the first year for qualified expenditures, and the amortization of additional expenses for 84 months. Additionally, timber depletion deductions allow forestland owners to recover all or a portion of their investment costs upon liquidation. Deductions also allow for casualty losses, timber theft, public condemnation, and other involuntary conversions (Haney et al. 2001).

Studies have demonstrated that the federal estate tax can force heirs to suboptimize their assets, in effect distorting market forces, by either harvesting timber prematurely or selling the timberland outright to pay the levied tax. For example, Greene et al. (2006) estimated that landowners harvest 2.4 million acres of forestland each year to pay the federal estate tax, which causes some forest landowners to fragment and parcelize their lands. While the estate tax has approached 55 percent (with exemption values), the current temporary tax package (passed by the 111th Congress) carries a 35 percent tax on estates worth more than $5 million ($10 million per couple) until December 31, 2012 when it returns to higher percentages and lower exemption levels.

Many aspects of private forestry infrastructure, including manufacturing plants, in-woods equipment investments, and sustained forest management have been encouraged by federal tax policies, such as tax rates more favorable than ordinary income rates, accelerated depreciation schedules, deductions, and tax credits (USFS 2011). Employing the functionality of the Federal tax code is preferable to subsidy programs since it provides for more equitable participation of private forest landowners.

The Unique Nature of Private Forestland Investments:
Investments in private forest management are unique in many respects. Typically, they: must be held for a long period of time (i.e., decades), are subject to substantial physical and economic risk, have a low degree of liquidity, and sometimes yield rates of return that are low relative to other capital investment opportunities. These investment characteristics can have serious adverse consequences for the nation's private forests where a significant investment might not yield an offsetting return for 20 to 120 years. This requires forest landowners to maintain recordkeeping systems over the life of timber stands.

Collectively, these factors discourage many forest owners from investing in forest management, and contribute to decreased timber production, liquidation of timber inventories, reduced interest in forest regeneration, and discrimination against forest ownership and timber investments in favor of nontimber businesses. The associated adverse impacts are substantial with respect to ensuring a sustained stream of forest products and environmental services into the future from the nation's private forests.

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