Biography

Garvey Jackson, CPA

- 1976 graduate of the University of Houston
- Practicing accounting and tax for 41 years
- Partner at Axley & Rode, LLP in Livingston TX
Tax Reform on the Horizon

- Stars aligning
  - Currently there is a Republican controlled presidency, house, senate. Along with this, is a speaker of the house and chairman of the House Ways and Means Committee passionate about tax reform.
  - This has not happened since 1986 which is arguably the most major tax reform act to ever take place.
Goals:

- Simplify tax code and filing
  - Reduce the individual tax bracket from 7 tax rates to 3
  - Eliminate additional taxes such as the alternative minimum tax
  - Simplify tax forms
  - Remove biased personal expenses and ultimately increase the standard deduction for everyone
- Reduce tax rates & burdens for individuals
  - Max tax rate from 39.6% to 33% (high concern)
  - Reduction in capital gains rates (low concern)
  - Repeal & replace Obamacare
Trump Proposed Reform (continued)

- Reduce tax rates for corporations & small businesses
  - Trying to pull corporations back onto domestic soil
  - Up front expensing for all capital expenditures
  - Move corporate rates from 35% to 15-20%
  - Re-patriation Holiday - One time 10% tax for offshore corporate earnings
- Eliminate estate taxation – “death tax”
  - A possible removal of the step-up in basis as exchange for the loss in revenue
Planning for Reform

- Defer recognition of income for possible future lower rates
- Takes losses now to use higher rate
- Plan for a more favorable tax in the future
- Defer estate tax planning techniques if possible
Timber Ownership:
Three distinct tax treatments

1. Property held for personal use
2. Ordinary Business
3. Timber Farm (Most Common)
Personal Property

- Generally small tracts purchased for personal enjoyment (home sites & getaways with small acreage).
- Disadvantageous for tax treatment – Little to no deductions.
- Major expenses added in with cost of real estate.
Ordinary Business

- Big business – lots of land with often recurring cutting and selling.
- Advanced financial and tax reporting – often required to use form T.
- Does not apply to majority of taxpayers.
Timber Farm

- Small to large tracts held long-term.
- Expenses are directly used and not limited as incurred if non-passive.
- Only occasional timber sales.
- Capital Gains rate treatment - typically 15%.
- Operations reported on Farm schedule – Sch F.
- Must materially participate to not be considered passive.
- Generally not required to file form T.
Annual Expenses

- Out of pocket directly related to the farm. Examples:
  - Supplies
  - Fuel / Automobile expenses
  - Legal & professional – Attorney, CPA, Foresters
  - Property taxes & insurance
  - Reforestation* / Planting / Fertilizer
  - Continuing education

- *Reforestation costs allowed up to $10k in single year with remainder spread out over 7 years.

- Depreciation of equipment.
Capital Purchases (equipment)

- **Bonus Depreciation – New Assets**
  - 2016-2017 – 50%
  - 2018 – 40%
  - 2019 & forward – 30%
- **Section 179 deduction - $500,000 on new or used. Phased out for annual accumulated purchases of $2 million or more.**
- **You must have “earned income” to use this 179 deduction.**
- **Regular depreciation – cost spread out over time.**
For most who have held their timber investment over a year, the tax is calculated on the gain on the sale.

This is the difference between what you received and your basis.

<table>
<thead>
<tr>
<th>Sales Price</th>
<th>$150,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Basis</td>
<td>($ 85,000)</td>
</tr>
<tr>
<td>Gain</td>
<td>$ 65,000</td>
</tr>
<tr>
<td>Tax Rate</td>
<td>15%*</td>
</tr>
<tr>
<td>Tax</td>
<td>$ 9,750</td>
</tr>
</tbody>
</table>

* Tax rate can vary from 0% to a maximum of 23.8% depending on your adjusted gross income.
Cost Basis

- Inherited property
  - Basis is value as of Date of Death (Step Up in Basis)
  - For future inherited property, recommend professional appraisal @ DOD.
- Gifted property (received as gift)
  - Original basis of gift giver transfers to gift receiver.
  - Gifting is not recommended if possible to avoid.
- Purchase
  - What was actually paid. Includes additional costs after purchase for land improvements.
The IRS has issued that at least one of these standards has to be met:

1. 500 hours of participation.
2. Your participation was substantially all of the participation of anyone for the year.
3. You participated more than 100 hours and as least as much as any other person for the tax year.
4. You materially participated for any 5 of the prior 10 tax years.
5. All indicators point to material participation along with 100 hours of work.
6. You participated at least 500 hours in total in several business activities and at least 100 in the timber activity.
Records

- If claiming items on tax return, a taxpayer should retain some of the following:
  1. Log book of hours worked and/or at property
  2. Log book of mileage of travel for operations
  3. Attend classes/seminars
  4. Gather budgets/plans from forester professionals and organizations
  5. Have the property cruised periodically
  6. Keep records and track of timber growth & cuts
  7. Have a separate bank account for distinct timber activity
  8. And of course, hang on to invoices & receipts
  9. Conduct your business in a business like manner!
What if you do not have any records

1. Gather what you do have and visit a CPA. A discussion should take place to find out your particular situation.

2. “Reverse Engineering” – Using a variety of sources and professionals such as foresters and realtors, a basis in your timber will be calculated to reconstruct what occurred when you originally acquired the land. Will require homework and additional cost.

3. Understand the risks. The statute of limitations on claimed deductions is 3 years. Can you survive an audit? For record retention, we recommend at minimum 3 year, 5 years on average, and 7 years maximum.
IRS Examinations

1. Usually occur with 2 – 2 ½ years of filing. Infrequent due to lack of current staffing and additional workload.

2. Starts with substantiation of expenses and depreciation

3. May want to view the property

4. Will try to determine if you materially participate taking the stance of a nondeductible hobby loss or passive activity.

5. Luck of the draw!
Questions?
Thank you!

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