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THE SMALL
TIMBER OWNER
and his
FEDERAL INCOME TAX



Agricultural Handbook No. 52

UNITED STATES DEPARTMENT OF AGRICULTURE
Forest Service

THE SMALL TIMBER OWNER AND HIS FEDERAL INCOME TAX

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Forest Service



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PREFACE

A COMMITTEE of the Society of American Foresters appointed in 1949 to study the effect of forest taxation on forest practices had an important part in the conception and development of this handbook. The members of this committee believe (1) that many, if not most, small forest-land owners pay more in income taxes on timber sold or harvested than the law requires; (2) that overpayment detracts from the economic incentive to practice forestry; and (3) that forest practices on small holdings would be improved if the owners were informed of their actual income-tax obligations and opportunities. Members of the committee were helpful in proposing the preparation of this publication, assisting in its organization, and reviewing the manuscript. The committee is composed of Ralph W. Marquis, chairman, Upper Darby, Pa.; Lloyd P. Blackwell, Ruston, La.; W. D. Hagenstein, Portland, Oreg.; E. G. Wiesehuegel, Norris, Tenn.; and E. T. F. Wohlenberg, Ukiah, Calif.

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CONTENTS

	Page
Introduction.....	1
Receipts from sales of timber and forest products.....	3
The method to use.....	3
Treating receipts as ordinary income.....	5
Treating receipts as capital gains.....	5
The recognized gain or loss and the depletion allowance.....	6
Separate schedule D.....	13
Losses from fire, windstorm, or other casualty.....	20
Types of loss that may be deducted.....	20
Determining the recognized loss.....	20
Calculating the tax deduction.....	22
Costs of forest ownership and operation.....	24
Operating expenses.....	24
Carrying charges and development expenditures.....	25
Capital expenditures.....	27
The land account.....	27
The timber account.....	28
The equipment account.....	28
Depreciation allowances.....	28
Concluding section.....	31
Questions and answers.....	31
Problems.....	36
Key for ready reference to taxpayer's situation.....	40
Appendix.....	41
Exhibit A: Individual income tax return (Form 1040).....	43
Exhibit B: Schedule of farm income and expenses (Form 1040F).....	47
Exhibit C: Schedule of profit (or loss) from business or profession (separate schedule C).....	50
Exhibit D: Schedule of gains and losses from sales or exchanges of property (separate schedule D).....	51
Exhibit E: Sample timber statement for use with separate schedule D.....	52
Exhibit F: Income tax estimated useful lives and depreciation rates.....	52
Exhibit G: Turpentine depletion.....	54

INTRODUCTION

How should timber receipts and expenditures be reported when making out a Federal income-tax return? Can a deduction be claimed when timber is damaged by fire or windstorm? How large a deduction will be allowed? Such questions are more easily asked than answered, since little material is available to tell the small owner in non-technical language how to handle the Federal income-tax aspects of his forest operations. This handbook is designed to meet this need.

Small timber owners are here thought of as those holding less than 5,000 acres. In the aggregate such owners possess three-fourths of the private commercial forest land area of the United States. The group is composed of some 3 million farmers whose forest holdings average 40 acres, and 1 million others with average holdings of 130 acres. The nonfarm properties are held by a wide diversity of owners including sawmill operators, investors, and business and professional persons; the great majority are absentee owners.

This handbook is intended not only for the timber owner himself, but also for those who may be called upon to advise him on his tax problems. Such persons will include extension foresters, service foresters, and consulting foresters; and in some cases the taxpayer's attorney, banker, accountant, or other business consultant.

There are a number of reasons why a handbook such as this may serve a useful purpose. The timber provisions of the Internal Revenue Code are complex, and it is likely that many timber owners are currently paying a larger tax than is required by law. At the same time higher prices for standing timber and forest products are directing more and more attention to the forest as a source of income. It is unfortunate both for the timber owner and for the community if timberlands are not fully utilized for production of forest products because of a mistaken belief that the proceeds will be largely taxed away. It is equally unfortunate if owners fail to protect, maintain, and improve their timber property because they do not understand that expenditures may be capitalized or treated as deductible expenses.

A clearer understanding of income-tax procedures should benefit the taxpayer financially and should at the same time encourage better forest management. It is hoped that savings realized through use of correct procedures in reporting timber receipts and expenditures will act as incentives for timber owners to grow more timber, to protect it better, and to utilize it more wisely.

As the table of contents indicates, the discussion falls under three broad headings. The first to be taken up is the treatment of receipts from the sale of timber and forest products. Both the so-called "ordinary income" method and the "capital gains" method will be de-

scribed. This section deals with the money taken in by the timber owner. Second is the treatment of timber losses from fire, windstorm, or other casualty. Such losses may or may not involve cash transactions, but they will mean a reduction in the value of the timber asset for which the taxpayer can in some cases claim credit in his tax return. The third is the treatment of timber expenditures, both those that may be deducted as operating expenses year by year and those that must be capitalized and recovered over a period of years through depletion or depreciation. This section deals with money paid out by the timber owner. The concluding section contains questions and answers, problems illustrating specific situations, and a key to assist the taxpayer in finding the tax procedure that applies to his particular situation. Sample income-tax forms are reproduced in the appendix.

The field of Federal income taxation is an extensive one. It has been practical to cover only the more usual questions of interest to the small individual timber owner. Larger owners, corporations, estates and partnerships, and those with special tax problems may need to consult their Director of Internal Revenue (formerly known as Collector of Internal Revenue), his deputy, or other tax authority.

In general, no attempt has been made to provide background information dealing with our Federal income-tax system as a whole, with accounting periods and methods, or with the filing of returns. For treatment of these and similar topics not related specifically to forest operations, the reader is referred to the following publications:

Your Federal Income Tax. Issued annually by the U. S. Treasury Department, Bureau of Internal Revenue. For sale by Superintendent of Documents, Washington 25, D. C., price 25 cents.

Farmers Income Tax. Issued annually. Prepared cooperatively by the State Extension Services and the U. S. Department of Agriculture. Obtainable from county agricultural agents.

RECEIPTS FROM SALES OF TIMBER AND FOREST PRODUCTS

There are two methods of treating receipts when preparing your Federal income-tax return. The first is known as the ordinary income method and the second as the capital gains method. In some situations you have no choice but must use the ordinary income method. In some other situations the tax return will involve the use of the ordinary income computation for certain types of receipts and use of the capital gains computation for other types of receipts.

THE METHOD TO USE

There are four situations in which you are required to report receipts from forest operations as ordinary income. The first and second relate to sales of standing timber, the third and fourth to sales of forest products.

(1) Proceeds from sales of standing timber "held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business" must be reported as ordinary income. This language is regarded as applying to dealers engaged in both buying and selling timber or forest properties and does not generally apply to the farmer or other timber owner making occasional sales.

(2) Proceeds from sales of standing timber sold under a "pay-as-cut" contract must be reported as ordinary income if the timber has been held for 6 months or less. A pay-as-cut contract is one in which you are paid on a scale basis at so much per thousand board feet, per cord, or other unit as the timber is cut. If you think that your timber sale fits this situation, you may wish to turn to numbered paragraph 3 of the section headed "Separate Schedule D," where the pay-as-cut contract is more fully explained.

(3) Proceeds from sales of forest products (logs, lumber, poles, mine timbers, cross ties, pulpwood, fence posts, fuel wood, etc.) must be treated as ordinary income, subject, however, to one very important qualification. If the products were processed from timber that you had held for more than 6 months before the beginning of your tax year you can, if you wish, consider the cutting of such timber during the year as a sale of the timber so cut, and report the transaction in two parts (a) the increase in value of the standing timber up to the time you cut it and (b) the increase in value due to cutting and processing. You can treat the increase in value under (a) as a capital gain, but you must treat the increase in value under (b) as ordinary income. This choice is discussed on pages 16-18.

The cutting of timber held 6 months or less does not give you the choice just described and income from the sale of resulting products must be treated as ordinary income.

(4) Proceeds from sales of products harvested from the standing tree such as naval stores, maple sirup, bark, fruits, nuts, oil, or Christmas greens must always be treated as ordinary income.

Except for the four situations just described, your timber receipts will normally be entitled to capital-gains treatment. A capital gain, in the case of assets held more than six months, may under certain conditions be taxed at less than the rate applying to your ordinary income. This means that use of the capital gains method can result in your having a substantially smaller tax to pay. On the other hand, the capital-gains method requires you to make a more lengthy calculation of your tax and also requires you to keep more detailed records of your forest operations. For these reasons many timber owners who usually sell only small amounts may not consider the capital-gains calculation to be worth while and may prefer to use a short cut by simply reporting their receipts as ordinary income.

The question "How small is small?" will be answered differently by different taxpayers, and each must decide for himself at what point his sales of timber justify the capital-gains calculation. As a guide in reaching this decision the table that follows may be of assistance.

The table shows for various tax brackets under 1952 tax rates, the saving in tax that could result through use of capital-gains treatment, assuming that the timber sold or cut has been held for more than 6 months and that the taxpayer is married and files a joint return. Note that the receipts listed in the first column are net of expenses of sale and allowance for depletion (the return of your investment in the timber cut). The income brackets refer to net income (item 3 of the tax computation on page 3 of your return), after personal exemptions have been subtracted. In view of present-day tax rates it seems likely that many taxpayers will wish to consider use of the capital-gains method when net proceeds from sales of timber exceed roughly \$100 in amount.

TABLE 1.—*Possible savings at 1952 tax rates through use of capital-gains treatment*

Timber receipts less expenses of sale and depletion allowance	Net income less exemptions			
	Up to \$4,000	\$4,001 to \$8,000	\$8,001 to \$12,000	\$12,001 to \$16,000
\$25.....	\$2. 78	\$3. 08	\$3. 63	\$4. 25
\$50.....	5. 55	6. 15	7. 25	8. 50
\$100.....	11. 10	12. 30	14. 50	17. 00
\$250.....	27. 75	30. 75	36. 25	42. 50
\$500.....	55. 50	61. 50	72. 50	85. 00
\$1,000.....	111. 00	123. 00	145. 00	170. 00

TREATING RECEIPTS AS ORDINARY INCOME

If you are a farmer and file Form 1040F (Schedule of Farm Income and Expenses) and use the cash method of accounting, you will enter your receipts from sale of timber or forest products on page 1 under item 3, "Other Farm Income," opposite either "wood and lumber" or "other forest products" as the case may be (see Exhibit B, Appendix). If you are a farmer using the accrual method of accounting, sales of timber or forest products will be reported on page 2 of Form 1040F along with your sales of other farm products.

You are permitted a reasonable allowance, known as depletion, for the return of your original capital investment in the timber cut. For example if, when you bought the farm, a reasonable allocation of the purchase price between timber, land and improvements if any, showed that the cost of the timber alone was \$1,500 and if this year you sold one-fifth of the timber, you may deduct \$300 (one-fifth of \$1,500) as depletion or return of capital. The depletion allowance that you are claiming together with a brief note as to how the figure was arrived at should be entered on page 3 of Form 1040F under "Other farm expenses."

The calculation of the depletion allowance can raise numerous questions when timber operations are larger and these are explained in detail under the paragraph heading *The Recognized Gain or Loss and the Depletion Allowance* on the following page. Such questions are not likely to arise, however, in connection with the ordinary income method.

If you are not a farmer and therefore do not file the farm schedule (Form 1040F), the way in which you report ordinary income from sales of timber or forest products will depend upon whether or not you are engaged in a business related to your timber operations, as for example sawmill operation, or manufacture of furniture, containers, etc. If you are engaged in such a business, receipts should be entered on separate Schedule C,¹ Profit (or Loss) from Business or Profession (see Exhibit C, Appendix) under item 1, "Total receipts from business or profession." The depletion allowance should be entered under item 19 with a note as to how the figure was determined.

If you are not engaged in a business related to your timber operations, your income from sales of timber should be entered directly on the return (Form 1040). Receipts should be listed on page 2, Schedule G, under income from other sources and should be shown net of depletion allowance. The depletion allowance should then be explained in an attached statement.

TREATING RECEIPTS AS CAPITAL GAINS

The calculation of capital gains and losses need not be difficult and if you will follow the steps outlined below, you should have little trouble in finding the amount to be reported. In reporting your

¹ Separate Schedule C should not be confused with the Schedule C Summary on page 2 of Form 1040. See Exhibit A, Appendix.

capital gain or loss you must make use of separate schedule D,² Gains and Losses from Sales or Exchanges of Property (see Exhibit D, Appendix). This form is required no matter whether you are a farmer and file the Schedule of Farm Income and Expenses (Form 1040F), or a businessman filing the Schedule of Profit (or Loss) from Business or Profession (Schedule C) or whether you file neither of these schedules. Before you start to fill out Schedule D, however, it is necessary to find the "recognized" gain or loss. This is the first step and will be taken up before describing the use of Schedule D.

The recognized gain or loss and the depletion allowance

The gain or loss recognized for tax purposes is found by taking the difference between the "gross sales price" (column 4 on separate Schedule D) on the one hand and the "cost or other basis" of the units sold or cut (column 6) on the other. These terms require explanation.

The gross sales price.—When you *sell* standing timber for cash, the gross sales price will simply be the cash received. If other property or obligations of the purchaser are taken in payment, their fair market value must be included. Fair market value is a question of fact that is determined in the light of the available evidence and may be defined as the cash price that a willing buyer would pay a willing seller, both being reasonably informed as to the facts.

When you *cut* timber for sale or for use in your business under the condition³ mentioned in numbered paragraph 3 on page 3, you may, as has been pointed out, report the increase in value in two parts and claim as a capital gain the increase in the value of the standing timber up to the time of cutting. (The date of valuation is given in the next paragraph below.) The law thus permits you in effect to treat the cutting of the timber as a fictional sale of the timber to yourself. While you are not required to follow this practice, it will ordinarily be to your interest to do so. Further reference to this option (Sec. 117 (k) (1) of the Internal Revenue Code) will be found on pages 16–18. At this point we are merely interested in finding the figure that should be used as the "gross sales price", assuming that you do follow this practice.

The law provides that the figure to use as the "gross sales price" in this situation shall be the fair market value of the timber as of the first day of the taxable year in which it is cut. If you use the calendar year basis of accounting, this means that you place a fair market value on the timber cut as it stood in the woods on January first.

As a practical matter, you are not likely to have great difficulty in placing a reasonable stumpage value⁴ on the timber that you have cut. Your extension or service forester or the local representative of the State Forester will probably be able to furnish the "going" price per thousand board feet, per cord, or other unit for stumpage in your area. This average figure can then be adjusted as may be

² Separate Schedule D should not be confused with the Schedule D printed on page 2 of Form 1040.

³ That is, that you have held (owned or had a contract right to cut) the timber for more than 6 months prior to the beginning of your taxable year.

⁴ Stumpage value is the value of timber as it stands uncut in the woods.

necessary to reflect the condition of your own timber. Among factors to be considered are (a) the character and quality of the timber as determined by species, age, size, and condition, (b) the quantity of the timber per acre, the total quantity of timber under consideration, and its location with reference to other timber, (c) accessibility of the timber from the standpoint of its distance from a common carrier and probable cost of cutting and transportation, (d) the freight rates charged by common carriers to important markets.

The Bureau of Internal Revenue will give due weight to all evidence that has a bearing on the fair market value of the timber in question. Such evidence can be classified under the following headings.⁵

1. *Sales of comparable tracts.*—These will usually furnish the best lead to fair market value provided the sales are close to the valuation date. Sales of other tracts may be useful as a guide even though the timber differs in certain respects if allowances in the value are made to reflect such differences.

2. *Realization value.*—This will be indicated by amounts actually realized from sales of forest products less costs of cutting, transportation, processing, and reasonable profit—in other words, the margin between cost of production and the price realized or what may be called the “net value back to the stump.”

3. *Offers to buy and sell comparable tracts.*—Such offers may serve to place upper or lower limits on the estimate of fair market value.

4. *Market conditions in the trade and business conditions in general.*—Prices of lumber, pulpwood, or other forest products will have a bearing on stumpage values, as will the underlying state of business confidence. Such factors will be useful in adjusting values of earlier sales to current conditions.

5. *Cost to the taxpayer of the timber in question.*—This, if the timber is of recent purchase, will assist in determining fair market value but must be adjusted to reflect conditions as of the valuation date.

6. *Valuations for other purposes.*—A market value established for a different purpose may be useful as a guide. Thus values placed upon timber for estate or gift-tax purposes, partnership accountings, in connection with litigation, or for State or local taxation can be given consideration. It should be borne in mind, however, that assessed valuation for local tax purposes will in many cases not coincide with true market value.

7. *Opinion testimony.*—Expert opinion of qualified individuals may serve to support estimates of fair market value, but the expert should, in each case, state the basis for his opinion. The facts upon which the opinion is based will determine the weight that will be attached to it.

To illustrate the determination of gross sales price, take the example mentioned in the preceding section, Treating Receipts as Ordinary Income. Assume first that you did not cut the timber yourself but sold it standing (as stumpage), and that the contract of sale called

⁵ The material in the following numbered paragraphs is based on “Tax Treatment of Timber Cutting under Section 117 (k) The Internal Revenue Code” by Charles W. Briggs, Forest Industries Committee on Timber Valuation and Taxation, 1319 Eighteenth Street NW., Washington 6, D. C. 1952. Pp. 10-14.

for lump sum payment of \$500. In this situation the gross sales price is clearly \$500. Assume now that you made the stumpage sale under a pay-as-cut contract with payment based upon the physical volume actually removed, and that you were paid \$540 for the volume cut during the year. Here the gross sales price is \$540. As a third alternative, assume that you cut the timber yourself and sold it in the form of logs. The money that you receive for the logs is *not* the "gross sales price" of the timber for capital-gains purposes, since your capital gain is calculated only on the increase in value up to time of cutting. You must therefore establish a "selling price," and this will be the fair market value of the stumpage on the first day of your tax year. The logs may have sold for \$1,200, but if the stumpage value was say \$540, then \$540 is the "gross sales price" of the timber from the standpoint of the capital-gains calculation.

The depletion allowance.—When you have found the "gross sales price" you have one of the two figures needed to determine the recognized gain or loss. The other figure is the "cost or other basis" of the timber sold or cut, which means the basis used in computing the depletion allowance. In its simplest form this is nothing more than the original cost of the timber in question as adjusted for any later capital additions or deductions. In terms of the illustration used previously, suppose that you had bought 100 acres of timberland in 1940 for a total price of \$2,500. You estimate that at time of purchase the fair value of the land was \$1,000 and the fair value of the timber was \$1,500. In 1952 you made a partial cutting that removed one-fifth of the original stand. What is your depletion allowance (assuming for purposes of the illustration that there have been no capital additions or deductions and that the volume has not been adjusted for growth since purchase)? Your cost will be one-fifth of \$1,500 or \$300, since that is the portion of the original purchase price that applies to the timber cut. This is your depletion allowance and represents the return of your capital investment in the timber harvested. Clearly, if the "gross sales price" of the timber sold or cut were \$500, your recognized gain is not the full \$500 but only the difference between \$500, the "selling price," and \$300 the cost, or \$200.

In discussing the depletion allowance, it will be useful to consider first the basis for depletion, second the adjusted basis, and third the unit depletion. These three terms all refer to your timber tract as a whole. The unit depletion when multiplied by the volume of timber sold or cut will then give the depletion allowance that may be claimed in calculating your recognized gain or loss for the year.

1. *The basis for depletion.*—This depends upon the manner in which the property was acquired, as for example by purchase, by gift or through inheritance.⁶ In the case of timber purchased on or after March 1, 1913 (the date that the Federal income tax law became effective), the basis is ordinarily the cost of the timber, excluding, as always, the value of the land and any improvements. The fair market value at time of purchase of personal services or nontimber property

⁶ A more complete discussion of this subject, including other means by which property may be acquired, will be found in the Treasury Department booklet, *Your Federal Income Tax*, listed in the introduction.

given in exchange should be considered part of the purchase price. Finding the basis of timber that was received in exchange for other timber can raise special questions and if you own timber acquired in this way you may need to consult your Director of Internal Revenue or other authority in order to ascertain the basis to be used.

Timber purchased before March 1, 1913, presents a somewhat different case from that bought on or after that date. If, as is likely to be the situation, the timber is being sold at a gain, your basis for depletion is the cost of the timber or its fair market value as of March 1, 1913, whichever is the greater. Thus, if the cost of timber, say in 1911 had been \$8,000, but its fair market value as of March 1, 1913, was only \$7,000, you would be entitled to use the higher figure and so would have a smaller taxable gain as compared with the sales price. In the unlikely event that your timber bought before March 1, 1913, is being sold at a loss, your basis for depletion is the actual cost.

The fair market value of your timber as of March 1, 1913, will often be difficult to estimate with accuracy. The assistance of a forester may be needed. Only the timber that was merchantable as of March 1, 1913, should be included in the valuation. This means that the present timber volume must be reduced by the amount of any timber growth since the basic date⁷ in order to find the merchantable volume at that time.⁸ The volume estimated to have been present on the basic date will then be multiplied by a fair unit value⁹ for the species, region, and year in question in order to find the fair market value on the basic date. If the stand in question was not of average quality, adjustments may need to be made.

The basis of timber acquired as a gift (except under a will) depends upon the date of gift. If received before January 1, 1921, the basis is the fair market value at the time of gift. If received on or after January 1, 1921, the basis used in determining a gain is the basis of the last preceding owner by whom the timber was not acquired as a gift. In determining a loss, you must use the basis of the last preceding owner by whom it was not acquired as a gift or the fair market value of the timber at the time of gift, whichever is less.

Timber acquired by inheritance or under will takes as its basis the fair market value at date of death, or 1 year thereafter if the executor of the estate valued the property for estate-tax purposes as of the later date.

2. *The adjusted basis.*—Some timber owners will have no adjustments to make to their basis for depletion and can proceed directly to the third step, the calculation of the unit depletion. Others, however, will have adjustments to make. Adjustments may be of two kinds, additions to the basis and deductions from the basis.

⁷ The basic date is the date as of which the basis is to be determined, in this case March 1, 1913.

⁸ See problem No. 3 in Concluding Section for an example of the method that a forester might use in calculating the merchantable timber volume as of a prior date.

⁹ Steer, H. B., "Stumpage Prices of Privately Owned Timber in the United States," U. S. Dept. Agr. Tech. Bul. No. 626, 1938, may be used as a guide in determining stumpage prices for earlier years.

Additions to the basis for depletion will result from acquisition of additional timber or from expenditures that have been capitalized and not deducted as ordinary expenses year by year as they were incurred. The first situation needs little explanation since your basis for depletion must naturally be adjusted upward to include the cost or other basis of any additional tracts of timber that you have acquired. This adjustment will take the form of charging (debiting) your timber account by the amount of the basis of additional timber acquired (see the sample Timber Account—Value on page 13. In general, you include all your timber in the same timber account unless it is so widely separated as not to form a single operating unit. An operating unit is thought of as all the timber that would logically go to a single given point of manufacture or which would logically be removed in a single logging development.

Additions to the depletion basis that result from capitalization of expenditures are discussed in the chapter dealing with costs of forest ownership and operation. If you have properly expensed timber expenditures in the past, you will not be entitled to adjust your basis for depletion with respect to such items.

Deductions from the basis for depletion must be made if you have cut or sold timber previously or if you have sustained a recognized loss of timber by reason of fire, windstorm, or other casualty. In such cases the depletion basis should be reduced, that is to say, the timber account should be credited by the depletion allowance that was claimed and allowed on the timber previously cut, sold, damaged, or destroyed. The treatment of fire and other casualty losses is taken up in the following chapter.

3. *The unit depletion.*—Assuming now that you have determined the basis for depletion of your timber tract as a whole and that the timber account has been charged or credited to reflect any necessary adjustments, it remains to find the unit depletion. This is done by dividing the basis or adjusted basis by the total volume of merchantable timber (as explained in the following paragraph) expressed in board feet, cords, or other unit. The quotient is the unit depletion expressed, for example, as so many dollars per thousand board feet. The unit depletion, multiplied by the number of units cut or sold during the year, then gives the depletion allowance. As depletion allowances are claimed from year to year, the basis must be reduced accordingly and when the entire basis or adjusted basis has been recovered the timber account will have been exhausted and no further depletion allowances may be taken.

The total volume of merchantable timber to use in the denominator of the fraction is found by taking the volume on hand on the basic date and adjusting it upward or downward for changes since that time. The original volume should be estimated on the basis of the full quantity of timber that the tract would have produced on the basic date if all the merchantable timber had been cut and utilized in accordance with the standards of utilization prevailing in the region at that time. The original volume should then be increased to include the volume of any timber that has been acquired since the original tract and also to include any changes in the original esti-

mates that result from timber growth, changed standards of utilization, correction of inaccuracies, or change in log rule. The volume should be reduced, on the other hand, by the quantity of any timber cut or sold, or lost through fire or other casualty up to the beginning of your current tax year.

Taking the illustration that has been used before assume that you bought 100 acres of timberland in 1940 and that \$1,500 of the purchase price was allocated to timber (3,000 board feet per acre or 300 M board feet in all, valued at \$5 per M board feet). In 1952 you sell 60 M board feet to a sawmill as stumpage. Assume further in order to simplify the illustration that you had no capital additions or deductions and have made no volume adjustment for growth since purchase. What is your basis, adjusted basis, unit depletion, and depletion allowance? The basis will be the original cost or \$1,500. The adjusted basis will be the same, since we are supposing for the moment that there have been no adjustments. The unit depletion will then be $\frac{\$1,500}{300 \text{ M bd. ft.}}$ or \$5 per M board feet. The depletion allowance will be 60 M board feet (the volume sold) multiplied by \$5, or \$300.

In many cases the calculation of the depletion allowance will not be as simple as that shown above. Assume, for example, that 10 years later in 1950 you purchased an additional tract of 50 acres for \$2,600, of which \$600 was allocated to land and \$2,000 to timber (4 M board feet per acre or 200 M board feet in all, valued at \$10 per M board feet or \$2,000). You make the same stumpage sale as before of 60 M board feet. This time you revise your timber volume to include the growth on the original tract. The growth between 1940 and 1952 is estimated to be 90 M board feet. What now is your basis, adjusted basis, unit depletion, and depletion allowance? Your basis will be \$1,500 as before but will be increased by \$2,000, the cost of the second tract (timber only), making the adjusted basis \$3,500. The timber volume is now the sum of three figures: The original volume of 300 M board feet, the estimated growth of 90 M board feet, and the original volume on the second tract¹⁰ of 200 M board feet, totaling 590 M board feet. The depletion unit is now

$\frac{\$3,500}{590 \text{ M board feet}}$ or \$5.93 per M board feet. The depletion allowance will then be $60 \times \$5.93$ or \$355.80. These figures will be found in the sample Timber Account on page 13.

While adjustments for changes in volume due to sales or cutting of timber are readily determined and may be made annually, it is more difficult to know the amount of annual growth, and such adjustments made at intervals such as every 5 years are usually acceptable. Note that when you increase the volume figure by including growth, it increases the denominator of the fraction and so results in a lower unit depletion and depletion allowance. It therefore has the effect of

¹⁰ Growth since purchase on the second tract could also be included, but is omitted in the interest of simplicity.

increasing the recognized gain. On the other hand, the addition of growth volume spreads the depletion over a longer period and postpones the day when, under sustained-yield operation, the basis for depletion will have been fully recovered.

In the preceding discussion it has been assumed that your timber is of reasonably uniform quality and that an average depletion rate over the stand as a whole will be satisfactory. Depletion is actually related to value rather than volume, however, and if the stand is a mixed one containing varied species or groups of species of differing value, it may be worth your while to calculate the unit depletion separately for each such group. This is known as species or value depletion, rather than average depletion, and is accomplished by establishing separate depletion accounts and allocating a proper portion of the total basis to each. In the same way you may wish to set up separate accounts to reflect varying age classes of timber, diameter limits, or quality—for example, timber yielding high-grade veneer logs. If such a separation is made, the removal of low-value trees in an improvement cutting will not reduce the basis for depletion disproportionately, but will leave a larger basis to be used when the crop trees are harvested. Furthermore, if high-quality trees are removed first, a higher depletion allowance may be taken and the recognized gain will be reduced accordingly. If you wish to claim species or group or selective depletion, the basis of the selection should be explained in a statement attached to your return. Probably most small timber owners will not need to establish separate depletion accounts but will find the average depletion method suited to their needs.

Records required.—The timber depletion account (or as it is often called, simply the timber account) is one of three of primary interest to the timber owner. The other two are the land account and the equipment account, both of which are discussed in the section Costs of Forest Ownership and Operation. In addition to these three basic accounts, taxpayers engaged in sawmill operation or other forest products manufacture will of course need the usual business records covering such activities.

The Income Tax Regulations do not call for any one type of timber account, but they do require that accurate records be kept in order that depletion allowances claimed may be supported. As a minimum, two records should be maintained. The first, expressed in dollars, will show the original cost or other basis of your timber adjusted from time to time as already described. The second, expressed in board feet, cords, or other physical unit will reflect the adjusted volume of your timber holdings. Below are examples that may be useful as a guide in setting up these accounts.

The Bureau of Internal Revenue Forest Industries Schedule (Form T—Timber) may be required of taxpayers claiming a depletion allowance. This form calls for a detailed statement of some 10 pages and in certain cases maps also, and is suited to the operations of the larger timber owners. The author understands that Form T will not ordinarily be required of the smaller owners such as those for whom this handbook is intended.

TIMBER ACCOUNT

Value

	Debit		Credit
Mar. 1, 1940:		July 10, 1952: Sold 60 M bd. ft.	
Tract No. 1 purchased at total cost.....	\$2,500	Dec. 31, 1952: Calculation of depletion allowance—	
Charged to land acct.....	1,000	\$3,500	
		590 M bd. ft.	
Charged to timber acct., 300 M bd. ft. at \$5/M.....	\$1,500.00	60 M bd. ft. × \$5.93.....	\$355.80
Aug. 15, 1950:			
Tract No. 2 purchased at total cost.....	2,600		
Charged to land acct.....	600		
Charged to timber acct., 200 M bd. ft. at \$10/M.....	2,000.00	Dec. 31, 1952: Adjusted basis for depletion carried forward.....	3,144.20
	3,500.00		3,500.00
Jan. 1, 1953: Adjusted basis for depletion brought forward.....	3,144.20		

Volume

	Debit (bd. ft.)		Credit (bd. ft.)
Mar. 1, 1940: Estimated merchantable timber volume at purchase, Tract No. 1.....	300,000	July 10, 1952: Sold.....	60,000
Aug. 15, 1950: Estimated merchantable timber volume at purchase, Tract No. 2.....	200,000		
Dec. 31, 1952: Growth since purchase of Tract No. 1.....	90,000	Dec. 31, 1952: Volume carried forward....	530,000
	590,000		590,000
Jan. 1, 1953: Volume brought forward....	530,000		

Separate Schedule D

This schedule (see Exhibit D, Appendix) is the foundation of the capital-gains calculation. Now that the gross sales price and the cost or other basis have been determined, thus giving the recognized gain or loss, you are ready to complete Schedule D. It is made up of two parts: (1) Capital Assets and (2) Property Other Than Capital Assets. The former is further divided into short-term and long-term capital gains and losses. The first step, then, is to classify your timber operations so that you will know which part of the schedule to use.

Classification of timber operations.—The usual types of timber operation giving rise to capital-gains treatment are listed below and will be taken up in turn.

1. Sale outright of standing timber held 6 months or less.

2. Sale outright of standing timber held more than 6 months.
3. Sale under a pay-as-cut contract of standing timber held more than 6 months.¹¹
4. Cutting by the taxpayer of timber held more than 6 months before the beginning of the tax year.¹²

(1) Sale outright¹³ of standing timber held 6 months or less. This type of sale is listed under the heading "Short-term capital gains and losses—assets held not more than 6 months." Note that the 6-months period is calculated back from the actual date of sale.

(2) Sale outright of standing timber held more than 6 months. This situation resembles the first, but now you enter the sale under the heading "Long-term capital gains and losses—assets held for more than 6 months."

(3) Sale under a pay-as-cut contract of standing timber held more than 6 months. This situation is often referred to as 117 (k) (2), since that is the section of the Internal Revenue Code which describes how it is to be handled. Before considering the procedure to follow, it is well to have a clear idea of just what is meant by a pay-as-cut contract.

The section of the Revenue Code in question speaks of "any form or type of contract by virtue of which the owner retains an economic interest in such timber." When, then, do you retain an economic interest in timber following its sale? The test is whether or not you receive income from the *severance and sale* of the timber. Thus if the contract provides that you are to be paid on a scale basis at so much per thousand board feet as the timber is cut, it will qualify as a pay-as-cut contract. So, too, if you are to be paid from the proceeds that the buyer realizes from his sale of logs or other products derived from your timber, it will be regarded as a pay-as-cut contract.¹⁴ On the other hand, the mere sale of timber with provision for installment payment whether or not the timber is cut would not be considered a pay-as-cut contract.

If your timber sale qualifies under section 117 (k) (2), your recognized gain or loss from the timber sale must be compared with the recognized gains or losses that you may have realized during the year from the following five sources:

(a) The sale or exchange of depreciable property used in your business and held more than 6 months—for example, trucks or tractors.

(b) The sale or exchange of real property used in your business and held more than 6 months—for example, part of your farm land.

¹¹ Proceeds from sale, under a pay-as-cut contract, of timber held 6 months or less must be treated as ordinary income.

¹² If the timber that you cut had been held 6 months or less, capital-gains treatment is not permitted.

¹³ By outright sale is meant a sale on a lump sum basis as, for example, an area or boundary sale rather than one under a pay-as-cut contract as described in paragraph 3 following.

¹⁴ Provided the contract does not make you a partner or joint venturer with the other party, instead of vendor or lessor.

(c) The sale or exchange under certain conditions of unharvested crops and of livestock held for draft, breeding, or dairy purposes.

(d) Damage by fire or other casualty or condemnation of the types of property listed under (a), (b), and (c) or of capital assets including standing timber held more than 6 months.

(e) Cutting of timber in accordance with procedure provided by section 117 (k) (1).

Further reference to (d) is made in the section on losses in this handbook, and to (e) later in this section. For a general discussion of the comparison of recognized gains and losses from the sources listed, see the chapter on Capital and Noncapital Gains and Losses in the Treasury booklet, "Your Federal Income Tax," listed in the Introduction.

If the total gains from the sources listed above exceed the total losses, then each gain and each loss must be stated separately on Schedule D under the heading "Long-term capital gains and losses—assets held for more than 6 months." But if the total gains are *not* greater than the total losses, then each gain and each loss must be listed separately at the foot of Schedule D under the heading, "Property Other Than Capital Assets," or in the case of loss by casualty as explained in the section on losses.

Two examples will serve to illustrate the way in which you compare gains and losses from timber sold under a pay-as-cut contract with the other kinds of gains and losses listed above.

Example A (gains exceed losses)

	Gain	Loss
Gain ¹ on sale of timber sold under pay-as-cut contract (117 (k) (2)) -	\$240	----
Gain on sale of tractor-----	100	----
Gain on sale of farm land-----	600	----
Loss on sale of livestock-----		\$400
Loss from forest fire-----		39
	940	439
Excess of gains over losses-----	501	

Each item must be listed individually on Schedule D as a long-term capital gain or loss.

Example B (gains do not exceed losses)

	Gain	Loss
Gain ¹ on sale of timber sold under pay-as-cut contract (117 (k) (2)) -	\$240	----
Gain on sale of tractor-----	100	----
Loss on sale of livestock-----		\$400
Loss from forest fire-----		39
	340	439
Excess of gains over losses-----	None	

Each item must be listed individually at the foot of Schedule D under "Property Other Than Capital Assets," or in the case of loss by casualty as explained in the section on losses.

¹ This is the recognized gain already described, that is to say, gross sales price less depletion allowance.

(4) Cutting by the taxpayer of timber held more than 6 months before the beginning of the taxable year. This is often referred to as the 117 (k) (1) situation and will apply to a large number of timber owners. Unlike the procedure under 117 (k) (2) just described, however, use of the treatment provided by section 117 (k) (1) is optional with the taxpayer, subject to the requirement that a consistent practice be followed from year to year. Although proceeds from the sale of standing timber have long been permitted capital-gains treatment, it was not until 1944 that similar treatment was accorded to timber owners who cut timber for sale or for use in their business. As previously mentioned, the purpose of section 117 (k) (1) is to allow you to take advantage of capital-gains treatment on the increase in value of your standing timber up to the time that it is cut (the date used is actually the first day of the taxable year). However, you must still pay at ordinary income rates on the difference between the value of the stumpage when cut and the price received for the products (logs, lumber, etc.) when sold, less all proper deductions for cost of manufacturing and selling.

The intent of section 117 (k) (1) will be clearer if you think of the cutting of the timber as a sale of the timber to yourself as of the first day of the taxable year at its fair market value on that date. The milling or other processing or manufacture of the timber is then a separate transaction and the value added by manufacture is treated like any other ordinary income. The five paragraphs that follow explain: (a) when you are permitted to use 117 (k) (1), (b) when it is to your interest to use 117 (k) (1), (c) how you indicate your election to use 117 (k) (1), (d) reporting the capital gain up to time of cutting, (e) reporting the increase in value from time of cutting to sale of products.

(a) When you are permitted to use 117 (k) (1). Four conditions must be met if you are to use this method. First, you must have owned, or had a contract right to cut, the timber more than 6 months before the beginning of the taxable year. If you report on a calendar year basis, this will mean that you must have held the timber before July first of the preceding year. Note that you can use the treatment provided by section 117 (k) (1) even though you are not the owner of the timber, provided that you have had for the required period a contract right to cut it. This means that if you *bought* timber from another under a pay-as-cut contract, let us say as a sawmill operator, you can use 117 (k) (1) when you cut the timber, provided the requisite period has elapsed. The second condition is that the timber must have been cut by the taxpayer and not sold standing. Timber cut by the taxpayer, personally, by those working for him or under contract to him, will satisfy this requirement. Third, the timber cut must be intended for sale or for use in your trade or business. This would rule out timber cut for your own use as domestic fuel, for example, or for use as fence posts on your own residential property. Fourth, you must elect to use 117 (k) (1) by making a statement to that effect on your return. The form of this election will be described under (c).

(b) When it is to your interest to use 117 (k) (1). In general you will find it in your interest to take advantage of the capital-gains

treatment provided by 117 (k) (1). Once the decision to use this method has been made, however, the decision is binding with respect to all future timber that you cut and that meets the holding period and other requirements listed above. You must get consent of the Bureau of Internal Revenue to stop using 117 (k) (1), and while this permission is freely given in cases where there is a showing of undue hardship, you are likely to find the Bureau reluctant to authorize resumption of the practice at a future date.

When only small amounts of timber are usually cut, you may prefer not to use 117 (k) (1) but may prefer instead to report sales of forest products as ordinary income and make no split between the increase in value up to time of cutting and the increase in value due to processing or manufacture. You may refer to table 1 in this connection, bearing in mind that the amounts shown in the first column will apply to the increase in stumpage values only and not to receipts as a whole.

It is possible to have a combination of circumstances in which use of 117 (k) (1) could actually cost you money. Suppose, for example, that the price of stumpage were to fall below your cost or other basis, so that you sustain a recognized loss up to time of cutting, and suppose also that you have an excess of gains over losses after making the comparison, as in example A above. In such case your timber loss would be treated as a capital loss and would reduce the net long-term capital gain to which the 50-percent reduction factor (after deducting any net short-term capital loss) would be applied. In view of the rising trend of stumpage prices over a long period of years, a drop in price sufficient to result in a recognized loss seems unlikely to occur with frequency. Hence the timber owner has little to fear from use of section 117 (k) (1).

As a general rule it would seem desirable to elect use of 117 (k) (1) in the first year in which a substantial saving can be secured.

(c) How you indicate your election to use 117 (k) (1). The election takes the form of a computation as explained in the following paragraph, and may be accompanied by a statement, "I claim gain (or loss) from the cutting of timber in accordance with section 117 (k) (1)." (See sample timber statement, Exhibit E, Appendix.)

(d) Reporting the gain realized up to time of cutting. As in the case of sales under cutting contract, the recognized timber gain or loss is compared with the recognized gain or loss that you have realized during the year from any of the sources listed on page 14. Examples A and B above apply equally well to the cutting of timber except that "Gain on cutting of timber in accordance with section 117 (k) (1)" should be substituted for the first item. As before, if the total gains exceed the total losses, each item is listed individually on Schedule D as a long-term capital gain or loss, but if total gains do not exceed total losses, each item is listed at the foot of Schedule D under "Property Other Than Capital Assets" or in the case of casualty losses as explained in the section on losses.

(e) Reporting the gain realized from time of cutting to sale of products. While this increase in value represents ordinary income, it is discussed here because it is closely related to the 117 (k) (1) situation just described. Since you are regarded as having sold the timber

to yourself as of the first day of the taxable year at its fair market value on that date, the fair market value that has been used becomes the "cost" of the timber for purposes of calculating the manufacturing profit. Suppose, for example, that you cut 60 M board feet of timber and that you sell the resulting logs during the same year for \$1,200. If the timber had an original cost or other basis of \$5 per thousand board feet or \$300 and its fair market value as of the first day of the taxable year was estimated to have been \$9 per thousand board feet or \$540, the difference or \$240 would be entitled to capital-gains treatment under 117 (k) (1) as already explained. The \$540 then becomes the "cost" of the timber cut and may be shown as an expense, together with logging, transportation, and other costs and will in effect be subtracted from the \$1,200 that you received for the logs in determining your taxable income. The sale of the logs may be listed at the foot of separate Schedule D under "Property Other Than Capital Assets," and the gain will thus be treated as ordinary income.

• If you did not sell the logs in the same year as the timber was cut but carry them as inventory at the year end, the same principle applies. The fair market value used in determining your capital gain under 117 (k) (1) or \$540 will be taken as the cost of the timber. To this should be added the costs of cutting, logging, and all other expenses incident to the cost of converting the standing timber into the products in inventory. The fact that the fair market value of the stumpage is taken as the cost of the timber, however, does not prevent taxpayers, using the "cost or market whichever is the lower" or other approved method of computing inventories, from continuing to do so.

A practical application of the use of section 117 (k) (1) is given in problem No. 4 in the concluding section.

Completion of Schedule D.—At the top of the schedule are eight column headings. These apply alike to short-term and long-term capital gains and to gains from property other than capital assets.

1. *Kind of property.*—Since more information is needed than can be shown in the space available, you can write "See statement attached." This statement may be entitled "Timber" and should contain the following information under the caption "description of property" (see sample statement, Exhibit E, Appendix):

Name, location, and acreage of tract where sale was made or cutting was done. Name of individual from whom tract was acquired and whether acquisition was by purchase, gift, inheritance, or in other manner.

Original cost of the tract as a whole. If land was included in the purchase show the allocation of the cost or other basis to land, to improvements, and to timber, respectively.

Description of merchantable timber present at time of acquisition. Show estimated volume, leading species, and character such as virgin or second growth.

Description of timber sold or cut during the taxable year (volume, leading species, and intended use as for example lumber, veneer, or fuel).

2. *Date acquired.*—Show here the date upon which the timber came into your possession, whether by purchase, gift, inheritance, or in other manner.

3. *Date sold.*—For outright sales of standing timber give the date that the sales contract was signed, or if the contract was verbal, the date the agreement was made. For sales under a pay-as-cut contract.

give the date the timber was cut.¹⁵ For timber that you cut and to which you wish to apply the capital-gains treatment under 117 (k) (1), write under Date Sold the first day of your taxable year. Thus if your return is made on the calendar year basis, you will write January 1.

4. *Gross sales price.*—The determination of the amount realized has already been explained in the section Treating Receipts as Capital Gains. If you sold stumpage outright, show here the full contract price; if you sold timber under a pay-as-cut contract, show the sum of payments actually received or accrued during the year. If you cut timber, show its fair market value on the first day of your taxable year (see Exhibit E, Appendix).

5. *Depreciation allowed.*—This heading does not apply to sales or cutting of timber. It would apply, however, to sales of such depreciable business assets as trucks, tractors, and logging equipment. Depreciation is discussed in the chapter on costs of forest ownership and operation.

6. *Cost or other basis.*—Here you show the depletion allowance, calculated as previously explained in the section treating receipts as capital gains. The calculation should be shown on the timber statement attached to the return (see Exhibit E, Appendix).

7. *Expense of sale.*—Here you show the sum of expenses related directly to the sale, such as advertising timber for sale; timber survey or cruise; cost of marking trees for cutting; fees for consulting foresters, accountants, or attorneys; travel; and other expenses of similar nature. The items making up the total should be listed on the timber statement.

8. *Gain or loss.*—This will be the gross sales price (column 4) less the sum of the cost or other basis (column 6) and the expense of sale (column 7).

The remainder of Schedule D and transfer of figures to Form 1040 should be carried through in accordance with the directions indicated on the schedule. An important change was made by the Revenue Act of 1951 in the method of determining net capital gain or loss. Formerly only 50 percent of the net long-term capital gain or loss was taken into account. The Act requires that long-term gains and losses for taxable years beginning on or after November 1, 1951, be taken into account in full, but allows a deduction from gross income equal to 50 percent of the amount by which the net long-term capital gain exceeds the net short-term capital loss. Schedule D for the calendar year 1952 reflects this change. Under certain conditions the new method will make no difference in your tax liability, under other conditions it can reduce, and under still other conditions it can increase your tax liability.

On Schedule D you will find provision for a computation of alternative tax. You need not be concerned with this calculation unless your net income less exemptions exceeds \$14,000 (\$28,000 if you file a joint return or, for 1952 or later years, \$20,000 if you file as head of a house-

¹⁵ Note, however, that the date of the contract is used in calculating the 6 months qualification period under 117 (k) (2).

hold). The effect of the computation is to limit the tax on net long-term capital gains to a maximum of 26 percent (formerly 25 percent) regardless of your tax bracket. If your net income less exemptions is below the amounts indicated, your effective rate of tax will be less than 26 percent in any case, so that the computation of alternative tax will be unnecessary.

LOSSES FROM FIRE, WINDSTORM, OR OTHER CASUALTY

If your timber has been damaged by fire or other casualty during the year, you may be entitled to claim a deduction on your income tax return. In order to do this, it is necessary to know what types of loss may be deducted, how the damage is to be measured, and how the tax deduction is calculated.

TYPES OF LOSS THAT MAY BE DEDUCTED

The losses that may be deducted comprise for the most part those which involve actual physical damage and are of sudden, unusual, or unexpected character. Some are caused by natural physical forces or "acts of God," such as lightning, windstorm, ice, hail, sleet, unusually heavy rains, flood, freezing, drought, and, if of epidemic nature, insect infestation or plant disease.¹⁶ Others are man-caused, such as those resulting from fire or plane crash or from war.

Two types of loss that differ from those just described but are treated in a similar manner, are those resulting from seizure or requisition by public authority through exercise or threat of exercise of the power of condemnation, and those resulting from theft.

Progressive deterioration resulting from a steadily operating cause such as soil erosion is not recognized for tax deduction, nor is loss of an incidental or minor character or mere retardation of growth. Losses resulting from the willful negligence of the taxpayer cannot be claimed as tax deductions.

DETERMINING THE RECOGNIZED LOSS

Since you must be able to support any statement of loss claimed as a deduction on your tax return, it is desirable to secure an accurate appraisal of the damage. This appraisal may be made immediately after the fire or other casualty if there is no doubt as to the death of the trees. On the other hand when there is doubt as to survival, the appraisal should not be made until after the following growing season. Since a casualty loss is deductible only for the year in which it occurred, you may need to file an amended return.

A consulting forester may be employed to estimate the damage if values are large and a substantial amount of work is involved. But in many cases the local district forester, forest fire warden, or other

¹⁶ Losses from forest insects or disease when of endemic character, that is, those resulting from a low level of pest incidence usually present under normal conditions, are not deductible.

representative of the State forestry department will be able to give you a damage estimate for attachment to your tax return as a proof of loss.

In requesting a damage estimate it is well to be specific as to just what information is needed, since the basis for calculating the tax deduction is frequently not understood. Your recognized loss for tax purposes with respect to timber intended for sale or for use in your business¹⁷ is the difference between the adjusted basis for depletion of the damaged timber and the sum of (a) the salvage value if any of the timber plus (b) any insurance recovery. This means that you need to do two things: Establish the "basis"¹⁸ of the timber damage, and find its salvage value. You should, therefore, ask the forester or other appraiser two questions: First, what is the volume, by leading species, of the damaged timber? Second, what is its salvage value on the stump? Unless the salvage value is less than your basis for loss, you do not have a recognized loss and can claim no deduction.

An example will help to clarify procedure in determining loss. The district forester in reply to the first question tells you that he estimates the fire to have burned over 5 acres with an average volume of 3,900 board feet to the acre or 19,500 board feet in all. This permits you to determine your basis for the timber damaged. Assuming that there is no compensation received by insurance or otherwise, that your original cost was \$5 per thousand, and that there have been no adjustments to the original cost figure, your depletion allowance is $\$5 \times 19,500$ board feet or \$97.50. Assume now that in answer to the second question you find the salvage value to be \$3 per thousand board feet or a total salvage value of \$58.50. Your recognized loss is \$97.50 less \$58.50, or \$39.00. If there were no salvage value, your recognized loss would be the full \$97.50.

Loss from theft of timber is calculated in the same way except that there will be no salvage value. In case of public condemnation there will likewise be no salvage value, but there will be a condemnation award. If the award falls short of the basis of the timber, you have a recognized loss to the extent of the difference.

In determining your recognized loss following damage to a plantation or to immature timber, whether planted or natural second growth, the same principle applies. In such cases, however, there is likely to be no salvage value. Your basis for loss on a plantation will be the original cost plus such carrying charges as have been properly capitalized up to the time of the fire or other casualty. In the case of natural second growth, you may have no basis for loss at all and in such event could claim no loss.

Confusion will be avoided if you bear in mind that the loss recognized for tax purposes is determined differently from, for example, an insurance loss or the amount of damages for which a negligent party might be sued. In the latter cases, the measure of damage will normally be the difference between the sound value of the timber before the casualty and its damaged value after the casualty. For tax pur-

¹⁷ In contrast with shade or ornamental trees, described below.

¹⁸ See the explanation under the paragraph heading *The depletion allowance* in the section *Treating Receipts as Capital Gains*.

poses, however, you need to find the difference between your adjusted basis for the damaged timber (intended for sale or for use in your business) and its damaged value after the casualty as increased by any insurance or other recovery.

A different method of determining the recognized loss is used in the case of damage to individual shade or ornamental trees standing on residential or other nonbusiness properties. In such cases the recognized loss is the difference in the value of the *property as a whole* before and after the windstorm, lightning, or other casualty. The deduction claimed may not be greater than the adjusted basis of the property as a whole and must be reduced by any insurance or other recovery. The following schedule while not officially accepted by the Treasury Department has been used in the past as a guide in claiming deductions for damage to shade or ornamental trees in certain residential areas. The figures are based upon replacement value up to 10 inches diameter and upon the basic value as a tree above that diameter.

Replacement values only:		Per inch
1-3 inch diameter	-----	\$10. 00
3-6 inch diameter	-----	15. 00
6-10 inch diameter	-----	20. 00
Basic value as a tree only (where replacement is not feasible):		
10-20 inch diameter	-----	22. 00
20-35 inch diameter	-----	25. 00
35 inches and over	-----	35. 00

The actual value of the tree may differ from that indicated above by reason of the relation of the tree to house, garden, or landscape scene, by reason of the hardness, age, or physical appearance of the tree, or by reason of prior injury. If the loss that you claim is not in accord with the figures shown in the schedule, an explanatory statement should be attached to your return.

If the tree is replaced by another tree, it seems likely that the actual replacement cost, provided such cost is reasonable in amount, will be accepted as the measure of loss.

CALCULATING THE TAX DEDUCTION

Once you have determined your recognized loss from fire or other casualty as outlined above, it must be entered at the appropriate place on the return.

If you had owned the damaged timber 6 months or less at the time of the casualty, the recognized loss is listed on Schedule D under the heading, "Short-term capital gains and losses—assets held not more than 6 months."

The recognized loss on a shade or ornamental tree standing on a residential or other nonbusiness property owned 6 months or less is not deductible from gross income in computing adjusted gross income, as are capital losses, and therefore it should be entered with an explanatory note on page 3 of Form 1040 under the heading, "Losses from fire, storm, or other casualty, or theft."

If you owned the damaged timber or shade tree more than 6 months, the recognized loss comes under paragraph (d) on page 15 and must be grouped with other recognized gains and losses listed on that page. If there is an excess of gains over losses, the fire or casualty loss is

listed on Schedule D as a long-term capital loss. If total gains do not exceed total losses, then a fire or other casualty loss on timber intended for sale or for use in your business must be listed on Schedule D under "Property other than capital assets," and a shade tree loss must be entered on page 3, Form 1040, under the heading, "Losses from fire, storm, or other casualty, or theft."

When making entries on Schedule D, the information called for by the eight column headings should be supplied in a manner similar to that outlined earlier under "Completion of Schedule D." Under "Date sold" in column 3 will be shown the date of the fire or other casualty. Under "Gross sales price" in column 4 should be shown the sum of the salvage value and any recoveries received, such as a condemnation award, recoveries under policies of insurance, or court awards for damages. In column 7 may be shown the sum of any expenses incurred in connection with the casualty as cost of appraisal, timber cruise, legal fees, etc. The sample timber statement (Exhibit E, Appendix) contains an entry relating to fire loss that will serve as a guide.

Your recovery following a casualty or condemnation may possibly exceed the adjusted basis of the damaged or condemned timber. Such a situation could arise, for example, as the result of a condemnation award or recovery under an insurance policy. Instead of a recognized loss you would have a recognized gain to the extent that the award or recovery exceeds the adjusted basis of the timber in question. If the timber had been held 6 months or less, the recognized gain would be listed under "Short-term capital gains and losses—assets held not more than 6 months." If the timber had been held more than 6 months the gain would be combined with other recognized gains and losses, as mentioned above.

There is one exception to the treatment of a recognized gain following a casualty or condemnation that should be borne in mind. The law provides that when the entire award or other recovery is promptly reinvested in similar property, no gain shall be recognized. If, on the other hand, only a portion of the recovery is reinvested in similar property, a gain is recognized to the extent that the amount reinvested falls short of the total recovery. For example, suppose that the adjusted basis of your damaged timber was \$1,200 but that its actual sound value before the fire was \$2,000. If your insurance recovery, assuming a total loss, were the full \$2,000, the recovery would be \$800 in excess of your adjusted basis. This \$800 would be recognized as a gain unless you promptly reinvested the entire \$2,000 in timber. If only \$1,500 were reinvested in timber, then a gain would be recognized to the extent of \$500 (\$2,000 less \$1,500).

Relatively little insurance is now being placed on standing timber and the situation just described is not likely to occur except in the case of a condemnation award. As forest insurance becomes increasingly common in the future, however, the principle just explained will be of growing importance. The timber owner who might hesitate to insure his timber for fear that the excess of any insurance recovery above his basis would be taxed as a capital gain, should not overlook the fact that such gain would not be recognized to the extent that he promptly reinvested his insurance proceeds in timber property.

If you find yourself in the position of having a recognized gain following timber casualty or condemnation, you may need to consult your Director of Internal Revenue or other tax authority as to the exact requirements relating to reinvestment of the proceeds.

COSTS OF FOREST OWNERSHIP AND OPERATION

From an income-tax standpoint two broad types of costs are recognized, charges against income and charges against capital. The former are "expensed," that is, treated as deductions from gross income year by year. The latter are "capitalized," that is, included in the adjusted basis¹⁹ of the property, and, for the most part, recovered through depreciation or depletion. With respect to certain items, moreover, you may choose either method.

The costs that are expensed year by year are, in general, the ordinary and necessary expenses directly related to the business of the taxpayer or related to the production of income. Also deducted annually are allowances for depreciation. The costs that must be capitalized include outlays for acquisition of property having a useful life of more than 1 year, such as land or equipment and also outlays for permanent improvements or betterments to such property. The costs that may be either expensed or capitalized include carrying charges, such as taxes and interest relating to unimproved and unproductive timber tracts and also development expenditures made for any forest lands with a view to production of income at a later time.

The costs of forest ownership and operation are considered under the following headings:

1. Operating expenses.
2. Carrying charges and development expenditures.
3. Capital expenditures.
4. Depreciation allowances.

OPERATING EXPENSES

Expenses for current operations are those directly related to the production of income and are thus incurred in connection with timber stands from which merchantable products are being harvested. Such expenses, provided that they are reasonable in amount, are deductible from your gross income year by year as they are paid or incurred.

Operating expenses include the cost of hired labor,²⁰ such as that engaged in timber cutting or processing; hire of animals, trucks, tractors, or other equipment; purchase of tools of short life or small cost such as axes, saws, sledges, wedges, etc.; cost of materials and supplies; incidental repairs; operating expenses of trucks, tractors, or other machines; construction of temporary roads; and management expenses including the fee of a consulting forester, lawyer, accountant, or other adviser. Advertising and other costs related directly to a specific sale of standing timber, however, should be treated as an

¹⁹ For the meaning of this term see page 9.

²⁰ The value of the taxpayer's own time or that of his dependent children cannot be treated as an operating expense.

expense of sale and, if a capital gain or loss is involved, should be listed on schedule D as described on page 19.

If you are a farmer and file the Schedule of Farm Income and Expenses (Form 1040F), your operating expenses will be listed on page 3 under the heading Farm Expenses for Taxable Year. If you file the Schedule of Profit (or Loss) from Business or Profession (separate Schedule C), your operating expenses will be listed either under "Cost of goods sold" or "Other business deductions." If you file neither Form 1040F nor Schedule C, your operating expenses may be listed in a separate statement attached to the return and should be deducted from the income reported in Schedule G, line 2 on page 2 of the return. If operating expenses exceed the income reported on line 2 of Schedule G, the difference should be shown as a red figure and subtracted in determining the total income figure to be entered as item 3, page 1 of the return.

CARRYING CHARGES AND DEVELOPMENT EXPENDITURES

You can either expense or capitalize carrying charges and development expenditures, as you may choose, provided that you follow a consistent practice from year to year. The nature of such costs will be explained before taking up the question of how they should be treated.

Carrying charges can be thought of as deductible costs that are incurred while timber lands are unimproved and unproductive or during the time that timber lands are being developed or improved. Annual taxes, interest payments, protection costs as for fire or pest control, and insurance premiums are examples of carrying charges.

General property taxes are payable annually irrespective of harvest operations and can be considered as carrying charges during the time that the property is unimproved and unproductive, or is being developed or improved. On the other hand, general property taxes incurred in connection with an income-producing property are in the nature of operating expenses and must be expensed. Yield or severance taxes are payable at the time of timber harvest and seem likewise to come under the classification of operating expenses. Taxes in the nature of assessments for local benefits that increase the value of the property as a whole cannot be expensed but may, however, be capitalized. Deduction of Federal income taxes, excess profits taxes, estate taxes, and gift taxes is prohibited by law.

Interest payments include those due on bank loans and other short-term credit and also those on mortgage indebtedness. Interest charges of an accounting character which represent the cost of capital invested in the property but which are not actual out-of-pocket expenditures may not be deducted.

Protection costs include expenditures for labor, materials, and tools needed in the maintenance of fire lanes (costs of constructing fire lanes are regarded as capital expenditures) or other protection measures including costs of actual fire suppression. Contributions to fire-protection associations also come under this heading. Protection costs incurred for the purpose of controlling forest insects or diseases are treated similarly.

Premiums for standing timber insurance are recognized as carrying charges and the same is true of the cost of fire or other insurance on buildings or other facilities. The cost of automobile insurance and workmen's compensation insurance, on the other hand, should normally be treated as operating expenses.

Interest payments, protection costs, and insurance premiums when incurred in connection with income-producing properties are in the nature of operating expenses and must be expensed.

Development expenditures are incurred during the "developmental period" of a farm or other property, during which the timber owner may be put to expense in caring for timber stands which, though already established, do not yet produce income. The cost of thinning and improving stands of young timber prior to the time that the production stage is reached come within the meaning of development expenditures. Such costs include expenditures for girdling, poisoning, pruning, and improvement cuttings but should be reduced by incidental amounts received for any salable products.

Since you have a choice as to whether you will expense or capitalize carrying charges and development expenditures, which course should you take? It seems clear that if you have income from which to deduct them, it will in general be to your advantage to expense all items that you are permitted to treat in this way. By doing so you take credit for the expense year by year as it is paid or incurred, and accordingly reduce your gross income and consequently your tax also. If, on the other hand, you capitalize an expenditure, the best you can do is to recover it through depreciation or depletion over the life of the asset or as the timber is harvested. Thus an expenditure of \$500 for an improvement cutting, if capitalized, would become an adjustment to the cost or other basis of your timber (see the section *Treating Receipts as Capital Gains*) and would become a part of the depletion allowance for which credit could eventually be taken as the timber was cut or sold. Most timber owners will doubtless feel that a bird in the hand is worth more than a bird in the bush and will prefer to expense their costs year by year to the extent permitted by law. Moreover, the bird in the bush may be only half a bird, since a cost that is capitalized and recovered through the depletion allowance, to the extent that it is used to offset a long-term capital gain, may be only half as effective in reducing your tax as would a straight expense deduction, because of the lower rate at which long-term capital gains may be taxed.

While it will usually be to your advantage to expense rather than capitalize your carrying charges and development expenses, this will not invariably be true. If you operated at a loss in a given year, for example, and had no adjusted gross income (line 4, page 1 of your return) against which the expenses could be offset, it may be preferable to capitalize the carrying charges and development expenditures. In this situation, however, it is suggested that you refer to the net operating loss carryback and carry over provisions explained in the Treasury publication *Your Federal Income Tax* listed in the Introduction. Again, an owner might for some reason prefer to capitalize his carrying charges with a view to building up his basis for depletion and in this way reduce his ultimate capital gain. On the whole, however, the

expensing of such items is likely to be the usual procedure, especially since the decision once made is binding for future years unless permission to make a change is secured from the Director of Internal Revenue.

The entries to make on your return when costs are expensed were described in the section on Operating Expenses; the entries to make when costs are capitalized will be described in the following section on Capital Expenditures.

CAPITAL EXPENDITURES

The timber owner may incur capital expenditures either for the acquisition of property or for permanent improvements or betterments that increase the value of property that he already owns. Examples of the former type of capital expenditures are purchases of timber and purchases of equipment having a useful life of more than 1 year. Examples of the latter type are expenditures for land improvements, such as construction of bridges, roads, and fire lanes; for timber "improvements," such as planting and seeding; and for major repair of equipment that prolongs its useful life. Capital expenditures whether for acquisition or improvement of property can be classified usefully under three headings: The land account, the timber account, and the equipment account.

The land account

The cost of bare-land purchases will be charged to the land account and will not be subject to recovery through depreciation. So, too, when tracts of mature or immature timber are acquired, the land account should be charged with its proportion of the total price paid. If it is desired to allocate something over and above the minimum bare-land value to the land account in recognition of the potential value of young growth of presently unmerchantable size, this may be done and such amounts may then be reallocated to the timber account when the young growth reaches merchantable size. Land improvements of a permanent or nondepreciable nature such as road construction, grading, ditching, etc., are likewise charged to the land account without recovery through depreciation. The construction cost of depreciable improvements, on the other hand, such as bridges, culverts, and fences, while also charged to the land account, may be recovered through depreciation.

Main line or "permanent" roads present a special problem although one not likely to affect many of the smaller timber owners. If you can establish that such roads, once the timber to which they give access has been cut, will not be needed again until a new timber crop has grown and are in fact depreciating in value during the waiting period, recovery of the capital investment through depreciation may be permitted. The dividing line between a permanent or nondepreciable asset on the one hand, and a depreciable asset on the other is sometimes hard to draw. To be the subject of depreciation, however, property must have a limited and determinable useful life and must be used in the taxpayer's business or for earning nonbusiness income.

The land account should be credited each year with the depreciation allowable as explained in the final section of this chapter.

The timber account

The timber value account (see sample on page 13) is charged with (a) the cost (excluding land value) or other basis of timber acquisitions whether acquired by purchase, inheritance, gift, or in other manner, together with the cost of cruising or examining the timber prior to purchase, (b) expenditures for timber "improvements" such as seeding and planting, and (c) such carrying charges and development costs as you may have elected to capitalize, rather than to expense year by year. The timber value account is credited when depletion allowances or casualty losses are claimed.

The timber volume account will show the volume of merchantable timber as adjusted from time to time. The timber account as a whole enables you to calculate the depletion allowance as explained in an earlier section.

The equipment account

This account will be charged with the cost of durable equipment such as trucks, tractors, or power saws. It will also be charged with any major repair or reconstruction costs that materially increase the value or prolong the life of such equipment.

The equipment account will be credited with the depreciation allowances taken year by year, as explained in the following section.

DEPRECIATION ALLOWANCES

Depreciation occurs when a capital asset wears out as a result of service; obsolescence occurs when a capital asset gradually becomes out of date before it is physically worn out. Both terms must be distinguished from depletion which results from the reduction or exhaustion of an asset such as timber or other natural resource. Depletion relates to the timber account whereas depreciation and obsolescence relate to the equipment account and to depreciable assets in the land account.

Allowances for depreciation and obsolescence differ from the three types of costs already taken up (operating expenses, carrying charges, and capital expenditures) in that they are accounting or bookkeeping items rather than actual outlays of money. They are, nevertheless, very real costs of forest ownership and operation, since they represent that portion of the cost or other basis of depreciable property that you estimate will be used up or that should be written off because of obsolescence during the current tax year. The purpose of the depreciation allowance is thus to permit you to recover, during the useful life of the property, the capital that you have invested in it, less the estimated salvage value.

Three elements enter into the determination of the depreciation allowance for a given piece of property: Its cost or other basis, its salvage value, and the period of its useful life. The basis of the asset will normally be its purchase price in the case of trucks, tractors,

power saws, and other equipment; or its cost of construction, including labor and materials, in the case of depreciable improvements in the land account such as buildings, roads, bridges, and culverts. From this basis the estimated salvage value, if any, at the end of the asset's useful life must be subtracted and the remainder is then divided by the estimated period of the asset's useful life. For example, equipment purchased at a cost of \$1,200 and estimated to have a salvage or trade-in value of \$200 after 5 years will normally be depreciated at the rate of one-fifth of the \$1,000 difference, or \$200 per year.

The method described is known as the straight-line method of depreciation and will doubtless meet the needs of most small timber owners, although other methods may be adopted if in accord with the actual character of your forest operations and if consistently followed from year to year. Thus, equipment that can be used only in a given logging operation may be depreciated over the period of the cut at a rate established by current exhaustion of stumpage, rather than on the basis of the physical life of the property.

Since the rate of depreciation will generally depend upon the useful life of the property, a guide to the estimated useful lives of machinery and equipment used in timber operations is needed. Such a guide is contained in Bulletin F published by the Treasury Department (see Exhibit F, Appendix). Items from the Lumber and Wood Products Schedule and from the Agriculture Schedule likely to be of interest to the small timber owner have been listed. Estimated useful lives for machinery used in lumber remanufacturing plants and creosoting plants may be found by referring to Bulletin F.

The depreciation allowances that you claim as deductions in any year must be itemized either in the Depreciation Schedule on page 3 of the farm form (Form 1040F), in Schedule C-1 on page 1 of the business form (separate Schedule C), or in Schedule H on page 2 of the return itself (Form 1040). The three schedules call for the same information and contain identical headings as shown in figure 1. These will be taken up in turn. Entries are assumed to have been taken from a tax return covering the year 1952.

[illegible]

FIGURE 1.—Depreciation schedule in Form 1040 (schedule H), Form 1040F, and schedule C.

1. *Kind of property.*—This description should be in sufficient detail to clearly identify the item and should be repeated in the same form from year to year, for example, Tractor No. 1 or Wire fencing, Tract No. 2.

2. *Date acquired.*—The month and date should be shown so that depreciation allowable (column 8) may be prorated on a monthly basis. If month and date are not given, only one-half the allowable annual depreciation may be claimed for the full year.

3. *Cost or other basis.*—Here will be entered the purchase price, or other basis if the asset was not acquired by purchase. The cost of any major repairs or improvements that prolong the useful life of the asset may be added to the basis to form the adjusted basis, or it may be carried as a separate item. If the latter course is adopted a useful life and depreciation allowance is calculated for the improvement.

If you maintain detailed ledger accounts covering your depreciable equipment, the basis or adjusted basis may be entered on the depreciation schedule directly from such accounts. Otherwise, the basis may be carried forward from your income tax return for the year before, subject to adjustments to reflect depreciation already charged off and improvements or repairs made during the taxable year.

4. *Depreciation allowed (or allowable) in prior years.*—This will be a cumulative figure including all depreciation claimed in earlier years and any depreciation that should have been claimed but was, in fact, not claimed. You are not permitted to claim in later years depreciation that applies to earlier years and such depreciation is, in effect, forfeited.

5. *Remaining cost or other basis to be recovered.*—This will be the difference between columns 3 and 4.

6. *Life used in accumulating depreciation.*—Here should be shown the estimated useful life of the asset in question (see Exhibit E). If major repairs have prolonged its useful life, the additional period should be added unless the improvement is being set up as a separate item as mentioned in numbered paragraph 3 above.

7. *Estimated life from beginning of year.*—This will be the total estimated useful life (from column 6) less the number of years that have already elapsed since the acquisition of the asset.

8. *Depreciation allowable this year.*—This will be the remaining cost or other basis to be recovered (column 5) less the estimated salvage value, if any, divided by the estimated life from beginning of year (column 7).

The sum of the depreciation allowances claimed on your depreciable assets for the taxable year will be carried by those using the farm schedule (Form 1040F) from page 3 either to line 7 of summary on page 1 (cash basis) or to line 8, page 2 (accrual basis). If you file the business schedule (separate Schedule C), the total depreciation as claimed in Schedule C-1 will be carried to item 17 of the same Schedule C, Depreciation and obsolescence.

If you sell a depreciable asset such as a tractor, the depreciation allowed or allowable in past years, that is the total depreciation that should have been claimed, must be entered under column 5 on Schedule D and will affect the calculation of the recognized gain or loss.

Turpentine depletion, although not strictly speaking a depreciation allowance, may logically be mentioned at this point since it involves annual deductions rather than periodic deductions at time of sale or cutting, as in the case of timber depletion. The Treasury Department has issued an information release dealing specifically with turpentine depletion and this is presented as Exhibit G, Appendix.

CONCLUDING SECTION

In the preparation of this handbook State Foresters and State Extension Foresters were given an opportunity to list the income-tax questions most frequently asked of their field representatives. The questions that follow are based very largely upon the responses.

Acknowledgment is also made to E. J. Russell, Associate Professor of Forestry, and Harold J. Smolinski, C. P. A., Professor of Accounting, Louisiana Polytechnic Institute, for use of material based upon their article, "Tips on Federal Income Tax Computations for the Small Woodland Owner," in the February 1952 issue of the Forest Farmer.

QUESTIONS AND ANSWERS

1. *What are two methods of treating receipts from sales of timber?*
The ordinary income method and the capital gains method.

2. *Should proceeds from sales of timber be reported with farm income or should they be reported separately?*

If the ordinary income method is used, timber sales should be reported on the farm schedule (Form 1040F), but should be listed separately. If the capital gains method is used, timber sales should be listed individually on separate Schedule D.

3. *Is income from forest land taxed at the same rate as income from farm land?*

While the tax rate itself does not differ with the source of income, forest land income may in effect be taxed at a lower rate than certain types of farm income, because of the capital gains provisions applying to timber sales.

4. *Should the timber owner fail to cut overmature timber in order to avoid increasing his income tax?*

Generally, no. It should be remembered that overmature timber is adding no net growth and may actually be decreasing in value. If capital gains treatment is used the tax cannot take more than 26 percent of the excess of the net long-term capital gain over any net short-term capital loss.

5. *Should a timber owner stagger his timber sales in order to keep down his income tax?*

Periodic cuts will tend to average out receipts from timber operations and will thus avoid large lump sum receipts that could have the effect of placing the taxpayer in a higher tax bracket. Periodic cuts, moreover, will usually be in accord with good forest management by maintaining the productivity of the stand. However, the tax rate

applicable to capital gains cannot exceed 26 percent of the profit on sales of standing timber held over 6 months.

6. *Under what conditions is there a maximum limit of 26 percent tax (formerly 25 percent) on long-term capital gains?*

Use of the alternative tax computation on separate schedule D means that under no circumstances can the tax amount to more than 26 percent of the excess of net long-term capital gain over net short-term capital loss. In effect this ceiling will reduce the tax of the larger taxpayer only (on a joint return if one-half the net income less one-half the exemptions exceeds \$14,000), since smaller taxpayers will be below the 26-percent limit.

7. *Can you handle the sale of timber under the capital gains treatment even though you do not treat your other income in this way?*
Yes.

8. *Does the income tax favor an owner who practices sustained yield operation?*

Not insofar as treatment of receipts is concerned, but provisions for expensing and capitalizing costs of forest ownership and operation do, in effect, encourage sustained yield operation.

9. *Is timber considered a long- or short-term investment?*

This will depend upon whether the timber has been held for more or less than 6 months.

10. *What is a long-term capital gain and what is a short-term capital gain?*

A long-term capital gain or loss results from the sale or exchange of a capital asset held for more than 6 months. A short-term capital gain or loss results from the sale or exchange of a capital asset held for 6 months or less.

11. *How should sale of land be treated when timber and land are sold together?*

The price received should be allocated on a reasonable basis between the two, and the recognized gain or loss on the land should be listed separately on Schedule D.

12. *Is timber growth taxable?*

Timber growth is not taxable as such. Increase in value of standing timber, whether due to growth or to market appreciation, is taxable at such time as the timber is sold or, in certain cases, when it is cut, but is not subject to income tax until that time.

13. *How should stumpage value be separated from returns due to labor in arriving at fair value of stumpage?*

The stumpage value should represent the price at which timber of comparable quality and location is currently selling as it stands uncut in the woods. The local district forester will usually be in a position to estimate the unit selling price for comparable timber.

14. *How should actual cost be allocated between timber, land, and buildings, when the property was bought substantially below (or above) fair market value?*

The actual amount paid for the property should be allocated over the timber, land, and buildings in the proportion that the fair market

value of each, as of the date of purchase, bears to the fair market value of the property as a whole, as of the date of purchase.

15. *How do you place a value upon timber as of its acquisition date?*

The volume of merchantable timber standing on the tract as of its acquisition date should be estimated and a fair unit stumpage value applied. (See page 9.)

16. *How do you place a value upon timber cut for home use?*

The fair market value of the timber cut should be estimated as it stood in the woods on the first day of the taxable year. This value will be indicated by current sales of stumpage of comparable quality and location.

17. *What is the difference between depletion and depreciation?*

Depletion is the reduction or exhaustion of an asset such as timber or other natural resource. Depreciation is the wearing out of an asset due to service.

18. *Under what circumstances will it pay a timber owner to set up his lands upon a depletion basis?*

Land is not subject to depletion for income tax purposes. All timber owners should establish the cost or other basis for depletion of their timber in order that the depletion allowance may be determined at such time as timber is sold or cut.

19. *What is meant by the basis for depletion or "basis" of a timber holding? What is meant by the adjusted basis? Suppose the property was not acquired by purchase.*

The basis for depletion represents the original capital investment in the property. The adjusted basis will reflect increases in the capital investment (as a result of acquiring additional timber or capitalizing costs) or decreases (as a result of recovering the capital investment through depletion allowances). If not acquired by purchase, the basis is determined as explained on page 9.

20. *What is the basis for depletion of a plantation?*

The actual cost to the taxpayer of establishing the plantation plus any carrying charges that have been properly capitalized.

21. *What is the basis for depletion of a stand that has resulted from natural reseeding of an idle field?*

Unless carrying charges or other costs have been capitalized, the basis for depletion will be zero.

22. *What is the depletion unit and what is the depletion allowance?*

The depletion unit is found by dividing the basis or adjusted basis of the timber by the total number of units (board feet, cords, etc.) in the timber account. The depletion allowance is found by multiplying the number of units sold or cut during the year by the depletion unit.

23. *What is species or selective depletion?*

The calculation of the depletion allowance separately for particular species, groups of species, or quality classes rather than for the timber as a whole.

24. *How can a farmer calculate the depletion allowance when cutting fence posts, pulpwood, or dogwood bolts?*

The depletion allowance is calculated in the same way, irrespective of the nature of the forest products harvested. Species or selection depletion may, however, be adopted as explained in the answer to the preceding question. Volumes should be converted to the same unit (such as board feet or cords) used in the timber account. If necessary your district forester can be asked to supply conversion factors.

25. *Is the depletion unit or the depletion allowance calculated differently in the case of selective cutting than in the case of clear-cutting?*

The same method applies in either situation.

26. *Are you allowed to claim a depletion allowance when your basis for depletion has been fully recovered?*

No. Once the cost or other basis has been fully recovered, the taxpayer has secured a return of his capital investment in the timber and no further depletion may be taken.

27. *Should a timber owner claim a depletion allowance when making an improvement cut or when thinning his stand?*

Depletion is not taken in the case of unmerchantable thinnings. When merchantable products having a "basis" are cut, depletion should be claimed, but the cutting may be deferred if you want to maintain the basis for depletion with a view to claiming depletion allowance, and so reducing the taxable gain at time of future harvest. Depletion should be claimed when merchantable timber is cut and cannot be deferred beyond the year of the cutting. If thinnings are of low grade, the depletion rate may be reduced pro rata in accordance with the actual value.

28. *When should land, on which timber has been cut, be depreciated?*

Land is not subject to depreciation at any time, although some land improvements such as bridges or fences may be depreciated.

29. *If depreciation is not taken in a given year may it be taken later?*

No. Depreciation not taken for the year when allowable is in effect forfeited as a deduction from income, and allowances claimed in later years may not be increased to include such depreciation.

30. *What is meant by a section 117 (k) (1) situation?*

This section of the Internal Revenue Code refers to the situation in which a timber owner cuts timber held more than 6 months, for sale or for use in his business (such as farming). The increase in value up to the beginning of the year in which the cut is made may be treated as a capital gain, but the increase in value due to processing must be reported as ordinary income. (See pages 16-18.)

31. *If a farmer cuts his own timber and sells the rough lumber, does he have to pay tax on the net profit or is it considered a capital gain?*

This situation is covered by section 117 (k) (1). The cutting of the timber can be thought of as a sale of the timber by the owner to himself at the price prevailing on the first day of the taxable year. The increase in value up to this point may then be treated as a capital gain. The net profit from sale of products is taxed as ordinary income.

32. *If timber is felled and the resulting logs are sold during the same year, must the transaction be reported in full in that year? If the logs were sold in a later year, what would be the status of the sale as well as of the inventory?*

In accordance with section 117 (k) (1) the capital gain up to the beginning of the year in which the cut is made is reported for that year. If the resulting logs are sold during the same year, the increase in value up to time of sale, minus processing and other costs, is reported as ordinary income for that year. If the logs are not sold by the end of the tax year, the stumpage value at time of cutting (used in determining the capital gain up to that point) is taken as the "cost" of the timber cut. This cost plus processing costs will then be the year-end inventory value.

33. *Is a timber owner likely to find it a hardship to continue using the capital-gains provision after electing to do so in a year when he has cut a large volume of timber?*

This should not prove burdensome, since the timber owner will already have set up his timber depletion account, and calculation of the depletion allowance would in any case be necessary if the ordinary income method were used. Moreover, the timber owner will be accustomed to the requirement relating to establishment of fair market value and to use of Schedule D.

34. *What is meant by a section 117 (k) (2) situation?*

This section of the Internal Revenue Code permits the taxpayer to claim capital gains treatment when timber held more than 6 months is sold under a pay-as-cut contract (see numbered paragraph 3 on page 14).

35. *Is it possible (and legal) to have prior agreement to sell timber on a scale basis, receiving payment as the timber is cut, and still use the capital gains treatment?*

Yes. This situation is covered by section 117 (k) (2).

36. *What are the two ways of treating costs of forest ownership and operation?*

Costs may either be expensed or capitalized.

37. *What is meant by expensing costs?*

Costs that are expensed are deducted from gross income for the year in which they were paid or incurred.

38. *What is meant by capitalizing costs?*

Costs that are capitalized are added to the basis or adjusted basis of the property and are recovered through depletion (in the case of timber) or through depreciation (in the case of equipment and other depreciable assets).

39. *Is it necessary to wait until timber harvest before deducting any or all expenses?*

No. Costs that are expensed may be deducted year by year from gross income. Costs that are capitalized, on the other hand, cannot be recovered until timber harvest.

40. *When do you have a choice between expensing and capitalizing costs of forest ownership and operation?*

Carrying charges and development expenditures allowable by law as deductions from income may be either expensed or capitalized as the taxpayer may choose, provided the practice is consistent from year to year.

41. *What costs may be expensed?*

Ordinary and necessary operating expenses if reasonable in amount and if paid or incurred during the taxable year. Also carrying charges, development expenditures, and depreciation allowances.

42. *Is a taxpayer permitted to deduct as an expense the value of his own labor?*

No.

43. *Can the expense of timber stand improvement such as poisoning, girdling, and removal of undesirable hardwood trees be deducted from taxable income?*

Yes. Development expenditures such as those for timber stand improvement may be expensed or they may be capitalized, but the practice adopted should be followed consistently.

44. *What costs must be capitalized?*

Those incurred for the acquisition of property having a useful life of more than 1 year and for permanent improvements or betterments to such property; also the cost of preparing land for seeding and planting.

45. *Can a landowner obtain a tax deduction for reforesting idle land?*

Costs of seeding and planting including labor are capitalized and may be recovered through future depletion; such costs cannot be expensed.

46. *How do you determine damage done to your timber by fire or other casualty?*

The local district forester can be asked to estimate the volume of timber damaged and its salvage value on the stump.

47. *Is the recognized loss following a fire or other casualty the difference between the sound value of the timber before the casualty and its damaged value afterwards?*

No. The loss recognized for tax purposes in the case of timber intended for sale or use in your business, will be the amount of your investment in the timber (the basis for depletion) less the salvage value and any insurance or other recoveries.

48. *Can a tax deduction be claimed for loss of future growth following a fire?*

No.

PROBLEMS

NUMBER 1

Smith made an outright sale of timber (lump sum basis) for \$800 in 1952. This was the first income that he had received from his timber since he purchased the property in 1915. The original purchase price did not include a timber value since there was no merchantable timber on the tract when acquired. Smith paid

general property taxes varying from 4 to 16 cents per acre over the 37-year period and deducted these year by year from his ordinary income when filing his income tax return. He had incurred no other carrying charges and had made no expenditures for development of his timber. How much of the \$800 that Smith received is taxable? Should it be treated as ordinary income or as a capital gain?

The entire amount should be reported on separate Schedule D as a long-term capital gain. Since Smith can allocate no part of the original purchase price to his timber and since he has not capitalized any costs, he has no basis for depletion and can claim no depletion allowance. If Smith had elected to capitalize his property taxes rather than to expense them year by year, he could deduct from his \$800 proceeds such part of the capitalized taxes as relate to the timber sold.

NUMBER 2

Jones sold 26,500 board feet of timber in 1952 under a pay-as-cut contract for \$30 per M board feet, or \$795 in all. Fee for timber cruise and other expenses of sale brought the net proceeds down to \$740. The farm had been bought in 1940 for \$6,500. How should Jones calculate the tax on his timber sale?

In order to determine his basis for depletion, Jones must allocate a reasonable portion of the purchase price to his timber. The farm had a total of 104 acres of which 23 acres were in timber. The buildings at time of purchase had been in very poor condition. A reasonable allocation was made as follows after taking into consideration sales of similar farms in the same general area:

Buildings and improvements-----	\$1, 500
Land-----	3, 000
Timber-----	2, 000
	6, 500

The timber sold was estimated to represent roughly 25 percent of the total merchantable volume at time of purchase, so that a depletion allowance of \$500 (one-quarter of \$2,000) was claimed. The recognized gain was then:

Gross sales price-----	\$795
Less expenses of sale-----	55
	\$740
Less depletion allowance-----	500
	240

The \$240 should be compared with other gains and losses as listed on pages 14-15 and then entered on separate Schedule D.

NUMBER 3

A widow in Wisconsin acquired two timber tracts, by inheritance from her husband in 1931. In 1944 the timber, amounting to 250,000 board feet of hardwoods, was sold outright (lump sum basis) for \$1,600, or the equivalent of \$6.40 per M board feet. The depletion allowance will depend upon the value of the timber as of the date of death. How should this be calculated?

The analysis that follows is more detailed than would be required in many cases, but is included as a guide to show the approach that a forester might use.

According to the purchaser-logger, the trees averaged about 17 inches in diameter at breast height. Trees of this size usually yield about 2 16-foot logs and would have a volume of 182 board feet by the Scribner log rule. On this basis, 250,000 board feet, log scale, the total volume sold would have been represented in 1,374 trees. The logger estimated that the total volume harvested in 1944 was distributed by species as follows:

	<i>Board feet</i>
Sugar maple-----	125, 000
Red oak, basswood, and soft elm-----	125, 000
	250, 000

Sugar maple in the Upper Mississippi Valley Region grows at an average rate of 1.1 inches in diameter, inside bark, in 10 years. The growth for 13 years thus would be $1.1 \times 1.3 = 1.43$ inches. The diameter breast high, outside bark = 109 percent of the diameter breast high, inside bark. It follows that sugar maples which measured 17 inches in diameter on the stump in 1944 were 15.60 inches in diameter at breast height, inside bark (17 divided by 1.09). This latter figure—15.60 inches—minus the growth (1.43 inches) gives the diameter, inside bark (14.17 inches) 13 years ago. By multiplying 14.17 by 109 percent we obtain the diameter, outside bark, at breast height of the trees 13 years ago. This amounts to 15.44 inches or to the nearest half inch, $15\frac{1}{2}$ inches. The corresponding volume figures are: 17-inch tree (1944) = 182 board feet; $15\frac{1}{2}$ -inch tree (1931) = 148 board feet.

Red oak, basswood, and soft elm grow at an estimated rate of 1.50 inches per 10 years, or 1.95 inches in 13 years. The diameter at breast height, outside bark, for these three species = 110 percent of the corresponding diameter, inside bark. Using the same method of computation as for sugar maple, we obtain:

17 inches d. b. h. (1943) = 15.45 inches (diameter inside bark, 1944)
1.10

15.45 inches minus 1.95 inches (13-year growth) equals 13.50 inches. Diameter inside bark at breast height in 1931 13.50 inches multiplied by 110 percent = 14.85 inches or to the nearest half-inch, 15 inches. This is the diameter outside bark in 1931. The corresponding volume figures per tree are: 17-inch tree (1944) = 182 board feet; 15-inch tree (1931) = 137 board feet.

Valuation of timber sold:

	<i>Board feet</i>
Volume of sugar maple—	
In 1944 equals 687 trees times 182 board feet.....	125, 000
In 1931 equals 687 trees times 148 board feet.....	101, 676
Accrual in growth.....	23, 324
Volume of red oak, basswood, and elm—	
In 1944 equals 687 trees times 182 board feet.....	125, 000
In 1931 equals 687 trees times 137 board feet.....	94, 119
Accrual in growth.....	30, 881
Volume of all species (maple, oak, elm, and basswood)—	
In 1944 equals 1,374 trees times 182 board feet.....	250, 000
Total growth since 1931.....	54, 205
Volume of timber cut in 1944 present in same trees in 1931.....	195, 795
Value of timber acquired by inheritance in 1931—	
195,795 board feet $\times$ \$4.00 per M ¹ = \$783.18. This is the depletion allowance.	

The recognized gain on sale of the timber amounts to the difference between \$1,600 (the gross sales price) and \$783.18 (the depletion allowance, or \$816.82. This should be reported on separate Schedule D as a long-term capital gain.

NUMBER 4

An elderly couple had a choice of selling the stumpage from their woodland or operating the timber themselves and selling the products. They chose to

¹ The average stumpage price in the Lake States region during the period 1923–1931 was \$6.16 according to an article by Henry B. Steer, "Relation of Stumpage and Log Prices to Other Commodity Prices," published in the *Journal of Forestry* in 1933 (vol. 31, pp. 783–795). The above figure is considered a safe average to use in this instance—with this difference: the 1944 sale price was \$6.40 as against a community average of \$10.00. The reason for this lower-than-average figure was attributed to the especially bad logging chance on a portion of the area cut over, and to the small size of the tract in question. Under the circumstances, it seems logical to place the 1931 valuation at a level of about 65% of the 1923–1931 unit value, i. e., \$6.16 times 65% = \$4.00 per M. In other words, the same factors which rendered the timber of less-than-average value in 1944 would have prevailed in 1931 as well.

harvest the timber themselves. Being unable to work in the woods, they had to hire all the work done at a total cost of \$946.17. They cut 32,695 board feet of saw and veneer logs, 1,781 tie cuts, and 950 board feet of aspen logs, and realized a total of \$3,044.79. How should their income tax be calculated?

Expenses:

Felling and bucking—	
32,695 board feet at \$3.75 per M-----	\$122.61
1,781 tie cuts at 18¢ per tie-----	320.58
950 board feet of aspen at \$3.75 per M-----	3.56
Skidding—	
32,695 board feet at \$3.50 per M-----	114.43
1,781 tie cuts at 12¢ per tie-----	213.72
950 board feet at \$3.50 per M-----	3.33
Reskidding for loading-----	29.13
Shelter barn for horses-----	66.05
Telephone calls-----	5.15
Insurance-----	67.61
	946.17

Revenue from products sold:

21,990 board feet veneer logs at \$58 per M-----	1,275.42
10,705 board feet sawlogs at \$35 per M-----	374.68
1,781 tie cuts at 70¢ per cut-----	1,246.70
950 board feet aspen logs at \$25.25 per M-----	23.99
Fuel from tops-----	124.00
	3,044.79

The couple elected to use the procedure provided by section 117 (k) (1) so that the tax is calculated in two parts: (a) The increase in value of the stumpage up to the beginning of the year in which the cut was made, and (b) the increase in value from time of cutting to sale of products.

(a) The increase in value of the stumpage up to time of cutting:

The fair market value of the stumpage cut as of the first day of the taxable year, was determined to be as follows:

32,695 board feet veneer logs and sawlogs at \$25 per M-----	\$817.38
1,781 tie cuts at \$0.35 per cut-----	623.35
950 board feet aspen at \$5 per M-----	4.75
	1,445.48

The depletion allowance was calculated as follows:

32,695 board feet veneer logs and sawings
71,240 board feet tie cuts (at 40 board feet per cut)
950 board feet aspen

104,885 board feet total cut.

Assuming a depletion unit of \$5 per M board feet, the depletion allowance is 104,885 board feet times \$5----- 524.43

Gain in value of stumpage----- 921.05

(b) The increase in value from time of cutting to sale of products:

Revenue from products sold-----	3,044.79
"Cost" of products (the fair stumpage value)-----	\$1,445.48
Expenses for felling, bucking, skidding, etc-----	946.17
	2,391.65

Gain from processing----- 653.14

The net effect of using the procedure provided by section 117 (k) (1) has been to secure the advantage of capital gains¹ treatment on \$921.05 and to pay at ordinary income rates on only \$653.14.

¹ Assuming that aggregate gains exceed aggregate losses in the comparison illustrated on page 15.

Revenue received from products sold-----	\$3, 044. 79
Less depletion allowance-----	\$524. 43
Expenses-----	946. 17
	<u>1, 470. 60</u>
Total gain-----	<u>1, 574. 19</u>
Taxed as capital gain-----	921. 05
Taxed as ordinary income-----	653. 14
	<u>1, 574. 19</u>

NUMBER 5

A young farmer is pruning and thinning in his 30-year-old stand. He has other management costs such as fencing, firebreaks, taxes, etc. Thirty years from now he may clear-cut. When and how should he report his expenses over the 30-year period?

The costs of firebreak construction and of fencing are regarded as capital improvements and should accordingly be capitalized. A permanent graded firebreak is not regarded as a depreciable or depletable asset. The expenditure for fencing, on the other hand, can be recovered over its useful life by means of a depreciation allowance.

The costs of pruning and thinning (less the proceeds of merchantable products), taxes, firebreak maintenance and other carrying charges, and development expenditures may either be expensed (deducted year by year as paid or incurred) or capitalized at the option of the taxpayer, provided a consistent practice is followed.

NUMBER 6

A Christmas tree grower recently suffered a serious fire and lost 2,500 trees, worth 50 cents each on the stump. This year he had no mature trees to sell. Can he claim a deduction for the trees destroyed by fire?

The owner's capital investment (basis for depletion) allocable to the trees destroyed, less any salvage or insurance recovery, is recognized as a loss and may be entered on Schedule D.

KEY FOR READY REFERENCE TO TAXPAYER'S SITUATION

Sales of standing timber:

Timber held 6 months or less—	<i>Page</i>
Sale outright-----	14
Sale under pay-as-cut contract-----	3
Timber held more than 6 months—	
Sale outright-----	14
Sale under pay-as-cut contract-----	14

Cutting of timber:

Timber held 6 months or less-----	3
Timber held more than 6 months-----	16

Sales of forest products:

Products derived from cutting of timber-----	3, 17
Products derived from standing tree-----	4

APPENDIX

EXHIBIT A

FORM 1040
U. S. Treasury Department
Internal Revenue Service

U. S. INDIVIDUAL INCOME TAX RETURN FOR CALENDAR YEAR 1952

1952

or taxable year beginning, 1952, and ending, 195.....		Do not write in these spaces
Name (PLEASE PRINT. If this is a joint return of husband and wife, use first names of both)		Serial No.
HOME ADDRESS (PLEASE PRINT. Street and number or rural route)		(Cashier's Stamp)
(City, town, or post office)	(Postal zone number)	(State)
Social Security No.		Occupation

Your exemptions	1. List your name. If your wife (or husband) had no income, or if this is a joint return, list also her (or his) name.		Check below if at the end of your taxable year you or your wife were—		On lines A. and B. below—	
	A. _____		65 or over ☐ Blind ☐		If neither 65 nor blind write the figure 1	
	B. (Your wife's name—do not list if exemption is claimed on another return) _____		65 or over ☐ Blind ☐		If either 65 or blind write the figure 2	
	C. List names of your children (including stepchildren and legally adopted children) with 1952 gross incomes of less than \$600 who received more than one-half of their support from you in 1952. See Instructions.		_____		If both 65 and blind write the figure 3	
	D. Enter number of exemptions claimed for close relatives listed in Schedule I on page 2		_____		Number of exemptions for you	
Your income	E. Enter total number of exemptions claimed in A to D above		_____		Number of her (or his) exemptions	
	2. Enter your total wages, salaries, bonuses, commissions, and other compensation received in 1952, before payroll deductions. Persons claiming traveling or reimbursed expenses, see Instructions.					
	Print Employer's Name		Where Employed (City and State)		Total Wage	Income Tax Withheld
	_____		_____		\$	\$
	_____		_____		\$	\$
How to figure the tax	3. If you received dividends, interest, or any other income, give details on page 2 and enter the total here		Enter total →		\$	
	4. Add income shown in items 2 and 3, and enter the total here					
	(Before figuring your tax, see Schedule J for "Head of Household." If you claim such status, check here ☐ .)					
	IF YOUR INCOME WAS LESS THAN \$5,000.—Use the tax table on page 4 unless you itemize deductions. The table allows about 10 percent of your income for charitable contributions, interest, taxes, medical expenses, etc. If your deductions exceed 10 percent, it will usually be to your advantage to itemize them and compute your tax on page 3.					
	IF YOUR INCOME WAS \$5,000 OR MORE.—Compute tax on page 3. Use standard deduction or itemize deductions, whichever is to your advantage.					
Tax due or refund	5. (A) Enter your tax from table on page 4, or from line 13, page 3. \$		(B) Enter your self-employment tax from line 35, separate Schedule C. \$		Enter total here → \$	
	6. How much have you paid on your 1952 income tax?					
	(A) By tax withheld (in item 2, above). Attach Original Forms W-2. \$		(B) By payments on 1952 Declaration of Estimated Tax (include any overpayment on your 1951 tax not claimed as a refund) \$		Enter total here → \$	
	7. If your tax (item 5) is larger than payments (item 6), enter balance of tax due here. This balance must be paid in full with return. \$					
	8. If your payments (item 6) are larger than your tax (item 5), enter the overpayment here. \$					
Enter amount of item 8 you want \$		(Refunded)		(Credited on 1953 estimated tax)		

Do you owe any prior year Federal tax for which you have been billed? (Yes or No) Is your wife (or husband) making a separate return for 1952? (Yes or No) If "yes," write her (or his) name

If you have filed a return for a prior year, state latest year Where filed?

To which director's (formerly collector's) office did you pay amount claimed in item 6 (B), above?

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is a true, correct, and complete return.

(Signature of person, other than taxpayer, preparing this return)	(Date)	(Signature of taxpayer)	(Date)
(Name of firm or employer, if any)		(Signature of taxpayer's wife or husband if this is a joint return)	

◆ To assure split-income benefits, husband and wife must include all their income and, even though only one has income, BOTH MUST SIGN.

EXHIBIT A—Continued

Schedule A.—INCOME FROM DIVIDENDS				Page 2			
Name of corporation declaring dividend	Amount	Name of corporation declaring dividend	Amount				
	\$		\$				
Enter total here—>				\$			
Schedule B.—INCOME FROM INTEREST							
Name of payer	Amount	Name of payer	Amount				
	\$		\$				
Enter total here—>				\$			
Schedule C Summary.—PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION, FARMING, AND PARTNERSHIP							
1. Business profit (or loss) from separate Schedule C, line 23.....				\$			
2. Farm profit (or loss) from separate schedule, Form 1040F.....							
3. Partnership, etc., profit (or loss) from Form 1065, Schedule K, Column 3.....							
4. Total of lines 1, 2, 3..... (Partnership name) (Address)				\$			
5. Less: Net operating loss deduction (attach statement).....							
6. Net profit (or loss) (line 4 less line 5).....				\$			
Schedule D.—NET GAIN OR LOSS FROM SALES OR EXCHANGES OF CAPITAL ASSETS, ETC.							
1. From sale or exchange of capital assets (from separate Schedule D).....							
2. From sale or exchange of property other than capital assets (from separate Schedule D).....							
Schedule E.—INCOME FROM ANNUITIES OR PENSIONS							
1. Cost of annuity (amount you paid).....				\$			
2. Cost received tax-free in past years.....							
3. Remainder of cost (line 1 less line 2).....				\$			
4. Amount received this year.....				\$			
5. Excess of line 4 over line 3.....							
6. Enter line 5, or 3 percent of line 1, whichever is greater (but not more than line 4).....							
Schedule F.—INCOME FROM RENTS AND ROYALTIES							
1. Kind and location of property	2. Amount of rent or royalty	3. Depreciation or depletion (explain in Schedule H)	4. Rentals (attach statement)	5. Other expenses (attach statement)			
	\$	\$	\$	\$			
1. Totals.....	\$	\$	\$	\$			
2. Net profit (or loss) (column 2 less sum of columns 3, 4, and 5).....							
Schedule G.—INCOME FROM ESTATES AND TRUSTS AND OTHER SOURCES							
1. Estate or trust..... (Name) (Address)							
2. Other sources (state nature).....							
Total income (or loss) from above sources (Enter here and as item 3, page 1).....				\$			
Schedule H.—EXPLANATION OF DEDUCTION FOR DEPRECIATION CLAIMED IN SCHEDULE F							
1. Kind of property (if buildings, state material of which constructed). Exclude land and other nondepreciable property	2. Date acquired	3. Cost or other basis	4. Depreciation allowed (or allowable) in prior years	5. Remaining cost or other basis to be recovered	6. Life used in accumulating depreciation	7. Estimated life from beginning of year	8. Depreciation allowable this year
		\$	\$	\$			\$
Schedule I.—EXEMPTIONS FOR CLOSE RELATIVES—(See instructions)							
1. Name of dependent relative. Also give address if different from yours		2. Relationship	3. Did dependent during 1952—			4. If answer to either 3(b) or 3(c) is "No" enter amount spent for dependent's support in 1952 by—	
			(a) Have gross income of \$500 or more?	(b) Reside in your home?	(c) Receive entire support from you?		
						You (and your wife if this is a joint return) \$	
						Others, and by dependent from own funds \$	
Enter here and as item 1D, page 1, the number of close relatives claimed above							
Schedule J.—HEAD OF HOUSEHOLD (See instructions)							
(Not applicable where wife or husband died during taxable year)							
1. Were you unmarried (or legally separated) at the close of your taxable year? (Yes or No).....				3. Did you furnish more than one half of the cost of maintaining the household during the taxable year? (Yes or No).....			
2. Did any person for whom you are entitled to an exemption, or your unmarried child, grandchild, or stepchild, even though not a dependent, share during your entire taxable year your home which was your principal residence? (Yes or No).....				If you did not furnish the entire cost, state total amount furnished by you \$..... by all others (including those sharing your home) \$.....			
List name(s) and relationship to you.....				4. If all of the above questions are answered "Yes," you may determine your tax as Head of a Household.			

EXHIBIT A—Continued

ITEMIZED DEDUCTIONS—FOR PERSONS NOT USING TAX TABLE ON PAGE 4 OR STANDARD DEDUCTION ON LINE 2 BELOW—

Page 3

If Husband and Wife (Not Legally Separated) File Separate Returns and One Itemizes Deductions, the Other Must Also Itemize

Describe Deductions and state to whom paid. If more space is needed, attach additional sheets.

Contributions		\$	
Allowable Contributions (not in excess of 20 percent of item 4, page 1).....		\$	
Interest		\$	
Total Interest.....			
Taxes		\$	
Total Taxes.....			
Losses from fire, storm, or other casualty, or theft		\$	
Total Allowable Losses (not compensated by insurance or otherwise).....			
Medical and dental expenses (if over 65 see Instructions)		\$	
Net Expenses (not compensated by insurance or otherwise).....		\$	
Enter 5 percent of item 4, page 1, and subtract from Net Expenses.			
Allowable Medical and Dental Expenses. See Instructions for limitation.....			
Miscellaneous (See Instructions)		\$	
Total Miscellaneous Deductions.....			
Total Deductions.....		\$	

TAX COMPUTATION—FOR PERSONS NOT USING TAX TABLE ON PAGE 4

1. Enter amount shown in item 4, page 1. This is your Adjusted Gross Income.....	\$	
2. If deductions are itemized above, enter total of such deductions. If deductions are not itemized and line 1, above, is \$5,000 or more: (a) married persons filing separately enter \$500, (b) all others enter 10 percent of line 1, but not more than \$1,000.....		
3. Subtract line 2 from line 1. Enter the difference here. This is your Net Income.....	\$	
4. Multiply \$600 by total number of exemptions claimed in item 1E, page 1. Enter total here.....		
5. Subtract line 4 from line 3. Enter difference here. (If line 1 includes partially tax-exempt interest, see Instructions).....	\$	
If line 5 is not more than \$2,000—		
6. Enter 22.2 percent of amount shown on line 5 and disregard lines 7, 8, and 9.....	\$	
If line 5 is more than \$2,000—		
7. And you are a single person, a married person filing separately, or a head of household— Single persons and married persons filing separately use Tax Rate Schedule I on page 12 of Instructions to figure tax on amount on line 5; heads of household use Tax Rate Schedule II.....	\$	
8. And you are filing a joint return— (a) Enter one-half of amount on line 5.....	\$	
(b) Use Tax Rate Schedule I on page 12 of Instructions to figure tax on amount on line 8 (a).....		
(c) Multiply amount on line 8 (b) by 2.....	\$	
9. If alternative tax computation is made, enter here tax from separate Schedule D.....	\$	
Disregard lines 10, 11, and 12, and copy on line 13 the same figure you entered on line 6, 7, 8 (c), or 9, unless you used itemized deductions		
10. Enter here any income tax payments to a foreign country or U. S. possession (attach Form 1116).....	\$	
11. Enter here any income tax paid at source on tax-free covenant bond interest.....	\$	
12. Add the figures on lines 10 and 11 and enter the total here.....	\$	
13. Subtract line 12 from line 6, 7, 8 (c), or 9. Enter difference here and as item 5 (A), page 1.....	\$	

EXHIBIT A—Continued

If you use this table, tear off this page and file only pages 1 and 2

Page 4

TAX TABLE FOR CALENDAR YEAR 1952

FOR PERSONS WITH INCOMES UNDER \$5,000 NOT COMPUTING TAX ON PAGE 3
 Read down the shaded columns below until you find the line covering the total income you entered in item 4, page 1. Then read across to the appropriate column headed by the number corresponding to the number of exemptions claimed in item 1E, page 1. Enter the tax you find there in item 5(A), Page 1.

And the number of exemptions claimed in item 1E, page 1, is—																				
1 2 3 4 or more																				
At least But less than																				
Single or a married person filing separately A head of a household Single or a married person filing jointly A married couple filing jointly																				
1 2 3 4 5 6 7 8 or more																				
Your tax is—																				
\$0	\$675	\$0	\$0	\$0	\$0	\$2,325	\$2,350	\$334	\$334	\$201	\$201	\$201	\$67	\$67	\$67	\$0	\$0	\$0	\$0	\$0
675	700	4	0	0	0	2,350	2,375	339	339	206	206	206	72	72	72	0	0	0	0	0
700	725	9	0	0	0	2,375	2,400	344	344	211	211	211	77	77	77	0	0	0	0	0
725	750	14	0	0	0	2,400	2,425	349	349	216	216	216	82	82	82	0	0	0	0	0
750	775	19	0	0	0	2,425	2,450	354	354	221	221	221	87	87	87	0	0	0	0	0
775	800	24	0	0	0	2,450	2,475	359	359	226	226	226	92	92	92	0	0	0	0	0
800	825	29	0	0	0	2,475	2,500	364	364	231	231	231	97	97	97	0	0	0	0	0
825	850	34	0	0	0	2,500	2,525	369	369	236	236	236	102	102	102	0	0	0	0	0
850	875	39	0	0	0	2,525	2,550	374	374	241	241	241	107	107	107	0	0	0	0	0
875	900	44	0	0	0	2,550	2,575	379	379	246	246	246	112	112	112	0	0	0	0	0
900	925	49	0	0	0	2,575	2,600	384	384	251	251	251	117	117	117	0	0	0	0	0
925	950	54	0	0	0	2,600	2,625	389	389	256	256	256	122	122	122	0	0	0	0	0
950	975	59	0	0	0	2,625	2,650	394	394	261	261	261	127	127	127	0	0	0	0	0
975	1,000	64	0	0	0	2,650	2,675	399	399	266	266	266	132	132	132	0	0	0	0	0
1,000	1,025	69	0	0	0	2,675	2,700	404	404	271	271	271	137	137	137	4	0	0	0	0
1,025	1,050	74	0	0	0	2,700	2,725	409	409	276	276	276	142	142	142	9	0	0	0	0
1,050	1,075	79	0	0	0	2,725	2,750	414	414	281	281	281	147	147	147	14	0	0	0	0
1,075	1,100	84	0	0	0	2,750	2,775	419	419	286	286	286	152	152	152	19	0	0	0	0
1,100	1,125	89	0	0	0	2,775	2,800	424	424	291	291	291	157	157	157	24	0	0	0	0
1,125	1,150	94	0	0	0	2,800	2,825	429	429	296	296	296	162	162	162	29	0	0	0	0
1,150	1,175	99	0	0	0	2,825	2,850	434	434	301	301	301	167	167	167	34	0	0	0	0
1,175	1,200	104	0	0	0	2,850	2,875	439	439	306	306	306	172	172	172	39	0	0	0	0
1,200	1,225	109	0	0	0	2,875	2,900	444	444	311	311	311	177	177	177	44	0	0	0	0
1,225	1,250	114	0	0	0	2,900	2,925	449	449	316	316	316	182	182	182	49	0	0	0	0
1,250	1,275	119	0	0	0	2,925	2,950	454	454	321	321	321	187	187	187	54	0	0	0	0
1,275	1,300	124	0	0	0	2,950	2,975	460	460	326	326	326	192	192	192	59	0	0	0	0
1,300	1,325	129	0	0	0	2,975	3,000	466	466	331	331	331	197	197	197	64	0	0	0	0
1,325	1,350	134	1	0	0	3,000	3,050	474	474	338	338	338	205	205	205	72	0	0	0	0
1,350	1,375	139	6	0	0	3,050	3,100	485	485	348	348	348	215	215	215	82	0	0	0	0
1,375	1,400	144	11	0	0	3,100	3,150	496	494	358	358	358	225	225	225	92	0	0	0	0
1,400	1,425	149	16	0	0	3,150	3,200	507	504	368	368	368	235	235	235	102	0	0	0	0
1,425	1,450	154	21	0	0	3,200	3,250	518	515	378	378	378	245	245	245	112	0	0	0	0
1,450	1,475	159	26	0	0	3,250	3,300	529	525	388	388	388	255	255	255	122	0	0	0	0
1,475	1,500	164	31	0	0	3,300	3,350	541	536	398	398	398	265	265	265	132	0	0	0	0
1,500	1,525	169	36	0	0	3,350	3,400	552	546	408	408	408	275	275	275	142	8	0	0	0
1,525	1,550	174	41	0	0	3,400	3,450	563	557	418	418	418	285	285	285	152	18	0	0	0
1,550	1,575	179	46	0	0	3,450	3,500	574	567	428	428	428	295	295	295	162	23	0	0	0
1,575	1,600	184	51	0	0	3,500	3,550	585	578	438	438	438	305	305	305	171	38	0	0	0
1,600	1,625	189	56	0	0	3,550	3,600	596	588	448	448	448	315	315	315	181	48	0	0	0
1,625	1,650	194	61	0	0	3,600	3,650	607	599	459	459	458	325	325	325	191	58	0	0	0
1,650	1,675	199	66	0	0	3,650	3,700	618	610	470	469	468	335	335	335	201	68	0	0	0
1,675	1,700	204	71	0	0	3,700	3,750	629	620	480	478	478	345	345	345	211	78	0	0	0
1,700	1,725	209	76	0	0	3,750	3,800	640	631	493	490	488	355	355	355	221	88	0	0	0
1,725	1,750	214	81	0	0	3,800	3,850	651	641	504	501	498	365	365	365	231	98	0	0	0
1,750	1,775	219	86	0	0	3,850	3,900	662	652	515	511	508	375	375	375	241	108	0	0	0
1,775	1,800	224	91	0	0	3,900	3,950	673	662	526	522	518	385	385	385	251	118	0	0	0
1,800	1,825	229	96	0	0	3,950	4,000	684	673	537	532	528	395	395	395	261	128	0	0	0
1,825	1,850	234	101	0	0	4,000	4,050	696	685	548	543	538	405	405	405	271	138	5	0	0
1,850	1,875	239	106	0	0	4,050	4,100	707	694	559	553	548	415	415	415	281	148	15	0	0
1,875	1,900	244	111	0	0	4,100	4,150	718	704	570	564	558	425	425	425	291	158	25	0	0
1,900	1,925	249	116	0	0	4,150	4,200	729	715	581	574	568	435	435	435	301	168	35	0	0
1,925	1,950	254	121	0	0	4,200	4,250	740	725	592	585	578	445	445	445	311	178	45	0	0
1,950	1,975	259	126	0	0	4,250	4,300	751	736	603	596	588	455	455	455	321	188	55	0	0
1,975	2,000	264	131	0	0	4,300	4,350	762	746	614	606	598	465	465	465	331	198	65	0	0
2,000	2,025	269	136	2	0	4,350	4,400	773	757	625	617	608	475	475	475	341	208	75	0	0
2,025	2,050	274	141	7	0	4,400	4,450	784	768	636	627	618	485	485	485	351	218	85	0	0
2,050	2,075	279	146	12	0	4,450	4,500	795	778	648	638	628	495	492	488	361	228	95	0	0
2,075	2,100	284	151	17	0	4,500	4,550	806	789	659	648	638	505	501	504	371	238	105	0	0
2,100	2,125	289	156	22	0	4,550	4,600	817	799	670	659	648	515	514	514	381	248	115	0	0
2,125	2,150	294	161	27	0	4,600	4,650	828	810	681	669	658	525	523	524	391	258	125	0	0
2,150	2,175	299	166	32	0	4,650	4,700	839	820	692	680	668	535	533	534	401	268	135	2	0
2,175	2,200	304	171	37	0	4,700	4,750	851	831	703	690	678	545	540	544	411	278	145	12	0
2,200	2,225	309	176	42	0	4,750	4,800	862	841	714	701	688	555	550	554	421	288	155	22	0
2,225	2,250	314	181	47	0	4,800	4,850	873	852	725	711	698	565	561	564	431	298	165	33	0
2,250	2,275	319	186	52	0	4,850	4,900	884	862	736	722	708	575	569	574	441	308	175	42	0
2,275	2,300	324	191	57	0	4,900	4,950	895	873	747	732	718	585	580	582	451	318	185	52	0
2,300	2,325	329	196	62	0	4,950	5,000	906	883	758	743	728	595	589	594	461	328	195	62	0

EXHIBIT B

FORM 1040 F
U. S. Treasury Department
Internal Revenue Service

SCHEDULE OF FARM INCOME AND EXPENSES

For Calendar Year 1952

1952

Attach This Form to Your
Income Tax Return Form
1040 and File It With the
Director (formerly Collector)
of Internal Revenue for Your
District.

Or taxable year beginning 1952, and ending 195

Name
Address
Location of farm or farms
Number of acres in each farm

If Your Accounts Are Kept on
a Cash Basis, Fill in Pages 1
and 3.

If You Keep Books on an
Accrual Basis and Desire to
Use This Form, Fill in Pages
2 and 3 Instead.

FARM INCOME FOR TAXABLE PERIOD COMPUTED ON CASH RECEIPTS AND DISBURSEMENTS BASIS

1. SALE OF LIVESTOCK RAISED			2. SALE OF PRODUCE RAISED			3. OTHER FARM INCOME	
Kind	Quantity	Amount	Kind	Quantity	Amount	Items	Amount
Cattle		\$	Grain		\$	Mdse. rec'd for produce ..	\$
Horses			Hay			Machine work	
Mules			Cotton			Hire of teams	
Sheep			Tobacco			Breeding fees	
Swine			Potatoes			Rent rec'd in crop shares ..	
			Sugar beets			Work off farm	
			Vegetables			Wood and lumber	
Chickens			Fruits			Other forest products	
Turkeys			Nuts			Agricultural program	
Ducks			Dairy products			payments	
Goats			Eggs			Patronage dividends, re-	
Bees			Meat products			bates or refunds, if	
Other			Poultry, dressed			not reported elsewhere	
(specify):			Wool and mo-			in return	
			hair			Other (specify):	
			Honey				
			Sirup and sugar				
			Other (specify):				
TOTAL		\$	TOTAL		\$	TOTAL	\$

(Enter on line 1 of summary below) (Enter on line 2 of summary below) (Enter on line 3 of summary below)

4. SALE OF LIVESTOCK AND OTHER ITEMS PURCHASED

1. Description	2. Date acquired	3. Gross sales price (contract price)	4. Cost or other basis	5. Depreciation allowed (or allowable) since acquisition or March 1, 1913	6. Profit (column 3 plus column 5 minus column 4)
		\$	\$	\$	\$
TOTAL (enter on line 4 of summary below)					\$

SUMMARY OF INCOME AND DEDUCTIONS COMPUTED ON A CASH RECEIPTS AND DISBURSEMENTS BASIS

1. Sale of livestock raised	\$	6. Expenses (from page 3)	\$
2. Sale of produce raised		7. Depreciation (from page 5)	
3. Other farm income		8. Other deductions (specify):	
4. Profit on sale of livestock and other items purchased			
5. GROSS PROFITS	\$	9. TOTAL DEDUCTIONS	\$
10. Net farm profit (or loss) (line 5 minus line 9) to be reported in Schedule C Summary, Form 1040	\$		

Page 2

[illegible]

SUMMARY OF INCOME AND DEDUCTIONS COMPUTED ON AN ACCRUAL BASIS

1. Inventory of livestock, crops, and products at end of year.....	\$.....	7. Expenses (from page 3).....	\$.....
2. Sales of livestock, crops, and products during year.....		8. Depreciation (from page 3).....	
2a. Other miscellaneous receipts (specify):		9. Other deductions (specify):	
3. TOTAL.....	\$.....		
4. Inventory of livestock, crops, and products at beginning of year.....	\$.....		
5. Cost of livestock and products purchased during year.....			
6. Gross profits (line 3 minus the sum of lines 4 and 5).....	\$.....	10. TOTAL DEDUCTIONS.....	\$.....
11. Net farm profit (or loss) (line 6 minus line 10) to be reported in Schedule C Summary, Form 1040.....		\$.....	

(Do not include personal or living expenses or expenses not attributable to production of farm income, such as taxes, insurance, repairs, etc., on your dwelling)

Page 3

1. Items	2. Amount	3. Items (Continued)	4. Amount (Continued)
Labor hired.....	\$.....	Rent of farm, part of farm, or pasture.....	\$.....
Feed purchased.....		Freight, yardage, express, and trucking.....	
Seed and plants purchased.....		Automobile upkeep (farm share).....	
Machine hire.....		Other farm expenses (specify):.....	
Supplies purchased.....			
Cost of repairs and maintenance.....			
Breeding fees.....			
Fertilizers and lime.....			
Veterinary and medicine for livestock.....			
Gasoline, other fuel and oil for farm business.....			
Storage and warehousing.....			
Taxes.....			
Insurance on property (except your dwelling).....			
Interest on farm notes and mortgages.....			
Water rent, electricity, and telephone.....			
TOTAL OF COLUMNS 2 AND 4 (enter on line 6 of summary on page 1 (cash basis) or line 7, page 2 (accrual basis)).....			
			\$.....

DEPRECIATION (See Instructions)[illegible]

EXHIBIT C

SCHEDULE C (Form 1040)
U. S. Treasury Department
Internal Revenue Service**PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION**

(For Computation of Self-Employment Tax, see Page 3)

1952

For Calendar Year 1952 or taxable year beginning _____, 1952, and ending _____, 195

Name and Address (from Form 1040)

(Partnerships and joint ventures should file on Form 1065)

(I) Principal business activity (see instructions) _____
 (Retail trade, wholesale trade, lawyer, etc.) (Principal product or service)

(II) Business name

(IV) Business address (see instructions) _____
 (Street and number or rural route) (City, town, post office) (County) (State)

(V) Were you the sole proprietor of this business in 1951? Yes ☐ No ☐. If "No," check whether this business in 1952 became a successor to a corporation ☐, a partnership ☐, another sole proprietorship ☐, or started as an entirely new business ☐. Where applicable, give name of such predecessor.

Do NOT include cost of goods withdrawn for personal use or deductions not connected with your business or profession

1. Total receipts from business or profession.....\$-----

COST OF GOODS SOLD

2. Inventory at beginning of year.....	\$-----	-----
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3. Merchandise bought for manufacture or sale.....	-----	-----	-----
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4. Cost of labor.....	-----	-----
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5. Material and supplies	-----	-----	-----
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6. Other costs (explain in Schedule C-2).....	_____	_____	_____
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7.	Total of lines 2 to 6.....	\$-----	-----
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8. Less inventory at end of year.....		
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9. Net cost of goods sold (line 7 less line 8).....		
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10. Gross profit (line 1 less line 9).....\$-----

OTHER BUSINESS DEDUCTIONS

11. Salaries and wages not included in line 4.....	\$.....	-----
--	---------	-------

12. Rent on business property.....	-----	-----
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13. Interest on business indebtedness	-----	-----
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14. Taxes on business and business property.....	-----	-----	
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15. Losses of business property (attach statement).....	-----	-----	-----
---	-------	-------	-------

16. Bad debts arising from sales or services.....	-----	-----
---	-------	-------

17. Depreciation and obsolescence (explain in Schedule C-1).	-----	-----	-----
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18. Repairs (explain in Schedule C-2).....	-----	-----	-----
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19. Depletion of mines, oil and gas wells, timber, etc. (submit schedule)	-----	-----	-----
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20. Amortization of emergency facilities (attach statement)	-----	-----	-----
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21. Other business expenses (explain in Schedule C-2).....

22.	Total of lines 11 to 21		
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23. Enter net profit (or loss) (line 10 less line 22). Also enter on line 24, page 3, and on line 1,

Schedule C Summary, Form 1040	\$	
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Schedule C-1. EXPLANATION OF DEDUCTION FOR DEPRECIATION CLAIMED ON LINE 17[illegible]**Schedule C-2. EXPLANATION OF LINES 6, 18, AND 21**[illegible]

EXHIBIT D

SCHEDULE D (Form 1040)
U. S. Treasury Department
Internal Revenue Service

GAINS AND LOSSES FROM SALES OR EXCHANGES OF PROPERTY**1952**

For Calendar Year 1952 or taxable year beginning, 1952, and ending, 195....

Name and address

(1) CAPITAL ASSETS

10-67109-1

1. Kind of property (if necessary, attach statement of descriptive details not shown below)	2. Date acquired Mo. Day Year	3. Date sold Mo. Day Year	4. Gross sales price (contract price)	5. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (attach schedule)	6. Cost or other basis and cost of subsequent improvements (if not purchased, attach explanation)	7. Expense of sale	8. Gain or loss (column 4 plus column 5 less sum of columns 6 and 7)
SHORT-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD NOT MORE THAN 6 MONTHS							
1.			\$	\$	\$	\$	\$
2. Enter your share of net short-term gain or loss from partnerships and common trust funds							\$
3. Enter unused capital loss carry-over from 5 preceding taxable years (attach statement)							\$
4. Enter sum of short-term gains or losses or difference between short-term gains and losses shown above. \$							\$
LONG-TERM CAPITAL GAINS AND LOSSES—ASSETS HELD FOR MORE THAN 6 MONTHS							
5.			\$	\$	\$	\$	\$
6. Enter the full amount of your share of net long-term gain or loss from partnerships and common trust funds							\$
7. Enter sum of long-term gains or losses or difference between long-term gains and losses shown above. \$							\$
							Gain or loss to be taken into account
							(a) Gain
							(b) Loss
8. Enter net short-term gain or loss from line 4.							\$
9. Enter net long-term gain or loss from line 7.							\$
Use lines 10 through 13 only if gains exceed losses in lines 8 and 9.							
10. Enter short-term gain (line 8, col. a) reduced by any long-term loss (line 9, col. b) ..							\$
11. Enter long-term gain (line 9, col. a) reduced by any short-term loss (line 8, col. b) ..							\$
12. Enter 50 percent of line 11.							\$
13. Enter here and on line 1, Schedule D, page 2, Form 1040, the sum of lines 10 and 12 ..							\$
Use lines 14 and 15 only if losses exceed gains in lines 8 and 9.							
14. Enter the excess of losses over gains on lines 8 and 9.							\$
15. Enter here and on line 1, Schedule D, page 2, Form 1040, the smallest of the following: (a) the amount on line 14; (b) net income computed without regard to capital gains and losses; or (c) \$1,000.							\$

COMPUTATION OF ALTERNATIVE TAX

Use only if you had a net long-term capital gain or an excess of net long-term capital gain over net short-term capital loss, and line 5 or 8(a), page 3, Form 1040, exceeds \$14,000

16. Enter from page 3, Form 1040, the income from line 5 if separate return or line 8 (a) if joint return.	\$
17. Enter amount from line 12, col. a, if separate return or half of such amount if joint return	\$
18. Balance (line 16 less line 17)	\$
19. Enter tax on amount on line 18 (use appropriate Tax Rate Schedule in Form 1040 Instructions) ..	\$
20. If joint return, multiply amount on line 19 by two.	\$
21. Enter 52 percent of amount on line 17.	\$
22. If joint return, multiply amount on line 21 by two.	\$
23. Alternative tax (line 19 plus line 21 if separate return; line 20 plus line 22 if joint return)	\$
24. Enter tax from page 3, Form 1040 (either line 7, or line 8 (c), whichever is applicable)	\$
25. Tax liability (line 23 or 24, whichever is smaller). Enter here and also on line 9, page 3, Form 1040.	\$

(2) PROPERTY OTHER THAN CAPITAL ASSETS

c2

1. Kind of property	2. Date acquired Mo. Day Year	3. Date sold Mo. Day Year	4. Gross sales price (contract price)	5. Depreciation allowed (or allowable) since acquisition or March 1, 1913 (attach schedule)	6. Cost or other basis and cost of subsequent improvements (if not purchased, attach explanation)	7. Expense of sale	8. Gain or loss (column 4 plus column 5 less sum of columns 6 and 7)
1.			\$	\$	\$	\$	\$
2. Enter here the sum of gains or losses or difference between gains and losses shown above. Also enter on line 2, Schedule D, page 2, Form 1040							\$

EXHIBIT E**SAMPLE TIMBER STATEMENT FOR USE WITH SEPARATE SCHEDULE D***Sale of Timber*

1. (a) Description of property. Tract No. 1, 100 acres adjacent to home farm. Acquired March 1, 1940, by purchase from John Smith. Original cost of tract \$2,500 of which \$1,000 allocated to land acct. and \$1,500 allocated to timber acct. Tract estimated to have contained 300 M. board feet of merchantable second-growth pine timber at time of purchase.

(b) Description of timber sold. 60 M board feet of pine stumpage sold on lump sum basis to William Brown of Oakdale, sawmill operator.

6. Cost or other basis. (Here show the calculation of the depletion allowance. As given in the sample timber account page 13 this would be \$355.80. Sufficient detail should be given to support the allowance claimed.)

Cutting of Timber

1. (a) Description of property. (The information needed will be similar to that shown under Sale of Timber above.)

(b) Description of timber cut. 60 M board feet of pine cut for sale as logs. I claim gain (or loss) from the cutting of such timber in accordance with section 117 (k) (1) of the Internal Revenue Code.

4. Gross sales price. (Explain how you arrived at the estimated fair market value of the stumpage as of the first day of your taxable year. For example, "Recent sales of pine stumpage on neighboring tracts averaged \$9 per M board feet according to information furnished by District Forester. Fair market value of timber cut \$540 (60 M board feet at \$9 per M board feet)."

6. Cost or other basis. (Calculation of depletion allowance will be similar to that under Sale of Timber above.)

Loss of timber by fire

1. (a) Description of property. (The information needed will be similar to that shown under Sale of Timber above.)

(b) Description of timber burned. Five acres pine burned over. Average volume per acre 3,900 board feet or 19,500 board feet in all. Salvage value estimated by District Forester to average \$3 per M. (Letter from District Forester may be attached.)

6. Cost or other basis. (Here show calculation of depletion allowance similar to that under Sale of Timber above.)

EXHIBIT F**INCOME TAX ESTIMATED USEFUL LIVES AND DEPRECIATION RATES ¹****LUMBER AND WOOD PRODUCTS**

Where depreciation is computed on a physical-life basis, accounts set up vary from single items through all degrees of group or classified accounts to a single composite plant account; but commonly three broad classifications are used, their composite lives being about as follows:

	<i>Years</i>
Logging machinery and equipment-----	10-15
Sawmill machinery and equipment-----	20-25
Portable sawmills and equipment-----	10-12

¹ Adapted from Income Tax Depreciation and Obsolescence: Estimated Useful Lives and Depreciation Rates, Bulletin F (Revised 1942), U. S. Treasury Department. For sale by Superintendent of Documents, Washington 25, D. C. Price 30 cents.

LOGGING MACHINERY AND EQUIPMENT

	<i>Average useful life (years)</i>		<i>Average useful life (years)</i>
Arches_____	10	Power shovels_____	15
Big wheels, horse-drawn_____	5	Saws, power_____	3
Blacksmith shop_____	15	Skidders_____	20
Caterpillar tractors_____	5	Sleds, horse-drawn_____	5
Harness_____	5	Trucks:	
Horses and mules_____	6	Heavy_____	5
Log wagons, horse-drawn_____	5	Light_____	2
Logloaders_____	20		

SAWMILL MACHINERY AND EQUIPMENT

	<i>Average useful life (years)</i>		<i>Average useful life (years)</i>
Bandmills_____	25	Hogs_____	10
Burners_____	15	Live rolls_____	25
Circular mills:		Log carriage and feed_____	20
Portable, complete_____	15	Lumber buggies_____	10
Stationary_____	25	Lumber docks, open_____	12
Conveyor chains_____	10	Niggers and turners_____	20
Dry kilns:		Plumbing_____	25
Blowers_____	20	Saw filing machinery_____	15
Brick and concrete_____	40	Slashers_____	25
Frame_____	20	Sprinkler systems_____	40
Steam coils and piping_____	20	Surfacers_____	20
Edgers_____	25	Trimmers_____	25
Fire-protection equipment_____	10		

AGRICULTURE

On a composite basis, agricultural property is generally divided into buildings, taking approximately a 50-year average life, and machinery and equipment, taking a 15-year average life.

	<i>Average useful life (years)</i>		<i>Average useful life (years)</i>
Animals:			
Horses, breeding or work_____	10	Furrow openers, disk_____	15
Mules, work_____	10	Harness_____	7
Barrels, dip_____	6	Planters_____	15
Cables_____	8	Plows_____	15
Carts:		Pumps:	
Dump and farm_____	8	Bucket_____	22
Hand_____	5	Centrifugal or rotary_____	20
Covers, canvas_____	8	Plunger_____	15
Culverts:		Saws, circular_____	15
Masonry and cast-iron pipe_____	50	Sprayers_____	15
Galvanized corrugated iron_____	25	Tanks:	
Riveted steel_____	33	Turpentine_____	5
Cups, turpentine_____	5	Water—	
Cutters:		Steel_____	40
Rotary stump_____	20	Wood_____	20
Engines:		Watering_____	20
Gasoline_____	10	Tarpaulins_____	8
Diesel_____	15	Tractors_____	10
Stationary, steam_____	20	Vats, dipping_____	10
Fence machines_____	5	Wagon beds and racks_____	6
Fence posts, steel_____	30	Wagon gear—wood wheels_____	12
Fences:		Wagons:	
Wood_____	15	Light_____	12
Fencing, woven wire_____	15	Trucking, heavy duty_____	10
Forges, portable_____	12		

EXHIBIT G**BUREAU OF INTERNAL REVENUE****Income Tax Unit**

Washington 25, D. C.

INCOME TAX INFORMATION RELEASE NO. 1

December 28, 1949.

Turpentine Depletion

Ordinarily the basis for turpentine depletion is cost, although the basis of property acquired prior to March 1, 1913, or subsequently by inheritance for example, is generally the fair market value at March 1, 1913, or the fair market value at date of inheritance. A brief summary of the basis of property for purposes of depletion is hereinafter set forth.

In circumstances which require the determination of fair market value as of any given date, the value of the timber should first be determined. Of the value so determined, a reasonable amount may be allocated to the turpentine, taking into account the difference in value between round and turpented timber. If the basis is cost, and only the turpentine rights were purchased or leased, the basis is obviously the consideration paid, but if a tract of land is purchased in fee, it is necessary to allocate the total cost between the land, timber, and any other elements of value in proportion to the relative values involved. The total cost allocated to the timber may then be divided, on a reasonable basis, between the turpentine and wood products.

It should be noted that there ordinarily would be no basis either for the timber or the turpentine in the case of timber which has grown to merchantable size during the ownership of the taxpayer. In other words, timber growth, as such, does not give rise to any increased basis for the determination of gain or loss or depletion.

That portion of the total cost or other basis assigned to turpentine may be amortized or recovered through depletion deductions on any reasonable basis over the period of actual turpentinng.

In the case of lessees, the cost of the lease may be recovered during the period of the lease on the basis of the number of cups or crops worked each year, or on a time basis if the operations are approximately equal from year to year. In cases in which the lessee pays a percentage of his gross receipts to the lessor, the amount paid is a proper deduction from the gross income of the lessee.

In the case of lessors and owner-operators, the cost or other basis may be recovered over the period required to exhaust the turpentine. In determining the annual deductions, consideration may be given to the fact that the yield and value per cup is decreased somewhat as the height of chipping increases.

The following depletion table is suggested for the ordinary type of lease:

	Lease period (years)		
	4	5	6
	Percent	Percent	Percent
First year	30	30	30
Second year	30	25	25
Third year	25	20	20
Fourth year	15	15	10
Fifth year		10	10
Sixth year			5

In cases in which long-term leases are involved, for example, 11 years (6 years face and 5 years back-face), the following depletion table is suggested:

Face:	Percent	Back-face:	Percent
First year-----	10	Seventh year-----	10
Second year-----	10	Eighth year-----	10
Third year-----	10	Ninth year-----	10
Fourth year-----	9	Tenth year-----	9
Fifth year-----	8	Eleventh year-----	8
Sixth year-----	6		

In the case of lessors receiving income on a percentage basis, either in kind or in cash, an estimate of the total production or receipts from the particular lease should be made and depletion deducted in proportion to the actual receipts. Lessors receiving a lump-sum cash payment should claim as depletion the proportionate part of the basis for the year in which the payment is received. For example, if a three-year lease is made for a lump-sum cash payment, and it is expected that the lease will be renewed for another period or periods, the proportionate part of the basis should be applied to the first payment.

Basis for depletion:

In accordance with section 114 (b) (1) of the Internal Revenue Code, the basis for depletion is the basis prescribed in section 113 (a), adjusted as provided in section 113 (b).

The basis for individual owners may be briefly summarized as follows:

- (1) Fair market value as of March 1, 1913, if acquired prior to that date, unless cost or basis otherwise determined with proper adjustment to March 1, 1913, is higher.
 - (2) Cost, if acquired by purchase subsequent to March 1, 1913.
 - (3) Fair market value at date of acquisition (date of death of decedent) if acquired by bequest, devise, or inheritance.
 - (4) Fair market value at date of gift or transfer in trust prior to January 1, 1921.
 - (5) Basis to the donor, or the last preceding owner by whom it was not acquired by gift, if acquired by the present owner subsequent to December 31, 1920.
- In the case of corporate owners, reference should be made to section 113 of the Code.

Correspondence regarding this release should be addressed to the Commissioner of Internal Revenue, Washington 25, D. C., attention: Engineering and Valuation Division, Income Tax Unit.

E. I. McLARNEY,
Deputy Commissioner, Income Tax Unit.