Chapter 8. Casualties, Thefts, and Condemnations

If part or all of your timber is destroyed or stolen, or if your forest land is condemned for public use, you may be entitled to claim a deduction on your income tax return. These types of losses are termed involuntary conversions. To take a deduction, you need to know the kinds of losses that are deductible, the tax and business structure of your activity, how to determine the amount of loss recognized for tax purposes, and how to determine the type of deduction—capital or ordinary. The nature of the deduction also depends on your purpose for holding the timber. If, because of salvage operations, insurance recovery, or other compensation, the destruction, theft, or condemnation results in a gain, you must include the gain in your income, unless you elect to postpone reporting such gain as explained later in the chapter. The passive activity loss restrictions, discussed beginning on page 40, generally do not apply to casualty and theft losses.

Operating losses, discussed in Chapter 5, are created when expenses associated with a trade or business, or an investment activity, exceed income in a tax year. Such losses do not involve the involuntary conversion of property discussed in this section.

The three basic categories of involuntary losses—physical damage or destruction, theft, and condemnation—are discussed in this chapter. Note that under certain circumstances a deductible loss results from the destruction or damage to property held as part of a trade or business or for the production of investment income even if the loss is not caused by a "casualty." Because losses resulting from theft (sometimes referred to as "timber trespass") and condemnation of property for public use are treated similarly to casualty losses, the discussion focuses on casualty losses first. The unique aspects of thefts and condemnations are then discussed separately.

Discussion Limited to "Timber"

This publication discusses timber held for the production of income as either a business or investment. If your trees are held for personal use, such as residential shade trees, see IRS Publication 547, *Casualties, Disasters, and Thefts (Business and Nonbusiness)*.

Normal Losses Not Deductible

To be allowed as a deduction, a loss must be evidenced by a closed and completed transaction fixed by an event or identifiable events and must actually have been sustained during the tax year. Timber lost due to natural factors typically associated with timber stands, referred to as natural mortality, is not a casualty loss. Natural mortality includes trees killed due to overtopping by larger, faster growing trees; normal levels of disease and insect infestations; and low rainfall. Natural mortality is reflected in your timber volume accounts, as discussed on page 25. Physical losses of timber generally will come under the heading of casualties, that is, losses caused by natural or other external forces acting in a sudden, unexpected, and unusual manner. A sudden event is one that is swift, not gradual or progressive. An unexpected event is one that ordinarily is unanticipated and one that you do not intend. An unusual event is one that is not a day-to-day occurrence and one that is not typical for the activity in which you were engaged when the damage or destruction occurred.

Noncasualty Losses

A deductible noncasualty loss may result if the precipitating event is unusual and unexpected. The suddenness test does not have to be met. Circumstances generating noncasualty losses are contrasted with casualty losses in the discussion below.

Casualty Losses

Casualty losses include but are not limited to those resulting from fire, hurricane, or other events, such as windstorm, sleetstorm, and hail. Casualty losses also include destruction or damage from plane crashes, automobile accidents, and similar events.

Disease or Insect Infestation

Trees grown for timber that are killed by disease or insect infestation ordinarily do not result in a casualty loss. Losses resulting from a low level of pest incidence, usually present under normal conditions, are not deductible. If the trees killed are shade trees, the sudden, unexpected, and unusual damage resulting from the Southern pine beetle or other species of insects may be deductible as a casualty loss (see the summary of Revenue Ruling 79-174, page 143). In addition, some attacks of Southern pine beetles or other species of insects may result in an unexpected and unusual noncasualty loss of timber, which qualifies for deduction (see the summary of Revenue Ruling 87-59, page 144).

Drought Loss

A casualty loss usually does not result when trees being grown for timber are killed by drought. In some cases, however, drought losses may result in an unexpected and unusual noncasualty loss, which is deductible (see the summary of Revenue Ruling 90-61, page 144).

Combinations of Factors

Combinations of factors sometimes cause timber damage. A nondestructive fire may be followed by insect attack. Trees weakened by interior rot or characterized by shallow root systems may be uprooted or broken off as a result of repeated windstorms or may die as a result of drought. When combinations of factors are involved, it may be necessary to consider the length of time from the precipitating event to the eventual loss of the timber to determine the suddenness of the loss.

Salvage Requirement

Every reasonable effort should be made to salvage the affected timber. A reasonable effort includes offering the damaged timber for sale. You should use the same marketing procedures as for any other timber sale. The market value may, however, be lower depending on the extent of damage to the timber, the volume of damaged timber on the market, and increased harvesting costs. If you do not normally harvest your own timber, you would not be expected to do so in order to recover some of the value in damaged timber for which you cannot find a buyer. If you are not able to salvage the timber after making a bona fide attempt to do so and you claim a loss deduction, you should keep a record of your efforts in order to show that the timber was not salvageable.

When losses of this character are heavy but the timber is not salvageable, you should adjust your timber account to reflect the loss of timber volume as an offset against growth in computing the depletion unit.

Determining the Amount of Deductible Loss

In light of the decisions Westvaco Corp. versus United States, 639 F.2d 700 (Ct. Cl. 1980), and Weyerhaeuser versus United States, 92 F.3d 1148 (1996) (reversing in part and affirming in part), 32 Fed. Cl. 80 (1994) (certiorari denied), 519 U.S. 1091 (1997), the IRS has revoked Revenue Ruling 66-9 and Revenue Ruling 73-51 (see the summary of Revenue Ruling 99-56, page 143). Generally, if your timber is damaged or destroyed by fire or other casualty, your deductible loss is the diminution in value, limited by the allowable basis in the timber damaged or destroyed, less any insurance or other compensation received. Timber damaged, but not made unmerchantable, should be salvaged if possible. If a gain results from the salvage activity, there is no casualty loss with respect to the salvaged timber. Determine your gain or loss from the salvage cutting, sale, or other disposal as you would for timber sales in general.

Determining Volume of Timber Destroyed. To claim a loss deduction, the single identifiable property damaged or destroyed must be identified. The Court of Claims, in Westvaco versus United States, decided that the single identifiable property damaged or destroyed by storms and fires included all of the taxpayer's standing timber in the district (block) directly affected by each casualty and not just the units of timber contained in the trees suffering mortal injury. The court enunciated the standard that the appropriate single identifiable property is any unit of property that has an identifiable adjusted basis and that is reasonable and logical and identifiable in relation to the area affected by the casualty. The court also held that the allowable loss for casualty is not limited to merchantable units of timber totally destroyed.

In *Weyerhaeuser versus United States*, the United States Court of Appeals for the Federal Circuit held that the single identifiable property damaged or destroyed by several forest fires and a volcanic eruption affecting the taxpayer's timber property was the block, that subdivision of a taxpayer's forest holdings selected by the taxpayer as a means of tracking the adjusted basis in the timber pursuant to Section 1.611-(3)(d)(1). Consistent with *Westvaco versus United States*, a casualty loss was allowed for trees that were damaged but not rendered worthless (see the summary of Revenue Ruling 99-56, page 143).

Generally, a deduction for a loss to a taxpayer's single identifiable property is expressed in terms of the number of timber units damaged or destroyed. The units of measurement used should be those utilized to maintain your timber accounts, such as board feet, cords, or cubic feet. The number of units of timber damaged or destroyed must be established by fair and reasonable measurement to justify a deduction. You may wish to employ a consulting forester to cruise the timber if the area is extensive and much work is involved. In some cases, however, the local representative of the State forestry agency may be able to furnish you with an estimate of the quantity destroyed.

Determining Basis of Timber Destroyed. Determine the basis of timber destroyed as you would for a sale or other disposition, as discussed in "Determining the Amount of Gain or Loss," page 45.

First, determine the depletion unit by dividing the adjusted basis for depletion as shown in your timber account by the quantity of merchantable timber in the account prior to the casualty. Then, multiply the depletion unit by the number of units destroyed to find the amount allowable as a loss. The volume used to calculate the depletion unit for the loss should include adjustments for growth for the year of the casualty, but is not reduced by the volume of timber destroyed. If the timber has no basis, you will not have a deductible loss.

Year of Deduction. A loss arising from a casualty generally is deducted in the year in which the casualty occurs. This is true even if you have not yet settled a reimbursement claim or have not received an agreed-upon insurance settlement or other compensation. If a claim for reimbursement has been made and you think you will recover all or part of the loss, reduce the reported loss by the amount you expect to recover, even though you have not yet received payment by the time the tax return for the year of the casualty is due. If you later recover less than the amount you estimated, you may deduct the difference for the year in which you become certain that no more reimbursement or recovery can be expected (see Example 8-1).

Example 8-1

Adjustment of loss deduction claimed. Timber that you owned was destroyed by fire in 1999. The fire was accidentally started by a contractor working on the property. The allowable basis of the timber destroyed was $5,500, and you expected to recover $3,500 of the loss from the contractor's liability insurance. Even though the insurance company does not make payment to you in 1999, your loss for 1999 is limited to $2,000, the difference between the loss and the amount you expect to recover. In 2000, the company offers to settle the claim for $3,000 and you accept. The $500 difference between the amount you expected and what you actually received may be claimed as a casualty loss on your return for 2000.

Report as income any reimbursement for more than the amount expected. If, after you have claimed a deduction for a loss, you receive reimbursement for more than you estimated would be recovered (but not more than the total amount of the loss computed), you must include such excess as income on your return for the year received. Do not file an amended return for the year in which you claimed the deduction (see Example 8-2).

Example 8-2

Adjustment of loss deduction claimed. Timber that you owned was destroyed by fire in 1999. For tax purposes, your loss from the casualty was $5,000, and you estimated that insurance would cover $4,500 of the loss. You therefore claimed a loss of $500 on your 1999 return. In 2000, the insurance company pays you $4,750, or $250 more than you estimated in computing your deductible loss for 1999. The $250 difference is included as income on your return for 2000.

Destruction of Unmerchantable Timber. The destruction of a premerchantable plantation or stand of naturally regenerated young growth may result in a deductible casualty loss. You can claim a loss only if: (1) you maintain separate plantation or young-growth accounts, as explained in “Timber Accounts,” page 25 and (2) you have costs allocated to such accounts (see the summary of Revenue Ruling 81-2, page 140). In addition, under certain circumstances the death of newly planted seedlings due to an unusual and unexpected drought may qualify as a noncasualty loss (see the summary of Revenue Ruling 90-61, page 144).

If these requirements are satisfied, generally you may figure your allowable basis for the unmerchantable timber destroyed by dividing the cost shown in the account by the number of acres in plantation or young growth and then multiplying that amount by the number of acres destroyed.

Buildings and Equipment. If buildings and equipment used in your business or held for the production of income (investment) are totally destroyed, your deductible loss is the adjusted basis of each specific item of property destroyed, less salvage value, less any insurance or other compensation received or expected to be received (see Example 8-3). If such property is only partially destroyed, your deductible loss is limited to the lesser of your adjusted basis reduced by any compensation you receive, or the decrease in the fair market value of the property reduced by any compensation (see Example 8-4).

Example 8-3

Loss when property is totally destroyed. Your portable sawmill was completely destroyed by a fire and you carried no insurance on the property. The adjusted basis for depreciation of the sawmill building and equipment at the time of the fire was $6,500, and its fair market value was $5,000. The value of the equipment after the fire was only scrap value, amounting to $300. Your deductible casualty loss is $6,200, the adjusted basis of $6,500 less salvage value of $300.

Example 8-4

Loss when property is partially destroyed. Assume that the sawmill in Example 8-3 was damaged by the fire but not completely destroyed. Just before the fire, the sawmill had a fair market value of $5,000; immediately after the fire, its fair market value was $3,500. Under these facts, your loss is limited to $1,500, the decrease in the fair market value, because this amount is less than the adjusted basis of $6,500.

Had the fair market value of the sawmill been $8,000 just before the fire and $1,000 just afterward, the decrease in fair market value would be $7,000 and your deductible casualty loss would be limited to your $6,500 adjusted basis in the property.

Determining the Decrease in Fair Market Value. The decrease in the fair market value of property resulting from a casualty should be determined by an appraisal of the values of the property immediately before and immediately after the casualty. The decrease is the difference between these two values. Your cost of restoring and cleaning up after the casualty may be acceptable as evidence of the decrease in the value of the property if: (1) such costs are necessary to restore the property to its precasualty condition, (2) the amount spent for restoration is not excessive, (3) the expenses do no more than take care of the damage suffered, and (4) the value of the property after restoration is not more than its value before the casualty.

Theft Losses

Determine the amount of loss you can claim from a theft of timber, frequently referred to as "timber trespass," as you would for a casualty loss. Your deductible loss is the allowable basis of the timber stolen—that is, the depletion unit multiplied by the number of units stolen—less insurance, damages, or other recoverable amounts received.

Year Deducted

Generally, theft losses are deducted in the year the theft is discovered. To establish a theft loss, you do not have to prove when the timber was stolen, only that the theft occurred and that you owned the property, and when you discovered it. Thus, the quantity of timber used in determining the depletion unit is the quantity at the time the theft was discovered.

Reduce Theft Loss by Anticipated Recovery

Your theft loss must be reduced by any amounts you expect to receive as a result of the theft. This is required even though you do not receive payment until after the close of the tax year. If you later recover less than the amount you estimated, you may deduct the difference for the year in which you became certain that no more reimbursement or recovery can be expected. Also, if you are reimbursed in a later year for more than you anticipated when you estimated the amount of the deductible loss, include the excess as ordinary income on your return for the year in which you receive it, as discussed with respect to casualty losses.

Multiple Damages

In many States, successful prosecution of timber trespassers results in the awarding of compensation to the victim. The award is sometimes two or three times the fair market value of the timber stolen. In the case of double or treble damages, one-half or one-third, respectively, of the award represents compensation for the timber stolen. This amount should be reported as proceeds of an involuntary conversion. The gain is determined as for any other disposal. The other one-half or two-thirds, representing a damage award, is fully taxable as ordinary income. It must be reported as "other income." An attachment explaining the entries made on your return should be filed with the return.

Condemnations

A condemnation is the lawful taking of private property by a government body for public use without the consent of the owner, but with payment of compensation. The tax consequences are the same if you sell property under the threat of condemnation. Therefore, if the public condemning authority tells you that it intends to acquire your property by negotiation, or if necessary by condemnation, and you sell the property to the authority at a mutually agreeable price, treat the sale as if your property had actually been condemned and you were granted an award.

The computation of your gain or loss when your forest land is condemned or sold under the threat of condemnation will in all cases involve the land, but may or may not involve standing timber, depending on whether you are permitted to harvest it. Determine the basis of your timber as you would for an ordinary sale. Your land account should show the part of the original basis that was allocated to land, exclusive of timber and any improvements (see page 23). The basis of the land condemned or sold under threat of condemnation is its basis as shown in the land account (see Example 8-5).

Example 8-5

Condemnation. You purchased a 50-acre timber tract and allocated $300 per acre, or $15,000, to the land account. A strip of land totaling 5 acres and running through the property was condemned for use in building a new highway. The basis of the land (exclusive of timber) to be used in computing the gain or loss on the condemnation is $1,500 ((5 ÷ 50) x $15,000).

Condemnations for Right-of-Way Easements

Condemnation of forest land for utility or other right-of-way easements generally involves the taking of any timber growing on the right-of-way and the right to grow future timber crops thereon, but not legal title to the land. In the case of powerlines or pipelines, the landowner may be allowed to grow crops on the right-of-way. The production of timber generally is not allowed because the tops and roots would interfere with the powerlines or pipelines. Any loss of future timber income should be included in the negotiations for the condemnation award. No deduction is allowed for future timber income foregone. The award received is reported as described on page 74.

Basis for Figuring Gain or Loss

The basis of the timber condemned is your depletion unit multiplied by the number of units standing on the property condemned, or the number of acres times the basis per acre for plantations or stands of young growth. If, however, the condemning authority allows you to harvest the merchantable timber before the land is taken, and you sell the timber or cut and sell the logs or other products, only the land would be involved in the computation. The gain or loss on the timber would be reported separately, as described in Chapter 6.

Condemnation of property for public use can raise many specialized questions. For example, besides receiving an award for your condemned property, you might receive severance damages or consequential damages resulting from a decrease in value or damage to that part of your property not condemned. A condemnation also might result in a special assessment being charged to you because of resulting improvements to your retained property. For a detailed explanation of the treatment of these special problems, see IRS Publication 547, *Casualties, Disasters, and Thefts (Business and Nonbusiness)*.

RECOVERY OF EXPENSES

Expenses are handled differently for casualties and thefts than they are for condemnations.

Casualties and Thefts

Appraisal, timber cruising, and other ordinary and necessary expenses for determining your loss are expenses in determining your tax liability. They are not part of the loss, but may otherwise be deductible (see Chapter 5).

Condemnations

Legal, appraisal, timber cruising, and other expenses incurred to receive a condemnation award are deducted from the award to determine the net award reported on your return.

POSTPONING GAINS FROM INVOLUNTARY CONVERSIONS

You may be able to defer gains realized from a forced disposition of timber as a result of an unexpected and unusual event, such as when the trees are killed by fire or an insect attack of epidemic proportions or downed by high wind, earthquake, fire, ice storm, or volcanic eruption. These events generally require the conversion or a salvage sale of the timber soon after the event or you will suffer a complete loss of it. To defer any gains realized, you must use the proceeds (amount realized) to purchase qualifying replacement property (see the summary of Revenue Ruling 80-175, page 143). Amounts realized from the involuntary conversion of timber include the amount realized from a lump-sum sale of the timber, the amount realized under Section 631(b) in the case of disposition of the timber under a pay-as-cut contract, and the fair market value under Section 631(a) in the case of cutting of the timber by the taxpayer. The purchase of qualifying replacement property includes the purchase of replacement timber sites; the cost of seeds and seedlings; your costs to plant trees or sow seed on currently owned, leased, or replacement timber sites; and the cost of purchasing stock in the acquisition or control of a corporation owning timber, timber land, or both.

An involuntary exchange occurs when your property is completely or partially destroyed, stolen, requisitioned, condemned for public use, or disposed of under the threat of condemnation and you receive insurance or a condemnation award. Involuntary exchanges also are called involuntary conversions. If you have a gain resulting from an involuntary exchange, you may elect to postpone paying tax on all or part of the gain even though the involuntary exchange may not necessarily qualify as a casualty. This occurs, for example, when damages are awarded by court order, or when parties who have damaged your property make a voluntary settlement. An example would be a settlement made by a logger working on property next to yours who inadvertently removed timber from your side of the property line.

Determining the Gain

A gain is realized on an involuntary conversion when the salvage sale proceeds, insurance, condemnation award, or other compensation that you receive is greater than your basis in the property. The amount of the gain is determined as described above for casualties, thefts, and condemnations. If you salvage your involuntarily converted timber by harvesting it instead of disposing of it on the stump, and a Section 631(a) election is in effect, the amount of the gain, if any, is based on the fair market value of the stumpage cut as described on page 55. Ordinarily, you would include the gain from an involuntary conversion in your income for the year it is realized. However, under certain conditions, you may defer the gain or a portion of it until you sell the replacement property you bought with the proceeds. The amount of the gain qualifying for deferment cannot exceed the fair market value of the assets converted.

Requirements to Postpone Gain

Your gain is not taxed in the year realized if within the allowable replacement period you purchase other property that is similar or related in service or use to the property converted, or the controlling interest in a corporation owning such property, at a cost that equals or exceeds the amount you received as compensation. For the condemnation of real property, such as standing timber, the replacement period ends 3 years after the close of the first tax year in which any portion of the gain from the conversion is realized. The replacement period is 2 years for property other than real property. The replacement period for both real and personal property is always 2 years from involuntary conversions other than condemnations. Note, however, that under State law, standing timber may not be classified as real property under all circumstances.

For involuntary conversions occurring after June 8, 1997, taxpayers generally cannot defer recognition of gain if the replacement property has been purchased from a related person. This rule does not apply to noncorporate taxpayers if the aggregate gain was $10,000 or less.

If you elect to defer reporting the gain, you must file a statement with your tax return that the election is being made and include all the pertinent information concerning the conversion and the replacement property. If you make the election, but do not spend all of your compensation, reimbursement, or proceeds on qualifying replacement property, you must report the difference as income.

Basis of Replacement Property

Your basis in replacement property is its cost minus any gain that you postpone. In this way, tax on the gain is deferred until you dispose of the replacement property.

REPORTING GAINS AND LOSSES FROM CASUALTIES, THEFTS, CONDEMNATIONS, AND NONCASUALTY LOSSES

Gains and losses are reported differently for casualties and thefts than they are for condemnations and for noncasualty business losses.

Casualties and Thefts

You first use Form 4684, “Casualties and Thefts,” to calculate and report casualty and theft losses and gains. Section B of Form 4684 is used for losses and gains from business and income-producing property. Your losses and gains are reported according to how long the property was held and the purpose for which it was used—such as business, rental, to produce royalties, or for investment. You also may be required to file Schedules C, D, and F of Form T.

Each item of property for which you are claiming a loss or gain must be listed separately. If more than four items were involved in any one casualty or theft, attach additional copies of the form. If you incurred losses or gains from more than one event you must use a separate Form 4684 for each event. Form 4684 summarizes your casualty and theft losses and gains and directs you to the proper form for reporting each.

Reporting Gain or Loss—Property Held for 1 Year or Less. Short-term losses (held 1 year or less) on business, rental, or royalty-producing property are combined on Form 4684 with your short-term gains from casualties and thefts. The resulting net gain or loss is reported on Form 4797.

Reporting Gain or Loss—Property Held for More than 1 Year. Long-term losses (held more than 1 year) on business, rental, or royalty-producing property are combined with your other long-term casualty and theft losses on Form 4684. Compare the combined losses to your long-term gains from casualties and thefts of business, rental, or royalty-producing property. If the combined losses are the same as or less than the gains, net the combined losses against your gains. Then enter the net gain on Form 4797.

If your combined losses are more than the gains, your long-term gains and losses are treated as ordinary gains and losses. Merge your long-term losses with your long-term gains.

Reporting Gain or Loss From Income-Producing Property. Your short-term losses from income-producing (investment) property are reported on Schedule A of Form 1040. Short-term gains from income-producing property are added to your gains from business, rental, and royalty-producing property to be offset against short-term losses from business, rental, and royalty-producing property on Schedule E of Form 1040, and are reported on Form 4797. Your total long-term loss on income-producing property is reported on Schedule A of Form 1040.

CONDEMNATIONS

The way in which you include a taxable gain or deductible loss from a condemnation in computing your income depends on the kind of property involved, when you acquired it, how long you held it, and whether or not a part of your gain is due to depreciation. Do not include condemnation gains in taxable income if you elect to defer tax on the gain by acquiring replacement property, as discussed above.

Property Held for 1 Year or Less. Treat a gain or loss from property used in your business or held for the production of rents or royalties as ordinary gain or loss on Form 4797. Report a gain or loss from property you held for investment as a short-term capital gain or loss on Schedule D of Form 1040.

Business or Investment Property Held for More Than 1 Year. If you held property for more than 1 year before it was condemned or sold under threat of condemnation, you must list the gain or loss on Form 4797, together with any other gains and losses from business property.

Property Held Primarily for Sale. Report a gain or loss from property you held primarily for sale to customers in the ordinary course of business as ordinary income or loss. Use the appropriate business schedule, either Schedule C or F of Form 1040, regardless of how long the property was held. You never report such transactions on Schedule D of Form 1040 or on Form 4797.

Property Held for Personal Use. Report the gain from property held for personal use as a short-term or long-term gain on Schedule D of Form 1040. Under no circumstances may you deduct a loss from the condemnation of property that you held for personal use.

For more information, see IRS Publications 225, *Farmer's Tax Guide*; 334, *Tax Guide for Small Business*, and 547, *Casualties, Disasters, and Thefts (Business and Nonbusiness)*.

NONCASUALTY LOSSES

Losses to timber held for use in a trade or business, such as those described in Revenue Rulings 87-59 and 90-61 (see page 144) are reported on Form 4797 to be netted against other gains and losses from disposals of business property.

Example 8-6

Comprehensive example: Walter Green owns 320 acres of forest land that was affected by hurricane-force winds on April 10, 1999. Walter is a calendar-year taxpayer and holds the timber for use in a trade or business activity. He maintains one timber account for all of the stands. The damage varied among the stands of loblolly and shortleaf pine of various ages. Almost all of the trees in some stands were uprooted and splintered so as to be unsaleable. Some stands or parts thereof were subject only to windthrow. Other stands or parts thereof suffered little damage.

Walter identified the stands that were undamaged and instructed his consulting forester to cruise all of the other stands to determine the extent of the damage. He used the cruise data and on-the-ground inspections to determine the stands that needed to be treated by a salvage cut. These stands were put up for sale in July, but by December 31, 1999, no offers had been received. The timber buyers Walter contacted all told him that because of the large acreage of timber damaged that spring there was more timber available than could be absorbed by the market. They suggested he contact them next spring.

Walter claimed as a loss his basis in the 1,200 cords of wood totally destroyed. The basis was determined as shown in Figure 8-1. Walter reported the loss on Form 1040, Schedules D and F (Form T), Form 4684, and Form 4797.

On November 10, 2000, Walter was able to sell the stands identified for salvage. In 1999, the forester estimated that these stands contained 2,100 cords. The buyer, however, estimated that the stands contained only 1,800 cords of merchantable wood. The difference was due to the degradation over two summers since the hurricane. Walter received $16,500 for the 1,800 cords. The allowable basis for this sale was determined as shown in Figure 8-2. The $1,233 loss should be reported as a noncasualty loss in 2000. The $9,102 gain on the salvage sale ($16,500 - $7,398) is reported on Schedule C of Form T. If Walter elected to pay tax on the gain, he would report it on Form 4797 as an involuntary conversion. If he elected to postpone paying tax on the gain by replanting the stands or otherwise acquiring qualifying replacement property, he would file an attachment to his 2000 return detailing such things as all facts relating to the hurricane, the amount realized on the sale, his computation of the gain, any gain to be reported, and the type and cost of replacement property acquired. If the replacement property would be acquired after the time for filing the return, Walter should indicate in the statement that he intends to acquire replacement property within the required time period. In the subsequent year of acquiring replacement property, a statement should be attached to the return, giving detailed information on the replacement property.

Figure 8-1. Schedule F of Form T (Timber): Capital Returnable Through Depletion.

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Schedule F Capital Returnable Through Depletion

On lines 27 through 42, give the data for each timber account separately. Cover any changes that have taken place during the tax year. Attach as many additional pages of this schedule as needed. If you deplete on the block basis, combine new purchases with the opening balances and use the average depletion rate shown on line 34 for all timber cut or sold, regardless of how long held. If you express timber quantity in MBF, log scale, name the log rule used ▶ ....

		(a) Quantity in MBF, log scale; cords; or other unit[1]	(b) Cost or other basis
27	Name of block and title of account ▶ Walter Green Timber Account		
28	Estimated quantity of timber and amount of capital returnable through depletion at end of the immediately preceding tax year	5,000 Cords	$22,300
29	Increase or decrease of quantity of timber required by way of correction[2]		
30a	Addition for growth (period covered ▶ 1 years)	220 Cords	
b	Transfers from premerchantable timber account		
c	Transfers from deferred reforestation account		
31	Timber acquired during year		
32	Addition to capital during year[3]		
33	Total at end of year, before depletion (add lines 28 through 32, in each column)	5,220 Cords	$22,300
34	Unit rate returnable through depletion, or basis of sales or losses (line 33, column (b), divided by line 33, column (a))		4.27
35	Quantity of timber cut during year		
36	Depletion sustained (line 34 multiplied by line 35)		
37	Quantity of standing timber sold or otherwise disposed of during year		
38	Allowable as basis of sale (line 34 multiplied by line 37)		
39	Quantity of standing timber lost by fire or other cause during year	1,200 Cords	
40	Allowable basis of loss (line 34 multiplied by line 39)		5,124
41	Total reductions during year:		
a	Add line 35, column (a); line 37, column (a); and line 39, column (a).	1,200 Cords	
b	Add line 36, column (b); line 38, column (b); and line 40, column (b).		5,124
42	Net quantity and value at end of year (line 33, column (a) less line 41a, column (a); and line 33, column (b) less line 41b, column (b)).	4,020 Cords	$17,176

[1] If MBF, log scale, is not the unit used, state what unit you used and explain it.

[2] Adjust the quantity in MBF, log scale, or other unit remaining at the end of the year for changes in reinventory, standards of use, scattered and/or indefinitely ascertained losses, inaccuracy of the former estimate, or change in the log scale if the log rule now in use differs from the one used as basis for depletion in earlier years. If you make a change, clearly state the basis for it.

[3] Analyze the addition to show the individual items included. Include expenditures for taxes, administration, protection, interest actually paid, etc., if you did not treat these expenditures as expense deductions on your return. Carry expenditures for reforestation, such as site preparation, planting, seeding, etc., in a separate deferred account.

43 Quantity of cut timber that was sold as logs or other rough products . . . . ______

44 Are you electing, or have you made an election in a prior tax year that is in effect, to report gain or loss from the cutting of timber in accordance with section 631(a)? (This election is binding for all eligible timber cut in the election year and all subsequent years. You may revoke the election only with IRS consent, unless you made the election for a tax year beginning before 1987.) . . . . ☐ **Yes** ☐ **No**

If "Yes," furnish the information asked for in items 45 through 51.

45 Gain or loss on standing timber as reported on **Form 4797**, Sales of Business Property. Show the adjusted basis for depletion and the fair market value, by species and unit rates if reported on a species basis. Section 631(a) requires you to determine the fair market value of timber cut during the year for timber you owned, or held under contract right to cut, for more than 1 year. The fair market value is the value of the timber as it stood in the forest on the first day of the tax year.

46 Furnish the date of acquisition of timber that was cut in the tax year, if acquired after March 1, 1913; the quantity of timber remaining (adjusted for growth, correction of estimates, changes in use, and any change in the log rule used); and the adjusted basis at the beginning of the tax year. State the acreage cut over and the amount of timber cut from it during the tax year and the log rule or other method you used to determine the quantity of timber cut. If you kept depletion accounts by separate tracts or purchases, give the information separately for each tract or timber purchase.

If you used an average depletion rate based on the average value or cost of a timber block in earlier years, the adjusted basis referred to in section 631(a) is the average basis shown on lines 34, after adjustment.

47 Describe in detail the characteristics of the timber that affect its value, such as total quantity, species, quality, quantity per acre, size of the average tree, logging conditions, distance to markets, and the like.

Figure 8-2. Schedule F of Form T (Timber): Capital Returnable Through Depletion.

Schedule F Capital Returnable Through Depletion

On lines 27 through 42, give the data for each timber account separately. Cover any changes that have taken place during the tax year. Attach as many additional pages of this schedule as needed. If you deplete on the block basis, combine new purchases with the opening balances and use the average depletion rate shown on line 34 for all timber cut or sold, regardless of how long held. If you express timber quantity in MBF, log scale, name the log rule used ▶ ....

Line		(a) Quantity in MBF, log scale; cords; or other unit[1]	(b) Cost or other basis
27	Name of block and title of account ▶ Walter Green Timber Account		
28	Estimated quantity of timber and amount of capital returnable through depletion at end of the immediately preceding tax year	4,020 Cords	$17,176
29	Increase or decrease of quantity of timber required by way of correction[2]		
30a	Addition for growth (period covered ▶ 1 years)	160 Cords	
b	Transfers from premerchantable timber account		
c	Transfers from deferred reforestation account		
31	Timber acquired during year		
32	Addition to capital during year[3]		
33	Total at end of year, before depletion (add lines 28 through 32, in each column)	4,180 Cords	$17,176
34	Unit rate returnable through depletion, or basis of sales or losses (line 33, column (b), divided by line 33, column (a))		4.11
35	Quantity of timber cut during year		
36	Depletion sustained (line 34 multiplied by line 35)		
37	Quantity of standing timber sold or otherwise disposed of during year	1,800 Cords	
38	Allowable as basis of sale (line 34 multiplied by line 37)		7,398
39	Quantity of standing timber lost by fire or other cause during year	300 Cords	
40	Allowable basis of loss (line 34 multiplied by line 39)		1,233
41	Total reductions during year:		
a	Add line 35, column (a); line 37, column (a); and line 39, column (a).	2,100 Cords	
b	Add line 36, column (b); line 38, column (b); and line 40, column (b).		8,631
42	Net quantity and value at end of year (line 33, column (a) less line 41a, column (a); and line 33, column (b) less line 41b, column (b)).	2,080 Cords	$ 8,545

[1] If MBF, log scale, is not the unit used, state what unit you used and explain it.

[2] Adjust the quantity in MBF, log scale, or other unit remaining at the end of the year for changes in reinventory, standards of use, scattered and/or indefinitely ascertained losses, inaccuracy of the former estimate, or change in the log scale if the log rule now in use differs from the one used as basis for depletion in earlier years. If you make a change, clearly state the basis for it.

[3] Analyze the addition to show the individual items included. Include expenditures for taxes, administration, protection, interest actually paid, etc., if you did not treat these expenditures as expense deductions on your return. Carry expenditures for reforestation, such as site preparation, planting, seeding, etc., in a separate deferred account.

43 Quantity of cut timber that was sold as logs or other rough products . . . . ________

44 Are you electing, or have you made an election in a prior tax year that is in effect, to report gain or loss from the cutting of timber in accordance with section 631(a)? (This election is binding for all eligible timber cut in the election year and all subsequent years. You may revoke the election only with IRS consent, unless you made the election for a tax year beginning before 1987.) . . . . ☐ **Yes** ☐ **No**

If "Yes," furnish the information asked for in items 45 through 51.

45 Gain or loss on standing timber as reported on **Form 4797**, Sales of Business Property. Show the adjusted basis for depletion and the fair market value, by species and unit rates if reported on a species basis. Section 631(a) requires you to determine the fair market value of timber cut during the year for timber you owned, or held under contract right to cut, for more than 1 year. The fair market value is the value of the timber as it stood in the forest on the first day of the tax year.

46 Furnish the date of acquisition of timber that was cut in the tax year, if acquired after March 1, 1913; the quantity of timber remaining (adjusted for growth, correction of estimates, changes in use, and any change in the log rule used); and the adjusted basis at the beginning of the tax year. State the acreage cut over and the amount of timber cut from it during the tax year and the log rule or other method you used to determine the quantity of timber cut. If you kept depletion accounts by separate tracts or purchases, give the information separately for each tract or timber purchase.

If you used an average depletion rate based on the average value or cost of a timber block in earlier years, the adjusted basis referred to in section 631(a) is the average basis shown on lines 34, after adjustment.

47 Describe in detail the characteristics of the timber that affect its value, such as total quantity, species, quality, quantity per acre, size of the average tree, logging conditions, distance to markets, and the like.