

Quick Cost Share Guide For Landowners



by Linda Wang

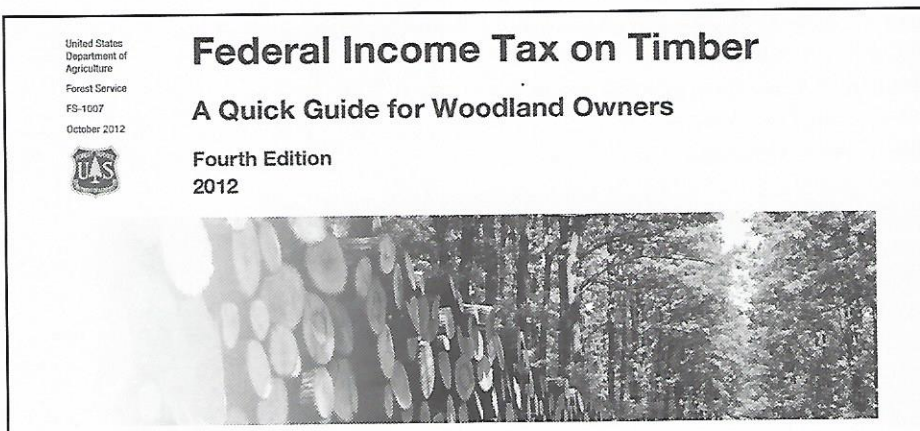
You may receive financial assistance through cost-share programs or other payments when you undertake forest management or conservation practices on your woodlands. The cost-share payments are reported on Form 1099-G, which is also sent to the IRS with your annual tax returns. You must also account for the payments in your tax return. Here is a general guide for when and how to report these payments.

Payments That Must Be Reported

Generally, cost-share payments are taxable income unless they qualify for the income exclusion. Here is how to treat payments, depending on your property classification.

- Forestry cost-share payments that are not used for capital expenditure (such as reforestation) must always be included in gross income.
- For a timber business, report the cost-share payment that must be included in your income on Form 1040 Schedule C.
- For timber investment property, the cost-share payment must be treated as income under "other income" on the front page of Form 1040.

Example: In 2014, you received a \$2,000 cost-share payment to improve the timber stands in your woodland, which you hold as an investment. Your own out-of-pocket cost for the improvement was \$5,500. Because the cost-share was used for tree stand improvement (a deductible expense rather than a capital expenditure), you report \$2,000 under "other income" on the front page of Form 1040. The expenses may then be deducted, subject to the passive activity rules for business and the 2 percent gross adjusted



This online publication is a great free reference for forest landowners with tax questions.

income floor rule for investment timber.

- An annual rental payment or the one-time incentive payment under the Conservation Reserve Program must be reported as income. These payments may not be excluded from gross income (as explained below).

Payments That May Be Excluded from Income

A qualified cost-share payment may be partially or entirely excluded from your gross income if the payment meets two criteria:

- The cost-share payment comes from approved federal or state programs, such as the Forest Health Protection Program, the Conservation Reserve Program, Conservation Security Program, Environmental Quality Incentives Program, Wildlife Habitat Incentives Program, and Wetlands Reserve Program. Several state programs also qualify.
- The cost-share payment is used for a capital expenditure. You cannot exclude a payment for an expense you can deduct in the year you incur it.

If your cost-share payment meets both criteria, use the following steps to determine the excludable amount:

Example: In 2014, you received a \$3,000 cost-share payment for a capital expenditure in your woodland from a qualified federal program. Such a cost-share payment qualifies for income exclusion:

- **If you had no income from the property in the last three years.** You can exclude \$3,876 ($\$2.50 \times 100 \text{ acres}$)/6.45 percent). The interest rate (6.45 percent) was from

the Farm Credit System Bank (see Rev. Rul. 2011-17 for interest rates at timbertax.org). The \$2.50 is fixed by the tax regulation.

- **If you had income from the property in the last three years.** If you had \$9,600 in income from the timber property, for example, use the greater of these two calculations to derive the excludable amount: \$320 (10 percent of $\$9,600/3$) or \$250 ($\$2.50 \times 100 \text{ acres}$). The 10 percent and division by three years and \$2.50 are fixed by the tax regulation. Because \$320 is greater than \$250, the excludable amount is $\$320/6.45 \text{ percent} = \$4,961$ (see above for the interest rate). Because the \$4,000 cost-share is less than the excludable amount of \$4,961, your entire cost-share of \$4,000 may be excluded.

Attach a statement to your return that specifically describes the qualified cost-share program, the management activity, and the calculation of the excludable portion. You may not deduct an expense reimbursed with a cost-share payment and at the same time exclude the cost-share from your income.

More information can be found in the Forest Service's tax publication, *Federal Income Tax on Timber: A Quick Guide for Woodland Owners* (2012) available free online at fs.fed.us/spf/coop/programs/loa/tax.shtml.

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