University of Georgia Warnell School of Forestry & Natural Resources

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After Hurricane Helene: How to Claim Timber Casualty Losses and Defer Taxes on Salvage Timber Sales

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October 28th, 2024

Photo credit: David C. Clabo

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Overview

The impact of Hurricane Helene has been devastating. As of October 21st, 2024, 91 Georgia counties have been declared by the President as federal disaster areas (DR-4830-GA) eligible for individual and/or public assistance (see Figure 1). Many timber owners in and near these areas have suffered significant timber losses. While full recovery will take time, there are some immediate actions timber owners can take to offset a portion of their losses. These include claiming timber casualty losses on federal income tax returns and conducting salvage timber sales.

This publication explains the special federal income tax provisions related to claiming timber casualty loss deductions and deferring taxes on income from salvage timber sales.

Key points for timber casualty losses resulting from a federally declared disaster like Hurricane Helene:

- **Timber casualty loss deduction.** You may be able to claim a deduction for timber casualty losses on your federal income tax return.
- **Choice of tax year to claim the loss.** If your damaged or destroyed timber was in a federally declared disaster area (see Figure 1), you can choose to claim the casualty loss on either your 2023 or 2024 tax return.
- **Method for determining loss.** Timber casualty losses should generally be determined using the timber depletion block approach, rather than simply adding up the value of the damaged or destroyed timber.
- **Deduction limit.** The deductible amount for timber casualty losses cannot exceed the adjusted basis of the affected timber depletion block. This amount is often lower than the retail value of the affected timber block.
- **Salvage timber sales.** Claiming a casualty loss deduction and conducting a salvage timber sale are separate events. You do not have to wait until you complete a savage sale to claim your timber casualty loss.
- **Tax deferral on gains from salvage sales.** You can defer taxes on profits from salvage timber sales if you use the proceeds to purchase qualifying replacement property.

Casualty losses for trees used in residential landscaping are treated differently for federal tax purposes and are covered in a separate publication. Although this publication focuses on Georgia timber owners affected by Hurricane Helene, the general principles apply to timber losses caused by other casualty events, such as fires, floods, hurricanes, and storms. Please visit FEMA for the list of federally declared disasters related to Hurricane Helene in Florida (DR-4828-FL), North Carolina (DR-4827-NC), and South Carolina (DR-4829-SC).

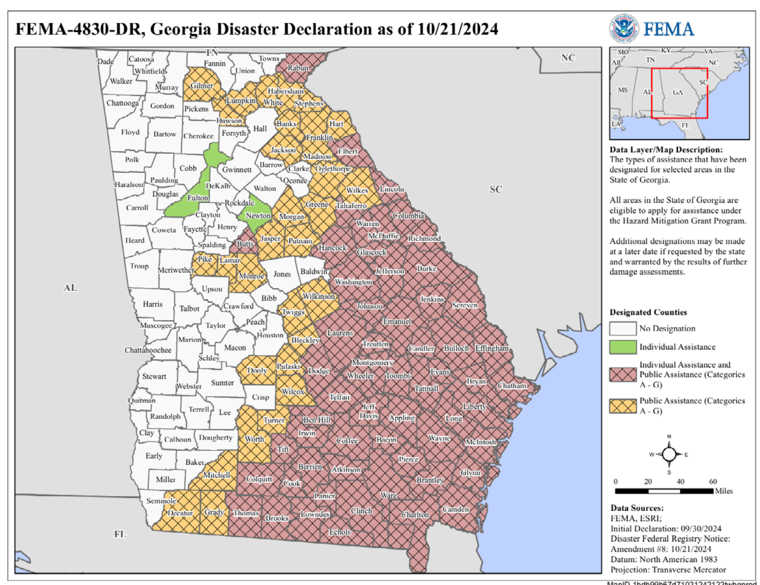

Figure 1. FEMA-4830-DR, Georgia disaster declaration as of October 21st, 2024

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Knowing the tax classification of your timber holding

The classification of your timber holding has important tax implications and affects your filing requirements. Generally, your timber holding falls into one of three broad categories:

- **Investment:** You have a profit motive (e.g., earning timber income or benefiting from land appreciation), but your forest management activities do not rise to the level of a business.
- **Trade or business:** You have a profit motive, and your forestry activities are conducted in a business-like manner.
- **Personal-use or hobby:** You own the property primarily for personal enjoyment, not for profit.

Identifying the Single Identifiable Property (SIP) affected by the casualty

When determining a timber casualty loss, the first step is to identify the Single Identifiable Property (SIP) damaged or destroyed by the casualty.[1] All steps in calculating the loss are made with reference to the SIP. The SIP is essentially your record-keeping unit (timber depletion block) used to track your timber basis for depletion purposes. It can be defined as an operational or logging unit, or by geographic or political boundaries.

Timber owners may group large tracts or multiple stands of timber into one SIP or keep separate accounts (SIPs) for each tract or stand. Whichever method you choose, it is important to remain consistent in how you maintain your timber depletion block (SIP) in the event of a casualty. The IRS does not allow changing block boundaries to include additional timber just to increase casualty loss deductions.

If you have elected to expense and/or amortize qualified reforestation costs under Section 194 of the Internal Revenue Code (IRC), those Qualified Timber Properties (QTPs) should be kept separately and cannot be combined with other timber depletion blocks. For more information, see IRS Notice 2006-47, 2006-20 I.R.B. 892.

Timber casualty losses are calculated with reference to the entire SIP, even if only a portion of the property was damaged or destroyed by the hurricane. Using the depletion block approach allows you to use basis from undamaged timber in the SIP when calculating your timber casualty loss.

Determining your deductible timber casualty loss

Once you have identified the SIP, the deductible timber casualty loss is the lesser of:

- The adjusted basis of the SIP before the casualty, or
- The decrease in fair market value (FMV) of the SIP due to the casualty.

This amount is then reduced by any compensation received from insurance or other sources. Note that income from salvage timber sales is not considered compensation.[2] If the adjusted timber basis of the SIP is zero, you would not be able to deduct any casualty loss, even if the actual timber losses are significant. Note that simply multiplying the volume of the timber damaged or destroyed by per unit stumpage timber prices (i.e., an additive valuation method) is generally not acceptable for estimating timber casualty losses.

To calculate the deductible timber casualty loss, follow these steps:

Step 1. Determine the adjusted basis of the timber

For each SIP damaged or destroyed, you need to locate your tax and management records[3] and determine the adjusted basis of the timber block. Your timber basis generally is your investment in the timber for tax purposes. It starts with the original timber basis, which depends on how the property was acquired:

- **Purchased property:** The original timber basis is the portion of total acquisition costs allocated to the timber. These costs may include purchase price, legal and regulatory fees, timber cruise (if performed), surveying, and other qualified expenses related to the purchase. Allocate the total cost basis among the land, timber, and other assets proportionally based on their respective shares in the total FMV of the whole property. A timber cruise within a year of purchase helps estimate the original timber volume on the property and acreage of pre merchantable timber.
- **Inherited property:** The original timber basis is the FMV of the timber on the decedent's death date (or the alternate valuation date, if elected). This usually results in a higher basis for the beneficiary, often referred to as a stepped-up basis.
- **Gifted property:** The original timber basis is typically the donor's basis plus any gift tax paid. Since the basis is transferred to the recipient, it is normally called a carryover basis.
- **Newly established timber stand.** The original timber basis is your direct costs for forestation or reforestation by planting, seeding, or natural generation.

Your timber basis adjusts over time. It increases when you invest in the property and decreases when the timber is sold or lost due to casualty or other events. For QTPs, the timber basis decreases when reforestation costs are recovered through expensing or amortization. The adjusted basis is the timber basis after these adjustments. Timber basis should not include the basis of the land or other assets.

If you have not established a timber basis, you can reconstruct it retroactively. A professional forester can help estimate the volume and value of timber when you acquired the property by evaluating current timber stock, timber growth rate, and local/regional historical timber stumpage prices. However, you may want to weigh the potential tax savings against the cost of establishing a basis before hiring a professional.

Some common situations where the timber basis may be zero or low:

- Naturally generated timber with little or no additional investment after acquisition.
- Planted timber where reforestation costs were fully recovered through Section 194 expensing and amortization.
- Timberland acquired over 30 years ago with no thinning or harvesting since the acquisition.
- Gifted timberland where the original basis was low.

1. Historically, the IRS took the position that each unit of timber is a single identifiable property for casualty loss deduction. Accordingly, timber casualty loss deduction is only limited to the basis of the destroyed timber. The rule was reversed when the agency issued the Rev. Rul. 99-56 in 1999.
2. Weyerhaeuser v. United States 92 F.3d 1148 (Fed. Cir. 1996).
3. See IRS guidance on reconstructing records after a natural disaster or casualty loss.

Step 2. Estimate the decrease in FMV of the timber block

You generally need a competent appraisal to estimate the decrease in FMV of the timber block (SIP) due to the casualty. According to the IRS's *Timber Casualty Loss Audit Techniques Guide* (2011), the appraisal should be objective, descriptive, and documented. The guide provides a list of specifics that should be included in the appraisal.

Also, timber casualty losses are limited to actual physical losses resulting from the disaster. A decrease in timber value because of the general market decline in or near the disaster area does not count as a timber casualty loss. The appraisal report should contain sufficient information and analysis to support the value estimation.

The appraisal should be conducted by a qualified appraiser who meets appropriate licensing and competency requirements. A registered consulting forester typically provides a competent appraisal. You can find a directory of consulting foresters on the Georgia Forestry Commission's website.

If you choose not to obtain a formal appraisal, ensure you keep sufficient evidence and documentation to support how you determined the FMV of the SIP immediately before and after the disaster in case of an IRS challenge. The cost of cleaning up is not part of a casualty loss.

Step 3. Determine the deductible timber casualty loss

For timber held as an investment or for business purposes, your allowable timber casualty loss deduction is the smaller of the adjusted timber basis (from Step 1) or the decrease in FMV (from Step 2).

For timber held for personal use, additional limits apply.[4] The amount of personal casualty loss deduction is the lesser of the adjusted timber basis or the decrease in FMV (as determined above), reduced by $100, and further reduced by 10 percent of your adjusted gross income (AGI). The $100 reduction applies once per casualty event, regardless of how many pieces of properties are involved in the event.

Example 1. Joe owns 100 acres of forestland as an investment. He keeps all timber, with a timber basis of $30,000, in a single timber block for depletion purposes. In October 2024, Hurricane Helene damaged 30 acres of the timber. A consulting forester helped him estimate the decrease in FMV of the timber block due to the disaster. Before the hurricane, the 100-ac timber block's FMV was $150,000. After the hurricane, the timber value dropped to $100,000, resulting in a $50,000 decrease in FMV. He compared the timber basis of the whole 100-ac block ($30,000) to the loss in FMV of the property ($50,000). He can deduct the lesser of these two numbers ($30,000) as casualty losses on his federal income tax return.

Example 2. The facts are the same as Example 1 except that Joe holds the property for personal use. His adjusted gross income (AGI) is $60,000 for 2024. The timber casualty loss deduction is limited to his timber basis ($30,000), then is reduced by $100 and 10% of his AGI. His allowable deduction for the timber casualty loss is $23,900 [$30,000 – $100 – ($60,000 × 10%)].

4. For tax years 2018 through 2025, personal casualty losses of individual taxpayers are deductible only if they are attributable to a federally declared disaster.

Reporting timber casualty loss

For timber held as an investment: Report the casualty loss in Section B (Business and Income-producing Property) of Form 4684. Then, enter the loss in Schedule A of Form 1040, line 16, as "Other Itemized Deductions."

For timber held in a trade or business: Report the casualty loss in Section B (Business and Income-producing Property) of Form 4684. Then, enter the loss in Form 4797, line 14, as "Net gain or (loss) from Form 4684." If it results in a loss after netting with other Section 1231 gains and losses, report it on Schedule 1 of Form 1040, line 4, as "Other gains or (losses)."

For timber held for personal use: Report the casualty loss in Section A (Personal Use Property) of Form 4684. Then, enter the loss in Schedule A, line 15, as "Casualty and Theft Losses."

To claim a casualty loss for timber held as an investment or for personal use, you need to itemize deductions. However, it is only beneficial to itemize if the total of your casualty loss deduction and other itemized deduction exceeds the standard deduction. Therefore, it is important to evaluate whether itemizing or taking the standard deduction is more favorable for your situation. You may also want to consider the impact on state income taxes. Effective January 1st, 2024, Georgia taxpayers may elect either the standard deduction or the sum of all federal itemized deductions. Georgia's standard deduction has increased significantly starting from the 2024 tax year.

Deducting your loss in the preceding year

In general, casualty losses are deducted in the year they occur. If you have a deductible timber loss due to Hurricane Helene, you can claim it on your 2024 tax return.

However, if the damaged or destroyed timber is in the federally designated areas for individual or/and public assistance (see Figure 1), your timber loss is classified as a disaster loss for tax purposes. A special rule applies to the loss. You can choose to deduct the loss on your 2024 tax return or amended 2023 tax return. This allows you to treat the loss as if it occurred in 2023. For calendar-year taxpayers, you have until October 15th, 2025, to amend your 2023 tax return to claim this loss.

Claiming a qualifying disaster loss on an amended tax return can help you recoup losses sooner, generate cash, and get greater tax savings, especially if your ordinary income tax rate was higher in 2023.

Postponing taxes on income from salvage timber sales

Timber casualty loss deductions and the subsequent salvage timber sale are treated as separate events.[5] You can claim a timber casualty loss deduction before salvaging the timber. You do not need to use the salvage income to offset the casualty loss. This is beneficial because casualty losses offset ordinary income while salvage timber income generally is treated as a long-term capital gain subject to lower tax rates if the one-year holding period requirement is met.[6]

A salvage timber sale is treated as an involuntary conversion under Treas. Reg. 1.1033(a)-1. Although salvaged timber might

5. Weyerhaeuser v. United States 92 F.3d 1148 (Fed. Cir. 1996).
6. See IRS Publication 544, Sales and Other Dispositions of Assets, for exceptions to this rule, such as property acquired by gift, inheritance, or like-kind exchange.

be sold at a discount due to damage and market oversupply, the sale can still result in a taxable capital gain when the sale proceeds exceed the timber's adjusted basis and selling expenses. If you have a gain, you can either:

- Pay capital gain taxes on the profit, or
- Postpone the taxes by purchasing qualifying replacement property within the allowable replacement period.

Qualifying replacement property should be similar or related in service or use to the replaced property. For standing timber, qualifying replacement property includes timber, timberland, reforestation costs, and stocks of a corporation that owns timber or/and timberland (if you gain 80% or more control of the corporation). You can defer the tax in full if the cost of your replacement property is higher than the sale proceeds (not just the profit). Otherwise, you need to pay tax on the difference between the proceeds and the replacement property cost.[7] You need to reduce the basis of your replacement property by the amount of the deferred gain. This defers the tax on the salvage timber sale until the replacement property is disposed of in the future.

A special rule applies to replacement property if the destroyed or damaged timber is held in a business or for investment and is in a federally declared disaster area (see Figure 1). In this case, any tangible replacement property for productive use in a trade or business is considered similar to the damaged or destroyed timber (IRC Section 1033(h)). The replacement property does not have to be in the disaster area.

To defer the gain, attach a statement to your tax return for the year your gain is realized. The statement should include the date and details of the casualty and how you figured the gain. If you plan to purchase the replacement property later, state your intent to replace it within the allowed period. After purchasing the property, attach another statement with details of the replacement property. In general, replacement property cannot be purchased from a related person. See IRC Section 1033(i) for more details.

The replacement period ends two years after the close of the first tax year in which any part of the gain is realized. For example, if you realized a gain from a salvage timber sale on January 15th, 2025, you have until December 31st, 2027, to replace the property. You may ask for an extension of the replacement period by submitting a written request to the IRS before the end of the replacement period.

Other tax considerations

Casualty loss of timber in a passive activity. If you do not materially participate in your timber business (i.e., passive activity), the timber casualty loss deduction is not subject to the passive activity loss limitations rule (Treas. Reg. 1.469-2(d)(2)(xi)).

State disaster relief grants for timber damage. Payments from state or local governments to compensate for timber damage are taxable. However, you can defer the tax by purchasing qualifying replacement property (see above) within the allowed period.

Large SIPs of timber businesses. Business timber owners of 10,000 acres or more in a single SIP may be subject to a special discount rule on timber casualty loss determination. Refer to the IRS field directive on timber casualty losses (2004) for more information.

Lessee of timberland. If you lease the land but own the timber, you are eligible for the timber casualty loss deduction. Be sure to provide proof of timber ownership.

Cost of appraisals. The cost of appraisals for determining the decrease in FMV of the timber property due to the hurricane is not part of the timber casualty loss but is an expense for determining your tax liability.

Qualified disaster recovery distribution from retirement funds. Under the SECURE 2.0 act of 2022, affected taxpayers can withdraw up to $22,000 from retirement plan funds penalty-free for qualified disaster recovery. This special distribution is available to those who suffer economic loss from a federally declared disaster like Hurricane Helene and their principal residence is in the disaster area. The distribution is tax-free if repaid within three years. See IRS FS-2024-19 for more information.

Documentation

Be sure to document the following:

- Photos of the property before and after the casualty (with dates).
- News articles about Hurricane Helene and its impacts on your local area.
- Proof of ownership (e.g., warranty deed, recorded plat from county courthouse, and/or county tax map of the property with parcel number).
- Forest management records.
- Timber accounting records and past income tax returns.
- Court or legal documents for inherited property.
- Proof of your effort to salvage the affected timber (if any).

Important note

This information is current as of October 28th, 2024. Future tax laws may provide additional relief to timber owners impacted by Hurricane Helene. Please visit the website of UGA Warnell School of Forestry and Natural Resources Outreach Website for updates.

Additional sources of information

- Dickens, E.D., D.C. Clabo, D.J. Moorhead, C. Bates, and S. Griffin. 2020. Assessing hurricane and tornado storm damaged forest stands. WSFNR-20-70C. Athens, GA.
- Greene, J., W. Siegel, W. Hoover, and M. Koontz. 2013. Forest landowners guide to the federal income tax.
- IRS. 2011. Timber casualty loss audit technique guide.
- IRS. 2024. Disaster relief frequently asked questions: Retirement plans and IRAs under the SECURE 2.0 Act of 2022. FS-2024-19.
- IRS. 2024. Publication 544. Sales and other dispositions of assets.
- IRS. 2024. Publication 547. Casualties, disasters, and thefts.
- National timber tax website. www.timbertax.org.

7. See IRS Publication 547 for example when the cost of replacement property is less than the proceeds received.

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