

Appendix 1. Summaries of Selected Revenue Rulings

Pertinent revenue rulings (Rev. Rul.) dealing with timber are summarized below. Obsolete and inconsequential rulings are not listed. Citations are given to the complete texts: Cumulative Bulletin (C.B.) published by the U.S. Department of the Treasury. The rulings are categorized by general subject and listed alphabetically within each general subject by key word. The complete text of rulings summarized here and the text of modified, obsolete, and related rulings are available at the Timber Tax Internet site, <http://www.fnr.purdue.edu/ttax>. This site also includes a findings list for rulings.

Basis and Depletion Allowance

Christmas trees, capital and operating expenditures—In connection with the cultivation, as a trade or business, of Christmas trees for purposes of sale when they are more than 6 years old, the expenditures incurred for planting must be capitalized. Expenditures incurred for silvicultural practices such as weeding, cleaning, and noncommercial thinning are deductible as ordinary and necessary trade or business expenses. The cost of land improvements is capitalized in the land account. The cost of purchased equipment and other depreciable assets, such as culverts and fences, should be capitalized and recovered through the allowance for depreciation. Modified by Rev. Rul. 71-228 Rev. Rul. 66-18, 1966-1 C.B. 59.

Christmas trees, capital and operating expenditures—Costs incurred for shearing and basal pruning of trees grown for the Christmas tree market are deductible business expenses. Rev. Rul. 66-18 modified. (Sec. 62.) Rev. Rul. 71-228, 1971-1 C.B. 53.

Cutting contract, advanced royalties—Advanced royalties paid or accrued by a lessee under a timber-cutting contract in a tax year for timber cut during that year are not deductible under the provisions of reg. 1.612-3(b)(3), but are to be added to the lessee's depletable basis in the timber. Treas. Reg. §§ 1.612-3, 1.631-2. (Secs. 612, 631.) Rev. Rul. 77-400, 1977-2 C.B. 206.

Logging roads, permanent vs. temporary, investment credit—A taxpayer's logging-truck roads are "Section 38 property" for investment credit purpose because they are an integral part of the operation of sawmills, the production of lumber and related products, or the manufacture of paper. Distinguished by Rev. Rul. 73-217. Treas. Reg. §§ 1.46-3(e)(4),(5); 1.46-3(c)(1); 1.48-1(k); 1.48-1(b)(4), 1.48-1(d)(2),(4). (Secs. 38, 48.) Rev. Rul. 68-281, 1968-1 C.B. 22.

Logging roads, depreciation—Depreciation of logging-truck roads is distinguished in situations where: (1) the road is expected to be useful to the taxpayer for an indefinite period and (2) the road has a determinable useful life to the taxpayer. In the first situation, where the surfacing, bridges, and culverts of a logging-truck road are expected to have a determinable useful life to the taxpayer, these assets are depreciable or amortizable. Because the roadbed of a well-maintained road has an indefinite useful life, its cost is not depreciable or amortizable. In the second situation, all components are depreciable or amortizable because all have a determinable useful life to the taxpayer. Rev. Rul. 88-99, 1988-2 C.B. 33.

Long-term contracts, royalties vs. rent—The fair market value of the timber existing at the time of the execution of a long-term timber-purchase contract constitutes the basis for depletion of the timber and payments in excess of the fair market value are consideration for the use of land deductible as a business expense. Amplified by Rev. Rul. 78-267. Treas. Reg. §§ 1.162-1, 1.612-1. (Secs. 162, 612.) Rev. Rul. 75-59, 1975-1 C.B. 177.

"Purchaser credit" road construction contract, Forest Service—The basis for cost depletion of timber does not include the "purchaser credit" earned for specified road construction under a Forest Service contract. Further, amounts expended for construction of such roads are recovered through depreciation if the roads are used for harvesting the timber or added to the

depletion basis if the roads are not used for harvesting the timber. Treas. Reg. §§ 1.611-5, 1.612-1, 1.631-1. (Secs. 611, 612, 631.) Rev. Rul. 71-354, 1971-2 C.B. 246.

Reforestation, replacing dead seedlings—A timber producer sustains no deductible loss on the death, not due to casualty, of tree seedlings planted to reforest land from which it has harvested the mature timber. Amounts paid or incurred in replanting to replace the lost seedlings must be capitalized in accordance with reg. 1.611-3(a). Modified by Rev. Rul. 90-61. Treas. Reg. §§ 1.165-1, 1.611-3. (Secs. 165, 611.) Rev. Rul. 81-2, 1981-1 C.B. 78.

Reforestation—Generally, direct costs of reforestation, including girdling, herbicide application, baiting of rodents, labor and tool expense, and the planting and seeding equipment depreciation, are capital expenditures recoverable through depletion allowances when the timber is cut or as adjusted basis if the timber is sold. Indirect costs, deducted in the year incurred or capitalized cumulatively under Section 266, include interest paid on money borrowed or service charges on performance bonds in lieu thereof to satisfy a State law requiring a deposit to guarantee reforestation. Rev. Rul. 55-252 superseded. Treas. Reg. §§ 1.263(a)-1, 1.611-3, 1.1011-1. (Secs. 263, 611, 1011.) Rev. Rul. 75-467, 1975-2 C.B. 93.

Reforestation, payments under forestry incentives program (FIP)—The excludable portion of cost-sharing payments received under the Forestry Incentives Program (FIP) is excludable from gross income, and the total costs of reforestation less the excludable portion are to be capitalized as a cost of timber. Under the election not to have Section 126 apply to the FIP payment, the entire payment is includible in gross income, and the total costs of reforestation (not reduced by any portion of the FIP payment) are to be capitalized as a cost of timber. Rev. Rul. 76-6 modified and superseded. Treas. Reg. §§ 1.61-1, 16A.126-1, 16A.126-2, 1.194-1, 1.611-3. (Secs. 61, 126, 194, 611.) Rev. Rul. 84-67, 1984-1 C.B. 28.

Reforestation expenditures—The expenditures for destroying undesirable hardwood trees and brush in naturally reforested stands of Southern

pine young-growth when related primarily to the seeding and establishment of the pine seedlings are capital expenditures recoverable through depletion. Treas. Reg. § 1.611-3. (Sec. 611.) Rev. Rul. 76-290, 1976-2 C.B. 188.

Cost sharing, payments under stewardship incentives program (SIP)—The stewardship incentives program (SIP) was determined to be substantially similar to the enumerated programs in Section 126 of the Internal Revenue Code (Code). Thus, SIP cost-sharing payments in connection with improvements in small watersheds may be eligible for exclusion from gross income under Section 126. (As a result, the excludable portion of these cost-sharing payments is excludable from gross income, and the total costs of improvements less the excludable portion are to be capitalized to the appropriate land or timber account.) Reg. §§ 1.61-1, 16A.126-1, 16A.126-2. (Secs. 61, 126.) Rev. Rul. 94-27 1994-1 C.B. 26.

Cost-share payments under Wetlands Reserve Program (WRP), Wildlife Habitat Incentives Program (WHIP), and Environmental Quality Incentives Program (EQIP)—The Wetlands Reserve Program (WRP), Wildlife Habitat Incentives Program (WHIP), and Environmental Quality Incentives Program (EQIP) were determined to be substantially similar to the type of program described in Section 126(a)(1) through (8) of the Internal Revenue Code. Thus, cost-share payments made under the programs may be excluded from gross income to the extent permitted under Section 126. Reg. §§ 16A.126-1, 16A.126-2. (Secs. 61, 126.) Rev. Rul. 97-55, I.R.B. 1997-52, 7.

Capital Gains

Cutting contract, “contract right to cut” defined—To be entitled to the benefits of Section 631(a) of the Internal Revenue Code (Code) as the holder of a “contract right to cut” timber, a taxpayer must have acquired under such contract a proprietary interest in the timber which he cuts. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 58-295, 1958-1 C.B. 249.

Cutting contract, contract right to cut, future right—An option on a right to cut timber that is transferred as part of an exchange of property is

not an enforceable contract right to cut for Section 631(a) purposes, in cases where the claimed right to cut is exercisable only after a future date or occurrence or is contingent upon an election or a transfer of additional consideration by a taxpayer. The holding period in such cases commences only when the right to cut becomes exercisable. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 74-529, 1974-2 C.B. 185.

Contract cutting, road credit—The amount subject to treatment under Section 631(b) by a corporate timber landowner that disposes of timber under a cutting contract that specifies the unit price for an estimated number of units and the amount of a “road credit” allowed the purchaser for building access roads is the actual amount realized, which is the total contract price reduced by the road credit. Treas. Reg. § 1.631-2. (Sec. 631.) Rev. Rul. 75-306, 1975-2 C.B. 243.

Christmas trees sold on “choose and cut” basis—Income realized from the sale of Christmas trees that are selected and cut on the taxpayer’s land by individual purchasers is ordinary income. However, the taxpayer may elect to treat the cutting of trees as sales or exchanges of timber as prescribed by reg. 1.631-1. Treas. Reg. §§ 1.631-1, 1.1231-1. (Secs. 631, 1231.) Rev. Rul. 77-229, 1977-2 C.B. 210.

Cutting contract, fair market value of timber cut—The terms of a contract under which the taxpayer acquired the unrestricted right to cut and use timber in its lumber manufacturing business are not relevant in determining the fair market value of timber cut. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 74-271, 1974-1 C.B. 151.

Cutting contract, payment for failure to cut—Amounts received under a timber-cutting contract for timber cut, the quantity of which is based upon a “cruise” rather than scaling, qualifies for treatment under Section 631(b). A penalty payment received for failure to cut any portion of the “cruised” or marked trees during the term of the contract is ordinary income. Treas. Reg. § 1.631-2. (Sec. 631.) Rev. Rul. 78-104, 1978-1 C.B. 194.

Cutting contract, quantity first determined, holding period—A taxpayer who acquired timber-cutting rights under a USDA Forest Service

cutting contract is considered to have first definitely determined the quantity of timber cut, for the purposes of the election to treat cutting of timber as a sale or exchange, when a truck scale was made using a bureau scaler at the time the logs arrived at the taxpayer’s sawmill even though a mill deck scale was made later by a Forest Service scaler. Distinguished by Rev. Rul. 73-489. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 73-267, 1973-1 C.B. 306.

Cutting contract, quantity first determined, holding period—A fiscal year accrual method taxpayer who acquired timber-cutting rights under USDA Forest Service cutting contracts requiring that, for payment purposes, logs be scaled by a Forest Service scaler and who elects to treat the cutting of timber as a sale or exchange is considered to have cut the timber for purposes of Section 631(a) when the logs are scaled on the mill deck by the Forest Service scaler in the ordinary course of business. Distinguishing Rev. Rul. 73-267. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 73-489, 1973-2 C.B. 208.

Default of performance bond—An amount received by the fee owner of certain timber lands from the default of a cash performance bond posted by a grantee under a contract involving the cutting and disposal of timber is not an amount realized from the disposal of timber and is taxable as ordinary income. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 61-56, 1961-1 C.B. 243.

Disposal, expenses for—Expenditures directly attributable to a disposal of timber are reductions of the amount received for purposes of computing gain or loss from such disposal. Whether expenditures are directly attributable to a disposal is determined on the strength or persuasiveness of each case and how closely related to the disposal the activities are in connection with the expenditures. Treas. Reg. § 1.631-2. (Sec. 631.) Rev. Rul. 71-334, 1971-2 C.B. 248.

Disposal, economic interest retained—In the case of the disposal of timber, held for the requisite period of time prior to disposal, by the owner thereof under any type of contract by virtue of which the owner retains an economic interest in such timber, the amount received qualifies for capital gain treatment regardless of the nature of

the taxpayer's business or the purpose for which the timber is held. (Secs. 631, 1231.) Rev. Rul. 57-90, 1957-1 C.B. 199.

Holding period—A taxpayer who acquired timber on December 31, 1962, and still owned it at the beginning of his tax year, which began July 1, 1963, has owned such timber for a period of more than 6 months before the beginning of such tax year for purposes of Section 631(a). Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 66-6, 1966-1 C.B. 160.

Holding period—A capital asset acquired on the last day of any calendar month, regardless of whether the month has 31 days, must not be disposed of until on or after the first day of the seventh succeeding month of the calendar in order to have been "held for more than 6 months" within the meaning of Sections 1222(3) and (4) and 1231. Rev. Rul. 66-7, 1966-1 C.B. 188.

Long-term contract, capital gains vs. ordinary income—Under a contract for a term of 60 years granting the right to grow timber and to cut timber growing and to be grown, a paper company was obligated to make yearly payments not contingent on the quantities of timber cut. Hence, the transaction is not a "disposal" of timber under Section 631(b). Payments equal to the fair market value of the timber existing at the execution of the contract are proceeds of a sale of timber and any gain included in this amount is a capital gain, provided the conditions of Sections 1221 or 1231 are met. Any excess of such payments over the fair market value of the timber existing at the execution of the contract is ordinary income. Amplified by Rev. Rul. 78-267. Treas. Reg. §§ 1.631-1, 1.1221-1, 1.1231-1. (Secs. 631, 1221, 1231.) Rev. Rul. 62-81, 1962-1 C.B. 153.

Long-term contract, unstated interest—The application of the unstated interest provisions to long-term timber contracts is described in situations in which the taxpayer is: (1) a landowner who receives the entire consideration under the contract in a lump sum on the date the contract is signed, (2) a landowner who is to receive payments over a period of 60 years under a contract for the sale of timber and lease of the land on which the timber is growing, and (3) a paper company that makes payments under a contract

similar to that in situation 2. Rev. Ruls. 62-81, 62-82, and 75-59 amplified. Treas. Reg. §§ 1.483-1, 1.1221-1, 1.1231-1. (Secs. 483, 1221, 1231.) Rev. Rul. 78-267, 1978-2 C.B. 171.

Long-term lease, lump-sum payment—A lump-sum payment received under a contract for the lease of land and the grant of the right to cut timber therefrom constitutes proceeds of the sale of timber to the extent of fair market value of the timber then existing. The resulting gain or loss is subject to the treatment described in Sections 1221 or 1231 provided the conditions thereof are met. Any excess of such payments over the fair market value of the existing timber is ordinary income. Amplified by Rev. Rul. 78-267. Treas. Reg. §§ 1.631-1, 1.1221-1, 1.1231-1. (Secs. 631, 1221, 1231.) Rev. Rul. 62-82, 1962-1 C.B. 155.

Pulpwood from tops and limbs of sawtimber tree—Treating the cutting of timber as the disposal of standing trees for capital gain purposes applies only to the disposal of standing trees and not to the sale of tree tops and limbs lying on the ground. Income from the sale of the tree tops and limbs is ordinary gain or loss; however, the Section 631(a) benefits apply to the entire standing tree. The method of computing the fair market value of such trees is specified. (Sec. 631.) Rev. Rul. 56-434, 1956-2 C.B. 334.

Right to cut and remove for landowner—A taxpayer who acquires by contract the right to cut, remove, and sell timber from the land of another for the account of the landowner, but not the right to cut the timber for sale on his own account or for use in his trade or business, is not the holder of "a contract right to cut" for purposes of the election under Section 631(a). Also, the taxpayer is not entitled to the treatment provided by Section 631(b), relating to a disposal by the owner. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 58-579, 1958-2 C.B. 361.

Timber land, sale of, used in trade or business—Gain realized by an electing small business corporation from the sale of timber land held primarily for the production of timber products and not for sale to customers is gain from the sale of real property used in a trade or business under Section 1231(b) of the Internal

Revenue Code (Code), subject to the provisions of Section 1.1375-1(d) of the regulations. Treas. Reg. §§ 1.1231-1, 1.1375-1. (Secs. 1231, 1375.) Rev. Rul. 73-222, 1973-1 C.B. 373.

When “cut”—For purposes of determining capital gain or loss, timber is considered “cut” at the time when in the ordinary course of business the quantity of timber felled is first definitely determined, rather than at the time of the felling. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 58-135, 1958-1 C.B. 519.

Timber land tracts, deeds in escrow, holding period—The holding period of each of several tracts in a timber acreage purchased under a single indivisible contract with annual payments and release of deeds from escrow based on tracts selected for cutting begins on the day after the execution of the contract. Treas. Reg. § 1.631-1. (Sec. 631.) Rev. Rul. 72-252, 1972-1 C.B. 193.

Tree stumps, investment property—Income from the sale of tree stumps by a timber landowner who is not in the business of buying or selling timber is taxable as a capital gain where the land was acquired in a cutover state as a real estate investment and the stumps were sold in one lot. (Sec. 1221.) Rev. Rul. 57-9, 1957-1 C.B. 265.

Like-Kind Exchanges

Exchange of land and timber for bare land—The taxpayer conveyed timber land consisting of both land and timber, receiving bare land in return. The exchange was one of like-kind properties under Section 1031(a) of the Internal Revenue Code (Code). The difference in the two properties concerned their grade and quality, not their nature or character. Treas. Reg. §§ 1.170A-4, 1.1011-2, 1.1031(a)-1, 1.1031(d)-1. (Secs. 170, 1011, 1031.) Rev. Rul. 78-163, 1978-1 C.B. 257.

Exchange of timber land with reservation of timber—cutting rights—A corporation’s exchange of timber land, with the corporation reserving the timber-cutting rights, for State-owned timber land of lesser fair market value was an exchange of like-kind properties. Treas. Reg. §§ 1.170A-1, 1.1030(a)-1. (Secs. 170, 1031.) Rev. Rul. 76-253, 1976-2 C.B. 51.

Timber land, like-kind exchange—The taxpayer conveyed to the United States timber land containing some virgin timber and also substantial second-growth timber in exchange for timber land supporting substantial virgin timber. The exchange qualified for nonrecognition of gain or loss under Section 1031(a) of the Internal Revenue Code (Code) because both the original and replacement lands were held for investment purposes. Treas. Reg. § 1.1031(a)-1(b). (Sec. 1031(a).) Rev. Rul. 72-515, 1972-2 C.B. 466.

Involuntary Conversions

Casualty loss, determining the amount of deductible loss—The Court of Claims, in *Westvaco versus United States*, decided that the single identifiable property (SIP) 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 SIP 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 SIP 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). Rev. Ruls. 66-9 and 73-51 revoked. Treas. Reg. § 1.165-7. (Sec. 165.) Rev. Rul. 99-56, 1999-51 I.R.B. 676.

Casualty loss, insect—The death of ornamental trees 5 to 10 days following a massive Southern pine beetle attack in an area not known for such massive attacks results in an allowable casualty loss deduction to the extent provided by Section 165(c). Modifies Rev. Rul. 57-599. Distinguished by Rev. Rul. 87-59. Treas. Reg. § 1.165-7. (Sec. 165.) Rev. Rul. 79-174, 1979-1 C.B. 99.

Casualty loss, nonrecognition of gain—The nonrecognition of gain provisions of Section 1033(a) are applicable to the proceeds received from the voluntary sale of timber downed by high winds, earthquake, or a volcanic eruption when the proceeds are used to purchase other standing timber. Rev. Rul. 72-372 revoked. Treas. Reg. § 1.1033(a)-2. (Sec. 1033.) Rev. Rul. 80-175, 1980-2 C.B. 230.

Losses, timber in trees killed by insects—Loss of timber over a 9-month period following an unexpected and unusual insect attack that killed the timber trees gives rise to an allowable noncasualty business loss deduction that must be netted with other noncasualty Section 1231 gains

and losses. Rev. Rul. 79-174 distinguished. Amplified by Rev. Rul. 90-61. Treas. Reg. §§ 1.48-1, 1.165-1, 1.165-7, 1.194-1, 1.611-3, 1.612-1, 1.1231-1. (Secs. 48, 165, 194, 611, 612, 1231.) Rev. Rul. 87-59, 1987-2 C.B. 59.

Losses, seedlings killed by drought—An unusual and unexpected drought that caused the death of tree seedlings planted for the commercial production of timber gives rise to an allowable noncasualty business loss deduction that must be netted with other noncasualty Section 1231 gains and losses. Rev. Rul. 81-2 distinguished, Rev. Rul. 87-59 amplified. Treas. Reg. §§ 1.48-1, 1.611-3, 1.194-1, 1.1231-1. (Secs. 48, 165, 194, 611, 1231.) Rev. Rul. 90-61, 1990-2 C.B. 39.