

Private Letter Ruling 9621012, 5/24/1996, IRC Sec(s). 1031

UIL No. 1031.03-00

Headnote:

Reference(s): Code Sec. 1031;

The Service has ruled that an exchange of a scenic conservation easement for a fee interest in timberland, farm land, or ranch land qualifies as a like-kind exchange under section 1031.

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Full Text:

Date: February 16, 1996

CC: DOM: IT&A: 05 - TR-31-2381-95

Taxpayer : ***

Taxpayer's Address : ***

Taxpayer's Identification Number : ***

LEGEND:

State Z = ***

County = ***

Ranch = ***

PRC = ***

\$X = ***

Y = ***

Z = ***

Section A = ***

Section B = ***

Section C = ***

Dear ***

This responds to your letter requesting a ruling on behalf of Taxpayer. Specifically¹ you have requested a ruling as to whether a proposed exchange will qualify as a like-kind exchange for purposes of section 1031 of the internal Revenue Code.

FACTS

Taxpayer owns approximately Y acres of ranch land (the "Ranch") in County. Taxpayer represents that he has operated the Ranch for more than 15 years for productive use in the trade or business of breeding, raising, and selling cattle. County wishes to acquire a perpetual scenic conservation easement over approximately Z acres of the westernmost portion of the Ranch for approximately \$X.

The purpose of the proposed transfer will be to perpetuate the critical viewshed of the State Z coastline, which State Z desires to maintain in perpetuity for the benefit of the public, as authorized and set forth in the PRC. Under the proposed scenic conservation easement, the property shall remain as scenic open space in perpetuity and Taxpayer will not be able to develop the property. Taxpayer retains the right to continue the uses of the property associated with ranching and grazing of existing grazing land.

Taxpayer is willing to convey the conservation easement to the County but only if he receives property of like kind that will qualify for nonrecognition of gain under section 1031. Taxpayer believes that he has identified the specific real property for which he will exchange the conservation easement, and he anticipates that it will be timberland property. If and to the extent he is unable to obtain sufficient timberland property in a like kind exchange, Taxpayer will exchange the conservation easement for either farm land or ranch land. In either event, Taxpayer represents that he will hold the replacement real property for investment or for productive use in a trade or business within the meaning of section 1031(a).

Taxpayer anticipates that he will accomplish this proposed transaction pursuant to a qualified three-party exchange, pursuant to which Taxpayer will convey the conservation easement to a third party in exchange for timberland, or, if necessary, farm land or ranch land, and that the third party will convey the conservation easement to the County in exchange for money.

ISSUE

Does an exchange of the scenic conservation easement for a fee simple interest in replacement real property (timberland, farm land, or ranch land) qualify as an exchange of like-kind property under section 1031?

APPLICABLE LAW & ANALYSIS

Section A of the State Z Civil Code provides, in part, that a conservation easement is an interest in real property voluntarily created and freely transferable in whole or in part for the purposes stated in Section B of the State Z Civil Code. Section B of the State Z Civil Code provides, in part, that a conservation easement means any limitation in a deed in the form of an easement, restriction, covenant, or condition, the purpose of which is to

retain land predominantly in its natural, scenic, historical, agricultural, forested, or open-space condition. Section C of the State Z Civil Code provides that a conservation easement shall be perpetual in duration.

Section 1031(a)(1) provides generally that no gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment.

Section 1.1031(a)-1(b) of the Income Tax Regulations provides generally that, as used in section 1031(a) of the Code, the words "like kind" have reference to the nature or character of the property and not to its grade or quality. One kind or class of property may not be exchanged for property of a different kind or class. The fact that any real estate involved is improved is not material, for that fact relates only to the grade or quality of the property and not to its kind or class. Unproductive real estate held by one other than a dealer for future use or future realization of the increment in value is held for investment and not primarily for sale. Section 1.1031(a)-1(c) provides, as an example, that no gain or loss is recognized if a taxpayer who is not a dealer in real estate exchanges city real estate for a ranch or farm, or exchanges a leasehold of a fee with 30 years or more to run for real estate, or exchanges improved real estate for unimproved real estate.

Rev. Rul. 55-749, 1955-2 C.B. 295 holds that where, under applicable state law, water rights are considered real property rights, the exchange of perpetual water rights for a fee interest in land constitutes a nontaxable exchange of property of like kind within the meaning of section 1031(a).

In Rev. Rul. 72-549, 1972-2 C.B. 472, an easement and right-of-way granted to an electric power company were held to be properties of like kind with improved real property received by the taxpayer.

Rev. Rul. 78-163, 1978-1 C.B. 257, holds that the exchange of timberland for bare land constitutes an exchange of like kind property within the meaning of section 1031(a).

Based upon the above authorities and the facts and representations that were submitted, and assuming the proposed conservation easement is, by virtue of state law, an interest in real property, the exchange of the easement for the proposed replacement property (timberland, farm land, or ranch land), to be held for investment or productive use in a trade or business, will qualify as an exchange of like-kind property for purposes of section 1031.

No opinion is expressed as to the tax treatment of these items (or transactions) under the provisions of any other section of the Code or regulations which may be applicable thereto, or the tax treatment of any conditions existing at the time of, or effects resulting from, the items (or transactions) described which are not specifically covered in the above ruling. Specifically, no opinion is expressed with respect to whether the proposed transaction meets the deferred like-kind exchange requirements of section 1.1031(k)-1.

A copy of this letter should be attached to the federal income tax-return for the year in which the transaction in question occurs.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent.

Sincerely,

Assistant Chief Counsel

(Income Tax & Accounting)

Douglas A. Fahey

Assistant to the Chief, Branch 5