



Pointers for Balancing IRS Audit Risk When Permitting Commercial Forestry on Tax-Deductible Conservation Easements

Background

The Land Trust Alliance offers the following information and suggestions in the hope of helping land trusts assess their own risk and response to a recent IRS assertion. In the U.S. Tax Court case of [*TOT Property Holdings v. Commissioner*](#) (2019), the IRS asserted in its brief that all commercial forestry, even with a management plan required to be consistent with the conservation purposes, is an inconsistent use and, therefore, the conservation easement is nondeductible. “Even when commercial forestry is conducted responsibly, it is inherently inconsistent with significant conservation interests,” wrote the IRS trial attorney. While the bench opinion in this case ignored this argument, and the Court denied the deduction based on the failure of the extinguishment proceeds clause language in the easement to meet the regulations, the Alliance is concerned that the IRS may use this argument in other cases.

The Alliance and its member land trusts disagree with this interpretation of the Tax Code and Treasury Regulations. The Alliance is taking steps to address this issue on behalf of its members with the IRS and the U.S. Treasury, with the U.S. Forest Service and NRCS and by filing friend of the court briefs in Tax Court and appellate courts should additional cases arise. Meanwhile, please evaluate your easement template with your land trust attorney.

The Alliance urges all land trusts and their advisors to take a balanced view of this IRS litigation strategy. At the same time, we suggest taking appropriate steps to be certain that *any* forestry clause, especially in a deductible or bargain sold easement, has substantial protections for conservation purposes and vests *conservation* decision-making in the land trust and its professional foresters or other advisors. The following drafting pointers will help you consider the minimum criteria for a sound forestry clause, whether the landowner manages the conserved land for timber income or whether forest management activities support personal use goals, such as firewood production, habitat improvement or recreation.

Drafting Pointers

If your donors or their advisers fear an IRS audit, they can reduce audit risk of the easement transaction by ensuring the appraisal value is moderate and fully substantiated, having fully substantiated documentation of the entire easement transaction and, finally, drafting all clauses with conservation purposes as the first priority. In all donated conservation easements, be sure to articulate that any forestry activities must be consistent with the overall conservation purposes of the easement and provide for the land trust or its designee (such as a professional forester or biologist) to make that determination. Ultimately, in all conservation easements, the land trust has the sole right and obligation to ensure consistency with conservation purposes. Responsibility for a donor’s tax deduction remains with the donor. Donors must seek advice from their own legal and tax counsel.

The following drafting pointers are a distillation of the key points from the Alliance's 2001 Working Forest Conservation Easements publication. That publication emerged from an extensive national learning circle on best practices in commercial forestry. The learning circle included land trusts and foresters across the country. This 2020 Pointer is not intended to replace or update that publication, but to offer land trusts some minimal basic suggestions for reviewing existing easement templates in light of the IRS increased disallowance of all types of permitted rights in deductible conservation easements. Land trusts may wish to consider some of the following alternatives, worded as developed by your attorney, other professional advisors (such as foresters or wildlife biologists), staff and board and informed by your state law, policies and experiences.

1. *Document how forest management activities support the conservation purposes and perpetual restrictions using one or more of these approaches or something similar.*
 - Include in the background statement or whereas clauses any relevant local, state or federal policies or programs that support the use of the property for forestry or forest conservation. This might include, for example, reference to the Forest Inventory and Analysis (FIA) Program of the U.S. Forest Service, as well as any state Forest Legacy Program priority areas.
 - Include in the purposes clauses forestry and/or forest conservation purposes, as well as other easement purposes. If such purposes are not stated, future easement interpreters may see the forest goals as unimportant, discretionary or even conflicting with other stated purposes.
 - If the easement articulates specific goals and restrictions to favor a defined forest type (see point 2, below), state the motivating conservation purposes for the goals upfront. If the major purposes relate to forest conservation and forestry, it may be advantageous to identify and prioritize those. Fully consider the likely changes to a forest over time and the forecasted changes from a different climate.

2. *Specify goals or objectives for any forest management activities, including personal use activities. Goals should be consistent with a perpetual document and the realization that land, soils, forests and climate will change over time.*
 - Without information as to what type of forest is desired, neither landowner nor easement holder, as advised by professional foresters, can determine if the forest is being managed in support of the purposes of the easement. As the link between easement purposes and forest management actions, the easement goals must be clearly articulated and defined. For example, if maintaining a particular natural community is the goal, then the goal should include sufficient information to measure success in maintaining that community.
 - To help the IRS comprehend the interrelationship of protected purposes and conservation goals, articulate the *intended benefits* in the purposes section and elaborate on them in the baseline documentation report.
 - State principles of management where the easement contemplates a variety of forest management possibilities. In these cases, management is not aimed at a specific desired future condition, but follows broad parameters set forth in the easement forestry clause. This approach is useful, for example, when the easement holder wants to encourage a landowner to keep the land in production by whatever means makes most sense (within the bounds of the easement) on lands where forest production is only marginally profitable. It is also used by easement holders who wish to avoid prescriptive terms that require extensive monitoring.
 - Alternatively, some land trusts prefer to state specific objectives of management, such as wildlife habitat improvement or water quality improvement, when the landowner and easement holder can describe a specific, mutually desired forestry outcome and the

easement holder can monitor that result. This approach can risk irrelevance over time unless the outcomes are broadly written or unless they include alternatives to address change.

- Consider articulating performance goals as a lens through which the land trust (or as advised by its forester) can review any required forest management plan or individual timber harvest. This approach can be useful when (1) timber value is high and owners manage regularly for commercial purposes and keep detailed inventory information, and/ or (2) the regulatory environment assures that detailed forest inventory data will be available. The specific restrictions on timber harvest (enumerated elsewhere in the easement) become the sidebars within which the landowner seeks to accomplish the performance goals over time.

3. *Design restrictions appropriate to protect the conservation purposes and to guide all forest management activities.*

- Most easements that allow for commercial forestry should require a forest management plan. The plan must be prepared by a knowledgeable professional, usually a licensed professional forester, and periodically updated. The easement holder must have a role in plan review or approval. The review ensures that the forest management plan conforms to the easement, conservation values are protected and easement holder interests are maintained.
- The plan, tailored to landowner and easement goals, should fully address protected conservation values, may decrease the need for prescriptive language, should provide clear guidance for monitoring and enforcement and can be revised to accommodate changed conditions, evolving technology or knowledge or disaster.
- While not all land trusts formally approve the plan itself, all must ensure that the plan's outcomes, as advised by a professional forester, wildlife biologist or other qualified individual, are consistent with the easement's conservation purposes. Only the land trust has the right to make that determination. Anything less is a red flag in an IRS audit.
- Many land trusts tie forest management activities to best management practices (BMPs) established and periodically updated by public agencies or educational institutions. The easement holder can draw on public experts, such as state or county foresters, to help interpret management issues. Most easements reference BMPs, either generally for all forest management activities, or specifically for road construction, erosion control and other defined issues. Easements that use BMPs should specify which BMPs are to be applied. Couple BMPs with a detailed forest management plan requirement to address the full scope of conservation values that an easement must protect. Note that BMPs vary across state lines and can be subject to the varied interpretation and level of enforcement of public agency representatives. They may also be minimal and often do not address other conservation values.
- Explore what other forestry standards or guidance exists from other public agencies or private institutions charged with habitat or other conservation purposes. Many sustainable forestry organizations offer certification standards that your land trust and its advisors might consider incorporating into the easement or using to assist with a determination that forestry activities are consistent with the conservation purposes.
- All timber production must be compatible with the maintenance of non-timber forest values, including overall ecosystem function, biological diversity, wildlife habitat, water quality and aesthetics. Add additional specific restrictions or management prescriptions to protect specific resources or define thresholds for acceptable management. These should address significant management issues, such as buffer zones for bodies of water, special management provisions for sensitive natural areas and size limits for clearcuts, roads, skid trails, landing areas, temporary structures and large equipment. Include only restrictions that are necessary to protect core purposes and goals.

4. *Limit additional landowner permitted rights related to forestry.*
 - Avoid incompatible uses and include a statement that no activity shall be permitted that is inconsistent with the purposes of the easement.
 - Limit new road construction and forestry related structures, such as sawmills, to minimize erosion and avoid sensitive areas and other adverse impacts to conservation values.
 - If gravel removal for access road construction or maintenance is contemplated, follow IRS requirements restricting surface mining or exclude the gravel location from the easement area.
 - Require restoration of all disturbed areas. You might also consider seasonal restrictions to avoid soil compaction or destruction.

5. *Ensure that the determination of whether a specific activity is consistent with the conservation purposes of the easement is made solely by the land trust, in consultation with its advisors.*
 - Courts appear to disfavor prior approval provisions that they may perceive as pressuring holders to approve landowner requests. The most common of these are approval formulations that require the holder to be “reasonable” or, conversely, that the holder’s approval “shall not be unreasonably withheld.” Land trusts should avoid these reasonableness standards and insist on mutual consent or sole discretion based on whether a requested activity is consistent with the conservation purposes.
 - Be sure to state both the review standard and that the consistency with conservation purposes is determined solely by the land trust in any approval statement. Such language can support the taxpayer’s claimed deduction.
 - Remember that in American jurisprudence, a reasonableness standard is tied to economics and commercial viability, not conservation. Land trusts must uphold conservation purposes and, to do so, must be designated as the sole determiner of that fact.

Stay the course: sound forestry practices enhance conservation values. Land trusts and their advisors can document this for the IRS in any deductible easement.

Questions?

Please call or write to Leslie Ratley-Beach, Conservation Defense Director, at 802-262-6051 or Sylvia Bates, Director of Standards and Educational Services, at 603-708-1073.

Disclaimer

The Land Trust Alliance designed this material to provide accurate, authoritative information about the subject matter covered, with the understanding that the Land Trust Alliance is not engaged in rendering legal, accounting, tax or other professional counsel. If a land trust or individual requires legal advice or other expert assistance, they should seek the services of competent professionals. The Land Trust Alliance is solely responsible for the content of this series.

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