

Rev. Rul. 59-121, 1959-1 CB 212, IRC Sec(s). 1231

Headnote:

Rev. Rul. 59-121, 1959-1 CB 212 -- IRC Sec. 1231 [CAUTION: This Rev Rul has been clarified by Rev Rul 68-291, 1968-1 CB 351.]

Reference(s): Code Sec. 1231; Reg § 1.1231-1

The consideration received for the granting of an easement with respect to land constitutes the proceeds from a sale of an interest in real property. The amount received should be applied as a reduction of the cost or other basis of the land subject to the easement. Any excess over basis constitutes recognized gain. Where the land affected was used by the taxpayer in his trade or business and held for more than six months, any recognized gain from the granting of the easement is to be treated in the manner provided in section 1231 of the Internal Revenue Code of 1954.

Full Text:

Advice has been requested as to the treatment for Federal income tax purposes of amounts received from the granting of easements under the circumstances described below.

The taxpayer is the owner in fee of certain land which he has used for many years for the grazing of livestock raised for sale. During the taxable year, the taxpayer entered into a contract with an industrial company by which the company was granted easements, of indefinite duration, with respect to specified portions of the taxpayer's land in return for a designated amount of money. The easements in question provide (1) for the construction of a dam across a creek located on the taxpayer's property in order to create a reservoir and impound water for industrial purposes, and (2) for the use of portions of the taxpayer's land as depositories for waste material produced as a by-product of the company's industrial process.

The easements further provide that the taxpayer retains all rights to explore for and produce oil, gas, or other minerals upon and from <Page 213> the land upon which easement rights are granted and shall have the rights of ingress and egress over and across such land in connection with such exploration and production. The taxpayer also retains the right to use and enjoy the land and any buildings thereon provided he does not interfere with the easement rights granted.

In I.T. 2621, C.B. XI-1, 67 (1932), it was held that the amount received from the sale of an easement to construct and maintain power transmission lines across farm land, where the owner retained more than the naked legal title to the land affected, should be applied against the cost or other basis of the land, and any excess over such basis for determining gain or loss would be taxable gain. See also G.C.M. 23162, C.B. 1942-1, 106, and Rev. Rul. 54-575, C.B. 1954-2, 145; *Raytheon Production Co. v. Commissioner*, 144 Fed. (2d) 110, certiorari denied, 323 U.S. 779; *Farmers and Merchants Bank of Catlettsburg, Ky. v. Commissioner*, 59 Fed. (2d) 912; *Telefilm, Inc. v. Commissioner*, 21 T.C. 688.

The facts of the instant case indicate that the taxpayer retains more than naked legal title to the property affected by the easements, inasmuch as he retains all oil, gas, and mineral rights and the use of buildings situated on the land for the entire period of the easements. Therefore, the contract between the taxpayer and the company constitutes the grant of easements in land and not the transfer of the ownership of such land. See I.T. 2621, *supra*. Since the easement is with respect to land, it constitutes an interest in real property. Compare I.T. 3693, C.B. 1944, 272, which holds that the interest of a lessee in oil and gas constitutes an interest in "real property" for Federal income tax purposes. Inasmuch as the land has been used for many years in conjunction with the taxpayer's business, such land constitutes property used in the trade or business.

Accordingly, the consideration received for the granting of an easement with respect to land constitutes the proceeds from a sale of an interest in real property. The amount received should be applied as a reduction of the cost or other basis of the land subject to the easement. Any excess over basis constitutes recognized gain. Where the land affected was used by the taxpayer in his trade or business and held for more than six months, any recognized gain from the granting of the easement is to be treated in the manner provided in section 1231 of the Code.