

Reconciling Mineral Rights and Conservation Easements

By Blair Fitzsimons, Executive Director, [Texas Agricultural Land Trust](#)

According to the Texas A&M *Land Trends* Study, Texas is losing its rural lands faster than any other state in the country. Mindful of this fact, leaders from the Texas Farm Bureau, Texas & Southwestern Cattle Raisers Association and Texas Wildlife Association came together in 2006 to create the Texas Agricultural Land Trust (TALT). While there are 49 land trusts in Texas, TALT is the only one whose sole mission is the protection of agricultural lands. The second largest land trust in Texas today, TALT works with landowners who *voluntarily* choose to place a perpetual agricultural conservation easement on their ranch. TALT is also unique among land trusts in that it proactively works with landowners to make conservation easements compatible with oil and gas development.

An agricultural conservation easement restricts development while allowing most other uses of the property. For landowners, this means that they can continue grazing cattle or hunting just as before. They can build fence, windmills and waterings without prior permission. Large buildings, like barns and houses, are confined to a “building envelope” that concentrates development in several areas around the ranch. Prohibitions extend to non-agricultural commercial activities, such as surface mining and wind-development. TALT and the landowner negotiate an agreement that works for that particular property and that family, making each agreement unique.

In return for voluntarily giving up the right in perpetuity to develop the property, the landowner receives significant income tax benefits. A donation of the value of the restrictions is made to the land trust, which is then entrusted with ensuring that those restrictions are upheld. Through an appraisal, this donation---or the difference between the value of the property before the restrictions versus the value of the property with the restrictions--- is determined. The landowner can then deduct that amount against 50% of adjusted gross income and carry forward the unused portion of the donation for 15 years. (These enhanced provisions expire at the end of 2011, when it reverts to 30% of AGI and a 5-year carry-forward.) Additionally, the value of the property is reduced, thus making it possible for one’s heirs to enjoy the property without having to sell all or part for estate tax purposes.

When I give presentations around the state, the first question typically asked is, “what about oil and gas development?” While lawyers much more qualified than I devote hour-long presentations to the subject, the answer can be boiled down to this: While surface mining is not allowed, the IRS permits sub-surface extraction as long as there is a “ limited, localized impact... that [is] not irretrievably destructive of significant conservation interests.”

What does that mean? Basically, as long as extraction of the minerals has minimal-to-no permanent impact on the conservation value of the easement, the IRS will probably allow the deduction. By inference, the landowner who is granting the conservation easement must have a degree of control over surface damages, either through a surface use agreement or surface protection provisions in the lease itself. Otherwise, the deductibility of the donation may be questioned by the IRS.

There are four different scenarios that typically play out when TALT assesses this issue for landowners interested in donating a conservation easement:

- **The landowner owns the minerals, and the minerals are not leased.** This scenario poses the least risk to the deductibility of a conservation easement. A landowner who owns the mineral

estate and has not previously leased the minerals can either subordinate the mineral interest to the conservation easement, or ensure adequate surface use protections when negotiating a lease. The landowner can also pursue a surface use agreement that specifically protects the conservation values as part of mineral development.

- **The landowner owns the minerals, and the minerals are leased.** The risk involved with donating a conservation easement under this scenario will depend on the terms of the lease. Unless expressly restricted in the lease, a mineral lessee's use of the surface will be governed by common law doctrine, which affords the landowner little protection from the mineral lessee's use of the surface. The landowner runs a risk of not qualifying for the tax deduction unless the mineral lessee agrees to subordinate its interest to the conservation easement or enter into a surface use agreement with surface protections.
- **The landowner does not own the minerals, and the minerals are not leased.** This scenario is a bit more complicated. The landowner must first determine who owns the oil and gas minerals. Once ownership is clarified, the deductibility of a conservation easement will depend on who controls surface mining and whether the conservation values can be protected through a surface use agreement.
- **The landowner does not own the minerals, and the minerals are leased.** As in the second scenario, here the landowner must look to the terms of the oil and gas lease to determine if there are adequate surface protections. If there are none in the lease, the mineral lessee will have the right to use the surface without restriction, in which case the landowner runs a high risk of not obtaining the deduction.

Placing a perpetual conservation easement on one's ranch is an enormous step, and should not be entered into without extensive due diligence: Is it right for the family? Is it consistent with one's goals for the ranch? Does it make financial sense? Equally important is to understand the implications of donating a conservation easement on land with a severed mineral estate. TALT encourages any landowner interested in a conservation easement to seek legal counsel. Through careful analysis and preparation, it is possible for Texas landowners to both develop their minerals and protect open space, agricultural lands and native wildlife habitats for generations to come.

Nothing in this article constitutes legal, financial or tax advice. TALT wishes to thank Joseph Fitzsimons and Trace Burton, of Uhl, Fitzsimons & Jewett, for their contributions to this article. For more information on TALT, please check their website at www.txaqlandtrust.org or call 210-826-0074.