Internal Revenue Service

Number: **202549006**
Release Date: 12/5/2025
Index Number: 856.01-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:FIP:B01
PLR-113482-23

Date:
September 03, 2025

Legend:

Taxpayer	=
Subsidiary	=
Program 1	=
Program 2	=
Program 3	=
Protocol A	=
Protocol B	=
State A	=
State B	=
Agency	=
State B Program	=
Organization 1	=
Organization 2	=
Organization 3	=
Project	=
a	=
b	=
c	=
d	=
e	=
f	=

g	=	
h	=	
Year 1	=	
Year 2	=	

Dear :

This letter is in reply to a letter from Taxpayer's representative dated June 30, 2023, and subsequent correspondence, in which Taxpayer requests rulings that (i) Taxpayer's income attributable to the issuance of Credits (defined below) will accrue under section 451 of the Internal Revenue Code ("Code") upon the earliest date on which such Credits are earned, received, or due, unless section 451(b)(1)(A) requires earlier inclusion, and (ii) pursuant to section 856(c)(5)(J)(ii), income attributable to the issuance of Credits will be considered qualifying income for purposes of section 856(c)(2) and (3).

Facts:

Taxpayer is a State A corporation that has elected under section 856 to be taxed as a real estate investment trust ("REIT") for federal income tax purposes. Taxpayer's accounting method is an accrual method, and its taxable year is the calendar year.

Taxpayer owns (directly or through disregarded entities) approximately a acres of timberlands in the United States. Taxpayer and Subsidiary, a qualified REIT subsidiary of Taxpayer, currently participate in a voluntary carbon credit program. Taxpayer (directly or through a disregarded entity) intends to participate in two other voluntary carbon credit programs, and a taxable REIT subsidiary ("TRS") (or a disregarded entity of the TRS) may be involved in all three programs. The methodologies implemented by the two other voluntary carbon credit programs are similar, and a project under one program generally can be converted into a project under the other.

Under each of the three programs, Taxpayer expects to receive verified credits or units corresponding to reductions in greenhouse gas emissions generated from Taxpayer's timberlands ("Credits"). Taxpayer represents that Credits will be issued to Taxpayer, or a disregarded entity of Taxpayer, and that Taxpayer (directly or through a disregarded entity) will bear the benefits and burdens of ownership of the relevant Credits until the sale of such Credits, unless the Credits are transferred to a taxable REIT subsidiary of Taxpayer prior to their sale.

Program 1

Taxpayer intends to participate in Program 1, a voluntary program managed by Organization 1, a tax-exempt organization. Under Program 1, participants comply with restrictions on timber harvesting and other uses of specified parcels of timberlands. In return, Organization 1 issues Credits to the Program 1 participants. The program allows entities to use Credits issued under the program to offset their emissions by retiring the Credits. Participants that earn Credits can sell them to entities that wish to use them.

Credits, when issued under Program 1, initially cannot be used to satisfy legal obligations of businesses subject to any mandatory cap-and-trade program. Such Credits, however, can be transitioned into credits that can be used toward compliance with State B Program (“State B Program Credits”), a cap-and-trade program of State B, upon a review of the related project documentation by Agency, an agency of State B. To transition the Credits into State B Program Credits, Agency conducts a full review of the project documentation. Upon verification that the respective Credits meet the requirements of the State B Program, the Credits issued under Program 1 can be transitioned into State B Program Credits that can be used toward compliance with the State B Program.

To be eligible to be issued Credits under Program 1, Taxpayer undertakes certain obligations and restrictions on the harvest of timber and use of specified parcels of timberland for the duration of a specified crediting period. These include:

- Identifying forested stands that adhere to the requirements and restrictions of Program 1 (each, a “Program 1 Property”);
- Refraining from converting each Program 1 Property to a non-eligible use, such as impermissibly harvesting the Program 1 Property;
- Modeling what Credits can be produced and monitoring each Program 1 Property to validate the model;
- Engaging a third-party auditor to review the model and reports of its monitoring, and to issue validation and verification reports if the auditor agrees with the findings;
- Sending such validation and verification reports to Organization 1 for Organization 1 to register the Credits for each Program 1 Property once such reports pass Organization 1’s review;
- Demonstrating that the permanence of carbon stock is maintained with respect to Program 1 Property on which tree harvesting occurs; and
- Putting in place management systems to ensure the carbon against which the Credits are issued is not lost during a final cut with no subsequent replanting or regeneration.

Each Program 1 Property will be owned by disregarded entities of Taxpayer. In addition, each Program 1 Property will consist of land, including unsevered natural products of land (e.g., trees), and qualify as real property within the meaning of section 856.

Credits are issued only after Organization 1 has reviewed the verification report and validation report, which include the quantity of emission reductions or removals for that Program 1 Property during the crediting period. Organization 1 will register the Credits issued under Program 1 over a period of years, based on the emissions sequestered each year compared to a baseline for each Program 1 Property. The crediting period for Program 1 can be from b to c years and be renewed d times, but in no event can the total crediting period exceed c years. Taxpayer plans to elect a term of b years.

Program 1 requires that a specified percentage of Credits be held in a pooled buffer account as "buffer credits." Buffer credits cannot be sold immediately. Buffer credits are intended to offset risks that arise in the event a Program 1 Property fails to produce the expected reductions in emissions.

After issuance of the Credits, Program 1 will periodically validate and verify each Program 1 Property. If a Program 1 Property fails to reduce emissions as expected, the cancellation of accumulated buffer credits is the sole mechanism to address the failure of a Program 1 Property to produce the anticipated greenhouse gas reduction or removal. Buffer credits can be released from the buffer pool over time and converted to Credits as the longevity of a project is demonstrated and risks associated with the project diminish.

Taxpayer represents that the Program 1 land-use restrictions described above are restrictions that could be recorded as easements under local law. However, since Organization 1 does not require recordation, Taxpayer does not intend to record easements under local law.

Program 2

Taxpayer also intends to participate in Program 2, a carbon offset program administered by Organization 2. Program 2 is a voluntary carbon market for owners of timberlands that can legally harvest timber. Under Program 2, participants commit to restrictions on timber harvesting within a geographic boundary (each, a "Program 2 Property"). The program offers a methodology to quantify the reduction in emissions attributable to a project through comparison of emissions of the project with the restrictions with certain baseline forest management practices.

Enrolling in Program 2 initiates an immediately effective, legally binding, and public-facing commitment to increase carbon stocks on the Program 2 Property for b years by harvesting less frequently or intensely. To be eligible to be issued Credits under Program 2, Taxpayer undertakes certain obligations and restrictions on the harvest of timber and use of each Program 2 Property for the duration of a specified crediting period. These include:

- Establishing that the project on each Program 2 Property exceeds the requirements of all currently effective laws and regulations;

- Evaluating the predominant forest management practices of the region and demonstrating that the project on each Program 2 Property will increase carbon sequestration compared to common practice;
- Providing evidence that the project on each Program 2 Property faces at least one barrier to implementation (financial, technical, or institutional);
- Limiting harvesting by harvesting less frequently or intensely within each Program 2 Property;
- Adhering to specified sustainable management requirements;
- Submitting to independent third-party validation; and
- Refraining from planting non-native plant species.

As noted above, because the methodologies implemented by Program 1 and Program 2 are similar, a project under one program generally can be converted into a project under another. Following the final internal review and verification by Organization 2, Program 2 issues Credits that can be retired or sold. Credits issued under Program 2 can be transitioned into State B Program Credits that can be used toward compliance with State B Program and then sold to third parties to satisfy a portion of their respective cap-and-trade program compliance obligations.

Each Program 2 Property will be owned by disregarded entities of Taxpayer. Each Program 2 Property will consist of land, including unsevered natural products of land (e.g., trees), and qualify as real property within the meaning of section 856.

Participants in Program 2, including Taxpayer, commit to limits on harvesting for a period of at least f crediting periods of g years. After each crediting period, the project's baselines and projections are recalculated and the project is subject to the latest standards and rules of Program 2.

Participation in Program 2 requires mitigation of the risk of loss of any sequestered carbon (whether it results from a natural disturbance or a decision of the participant). To offset risk, a Program 2 participant may have buffer credits held in a buffer pool (as in Program 1), obtain insurance, or use another mitigation strategy approved by Program 2. Taxpayer intends to mitigate risk with buffer credits for its initial participation in Program 2 but may elect another method for future properties. As is the case for Program 1, if a Program 2 Property fails to reduce emissions as expected, the cancelation of buffer credits is the mechanism to address the failure.

Also, as with Program 1, Taxpayer represents that the Program 2 land-use restrictions are restrictions that could be recorded as easements under local law. However, since Organization 2 does not require recordation, Taxpayer does not intend to record easements under local law in connection with Program 2.

Program 3

Taxpayer owns Project, which is currently registered with Program 3, through Subsidiary. Project consists of land, including unsevered natural products of land (e.g., trees), and qualifies as real property within the meaning of section 856. Program 3 is a carbon offset program administered by Organization 3, a tax-exempt organization. Project was developed and registered with Program 3 in Year 1 and subsequently registered with State B Program in Year 2.

Program 3 administers two separate protocols, Protocol A and Protocol B. Under Protocol A, Program 3 issues a type of credit that can be sold on a voluntary market. Taxpayer currently does not participate in Protocol A. Taxpayer and Subsidiary are currently participating in Program 3's Protocol B.

Under Protocol B, Program 3 issues Credits in a form that cannot be sold. Upon review by Agency, however, those Credits can be transitioned to State B Program Credits, which can be sold to third parties. Under Protocol B, the criteria for issuing Credits that can be transitioned to State B Program Credits is similar to those for issuing Credits under Program 1 and Program 2. Under Program 3, the project term for Protocol B is h years, and the crediting term is e years. If the participant decides not to transition the Credits issued under Protocol B of Program 3 to State B Program Credits, generally the participant can work with Program 3 to convert the Credits into Credits that can be sold on Program 3's voluntary registry.

Following the completion of a crediting term, a project may be renewed for subsequent h-year crediting periods, subject to approval at that time and use of the quantification methods in the most recent approved version of the relevant protocol at the time of renewal.

As with Programs 1 and 2, Program 3 mandates, and Taxpayer complies with, the use of risk reduction measures. Program 3 requires that all forest projects contribute a certain number of buffer credits to a pooled buffer account. The number of buffer credits is a percentage of the total number of the project's Credits, and the percentage is determined by a project-specific risk rating. If a project experiences an unintentional reversal (e.g., fire or disease), Credits that have already been issued are not cancelled or reversed; rather, buffer credits are retired in an amount equal to the total amount of carbon that was reversed.

As noted above, Project is registered under Protocol B of Program 3. Taxpayer's participation in Program 3 is voluntary, even though Taxpayer ultimately receives Credits that meet the requirements of State B Program and sells those Credits to entities that are required to comply with State B Program.

With respect to Project and future projects under Program 3, Protocol B (either, a "Program 3 Property"), Taxpayer is required to comply with all requirements and land-use restrictions of Program 3 in accordance with Protocol B. These include:

- Establishing that the project on each Program 3 Property exceeds the requirements of all currently effective laws and regulations;
- Demonstrating that the project on each Program 3 Property exceeds the emissions reductions that would otherwise occur in a conservative business-as-usual baseline scenario;
- Maintaining or increasing the pre-existing live carbon stock throughout the life of each Program 3 Property;
- Monitoring greenhouse gas emissions within each Program 3 Property;
- Quantifying the emissions reductions within each Program 3 Property;
- Obtaining verification services from an accredited entity;
- Employing and demonstrating sustainable long-term harvesting practices; and
- Promoting and maintaining a diversity of native plant species.

Recordation of an easement is not required to participate in the program, but an easement on the property was recorded under local law to retain the land in its natural forested condition and prevent uses that would significantly impair its conservation values.

Program Advisors and Activities

Taxpayer (directly or through a disregarded entity) intends to engage unrelated third-party companies (each an "Advisor") to conduct activities related to each program ("Program Activities"). Program Activities typically carried out by an Advisor include: (i) developing a project through the program and (ii) acting as an authorized representative of Taxpayer. Program Activities carried out jointly by the Taxpayer and its Advisor(s) include: (i) coordinating and facilitating audits; (ii) completing tasks to maintain the registration of the project, such as on-going monitoring, modeling, assessments, reports, and coordination of verification audits; and (iii) marketing and coordinating the sale of Credits. Program Activities typically carried out by Taxpayer include: (i) acting as the project proponent to which the program issues Credits following final internal review and verification and (ii) acting as the general account holder and administrator of Taxpayer's accounts with respect to Credits, including, but not limited to, ongoing annual administration of the transfer, export, and retirement of Credits. With respect to Programs 1 and 2, Taxpayer intends to pay Advisors a commission in cash based on the number of Credits issued, the purchase price of the Credits sold, or both.

With respect to Program 3, an Advisor receives a percentage of Credits that are initially issued to Taxpayer as a payment-in-kind for the services provided to Taxpayer.

Sale of Credits

As noted above, Taxpayer sells Credits issued under Program 3 to entities covered by State B Program. In the future, Taxpayer may transition Credits issued under Program 1 and Program 2 to State B Program Credits that can also be sold to entities covered by State B Program. On behalf of Taxpayer, an Advisor will market Credits, or assist Taxpayer or a TRS of Taxpayer in marketing Credits, including Credits that are transitioned into credits that can be used in State B Program, to unrelated third-party purchasers.

Taxpayer represents that it does not intend to hold Credits for purposes of speculating on their future appreciation. Taxpayer represents that Taxpayer will include the fair market value of the Credits upon issuance in gross income. Taxpayer further represents that gain, if any, recognized on the sale, transfer, or exchange of Credits will be treated as income not qualifying under section 856(c)(2) and (3).

Law and Analysis:

Section 61(a) defines gross income as "income from whatever source derived," except as otherwise provided by law. See section 1.61-1(a) of the Income Tax Regulations. Gross income includes income realized in any form, whether in money, property, or services. Id. This definition encompasses all "accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." Commissioner v. Glenshaw Glass Co., 348 U.S. 426, 431 (1955).

Section 451 and the regulations thereunder provide rules for determining the taxable year of inclusion for items of gross income.

Under an accrual method of accounting, unless section 451(b)(1)(A) requires earlier inclusion, an item of gross income is generally includible when all the events have occurred which fix the right to receive such income and the amount thereof can be determined with reasonable accuracy. All the events that fix the right to receive income generally occur upon the earliest of the following: (1) the required performance takes place, (2) payment is due, or (3) payment is made. See Schlude v. Commissioner, 372 U.S. 128 (1963); Rev. Rul. 84-31, 1984-1 C.B. 127; Rev. Rul. 80-308, 1980-2 C.B. 162.

Section 856(c)(2) provides that, for a corporation to qualify as a REIT for any taxable year, at least 95 percent of the corporation's gross income for the year (excluding gross income from prohibited transactions) must be derived from dividends, interest, rents from real property, gain from the sale or other disposition of stock, securities, and real property (other than property described in section 1221(a)(1)), abatements and refunds of taxes on real property, income and gain derived from foreclosure property, certain commitment fees, gain from certain sales or other dispositions of real estate assets, and certain mineral royalty income.

Section 856(c)(3) provides that, for a corporation to qualify as a REIT for any taxable year, at least 75 percent of the corporation's gross income for the year (excluding gross income from prohibited transactions) must be derived from rents from real property, interest on obligations secured by mortgages on real property or on interests in real property, gain from the sale or other disposition of real property (other than property described in section 1221(a)(1)), dividends or other distributions on and gain from the sale or other disposition of REIT stock, abatements and refunds of taxes on real property, income and gain derived from foreclosure property, certain commitment fees, gain from certain sales or other dispositions of real estate assets, and qualified temporary investment income.

Section 856(d)(1) provides that rents from real property include (subject to exclusions provided in section 856(d)(2)): (A) rents from interests in real property; (B) charges for services customarily furnished or rendered in connection with the rental of real property, whether or not such charges are separately stated; and (C) rent attributable to personal property which is leased under, or in connection with, a lease of real property, but only if the rent attributable to such personal property for the taxable year does not exceed 15 percent of the total rent for the taxable year attributable to both the real and personal property leased under, or in connection with, such lease.

Section 1.856-4(a)(1) provides that, subject to the exceptions of section 856(d) and section 1.856-4(b), the term "rents from real property" means, generally, the gross amounts received for the use of, or the right to use, real property of the REIT.

Section 856(c)(5)(J) provides that to the extent necessary to carry out the purposes of part II of subchapter M of chapter 1 of the Code, the Secretary is authorized to determine, solely for purposes of such part, whether any item of income or gain which (i) does not otherwise qualify under section 856(c)(2) or (3) may be considered as not constituting gross income for purposes of section 856(c)(2) or (3), or (ii) otherwise constitutes gross income not qualifying under section 856(c)(2) or (3) may be considered as gross income which qualifies under section 856(c)(2) or (3).

Legislative history indicates that Congress intended part II of subchapter M of chapter 1 of the Code to apply to certain "organizations specializing in investments in real estate and real estate mortgages." H.R. Rep. No. 2020, 86th Cong., 2d Sess. 4 (1960), 1960-2 C.B. 819, 820. Congress intended to restrict the beneficial tax treatment of part II of subchapter M of chapter 1 of the Code to "what is clearly passive income from real estate investments, as contrasted to income from the active operation of businesses involving real estate." Id.

Taxpayer will earn Credits for complying with restrictions and limitations on the use of its property that satisfy the standards of the relevant Program for reductions in greenhouse gas emissions. Taxpayer has represented that the land-use restrictions required under each Program could be recorded as easements under local law, and in the case of Project has been recorded as an easement under local law. Taxpayer will incur significant penalties if Taxpayer does not abide by the restrictions to which it has agreed. Thus, the Credits are akin to payments received for granting an easement for a term of years with respect to real property. Cf. Wineberg v. Commissioner, 326 F.2d 157, 169-70 (9th Cir. 1963) (holding amount received for granting 10-year right to use a road was rent rather than sale of an interest in land), aff'g T.C. Memo. 1961-336; Nay v. Commissioner, 19 T.C. 114, 119 (1952) (concluding amount received for granting a "right of way" for a term not to exceed three years is ordinary income because such a "limited easement" does not constitute sale of real property). Under these circumstances, treating Taxpayer's income with respect to the issuance of Credits as qualifying income for purposes of section 856(c)(2) and (3) is consistent with the purposes of part II of subchapter M of chapter 1 of the Code.

Conclusion:

Based on the information submitted and representations made, we rule as follows:

(i) Taxpayer's income attributable to the issuance of the Credits will accrue under section 451 upon the earliest date on which such Credits are earned, received, or due, unless section 451(b)(1)(A) requires earlier inclusion; and

(ii) Pursuant to section 856(c)(5)(J)(ii), income from the issuance of the Credits will be considered qualifying income for purposes of section 856(c)(2) and (3).

This ruling's application is limited to the facts, representations, Code sections, and regulations cited herein. Except as specifically ruled upon above, no opinion is expressed or implied concerning any Federal income tax consequences related to the facts herein under any other provisions of the Code. Specifically, we express no opinion whether Taxpayer qualifies as a REIT under part II of subchapter M of chapter 1 of the Code. Further, we express no opinion on the tax consequences of any dispositions of Credits, including: (A) whether any conversion, transition, or other change to a Credit results in an exchange of the Credit for federal tax purposes or (B) whether any sale, transfer, exchange, or other disposition of Credits: (i) gives rise to qualifying income under section 856(c)(2) or (3), or (ii) constitutes a prohibited transaction described in section 857(b)(6)(B)(iii).

The rulings in this letter are based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. Although this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

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

In accordance with the provisions of a Power of Attorney on file, we are sending a copy of this letter ruling to your authorized representatives.

Sincerely,

Steven Harrison
Chief, Branch 1
Office of Associate Chief Counsel
(Financial Institutions & Products)

cc: