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Conservation easements on land need to be thought through
By Curtis Seltzer

BLUE GRASS, Va.—About 10.6 million privately owned acres -- an area about twice the size of Connecticut -- now carry conservation easements. This land base is growing by more than one million acres annually. Almost 30 million more acres have been conserved through sale, acquisition by government agencies and other means, according to Russell Shay, Director of Public Policy at the Land Trust Alliance in Washington, D.C.

Conservation easements enable landowners -- individuals and corporations -- to donate one or more rights in environmentally important land to a government agency or tax-exempt, charitable organization like a land trust. In return, landowners preserve the look or current uses of their properties and enjoy substantial local, state and federal tax benefits.

An easement can also be sold to a qualified organization. A conservation easement (CE) runs with the land and restricts the use of a property forever. A donated CE allows a landowner to give away -- that is, terminate -- some right in the property while retaining all other rights. The organization that receives the CE is responsible for its enforcement. Once a right is donated, it cannot be retrieved.

CEs promote or protect a conservation purpose in land that has a significant environmental value. If land lacks a conservation importance, it won't qualify. A CE prohibits or limits some activity or use of a property that has a current dollar value.

A common CE is the donation of the right to develop farmland or other undeveloped property for housing and commerce. CEs can also be written that allow limited development as well as the construction of facilities that promote a non-prohibited use, such as building agricultural buildings on preserved farmland.

A CE might also be donated to protect a scenic view, important habitat, watershed, public recreation or open space. The most common purposes are protection of natural areas and wildlife habitat, open space and water resources/wetlands, according to the most recent National Land Trust Census in 2005 at www.lta.org/census/2005. Easements also preserve farmland, prairie, desert, coastal areas and forests.

An appraiser calculates the fair market dollar value of the right being donated. The donation value equals the difference between what the property is worth with the terminated right at its highest and best use and without.

The 100-acre Smith farm near a suburb might be worth \$1.5 million with its development rights; without, it's worth \$500,000. The value of the landowner's donation of all development rights would be \$1 million.

Landowners might also donate the rights to cut timber for commercial purposes, produce minerals, establish a wind farm, erect towers, disturb sensitive habitat, use water in certain ways, hunt or fish and run livestock, among other things.

Every state now authorizes the use of conservation easements to one degree or another. Apart from preserving things as they are, why are more and more landowners placing restrictions on their properties? The answer is simple: tax benefits. A CE's first benefit comes on federal taxes. When an easement is granted in perpetuity, its full market value can be deducted from taxable income.

As of 2007, an individual taxpayer could deduct up to 50 percent of his adjusted gross income a year for charitable contributions, which included cash, goods and CEs. The taxpayer had 15 years to use up his CE amount. The CE charitable deduction reduces the individual's taxable income and, hence, the amount of tax owed. The more the donation value, the less income tax owed. Farmers and ranchers could donate an easement that kept their land in agriculture or livestock production.

Those farmers or ranchers whose gross income from agriculture was more than 50 percent of their total gross income could deduct up to 100 percent of their adjusted gross income in 2007 as long as the income-producing land remained available for farming and ranching. The generous 2006-2007 incentives described above have yet to be extended for 2008. Legislation is currently in conference committee.

Second, CEs lower the value of an individual's taxable estate by the dollar amount of the donation. In addition, the taxpayer's executor is allowed in certain circumstances to exclude from the taxable estate an additional 40 percent of the value of land that bears the CE. The \$1.5 million Smith farm would be valued at \$500,000 after donating its \$1 million in development rights; and for estate purposes, possibly only \$300,000. The 40 percent exclusion cannot exceed \$500,000.

A CE donation can reduce an estate sufficiently to keep it free of any estate tax -- federal and state -- under current rules. Lower estate taxes help to reduce the likelihood that land will have to be sold to pay them. This CE estate-tax benefit helps those who are land rich and cash poor.

A third tax benefit is local. Once a right is donated, the fair market value of a

property should be lowered by the value of the donation. A landowner's property taxes should drop in line with the land's lowered value. Organizations that hold easements don't pay local property taxes on the value of the property rights they own.

State CE tax benefits vary. A CE should help a taxpayer on state income tax. Nine states allow taxpayers to sell the CE tax credit for cash, which generally results in the taxpayer pocketing about 80 percent of its face value. CE tax rules are complicated and changing. Any landowner considering a CE must be led through the process by a knowledgeable and experienced lawyer and CPA. This is not a DIY chore for a Saturday morning. Steve Small, a Boston lawyer who is a leading CE authority, advises clients to "run the numbers" before making any decision. (www.stevesmall.com.)

Critics come at conservation easements from several angles.

First, once development rights are terminated, property will never be worth what it would be if they were still in place. A great deal of money in appreciated value can be lost over the years after development rights are severed. Heirs may not like the results. CEs seem to work best for wealthy individuals who have large, diversified portfolios of assets, including cash. They can be less appropriate for estates where land is the main asset.

Second, CEs have been manipulated to bring more-than-deserved tax benefits to donors by using inflated valuations of the donated rights.

Third, tax benefits have been obtained for donated rights that had no conservation value, such as wetlands that couldn't be developed, or lawns or properties whose scenic views the public could not see.

Fourth, CEs come with a cost. At the federal level, less tax revenue coming from conservation-minded landowners must be made up with revenues from other individuals and sources. This, sadly, applies to all tax breaks. At the local level, reduced property taxes on easement land means less tax revenue, which is either made up from somebody else or done without.

Conservation easements allow private landowners to invest their property with a public purpose—and make it profitable for them to do so. They are increasingly popular, cover more and more ground and are producing significant preservation benefits. If you think a CE might work for you, start your research. Contact organizations that administer easements in your area. Then get competent, experienced legal and tax advice.

If you can preserve both your property's environment and your assets through a conservation easement, you've won twice. But you may have to choose between some money now in the form of tax relief and a lot of money in the

future for your heirs. No lunch is free, even the one that's good for everybody and looks like it's on the house.

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