CONSERVATION EASEMENTS AND TAX CONSEQUENCES

• The Farm Bill enhanced deduction to the end of 2009.
• December 31, 2007 - January 1, 2010
• Recent Tax Changes extend it through 2013

Farm Bill § 15302; I.R.C. § 170(b)(1)(E)(vi) and (2)(B)(iii)
Basic CE Provisions (PPA)

- All taxpayers other than corporations to deduct donations of conservation easements up to 50% of their AGI
- Ranchers and farmers (who receive more than 50% of their gross income from farm or ranch business activities) to deduct donations of conservation easements up to 100% of their AGI
Enhanced Provisions of PPA

• Corporate farmers and ranchers could deduct up to 100% of their taxable income
• Excess charitable deduction from easement donation could be carried forward for up to 15 years
Qualified Farmers and Ranchers

• Qualified farmer or rancher for this provision means a taxpayer whose gross income from the trade or business of farming is greater than 50% of the taxpayer’s total gross income for the year

• (conducting a timber sale to meet these provisions in the year of a donation may be a means of meeting this definition)
Farming is...

1. Cultivating the soil, or raising or harvesting any agricultural or horticultural commodity (including the raising, shearing, feeding, caring for, training, and management of animals) on a farm
Farming is...

2. Handling, drying, packing, grading, or storing on a farm any agricultural or horticultural commodity in its unmanufactured state,

• but only if the owner, tenant, or operator of the farm regularly produces more than half of the commodity
Farming is...

3. Planting, cultivating, caring for, or cutting trees, or the preparation (other than milling) of trees for market

[I.R.C. § 2032A(e)(5)]
Conservation Easements

• “Conservation easement” is a term applied to easements granted for scenic, ecological, wildlife habitat or almost any other conservation purpose

• includes the preservation of open space (including farmland and forest land)
Conservation Easement

• A conservation easement allows qualifying not-for-profit organizations and government units to maintain the scenic and environmental benefits from private land without buying the land outright.
General Rule for CE

• Payments for the sale of a qualifying conservation easement are subject to the general rules for the sale of an easement.
• Landowner is allowed to compare the amount received for the easement with the adjusted tax basis of the property that is affected by the easement.
Sale of CE

• If the payments are less than the adjusted tax basis of the affected property, there is no income to be recognized by the landowner

• the basis of the affected property is reduced by the amount of the payments received

[Rev. Rul. 77-414, 1977-2 CB 299]
Basis Allocation - Easement

• Basis allocation is between the rights retained by the taxpayer and the easement rights that are sold.

• GR: property basis must be allocated between the interest sold and the interest retained in the proportions that their respective fair market values bear to the fair market value of the entire property

CE Sale in Excess of Basis

- 60-acre farm.
- Adjusted basis in the farm is $45,000.
- Sold to maintain working farm / green space, the county offer -$2,000 per acre the development rights

Sale proceeds $120,000

Property Basis $ 45,000
LTCG $ 75,000
Realistic CE Sale in Excess of Basis

Sale proceeds $120,000
Property Basis $ 45,000

Costs of Sale:

Survey $ 3,000
Appraisal(s) $ 3,000
Baseline Doc. $ 2,000

LTCG $ 67,000*

* Land Trusts may require an endowment donation (≈ 5%)
**CE Sale Less Than Basis**

Sale proceeds $ 900,000

Property Basis $ 1,000,000

Remaining Basis $ 100,000

LTCG $ 0

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CE Like Kind Exchange

• L.O. trades CE for fee simple interest in other tract. Easement Value $120K. FMV=$400K Post CE MV= $280. Property basis = $80K

• L.O. has no gain from the exchange, but must allocate his $80K basis in his existing timberland between the conservation easement and the interest he retains in the CE property
# Like Kind CE Basis - After

<table>
<thead>
<tr>
<th>Interest in Property</th>
<th>Fair Market Value (FMV)</th>
<th>Percent of FMV</th>
<th>Allocation of Basis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Timberland after CE</td>
<td>$280,000</td>
<td>70%</td>
<td>$56,000</td>
</tr>
<tr>
<td>Conservation Easement Value</td>
<td>$120,000</td>
<td>30%</td>
<td>$24,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$400,000</strong></td>
<td><strong>100%</strong></td>
<td><strong>$80,000</strong></td>
</tr>
</tbody>
</table>

Existing timberland basis drops from $80 K to $ 56 K
Old basis from timberland transfers to new timberland proportionately ( $24,000 is basis in new timberland)
IRS Scrutiny of C E Donations

- Improper charitable deductions for transfers of conservation easements
- May disallow deductions, impose penalties and excise taxes
Estate Tax Treatment of CE Land

- The Taxpayer Relief Act of 1997 [P.L. 105-34, §508] added I.R.C. §2031(c), allowing an estate to exclude up to 40% of the value of the retained interest in land for which a conservation easement was donated to a qualified organization.

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Estate Tax Treatment of CE Land

- The full exclusion is available if the easement represents at least 30% of the land value.
- Exclusion is reduced by two percentage points for each point the value of the conservation easement falls below 30% of the value of the land.
Estate Tax Treatment of CE Land

- The value of the land is its fair market value without considering the easement but reduced by the value of any development rights retained by the landowner

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Conservation & Tax Deductability

- **Must serve a public benefit**
  - Watershed protection,
  - Conservation of natural areas
  - Conservation of natural or scenic river
  - Conservation of predominantly natural parkland, or
  - Historic landscape conservation
QUESTIONS?

Thank You!!

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