

Conservation Trust For North Carolina

A LANDOWNER'S GUIDE TO CONSERVATION EASEMENTS

By planning today for the future of their lands, North Carolina landowners are leaving an irreplaceable legacy of preserved open space and natural resources for the use and enjoyment of many future generations.

Conservation Easements

Landowners are the primary stewards of the natural and historic heritage of our countryside. Unprecedented development pressures are escalating land values and forcing many landowners to make the decisions regarding the future of their land. Often these decisions are driven by financial needs and estate tax burdens. Fortunately, the use of conservation easements provides a flexible option for private landowners who wish to preserve the natural resources of their lands while meeting their financial objectives.

What is a Conservation Easement?

A conservation easement is a flexible tool that protects land while leaving it in private ownership.

It is a legal and binding agreement between a landowner and a qualified conservation organization such as the Conservation Trust for North Carolina and your local land trust.

Conservation easements can also be held by other qualified entities such as governmental bodies.

The conservation easement agreement in perpetuity is recorded with the deed to the property, and applies to all future owners.

Under the terms of the conservation easement agreement, the landowner agrees to restrict certain future uses of the property, and the conservation organization agrees to see that those restrictions are upheld in the future. The usual restrictions serve to:

1. *protect the special natural, historic and scenic features* of the property (such as woodlands, wetlands, streams, open fields, steep slopes, historic buildings and scenic views);
2. *limit the number, type and location of dwellings and other buildings* on the property. Future dwelling sites are often designated depending upon the size of the property and the nature of the resources being protected; and
3. *prevent harmful activities* such as commercial and industrial uses, quarrying and excavation, and the dumping of solid or liquid waste.

Some conservation easements may specifically allow for future management of land for agricultural and forestry uses.

The landowner *retains title to the property* and continues to have all rights of ownership except for those *rights specifically restricted* under the terms of the easement. The retained rights include the right to sell, lease, bequeath, and subdivide the property subject to the terms of the easement.

The conservation easement *does not necessarily permit public access* to the property unless it is the specific desire of the landowner to include an accessible area or a trail easement corridor as part of the easement.

How Do Conservation Easements Benefit the Community?

Conservation easements serve to protect the community's important natural and scenic assets – its water resources, wildlife habitats, agricultural lands, open space, historic structures, trails, and scenic views – without the need for appropriating public funds.

Lands under conservation easement remain in private ownership and do not require public funds for support and maintenance.

Lands under conservation easement remain on the tax rolls of the community.

Because conservation easements are granted in perpetuity, the community can depend upon eased lands as permanently protected open spaces – a lasting result not possible through zoning or other land use regulations.

How Do Conservation Easements Benefit the Landowner?

Landowners who donate conservation easements derive immense satisfaction from knowing that the scenic and natural resources of the land that they have lived on and cared for will be protected for the use and enjoyment of future generations.

Conservation easements provide families with the opportunity to plan together for the future use of the land thereby avoiding possible conflict and misunderstanding at a later time.

Neighboring landowners who donate conservation easements on contiguous properties can provide mutual protection against unplanned development, and share

the benefits of protecting larger resource areas such as watersheds, agricultural areas, and scenic landscapes.

Landowners who donate conservation easements may be eligible for significant financial benefits through the reduction of federal income, gift, and estate tax.

Financial Considerations for the Landowner

FEDERAL INCOME TAX BENEFITS

In 1969 Congress enacted legislation which permits a landowner to take a *charitable deduction* for the donation value of a qualified conservation easement. Internal Revenue Service regulations issued in 1986 better defined the guidelines, including certain “**conservation purposes**” which must be met for an easement to qualify as a tax deductible charitable donation. (Reg. Sec. 1.170A-14).

PASSING THE “CONSERVATION PURPOSES” TEST

The value of an easement may be deductible for federal income tax purposes if the easement is donated to a qualified organization and meets *at least one of* the following “conservation purposes”:

1. The preservation of land areas for recreation by, or the education of, the general public.
2. The protection of a relatively natural habitat of fish, wildlife, or plants, and similar ecosystems.
3. The preservation of open space, including woodland and farmland, for either the scenic enjoyment of the general public or when such preservation is pursuant to a clearly delineating governmental conservation policy. In either case, a significant public benefit must result from the preservation of such open space.
4. The preservation of an historically important land area or certified historic structure.

The majority of the conservation easements which have been donated have been drafted with the third conservation purpose in mind, for “*the preservation of open space*” and “*the scenic enjoyment of the general public*”.

In addition to meeting at least one of the four conservation purposes, the IRS requires that an easement must *be granted in perpetuity* and be given to a *qualified recipient* organization. The Conservation Trust for North Carolina and more than two dozen regional and local land trusts across the state are such qualified recipient organizations. Federal regulations also require that the holder of an easement be able to enforce the easement. The holder should inspect the easement at least once a year and be prepared to take legal action, if necessary, to uphold the terms of the easement.

VALUE THE DONATION

The value of the donation must be determined by a *qualified appraisal* and is generally equal to the difference between the fair market value of the property before the donation of the easement (the “before value”) and the fair market value of the property after the donation of the easement (the “after value”). The difference between the “before value” and the “after value” is the amount that can be treated as a charitable donation for income tax purposes.

Assume, for example, that the owners of an unrestricted property worth \$1,000,000 place an easement on the land that precludes all future residential development. A qualified appraiser then determines that the land’s fair market value as reduced by the easement is worth \$600,000. In this case the charitable *donation would be valued at* \$400,000. The potential tax savings under this scenario may approximately be computed as follows:

$$\text{Donation} \times \text{Tax Rate} = \text{Approximate Tax Savings}$$

If the donor is in the 40% tax bracket, the calculation would be:

$$\$400,000 \times 40\% = \$160,000 \text{ (Approximate Tax Savings)}$$

While virtually all conservation easements reduce property values, there is no rule of thumb for determining what the diminution in value will be. Reductions can range in value from less than 10% to more than 90% of the fair market value. In general, *the reduction tends to be greatest where a highly restrictive easement is placed on prime development land in an area experiencing intense growth.*

The 30% Limitation

The tax law limits the maximum annual charitable deduction a donor can take. For a gift of appreciated property (which includes most gifts of land and conservation easements), the amount you can deduct in the year of the donation is limited to 30% of your adjusted gross income. If the value of your gift exceeds that level, you may carry forward the excess tax deduction for up to five additional years, applying the 20% of adjusted gross income limit each year. Any remaining portion of the deduction, after the sixth year, cannot be used.

The 50% Election

As an alternative, a taxpayer may use the property’s basis (usually the purchase price or its value when inherited) as the before value rather than using the current market value. In that case, an annual deduction of up to 50% of adjusted gross income is allowed, with any unused deduction carried forward for up to five additional years, applying the 50% of adjusted gross income limit each year. Where property has appreciated in value, the 30% option may be more advantageous. The 50% election is most appropriate for taxpayers whose property has appreciated little, who anticipate a large drop in income, who recently purchased or inherited land, or who do not expect to live to take advantage of the full five year carry forward period.

STATE TAX CREDIT

North Carolina has a unique incentive program to assist landowners to protect the environment and the quality of life. A credit is allowed against individual and corporate income taxes when real property is donated for conservation purposes. Interests in property that promote specific public benefits may be donated to a qualified recipient. Such conservation donations qualify for a substantial tax credit pursuant to North Carolina General Statutes 105-151.12 and 105-130.34. A tax credit is a dollar for dollar reduction in your state tax bill.

Donations must serve a public benefit

They must provide one or more of the following:

- Public beach access and use
- Public access to public waters
- Public access to public trails
- Fish and wildlife conservation
- Other similar land conservation purposes

Other Conditions:

The tax return must be accompanied by a certification form the Department of Environment and Natural Resources that the donation is suitable for one or more of the required public benefits. The property interests covered are outright donations of property and donations of conservation easements. Any portion of the fair market value of donations that is not eligible or taken for credit may be considered as a charitable contribution under NCGS 105-130.9.

Amount of Credit:

Tax credit allowed equals 25% of fair market value of donated property interest, up to a maximum credit of \$250,000.00 for individuals and \$500,000.00 for corporations. Any unused portion of the credit may be carried forward for five succeeding years.

FEDERAL ESTATE TAX BENEFITS

Estate taxes at rates as high as 55% or higher may prevent a family from passing land on from one generation to the next. When landowners die and leave land to their children, the heirs may find that the property has appreciated dramatically since it was purchased, making it difficult to pay inheritance and estate taxes. In some instances, heirs may be forced to sell all or part of the land to pay the estate tax.

The federal estate tax is based on the fair market value of a property at the time of a landowner's death. Because conservation easements reduce the appraised fair market value of the land, an easement donated by a landowner prior to death, or by will, will reduce the total value of the state. While income tax deductions are limited (as discussed above) *no such restrictions apply to federal estate taxes, so estate tax savings can be substantial.*

Estate Tax Exclusion

As part of the Tax Relief Act of 1997, a landowner's estate is now additionally entitled to exclude from taxation a portion of the estate net assets amounting to a percentage of the value of a qualified conservation easement. The maximum exclusion is \$100,000 for estates of decedents dying within 1998 and thereafter it escalates at the rate of \$100,000 per year to a total of \$500,000 in the year 2002. The qualification for and calculation of this exclusion is dependent upon a number of considerations that should be carefully reviewed by the landowner and his or her advisors.

Donating and Easement by Will

A conservation easement can also be granted by will. With this option estate taxes will be reduced; however, you will not receive an income tax benefit. If you intend to donate an easement by will, it is necessary, during your lifetime, to establish the terms of the easement with the intended holder of the easement.

This collaborative planning ensures that the easement meets your conservation goals as well as the objectives of the long-term easement holder. The proposed easement may be added as a codicil to your will now, with specific instructions to your executor to complete the easement in the event of your death. Your will can be amended later if family or financial circumstances change, or if you grant the easement in your lifetime. Meanwhile, you will have protected the land and lowered your estate taxes.

Federal Gift Tax Benefits

The donation of a conservation easement reduces the appraised value of the land, and thus may reduce federal gift taxes associated with a gift of land to other during your lifetime.

Landowners considering the donation of a conservation easement should consult their personal advisors regarding all legal and tax implications

NOTE: For more detailed information on tax planning and family lands, ask your land trust for a copy of "Preserving Family Lands" by Stephen J. Small.

The Conservation Easement Planning Process

The most important part of the easement process for the land trust *is to understand your individual needs and desires in planning for the future of your property.* We will then work closely with you to design a Conservation Plan which will preserve the natural and scenic characteristics of the property, meet your specific financial objectives, and further the conservation goal of the land trust and the community. The Conservation Plan must meet the criteria for accepting easements established by the land trust. For property owners interested in receiving favorable tax treatment, the land trust will carefully research and document the “conservation purposes” of the easement.

The process for planning a conservation easement includes the following steps:

1. ***Defining the Landowner’s Objectives***

The land trust will meet to discuss landowners’ desires for the future preservation of the property and to understand the family’s financial and tax planning considerations. We will walk the property with the landowner and evaluate the natural, historic and scenic resources of the property.

2. ***The Proposal and Cost Estimate***

A proposal and cost estimate will be presented to the landowner for planning and preparation of the easement documents.

3. ***Evaluation of the Property Preparation of Natural Features Map***

The land trust will prepare a natural features map of the property that carefully details its physical characteristics, highlighting sensitive resources.

4. ***Conservation Plan proposals***

A draft conservation plan will be proposed for the landowner’s consideration.

5. ***Preparation of the Conservation Plan/Draft Conservation Easement Agreement***

The land trust staff will draft conservation easement documents for review by landowner and his or her advisors.

6. ***Preparation of Background Documentation Report***

The land trust will prepare background documentation report establishing current condition of the property including research intended to meet IRS requirements for easement donations.

7. ***Approval, Signing, and Recording of the Final Easement Agreement***

The final easement agreement will be approved, signed and recorded with copies of documents delivered to landowner for safekeeping.

Note: If there is an existing mortgage on the property at the time of the easement donations the lender is *required to subordinate the mortgage to the conservation easement.*

Estimating the Costs of Preparing an Easement

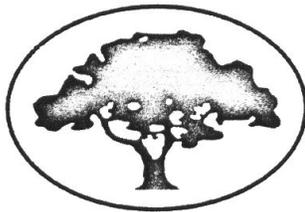
In order to be able to continue our work, we ask that the landowner help reimburse the land trust for its costs in preparing an easement.

These costs will be estimated in the proposal prepared for the landowner at the outset of the project, and will cover the materials and staff time needed to complete the easement. In addition, easement donors will have their own legal, appraisal, and in some cases, surveying costs to consider. Surveying needs vary widely and depend upon the nature of the Conservation Plan in which the landowner is interested. In many cases no surveying is required.

In addition to the preparation costs, we request a one time contribution toward our *easement stewardship fund* in order to assure that the land trust is able to meet its obligation to uphold the terms of the easement in perpetuity. The amount of endowment requested is based on the size of the property, the complexity of the easement, and the amount of staff time that will be required on an annual basis to administer and monitor the easement. A certain amount of each endowment contribution is designate for legal fees should the need ever arise in the future for the land trust to meet its obligation to defend the terms of the easement.

Note: The easement stewardship contribution and most of the costs of preparing the easement are deductible for income tax purposes.

For more information regarding conservation easements and other conservation options for landowners, please contact the
Conservation Trust for North Carolina



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