

Introduction to Conservation Easements



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What is a Conservation Easement?

A voluntary, legal agreement between a landowner and a qualified holder that permanently limits a property's uses in order to protect the property's conservation values.



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What is a Conservation Easement?

- **A real property interest**
- **Filed at the courthouse**
- **Runs with the land**



What is a Conservation Easement?

- Part of the title of the land
- Land can be sold or gifted
- Will be binding on all future owners



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What is a Conservation Easement?

- **Selectively removes rights from the title of the land**
- **Very little is required**
- **Each easement is individually tailored**



What is a Conservation Easement?

- **Provided for in the state law by Texas Natural Resources Code Section 183**



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Types of Conservation Easements

Donated easements, governed by IRS regulations – must be perpetual to qualify for a deduction (Section 170(h) IRC)

Purchased easements (a.k.a Purchase of Development Rights – PDR; or Purchase of Agricultural Conservation Easement – PACE), governed by the rules of the organization making the purchase; depending on the funder, can be for a term of years

Bargain Sale, or a combination of a donated and purchased easement, most commonly used to offset tax considerations



Purpose of Conservation Easements

Conservation easements have different purposes

- Protection of significant natural resources including water and/or endangered species and their habitats
- Protection of historical resources
- Public access, for recreation and/or education

The purpose of an **agricultural conservation easement** is to protect the viability and productivity of agricultural lands while also protecting other conservation values such as wildlife habitat, water quality; and/or scenic landscapes.



Agricultural Conservation Easement

- Limits future non-ag use of the land
- Encourages the business of ranching or farming
- Flexibility allows ranch or farm to adapt to changing economic conditions
- Permits construction of new ag buildings and residential dwellings;
- Does not require public access
- Landowner retains private ownership of the ranch or farm subject to the easement restrictions
- Allows for oil and gas activity as long as there is minimal permanent damage to the surface



Oil & Gas Production

Sub-surface extraction is allowed if there is minimal permanent damage to the surface

- Driven by IRC requirements
- “Limited and Localized”
- Restoration after production
- May involve surface use agreements



Other Minerals

- Surface Mining is Prohibited
- Required by the IRC
- Techniques to deal with borrow pits



Agricultural Conservation Easement

The process is essentially the same for donated and purchased easements

- Determine reserved rights (how many partitions will be allowed, how many “building envelopes”, etc.)
- Get an appraisal, preferably from an appraiser who has experience appraising conservation easements
- Develop a “baseline report” that documents the condition of the property at the time of the transaction



Other considerations

- Term or perpetual
- Condemnation
- Termination



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Tax Savings: An Overview

How a CE provides tax savings

- Income tax deduction when donated
- Lower appraised value in estate



Tax Incentives – Donated Easements

Current tax scenario:

- Can deduct donation against 30% of adjusted gross income (AGI)
- Carry-forward = In addition to the year of the donation, 5 years

Enhanced tax incentives (pending in Congress):

- Can deduct donation against 50% of adjusted gross income (AGI)
- Carry-forward = In addition to the year of the donation, 15 years



Tax Incentive: How it works

Hypothetical Example:

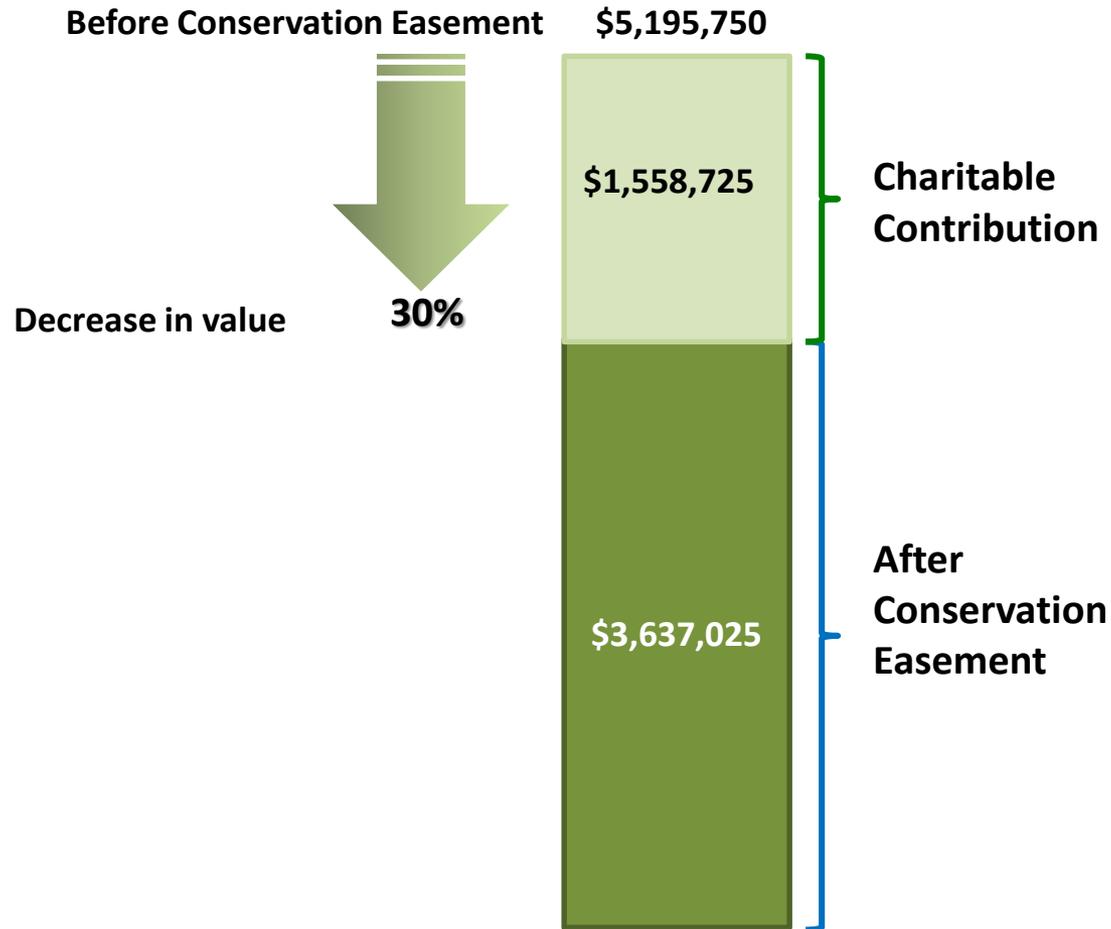
1,750 acre ranch in Central Texas

Average price per acre = \$2,969*

Market value: \$5,195,750

*source: Texas A&M Real Estate Center, Rural Land Values, Texas Region 7:
Austin, Waco, Hill Country

Tax Incentive: How it works





Tax Deduction: Current Scenario

Let's assume that the landowner's annual adjusted gross income for income tax purposes is \$200,000, which remains constant.

The deduction resulting from the easement is as follows:

(30 percent of \$200,000 = \$60,000)

Year of Contribution	\$60,000
Carry-forward to Year 1	\$60,000
Carry-forward to Year 2	\$60,000
Carry-forward to Years 3-5	<u>\$180,000</u>
TOTAL DEDUCTION	\$ 360,000

Potential charitable deduction (from previous slide) = \$1,558,725

Bottom line: Does not work for this landowner!



Tax Deduction: Enhanced Incentive

Let's assume that the landowner's annual adjusted gross income for income tax purposes is \$200,000 which remains constant.

The deduction resulting from the easement is as follows:
(50 percent of \$200,000 = \$100,000)

Year of Contribution	\$100,000
Carry Forward to Year 1	\$100,000
Carry Forward to Year 2	\$100,000
Carry Forward to Years 3 – 14	<u>\$1,300,000</u>
TOTAL DEDUCTION	\$ 1,600,000

Bottom line: The Landowner is able to use up the entire deduction

Estate Tax Considerations



Estate Tax Considerations

\$17 Million



Jones Ranch

\$17 Million



Smith Ranch

Estate Tax Considerations

\$17 Million



Jones Ranch

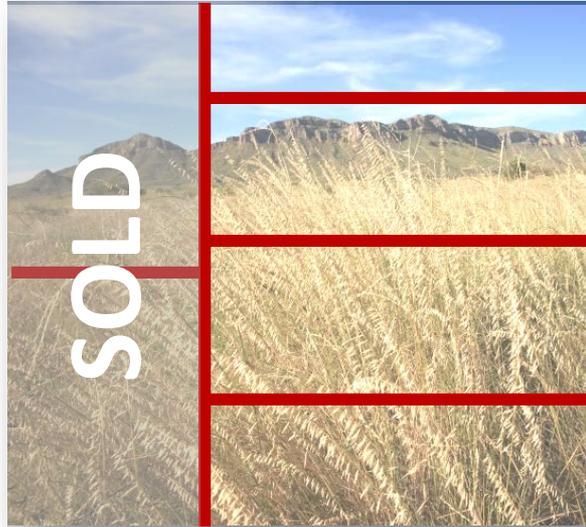
~~\$17~~ 9 Million



Smith Ranch

Estate Tax Considerations

\$17 Million



Jones Ranch

~~\$17~~ 9 Million



Smith Ranch

FET / Sales to pay taxes / divisions for heirs



Purchased Agricultural Conservation Easements

Federal (Purchase of Development Rights)

- Agricultural Conservation Easement Program (formerly known as the NRCS Grasslands Reserve Program and the Farm & Ranch Protection Program)
- Passed within the 2014 Farm Bill
- May 1 USDA announced \$386 Million for ACEP



Purchased Agricultural Conservation Easements

State

- **Texas Farm & Ranch Lands Conservation Program**
 - Managed by Texas Parks & Wildlife Department
 - Oversight board = representatives from statewide agricultural organizations
 - Received a \$2m appropriation in last legislative session



Purchased Agricultural Conservation Easements

Local / Resource Specific

- City of San Antonio \$360 million Aquifer Protection Initiative, 2000, 2005, 2010 and 2015 – to protect the Edwards Aquifer
- City of Austin \$50 million open space protection bond initiative, 2006 – to protect Barton Springs
- U.S. Army ACUB Program – to create open space buffers around military installations



The Easement Holder

- A non-profit land trust whose mission is land conservation; or a governmental entity
- Has the right to monitor and enforce the easement
- Typically visits the property once a year to ensure that the terms of the easement are being upheld
- 26 Texas land trusts, each with a specific mission



Texas Agricultural Land Trust

- Mission is to halt the loss and fragmentation of rural, agricultural lands in Texas
- Board comprised of landowners who understand the day-to-day challenges of working lands
- Holds agricultural conservation easements on rangeland, farmland and native wildlife habitat throughout the state
- Does not interfere in day-to-day management of farming or ranching

What are the benefits and drawbacks?



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Benefits

- A voluntary mechanism to protect property from fragmentation or development – fits family’s long-term stewardship goals for the farm or ranch
- Income tax deduction
- Estate tax benefits/facilitates inter-generational transfer
- Convert equity to cash (purchased easements)
- Accomplishes the objectives of some landowners



Drawbacks

- Projects are expensive
- Cash match isn't always available
- Take a long time to complete
- Do not ensure that the land will continue to be farmed, ranched or managed for wildlife – only that the land will be available for agriculture and hunting
- Sale of conservation easement is subject to capital gains tax
- Tax benefits are generally only available to the first generation of easement donors
- Use of property is limited for the future
- Value of the property is reduced by the conservation easement



Informational Resources

Texas Agricultural Land Trust www.txaglandtrust.org

Texas A&M Land Trends Study www.texaslandtrends.org

Texas Land Trust Council <http://www.texaslandtrustcouncil.org/>

Land Trust Alliance www.lta.org

American Farmland Trust www.farmland.org;
www.farmlandinfo.org



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Texas Agricultural Land Trust

www.txaglandtrust.org

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