CONSERVATION EASEMENTS IN PRIVATE PRACTICE

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Editors' Synopsis: This Article presents an overview of conservation easements that is designed to help practitioners better incorporate the tool into practice in order to reap the myriad benefits that state and federal law authorize. By providing an account of the development of conservation easements, an outline of current available legal benefits, and examples of hypothetical treatment in various states, the Author provides practitioners with that which is necessary to put the conservation easement to use for their clients.

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I. INTRODUCTION

"[W]e seem ultimately always thrown back on individual ethics as the basis of conservation policy. It is hard to make a man, by pressure of law or money, do a thing which does not spring naturally from his own personal sense of right and wrong."[1]

Aldo Leopold, thought of by many as the father of land conservation, understood keenly that economics and the conservation of land do not go hand in hand. In fact, in a market-driven nation focused on minimal government intervention and possessing strong views of private property rights, the conservation of American lands has faced significant cultural headwinds. This cultural backdrop begs the question: if we do not depend on government measures to protect land for future generations, how can we achieve such an important goal?

Enter the conservation easement. This unique legal construct provides private landowners with both the financial motivation and the legal framework to conserve their lands in perpetuity. State enabling acts—adopted in some form in all fifty states—supply the legal underpinnings for this wholly American form of land conservation. One author has suggested that the related American ideals of freedom of contract and the right of the individual to make long-term land use agreements have fostered the American enchantment with the conservation easement.[2] Instead of being forced by government regulation to limit the use of their land, landowners are free to make personal decisions regarding their land and to work with local nonprofit partners to tailor conservation agreements that meet specific personal needs and qualify for meaningful tax benefits.[3] In short, the conservation

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[1] Aldo Leopold, *Conservationist in Mexico*, AMERICAN FORESTS (March 1937), *reprinted* in ALDO LEOPOLD'S SOUTHWEST 207, (David E. Brown & Neil B. Carmody eds., 1990).

[2] *See* Jessica Owley Lippmann, *The Emergence of Exacted Conservation Easements*, 84 NEB. L. REV. 1043, 1072 (2006).

[3] *See id.* at 1090.

easement is a distinctly American answer to the dilemma articulated by Leopold.

For practitioners, the tax benefits of conservation easements provide important tax and estate planning opportunities.[4] Additionally, this tool provides the practitioner a better way to serve a growing segment of conservation-minded clients who are concerned about the long-term status of their lands for legacy or environmental purposes.[5] In light of these tremendous opportunities, lawyers involved in tax planning, environmental law, and real property law should understand the nature of the conservation easement and strive to incorporate the tool in their practices.

This Article addresses three distinct subjects pertaining to the conservation easement. Part II discusses the real property origins, enabling statute framework, and history of the conservation easement. Part III provides an in-depth review of conservation easement tax law and examples of potential tax benefits. Part IV addresses the often-altruistic client motivations that drive the conservation easement field and presents the case for widespread use of the conservation easement in private legal practice.

II. ORIGINS AND HISTORY OF THE CONSERVATION EASEMENT

A. Defining the Conservation Easement

In a 1959 paper, urban planner William Whyte coined the term "conservation easement" and favored the term for its broad representation of the benefits offered by this unique servitude.[6] His ideas centered on the premise that limiting the development of land could benefit the public.[7] Originally, Whyte's ideas were quite radical, but both politicians and the public—who increasingly understand the toll of urban sprawl, population growth, and environmental degradation on society—have embraced the ideas.[8] The term "conservation easement" is now widely used, and "has proven more durable than any single attempt to articulate the legal nature of a conservation easement."[9]

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[4] *See id.* at 1090–91.

[5] *See id.*

[6] *See* Duncan M. Greene, *Dynamic Conservation Easements: Facing the Problem of Perpetuity in Land Conservation*, 28 SEATTLE U. L. REV. 883, 890 (2005).

[7] *See id.*

[8] *See id.*

[9] *Id. But see* RESTATEMENT (THIRD) OF PROP. (SERVITUDES) § 1.6 (2000) (employing the term *conservation servitude* rather than *conservation easement*).

Conservation easements are created "by the landowner's conveyance of a deed that splits fee simple ownership of property into possessory and development rights, with the landowner . . . retaining possessory rights and relinquishing certain development rights to an organization qualified to hold conservation easements."[10] After the negotiation, drafting, and recording of the deed, the landowner continues to own the land subject to the conservation easement.[11] The holder of the conservation easement—in many cases a nonprofit entity called a "land trust"—has the right and obligation to enforce the terms of the easement, which typically include prohibitions on extensive subdivision of the land, commercial use, and environmental degradation.[12] Conservation easements are flexible and regularly allow landowners to live on the land, practice agriculture, or manage timber, among other permissible uses.[13]

The conveyance of development rights to a third party generally reduces the value of the property subject to the conservation easement because the land is limited in its future use.[14] Land subject to a conservation easement may lose between fifty and eighty percent of its fair market value, depending on the value of the development rights when relinquished.[15] Landowners, however, may recoup some of the cost of conveying these easements (in terms of lost fair market value) by taking advantage of significant federal income and estate tax benefits.[16] In addition, twelve states grant state income tax credits for qualifying conservation easement donations.[17] The loss in fair market value in the property also may result in lower property taxes for the taxpayer.[18] In sum, while landowners do deed away valuable development rights, they may receive a package of valuable tax benefits in return that cumulatively equals or exceeds the value lost in the conveyance. For landowners who plan never to develop their land, wish to protect a working farm, desire to keep land in the family, or want to protect

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[10] Greene, *supra* note 6 at 889.

[11] *See id.*

[12] *See id.*

[13] *See* Lippmann, *supra* note 2, at 1072–74.

[14] Christen Linke Young, *Conservation Easement Tax Credits in Environmental Federalism*, 117 YALE L.J. POCKET PART 218, 218–19 (2008).

[15] *See id.*

[16] *See id.*

[17] *See id.*

[18] *See* Burnet R. Maybank, III, *Tax Implications of Conservation Easements in South Carolina*, 7 S.C. ENVTL. L.J. 1, 1–2 (1998).

the environmental integrity of their acreage, this arrangement can provide substantial tax benefits at minimal subjective cost.[19]

Of course, the donation of a perpetual conservation easement is irrevocable, and cannot be undone if the landowner has a change of heart or a change in fortune. In addition, in reducing the value of his or her land, the landowner also will reduce the amount to be received upon a subsequent sale of the land, or the size of the estate to be left at his or her death to descendants or other beneficiaries.

B. History of Conservation Easement Use

The use of common law easements to conserve lands dates from 1893, when Massachusetts "authorized acquisition of rights in land"[20] "to protect an 'emerald necklace' of parks around Boston."[21] In addition, the federal government used easements to protect "viewsheds" from the Blue Ridge and Natchez Trace Parkways in the 1930s.[22] However, because common law obstacles hindered the use of easements for such purposes, states ultimately developed enabling statutes that created a new type of real property servitude—the conservation easement.[23]

Massachusetts and California were the first states to adopt enabling acts for conservation easements, in 1956 and 1959, respectively.[24] Originally, these statutes allowed only government entities to hold an easement and failed to provide clear guidance on how the new servitudes would operate.[25] These aspects of the first statutes made the conservation easement an unpopular tool at its outset.[26] In 1969, Massachusetts became the first state to allow nonprofits to hold conservation easements, a feature subsequently adopted by every other state.[27] Nonprofit entities since have become com-

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[19] *See e.g.*, Lippmann, *supra* note 2, at 1089–94.

[20] *Id.* at 1096.

[21] Mary Ann King & Sally K. Fairfax, *Public Accountability and Conservation Easements: Learning from the Uniform Conservation Easement Act Debates*, 46 NAT. RESOURCES J. 65, 71 (2006).

[22] *See id.*

[23] *See* Lippmann, *supra* note 2, at 1085–86.

[24] *See id.,* at 1086.

[25] *See id.*

[26] *See id.*

[27] *See id.*; Debra Pentz, *State Conservation Tax Credits: Impact and Analysis,* 32–34 (Conservation Resource Center 2007), *available at* http://www.landtrustalliance.org/policy/documents/state-tax-credits-report.pdf.

monplace holders of conservation easements.[28] Certain nonprofit entities that specialize in holding, managing, and enforcing conservation easements are known as "land trusts."[29] These entities generally are organized to serve landowners in a specific area, and thus have local knowledge of and are familiar to the communities they serve.[30] Such local advantages have helped land trusts to stimulate dramatic increases in land conservation through the use of conservation easements.[31]

The success of conservation easements in protecting land and bolstering local communities is illustrated best through an example. Near the town of Walhalla, South Carolina, nearly 1,000 acres surrounding Civil-War-era railroad tunnels and a treasured 100-foot waterfall have been permanently protected, in large part, through the use of conservation easements.[32] The protected area, which surrounds Stumphouse Mountain and Issaqueena Falls in the Blue Ridge Mountains, contains important natural habitat and provides a tourism draw for the local community.[33] This conservation easement transaction provides long-term economic and natural-resource benefits for residents of the area.[34] Such community benefits and conservation success stories exist in nearly every corner of the United States.[35] The conservation easement has been utilized to protect jewels as diverse as historic farms in the mountainous High Country of North Carolina and natural habitat and prehistoric rock art near Taos, New Mexico.[36]

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[28] *See, e.g.*, William C. Means, Jr., *The Economic Value of Conserved Land: Examining Whether Conservation Easements Represent a Sufficient Source of Land Value to Influence the Outcome of Regulatory Takings Claims*, 69 OHIO ST. L.J. 743, 777 (2008).

[29] *See, e.g.*, Green, *supra* note 6, at 887–88.

[30] *See* Lippmann, *supra* note 2, at 1072.

[31] *See id.* at 1072–73.

[32] Press Release, The Nature Conservancy, Stumphouse is Saved! (Aug. 30, 2007), *available at* www.nature.org/wherewework/northamerica/states/southcarolina/press3114.html (last visited Dec. 22, 2009).

[33] *See id.*

[34] *See id.*

[35] *See, e.g.*, LAND TRUST ALLIANCE, INSPIRING PLACES, INSPIRED PEOPLE: 2008 ANNUAL REPORT 2 (2009), *available at* http://www.landtrustalliance.org/about-us/who-we-are/Alliance-2008-Annual-Report.pdf.

[36] The Land Trust Alliance, *History Lives in North Carolina,* http://www.landtrustalliance.org/community/Regions/southeast/success-stories/history-nc/ (last visited Feb. 4, 2009); The Land Trust Alliance, *Over a Thousand Acres More,* http://www.landtrustalliance.org/community/Regions/west/success-stories/thousand-acres/ (last visited Feb. 4, 2009).

The modern national trend in using conservation easements to conserve privately owned land is clear:

> By 1990, land trusts had used conservation easements to protect 450,000 acres. By 2000, conservation easements had been used by land trusts to protect nearly 2.6 million acres, representing an almost fivefold increase in their use. And by 2003, conservation easements had been used to protect more than five million acres, tripling the number of acres protected three years earlier.[37]

Statistics show that this national trend has continued. The 2005 National Land Trust Census revealed that local and state land trusts utilized "these private, voluntary agreements [to] save 6,245,969 acres in 2005, versus 2,514,566 just five years [earlier]."[38] Part of this trend in growth is tied to the increasing presence of land trusts in local communities. Between 2000 and 2005, land trusts increased in number from 1,263 to 1,667.[39]

According to the 2005 census, California, Maine, Colorado, Montana, Virginia, New York, Vermont, New Mexico, Pennsylvania, and Massachusetts are the states with the most local acres bound by conservation easements.[40] The American West and Southeast represent the fastest growing regions in terms of acres conserved and number of land trusts.[41] In subsequent Sections this Article examines the full range of motivations and incentives that drive the success of conservation easement transactions, but generally speaking, "[p]rivate conservation works because it's locally driven, supported by sound tax policy, and people-oriented."[42]

C. Unique Place of the Conservation Easement in Real Property Law

From a real property perspective, the conservation easement "splits the 'Blackstonian bundle' of property rights."[43] To take the analogy a step further, the conservation easement perhaps can be viewed as an entirely new stick in a property owner's bundle. The following discussion traces the con-

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[37] Greene, *supra* note 6, at 888.

[38] Press Release, The Land Trust Alliance, Private Land Conservation in U.S. Soars (Nov. 30, 2006), *available at* http://www.landtrustalliance.org/about-us/news/alliance-news/private-land-conservation-in-u.s.-soars (last visited Dec. 23, 2009) (citations omitted).

[39] *See id.*

[40] *See id.*

[41] *See id.*

[42] *See id.*

[43] Young, *supra* note 14, at 218.

servation easement's evolution from common law roots to modern statutory enactments and reveals the truly unique nature of this servitude. The real property concepts most similar to conservation easements include the traditional easement, the real covenant, and the equitable servitude.

The common law easement is one of the oldest forms of land use restriction.[44] *Black's Law Dictionary* defines an *easement* as:

> An interest in land owned by another person, consisting in the right to use or control the land . . . for a specific limited purpose. . . . The land benefiting from an easement is called the *dominant estate*; the land burdened by an easement is called the *servient estate*. [A]n easement may last forever, but it does not give the holder the right to possess, take from, improve, or sell the land.[45]

Easements have several key elements, but among the most important are whether the easement is affirmative or negative, and whether the easement is appurtenant or in gross.[46] While an affirmative easement requires the owner of the servient estate to allow the easement holder to perform an affirmative act on the servient estate (such as the use of a right of way), a negative easement prohibits the owner of the servient estate from doing something he would otherwise be entitled to do.[47]

Although American courts routinely uphold affirmative easements, the courts limit the validity of negative easements to specialized categories in reliance on foundational English law.[48] Currently, American courts generally recognize the validity of negative easements for the protection of: (1) flow of air, (2) stream of light for a building or for solar panels, (3) physical support of a building, (4) "flow of an artificial stream," and (5) an unobstructed view.[49]

The second key element of an easement is whether it is appurtenant or in gross. An easement appurtenant involves obligations that are tied to land—it is created to both benefit a dominant tract and burden the servient

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[44] *See* Lippmann, *supra* note 2, at 1075.

[45] BLACK'S LAW DICTIONARY (9th ed. 2009) (emphasis in original); *see also* 28A C.J.S. Easements § 2 (2008).

[46] *See* Lippmann, *supra* note 2, at 1075.

[47] *See* BLACK'S LAW DICTIONARY 586–87 (9th ed. 2009) (affirmative easement & negative easement); *see also* 25 AM. JUR. 2D EASEMENTS AND LICENSES § 6 (2008).

[48] *See* Lippmann, *supra* note 2, at 1075–76.

[49] BLACK'S LAW DICTIONARY 587 (9th ed. 2009); *see also* Lippmann, *supra* note 2, at 1075–76.

tract.[50] Because an easement appurtenant is fixed to the dominant and servient properties, future owners of the dominant and servient estates will be bound by the same benefits and obligation as were the original parties to the easement.[51]

An easement in gross is an easement that benefits a particular person. Frequently, the easement holder does not own any land adjoining the servient property.[52] American courts favor easements appurtenant over easements in gross and will interpret an ambiguous instrument accordingly.[53] Notably, jurisdictions differ as to whether easements in gross are transferable or assignable.[54]

Traditionally, parties may enforce an easement through a suit at law for monetary damages or through the equitable relief of an injunction. In limited cases, "self-help" is available, as easement holders may "personally remove obstacles to an easement."[55] Easements generally may be terminated by agreement of the parties or by the running of a fixed term or after a specified event stipulated in the original agreement.[56] Although state law varies widely on the subject, easements may also be terminated by release, abandonment, estoppel, prescription, merger, or eminent domain.[57]

While common law rules concerning easements provide ways to restrict the use of land, they also substantially restrict a landowner's ability to conserve land in perpetuity.[58] Landowners intending to conserve their property for future generations might wish to create a servitude that limits present and future owners from performing acts on the property that run counter to certain conservation purposes.[59] Such a negative enforcement right held by another party—as opposed to a right tied to the land—is best described as a "negative easement in gross."[60] Landowners seeking to conserve their land with such a tool also might want the servitude to be assignable or transfera-

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[50] BLACK'S LAW DICTIONARY 586 (9th ed. 2009).

[51] *See* Lippmann, *supra* note 2, at 1076.

[52] BLACK'S LAW DICTIONARY 586 (9th ed. 2009).

[53] *See* Lippmann, *supra* note 2, at 1076.

[54] *See id.* at 1077; *see also* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 4.6 (2000) (favoring free transfer and assignability of easements in gross when not personal in nature).

[55] *See* Lippmann, *supra* note 2, at 1077.

[56] RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 7.1 (2000).

[57] *See id.*; *see also* Lippmann, *supra* note 2, at 1077.

[58] Lippmann, *supra* note 2, at 1084–85.

[59] *See id.*

[60] *Id.*

ble if the original enforcing party should become incapable or cease to exist.[61]

Unfortunately for a landowner interested in such an easement, the common law only recognized limited forms of negative easements, none of which were in gross (tied only to an enforcing party rather than a dominant estate).[62] Additionally, while courts increasingly have recognized the ability to assign or transfer easements in gross, such transferability could be called into question if the easement were negative in nature.[63] Thus, the common law easement was ill-suited to achieve even the most basic of a land owner's conservation goals.

Because the traditional rules of common law easements cannot be relied upon to accomplish a landowner's long-term conservation goals, alternative real property tools, including the real covenant and equitable servitude, merit consideration as potential solutions. While real covenants allow negative restrictions on land, the limitations of technical privity requirements make them awkward tools for land conservation purposes.[64] Additionally, many jurisdictions limit the "running of the burden"—the obligation of the bound party—when the benefit of the real covenant is in gross.[65] Finally, the violation of a real covenant generally results only in money damages to an enforcing party.[66] When the goal is to conserve the environmental, habitat, or scenic values of the land, a monetary remedy may be inadequate or irrelevant.

Equitable servitudes are another option for land conservation and appear more attractive than the real covenant because of the lack of privity requirements for the burden and benefit to run.[67] However, in many jurisdictions equitable servitudes are also subject to the rule that the burden of the servitude will not run when the benefit is in gross. And because land trusts and government entities most often hold the benefit of conservation easements in gross, this rule would prevent such easements from binding a future land owner. The fundamental common law rules applicable to real

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[61] *See id.* at 1084.

[62] *See id.*; *see also* BLACK'S LAW DICTIONARY 587 (9th ed. 2009).

[63] *See* Lippmann, *supra* note 2, at 1084; *see also* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 4.6 cmt. b (2000).

[64] *See* Lippmann, *supra* note 2, at 1084.

[65] *Id. But see* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 2.6, § 4.6 (eliminating the traditional limitation on burden running when benefit is in gross).

[66] *See* 20 AM. JUR. 2D COVENANTS, ETC. § 52 (2008).

[67] *See* Lippmann, *supra* note 2, at 1085.

covenants and equitable servitudes thus reduce their usefulness in attaining perpetual land conservation goals.

The Restatement (Third) of Property notes that "[t]he uncertainty and difficulties imposed by the common law of servitudes led to the widespread enactment of statutes."[68] These statutes (sometimes referred to as conservation easement enabling statutes) validate conservation easements without regard to common law limitations, "but limit their coverage to servitudes held by governmental bodies and charitable organizations."[69] Thus, legislative acts, rather than common law precedent, generally underlie the ultimate validity of the conservation easement. While the *Restatement (Third)* has taken positions that mitigate many of the common law restrictions on conservation easements, the enabling statutes have ensured that conservation easements will be valid and enforceable under state law.[70] As a result of such legislation, conservation easements are often referred to as statutorily authorized negative easements in gross.[71]

Because of their status as public and, in many cases, charitable assets, conservation easements also may be protected from certain modification and termination rules that apply to private servitudes.[72] The *Restatement (Third),* federal tax law, and the comments to the Uniform Trust Code and Uniform Conservation Easement Act all contemplate that the charitable trust doctrine of cy pres should be utilized to reform a conservation easement when changed conditions make the original goals of the easement untenable.[73] In this context, cy pres may serve to protect the public's inter-

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[68] RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 1.6 cmt. a (2000).

[69] *Id.*

[70] *See id.* § 2.6, §4.6 (mitigating common law barriers regarding traditional servitudes); *see also* Bennett v. Comm'r of Food & Agric., 576 N.E.2d 1365, 1367 (Mass. 1991); ("Where the beneficiary of the restriction is the public and the restriction reinforces a legislatively stated public purpose, old common law rules barring the creation and enforcement of easements in gross have no continuing force.") United States v. Blackman, 613 S.E.2d 442 (Va. 2005) (in gross conservation easement valid under the common law).

[71] *See* Lippmann, *supra* note 2, at 1085.

[72] *See* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 7.11.

[73] *See id.*; UNIF. CONSERVATION EASEMENT ACT § 3 cmt.; 12 U.L.A. 165, 185 (2008); Unif. Trust Code § 414 cmt., 7C U.L.A. 362, 512–13 (2006); Treas. Reg. § 1.170A-14(g)(6) (1999). For academic support for applying *cy pres* to conservation easements, see for example, Jeffrey A. Blackie, *Conservation Easements and the Doctrine of Changed Conditions*, 40 HASTINGS L. J. 1187, 1216–17 (1989); Nancy A. McLaughlin, *Conservation Easements: Perpetuity and Beyond,* 34 ECOLOGY L.Q. 101 (2007); Jeffrey Tapick, *Threats to the Continued Existence of Conservation Easements,* 27 COLUM. J. ENVTL. L. 257 (2002); Alexander R. Arpad, Note, *Private Transactions, Public Benefits, and Perpetual Control*

est and investment in conservation easements by retaining the servitudes' overarching conservation goals while accommodating certain inevitable changes to land use and the environment.[74] The argument that cy pres doctrine should apply to reform conservation easements often is based on a perceived public legal interest in these instruments—a perception supported by substantial public investment in such easements through taxpayer-funded federal and state subsidies.[75] Thus, the application of cy pres may be appropriate for conservation easements held by government bodies or conservation organization because such easements are routinely supported by tax incentives or appropriations.[76] However, despite the *Restatement,* uniform laws, federal tax law, and academic support, the application of cy pres in this area is still a matter of some debate and uncertainty.[77] In any case, the fact that charitable trust principles may apply to this servitude again demonstrates the unique nature of the conservation easement.

The conservation easement occupies a unique space in the universe of real property law. While sharing some attributes of common law servitudes, easements, and covenants, the tool is distinct. Thus, practitioners should give special care to the drafting of and counsel concerning such easements. Practitioners should understand and emphasize to clients that these unique

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Over the Use of Real Property: Interpreting Conservation Easements as Charitable Trusts, 37 REAL PROP. PROB. & TR. J. 91 (2002).

[74] *See* Blackie, *supra* note 73, at 1217.

[75] *See id.*

[76] *See* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 7.11 cmt. a (2000).

[77] *See* Nancy A. McLaughlin, *Rethinking the Perpetual Nature of Conservation Easements,* 29 HARV. ENVTL. L. REV. 421, 461 (2005) (presenting a well-formed argument that cy pres should apply in the conservation easement context, but noting that "[t]o date, there have been no reported cases in which a court has applied the doctrine of cy pres to modify or terminate a conservation easement"). Cases in this area have a habit of settling. *See, e.g.*, Salzburg v. Dowd, Stipulated Judgment, Civil Action No. CV-2008-79 (Feb. 17, 2010) (approving a settlement in which a County's attempted termination of a tax-deductible perpetual conservation easement was declared null and void; the Wyoming Attorney General brought suit against the County and the owner of the land for improper termination, and prominent among the legal arguments made by the Attorney General was the claim that the County breached its fiduciary duties to both the easement donor and the public by agreeing to terminate the easement without obtaining court approval in a *cy pres* proceeding) (on file with Author); Nancy A. McLaughlin & Mark Benjamin Machlis, *Amending and Terminating Perpetual Conservation Easements*, 23 PROB. & PROP. 52 (2009) (discussing other cases in which the amendment or termination of a perpetual conservation easement was challenged by the state attorney general or others, and the cases either settled or were decided with the easement remaining intact or the violator paying significant damages to replace lost conservation values).

servitudes are notably different from traditional easements and other common law concepts.

D. Conservation Easement Enabling Legislation

As noted above, both the states and the federal government experimented with the use of easements to conserve land relatively early in American history.[78] However, only after the nonprofit entity emerged as a viable conservation easement holder and possible common law obstacles to the servitude were abrogated did the tool become practical for private landowners. The Uniform Conservation Easement Act (UCEA), formally approved by the National Conference of Commissioners on Uniform State Laws (NCCUSL) in 1981, provided states with a model statute that swept away certain common law impediments that might otherwise undermine a conservation easement's validity.[79] The American Bar Association initially assigned NCCUSL the daunting task of drafting a uniform act for conservation easements in 1975, prompted by the concerns of lawyers, legislator confusion, the potential common law obstacles to conservation easements, and a lack of uniformity in existing state laws.[80] The UCEA also, notably, allowed third party nonprofit organizations to hold such easements.[81]

Most states have adopted either the UCEA in whole or a statute that reflects the chief features of the act's provisions.[82] Currently, all fifty states and the District of Columbia have enacted some form of a conservation-easement enabling statute that removes common law impediments to the servitude.[83] These state statutes generally require that the easements be conveyed for one or more conservation purposes (as provided in the statute) and to either a government agency or charitable organization (such as a land trust).[84] Ultimately, the UCEA and subsequent state adoption of conservation-easement enabling statutes have provided a strong legal foundation for the validity and enforcement of this unique servitude.

The UCEA defines a conservation easement as:

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[78] *See supra* notes 20–24 and accompanying text.

[79] *See* UNIF. CONSERVATION EASEMENT ACT, Commissioners' Prefatory Note, 12 U.L.A. 165, 166 (2008).

[80] *See* King & Fairfax, *supra* note 21, at 73–74.

[81] *See* UNIF. CONSERVATION EASEMENT ACT § 1, 12 U.L.A. 165, 174 (2008).

[82] *See* RICHARD BREWER, CONSERVANCY: THE LAND TRUST MOVEMENT IN AMERICA 150 (UPNE 2003).

[83] *See* McLaughlin, *supra* note 77, at 426.

[84] *Id.*

> A nonpossessory interest of a holder in real property imposing limitations or affirmative obligations the purposes of which include retaining or protecting natural, scenic, or open-space values of real property, assuring its availability for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.[85]

Most states have adopted this definition or a similar variant.[86] While exploring the details of each state enabling act is beyond the scope of this Article, it is important to understand that these acts represent the legal underpinning of the conservation easement in every American jurisdiction and wholly dispense with historical common law obstacles to the creation and enforcement of such easements.[87]

III. FEDERAL AND STATE LAW AND THE CONSERVATION EASEMENT

> *Note to reader: This Article was written in early 2009, when certain federal tax laws were in effect. At the end of 2009, federal tax laws passed in the EGTRRA reforms of 2001 and other federal tax provisions related to conservation easement donations lapsed without Congressional intervention. As a result, the reader should understand that the law discussed herein is that which was effective in 2009, and is not necessarily the law as it applies currently. While the future tax treatment of conservation easements is unclear, there are efforts underway to extend the generous tax benefits in effect in 2009 through 2010 and retroactive to January 1, 2010.*[88] *If*

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[85] *See* UNIF. CONSERVATION EASEMENT ACT § 1, 12 U.L.A. at 174.

[86] BREWER, *supra* note 82, at 150. While minor, but important, distinctions exist in nearly all state enabling statutes, this Article does not attempt to catalogue those distinctions.

[87] *See id.*

[88] *See* Land Trust Alliance, Senate Passes One-Year Extension of the Enhanced Easement Incentive!, www.landtrustalliance.org/policy/advocates/adv-031010 (last visited March 17, 2010). Note that, as of March 16, 2010, both the House and Senate have passed similar bills that would retroactively reinstate a one year extension of the higher tax incentives for conservation easement donations, which would be applicable for donations made from January 1, 2010 to December 31, 2010. Congress must reconcile differences in

such an extension is passed, the law discussed herein will likely apply in whole, or in substantial part to 2010 (and possibly to future transactions).

A. Summary of the Different Tax Incentives for Conservation Easements

The chief tax incentives available to the donor of a conservation easement are federal income and estate tax deductions, a federal estate tax exclusion, and state income tax credits.[89] Property tax incentives also exist in certain jurisdictions.[90]

The federal income tax deduction is based on Code section 170(h)[91] and relevant regulations, which contain the unique "conservation purposes" test and a host of other requirements that qualifying donations must satisfy. Federal estate tax benefits are based primarily on two concepts. First, the land no longer is worth its full fair market value (because of its lost development potential), which reduces the value of land includable in the landowner's gross estate.[92] Second, Code section 2031(c) provides that the landowner can exclude up to an additional 40% from the already-reduced value of the easement-encumbered property, subject to key limiting provisions.[93]

In some states, laws allow landowners to offset their state taxable income with state income tax credits received as a result of an easement donation.[94] State laws governing the type and amount of credits offered for qualifying donations vary greatly.[95] While only twelve states currently have such credit incentives, it appears likely that more states will enact similar programs in the near future.[96]

Reduction in property values also should result in lower property taxes, although local assessors in some parts of the country have been reluctant to apply the reduced land values.[97] A few states have enacted statutes that

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the bills and approve a final statute before this tax benefit extension is law. If passed, the tax incentives and rules discussed in this Article will again be applicable. *See id.*

[89] *See* Maybank, *supra* note 18, at 1–2.

[90] *See id.*

[91] I.R.C. § 170(h).

[92] *See* Maybank, *supra* note 18, at 2.

[93] *See* I.R.C. § 2031(c).

[94] *See* Nancy A. McLaughlin, *Increasing the Tax Incentives for Conservation Easement Donations—A Responsible Approach*, 31 ECOLOGY L.Q. 1, 39 (2004).

[95] *See* Pentz, *supra* note 27, at 23–34.

[96] *See id.* at 9.

[97] *See* Adam E. Draper, *Conservation Easements: Now More Than Ever—Overcoming Obstacles to Protect Private Lands*, 34 ENVTL. L. 247, 271 (2004).

require local assessors to accept and utilize a lower value for property that is subject to a conservation easement.[98]

Collectively, this cornucopia of tax ameliorants may provide landowners with substantial tax savings to help offset the fair market value lost by the donation of the conservation easement.[99]

B. History of the Federal Tax Law of Conservation Easements

The Internal Revenue Service (Service) first officially sanctioned a charitable income tax deduction for a conservation easement in a 1964 Revenue Ruling concerning the charitable gift of a perpetual conservation easement on privately owned land adjacent to a federal highway.[100] The United States wished to preserve the wooded appearance of the taxpayer's land—as well as the wooded appearance of other land adjacent to the highway—to maintain the scenic view afforded highway travelers.[101] A subsequent Service news release in 1965 informed the public that similar "scenic easements" granted to federal, state, and local governments would receive the same favorable charitable income tax deduction treatment.[102]

The Tax Reform Act of 1969 later revised the Code to deny income, gift, and estate tax deductions for charitable contributions of most partial interests in property.[103] This change technically excluded conservation easements from charitable tax treatment because the servitudes represent, in their legal form, a "partial interest in property."[104] Apparently aware of this result, the committee preparing the Conference Report on the 1969 Act attempted to salvage the charitable deduction for "open space easements" by inserting post-hoc language in the report, stating that the servitudes were to be considered "undivided interests" for tax purposes.[105] The language in the Conference Report, however, was not enough to overcome taxpayer hesitance and uncertainty in the absence of express statutory authority.[106]

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[98] *See, e.g.*, N.C. GEN. STAT. ANN. § 105–277.15 (2009) (eff. Date July 1, 2010); OR. REV. STAT. § 271.785 (2007).

[99] William T. Hutton, The Munificent Conservation Easement: Tax Issues and Planning Strategies, Presented at American Law Institute Continuing Legal Education Course (Mar. 2008).

[100] *See* McLaughlin, *supra* note 94, at 10–11.

[101] *See id.* at 11.

[102] *See id.*

[103] *See id.*

[104] *Id.*

[105] *Id.* at 11–12.

[106] *See id.* at 12.

Congress finally provided explicit statutory authority for charitable income, gift, and estate tax treatment of conservation easements in the 1976 Tax Reform Act.[107] This law was the first to allow a deduction for conservation easements other than scenic easements. The 1976 Act allowed a deduction for a conservation easement if the donation met one of three "conservation purposes," including a donation for the preservation of important historical structures and a donation for the protection of "natural environmental systems."[108] Subsequent amendments to federal tax law retained the expanded permissible types of conservation easements.

The 1977 Tax Reduction and Simplification Act disallowed deductions for "term" easements (those donated for a period of years) and ensured that only conservation easements that meet the qualifications of the 1976 Act and are granted in perpetuity would be eligible for beneficial charitable deduction treatment.[109]

The Tax Treatment Extension Act of 1980 made the conservation easement deduction provision a permanent fixture of the Code.[110] However, Code section 170(h), as enacted, imposed significant limitations on the deduction.[111] Under section 170(h), a conservation easement is deductible as a charitable donation only if it is donated "(i) in perpetuity, (ii) to a governmental unit or publicly-supported charity, and (iii) for one or more of four qualified conservation purposes."[112] In sum, the 1980 Act provided new opportunities for the charitable deduction by codifying the open space easement possibility—including so-called scenic easements—but set forth clear limitations in the Code.[113]

The Treasury published final regulations interpreting, explaining, and providing examples for section 170(h) in 1986 after convening with and receiving input from conservation organizations accustomed to accepting and holding such easements.[114] Importantly, the Tax Reform Act of 1986 dispensed with the conservation purposes test requirement for the charitable deduction of conservation easements in the estate tax and gift tax realms.[115]

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[107] *See id.*

[108] I.R.C. § 170(f)(3)(B)(iii) (1976).

[109] *See* McLaughlin, *supra* note 94, at 13.

[110] *See id.* at 14.

[111] *See id.*

[112] *Id. See infra* Section C.

[113] *See id.*

[114] *See id.* at 15.

[115] *See id.* at 16.

While this portion of the test remains stringent and fully effective for donors claiming income tax benefits under section 170(h), apparently

> Congress considered it unfair to subject easement donors or their estates to gift or estate tax under such circumstances because the donation of an easement is irreversible and the donor or the donor's estate might not have other property or funds with which to pay the gift or estate tax.[116]

The Taxpayer Relief Act of 1997 (the 1997 Act) added a substantial estate tax benefit to donors' estates under Code section 2031(c). This law permits the exclusion of up to 40% of the value of land encumbered by a conservation easement from the donor's estate for estate tax purposes.[117] This significant estate tax exclusion is available, however, only if the donation of the conservation easement meets the full requirements for the charitable income tax deduction under section 170(h), as well as other requirements specific to section 2031(c).[118] Thus, to receive this additional estate tax exclusion, the donation must qualify under the stringent conservation purposes test.[119] While the 1997 Act originally limited the application of Code section 2031(c) to conservation easements encumbering land within specific and limited geographic areas, the Economic Growth and Tax Reconciliation Act of 2001 (EGTRA) expanded section 2031(c) to allow the estate exclusion for conservation easements encumbering any land within the United States.[120]

Originally, income tax deductions under federal law "were subject to the same limitations and carryover rules as other charitable contributions of capital gain property, namely, a deduction at the [conservation easement's] fair market value up to 30% of the taxpayer's adjusted gross income (AGI), with a five-year carryover of any excess."[121] However, the Pension Protection Act (PPA) of 2006[122] substantially sweetened the income tax benefit by expanding the income tax annual deduction to the fair market value of the

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[116] *Id.*

[117] *See id.* at 17, *see also* I.R.C § 2031(c)(1)–(2).

[118] *See* I.R.C. § 2031(c)(8)(B).

[119] *See id.* at 14.

[120] *See* McLaughlin, *supra* note 94, at 17; *see also* Economic Growth and Tax Reconciliation Act of 2001, Pub. L. No. 107-16 § 551, 115 Stat. 38, 86.

[121] Hutton, *supra* note 99, at Sec. IV, A.

[122] Pension Protection Act of 2006, Pub. L. No. 109–280, 120 Stat. 780.

donated easement up to 50% of the taxpayer's AGI, with a fifteen-year carry-forward for any excess.[123]

While the provisions of the PPA sunsetted in 2007, and the income tax deduction temporarily reverted to the previous 30% annual deduction limit, the Food, Conservation, and Energy Act of 2008 extended the 50% deduction with a fifteen-year carry-forward through 2009.[124] Thus, income tax deductions for donated conservation easements are allowed in an amount equal to the fair market value of the donated easement and, from 2006 through 2009, may be taken at an annual rate of 50% of the donor's AGI with a fifteen-year carry-forward for any unused portion of the deduction.[125] Although these favorable provisions expired at the end of 2009, efforts are underway to make them permanent.[126]

C. The Federal Income Tax Deduction: Mechanics of the Tax Incentive

While a federal charitable income tax deduction is not generally available for donations of "partial interests" in property, the Code provides an exception for "qualified conservation contributions."[127] Conservation easements will qualify for this exception if the donation meets Code and regulatory requirements, thus qualifying for charitable deduction treatment despite their true nature as partial interests in property.[128] Thus, from an income tax planning perspective, it is imperative that a donation meet the definition of qualified conservation contribution.

To meet this definition, the conservation easement must fit within three key subsidiary definitions: The donation must be a "qualified real property interest," given to a "qualified organization," "exclusively for conservation purposes."[129] For practitioners seeking to qualify conservation easement donations for charitable deduction treatment, this section amounts to a three-part test. This Section addresses the three definitional requirements in succession, keeping in mind that satisfaction of each of these definitions is

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[123] *See* I.R.C. § 170(b)(1)(E).

[124] Food, Conservation, and Energy Security Act of 2008, Pub. L. No. 110-234, § 15302, 122 Stat. 923, 1501.

[125] *See id.*

[126] *See* Land Trust Alliance, *Easement Incentive to Expire December 31st; Likely to be Renewed Retroactively*, ADVOCATES ALERT (Dec. 18, 2009), http://www.landtrustalliance.org/policy/advocates/adv-121809 (last viewed March 19, 2010).

[127] Treas. Reg. § 1.170A-14(a) (1999).

[128] *See id.*

[129] *Id.*

necessary for a donor to claim a charitable deduction for a qualified conservation contribution.

1. Qualified Real Property Interest

A qualified real property interest is a "perpetual conservation restriction," which is "a restriction granted in perpetuity on the use which may be made of real property—including, an easement or other interest in real property that under state law has attributes similar to an easement (e.g., a restrictive covenant or equitable servitude)."[130] Thus, a conservation easement valid under state law and donated in perpetuity will meet the definition of a perpetual conservation restriction that qualifies as a qualified real property interest.

2. Qualified Organization

The charitable deduction is allowed only when the qualified real property interest is donated to a qualified organization that is considered to be an "eligible donee," as defined in the regulations interpreting section 170(h).[131] According to the regulations:

> In order to be an "eligible donee" of a tax deductible conservation easement, an organization must meet the following requirements: (i) the organization must be either a local, state, or federal governmental agency, or a public charity qualified under IRC § 501(c)(3); (ii) the organization must have a commitment to protect the conservation purposes of the donation . . . and (iii) the organization must have the resources to enforce the restrictions imposed by the easement.[132]

Evidence of the commitment required in part (ii) is generally "found in the articles of incorporation or by-laws of a private organization."[133] Some local, state, and federal governmental agencies may not meet the commitment requirement outlined in the regulation.[134] Thus, when donating an easement to an eligible donee in the private or public sphere, the practition-

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[130] Treas. Reg. § 1.170A-14(b)(2) (1999).

[131] Treas. Reg. § 1.170A-14(c)(1) (1999).

[132] *See* C. Timothy Lindstrom, *A Guide to the Tax Aspects of Conservation Easement Contributions,* 7 WYO. L. REV. 441, 450 (2007).

[133] *Id.* at 450–51.

[134] *See id.* at 451.

er should ensure that the donee has legitimate substantiation of such commitment.

Although the regulations expressly state that "[a] qualified organization need not set aside funds to enforce the restrictions that are the subject of the contribution" to meet prong (iii) of the eligible donee test above, a land trust, or other conservation easement holder, likely could not properly enforce the servitude without such reserve funds.[135]

The qualified organization/eligible donee regulation also provides that the instrument of conveyance must prohibit all future transfers of the easement by any grantee (whether or not for consideration) except for transfers made to another qualified organization that agrees to continue to enforce the easement in perpetuity.[136] The Regulations also clarify that this "restriction on transfer" requirement will be met even if the conservation easement is subsequently extinguished due to "impossibility or impracticality," provided the proceeds from any sale or exchange of the property are used by the donee in a manner consistent with the conservation purposes of the original contribution.[137] This section of the Regulations cross-references to a later section in the Regulations, which provides that:

> If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds [determined as set forth in the regulations] from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.[138]

The easement holder with whom the practitioner or landowner works must fully understand these additional guidelines governing transferability and the possible (albeit rare) termination of a conservation easement. Addi-

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[135] *See id.* at 450–51.

[136] See Treas. Reg. § 1.170A-14(c)(2) (1999).

[137] *See id.*

[138] To make sense of the cross-references, one must refer to Proposed Treasury Regulations Section 1.170A-13, published in the Federal Register on July 21, 1983, because the Treasury inadvertently failed to update the cross-references in the Final Regulations.

tionally, these requirements provide concrete terms that must be included in any tax deductible conservation easement "instrument of conveyance."[139]

3. Exclusively for Conservation Purposes

The conservation easement also must advance specifically outlined conservation purposes for the donation to receive charitable deduction treatment.[140] The recitals (or "whereas clauses") of the conservation easement should explicitly name at least one of the following purposes and should reasonably describe the characteristics and features of the land subject to the easement that support the conservation purpose.[141] There are four qualified conservation purposes for which a tax-deductible conservation easement may be donated:

> 1. The preservation of land areas for outdoor recreation or education of the general public,
>
> 2. The protection of a relatively natural habitat of a fish, wildlife, or plant community or similar ecosystem,
>
> 3. The preservation of certain open space (including farmland and forest land) areas, and
>
> 4. The preservation of a historically important land area or a certified historic structure.[142]

The Service recently has challenged easements that allegedly fall outside of these four enumerated purposes. Among the challenges, the Service argued in *Glass v. Commissioner* that land subject to a donated conservation easement was too small to support the conservation purpose identified in the tax claim, and that unrestricted development rights of neighbors defeated or would defeat the conservation purpose of the easement.[143] The Tax Court rejected both arguments and upheld the claimed deduction for the donation of the conservation easement, the conservation purpose of which was the protection of a relatively small portion of land (11,000 square feet out of

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[139] Treas. Reg. § 1.170A-14(c)(2) (1999); I.R.S. Priv. Ltr. Rul. 200836014 (June 3, 2008) (providing that the easement at issue met the requirements of Treas. Reg. Section 1.170A-14(g)(6) because, for example, it "provides for no means to extinguish the restrictions other than by judicial proceeding and all proceeds received by the Donee are to be used in a manner consistent with the original conservation purposes of the Easement").

[140] *See* Treas. Reg. § 1.170A-14(a) (1999).

[141] *See* Lindstrom, *supra* note 132, at 452–53.

[142] Treas. Reg. § 1.170A-14(d)(1) (1999).

[143] *See* Glass v. Comm'r, 124 T.C. 16 (2005), *aff'd*, 471 F.3d 698 (6th Cir. 2006) (finding the taxpayer's deduction valid based on a qualifying conservation purpose).

eleven total acres) as habitat.[144] Despite the favorable tax ruling, perhaps the most important aspect of *Glass* and other cases challenging conservation purposes is that the Service is, in fact, pursuing such claims.[145]

These challenges have made clear that the Service "expects the easement document to include a thorough description of the conservation purposes of the conservation easement and . . . how protection of the property advances those purposes."[146] Practitioners can help to ensure that a donation will meet the conservation purposes test by applying the following methods when drafting a conservation easement document: (1) the recital clauses of the document should explicitly name "one or more of the conservation purposes identified in the regulations," ideally using the language provided by the regulations; (2) the recitals should provide detailed information "describing and elaborating on the characteristics of the land being made subject to the easement that support the conservation purposes of the easement"; and (3) the characteristics of the land subject to the easement "should be detailed in the 'natural resources inventory' required by the Regulations" and the recital clauses should incorporate the inventory by reference.[147]

The four qualifying conservation purposes are described below.

(a) *Outdoor Recreation or Education of the General Public*

The governing tax regulations note that "[t]he donation of a qualified real property interest to preserve land areas for the outdoor recreation of the general public or for the education of the general public will meet the conservation purposes test of this section."[148] The regulation then provides examples of purposes falling under the umbrella of the "general public" purpose, including "the preservation of a water area for the use of the public for boating or fishing, or a nature or hiking trail for the use of the public."[149] The regulation also requires that "the recreation or education is for the *substantial* and *regular* use of the general public" for the donation to qualify under the purpose.[150] While the regulations do not elaborate on the definitions of *substantial* or *regular*, year-round access clearly would qualify

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[144] *See id.* at 283–84.

[145] *See id.*; *see also* Turner v. Comm'r, 126 T.C. 16 (2006) (finding for the Service).

[146] Lindstrom, *supra* note 132, at 452–53.

[147] *Id.* at 453.

[148] Treas. Reg. § 1.170A-14(d)(2)(i) (1999).

[149] *Id.*

[150] Treas. Reg. § 1.170A-14(d)(2)(ii) (1999) (emphasis added).

while very limited access (for example, one-week-per-year access to a hiking trail) likely would not.[151] The majority of landowners do not rely on the outdoor recreation or education conservation purpose in crafting a conservation easement because the burden of allowing consistent public use represents a heavy yoke to many donors.[152]

(b) *Protection of Relatively Natural Habitat*

The regulation notes that the donation of a conservation easement "to protect a significant relatively natural habitat in which a fish, wildlife, or plant community, or similar ecosystem normally lives will meet the conservation purposes test" of the section.[153] The regulation also indicates that the land need not be unaltered by human activity. So long as the fish, wildlife, or plants continue "to exist there in a relatively natural state," a purpose crafted to protect them may qualify.[154] The regulation requires that the habitat or ecosystem be "significant."[155] The regulation goes on to note that significant habitats and ecosystems include, but are not limited to, "habitats for rare, endangered, or threatened species of animal, fish, or plants" and "natural areas that represent high quality examples of a terrestrial . . . or aquatic community."[156] A natural area that contributes to the "ecological viability" of a park, nature preserve, wildlife refuge, or similar conservation area also qualifies under this purpose.[157] The protection of habitat qualified conservation purpose does not require any public access.[158] A recent case suggests that the presence of one Bald Eagle roost or a single endangered plant will be sufficient to qualify a conservation easement under the habitat conservation purpose test.[159]

(c) *Preservation of Open Space*

Another regulation notes that the donation of a conservation easement "to preserve open space (including farmland and forest land) will meet the

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[151] *See* Lindstrom, *supra* note 132, at 454.

[152] *See* David Braun, *Strategies for Using Conservation Easements in Tax and Estate Planning*, PROB. & PROP., Nov.-Dec. 2002, at 18; *see also* Hutton, *supra* note 99, at Sec. II, C, 1.

[153] Treas. Reg. § 1.170A-14(d)(3)(i) (1999).

[154] *Id.*

[155] Treas. Reg. § 1.170A-14(d)(3)(ii) (1999).

[156] *Id.*

[157] *Id.*

[158] *See* Treas. Reg. § 1.170A-14(d)(3)(iii) (1999).

[159] *See* Glass v. Comm'r, 124 T.C. 16 (2005), *aff'd.* 471 F.3d 698 (6th Cir. 2006).

conservation purposes test" if the preservation is either (i) "[f]or the scenic enjoyment of the general public and will yield a significant public benefit" or (ii) "[p]ursuant to a clearly delineated Federal, state, or local governmental conservation policy and will yield a significant public benefit."[160] Hence, the regulation lays out two separate ways to have a qualifying purpose under the "open space" designation.

The first manner in which an easement can qualify under the open space purpose is by meeting the "scenic" designation. The regulations note that land qualifying for this purpose includes land that, if developed, "would impair the scenic character of the local rural or urban landscape or would interfere with a scenic panorama that can be enjoyed from a park, . . . road, waterbody, [or] trail."[161] The regulation then provides a set of eight objective factors to be considered in determining whether a view qualifies as scenic, but also notes that "'[s]cenic enjoyment' will be evaluated by considering all pertinent facts and circumstances."[162] The objective factors listed in the regulation include easily applied concepts such as "[t]he compatibility of the land use with other land in the vicinity," as well as less-helpful examples, including "[t]he harmonious variety of shapes and textures."[163] While the eight objective factors should be considered in determining if the donation will qualify for a scenic open space purpose, the regulation also states that "[r]egional variations in topography, geology, biology, . . . cultural and economic conditions require flexibility in the application of this test, but do not lessen the burden on the taxpayer to demonstrate the scenic characteristics of [the] donation."[164] As one commentator has remarked, "[i]n other words, you will know a scenic view when you see it."[165]

To satisfy the scenic conservation purpose test there must also be public viewing access—not physical access—over the property or a significant portion of the property.[166] The regulations provide "the preservation of a unique natural land formation for the [visual] enjoyment of the general public" and "the preservation of a stretch of undeveloped property located between a public highway and the ocean . . . to maintain the scenic ocean view

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[160] Treas. Reg. § 1.170A-14(d)(4)(i) (1999).

[161] Treas. Reg. § 1.170A-14(d)(4)(ii)(A) (1999).

[162] *Id.*

[163] Treas. Reg. § 1.170A-14(d)(4)(ii)(A)(1.5) (1999).

[164] Treas. Reg. § 1.170A-14(d)(4)(ii)(A) (1999).

[165] Lindstrom, *supra* note 132, at 456.

[166] *See* Treas. Reg. § 1.170A-14(d)(4)(ii)(B) (1999).

from the highway" as two examples of donations qualifying for the scenic open space purpose.[167]

The second manner in which a donation can qualify under the open space purpose is when the preservation is "[p]ursuant to a clearly delineated. . . governmental conservation policy."[168] This type of open space purpose allows donations that further certain local, state, or federal conservation programs or policies to qualify under the regulation. The regulations note that a "general declaration of conservation goals by a single official or legislative body is not [a] sufficient" program or policy, however, a qualifying program need not certify each donation.[169] By way of example, the regulations provide that donations will meet this requirement where they

> further a specific, identified conservation project, such as . . . the preservation of a wild or scenic river, the preservation of farmland pursuant to a state program for flood prevention and control; or the protection of the scenic, ecological, or historic character of land that is contiguous to, or an integral part of, the surroundings of existing recreation or conservation sites."[170]

Note that the land preserved under this purpose will qualify if it is adjacent to an existing recreation or conservation site, whether or not it is within a relevant government-sponsored conservation area.[171]

While government bodies are among the entities able to accept tax-deductible conservation easement donations, the acceptance of a donation by a government body, "without more, is not sufficient" to qualify the donation for the charitable deduction.[172] The more a government agency or body scrutinizes the donations it accepts under its established conservation program, the more the acceptance tends to establish the delineated government policy.[173]

For both the scenic and the "delineated governmental policy" open space purposes, the regulations also require that the donation yield a "signif-

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[167] Treas. Reg. § 1.170A-14(d)(4)(iv)(B) (1999).

[168] Treas. Reg. § 1.170A-14(d)(4)(iii)(A) (1999).

[169] *Id.*

[170] *Id.*

[171] *See id.*

[172] Treas. Reg. § 1.170A-14(d)(4)(iii)(B) (1999).

[173] *See id.*

icant public benefit."[174] The regulations list eleven important criteria to be considered when evaluating whether an open space donation provides significant public benefit, although "[p]ublic benefit will be evaluated by considering all pertinent facts and circumstances."[175] The regulation notes that none of the following factors will be singularly dispositive in establishing significant public benefit, but all will be considered:

> (1) The uniqueness of the property to the area;
>
> (2) The intensity of land development in the vicinity of the property (both existing development and foreseeable trends of development);
>
> (3) The consistency of the proposed open space use with public programs (whether Federal, state or local) for conservation in the region, including programs for outdoor recreation, irrigation or water supply protection, water quality maintenance or enhancement, flood prevention and control, erosion control, shoreline protection, and protection of land areas included in, or related to, a government approved master plan or land management area;
>
> (4) The consistency of the proposed open space use with existing private conservation programs in the area, as evidenced by other land protected by easement or fee ownership by organizations . . . in close proximity to the property;
>
> (5) The likelihood that development of the property would lead to or contribute to degradation of the scenic, natural, or historic character of the area;
>
> (6) The opportunity for the general public to use the property or to appreciate its scenic values;
>
> (7) The importance of the property in preserving a local or regional landscape or resource that attracts tourism or commerce to the area;
>
> (8) The likelihood that the donee will acquire equally desirable and valuable substitute property or property rights;

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[174] Treas. Reg. §§ 1.170A-14(d)(4)(i)(A)–(B) (1999).

[175] Treas. Reg. § 1.170A-14(d)(4)(iv)(A) (1999).

> (9) The cost to the donee of enforcing the terms of the conservation restriction;
>
> (10) The population density in the area of the property; and
>
> (11) The consistency of the proposed open space use with a legislatively mandated program identifying particular parcels of land for future protection.[176]

The regulation later notes that although "[t]he preservation of an ordinary tract of land would not in and of itself yield a significant public benefit," the preservation of such property "in conjunction with other factors that demonstrate significant public benefit or the preservation of a unique land area for public enjoyment would yield a significant public benefit."[177] The regulation then lists several donations that would qualify as yielding a significant public benefit under the open space purpose guidelines, including "[t]he preservation of farmland pursuant to a state program for flood prevention and control . . . [and] the preservation of woodland along a public highway pursuant to a government program to preserve the appearance of the area so as to maintain the scenic view from the highway."[178]

Although reasonable minds may dispute the applicability of the preceding factors to a given donation, the regulations strongly suggest that ordinary tracts of land, whether plain agricultural land or monoculture timber tracts, would not provide significant public benefit without additional conservation value and, thus, likely would not qualify under the open space qualified conservation purpose.

Additionally, in order to qualify under either the scenic or delineated governmental policy open space purpose, the conservation easement must not allow "a degree of intrusion or future development that would interfere with the essential scenic quality of the land or with the governmental conservation policy that is being furthered by the donation."[179] This condition generally is not an issue with conservation easement donations because most land trusts and other qualified easement holders will insist on limiting retained development rights. However, the requirement does suggest that, when a landowner donates a conservation easement intended to qualify under the open space conservation purpose test and retains rights to build a

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[176] *Id.*

[177] Treas. Reg. § 1.170A-14(d)(4)(iv)(B) (1999).

[178] *Id.*

[179] Treas. Reg. § 1.170A-14(d)(4)(v) (1999).

small number of additional structures on the property—as is common and does not in itself preclude qualification of the easement for the charitable deduction—the additional structures should be allowed only in areas where their presence will not interfere with the scenic or other conservation values protected by the conservation easement.[180] Thus, while scenic and clearly delineated governmental policy donations each have specific requirements for validity, both must yield a significant public benefit and both must limit future development.

(d) *Historic Preservation*

Donations that further the "[t]he preservation of a historically important land area or . . . certified historic structure[s]" fit into the final category of qualified conservation purpose.[181] For this purpose, "historically important land areas" include:

> (A) An independently significant land area including any related historic resources (for example, an archaeological site or a Civil War battlefield with related monuments, bridges, cannons, or houses) that meets the National Register Criteria for Evaluation . . .
>
> (B) Any land area within a registered historic district including any buildings on the land area that can reasonably be considered as contributing to the significance of the district; and
>
> (C) Any land area (including related historic resources) adjacent to a property listed individually in the National Register of Historic Places (but not within a registered historic district) in a case where the physical or environmental features of the land area contribute to the historic or cultural integrity of the property.[182]

"Certified historic structures" include any "building, structure or land area" that is:

> (i) Listed in the National Register, or
>
> (ii) Located in a registered historic district . . . and is certified by the Secretary of the Interior . . . to the

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[180] *See*, *e.g.*, Treas. Reg. § 1.170A-14(f), Ex. 3–4.

[181] Treas. Reg. § 1.170A-14(d)(1) (1999).

[182] Treas. Reg. §§ 1.170A-14(d)(5)(ii)(A)–(C) (1999).

> Secretary of the Treasury as being of historic significance to the district.[183]

In 2006, Congress amended Code section 170(h) through the Pension Protection Act to require that all certified historic structure easements designed only to preserve the exterior of the building must protect the complete exterior of the building, rather than, for example, merely the front or one side.[184] The amendment also requires that such "façade easements" prohibit the alteration of the building's exterior in any manner inconsistent with the historical integrity of the structure and require that a written agreement verify the donee organization is a qualified organization with resources sufficient to enforce and manage the restrictions.[185] The amendment requires that the taxpayer claiming the section 170(h) charitable deduction for historic structure preservation submit photographs, a "qualified appraisal," and a description of the restrictions on the structure.[186]

Some public visual access—such as that from a street, sidewalk, or public trail—is required to qualify a donation as protecting either "historically important land" or a "certified historic structure."[187] Recent case law suggests that land merely in proximity to a historically important structure or landmark will not satisfy the historic preservation conservation purpose test if there are no historically important features to the land itself, and also will not qualify under the open space or habitat conservation purposes tests if the land has no other viable conservation values.[188] The regulations also, however, expressly provide that private residences may qualify under this purpose.[189]

D. Additional Requirements of the Federal Income Tax Incentive

The three chief requirements for federal income tax deductibility of conservation easements are: (1) a qualified real property interest, (2) donated to a qualified organization, (3) given exclusively for conservation purposes. However, several additional requirements determine the deductibility of conservation easement donations.

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[183] Treas. Reg. §§ 1.170A-14(d)(5)(iii)(A)–(B) (1999).

[184] *See* I.R.C. § 170(h)(4)(B)(i); *see also* Pension Protection Act, 29 U.S.C. § 1206 (2006).

[185] *See* I.R.C. §§ 170(h)(4)(B)(i)–(ii).

[186] I.R.C. § 170(h)(4)(B)(iii).

[187] Treas. Reg. § 1.170A-14(d)(5)(iv) (1999).

[188] *See* Turner v. Comm'r, 126 T.C. 16 (2006).

[189] *See id.*

1. Enforceability in Perpetuity

Among the key additional factors determining federal deductibility is the requirement that the restrictions in the conservation easement must be enforceable in perpetuity.[190] While the perpetuity provision leads critics to debate the propriety of current landowners binding all future owners to non-developmental uses, such debate overlooks the binding nature of many land use decisions made by current owners, from strip mining to mountaintop removal mining, which physically alter the land to such an extent as to eliminate most options of future landowners in deciding how to use the land.[191]

The Regulations contain a variety of requirements that must be satisfied for the conservation easement to be considered enforceable in perpetuity:

(1) Any interest in the property retained by the donor (and the donor's successors in interest) must be subject to legally enforceable restrictions (for example, by recordation in the land records of the jurisdiction in which the property is located) that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation.

(2) All existing mortgages must be subordinate to the easement.[192] While convincing a lender to subordinate its mortgage may appear burdensome, landowners with sufficient equity in their property rarely have difficulty meeting this requirement.[193] "[T]he best practice is for the mortgage holder to join in the easement deed."[194] Also, while the regulations do not expressly provide the requirement, the subordination should be complete by the date of filing the tax return in the year in which deductibility is first sought.[195]

(3) On the date of the gift, the possibility that the easement will be defeated by the performance of some act or the happening of some event must be so remote as to be negligible. However, a state's statutory requirement that land use restrictions must be rerecorded every thirty years to remain enforceable (i.e., a state's Marketable Title Act) will not, by itself, render an easement nonperpetual.

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[190] *See* Treas. Reg. § 1.170A-14(a) (1999).

[191] *See e.g.*, Appalachian Voices, *What are the Economic Consequences of Mountaintop Removal in Appalachia?,* http://www.appvoices.org/index.php?/mtr/economics/ (last visited Feb. 4, 2009) (discussing lost tourism opportunities and dramatic loss of water quality as a result of the mining practice labeled "mountaintop removal").

[192] Treas. Reg. § 1.170A-14(g)(2) (1999).

[193] *See* Lindstrom, *supra* note 132, at 471.

[194] *Id.*

[195] *See id.*

(4) The grantor's retention of a "qualified mineral interest" that may be subject to exploitation by any surface mining technique also defeats federal income tax deductibility.[196] The regulations define a *qualified mineral interest* as "the owner's interest in subsurface oil, gas, or other minerals and the right of access to such minerals."[197] There is an exception to this rule for interests that have been severed from the surface rights and are not owned by the grantor of the easement (as is common in the American West), if the likelihood of surface mining pursuant to these rights is "so remote as to be negligible."[198] In such cases, the opinion of a qualified geologist as to the improbability of such surface mining occurring will be helpful in providing evidence sufficient to retain deductibility on split estate lands.[199] Importantly, conservation easements cannot control rights or interests held by third parties—such as government-retained mineral rights—and in split-estate cases, the holder of mineral rights must join in or subordinate their interest to the easement to meet the requirements for federal deductibility.[200] While surface mining must be expressly prohibited, certain other types of mining may not defeat deductibility when the mining will have only a limited, localized impact on the property and will not be "irremediably destructive of significant conservation interests."[201] Even otherwise-proper non-surface mining is disallowed when the action is inconsistent with a conservation value.[202]

(5) The grantee must be provided with documentation, notice, and access rights sufficient to enable it to enforce the terms of the easement. Thus, prior to donating conservation easements, landowners must prepare a written "natural resource inventory" of the land and make the report available to the donee and easement holder to qualify for the federal tax deduction.[203] Treasury regulation sections 1.170A-14(g)(5)(i)(A)–(D) describe items that should be covered in the report. The natural resource inventory provides a vital snapshot of the land for the easement holder, and will allow

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[196] *See* Treas. Reg. § 1.170A-14(g)(4)(i) (1999).

[197] Treas. Reg. § 1.170A-14(b)(1)(i) (1999).

[198] Treas. Reg. § 1.170A-14(g)(3) (1999); *see also* Lindstrom, *supra* note 132, at 477 (noting that the "split estate" problem involving severed mineral rights is common in Western states).

[199] *See* Lindstrom, *supra* note 132, at 477.

[200] *See id.* at 477–81. Note that this is not required where the donor obtains a geologist's report that the likelihood of surface mining is so remote as to be negligible.

[201] Treas. Reg. § 1.170A-14(g)(4)(i) (1999).

[202] *See id.*

[203] *See* Treas. Reg. § 1.170A-14(g)(5)(i) (1999).

it to properly monitor and, if necessary, enforce the easement in the future.[204]

Landowners commonly reserve rights that allow limited improvements to their property, including the construction of an additional single family residence, a barn, or storage structures. The reservation of appropriately limited development rights will not defeat the federal tax deduction, but landowners are required to notify the easement holder prior to exercising such rights if the use might interfere with the conservation interest of the easement.[205] This notice requirement allows the easement holder to ensure the long-term protection of the conservation interests and helps avoid unnecessary enforcement actions. Thus, conservation easements should contain language requiring notice prior to an exercise that might impair a conservation interest.[206]

The governing document also must grant the easement holder the right to enter the land at reasonable times to inspect the property for easement compliance.[207] While land trusts and other easement holders routinely notify landowners before entering the land for monitoring, to qualify for the federal deduction, the entry rights may not be conditioned on landowner approval.[208]

The easement also must expressly grant the holder the right to enforce the terms of the easement, "including, but not limited to, the right to require the restoration" of impaired land to the condition existing on the date of easement conveyance.[209]

(6) Finally, unexpected termination of a conservation easement will not defeat its favorable federal income tax treatment if termination: (1) can occur only by court order, (2) is due to "changed circumstances" making continued use of the property for conservation purposes impossible or impractical, and (3) the easement holder is required to use proceeds gained from the termination in a manner that furthers the conservation purposes originally advanced by the easement.[210] To meet the third requirement, the

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[204] *See* Lindstrom, *supra* note 132, at 482.

[205] *See* Treas. Reg. § 1.170A-14(g)(5)(ii) (1999).

[206] *See* Lindstrom, *supra* note 132, at 482.

[207] *See* Treas. Reg. § 1.170A-14(g)(5)(ii) (1999).

[208] *See id.*; *see also* Lindstrom, *supra* note 132, at 482.

[209] Treas. Reg. § 1.170A-14(g)(5)(ii) (1999).

[210] *See* Treas. Reg. § 1.170A-14(g)(6)(i) (1999); *see also* Lindstrom, *supra* note 132 at 483–84 (noting that the statute does not contemplate modifications or terminations other than by court order, and suggesting that this gap has prompted the discussion about the applicability of cy pres in the conservation easement context).

regulations further require that the donor agree to several provisions: (1) that the conservation easement represents a vested property interest in the donee; (2) that such interest has a "fair market value which is *at least* equal to the proportionate value" of the easement at the time of its donation in relation to the whole value of the land; (3) that such proportionate or floor value of the easement will remain constant; and (4) that, in the event of a court-approved termination, proceeds from a subsequent sale or development of the land will be divided in a manner that provides the easement holder with a share no less than the fixed proportionate floor value of the easement.[211]

The regulations provide for certain unexpected circumstances in which a court may terminate the easement after the deduction is allowed, which generally relate to unforeseen changes or "remote and future" events over which landowners have no control.[212] Courts may also terminate or modify conservation easements if unforeseen "changed conditions" defeat the original charitable purpose of the easement.[213] These provisions properly may be viewed as exceptions to the perpetuity requirement, but in all cases the servitude must be created and intended as a perpetual restriction on the use of the property.

2. Prohibition of Inconsistent Uses

All uses that are inconsistent with conservation values must be prohibited. The federal deduction will not be allowed if the donor retains rights to use the land in a manner that would destroy conservation values, even if those conservation values are not identified in or related to the specific conservation purpose of the donated easement.[214] An example provided in the regulations explains that a conservation easement on a farm would not qualify for the Code section 170(h) tax deduction if the use of pesticides would "injure" or "destroy" a "significant naturally occurring ecosystem" on the property.[215] The "inconsistent use" prohibition will also thwart deductibility for a scenic conservation easement that allows land use that effectively de-

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[211] Treas. Reg. § 1.170A-14(g)(6)(ii) (1999).

[212] Treas. Reg. § 1.170A-14(g)(3) (1999) (note that this section refers specifically to marketability acts that require re-recording of inchoate interests, such as conservation easements, in order to avoid termination).

[213] Treas. Reg. § 1.170A-14(g)(6)(i) (1999); *see also* Lindstrom, *supra* note 132, at 470 (noting that this doctrine is related to traditional trust concepts).

[214] *See id.* at 472.

[215] Treas. Reg. § 1.170A-14(e)(2) (1999).

stroys the scenic public benefit.[216] On the other hand, the regulations state that "this requirement is not intended to prohibit uses of the property, such as selective timber harvesting or selective farming if . . . those uses do not impair significant conservation interests."[217] The regulations also note that a use of the land that causes injury or destruction to a conservation value may be tolerated if—and only if—the use is necessary "for the protection of the conservation interests that are the subject" of the conservation easement.[218]

3. Donative Intent Required

Conservation easement donors must also possess the intent to make a charitable donation in order to be eligible for the section 170(h) tax benefit.[219] This requirement disallows charitable deductions for conservation easements procured (or required) by some regulatory or contractual force.[220] The donative intent requirement works to deny the federal tax benefit in the case of quid pro quo transactions, including easement "donations" made by developers to gain beneficial zoning allowances or contracts in which neighbors agree to donate reciprocal conservation easements.[221]

E. The Importance of Valuation in Conservation Easement Transactions

The valuation of the conservation easement is one of the most important steps in the tax qualification process. An appraisal will set the value of the conservation easement, forming the baseline for determining estate and income tax benefits. Valuation is also one of the most scrutinized facets of easement donations as a result of abusive transactions that manipulate valuation to garner undeserved tax benefits.[222] The Service has put taxpayers on notice that it will not tolerate any misrepresentation or fraud in this area and it will levy fines and penalties on taxpayers attempting to game the system.[223] Because of this heightened scrutiny and the importance of valuation

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[216] Treas. Reg. § 1.170A-14(d)(4)(v) (1999).

[217] Treas. Reg. § 1.170A-14(e)(2) (1999).

[218] Treas. Reg. § 1.170A-14(e)(3) (1999).

[219] *See* Lindstrom, *supra* note 132, at 506; Rev. Rul. 67-246, 1967-2 C.B. 104.

[220] *See* Lindstrom, *supra* note 132, at 506. Note that this prohibition would negate favorable tax treatment for "exacted" easements negotiated by government entities. Such regulatory easements are discussed at length in Lippmann, *supra* note 2.

[221] *See* Lindstrom, *supra* note 132, at 506–09.

[222] *See* McLaughlin, *supra* note 94, at 76–78.

[223] *See* I.R.C. §§ 6662(a), 6663, 6700; *see also* I.R.S. News Release IR-2004-86 (June 30, 2004).

in determining a donation's net tax benefits, practitioners should pay careful attention to this aspect of conservation easement transactions.[224]

The Service has set forth several acceptable appraisal methods for valuing conservation easements. The first, and preferred, method is called the "comparable sales" approach, which calculates the value of land based on comparable sales of other conservation easement land in the area of the donation.[225] However, few practitioners utilize this method, as in many communities few (or no) sales of comparable conservation easement land exist upon which a new appraisal might be based.[226]

The second, and most common, approach is called the "before and after valuation method," which determines conservation easement value by measuring the difference in the fair market value of the land before the easement and after the easement.[227] An appraiser using this method will typically look at other properties with similar zoning requirements, land use restrictions, physical access, proximity to services, land size, and physical characteristics to determine the before value of the land.[228] The appraiser will then estimate the after value of the land by assuming the easement is effective, paying attention to the specific loss in value attributed to the new restrictions.[229] While appraisers often choose the "subdivision development analysis" (or "build out") method to determine the "highest and best use" pre-easement value of land, this method is prone to abuse and is likely to invite the Service's attention.[230] This method estimates values based on hypothetical scenarios in which the entire land area is divided into parcels and sold for development.[231] This approach is prone to error because many appraisers do not take into account existing limitations—including zoning requirements, physical development restrictions (for example, mountainsides or wetlands)—and existing market demand when calculating values.[232] Appraisers utilizing these methods to determine pre-easement value now

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[224] For an in-depth discussion of conservation easement valuation, see *McLaughlin, supra* note 94, at 68–91.

[225] *See* Treas. Reg. § 1.170A-14(h)(3)(i) (1999).

[226] *See* Lindstrom, *supra* note 132, at 500–01.

[227] *Id.* at 498.

[228] *See id.*

[229] *See id.*

[230] *Id.* at 500; *see also* McLaughlin, *supra* note 94, at 83–86.

[231] *See* Lindstrom, *supra* note 132 at 500; McLaughlin, *supra* note 94, at 83–86.

[232] *See* Lindstrom, *supra* note 132, at 500.

must address these and other issues, in accordance with Treasury regulations.[233]

Regardless of the valuation method used, the appraisal must be substantiated. Any tax return claiming a conservation easement deduction exceeding $5,000 must be accompanied by a qualified appraisal prepared by a qualified appraiser.[234] The "Noncash Charitable Contribution" form (Form 8283)—in which the donee organization acknowledges receipt of the property—must also accompany any conservation easement tax claim.[235] If the donation exceeds $500,000 in value, the Service requires that the complete appraisal accompany the tax claim.[236] The landowner or practitioner must insure that the substantiation documentation is complete no earlier than sixty days prior to the conveyance and no later than the tax filing due date for the year in which the benefit is first claimed.[237] The appraisal must reflect the value of the conservation easement at the time of the easement's donation.[238]

A few important rules limit the appraised value of conservation easements. The "entire contiguous property" rule states that "the deduction in the case of . . . a perpetual conservation restriction covering a portion of the contiguous property owned by a donor and the donor's family . . . is the difference between the fair market value of the entire contiguous parcel of property before and after the granting of the restriction."[239] The similar "enhancement" rule takes into account the increase in value of any land held by the donor or a "related person" as a result of the conservation easement donation.[240] Any such "enhancement" in the value of other land then must be subtracted from the value of the conservation easement.[241] Both of these rules lower conservation easement value based on the perceived benefit gained by the taxpayer through the appreciation in value of other lands

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[233] *See id.*

[234] *See* Treas. Reg. § 1.170A-13(c)(2), (c)(3), (c)(5) (1996) (defining a "qualified appraiser").

[235] *See* Treas. Reg. § 1.170A-13(f) (1996).

[236] *See* I.R.C. § 170(f)(11)(D).

[237] *See* Treas. Reg. § 1.170A-13(c)(3)(A) (1996).

[238] *See* Treas. Reg. § 1.170A-13(c)(3)(ii)(I) (1996).

[239] Treas. Reg. § 1.170A-14(h)(3)(i) (1999).

[240] *Id.* Note that the regulation suggests the "enhanced" land need not be adjacent to the conservation easement land for this rule to have effect. For purposes of the regulation, a related person is an individual donor's siblings, spouse, ancestors, and lineal descendents, as defined by Code sections 267(b) and 707(b).

[241] *See* Lindstrom, *supra* note 132, at 504.

owned by the taxpayer, or a family member or other "related person." In addition, the appraiser must subtract from the value of the conservation easement any financial payment or economic benefit received—or reasonably expected to be received—by the donor or a related person for the donation.[242]

These guidelines provide only a brief synopsis of the appraisal requirements that must be satisfied upon the donation of a tax-deductible conservation easement. Practitioners should take the time to locate a qualified appraiser, preferably with conservation easement experience, who will employ accurate and defensible appraisal methods. Exaggerating or misrepresenting the value of the conservation easement likely will result in disallowance of the claimed tax benefits and the imposition of fines and penalties, all while the extensive land use restrictions remain in place in perpetuity.[243] In fact, attorneys may find themselves subject to discipline and financial penalty for abusive valuations. A 2004 Service Notice specifically warned that "other persons involved in these transactions may be subject to penalties under . . . . [Code section] 6694," which provides financial liability for both signed and unsigned tax preparers and may extend to attorneys providing tax guidance for such donations.[244] Accordingly, lessons from the past and warnings by tax authorities indicate that abuse will not be tolerated in this field.

F. Measuring the Benefits Provided by the Federal Income Tax Incentive

As of January 1, 2010, the federal tax law provisions pertaining to conservation easements in 2009 are no longer effective. While there remains a significant federal incentive for the donation of conservation easements, the levels of income deductibility have reverted to the law that existed prior to 2006.[245] *As of March 16, 2010, the following key differences apply to current conservation easement donations in 2010:*

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[242] *See* Treas. Reg. § 1.170A-14(h)(3)(i) (1999).

[243] *See* I.R.S. News Release IR-2004-86 (June 30, 2004); *see also* I.R.S. News Release IR-84-125 (Dec. 10, 1984).

[244] I.R.S. Notice 2004-41, 2004-28 I.R.B.31; *See* I.R.C. § 6694.

[245] *See* Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (Note that the Pension Protection Act of 2006 originally brought the increased income tax incentives related to conservation easement donations. The law in 2010, as of March 16, 2010, is the law that applied prior to this Act.)

With regard to the federal income tax deduction under Code section 170(h) as of March 16, 2010:

- *Treatment for conservation easements differs based on whether the easement is considered short-term or long-term capital gain property.*[246]
  - *Short term capital gain conservation easements are those donated on land owned for less than one year by the donor.*[247]
  - *Long term capital gain conservation easements are those donated on land owned for more than one year by the donor.*[248]
- *Long-term capital gain conservation easements: Are now limited to 30% of the donor's adjusted gross income in a given year.*[249]
- *Short-term capital gain conservation easements: Are now limited to 50% of the donor's adjusted gross income, and also are limited to the donor's basis in the conservation easement due to the treatment of short-term capital gain conservation easements as ordinary income property.*[250]
- *Any remaining (unused) credit may be carried forward for 5 years.*[251]
- *The enhanced tax incentive for qualified farmers does not exist under current law. Taxpayers considered qualified farmers under 2006-2009 law are treated under the generally applicable 2010 rules noted above.*
  - *The law noted above (effective in 2010) will likely remain in effect until Congress passes a one-year extension of the 2006–2009 enhanced conservation easement incentives (those incentives addressed in this Article) or passes a law making those enhanced incentives permanent.*

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[246] Lindstrom, *supra* note 132 at 487–88.
[247] *See id.*
[248] *See id.*
[249] *See* Treas. Reg. § 1.170A-8(e) (as amended in 1972).
[250] *See* I.R.C. §§ 170(e)(1)–(2) (2004); Treas. Reg. § 1.170A-8(b) (as amended in 1972).
[251] *See* Treas. Reg. § 170A-10(c)(1)(ii) (as amended in 1975).

- *Changes have also been made to the federal estate tax, which are summarized at Section III.H.*

This Section of the Article applies the tax rules which were in place during 2006–2009 and which may be reintroduced in the future.

Before attempting to comply with the regulatory requirements and permanently relinquishing valuable development rights, clients rightly are interested in the amount of tax savings they can expect to receive as the result of a conservation easement donation. The value of a conservation easement contributed in compliance with Code section 170(h) may be deducted from the donor's income in calculating his federal income tax liability.[252] As described in detail above, generally the "value for [a qualifying conservation easement] is the difference between the fair market value of the property at its highest and best use immediately prior to the imposition of the easement, and immediately subsequent to the grant."[253] Conservation easements range widely in value, with courts having accepted valuations ranging between 25% and 90% of the entire property.[254]

The maximum federal income tax benefit that may be achieved through a qualified conservation easement donation is found by multiplying the value of the easement by the highest federal income tax rate.[255] The nature of the section 170(h) tax incentive as a deduction necessarily means that it will be most beneficial to top-income tax bracket taxpayers. The utility of an income tax deduction decreases significantly for taxpayers in lower income-tax-brackets with less income to offset. Existing state tax "credit" programs may ameliorate the bias of the section 170(h) deduction toward wealthy taxpayers because credits benefit all taxpayers on a dollar-for-dollar basis, especially when such state programs allow transferable or refundable credits.[256]

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[252] *See* Maybank, *supra* note 18, at 22.

[253] Maybank, *supra* note 18, at 25. For more on this before and after method, see Hutton, *supra* note 99, Sec. III(E).

[254] *See* Stephen J. Small, Conservation Easements: Tax, Valuation and Appraisal Issues, Sec. V,9(d)(i), American Law Institute Continuing Legal Education Course (Nov. 2005).

[255] *See* Lindstrom, *supra* note 132, at 485–86. Note that this highest possible easement value will only apply to a given taxpayer if they pay taxes at that highest applicable rate.

[256] *See* Pentz, *supra* note 27, at 23.

The federal income tax deduction under section 170(h) is subject to a yearly cap.[257] The annual limitation on the deduction is tied to the Code treatment of other donated long-term capital gain property.[258] Put simply, a conservation easement annual deduction in 2009 and possibly in the future, when combined with other charitable contributions, may not exceed 50% of a donor's "contribution base."[259] An individual's contribution base generally is defined as "adjusted gross income without regard to the amount of the contribution and without regard to any 'net operating loss carry-back.'"[260] For many taxpayers, the deduction is limited to 50% of their adjusted gross income in a given tax year. Unlike prior law, which limited annual deductions based on length of ownership prior to donation,[261] the law during 2009[262] was more liberal and allowed for the 50% annual deduction regardless of duration of ownership preceding donation.[263]

The annual limitation under Code section 170(h) has been substantially higher for "qualified farmers and ranchers" under increased tax benefit legislation reenacted through 2009 after a temporary lapse and which may be reenacted in the future.[264] Qualified farmer taxpayers could deduct the easement contribution against 100% of the donor's contribution base annually.[265] In many cases, this deduction means that qualified farmers and ranchers can offset 100% of their adjusted gross income in a given tax year. "A qualified farmer or rancher is someone more than 50% of whose income comes from the 'business of farming.'"[266] Note that a qualified farmer or

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[257] *See* Lindstrom, *supra* note 132, at 487.

[258] *See id.*

[259] *Id.* at 487–88.

[260] I.R.C. § 170(e)(2); *See also* Treas. Reg. § 1.170A-8(b) (1972).

[261] *See* I.R.C. § 170(e)(2); Treas. Reg. § 1.170A-8(b) (as amended in 1972).

[262] Please see the introduction in Section III.F, describing important tax changes which apply as of January 1, 2010.

[263] *See* Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, § 15302, 122 Stat. 923; Lindstrom, *supra* note 132, at 489.

[264] *See* Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, § 15302, 122 Stat. 923 (note that this section merely continued the extended tax benefits originally granted in the Pension Protection Act of 2006 at 29 U.S.C. § 1206 (2006)); I.R.C. § 170(b)(2)(8). Please see the introduction in Section III.F describing important tax changes which apply as of January 1, 2010.

[265] *See* Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, § 15302122 Stat. 923; I.R.C. § 170(b)(2)(B)(i)(I); Lindstrom, *supra* note 132, at 489.

[266] Lindstrom, *supra* note 132, at 489 (citing I.R.C. § 170(b)(1)(E)(v)). The Code defines farming for purposes of qualifying for this increased tax incentive as: "(A) cultivating the soil or raising or harvesting any agricultural or horticultural commodity

rancher may include a corporation so long as "the stock of which is not readily tradable on an established securities market."[267]

To qualify for the additional qualified farmer deduction benefit, the taxpayer must keep the land subject to the easement available for agriculture (although the land does not have to be actively used in such a manner).[268] Additionally, it appears that a qualified farmer or rancher must only meet the minimal income from farming percentage requirement in the year of donation.[269] A shift in farming income below this percentage in subsequent years does not appear to defeat the higher annual limitation benefit.[270]

Although the applicable annual limitation on conservation easement deductions will reduce the benefit to the taxpayer in a given year, the law in 2009, which may be reintroduced, afforded a generous fifteen-year carry-forward, during which the taxpayer may use any unused portion of the fair market value of the donated easement to offset income.[271] If a taxpayer had other charitable contributions subject to a shorter five-year carry-forward period, he wisely could elect to use the deductions from those contributions prior to the long-surviving conservation easement benefits.[272]

Practitioners should note another important limitation applicable to donations with respect to land owned one year or less by the donor. In such a

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(including the raising, shearing, feeding, caring for, training, and management of animals) on a farm; (B) 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 one-half of the commodity so treated; and (C) (i) the planting, cultivating, caring for, cutting of trees, or (ii) the preparation (other than milling) of trees for market." I.R.C. § 2032A(e)(5).

"The term 'farm' includes stock, dairy, poultry, fruit, furbearing animal, and truck farms, plantations, ranches, nurseries, ranges, greenhouses or other similar structures used primarily for the raising of agricultural or horticultural commodities, and orchards and woodlands." I.R.C. § 2032A(e)(4).

[267] I.R.C. § 170(b)(2)(B)(i)(I); *see also* Lindstrom, *supra* note 132, at 489, Lindstrom, *supra* note 132, at 489 n.112 (suggesting that LLC entities would likely benefit from this same treatment).

[268] *See* I.R.C. § 170(b)(1)(E)(iv)(II).

[269] *See* Lindstrom, *supra* note 132, at 490.

[270] *See id.*

[271] *See* I.R.C. § 170(b)(1)(E)(ii).

[272] *See* Lindstrom, *supra* note 132, at 494–95 (noting that cumulatively the annual limitation and fifteen-year carry-forward may still not allow a landowner to recover the full value of the donated easement). In order to achieve such full recovery, landowners often elect to "phase in" easements over time. This phase in involves donating easements on portions of land over time, until the entire area is made subject to easements and a maximum tax benefit is achieved. The process of phasing-in easements is discussed in McLaughlin, *supra* note 94, at 33–36.

case, the deduction under section 170(h) is limited to the owner's basis in the conservation easement.[273] This limitation may influence the timing of a conservation easement donation.[274]

Also note that a conservation easement donation will lower a donor's basis in the land subject to the conservation easement.[275] The donor's basis in the land must be reduced by the value of the conservation easement, as determined by the proportion of the land's overall value attributable to the conservation easement.[276]

The technical rules described above determine the tax benefit that may be enjoyed by a given taxpayer upon the donation of a conservation easement. The following examples, applying the law as it existed through 2009, demonstrate the potential dollar savings from a section-170(h)-qualified conservation easement donation.

G. Examples of the Federal Income Tax Benefit

> *Reminder: The following examples are based on the law effective in 2009, many of which provisions have lapsed. While the future tax treatment of conservation easements is unclear, there are efforts underway to reenact these more generous benefits. As such, the examples which follow may also apply in the future.*

1. Example One: Full Deduction Taken

Mr. Leopold owns land nestled in the biologically rich escarpment area of the Blue Ridge Mountains. In 2009 Leopold donates a conservation easement on the land to a qualified organization, an experienced land trust. The donation satisfies all Code section 170(h) requirements, including the habitat conservation purpose test, as the land remains in an overwhelmingly natural state and even harbors the Oconee Bell, a rare plant species. The donation also satisfies the open space conservation purpose test as the land provides a beautiful vista from county roads that surround the property.

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[273] *See* Lindstrom, *supra* note 132, at 496.

[274] *See id.*

[275] *See* Treas. Reg. § 1.170A-14(h)(3)(iii) (1999).

[276] *See id.*; *see also* Lindstrom, *supra* note 132, at 513 (discussing a rule that limits real estate developers in regard to the "ordinary income" character of "lots" they sell, which, in the conservation easement context, generally limits their deduction to basis in the real property).

The land was worth $3,000,000 before and $2,000,000 after the easement donation. The value of the easement is the difference between those two values, or $1,000,000.

Leopold had earned income of $3,000,000 in 2009, so, the entire $1,000,000 represented by the easement deduction would otherwise be taxed at the current top income tax rate of 35%. Therefore, the real value of the section 170(h) conservation easement deduction to Leopold is $350,000 (35% x $1,000,000).

Since Leopold earned so much in 2009, he can take the entire deduction in one year as the value of the easement does not exceed 50% of his annual income.

2. Example Two: Carry-Forward Deduction

Assume the same facts as Example One, but now assume Mr. Leopold earned only $500,000 in income for the year. In this instance, he would not be able to utilize the entire $1,000,000 deduction in one year. He would be subject to the limitation that a donor may only use a deduction against as much as 50% of their income in a given year. In this lower income example, he would be restricted to a deduction of $250,000 in the year of donation. Under the law in effect in 2009, Leopold could carry forward the remaining $750,000 deduction for a total of fifteen years. If Leopold continued to earn $500,000 in annual income, he would continue to be able to take $250,000 deductions each year and would use the entire deduction in four years.

3. Example Three: Deduction as Qualified Farmer

Assume the same facts as Example Two, but now assume that Mr. Leopold uses the entirety of his land as a farm where he raises and harvests sustainable timber and grows valuable organic vegetables. Also assume that Mr. Leopold earns $500,000 in income every year from these farming operations.

Leopold, applying the law in effect in 2009, could claim the deduction each year in an amount equal to 100% of his adjusted gross income as he is a qualified farmer under Code section 2032A and is no longer restricted by the annual limitation on the deduction to 50% of income. Thus, Leopold can deduct $500,000 in the year of donation. Assuming he earns at least $500,000 in income again the following year, the remaining $500,000 of his deduction may be deducted in year two. By meeting the definition of qualified farmer, Leopold is able to use his deduction in half the time of non-qualifying taxpayers.

Note that in each of the preceding examples, Mr. Leopold has given away development rights (for example, the right to subdivide extensively or use the land for commercial, non-agricultural purposes) through the donation. If Leopold never desired to use this land for any such purpose, he has generated substantial tax benefit ($350,000 real-dollar tax savings) at minimal subjective cost.

H. The Federal Estate Tax Incentives: Mechanics and Potential Benefits

Note to reader: As noted earlier, this Article was written in 2009, apply the tax laws then in effect. As of March 16, 2010 the following key differences in regard to the federal estate tax apply to current conservation easement donations in 2010.

- *The $3.5 million personal exemption against estate tax discussed herein lapsed on January 1, 2010.*[277]
- *Currently, there is no estate tax and no personal exemption against estate tax.*[278]
- *Additionally, the lapse of the 2009 law under EGTRRA provisions brought about the loss of the stepped up basis rules that generally applied to gifts by devise or bequest. In 2010, modified carry over basis rules apply.*[279] *The most important facet of the modified carry over basis rules is that those receiving property by bequest or devise (such as inherited land) will be forced to take a carry over basis in the property, subject to important qualifications and a permitted upward adjustment in basis.*[280]
- *The estate tax provisions effective in 2010 will continue throughout the year. As of January 1, 2011, the estate tax provisions embodied in the EGTRRA reforms will "sunset," causing the estate tax to be reinstated at a very low*

[277] *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No.107-16, 115 Stat 38 (2001).

[278] *Id.*

[279] *See* I.R.C. §§ 1014(f), 1022(a)

[280] *See* I.R.C. §§ 1022(a), 1022(b)(2)(B), 1022(b)(c) (Note that under the modified carry over basis rules of section 1022, a decedent's personal representative is permitted to allocate an aggregate basis increase of $1.3 million (or up to 3 million for a surviving spouse) to certain property owned by the decedent as of death). *See* I.R.C. § 1022 for several additional important rules regarding the "modified carry over basis" in effect throughout 2010.

personal exemption against estate tax of $1 million.[281] *The top tax rate for estate tax in 2011 will rise to 55%.*[282] *Also, in 2011, the modified carry over basis rules will lapse, again replaced by the familiar carry-over basis traditionally applicable to gifts by devise or bequest.*[283]

- *The "no estate tax" rules applicable in 2010 have effectively rendered moot the potential estate tax benefits achievable through conservation easement donations. However, if Congress fails to take decisive action on the subject later this year and the default sunset rules applicable in 2011 become law, the effect likely will be to drive the large percentage of Americans (who will suddenly be vulnerable to the estate tax due to the low $1 million exemption level) to consider conservation easements as an estate tax planning strategy. Of course, there is no way to predict Congressional action (or inaction) on the matter and practitioners should pay close attention to tax law developments as they effect conservation easements in the estate tax realm.*

Donating a conservation easement provides two distinct estate tax benefits to donors and their estates. The first is the logical benefit gained by reducing the fair market value of the land subject to the easement, which decreases the taxable estate of the decedent.[284] Code section 2031(c) provides the second benefit by allowing up to an additional 40% of the value of the land subject to the easement to be excluded from the decedent's taxable estate. Perhaps more importantly, a conservation easement allows specific and enduring "dead hand" control for those donors who desire that their land be managed or used in specific ways after their death,[285] although easement donors should take precautions to ensure that their wishes are actually honored over time by the donees.[286]

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[281] *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No.107-16, 115 Stat 38 (2001).

[282] *See id.*

[283] *See id.*, *see also* I.R.C. § 1014.

[284] *See* I.R.C. § 170(b)(1)(E).

[285] *See* Lindstrom, *supra* note 132, at 524.

[286] *See* Nancy A. McLaughlin & Mark Benjamin Machlis, *Amending and Terminating Perpetual Conservation Easements,* 23 PROB. & PROP. 52 (2009) (providing drafting tips to help ensure the intent of the easement donor is honored over time); *see also,* Nancy A. McLaughlin & W. William Weeks, *In Defense of Conservation Easements: A Response to*

A conservation easement generally reduces the value of the subject land for estate tax purposes.[287] Notably, this reduction will reduce the land's estate tax value whether the conservation easement is donated or sold.[288] The value of the land subject to the conservation easement is determined at the same time as other estate property—at the time of decedent's death or the alternate valuation date (six months after decedent's death, if elected).[289] While restrictions on the use of real property generally cannot be used as a factor in determining the value of real property for estate tax purposes, qualified easements meeting the requirements of Code section 170(h) during a donor's lifetime are exempt from this provision.[290]

Generally, lifetime gifts are subject to the federal gift tax, and will result in tax liability for the taxpayer once the allowable gift tax credit is exhausted.[291] Donations of conservation easements that satisfy the requirements of Code section 170(h) are deductible under section 2522(d).[292] Conservation easement donations that qualify under section 170(h) are also deductible for estate tax purposes.[293] The deduction is the value of the easement as determined by the relevant valuation methods.[294] Interestingly, while the estate and gift tax deductions require general adherence to the section 170(h) guidelines, the deductions will be allowed even if the easement fails the burdensome conservation purposes test.[295] The apparent policy behind this Service concession is to avoid enforceable restrictions on land made by will (or otherwise) that inadvertently fail to qualify for the tax benefit because they fail the technical conservation purposes requirement.[296]

The End of Perpetuity, 9 WYO. L. REV. 1 (2009) (explaining that some holders take the position that they are entitled to agree to modify or terminate perpetual conservation easements "in the same manner as other easements," regardless of the express terms of the easements or their status as tax-deductible perpetual charitable gifts).

[287] *See id.* at 525.

[288] *See id.*

[289] *See id.*

[290] *See id.* at 526–27.

[291] *See id.* at 528.

[292] *See* I.R.C. § 2522(d); Lindstrom, *supra* note 132, at 528.

[293] *See* Lindstrom, *supra* note 132, at 528.

[294] *See id.* at 528; *see also id.* at 498.

[295] *See id.* at 528.

[296] *See* Tax Reform Act of 1986, Pub. L. No. 99-514 § 1422, 100 Stat. 2085. No regulations or cases provide further guidance on this provision to practitioners. *But see supra* note 116 and accompanying text.

The second major estate tax benefit provided by a conservation easement donation—an exclusion of up to 40% of the value of land subject to a qualified conservation easement from the decedent's estate[297]—applies in addition to any reduction in taxable value or estate tax deduction that results from the donation of an easement.[298] The 40% estate tax exclusion provided by section 2031(c) does not apply to all "qualified conservation *contributions*," but only to "qualified conservation *easements*."[299] Conservation easements donated under the terms of section 170(h) will meet nearly all requirements of the qualified conservation easement provisions required for the 40% exclusion.[300] However, the definition imposes several additional requirements on easement donations, including:

> (1) the easement must apply to land held by the decedent or member of the decedent's family for at least a three-year period immediately preceding the decedent's death;
>
> (2) the easement contribution must have been made by the decedent or a member of the decedent's family (as defined . . .[in section 2032A(e)(2)]);
>
> (3) the conservation purpose of the easement cannot be limited to historic preservation; and
>
> (4) the easement can allow no more than a "*de minimis* commercial recreational use."[301]

The donation must also meet the full requirements of section 170(h) to receive the section 2031(c) estate tax exclusion, including the conservation purposes test,[302] but conservation easements that satisfy only the historic preservation conservation purpose test are not extended the benefit of the section 2031(c) exclusion.[303]

Up to 40% of the estate tax value of the land subject to the qualified conservation easement can be excluded from the decedent's estate under

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[297] *See* I.R.C. § 2031(c).

[298] *See* Lindstrom, *supra* note 132, at 529.

[299] I.R.C. § 2031(c)(1)(A) (emphasis added).

[300] *See* Lindstrom, *supra* note 132, at 529–30 (describing the differences between a qualified conservation easement and a qualified conservation contribution).

[301] *See id.* at 530.

[302] *See* I.R.C. § 2031(c)(8)(B); Lindstrom, *supra* note 132 at 531.

[303] *See* Lindstrom, *supra* note 132, at 530.

section 2031(c).[304] However, the conservation easement must reduce the value of the land subject to the easement by at least 30% to qualify for the full 40% exclusion.[305] The statute notes that the 40% exclusion must be reduced by two percentage points for every one percentage point the conservation easement fails to reduce the value of the land by 30%.[306] The exclusion also applies only to the value of the land subject to the conservation easement; it does not apply to the value of any improvements on the land.[307] The total exclusion is capped at $500,000 per estate under section 2031(c)(1).[308] Any outstanding debt incurred in connection with the purchase of land subject to the conservation easement must be subtracted from the value of the land before calculating the exclusion.[309] However, Code section 2053(a)(4) allows the deduction of such debt when calculating the value of an estate subject to tax.[310] The exclusion applies to the value of land, determined at the date of the decedent's death or the alternate valuation date (6 months after decedent's death, if elected).[311]

Importantly, the exclusion will not apply to the value of any "retained development rights."[312] The statute defines *retained development rights* as "any right to use the land . . . retained for any commercial purpose which is not subordinate to and directly supportive of the use of such land as a farm for farming purposes. . . ."[313] But "[r]ights to maintain a residence for the owner's use, as well as normal farming, ranching, and forestry practices should not be considered retained development rights."[314] Rights reserved to build an additional house on the conservation land for non-commercial purposes—not for rent or sale—likely would not be considered retained devel-

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[304] *See* I.R.C. § 2031(c).

[305] *See* I.R.C. § 2031(c)(2).

[306] *See id.* For purposes of determining if the 30% reduction is met, relevant values are those determined at time of contribution. The purpose of rule is to keep people from claiming the exclusion on insignificant easements. *See* Lindstrom, *supra* note 132, at 539.

[307] *See* Lindstrom, *supra* note 132, at 531.

[308] *But see id.* at 534–36 (demonstrating how the exclusion may be multiplied beyond the per estate $500,000 cap when the easement land will be devised by several estates, such as occurs via tenancy in common ownership of conservation easement land).

[309] *See* I.R.C. § 2031(c)(4)(A).

[310] *See* I.R.C. § 2053(a)(4).

[311] *See* Lindstrom, *supra* note 132, at 539.

[312] *Id.* at 540–41.

[313] I.R.C. § 2031(c)(5)(D).

[314] Lindstrom, *supra* note 132, at 541.

opment rights.[315] On the other hand, retained rights to sell portions of the land for development or to develop a commercial enterprise likely would constitute retained development rights and reduce the value of the exclusion.[316] If a conservation easement includes retained development rights, heirs to the property may agree to terminate such rights before the estate tax return is due and the exclusion will apply as though the development rights never existed.[317]

Note also that general commercial use of land subject to an easement will prevent a section 2031(c) exclusion pursuant to a statutory provision that prohibits all but de minimis commercial recreational use of the property.[318] While a statement by the Joint Committee on Taxation notes that retained rights to grant hunting and fishing licenses would be considered de minimis practices, further guidance on this issue is hard to find.[319] Due to the uncertain scope of this requirement, a landowner seeking the section 2031(c) exclusion should consider prohibiting all commercial use of the conservation property or "any commercial recreational use, except those uses considered de minimis according to the provisions of § 2031(c)(8)(B) of the Internal Revenue Code."[320]

The section 2031(c) exclusion is also available to future generations and future estates so long as the family of the donor continues to hold conservation easement land.[321] Thus, the section 2031(c) exclusion creates multiple generations of benefits for "legacy" properties and creates an incentive for heirs to keep conservation property under family control.[322]

While the 40% exclusion provided by section 2031(c) is a hefty incentive for estate-tax-vulnerable taxpayers, such an election will impose a carry-over basis in the land on the transferees to the extent of the exclusion.[323] This treatment differs from that normally given property passing through devise, which generally receives the more advantageous stepped-up

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[315] *See id.*

[316] *See id.*

[317] *See* I.R.C. §§ 2031(c)(5)(A), (B); Lindstrom, *supra* note 132, at 540.

[318] *See* I.R.C. § 2031(c)(8)(B).

[319] *See* STAFF OF JOINT COMM. ON TAXATION, 109TH CONG., GENERAL EXPLANATION OF TAX LEGISLATION ENACTED IN THE 109TH CONGRESS Title XII.A.3 (Comm. Print 2007); Lindstrom, *supra* note 132, at 542.

[320] Lindstrom, *supra* note 132, at 542.

[321] *See id.* at 537.

[322] *See id.* at 537–38.

[323] *See* I.R.C. § 1014(a)(4).

basis under section 1014(a)(1).[324] The carry-over basis rule will likely cause the recognition of capital gain income for inheritors who sell conservation lands that had low basis in the hands of the decedent.[325] In any event, this carry-over basis provision provides a disincentive for a taxpayer to elect the section 2031(c) exclusion when the tax savings would be small or non-existent, and, of course, there are no reasons to elect the exclusion when an estate has insufficient value to trigger estate tax.[326]

The section 2031(c) exclusion only applies to exclude estate tax and does not apply to reduce gift tax.[327] Thus, landowners who make gratuitous inter vivos transfers of conservation easement land that would otherwise qualify under section 2031(c) miss the opportunity for a valuable estate tax exclusion and will receive no similar gift tax benefit. While the tax benefits provided by lifetime transfers may provide ample countervailing advantages, an estate planner should carefully consider the section 2031(c) exclusion prior to a lifetime gift of conservation easement property.

If the decedent's interest in qualifying conservation easement land under section 2031(c) is an interest held though a corporation, partnership, or trust, the estate still will be able to claim the exclusion to the extent of the decedent's interest in the entity so long as the decedent owned at least a 30% interest in the entity.[328] While the statute does not contemplate whether interests in an LLC would receive similar treatment, this section likely would apply because the LLC entity is treated as a partnership for tax purposes (absent a Code-section-7701 election).[329]

Among other section 2031(c) technicalities, the exclusion only applies to estates of decedents dying after December 31, 1997.[330] The decedent's executor or trustee must affirmatively elect the exclusion by the date on which the estate tax return is due.[331] A failure to elect in one generation will

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[324] *See* I.R.C. § 1014(a)(1).

[325] *See* I.R.C. § 1014(a)(4).

[326] *See* Lindstrom, *supra* note 132, at 539.

[327] *See id.* at 532.

[328] *See* I.R.C. § 2031(c)(10).

[329] *See* I.R.C. § 7701(a)(2) (defining partnership broadly to incorporate limited liability companies that fall under the umbrella of a "group . . . or . . . other unincorporated organization through . . . which . . . [a] business . . . [or] venture is carried on").

[330] *See* Lindstrom, *supra* note 132, at 533.

[331] *See id.* at 538–39. The election for this purpose is Schedule U (Qualified Conservation Easement Exclusion) of Form 706, the federal estate tax return. *See* I.R.S. Form 706, 38 (2009), *available at* http://www.irs.gov/pub/irs-pdf/f706.pdf.

not bar future generations from claiming the section 2031(c) benefit.[332] Pursuant to a provision in the EGTRA, land located anywhere in the United States may qualify for the benefit under section 2031(c).[333] The previous standard limited lands that could qualify under section 2031(c) to property located within a twenty-five mile radius of a Metropolitan Statistical Area (MSA), national park, or national wilderness area.[334]

The section 2031(c) exclusion, which may be made *after* the death of the decedent, is a key opportunity for executors of estates, trustees, and interested inheritors of land.[335] A "post-mortem" conservation easement must be donated before the final date for filing the decedent's estate tax return, including extensions, to qualify for the exclusion.[336] A post-mortem donation will also qualify for an estate tax deduction under section 2055(f), but only if no parties take a section170(h) income tax deduction in relation to the donation.[337] The post-mortem opportunity under section 2031(c) provides executors and trustees a "look-back" period to fully evaluate the estate tax benefit of such a donation.[338] For landowners with estates possibly subject to the estate tax, these provisions provide an incentive to refrain from donating an easement during life—assuming estate tax avoidance is the landowner's primary motive—and instead allow the executor or trustee to make the ultimate decision. The post-mortem opportunity may also benefit "land rich, cash poor" families, or inheritors who otherwise could not afford the estate taxes incurred in connection with the devise of valuable land.[339]

I. Examples of Federal Estate Tax Benefits

Reminder: The following examples are based on the law in effect in 2009. Please see the introduction to Section III.H for a description of the key differences as of March

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[332] *See id.* at 539.

[333] *See* Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No.107-16 § 551(a), 115 Stat. 38, 86; I.R.C. § 2031(c)(8)(i). Without congressional action, it appears the pending sunset of the EGTRA provisions in 2010 will cause the previous, more restrictive standard to come back into effect. Such a change ultimately would limit taxpayer use of the section 2031(c) incentive.

[334] *See* I.R.C. § 2031(c)(8)(A)(i) (1997) (current version at I.R.C. § 2031 (c)(B)(A)(i) (2006)).

[335] *See* I.R.C. §§ 2031(c)(8)(C), (c)(9).

[336] *See* I.R.C. § 2031(c)(8)(A)(iii).

[337] *See* I.R.C. § 2031(c)(9); Lindstrom, *supra* note 132, at 546.

[338] *See* Lindstrom, *supra* note 132, at 546.

[339] *See* McLaughlin, *supra* note 94, at 16–17.

16, 2010 in regard to the federal estate tax that apply to conservation easement donations in 2010.

1. Example One: Inter Vivos Donation

Before he died, Mr. Marion donated a conservation easement on his picturesque farm on the Edisto River to a qualified land trust. This donation reduced the value of the farm from $4,000,000 to $2,000,000. The value of the farm on the date of Marion's death remained at $2,000,000, taking into account the restrictions of the easement. In 2009 Marion's executor elects to exclude 40% of the value of the farm subject to the conservation easement from Marion's estate under Code section 2031(c). The full $800,000 (40% x $2,000,000) is not eligible for exclusion, however, because section 2031(c) caps the total exclusion to $500,000. Therefore, the easement has reduced the taxable value in Marion's estate by a total of $2,500,000—Marion received an initial $2,000,000 discount based on the value of the land (as restricted) at death and an additional $500,000 reduction based on the section 2031(c) exclusion.

2. Example Two: Post-Mortem Donation

Mr. Kilmer owns a large tobacco farm in the rugged mountains of the High Country of North Carolina. The land in the area has appreciated in value substantially in recent years, and, as a result, Kilmer has a very valuable estate. Kilmer earns a low taxable income each year, so he would not benefit from an income tax deduction. The entire Kilmer family loves the farm and no one wants it to be sold outside of the family.

Because of his tight financial situation, Kilmer does not want to bind the land with a conservation easement; he wants to be able to sell it should the need arise. Therefore, Kilmer provides in his will for the donation of a conservation easement on the farm. Kilmer includes with the will a complete draft of the instrument so the executor does not have to guess what Kilmer might have wanted in the easement.

Kilmer dies in 2007 while plowing his tobacco field. The executor values the Kilmer farm on the date of his death at $6,000,000 before the easement and at $3,500,000 after the easement. The executor is able to deduct the $2,500,000 value of the easement under Code section 2055(f). The easement saves Kilmer's family $1,125,000 in estate taxes because the entire $2,500,000 would have otherwise been subject to the 45% marginal estate tax rate (assuming an estate tax exemption of $3,500,000 and estate tax rate of 45%). If Kilmer has no more assets in his estate, he will owe no estate tax because his estate equals the personal exemption of $3,500,000.

If Mr. Kilmer has other assets in his estate, his executor may use section 2031(c) to exclude an additional $500,000 from the estate's value (section 2031(c) will exclude the lesser of 40% of the restricted value of the land or $500,000).

Note that under Code section 2031(c)(9), even if Mr. Kilmer had not made a provision in his will for the easement, his heirs could have directed the executor to donate a post-mortem easement that would have provided the estate the same tax benefits as given by the testamentary easement above.

3. Example Three: Combined Federal Income and Estate Tax Incentives

Ms. Hampton owns a large acreage tract adjoining Congaree National Park, near Columbia, South Carolina. Hampton in 2006 donated a conservation easement on this land to a qualified organization, an experienced local land trust. The easement satisfies the requirements under Code section 170(h), including the habitat conservation purpose test because the land remains in a relatively natural state and abounds in local flora and fauna. The value of the land before the donation was $4,000,000 and the value of the land after the donation is $2,000,000. Thus, the value of the conservation easement and Ms. Hampton's federal income tax deduction is $2,000,000 ($4,000,000–$2,000,000).

Hampton earns income of $500,000 in the year of the donation. Code section 170(h) in effect in 2006 would have allowed her to take an income deduction each year in an amount equal to 50% of her annual income. Thus, with an income of $500,000, Hampton may take an income tax deduction of $250,000 in year one. Since this $250,000 otherwise would fall into the highest current income tax bracket (35%), this year's deduction is worth $87,500 in real dollar terms to Hampton (35% x $250,000). Under prior law, if Hampton continues to earn $500,000 annually, she can continue to take deductions of $250,000 (50% of annual income) each year until she has used the total conservation easement value of $2,000,000. Assuming this annual income, Hampton will be able to use the complete deduction in eight years—well under the allowable fifteen-year carry-forward. The net result of the donation is an income tax deduction of $2,000,000 spread over eight years generating real dollar savings of $700,000 for Hampton.[340] Note that

[340] Considering the time value of money, the actual current value of the deferred deductions would be less.

Hampton also would benefit from tax savings afforded by South Carolina's income tax credit program for conservation easement donations.[341]

In year ten, Ms. Hampton passes away while leaning against an old-growth pine tree on her property. The easement land has risen in value since she placed the easement on the property to $3,500,000. If the land were not subject to the easement, it would be worth $6,500,000 on the date of her death. In valuing Hampton's estate, her executor must include only the value of the land as restricted in her estate. Thus, assuming a personal estate tax exemption of $3,500,000 (the 2009 level), because of the land's loss of fair market value, her estate would avoid taxation on $3,000,000. Hampton will save at least $1,350,000 in estate taxes assuming a marginal estate tax rate (45% x $3,000,000). If the land is the only asset in Hampton's estate, the taxable estate will now equal the $3,500,000 personal estate tax exemption, and there will be no estate tax.[342] If, however, other assets increase the value of her estate to above the $3,500,000 exemption, her executor may elect the Code section 2031(c) exclusion to reduce her taxable estate by another $500,000, resulting in additional real-dollar estate tax savings of at least $225,000 (45% x $500,000).

In this transaction, Ms. Hampton utilized Code section 170(h) to generate a $2,000,000 deduction that resulted in a real income tax savings of $700,000. Additionally, Hampton used federal estate tax provisions—including 2031(c) and 2032(a)[343] —to reduce the value of her estate by at least $3,500,000, resulting in potential estate tax savings of $1,575,000 (45% x $3,500,000). Hampton and her heirs saved more than $2,000,000 in taxes through the donation of the conservation easement.

J. History of State Tax Incentives for Conservation Easements

Some states have adopted state tax policies that favor conservation easements. Generally, such measures fall into four categories: state income tax credits, state income tax deductions, property tax credits, and low prop-

[341] *See* Pentz, *supra* note 27, at 34.

[342] *See* I.R.C. § 2055(A).

[343] *See also* Treas. Reg. §25.2703-1(b)(4) (1992). While restrictions on the use of real property can not usually be considered for purposes of valuing real estate for estate tax purposes, the treasury regulation cited herein expressly allows for such a reduction in gross estate value for real property encumbered by qualified easements made subject to Code section 170(h). Note also that the inter vivos donation contemplated in this hypothetical would be deductible for gift tax purposes as well under Code section 2522(d).

erty assessments for property tax purposes.[344] While each of these measures undoubtedly helps motivate landowners to consider donating conservation easements, "the most successful [measure] has been the state income tax credit."[345] Because state income tax credits generally provide the most significant benefit for landowners, this Section will primarily cover their history, variety, and use, with limited treatment of the other tax policies that states have adopted.

Numerous states offer state income tax credits to landowners who voluntarily conserve their land through donations of conservation easements or fee title. These credits are sometimes referred to as "conservation credits".[346] Each state with such a program imposes certain requirements to ensure the donations generate sufficient public benefit.[347] In many credit programs, the requirements closely parallel the federal tax requirements in Code section 170(h).[348] States have considered the following issues, among others, in the development of their credit programs: valuation of the credit; transferability of credits; refundability of credits; types of entity that can receive credits; maximum value of credits that can be taken in a given year; carry-forward period; and statewide caps on credits honored.[349] A review of current credit programs reveals that states have adopted a "stunning variety" of approaches to reward landowners who voluntarily encumber their land through the use of conservation easements.[350] The diversity of state positions on income tax credit benefits contrasts markedly with the homogeneity of the federal tax incentives, as well as the general uniformity of state property law concerning conservation easements.

State statutory incentives are relatively new creatures—North Carolina authorized the first conservation credit statute in 1983.[351] Currently, twelve states—California, Colorado, Connecticut, Delaware, Georgia, Maryland, Mississippi, New Mexico, New York, North Carolina, South Carolina, and

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[344] *See* Pentz, *supra* note 27, at 32–34 (laying out each state statute and features in a helpful matrix for easy comparison).

[345] *Id.* at 36 n.1.

[346] *See id.*

[347] *See id.*

[348] *See id.* at 32–34.

[349] *See id.* at 17–29.

[350] Young, *supra* note 14, at 218–19.

[351] *See* Carol Greenberger, *Conservation Easements*, CHATTOOGA CONSERVANCY 2004, http://www.chattoogariver.org/index.php?quart=F2004&req=easements (last visited Feb. 12, 2009).

Virginia—have adopted a conservation easement state income tax credit program.[352]

Seven "high credit value" states offer credits valued at $100,000 or more for the donation of a conservation easement.[353] In contrast, "low credit value" states, such as Delaware and Mississippi, restrict maximum credit allowances to $50,000 and $10,000 respectively.[354] States also restrict the fiscal impact of conservation credit programs by limiting the amount of credit that a taxpayer may use in any one year, ranging from $5,000 in New York and Maryland to $375,000 in Colorado.[355] A handful of states also have placed caps on the amount of credits that the state will honor in a fiscal year, in an effort to cushion state treasuries from the potential impact of these new programs.[356] The majority of participating states tie credit valuation to the fair market value of the donated conservation easement.[357]

Closely related to the maximum allowable credit, another important provision in state credit programs is the carry-forward period—the time limit during which any unused credit can be used. Long carry-forward periods benefit taxpayers with lower state incomes and high-value easement donations.[358] While land-rich, cash-poor taxpayers may not use fully a large credit to offset their modest incomes in a small period of time, states offering longer carry-forward periods—or an unlimited carry-forward, as in South Carolina—may allow such incomes to be offset fully by the credit for a number of years.[359] Currently, all states offer at least a five-year carry-forward period.[360]

Credit "transferability" is one variable in such programs that has received ample attention—both for its beneficial tendency to spur land conservation and its potential for taxpayer abuse.[361] States that have adopted this element in their programs allow the assignment, transfer, or sale of unused credits to third party buyers. Because income tax credits are only

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[352] *See* Young, *supra* note 14, at 218–19.

[353] *See* Pentz, *supra* note 27, at 32–34.

[354] *See id.*

[355] *See id.*

[356] *See id.* at 20, 32–34.

[357] *See id.* at 19.

[358] *See id.* at 23.

[359] *See id.* at 23–24.

[360] *See id.* at 23.

[361] *See* McLaughlin, *supra* note 94 at 23–25 (describing an increase in easement donations in Virginia as a result of transfer programs); *see also* Young, *supra* note 14, at 223–24 (noting perceived abuse potential in transfer programs).

useful to those landowners who earn sufficient annual income to use them, transferability makes the donation of a conservation easement appeal to a broader class of landowners, including land-rich, cash-poor taxpayers.[362]

To date, only Virginia, Colorado, South Carolina, and New Mexico have adopted credit transferability.[363] While South Carolina's transferable credit program perhaps suffers from the fact that only a relatively small value of credits may be used in a given year ($52,500), the programs in Colorado and Virginia, with higher annual credit limits, have fueled the development of successful credit trading markets and spurred measurable increases in conservation easement donations.[364] However, such programs have also spurred concerns over taxpayer abuse and a potentially overwhelming fiscal drain.[365] Fear that transferability invites inflated valuations and donations of conservation easements that lack adequate conservation value may prompt allegations of fraud such as those that sparked the Service to audit hundreds of donors participating in Colorado's transferability program.[366] However, in view of the potential public benefits from increased easement donations and the broad appeal transferability has for landowners, transferability seems likely to be incorporated into more state credit programs.[367]

The refundability of credits provision has also garnered attention, but has been adopted only in Colorado and New York.[368] While this provision clearly motivates property owners to donate land, "[l]egislatures are generally loath to make any type of tax credits refundable."[369] The Colorado Legislature authorized the state to pay taxpayers up to $50,000 for the value of credits earned through the donation of a conservation easement, but only in

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[362] *See* McLaughlin, *supra* note 94 at 98.

[363] *See* Pentz, *supra* note 27, at 23.

[364] *See id.* at 14; *see also id.* at 32–34 (As of 2009, Virginia and Colorado's limits on credits that may be applied against taxes in a given year were $50,000 and $375,000, respectively.

[365] *See* Young, *supra* note 14, at 223–24.

[366] *See id.*

[367] *See* Pentz, *supra* note 27, at 24 (noting that the majority of states with credit programs without a transfer element have indicated a desire to incorporate such a feature).

[368] *See id.* at 24.

[369] *Id*;

budget surplus years.[370] The budget surplus requirement means Colorado credit holders frequently have been unable to get credit refunds.[371]

A separate category of state-level tax incentives for conservation easement donations includes those that provide for lower property tax assessments, or, as in New York, provide a state tax credit that may be used to offset property taxes.[372] The donation of a conservation easement involves giving away some of the rights associated with owning land. Thus, the fair market value of the land is generally diminished and lower local property taxes should result.[373] However, local assessors have been reluctant to find lower fair market values of land subject to a conservation easement, presumably haunted by "[t]he specter of declining property tax revenues."[374] Confronted by local hesitation, some state legislatures have adopted measures to guarantee a new property tax valuation after the donation of a conservation easement. For example, Oregon's conservation easement enabling act mandates that "real property . . . subject to a highway scenic preservation easement shall be assessed on the basis of the real market value of the property less any reduction in value caused by the . . . easement."[375] North Carolina recently enacted a similar law directing qualified conservation land to be taxed at the same reduced rate as is agricultural land.[376] In 2006, New York enacted a program that goes one step further, providing easement donors with a credit "for twenty-five percent of the allowable school district, county and town real property taxes on such land."[377] In states where the legislature has not expressly mandated the revaluation of conservation easement-encumbered property or adopted the New York credit approach, landowners may still be entitled to a reduction in property taxes due to their land's loss in development value, but may face an uphill struggle with local property assessors.

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[370] *See* COLO. REV. STAT. § 39-22-522(5)(b)(II)–(III) (2009).

[371] *See* Pentz, *supra* note 27, at 24 (The New York refundability program is tightly limited by a $5,000 cap. New York credits are only refundable if a taxpayer earns income tax credits in excess of taxes due.).

[372] *See* N.Y. TAX § 606(kk)(1) (McKinney 2006 & Supp. 2010).

[373] *See* Maybank, *supra* note 18, at 2.

[374] Draper, *supra* note 97, at 271.

[375] OR. REV. STAT. § 271.785 (2007).

[376] *See* N.C. GEN. STAT. ANN. § 105-277.15(b).

[377] N.Y. TAX § 606(kk)(1) (McKinney 2006 & Supp. 2010).

K. The State Income Tax Credits: Mechanics of the Incentives

Fortunately for practitioners, state income tax programs are generally tied to the Code section 170(h) requirements for federal deductibility.[378] Thus, often it is only necessary to qualify under the federal standards for the landowner to be eligible for state tax benefits.[379] Specifically, states have adopted the section 170(h) standards regarding (1) the type of conservation easement that qualifies for the credits (paralleling the conservation purposes test) and (2) the entities that may hold such easements (paralleling the eligible donee test).[380] Practitioners should note, however, that the majority of states further define the types of land to which the state benefit will apply.[381] Many states grant per se beneficial tax status to certain types of conservation easement donations (for example, those protecting watersheds, wetlands, and prime agricultural lands).[382] But other states significantly limit the type of donations that qualify for state tax benefits. For example, Mississippi requires that properties either be designated officially as conservation sites or adjacent to such sites in order to claim the state tax benefit.[383] This latter example reveals that while many state statutes closely parallel the section 170(h) requirements, practitioners must review the relevant state statutes carefully for specific state law requirements.[384]

L. Potential Benefits Under Several State Income Tax Credit Programs

While most state programs closely (or entirely) follow the federal tax code and Treasury regulation requirements regarding the type of conservation easement donations that qualify for tax benefits, states vary widely in the character of the tax credit benefits offered.[385] States differ in several key categories, including: valuation of the credits; carry-forward period; maxi-

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[378] *See* Pentz, *supra* note 27, at 19.

[379] *See id.* at 32–34.

[380] *See id.*

[381] *See id.*

[382] *See, e.g.*, GA. CODE ANN. § 48-7-29.12 (2006); N.M. STAT. ANN. §§ 75-9-1–75-9-5, 7-2-18.10 (LexisNexis 2004); N.M. CODE R. § 3.13.20 (Weil 2004).

[383] *See* MISS. CODE ANN. § 27-7-22.21 (2003) (restricting eligibility to non-industrial private lands either contiguous with a stream "nominated to the Mississippi Scenic Streams, Stewardship Program," or lands designated "priority sites for conservation under the Mississippi Natural Heritage Program").

[384] *See* Pentz, *supra* note 27, at 22 (noting that additional requirements may commonly be found in a state's conservation easement enabling legislation or conservation tax credit legislation). For a summarized review of relevant state statutes see *id.* at 32–34.

[385] *See id.* at 32–34.

mum income tax credits allowed per donation; cap on credits that may be applied against taxes in a tax year; and the number of different credits that may be claimed by a taxpayer annually.[386] While an exhaustive discussion of each state program is beyond the scope of this Article, the following comparison and assessment of three programs provides contrast and demonstrates the diversity of benefits offered under different state regimes.

1. South Carolina's Income Tax Credit Program: S.C. Code Ann. § 12-6-3515

The South Carolina income tax credit program provides a tax credit on the donation of a conservation easement equal to the lesser of $250 per encumbered acre or 25% of the value of the federal conservation easement deduction.[387] This valuation regime gives South Carolinians credits that are less valuable than those afforded residents of other states.[388] However, the state does not cap the value of a state income tax credit for a conservation easement donation, and has an unlimited carry-forward period in which to utilize the credit.[389] South Carolina limits the amount of a conservation income tax credit available to a taxpayer in a given year at $52,500.[390] While South Carolina does not limit the number of different conservation credits available in a given year, it remains unclear whether the overall $52,500 limit on credits applied in a given year restricts the credit from one easement donation or multiple donations.[391] Notably, South Carolina allows credit transferability—the sale of credits to taxpayers who may better use them—which greatly increases the efficacy of a state conservation incentive program.[392] Transferability benefits landowners who otherwise would not be able to offset relatively low incomes with credits by providing cash in hand when credits are sold to purchasing taxpayers who buy the credits at a slight discount.[393] South Carolina's income tax credit program may be fiscally conservative, but it is thoughtful. The state's regime allows all landowners to benefit on a nearly egalitarian basis through transferability, but

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[386] *See id.* at 18–24.

[387] *See* S.C. CODE ANN. §12-6-3515(c)(1) (2006).

[388] *See* Pentz, *supra* note 27, at 14.

[389] *See* S.C. CODE ANN. § 12-6-3515(A).

[390] *See* S.C. CODE ANN. § 12-6-3515(c)(2).

[391] *See id.*

[392] *See* Pentz, *supra* note 27, at 13, 23.

[393] *See id.*

limits the overall incentive (and arguably, efficacy) of the program through restrictive credit valuation standards.[394]

2. North Carolina's Income Tax Credit Program: N.C. Gen. Stat. § 105-151.12 and § 105-130.34

The North Carolina conservation incentive program provides an income tax credit for conservation easement donations equal to 25% of the fair market value of the conservation easement.[395] North Carolina limits the maximum credit allowed for a conservation easement donation to $250,000 for individuals and $500,000 for corporations.[396] While these valuation standards compare favorably to South Carolina's more restrictive approach, North Carolina only allows a five-year carry forward and does not allow transferability.[397] On the other hand, North Carolina does not limit the number of different conservation easement transactions a taxpayer may claim credits for in a given year.[398] Notably, unlike most states, to qualify for income tax credits, North Carolina does not require that donated easements meet the requirements of Code section 170(h). Instead, North Carolina requires that each donation qualify in one of nine categories of public benefits that provide eligibility for state tax credits, including fish and wildlife conservation, farmland preservation, and conservation of natural areas.[399] For a donation to earn the credits, North Carolina requires that a state agency certify the donation as achieving one of the qualifying public benefits.[400] North Carolina's program properly may be viewed as a middle of the road incentive offering. While the maximum credit amounts are fairly high, the lack of transferability may leave lower income landowners without sufficient incentive to donate conservation easements protecting the farms, forests, and mountainsides that characterize natural North Carolina.

3. Colorado's Income Tax Credit Program: Colo. Rev. Stat. § 39-22-522

Colorado's income tax credit program appears to be the most donor friendly in the nation. The Colorado incentive program provides an income

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[394] *See* Pentz, *supra* note 27, at 32–34 (displaying a graphical matrix for comparison of all state conservation tax credit statutes).

[395] *See* N.C. GEN. STAT. § 105-151.12 (a) (amended 2009).

[396] *See id.* § 105-151.12 (a)(1), (a)(2).

[397] *See id.* § 105-151.12 (b); Pentz, *supra* note 27, at 33.

[398] *See* Pentz, *supra* note 27, at 33.

[399] *See* N.C. GEN. STAT. § 105-151.12 (a), (a)(1).

[400] *See id.* § 105-151.12 (a)(1).

tax credit for conservation easement donations equal to a substantial 50% of the fair market value of the conservation easement and allows a taxpayer to claim up to $375,000 of state income tax credits for a single donation.[401] The state limits the amount of credits that a taxpayer may claim in a given year to $375,000 and limits taxpayers to claiming the tax credits on one conservation easement donation per year.[402] Colorado also provides a generous twenty-year carry-forward period during which taxpayers may use any excess credit generated by a donation.[403] In addition, Colorado allows transferability of tax credits.[404] Colorado's transferability program enjoys great success due to the high credit valuations.[405] Colorado is also the only state to make tax credits refundable during state budget surplus years.[406] While the states' promise to pay cash for income tax credits sounds wonderful to eligible taxpayers, the budget surplus year limitation has rendered the refundable element of the program moot in all but a few years.[407] Regardless, Colorado's high value credits, coupled with a long carry-forward period and transferability, give the state's landowners substantial conservation incentive. While the state arguably takes fiscal risk by being the first to offer such lucrative tax incentives, Colorado has taken a bold stand, successfully spurring conservation of land in an ecologically important part of the country.

In summary, state income tax credit programs employ requirements for qualifying conservation easement donations that generally are similar to those under federal law, while the state tax benefits vary widely. A practitioner in one of the twelve participating states should carefully review and understand the applicable conservation credit statute, and ensure that clients benefit from both state and federal tax benefits with respect to donations. Examples involving different state income tax credit programs are set forth below.

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[401] *See* COLO. REV. STAT. § 39-22-522(4)(a)(II) (2009).

[402] *See id.* § 39-22-522(4)(a)(III).

[403] *See id.* § 39-22-522(5)(a).

[404] *See id.* § 39-22-522(7).

[405] *See* Pentz, *supra* note 27, at 14.

[406] *See* COLO. REV. STAT. § 39-22-522(5).

[407] *See* Pentz, *supra* note 27, at 24.

M. Examples of State Income Tax Credit Effects

1. Example One: South Carolina

Mr. Micheaux owns 100 acres of spectacular wooded property near the Chattooga River in the mountains of South Carolina. Micheaux decides to place a conservation easement on the property because he values the unique ecology of the area and wants it to remain undeveloped. However, Micheaux is also interested in all available tax benefits because he wants to offset a recent increase in his income from his new book on Appalachian ecosystems.

After consulting an attorney and an experienced land trust, Micheaux donates a conservation easement that satisfies all of the requirements of Code section 170(h). Because the conservation easement reduced the value of Micheaux's land from $1,000,000 to $400,000, the easement is worth $600,000. Micheaux thus (if the 2009 federal tax law were in place) has a $600,000 federal charitable income tax deduction that he may use over as many as fifteen years.

South Carolina has a state income tax credit program that grants credits for donations that meet the requirements of Code section 170(h).[408] Thus, Micheaux's donation does not require additional compliance steps to qualify for income tax credits from the state. South Carolina's tax incentive program provides tax credits equal in value to the lesser of $250 per encumbered acre or 25% of the Federal income tax deduction granted under section 170(h).[409] Because multiplying Micheaux's acreage by the per acre value yields a sum of $25,000 (100 acres x $250) and 25% of his federal deduction is $150,000 (25% x $600,000), Micheaux will receive a state income tax credit equal to the lesser of these two figures, $25,000.

Micheaux is excited about his $25,000 state income tax credit, but he is only able to use $10,000 worth of the credits because that is the extent of his state income tax liability for the year. Additionally, Micheaux plans to retire after the success of his book and foresees no taxable income over the next several years. Fortunately for Micheaux, South Carolina is one of four states to offer transferable income tax credits, meaning that Micheaux can sell his remaining tax credits ($15,000) to a South Carolina taxpayer who can use them.[410] Micheaux uses a conservation credit exchange service in South

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[408] *See supra* note 387 and accompanying text.

[409] *See supra* note 387 and accompanying text.

[410] *See* Pentz, *supra* note 27, at 23.

Carolina that assists him in finding a buyer for his credits.[411] Additionally, Micheaux works with his attorney and the exchange service to ensure that the transfer is certified by the South Carolina Department of Revenue, as required by law.[412] Micheaux sells his unused credits for 80% of their fair market value and receives $12,000 cash in hand as a result.

Ultimately, Micheaux is able to offset $10,000 in state income taxes and receive $12,000 cash in the year of his conservation easement donation.[413]

2. Example Two: North Carolina

Assume that Mr. Bartram owns land with the same acreage and before and after values as Mr. Micheaux above. Bartram also owns pristine forested land near the Chattooga River, but his land is located just across the state line in North Carolina. Bartram claims the same Federal income tax deduction ($600,000), however, when Bartram consults with his attorney, he learns that completely different rules apply.

The state of North Carolina has an income tax credit program that grants credits for conservation easement donations according to requirements outside those of Code section 170(h). North Carolina grants such credits if the donation meets one of nine enumerated public benefit purposes.[414] The statute also requires that the donor make the donation in perpetuity to a government agency or qualified charity, that the claim be

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[411] *See* South Carolina Conservation Credit Exchange, http://www.conservesc.com, (last visited Feb. 22, 2009).

[412] *See* S.C. Rev. Proc. #08-1, *Transfer, Devise, or Distribution of a Conservation Credit Under Code Section 12-6-3515, available at* http://www.conservesc.com/documents/SCTaxRevenueBulletin041508.pdf (last visited Feb. 22, 2009) (describing process for certification of credit transfer in South Carolina).

[413] *See* Lindstrom, *supra* note 132**,** at 521–22 (discussing the effect of transferring (selling) a tax credit on both the transferor's and recipient's federal income tax liability). To date, it appears that the Service has taken the position that the use of a state income tax credit to offset the original donor's state tax liability is not taxable, but that any proceeds received by the seller from the sale of the tax credit will be taxed as ordinary income under Code section 1001. *See id.* The IRS also has suggested that the recipient (purchaser) of a state tax credit may deduct the value of the credit used against state tax for federal income tax purposes under Code section 164(a). *See id.* Further effects stemming from the interrelation between state income tax credit claims and federal tax liability are explored further at the reference cited herein, but the reader should note that these questions are largely unresolved. Perhaps more disquieting, there remains the possibility that the Service may view the receipt of state income tax credits as a "quid pro quo" transaction violating the donative intent requirement under Code section 170(h), which would provide grounds to disallow the federal tax benefit to state credit recipients. To date, the Service has not spoken to this issue.

[414] *See* N.C. GEN. STAT. § 105-151.12(a) (2009).

accompanied by a summary appraisal, and that a state agency certify that the donation meets one of the nine public benefit purposes.[415]

With the aid of his attorney, Bartram is confident that his donation achieves the public benefit purpose of forestland conservation.[416] The donee local land trust meets the requirement of an eligible easement holder under the statute. Bartram later submits his credit claim to the appropriate state agency, the North Carolina Department of Environment and Natural Resources, and the state agency certifies that his donation meets the forestland conservation purpose.

North Carolina's credit program values credits at 25% of the easement's fair market value.[417] Thus, Bartram will receive $150,000 of North Carolina income tax credits (25% x $600,000). (Note that North Carolina's program provides Bartram with much more credit than his South Carolina peer for a virtually identical donation).

Assume Bartram, like Micheaux above, has only $10,000 in state income tax due for the year. Bartram happily offsets his $10,000 in state income for the year, but is concerned about what to do with the remaining $140,000 in income tax credits, as he expects to earn no income for the next two years while he writes his next book, "Rare Flora in the Chattooga River Basin." Unlike in South Carolina, North Carolina credits are not transferable, so Bartram may not sell his unused credits and receive cash.[418]

Fortunately for Bartram, North Carolina affords a five year carry-forward for the state income tax credits.[419] When Bartram has state income tax liabilities of $20,000 and $30,000 in years four and five (due to the success of his new book), he will be able to use an additional $50,000 of his remaining $140,000 tax credits to offset these taxes. However, despite Bartram's book income in subsequent years, he will be unable to use any more of his tax credits because the carry-forward period has expired. As a result, $90,000 in tax credits go to waste. This example reveals how the lack of a transferability element and a relatively short carry-forward period [420] can greatly diminish a landowner's ability to use state income tax credits. De-

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[415] *See id.*

[416] *See id.*

[417] *See id.*

[418] *See* Pentz, *supra* note 27, at 23.

[419] *See* N.C. GEN. STAT. § 105.151.12(b).

[420] *See* Pentz, *supra* note 27, at 32–34 (graphic matrix comparing different state credit programs reveals that North Carolina's carry-forward period is shorter than those of many peer states).

spite the "wasted" credits, Bartram still has been able to offset $60,000 in state income taxes over a period of five years.

N. Abuse in the Conservation Easement Field: Cause for Concern?

The drafters of the UCEA and the states that adopted the uniform statute or similar acts believed that limiting the holder of easements to government or qualified charitable organizations provided a sufficient oversight mechanism to prevent abuse.[421] The drafters believed that these holders were trustworthy parties and that tax and charitable organization legal backstops would prevent abuse.[422] Thus, they installed no mechanism for public review or additional safeguards ensuring the public benefit of easement donations into the UCEA. Subsequent future events, however, revealed substantial abuses and cast doubt on the future of the conservation easement.

Jason A. Richardson's 2005 article provides several examples of negative publicity about abuses involving conservation easements.[423] However, the reporting that "blew the door open for Congressional involvement" surfaced in a 2003 series in the *Washington Post*.[424] The *Post* series exposed questionable transactions involving Code section 170(h).[425] The transactions reported in these articles involved such important conservation players as the Nature Conservancy and involved donations of easements on land that never had significant development value (for example, land with steep slopes or in floodplains).[426] The series also specifically discussed the donation of easements on golf courses.[427]

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[421] *See* King & Fairfax, *supra* note 21, at 86.

[422] *See id.*

[423] *See* Jason A. Richardson, *Increased Scrutiny on Conservation Easement Donations: How a Crackdown on Tax Fraud by the IRS Could Impact Environmental Protection*, 1 ENVTL & ENERGY L. & POL'Y J. 273, 273–75 (2005).

[424] *Id.* at 275.

[425] *See id.* (citing David B. Ottaway & Joe Stephens, *Nonprofit Sells Scenic Acreage to Allies at a Loss*, WASH. POST, May 4, 2003, at A1; Joe Stephens & David B. Ottaway, *How a Bid to Save a Species Came to Grief*, WASH. POST, May 5, 2003, at A1; Joe Stephens & David B. Ottaway, *Nonprofit Sells Scenic Acreage to Allies at a Loss*, WASH. POST, May 6, 2003, at A1).

[426] *See id.*

[427] *See id.*

1. Federal Response

The *Washington Post* articles sparked the Congressional Joint Committee on Taxation to review the tax treatment of conservation easements, recommending the elimination of "the charitable contribution deduction with respect to . . . conservation easements relating to personal residence properties, [a substantial reduction in] the deduction for all other qualified conservation contributions, and . . . new standards on appraisals and appraisers regarding the valuation of such contributions."[428]

In another response to the abuse scandal, the Senate Finance Committee launched an independent review of the transactions of The Nature Conservancy targeted in the *Post* articles.[429] In its resulting report, the Finance Committee recommended revocation of a conservation organization's tax-exempt status if it "regularly and continuously fails to monitor and enforce conservation easements." Among other suggestions, the report recommended "implementation of an accreditation system for conservation organizations," limiting tax deductions for "certain small easement donations," while authorizing the Service to pre-approve such donations, and recommending that the Service "issue guidance [as to the] factors . . . necessary to establish minimum levels of compliance" in monitoring easements.[430]

The Service responded to the scandal with a June 2004 news release that revealed its awareness of fraudulent practices in the conservation easement field.[431] Service Commissioner Mark W. Everson's remark quoted in the release was a shot over the bows of unscrupulous donors and complacent nonprofits: "Taxpayers who want to game the system and the charities that assist them will be called to account."[432]

Following the news release, the Service published a notice titled "Charitable Contributions and Conservation Easements" in July 2004.[433] The notice warned that the Service would investigate charitable income deduc-

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[428] STAFF OF J. COMM. ON TAXATION, 110TH CONG., OPTIONS TO IMPROVE TAX COMPLIANCE AND REFORM TAX EXPENDITURES 281 (Comm. Print 2005), *available at* hppt://jct.gov/s-205.pdf.

[429] *See* Jonathan M. Burke, Note, *A Critical Analysis of Glass v. Commissioner: Why Size Should Matter for Conservation Easements*, 61 TAX LAW. 599, 604 (2008).

[430] STAFF OF S. COMM. ON FINANCE, 110TH CONG., COMMITTEE REPORT ON THE NATURE CONSERVANCY, EXECUTIVE SUMMARY 10-11 (Comm. Print 2005), *available at* http://finance.senate.gov/hearings/other/tncontents.pdf; *see also* Burke, *supra* note 429, at 604.

[431] *See* I.R.S. News Release IR-2004-86 (June 30, 2004).

[432] *Id.*

[433] *See* I.R.S. Notice 2004-41, 2004-28 I.R.B. 31.

tions claimed under Code section 170(h) and impose penalties and excise taxes to cut abuse from the system.[434] The notice also described penalties for promoters of abusive conservation easement deals.[435]

As one commentator notes, "[d]espite these recommendations, Congress made no changes to the requirements of [section] 170(h), and in fact 'sweetened' the appeal of conservation easements" by passing legislation improving the tax treatment of conservation easement donations.[436] However, the scandal did result in changes in the practices of major conservation organizations. The review of the Senate Finance Committee spurred The Nature Conservancy "to ban a range of practices in conducting easement transactions."[437] The Land Trust Alliance—the chief lobbying and organizational group for land trusts—responded to the scandal "by implementing training and accreditation programs to improve ethics and fiscal accountability by land trusts across the country."[438] Three years later, the first land trusts to enter the program received accreditation from the Land Trust Accreditation Commission.[439] Land trust accreditation is intended to help assure landowners, government entities, professional advisors, and the general public that the certified nonprofit has the "capacity . . . and expertise" to perform properly this important work[440] but accreditation is voluntary, and accreditation decisions are made by those who work for and with the land trusts seeking accreditation.[441]

In the wake of federal scrutiny and subsequent curative steps on behalf of conservation organizations, statistics from across the nation reveal that conservation easement donations continue to rise exponentially.[442] If the willingness of taxpayers to continue donating conservation easements is any

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[434] *See id.*; *see also* Richardson, *supra* note 423, at sec. IV.

[435] *See* I.R.S. Notice 2004-41, 2004-28 I.R.B. 31.

[436] Burke, *supra* note 429, at 604–05.

[437] Richardson, *supra* note 423, at 276.

[438] *Id.*

[439] *See* Land Trust Accreditation Commission, *August 2008 Accreditation Decisions,* Aug. 2008, *available at* http://www.landtrustaccreditation.org/about-the-commission/notice-of-decisions/40-notice-of-decisions/61-august-2008-meeting (last visited Feb. 12, 2009).

[440] E-mail interview with Brad Wyche, Executive Director, Upstate Forever Land Trust, Greenville, SC (Nov. 10, 2008) (on file with author).

[441] *See* Commissioners, http://www.landtrustaccreditation.org/about-the-commission/commissioners (describing the backgrounds and employment of the accreditation commissioners) (last visited Mar. 11, 2010).

[442] *See* The Land Trust Alliance, *Private Land Conservation in U.S. Soars*, Nov. 30, 2006, http://www.landtrustalliance.org/about-us/news/alliance-news/private-land-conservation-in-u.s.-soars (last visited Feb. 4, 2009).

indication, the federal abuse investigations and resulting action did not diminish landowner enthusiasm. The federal audits and investigations do, however, provide important guidance to practitioners working with conservation easements regarding specific issues (such as valuation) to which attorneys must pay particular attention.[443]

2. State Response

Inquiries into abusive donations did not stop at the federal level. Individual states have been quick to detect and uncover abusive easements.[444] The states offering income tax credits have a substantial budgetary motivation to quell abuses. The size of the potential fiscal liability is huge. For example, a South Carolina Department of Revenue (SCDOR) audit of a mere fifty-one conservation easements revealed that conservation easement donors valued those donations at over $255 million.[445] Burnet R. Maybank III, then director of SCDOR, focused his scrutiny on the same issues focused on by the Service, including valuation fraud, unscrupulous promoters of golf course or development-related easements, and the qualifications of the conservation organizations receiving the donations.[446] Maybank also testified at the federal Senate hearings and echoed the concern of many state treasury officials, noting, "I don't think Congress had golf courses in mind when it set up the provision."[447] At the same hearing, Maybank revealed that more than $125 million in easements were placed on golf fairways in South Carolina in the years preceding the Senate inquiry.[448]

Certain states had additional reasons to worry. History suggests that state income tax credit programs allowing transferability or sale of high value tax credits tend to fuel abuse. Colorado, a state with such a credit

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[443] *See supra* Part III.C, for a discussion of specific areas that practitioners should scrutinize.

[444] *See* Connie Kertz, *Conservation Easements at the Crossroads*, 34 REAL EST. L. J. 139, 150 (2005); *see also* S.C. DEP'T OF REVENUE, LOCAL, STATE AND FEDERAL TAX INCENTIVES FOR CONSERVATION EASEMENTS 108, 120 (3d. ed. 2005), *available at* http://www.sctax.org/NR/rdonlyres/0a5a6241-e75f-4a85-939e-dbc9d2c0ccdd/0/conservationEasementthird.pdf.

[445] *See* John O'Conner & Gina Smith, *Conservation Easements Face Scrutiny: Some Landowners May be Seeing Inflated Tax Breaks*, THE STATE (COLUMBIA, S.C.) Feb. 20, 2005, at B1; *available at* http://envirovaluation.org/index.php/2005/02/20/the_state_south_carolina_www_thestate_co (noting that, in comparison, South Carolina collected approximately $420 million in corporate taxes during the same time period).

[446] *See id.*

[447] Quoted in Kertz, *supra* note 444, at 150.

[448] *See id.*

program, has played the unenviable role of demonstrating this potential for abuse. Indeed, a double—federal and state—incentive for donors to misrepresent the value of a donation has led to clear abuse, worthy of attracting both state and federal attention.[449] The Colorado incentive regime led to a variety of unintended consequences including the "manufacturing" of Colorado taxpayers and the fragmentation of conservation land so that donations could be staggered.[450] These and other schemes are intended to qualify non-Colorado residents for the state's tax credits and maximize total credits by circumventing per-donation tax credit limits.[451] Ultimately, such abuses of the state program unfairly burden the state (and non-donor taxpayers).[452]

States have enacted several oversight and accountability mechanisms to counter fraud in the easement donation context. Both South Carolina and Colorado now use audits in which the states review nominally qualifying donations to determine their validity.[453] The donations may be disqualified at any time within the relevant statute of limitations period.[454] In addition to performing audits, South Carolina also requires state certification of an easement donation before the transfer (sale) of earned tax credits.[455] Seven other states follow such a certification approach, while other states use a "transactional screen" to review credits at the time of donation and weed out clearly abusive donations.[456]

Despite a period of perceived and actual abuse in states offering conservation easement benefits, a consensus of reports and experts agree that abusive donations represent only a small percentage of all transactions.[457] Additionally, the increase in public benefit garnered by increased incentives, such as transferability, has been measured by large-percentage in-

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[449] *See* Young, *supra* note 14 at 223–24.

[450] *See* Jessica E. Jay, *Changes to Colorado's Conservation Income Tax Credit Law*, COLO. LAW., Feb. 2003, at 68–70, *updated version available at* http://conservationlaw.org/_wsn/page3.html (last visited Feb. 12, 2009).

[451] *See id.*

[452] *See id.* at 69.

[453] *See* Pentz, *supra* note 27, at 25–26.

[454] *See id.* at 25.

[455] *See id.* at 26.

[456] *See id*. at 25–26, 28–29. The transactional screen method works to review transaction both before and immediately after the tax claim for the donation is made.. This expedited review process is intended to ensure that every donation meets minimum standards. Such programs also attempt to deny outright clearly abusive or improper donations and preserve the right to raise objections on more specific questions pertaining to a donation at a later date. *See id.*

[457] *See* Richardson, *supra* note 423, at 274–75.

creases in conservation easement donations in participating states.[458] Because of the efficacy of these programs and the relatively low incidence of abuse, transferability and additional easement incentives likely will be adopted, albeit carefully, by additional states seeking to spur the conservation of private lands.[459]

IV. CLIENTS AND PRACTITIONERS: INTERESTS IN THE CONSERVATION EASEMENT

A. The State of the Conservation Easement Field Today

After a history replete with an abuse scandal and explosive growth, the conservation easement today likely is more established than ever before, and the use of the conservation easement continues to expand.[460] While commentators may disagree as to whether the prolonged popularity of this mechanism is founded on a growing appreciation of ecological stewardship or financial incentives,[461] it makes little difference for the practitioner. Landowners continue to find the conservation easement an ideal tool with which to achieve a variety of personal goals. Moreover, the exponential growth in donations over the last two decades suggests that many taxpayers may only now be learning about the easement and its diverse benefits.[462] On the legal front, state enabling statutes have provided a solid legal framework for the use of the conservation easement, while Congress has increased the tax incentives, fanning client demand.[463] Additionally, the conservation easement continues to enjoy broad political appeal, thanks to its ability to

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[458] *See* Pentz, *supra* note 27, at 10–15.

[459] *See id.* at 9, 24 (noting that several states intend to increase valuation of credits, plan to create state tax credit programs, or have recently taken action supporting conservation easement donation and suggesting that at least seven new states are interested in implementing a transferability program).

[460] *See* Land Trust Alliance, *supra* note 35.

[461] *See* Greene, *supra* note 6, at 888 (citing PROTECTING THE LAND: CONSERVATION EASEMENTS POST, PRESENT, AND FUTURE, xxi (Julie Ann Constanski & Roderick H. Squires, eds., 2000)).

[462] *See* Greene, *supra* note 6, at 888 (documenting the dramatic increase in conservation easement donations from 1990 to 2000); Land Trust Alliance, *supra* note 35 (documenting the increase in conservation easement donations between 2000 and 2005).

[463] *See* Press Release, Lowcountry Open Land Trust, Federal Tax Benefits for Conservation Easement Donors Extended Through Dec 31, 2009, May 22, 2008, http://www.lolt.org/TaxEnhancementsExpired (last viewed Oct. 28, 2008) (describing extension of heightened conservation easement tax incentives through the 2008 Farm Bill).

accomplish land conservation without mandated regulatory strictures.[464] Although abuse scandals have brought uncomfortable scrutiny, this scrutiny left landowner enthusiasm unscathed while providing valuable guidance for legislators and attorneys.

B. Motivations for Landowners: Tax or Something Else?

Given the significant federal and state tax benefits associated with conservation easement donations, one might believe that conservation easements have enjoyed popularity only as a tax-savings mechanism. The tax incentives, however, seldom will be the sole motivating factor for clients. The potential flexibility of the conservation easement helps drive donations. While the tax benefits discussed in this Article may be the primary motivating factor for some clients, landowners are also comfortable with conservation easements "because they are voluntary . . . [and] the restrictions in a conservation easement can be tailored to the particular characteristics of the land and the particular desires of the landowner."[465] The landowner can use the land in any way consistent with the purposes of the easement, and burdensome measures—such as granting public access—are not necessary.[466] This flexibility and control over easement terms make them attractive to many donors.

For most landowners the primary motivation for donating a conservation easement is an altruistic love of their property.[467] Commentators speculate that such altruism and dedication to land is based on new public awareness of the impacts of urban sprawl, farm land extinction, open space loss, and natural resource degradation.[468] Several surveys provide support. In a 1985 survey conducted by the Land Trust Exchange—an organization now known as the Land Trust Alliance—data revealed that "67 percent of the easement program administrators who responded to the survey . . . regarded 'love for the land' as the primary factor that motivates landowners to donate easements. . . . [while] 22 percent of the Administrators regarded the charitable income tax deduction as the primary factor that

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[464] *See* Young, *supra* note 14, at 218.

[465] Nancy A. McLaughlin, *Conservation Easements—A Troubled Adolescence,* 26 J. LAND RESOURCES & ENVTL. L. 47, 52 (2005).

[466] *See id.*

[467] *See generally* Greene, *supra* note 6, at 883–84.

[468] *See, e.g.*, Draper, *supra* note 97, at 252–54 (discussing negative effects of urban sprawl); Greene, *supra* note 6, at 883–84 (citing urban sprawl and environmental degradation as motivations for popular support of land conservation).

motivates landowners to donate easements."[469] A 1995 University of Michigan survey of motivations underlying land donations including conservation easements supports the Land Trust Exchange survey findings—the top three reported motivations for such donations include (in order of rank): "a deep and personal commitment to the future of the land," "a concern about ecological stewardship," and "economic concerns, including the ability to claim a tax deduction as a result of the donation."[470] Finally, a 1997 State University of New York survey found that "[m]ore externalized concerns of tax breaks and pressure from family or friends are *not* primary motivations to restrict a piece of land."[471] A review of these surveys supports the conclusion that most landowners donate conservation easements to conserve the land to which they are personally attached or for ecological reasons, rather than solely to gain tax benefits.

Tax benefits do play an important secondary role as a motivator in conservation easement donations,[472] and tax incentives have increased since these surveys were conducted.[473] These increased tax benefits may change the primary motivations of individuals who participate in conservation easement donation. However, recent polls suggest that public support for environmental causes remains strong.[474] Increased interest in conservation or ecological values may reinforce the altruistic motivations previous easement donation surveys found. The practitioner likely can expect clients to be drawn to conservation easements for a combination of reasons, with personal attachment to the land playing a leading role.

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[469] McLaughlin, *supra* note 94, at 41–42.

[470] *Id.* at 42–43.

[471] *Id.* at 44–46 (emphasis added).

[472] *See id.* at 41–48.

[473] *See id.* 16–18 (describing acts passed in both 1997 and 2001 that adopted new tax incentives for conservation easement donations—the latest survey cited above was compiled in 1997).

[474] *See, e.g.*, Lydia Saad, *Environmental Concern Holds Firm During Past Year*, Mar. 26, 2007, http://www.gallup.com/poll/26971/Environmental-Concern-Holds-Firm-During-Past-Year.aspx; Dennis Jacobe, *Half the Public Favors the Environment Over Growth*, Mar. 26, 2008, http://www.gallup.com/poll/105715/Half-Public-Favors-Environment-Over-Growth.aspx; Jeffrey M. Jones, *In the U.S., 28% Report Major Changes to Live "Green,"* Apr. 18, 2008, http://www.gallup.com/poll/106624/US-28-Report-Major-Changes-Live-Green.aspx (hereinafter "Gallup Environmental Polls") (all three internet sources last visited Feb. 14, 2009).

C. The Problem with Tax-Driven Clients

While tax-concerned clients may constitute a portion of the market for conservation easements, the vast majority of landowners who pursue this course of action are motivated primarily by their affection for their land.[475] Nonprofit entities that hold conservation easements may prefer to engage in transactions with landowners who are motivated, at least in part, by a legitimate passion to protect their land. Brad Wyche, executive director of an accredited land trust based in Greenville, South Carolina, notes that financial incentives generally should represent the "icing on the cake" and should not be the driving force behind transactions.[476] Easement holders are understandably reluctant to engage in transactions with donors only interested in monetary benefit; such donors may prove difficult to work with if uncommitted to the true conservation purposes of the easement. The relationship between the easement holder and donor is of great importance because of the responsibility and right of the holder to periodically monitor the condition of the land. A donor who abuses the terms of the conservation easement and is unwilling to work with the nonprofit partner to remedy the situation may necessitate an enforcement action. Such legal action is a last resort for nonprofits in the field and represents a burdensome and costly effort.[477] Thus, it is in the best interest of land trusts, and other easement holders, to ensure that easement donors truly are committed to conservation purposes. In practice, a majority of donors are dedicated to the conservation of their land and enjoy mutually beneficial relationships with their nonprofit partners.[478]

D. The Utility of Conservation Easements for Environmental and Conservation Purposes

While the use of conservation easements motivated by tax savings is well-established, several recent Gallup polls indicate a widespread interest in achieving environmental goals. These polls allow an interesting glimpse into current American societal views regarding the environment, revealing

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[475] *See* e-mail interview with Brad Wyche, *supra* note 440 (noting that "[t]he leading motivation for the landowner should always be to protect his or her property, and I think this is true for the vast majority of conservation easements in the country").

[476] *See id.*

[477] *See* McLaughlin, *supra* note 94, at 62–64 (discussing the inherent cost and difficulty in the monitoring and enforcement of conservation easements).

[478] *See id.* at 42–43 (citing 1995 Univ. of Michigan survey finding concern for the "future of the land" and ecological stewardship as the leading motivators for easement donation).

that more than half of Americans value environmental protection over economic growth, more than a quarter of the population reports having made "major changes" in their lives to "go green," and that, for most Americans, the "environment and pollution" represents the "most important problem" facing the United States in the next twenty-five years.[479] While the connection between such general environmental concerns and the donation of easements is arguably attenuated, the public's increased interest in environmental issues likely will translate into increased support for broader land conservation issues. Increased environmental concern may also spur greater numbers of individuals to take personal action to support their "green" commitment. Given the increased prominence of the conservation easement as a land conservation tool, many of these individuals likely will consider granting an easement on their land. Given changing attitudes about the environment, land use, and sustainability, the conservation easement thus may play a still greater role in American society.

While many industries have responded to the new American environmental priority (for example, construction of "green" homes and buildings),[480] it is unclear whether the legal profession has adequately responded to this growing client demand. The conservation easement provides practitioners with a highly effective method of serving the likely increasing pool of clients with a "green" perspective.

V. CONCLUSION

The conservation easement has blazed a unique path. From its odd common law pedigree to its ascension as a preferred mechanism for land conservation and tax planning, there is no other legal concept that claims such a background. Private landowners can make deeply personal, lasting contractual decisions about the conservation of their land without government mandate. The distinctly American appeal of the instrument has only swelled with growing societal appreciation for environmental issues and land conservation. Despite storms of scandal and consistent academic prodding, the conservation easement has fared well. In fact, the conservation easement arguably holds a more powerful position in the American legal landscape than ever before in its meandering history.

As legal counselors to American landowners, attorneys no longer can afford to ignore the conservation easement—especially real property attor-

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[479] *See* Gallup Environmental Polls, *supra* note 474.

[480] *See* Greener Buildings, *Big Jump in Growth, Profits Projected for Green Building Worldwide: Report*, Sep. 21, 2008, http://www.greenerbuildings.com/news/2008/09/22/big-jump-growth-profits-projected-green-building-worldwidereport (last visited Feb. 18, 2009).

neys, who have traditionally ceded this practice area to tax and estate planning attorneys. While the efforts of tax attorneys stimulate intense exploration and employment of the conservation easement for financial reasons, landowners with other personal goals may never get the message. In fact, data suggests that the majority of landowners choose the conservation easement for altruistic purposes, including the simple love of their land or the wildlife that abounds upon it. Real estate attorneys—familiar with land use restrictions and real property law—arguably are best positioned to take advantage of this client segment in an important, expanding field.

Regardless of client motivation, the attorney's role in this context is clear: to tell their clients about the opportunities provided by the law of conservation easements. Only the attorney's affirmative role can ensure American landowners do not forgo this valuable opportunity and instead reach important personal goals.

Finally, the job of the American attorney is built upon a foundation of public service and justice. Incorporating the conservation easement more fully into legal practice wholly supports these pillars of the attorney role. President Theodore Roosevelt understood the value of conservation and the inherent lack of equity involved in the waste of land:

> To waste, to destroy, our natural resources, to skin and exhaust the land instead of using it so as to increase its usefulness, will result in undermining the days of our children the very prosperity which we ought by right to hand down to them amplified . . .[481]

In response to the concerns of both Aldo Leopold and Theodore Roosevelt, let practitioners not fail to grasp a powerful, culturally acceptable tool to help conserve the American landscape. The long term protection of American farms, fields, mountainsides, and coast is in the hands of the private legal practitioner.

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[481] President Theodore Roosevelt, 26th U.S. Pres., Seventh State of the Union Address (December 12, 1907), *available at* www.thodoreroosevelt.com/sofu.html.