

What You Should Know About Conservation Easements (With Form)

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Conservation easements can offer significant tax advantages – if you structure them correctly.

A CONSERVATION EASEMENT in real property may be created by dedicating the right to use all or a portion of that property to a governmental entity or to a charitable or educational association, corporation, trust, or other tax-exempt entity. See, e.g., Mich. Comp. Laws §324.2141. A conservation easement is defined as follows:

"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, archeological or cultural aspects of real property."

Thomas Grier, Comment, *Conservation Easements: Michigan's Preservations Tool of the 1990s*, 68 U. Det. Mercy L. Rev. 193, 194 (1991) (quoting Uniform Conservation Easement Act §1(1), 12 U.L.A. 174 (1981)).

A conservation easement is a perpetual negative easement in gross. See, e.g., *United States v Blackman*, 613 S.E.2d 442 (Va. 2005). A "negative easement"

prohibits the owner of the servient estate from doing something otherwise lawful on his or her property. 550 *Black's Law Dictionary* 587 (9th ed. 2009). An "easement in gross" is an easement benefiting a particular person and not a particular piece of land. *Id.* at 586.

More simply defined, a conservation easement is a transfer of an interest in land whereby "[t]he landowner retains fee ownership, but conveys certain specified rights to a land conservation organization or a public body to prevent development of the land" forever. John D. Noonan, *Conservation Easements in Northern Michigan*, 70 Mich. B. J. (May, 1991). It creates a continuing restriction on the property that is enforceable against all future owners when granted to one of the entities listed above. *Id.* at 423. *See also* Jonathan L. Hafetz, *Fostering Protection of the Marine Environment and Economic Development: Article 121(3) of the Third Law of the Sea Convention*, 15 Am. U. Int'l L. Rev. 583, 635 (2000). A conservation easement may be created by reservation as well as by grant. *Madden v Nature Conservancy*, 823 F. Supp. 815 (D. Mont. 1992).

1. Tax Benefits Available For A Conservation Easement

A conservation easement may serve to reduce real property and estate taxes on the dedicated property. In addition, if a conservation easement over land is donated to a qualified organization, the existence of this conservation easement may entitle the grantor to deduct the value of the donated rights (i.e., the loss in the real property's value caused by the conservation easement) from the grantor's federal income taxes. Aside from the intrinsic appeal of conservation, these are among the reasons conservation easement grants are being used with increasing frequency.

a. Real Property Tax Reduction. A landowner who donates a conservation easement to a qualified organization may be eligible to receive property tax relief on the property burdened by the conservation easement. *See* Michigan Tax Tribunal, MTT Docket No. 157543, 205036 (February 17, 1995) (MTT); Grier at 207 (citing Daniel C. Stockford, Comment, *Property Tax Assessment of Conservation Easements*, 17 B.C. Env'tl. Aff. L. Rev. 823, 830-832 (1990)). *See also* Jessica Owley Lippmann, *The Emergence of Exacted Conservation Easements*, 84 Neb. L. Rev. 1043, 1099 (2006). The notion is that prohibiting development on the dedicated land by means of a conservation easement devalues the fair market value of the property even though it may still remain privately owned. *Id.*; George P. Smith II and Michael W. Sweeney, *The Public Trust Doctrine and Natural Law: Emanations Within a Penumbra*, 33 17 B.C. Env'tl. Aff. L. Rev. 307, 331 (2006). For example, the Michigan Tax Tribunal has addressed determination of the tax savings attributable to a parcel of property that is subject to a conservation easement. On February 17, 1995, the Tax Tribunal declared that this type of "restrictive easement does affect value [when] created in accordance with State and Federal law with the express intent of placing permanent

limitations upon the property that negatively affect the market value." MTT at 11. Thus, it adopted the "Before and After" market test to determine the fair market value for property tax purposes of land burdened by a conservation easement. *Id.* The "Before and After" market test is a formula borrowed from the Internal Revenue Code (Code). To determine the value of a conservation easement for property tax purposes, the formula works as follows: the Before Value minus the Difference equals the After Value of the property (BV-D=AV). *Id.* at 5. (see Internal Revenue Service (IRS) Revenue Ruling 73-339 and Treas. Reg. §1-170A-14(h)(3)(iii) for a more detailed explanation of this formula). The Before Value is the true cash value of the highest and best use of the property as though the conservation easement had not been granted. *Id.* The After Value is the true cash value of the highest and best use of the property after the conservation easement has been granted. *Id.*

A number of states have adopted legislation establishing specific tax credits for conservation easements. Among them are:

- California. Cal. Public Resource Code §§37000-37042;
- Connecticut. Conn. Gen. Stat. §12-217dd;
- Delaware. Del. Code Ann. tit. 30, §§1801-1807; tit. 7, §§6901-6905;
- Georgia. Ga. Code Ann. §48-7-29.12;
- Maryland. Md. Code Ann Tax-Gen. §10-723;
- Mississippi. Miss. Code Ann. §27-7-22.21;
- New Mexico. N.M. Stat. §§75-9-1 through 6, §7-2-18.10; N.M. Code R. §3.13.20.1 et seq.;
- New York. N.Y. Tax Law §606(kk);
- North Carolina. N.C. Gen. Stat. §105-151.12 and §105-130.34;
- South Carolina. S.C. Code Ann. §12-6-3515
- Virginia. Va. Code Ann. §§58.1-510 through 513.

These statutes are cited in William Sylvester, Benton Williamson, and David Callies, *The Current Status, At The Beginning of 2010, of Land Conservation Issues*, the ACREL Papers at 141 (Spring 2010) (Sylvester, Williamson, and Callies).

Property owners should nevertheless proceed with caution. A conservation easement may enhance the value of the surrounding land. Howard Meyerson, *Nature Planning New Director Helps Group Tackle Challenge of Conserving Lands*, Grand Rapids Press (July 31, 1993). The benefit received by a property tax reduction attributable to the decreased true cash value of the burdened property may be lost by the increased true cash value of the abutting properties if this property is also owned by the grantor. Note however, that under Michigan law, until there is a "transfer of ownership," Public Act No. 415 may not permit an uncapping of the "taxable value" to reflect the increase in the surrounding parcels' true

cash value. Mich. Com. Laws §211.27a(6). Some states have imposed similar property tax caps; many have not.

b. Tax Deduction. Much of the form of a conservation easement is dictated by the requirements of the Code for obtaining a charitable deduction from federal income taxes in connection with the donation of a conservation easement. Noonan, *supra*, at 427; Lippmann, *supra*, at 1091. Note that there have been several Congressional attempts to eliminate this tax deduction due to abuse. Section 170(b)(1)(E) of the Code permits federal taxpayers to deduct the value of qualified conservation contributions to the extent the aggregate of such contributions does not exceed the excess of 50 percent of the taxpayer's adjusted gross income over the amount of his or her other allowable charitable contributions. Any excess may be spread over the 15 succeeding years.

To be eligible for this tax deduction, the Code provides that the conservation easement must be a "qualified conservation contribution." The Code permits a deduction under Code section 170(f)(3)(B)(iii) and (h) for contributions of certain partial interests in real property for conservation purposes if three requirements are met:

- The property contributed must be a "qualified real property interest;"
- The property must be donated to a "qualified organization";
- The gift must be "exclusively for conservation purposes."

A "qualified real property interest" includes a perpetual conservation restriction, which may take the form of an easement, restrictive covenants, or equitable servitudes. Tax Management Portfolio vol. 521-3rd at A-78; (Reg. §1.170A-14(b)(2)). The conservation easement must be given to an organization that is eligible to receive qualified conservation contributions. The Code indicates that a section 501(c)(3) charitable organization is such a qualified organization, as are governmental units and other eleemosynary organizations. Code §170(h)(3). The regulations further provide that, in addition to being a qualified organization, the charitable organization "must have a commitment to protect the conservation purposes of the donation." Tax Management Portfolio vol. 521-3rd A-79 (citing Reg. §1.170A-14(c)(1)). "The necessary commitment is deemed to be present if the donee [the charitable organization] is organized or operated primarily or substantially for a conservation purpose," and has adequate resources to enforce the restrictions in the conservation easement. Tax Management Portfolio vol. 521-3rd A-79 (citing Reg. §1.170A-14(c)(1)).

The third requirement under the Code mandates that the qualified conservation contribution be made for one or more of the following permitted "conservation purposes":