

Conservation Tax Incentives Fact Sheet (courtesy Land Trust Alliance)

Adjusted Deduction for Conservation Easement Donations Will Help Farmers and Ranchers

Section 1206 of the pensions bill (HR 4) recently passed by Congress will help family farmers, ranchers, and other moderate-income landowners get a significant tax benefit for making the extraordinarily valuable donation of a conservation easement, restricting future development of their land to protect a resource important to the public. Most such donations are made to local, community-based charities dedicated to keeping land in agriculture, conserving important wildlife habitats, and protecting important open space and historic resources. This proposal will:

- Raise the maximum deduction a donor can take for donating a conservation easement from 30% of their adjusted gross income (AGI) in any year to 50%;
- Allow qualifying farmers and ranchers to deduct up to 100% of their AGI; and
- Increase the number of years over which a donor can take deductions from 6 years to 16 years.

This provision would be effective for donations made from January 1, 2006 through December 31, 2007. After that, the law would revert back to previous provisions, unless Congress extend the provision prior to the deadline.

Conservation Incentive Combined with Solid Tax Reforms

Section 1219 of the bill sets higher standards for appraisers and appraisals of all donated property, and sets higher penalties for abusive appraisals. Conservationists support this to ensure the integrity of the charitable donation process. Section 1213 tightens restrictions on donations of easements to protect historic buildings.

Questions and Answers About the New Tax Incentive

The Congress has just approved a significant expansion of the federal tax incentive for conservation easement donations, along with several reasonable reforms to help prevent abuse of that incentive.

Below we have tried to answer the most commonly asked questions.

A. Expanded Tax Incentive

1. How does the bill change the current tax incentive for conservation donations?

The new law:

- Raises the deduction a donor can take for donating a conservation easement from 30% of their adjusted gross income in any year to 50%;
- Allows qualifying farmers and ranchers to deduct up to 100% of their income; and

- Increases the number of years over which a donor can take deductions from 6 years to 16 years.

2. Can you give me an example?

Under the previous rules, a landowner earning \$50,000 a year who donated a \$1 million conservation easement could take a \$15,000 deduction for the year of the donation and for an additional 5 years – a total of \$90,000 in tax deductions.

The new rules allow that landowner to deduct \$25,000 for the year of the donation and then for an additional 15 years. That's \$400,000 in deductions. If the landowner qualifies as a farmer or rancher, they can zero out their taxes. In that case, they could take a maximum of \$800,000 in deductions for their million dollar gift.

3. Can anyone deduct more than the value of their gift?

One can never deduct more than the fair market value of the gift. This change simply allows landowners who previously could not deduct the full value of their gift to deduct more of that value.

4. Who qualifies as a farmer or rancher?

The new law defines a farmer or rancher as someone who receives more than 50% of their income from “the trade or business of farming”. The law references an estate tax provision (Internal Revenue Code (IRC) 2032A(e)(5)) to define activities that count as farming. Specifically, those activities include:

- cultivating the soil or raising or harvesting any agricultural or horticultural commodity (including the raising, shearing, feeding, caring for, training, and management of animals) on a farm;
- 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
- the planting, cultivating, caring for, or cutting of trees, or the preparation (other than milling) of trees for market.

The qualified farmer or rancher provision also applies to farmers who are organized as C corporations. For an easement to qualify for the special treatment, it must contain a restriction requiring that the land remain “available for agriculture”.

5. Do these changes apply to gifts of land?

This expanded incentive applies to the various specific gifts of partial interests in land specified as a “qualified real property interest” under IRC 170(h)(2). A landowner who is considering a gift of their entire interest in a piece of land

should consult with an attorney to determine whether he or she may be able to utilize this new incentive.

6. Does this only apply to conservation easements?

The expanded incentive applies to all donations covered in IRC section 170(h)(2), which includes donations of the entire interest of the donor other than a qualified mineral interest; a remainder interest; or a permanent conservation or historic preservation easement.

7. What is the timeline for this expanded incentive?

The new law applies to all easements donated in 2006 and 2007.

LTA will work hard to make this change permanent -- but as it stands it will expire at the end of 2007. If a donor qualifies under this provision, they can continue to apply its formulas to the amount of their contribution that they carry over into years beyond 2007.

8. What other restrictions apply?

Conservation easement donations are subject to the same restrictions as they were before. For example, easements must meet the “conservation purposes” test defined in the existing law; they cannot be donated as part of a “quid pro quo” agreement; and they must be donated to a qualified organization – a governmental unit or a publicly-supported charity that has “a commitment to protect the conservation purposes of the donation, and ..the resources to enforce the restrictions.”

Learn more about Treasury Regulations on conservation easement donations.

9. Will donors who use this provision be audited?

Taking advantage of this new law will not necessarily affect one's likelihood of being audited. All donors should note, however, that the IRS has been increasing the number of tax returns it audits – the number has doubled in the last two years. The IRS has also indicated that high value donations of property – including donations of conservation easements -- will receive more attention from the IRS than most tax returns.

That makes it particularly important for a donor to know and follow the law, and utilize a reputable, professional appraiser who has experience in the appraisal of conservation easements.

B. Reforms to the Rules for Easement Donors

1. How does the new law prevent abuse?

Under the new law, the definitions of substantial and gross misstatements of value have been changed. Previously, a taxpayer whose donation was finally determined to be worth \$200,000 would have been guilty of a substantial misstatement if they had claimed a value of \$400,000, and guilty of a gross misstatement if they had claimed a value of \$800,000. Now, they would be guilty of a substantial misstatement for claiming a value of \$300,000, and of a gross misstatement if they claimed a value of \$400,000. There are substantial additional tax penalties for such misstatements for the taxpayer, and they make the appraiser subject to penalties of up to 125% of their fee plus potential disbarment from working on federal tax matters.

The law also redefines who is a “qualified appraiser”, and gives the IRS the power to issue new regulations on appraiser qualifications. This is important: as of the date of enactment of this law, appraisers will need to show donors that they are qualified under the new law and any new Treasury regulations or guidance that may follow from it. Lastly, the law states that a qualified appraiser must “demonstrate verifiable education and experience in valuing the type of property subject to the appraisal.”

These new rules apply not just to conservation easements, but to all charitable donations of property.

2. Will this make appraisals more expensive?

It is possible that appraisals for conservation easements will be marginally more expensive. But these reforms are important steps towards ensuring that appraisals accurately reflect the value of charitable gifts.

3. How does the new law affect easements that protect both conservation and historic preservation values?

The new law tightens the rules for easements on “certified historic structures.” If you are protecting a property that includes such a structure (e.g. a farm with a historic stone barn that is listed in the National Register) these new regulations may apply to you. Donors and donees of easements protecting historic structures need to understand the new rules, which include a filing fee for donors and specific appraisal requirements.

Some of the new rules apply to historic structure easements donated as early as July 25, 2006. Any donor who has donated a historic preservation easement since that date should be made aware of the new rules.

4. What about land with historic value, like battlefields and Native American burial grounds?

There is no change in the law for easements covering battlefields or other land with historic value. IRC 170(h)(4)(A)(iv) distinguishes between “historically important land areas” and “certified historic structures”. Only easements protecting the latter should be affected by the new law.

5. What is the timeline for the reforms?

The new law applies to all donations made after the date of enactment of this new law. The law makes these reforms permanent. As noted above, sections of the legislation applying to historic preservation easements are retroactive and apply to easements donated since July 25, 2005.

6. Have there been other changes besides this tax bill?

Yes! The IRS has changed the instructions for Form 8283, and now asks for additional information from easement donors. In addition, the IRS has revised Form 990 – the tax return all charities complete. The IRS has also changed Form 1023, the application for nonprofit status, and in 2004 issued a cautionary notice regarding conservation donations ([Notice 2004-41](#)).

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