

## **GUIDE TO AGRICULTURAL CONSERVATION EASEMENTS**

Agricultural conservation easements can help protect farming and ranching as a way of life and also be an effective and practical planning tool that benefits the farm or ranch, as well as the bottom line. The land, business, estate and financial planning should all be considered. This process can be an integral step in succession planning.

An agricultural conservation easement is a voluntary agreement between a landowner and a land trust, such as The Land Conservancy of San Luis Obispo County (LCSLO), or a public agency to permanently protect a property's agricultural values by allowing for continued farming or ranching while limiting future development and other harmful uses. Easements "run with the land" meaning they remain in place even after the property changes ownership.

Below are some frequently asked questions:

### **How does a conservation easement affect property rights and value?**

Landowners still hold title to their property and the rights of ownership, such as the right to sell the property, lease the land, leave it to their heirs, the right to privacy; in addition, property also has other rights such as the right to harvest timber and minerals, use and divert water, till the earth, raise livestock or subdivide and develop. A conservation easement will restrict some of these property rights, while retaining agricultural uses.

By restricting certain property rights, conservation easements may reduce the value of the property. This can help a family pass land to the next generation without subdividing and/or developing it to pay the inheritance taxes. This is particularly important in agricultural areas facing the conversion of agricultural lands to urban uses.

### **Does the easement have value and how is it determined?**

The easement restricts certain property rights, and the value of the conservation easement is the difference between the value of the highest market value for the property before the easement, and the market value of the property after the easement is in place. This is called the "before and after" approach to valuation; the "after" value typically reflects the property's restricted value. A qualified, credentialed appraisal is always used to determine the easement value.

The value of the easement may be donated or if funding is available, all or a portion (bargain sale) may be purchased by LCSLO through funding from public or private grants. Funding for easements is very limited and must be compatible to the landowner's uses and goals for the property. If some or all of the easement value is purchased, it may take several months to a few years for LCSLO to locate and obtain the funding, and there is no guarantee that grant funds can be located. Donated easements have income tax benefits that are discussed on the following page.

**Does a conservation easement cover the entire property?**

In most cases the conservation easement covers the entire property, but a landowner can exclude specific areas.

**Do landowners need an attorney to place a conservation easement on their property?**

Placing a conservation easement on your property can have significant land use, income tax and estate planning consequences. It is the policy of LCSLO to require landowners to have qualified legal counsel before completing a transaction to assist in the decision making process and review of legal documents.

**What are the tax implications for a landowner placing a conservation easement on their property?**

It is important for the landowner to secure the advice of a qualified tax advisor to obtain information regarding the specific tax consequences for either the donation or sale of an easement.

Estate Tax: Conservation easements may help reduce estate taxes by excluding the easement value from the taxable value of the estate. This can help a family pass land to the next generation without having to sell, subdivide or develop their family's land to pay for the estate taxes. The Federal Taxpayers Relief Act of 1997 allows beneficiaries to exclude from the taxable estate 40% of the value of land for qualifying conservation easements subject to limits. This is in addition to the reduction in the value of the land resulting from the easement itself.

Income Tax: The landowner may be able to take a Federal income tax deduction if the easement is permanent and donated as a bona fide charitable contribution.

Property Tax: The property taxes could be significantly lowered once the easement is placed on the property, however if the landowner's basis in the property is lower than the easement value, there may be no property tax reduction realized. In some cases, depending on the circumstances, the assessor has not lowered property taxes, and therefore no guarantee is offered. It is always best to speak directly to the county tax assessor regarding your situation.

**Capital Gains Tax:** Selling an easement is considered as a sale of a capital asset and is treated as capital gain to the extent that the proceeds exceed the basis in the property. The sale of an easement may qualify for a 1031 “in-kind” exchange to defer capital gains taxes while allowing the property owner to acquire additional property. It is strongly recommended that an attorney experienced in 1031 exchanges is consulted if considering this method of tax deferral of capital gains.

The Land Conservancy of San Luis Obispo County strongly urges all landowners to seek out their own counsel on tax and legal issues.

**Does a conservation easement affect borrowing power?**

Not necessarily. The easement itself does not restrict use of the property as collateral for borrowing; and the property may still have significant value even with a conservation easement.

**Is a mortgage affected by a conservation easement?**

Yes, any mortgage or deed of trust or other monetary lien on the property must be either discharged prior to the easement or subordinated to the easement. In the case of subordination it is advisable to talk to your lender well in advance of placing an easement on the property to determine what, if any, requirements they may have.

**How is the amount of the easement project and stewardship funding determined?**

A conservation easement is a perpetual obligation and responsibility, and it is important that funds are available to LCSLO to ensure the conservation easement is upheld. Funding is a necessity for the monitoring and enforcement of easements along with the related easement project costs.

LCSLO generally requests a donation for each conservation easement it acquires. The amount can vary, but it is usually 3% of the easement value for purchased easements, and a minimum of \$10,000 for donated easements.

**How long will the conservation easement process take?**

It depends on whether the easement that is contemplated is being donated or sold. Locating and obtaining funding may be a several year process. Donating an easement still requires appropriate time to negotiate the easement, secure an appraisal, title documents, prepare a baseline conditions report and obtain legal review.

**What are the associated costs to a conservation easement?**

Potential costs are all or part of the appraisal costs, stewardship endowment donation, and attorney fees for the legal review.

### **How is the conservation easement monitored?**

LCSLO visits each of its easement-protected properties at least once each year with the landowner. These planned visits provide an opportunity to exchange information, to answer questions about the easement, and to compare the condition of the property with the baseline conditions report.

### **What is the next step?**

LCSLO staff will visit the property with the landowner to discuss the potential conservation easement, evaluate the property, and then prepare a report to be presented to the Board of Trustees. Upon approval of the project by the Board of Trustees, LCSLO will send an approval letter to the landowner outlining the process.