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# Tax Break With a View

## Landowners Rush to Take Advantage of New Law That Boosts Deductions for Blocking Development; a Crackdown on Abuse

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Muscoe R.H. Garnett Jr.'s farm in Loretto, Va., hasn't changed much since the family acquired it in the 1600s. Now, the retired insurance executive has made sure it will stay that way.

Encouraged by recent tax legislation, Mr. Garnett has placed a "conservation easement" on much of his property, located about 80 miles from Washington, D.C. The move permanently shields the rolling pastures, timber forests and croplands from being turned into a housing subdivision or business park. Under the easement, which is a binding agreement typically made with a land trust, the Garnett family still owns the land and can continue to use it for farming and timber but most of it can never be developed.

Landowners who place conservation easements on their scenic, environmentally sensitive or historic properties have long been able to get tax breaks from the federal government, and some states have also begun offering tax incentives. Now, a little-noticed provision in the wide-ranging pension law Congress passed last summer has made the federal tax breaks even more generous. Conservation groups say this has spurred a sharp increase in the number of landowners interested in placing easements on their property.

"The incentives are fantastic, and I don't think a lot of people realize it," Mr. Garnett says.

But the expanded federal incentives, backed by some influential lawmakers from agricultural states, are due to expire at the end of this year, unless Congress acts to extend them. (A bill recently introduced in the Senate would make the changes permanent, and President Bush also called for them to be made permanent in this week's budget proposal.) For now, landowners might need to act quickly, since conservation easements can take several months to put together.

Here's how it works: A landowner typically donates a conservation easement to a land trust, a type of non-profit organization that helps put together the easement and monitors its restrictions over time. The value of the donation for income-tax purposes generally is the difference between the land's unrestricted value and its new value with limited development or usage rights.

Be careful, though. The Internal Revenue Service and Congress in recent years have been concerned with easement abuses in which donors have taken inflated deductions or placed restrictions on land with little conservation value, such as golf courses. The new law includes stiffer rules and penalties regarding appraisals, to prevent donors from overstating the deduction for their land. The IRS says it is currently auditing hundreds of easements.

But the law is designed to encourage easement donations by allowing larger tax deductions. Landowners can now deduct the value of a donation up to 50% of their adjusted gross income per year, up from the previous ceiling of 30%. That means if your adjusted gross income is $100,000, you are now eligible for as much as a $50,000 tax deduction a year, instead of $30,000. And if your income is too low to deduct the full amount of your gift in one year, you can now carry forward the deduction for 15 additional years, up from five years previously.

Property held in family limited partnerships, limited liability companies and some types of corporations may also be able to take advantage of the increased deduction limits, says Stephen J. Small, a Boston tax lawyer who specializes in conservation easements.

The law is even more generous for career farmers and ranchers who earn at least half their income from their land. These property owners, who are often land-rich, but cash-poor, can now deduct up to 100% of their income. "If you're a farmer you could pay no federal income taxes for 16 years," says Rand Wentworth, president of the Land Trust Alliance, a coalition of 1,600 land trusts across the country.

Colorado rancher Jay Fetcher in recent years placed conservation easements on two large parcels of his 2,000-acre cattle ranch near ski resort Steamboat Springs. The first donation, on 1,350 acres, was worth about $1.1 million for tax purposes. But Mr. Fetcher, limited at the time to deducting a small portion of his income, was able to take only about $60,000 of that donation in deductions over six years. "We left almost all of the donation on the table," he says.

Mr. Fetcher is planning this year to make another easement donation on 270 acres to a Colorado land trust. He expects the value of the donation will be about $1.2 million, and thinks he will be able to recoup roughly half that amount because of the higher federal tax deductions and an increase in state tax credits. "The changes helped us," says Mr. Fetcher. Still, he says the financial incentives are secondary to his desire to preserve the land, in his family since 1949, with its sweeping views of mountains and pine forest. "Our family has no desire to ever see the ranch developed. That's at the beginning of it all," says Mr. Fetcher.

The tax-rule change has generated sharply increased interest in conservation easements, say land trust officials from Washington and Wyoming to Georgia. "Some landowners whom we've been talking to for five or almost 10 years say that now it makes economic sense for them," says Laurie Wayburn, president of the Pacific Forest Trust in San Francisco.

Conservation easements can generate other tax benefits, too. They can cut estate taxes, because the land is considered to be worth less under an easement. A growing number of states offer a range of income tax breaks. Colorado and Virginia, for example, give donors state income tax credits that are transferable, which means that landowners who don't need the tax credits can sell the credits to other taxpayers for instant cash. You may even get a property tax break, depending on where you live.

Conservation easements can vary. A farm owner, for instance, could still retain the right to farm the land and to build a couple additional homes or barns, but could limit the land from being further subdivided. Property owners can sell their land, but buyers are obligated to honor the easement.

Peter Bance recently placed a conservation easement on 65 acres of the Virginia farmland that has been in his family since 1840. The property was zoned to allow construction of six housing sites, and he donated the rights to five of those sites to a state-run land trust. (He kept one site in case a descendant wanted to build a house in the future.) "We think we have a piece of heaven and we hope to keep it that way for generations to come," says Mr. Bance, 55, who is an executive with Wachovia Corp.

If you're thinking of doing a conservation easement, it's best to contact a land trust in your area to find out if your property qualifies. (Try www.lta.org, the Web site of the Land Trust Alliance.) There's no minimum size, but in order to get a tax deduction the property has to meet certain criteria, such as having significant environmental, scenic or historic value. Also, be sure to work with a tax and legal adviser familiar with local applicable laws.

The land has to be appraised (try www.appraisers.org, the Web site of the American Society of Appraisers) and may need to be surveyed, which can cost a few thousand dollars. There are also legal fees to draw up the easement, which can cost several thousand dollars, depending on the complexity of the deal. Some land trusts also recommend landowners make cash donations to the land trust to help fund the organization's future monitoring of the easement.

Because easements are placed in perpetuity, a family has to be sure it wants to permanently restrict development -- and the potential for a big windfall -- before committing.

Several months ago, after discussions with his wife, children and grandchildren, Eslick Daniel placed a conservation easement on his 200-acre farm in Columbia, Tenn., near Nashville. The easement on the farm, called "Sweet Easy," limits development, except for a couple of building sites that Dr. Daniel's descendants could use for housing. For Dr. Daniel, 65 years old and a retired orthopedic surgeon, the tax incentives weren't a factor. "We wanted to keep it where it would be open land for our family and for other people," he says.

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