

TAX BENEFITS OF CONSERVATION EASEMENTS

The gift of an open-space easement in perpetuity to the Virginia Outdoors Foundation (VOF) may qualify as a non-cash charitable gift, providing the donor with various tax benefits. A donor applying for tax benefits must retain an independent certified appraiser to establish the value of the easement, which value is primarily based on the value of the development rights relinquished. Once that value is established, it becomes the basis for calculating tax benefits.

Federal Income Tax Deduction. Donations of open-space easements that meet federal tax code requirements may entitle the donor to federal income tax deductions. For tax year 2022 and thereafter, the deduction is limited to 50% of adjusted gross income, which if not used up in 2022, may be carried forward at 50% of adjusted gross income for an additional fifteen years or until the donation is fully expended, whichever comes first. In addition, a farmer or rancher who receives in 2021 or thereafter more than 50% of adjusted gross income from the trade or business of farming or ranching is eligible for a tax deduction of 100% of adjusted gross income with the same carry forward right. IRS Form 8283 must be filed to obtain this deduction. Form 8283 requires attachment of a copy of the appraisal, an appraiser's declaration, VOF's acknowledgement of the gift, copies of the deed as recorded and the baseline documentation report. The full appraisal will have to be shared with VOF when Form 8283 is submitted to VOF for its signature.

*Certain federal court cases raise serious questions as to (1) whether an easement provision that allows substitution of property not under easement for property initially placed under easement or (2) whether an easement that does not provide for building envelopes or that allows for movement of building envelopes on the property ("floating" building envelopes) meets the requirements of the Internal Revenue Code and allows the federal deduction for the contribution of a conservation or open-space easement. There are conflicting court opinions amongst recent cases, and the issue has not yet been addressed by the Fourth Circuit Court of Appeals covering conservation easements granted in Virginia. See in particular *Bosque Canyon Ranch II, L. P. v. Commissioner*, 867 F. 3d 547 (5th Cir. 2017), *Pine Mountain Preserve, LLLP v. Commissioner* 151 T. C. 14 (2018), and *Pine Mountain Preserve, LLLP v. Commissioner*, No. 19-11795 (11th Cir. 2020) overruling the 2018 tax court decision. Check with an attorney about whether to provide for building envelopes in an easement.*

Reduction in Federal Charitable Deduction: Treasury Regulations, effective August 28, 2018, reduce the federal charitable deductions for gifts of qualifying open-space or conservation easements by the amount of the land preservation tax credit (40% of the easement value). For example, if a landowner gives VOF an open-space easement with an easement value of \$500,000, the state tax credit would be \$200,000 and the federal deduction would be reduced from \$500,000 to \$300,000.

Federal Estate Tax Reduction and Exclusion.

- a. Extinguishing some or all of the development rights for a parcel of land through a conservation easement may substantially reduce the value of the land for estate tax purposes, thus reducing estate taxes.
- b. In addition, Section 2031(c) of the Internal Revenue Code provides an estate tax exclusion from the gross estate of up to 40% of the easement-encumbered value of the land protected by a qualified conservation easement. The exclusion is capped at \$500,000 and is reduced if the conservation easement reduced the land's value by less than 30% at the time of the contribution. To qualify the easement must prohibit all but "de minimis commercial recreational use" of the property, and a number of other requirements must be met. Consult your tax advisor about this exclusion.

Virginia Land Preservation State Tax Credit. A Virginia land preservation state tax credit has been established for conservation easements at 40% of the value of the easement. The amount of the credit claimed by a taxpayer, including amounts carried over from prior taxable years, may not exceed \$20,000 for taxable year 2022, but you may carry over any unused credit for a maximum of 10 consecutive taxable years following the taxable year in which the credit originated. For each taxpayer, in any one taxable year, the credit used may not exceed the amount of income tax otherwise due. In addition, any unexpended portion may be transferred to another Virginia taxpayer. A recent tax court opinion suggests that the income from the sale of tax credits held for more than one year prior to sale may receive more favorable long-term capital gains treatment. (Check with your tax advisor or attorney to determine whether and when tax credits should be sold.) Tax credits of \$1 million or more will be issued only if the conservation value of the donation has been verified by the Director of the Department of Conservation and Recreation (DCR) based on criteria adopted by the Virginia Land Conservation Foundation. Pre-filing review of the conservation value is available through DCR. There is a \$75 million limit on the amount of tax credits that the Department of Taxation may issue in each calendar year. Form LPC-1 must be filed with the Department of Taxation for registration of credits and Form LPC-2 for transfer of credits. **Timing of tax credit application: For the conveyance of a conservation easement made on or after January 1, 2020, no credit shall be allowed unless a complete application for tax credit has been filed with the Department of Taxation by December 31 of the second year following the calendar year of the conveyance.**

Local Property Taxes. Local property taxes may be reduced with respect to land (but not dwellings, farm buildings, or other improvements on the land). However, if land is already assessed at “use value”, for example, enrolled in a locality’s land-use assessment taxation program, an additional reduction in taxes is unlikely.

VOF provides this information about tax benefits to assist landowners, but not as tax advice. Please check with your tax advisor or attorney about qualifying for any tax benefits associated with conservation easements.