

Conservation Easements

Conservation Basics & Income and Estate Tax Benefits

Saving Family Lands 2019

WE ARE ADVOCATES FOR YOU AND YOUR LAND



Three companies, same mission.



Protecting and
preserving
private, rural
land.



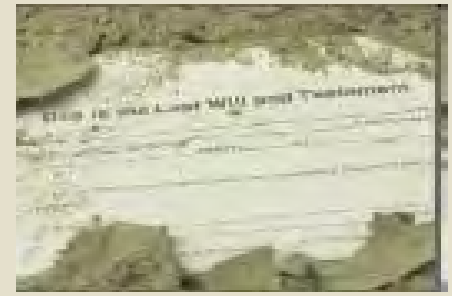
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Estate Planning for Legacy Land



Your goals should guide the planning process.

Estate Planning - A Layman's Definition



Proper Estate Planning Allows Us To:

- 1. PROTECT our property;**
- 2. PROVIDE for ourselves & our loved ones without giving up control of our affairs;**
- 3. PLAN for the possibility of our own disability;**
- 4. GIVE what we own to who we want, the way we want them to receive it, and when we want them to receive it;**
- 5. SAVE every tax dollar, professional fee and court cost that are legally possible to save.**

Why Would Someone Reduce the Market Value of Their Land?

- To unlock the value that is attributable to the development rights they do not intend to use
- To reduce taxes



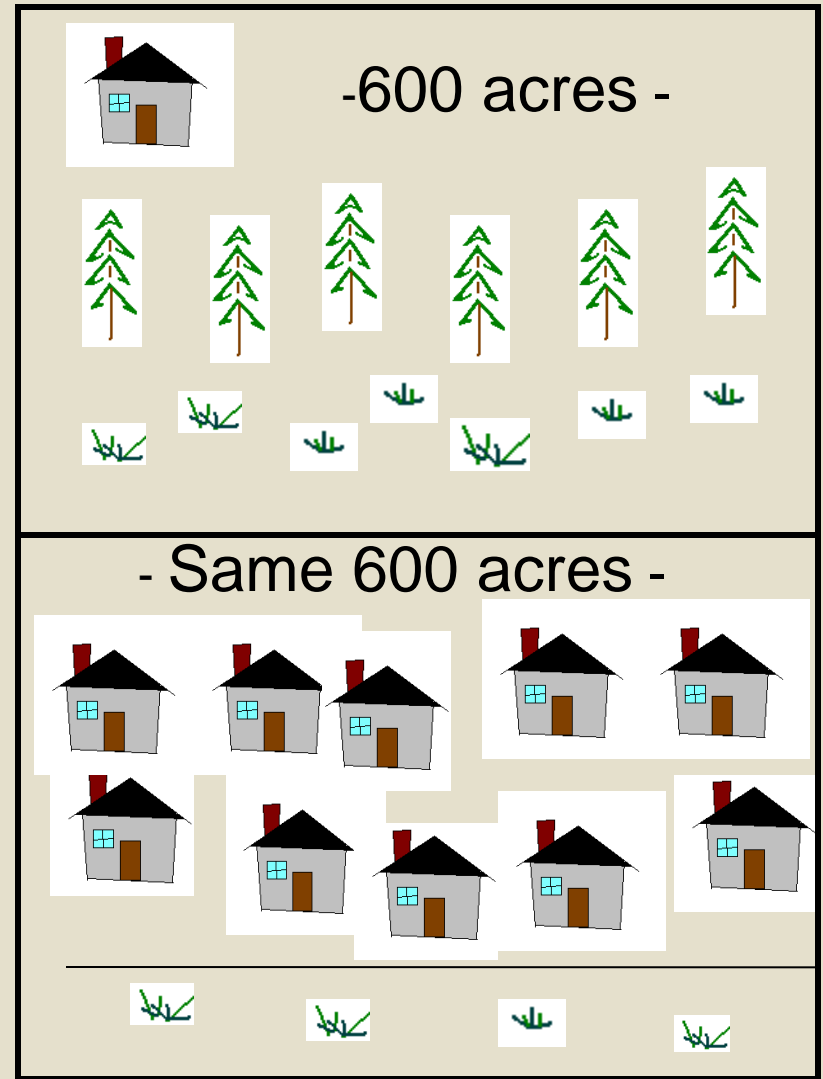
“Development Value” is Unused

1975 - \$300,000 (\$500/ac)

- 70% recreation or agriculture value

2019 - \$7,200,000
(\$12,000/ac)

- 70% potential unused
“development” value

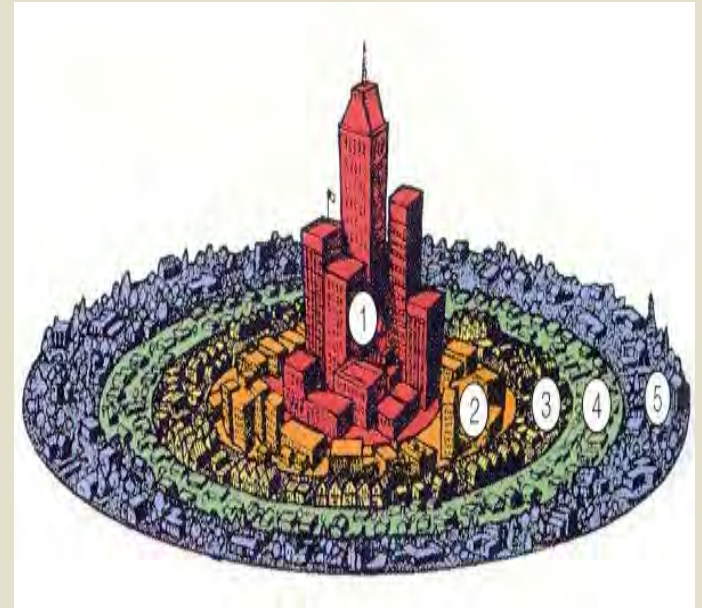


Valuation

RULE OF THUMB -- How CE Impacts Land Value:

Near cities reduction/deduction can be 50-90% of land's appraised value

Rural land reduction/deduction can be 30-60% of land's appraised value



CE Financial Benefits



- Donation of CE = FIT tax savings
- Sale of CE = cash
- Bargain sale = \$ + tax savings
- Estate tax savings = smaller estate
- Phasing in CE over multiple tax years
- Tax Credits in certain states (CO)

Estate Planning 101: Federal Estate Tax



2019

- FET exemption = \$11,400,000/ person
- Deceased spouse's assets pass to the surviving spouse outright or in qualified trust without FET
- Deceased spouse's unused FET exemption can be transferred to the surviving spouse
- FET exemption on the second death is \$22,800,000

Change in Focus: Federal Income Tax Planning



New exemption/credit addresses the FET threat for many families

Strategy: maximize charitable deduction for Federal Income Tax Savings

Income Tax Savings 2019 - 2034

Donor's AGI	\$ 250,000
Tax Rate	24%
Value of CE (69% FMV)	\$ 5,000,000
Max. Annual Deduction (<u>50%</u> AGI)	\$ 125,000
Annual Tax Savings (22% tax rate)	\$ 30,000
Number Years to Use Deduction	16

TOTAL TAX SAVINGS	\$ 480,000
Unused Deduction \$3M	

Income Tax Savings

Qualified Farmer or Rancher

Donor's AGI	\$ 250,000
Tax Rate	24%
Value of CE (69% FMV)	\$ 5,000,000
Max. Annual Deduction (<u>100%</u> AGI)	\$ 250,000
Annual Tax Savings	\$ 60,000
16 Years to Use Deduction	

TOTAL TAX SAVINGS	\$ 960,000
Unused Deduction \$1M	

Using the Business Entity

- Mom and Dad Landowner form Family Ranch, LLC and transfer the rural land to the LLC
- Mom and Dad, as LLC members, gift 48% of their member interest to their two children
- The gift will create a gift tax event, subject to the gift tax unified credit (but \$11,400,000 is available)
- The children, as members of LLC, share in the charitable deduction for the CE donation

Results

- Each member can claim part of the donation of the CE on their tax returns.
- Mom and Dad - \$250,000 annual income. As owners of 52% of the LLC, they get \$2.6M of the deduction and use \$2M of it. *\$600,000 is unused.*
- Child 1 - \$400,000 annual income. As an owner of 24% of the LLC, she gets \$1.2M of the deduction and uses all of it in 6 years.
- Child 2 - \$170,000 annual income. As an owner of 24% of the LLC, he gets \$1.2M of the deduction and uses all of it in 15 years.

Land Owned by a Trust

IRS disallows the charitable deduction for an irrev. trust unless the donation is a) authorized in the trust agreement *and* b) a donation of gross income

CE is not a donation of gross income.

Strategies to get the land out of the trust:

- Purchase it
- Ask a Court to authorize distribution

Capital Gains Tax Savings (upon a later sale)

**Strategy: Donate CE
worth \$5,000,000 in 2019 (69%)**

**Ranch value = \$2,200,000 because of the
restriction on development.**



Capital gains tax: sale without CE donation = \$1,642,200 (23.8%)

Capital gains tax: sale with CE donation = \$401,363 (18.8%)

Federal Estate Tax Savings

- The donation reduces the size of the estate
- Some CE donations qualify for an additional exclusion from the gross estate, up to \$500,000

IRC § 2031(c)

- CE must have one or more conservation purposes
- Donor must own at least 30% of an entity that donates
- Land must have been owned by the donor/family for at least 3 years before date of death
- Donor did not retain development rights and restricted commercial recreational uses

Calculate FET Savings with \$5M CE Donation

Single Landowner's Taxable Estate before CE = \$17.0M

$\$17\text{M} - \$11,400,000 = \$5,600,000 \times 40\% = \$2,240,000$ FET

After the CE, the Taxable Estate is \$11.5M b/c lower ranch value and the landowner qualified for the extra \$500,000 exclusion

$\$11.5\text{M} - \$11,400,000 = \$100,000 \times 34\% = \$34,000$ FET

TAX SAVINGS = \$2,206,000



Result After Easement



Easement Holder:

- Conserve
Habitat
Water quality
Open spaces
- Low cost

Landowner:

- Cash or deduction
- Still use land
- Land value continues
to appreciate
- Unlocked value
- Tax savings

Sale of Conservation Easement



Sources of Funding

- **Local Programs**

Hays County Open Space Bond

Travis County Open Space Bond

San Antonio Aquifer Protection Bond

County Habitat Conservation Plans and Mitigation Banks

- **State wide Programs**

TX Farm & Ranchland CP \$2 million

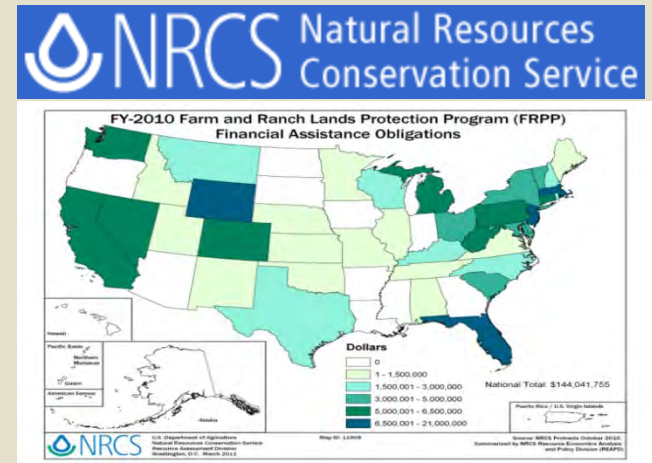
- **Federal Programs**

NRCS ACEP =

Agricultural Land Easement

Wetland Reserve Easement

2016 = \$6 million in Texas



City of San Antonio Program

Aquifer Protection Program

- 2000 \$45MM
- 2005 \$90MM
- 2010 \$90MM
- 2015 \$100MM

= >152,000 acres protected



Tax Consequences

- Most sales are bargain sales: there is a sale component and a donation component. The sale will be subject to capital gains tax.
- Landowners can claim a charitable deduction based on the value of the donation.
- Because of the income generated by the sale, much of that deduction is used in the first tax year.

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BRAUN & GRESHAM

ATTORNEYS AT LAW

Margaret Menicucci

mmenicucci@braungresham.com

(512) 894-5426

www.braungresham.com

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