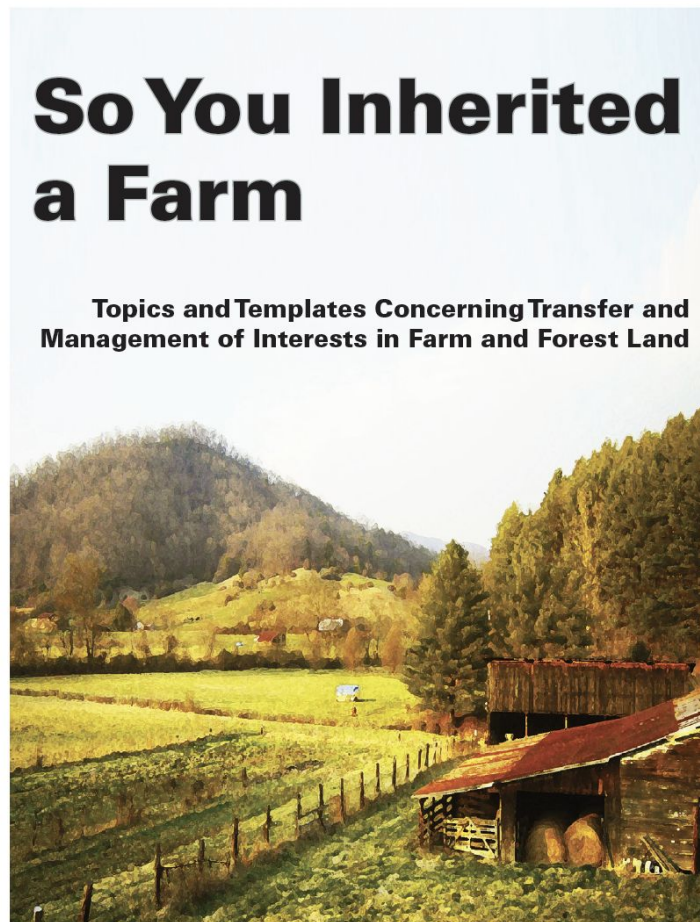


Conservation Easements and Farm Succession



New *Draft* Publication



farmlaw.ces.ncsu.edu

Land Summits

Carthage - March 17

West Jefferson -
March 30

A Question for the Ages

- “We think it enough that our title is derived by the grant of the former proprietor, by descent from our ancestors, or by the last will and testament of the dying owner; not caring to reflect that (accurately and strictly speaking) there is no foundation in nature or in natural law, why a set of words upon parchment should convey the dominion of land: **why the son should have a right to exclude his fellow-creatures from a determinate spot of ground, because his father had done so before him**: or **why the occupier of a particular field or of a jewel, when lying on his death-bed, and no longer able to maintain possession, should be entitled to tell the rest of the world which of them should enjoy it after him**”. - Sir William Blackstone, 1753

Review of Title Situations

- Real Property Titling
 - Joint Tenancy/Tenancy by the Entireties = survivorship = non-alienable/severable
 - Inherited land is not **joint property**
 - Spouse may have rights to inherited property at owner's death or divorce
 - Tenancy in Common = severable/alienable interests
 - Inherited land with siblings is often Co-Tenancy Land
 - **ALL Cotenants must agree to disposition of interest, including severable interests (timber, water transfer, farm lease etc.)**
 - Life Tenancy = remainder interest is *vested*
 - must have agreement of both life tenant and *all* remainders to transfer interest
- Article Draft: [Understanding Rights in Property](#)

Only Three Ways to Dispose of Property

- **Sale**

- Completely relinquish rights in property, receive fair market value in cash or equivalent (aka consideration)
- May reserve rights (timber, an easement, etc.)
- Tax consequence: capital gains on sale income (if held for more than one year)

- **Gift**

- Completely relinquish rights in property, nothing in return
- File gift tax return for gifts over \$15,000/donee/year
- Tax Consequence: Carry-over basis

- **Death**

- Property interests pass to heirs at law, or devisees in will
- Tax Consequence
 - Subject to federal estate tax
 - Property exempted up to \$11.4 million per person

The Short of it...

- Landowner should try and avoid creating co-tenancy in inherited property
 - land is often sold by ‘heirs’ or an agreed subdivision is reached
 - ‘heirs’ struggle to agree on subdivision
- A conservation easement *may* be subdivided, but there are permissions and restrictions
- As best as possible, sync up **title distribution plan** with **conservation deed language and baseline options** a *planned* subdivision

General “Estate Planning” Benefits of Conservation Easements

Reduction in value for federal estate tax purposes

- [IRC §2031\(c\)](#) allows an executor to exclude up to 40% value of land subject to CE, with cap of \$500,000
- **Federal Exemption = \$11,400,000 per individual (federal only)**

Possible reduction in income tax liability due to allowed deductions (frees cash for other operational purposes, ie. keep up farm infrastructure, expansion, etc.

Can provide cash money for:

- purchase of whole life insurance policy (to provide an “estate share” for “non-successors”
- can distribute cash money to “non-successors” as “estate share”
- pay down debt that may burden farm in succession
- purchase additional land to expand farm in succession

However, little or no research on how families have used CE funds, or how property has been distributed/disposed. Would be a great research project...

Property Tax Benefits: PUV

Property must qualify for PUV to be eligible for ADFPTF funds

Though county tax appraisals are normally made on an octennial cycle (i.e. review of appraisals for one-eighth of county properties occurs in any given year), a parcel of real property whose development rights have been severed **qualifies for an off-cycle re-appraisal** to reflect a reduction in fair market value... N.C.G.S. §105-287(a)(2a)

For a CE to qualify property for permanent PUV enrollment (without regard to income requirement), the conservation easement must be in perpetuity and the **landowner (grantor/donor) cannot have received more than 75% in compensation** for the value of the conservation easement (development rights). N.C.G.S. §105-277.3(d1)

Disposition at Death

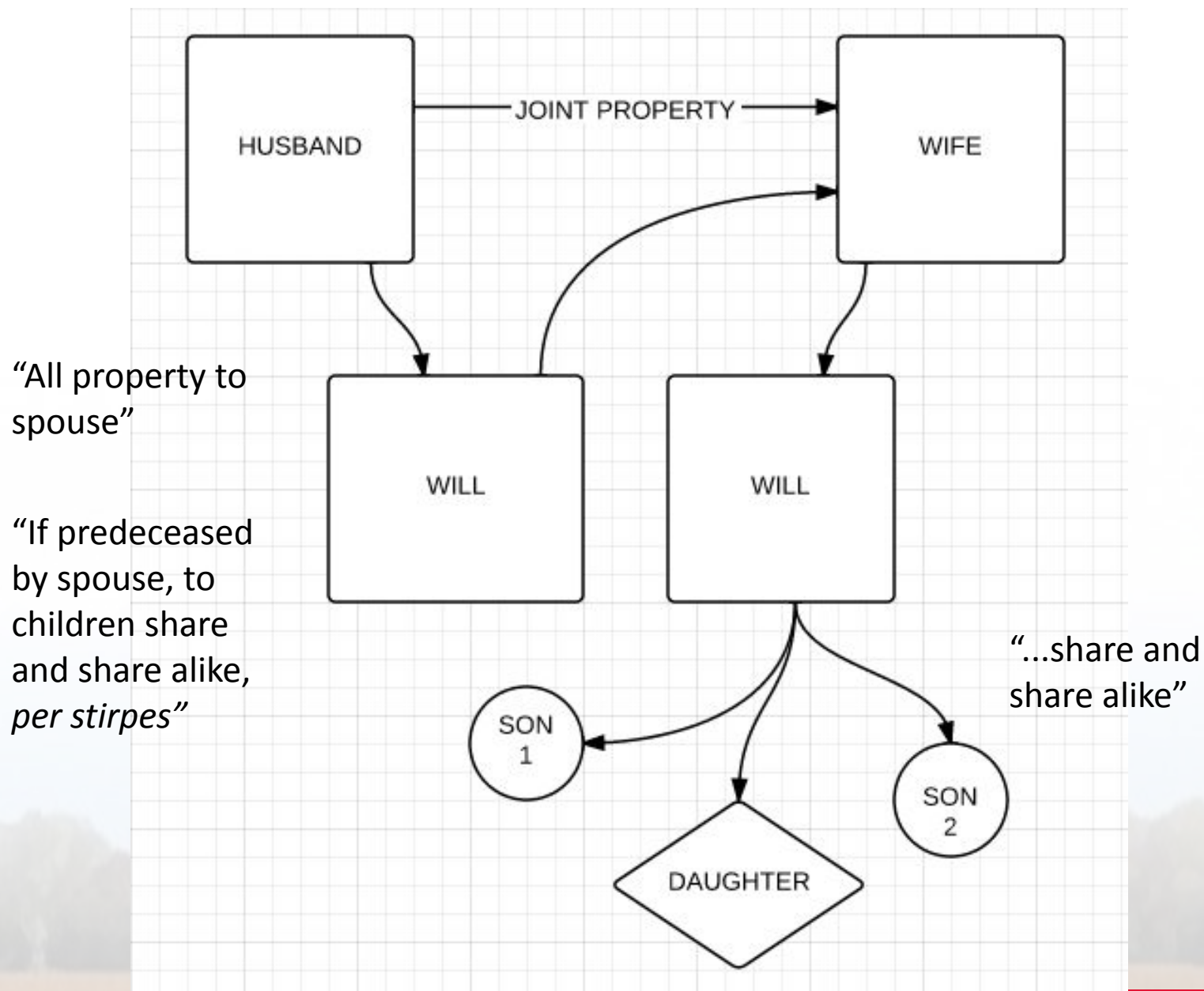
- **Testate:** person dies (decedent) with a valid will
 - late 15c., from Latin *testatus* "public, manifest, published"
- **Intestate:** person dies without a valid will, property is distributed according to **Intestate Succession Act** ([N.C.G.S. Chapter 29](#))
 - Distributions to spouse, lineal descendants, lateral descendants, or ancestors depending on facts at moment of death
 - Spouse % varies with # of children or grandchildren
 - Children and grandchildren (% varies by class)
 - Siblings and parents (depends on whether lineal descendants alive)

Creating a valid Will

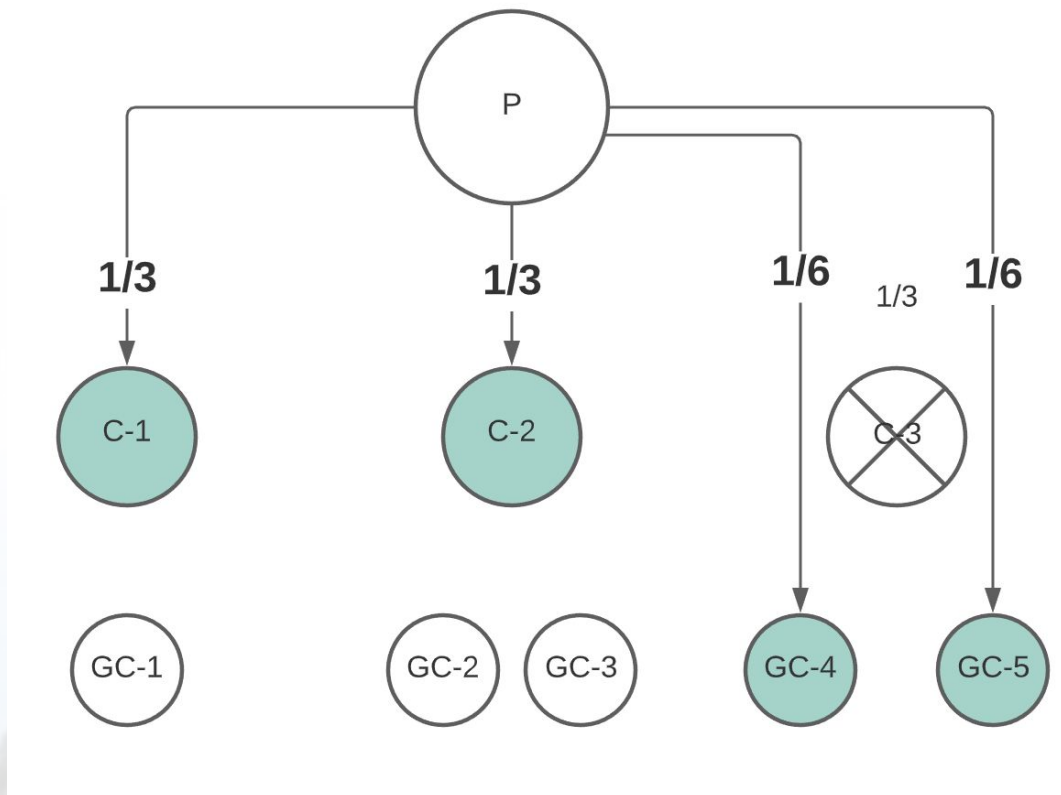
- Requirements codified N.C.G.S. § 31-1
- Testator (age 18+) must have mental capacity
 - Understand you are making a will
 - Understand Nature of property you own
 - Understand Who you are leaving it to
- Testator must sign
 - In the presence of two “disinterested” witnesses
 - Have no inheritable interest under the will
 - **Self-Proving Will:** Testator and witnesses sign in the presence of a notary public
 - With no notary, Clerk must call in will witnesses to testify as to validity of signature
- **Holographic Wills:** written and signed in handwriting of testator (N.C.G.S. § 31-3.4)
 - If found among testators “valuable papers”, safe deposit box, etc.
- **Clerk must decide if will meets legal sufficiency for entry into probate**

The Trust

- A separate legal entity
- Settlor (or Grantor): the person(s) who create(s) the trust and funds it (assigns property to the trust)
- **Trustee:** the “legal owner” of the trust property, bound by a fiduciary duty (state law) and by terms of the trust
 - **Fiduciary powers of trustee NCGS**
- **Beneficiary:** The person(s) who receive the benefit of the trust
 - income from assets
 - distribution of assets
- Language of the Trust controls distribution
- Trusts are **private**, assets not part of probate estate (but part of taxable estate if trust is revocable)
- Often used as “will substitutes”: trust determines distribution of property
- **Can empower Trustee to place conservation easement, place land in entity, etc.**



Multiple Generations of Co-Tenants



Types of Trusts

- Testamentary Trust (established by executor pursuant to a will)
- **Revocable Trust**
 - Fund during lifetime (put in, take out)
 - Fund through ‘pour over’ will
 - Amend as needed
- Irrevocable Trust
 - Insurance Trust (ILIT)
 - “Asset-Protection”
- Special Needs Trust
- Charitable Trusts
- “Dynasty” Trusts
 - Revocation of “rule against perpetuities”

Use of Business Entities

- Most prevalent: Limited Liability Company
- Often used to hold “family” land
 - Governing document (e.g. Operating Agreement) controls disposition of interests in entity
 - The Buy-Sell Agreement (option, valuation (purchase price, payment))
 - May limit ownership to “lineal descendants”
 - Business Entity interest (shares, membership) = **intangible personal property**
 - Gifts of interest to create equity in younger generation
 - Land titled to business entity = personal property
- May transfer interests in business entity to successors by gift, sale or at death

Care in Using Devices

- The Will
 - title passes at moment of death
 - **unless specific property devises/bequests**, property passes by class
 - e.g. “To my children”: 3 children
 - 3 parcels of land, farm equipment/livestock, personal property
 - each child takes $\frac{1}{3}$ co-tenancy interest in land, $\frac{1}{3}$ interest in all personal property
 - Executor (and Clerk of Court) without authority to decide who gets specifically what
- The Trust
 - not ideal as long-term landowning device for farmland (rent may be insufficient to cover costs)
- The LLC - the family members are ‘in business’ with one another

Principal Challenges

Adapt distribution scheme in estate plan (will and trust) to:

- ensure equal distribution of wealth (a goal of many families)
- avoid co-tenancy ownership in conservation easement tract (no guarantee of subdivision)
- preserve cash (or its equivalent) from development rights sale for distribution to 'heirs' (it gets spent quickly)

Design conservation easement deed language to:

- allow subdivision of parcel (to extent possible per zoning and funding restriction)
- plan building envelopes and impervious surface growth
 - financing for construction of allowed structure will encumber entire parcel unless subdivision **allowed**

Principal “Title” Effects of Conservation Easement

- **Subdivision Restriction**
 - can owner subdivide parcel in estate plan so that each heir ‘takes their own’?
 - Subject to funder flexibility and deed language
 - See [NCGS §106-744\(b\)\(1\)](#)
- **Defeats Partition Rights**
 - if land held in co-tenancy
 - can a Clerk of Court force in-kind subdivision under [NCGS § 46A-1](#)?
- **Impervious Surface Restrictions**
 - limitation on new structures and paved surfaces in event of subdivision

Under what circumstances may a conservation easement be modified?

Article Draft: [Conservation Agreements and Easements: Obligations, Modification and Termination](#)

Federal Tax Limitation on Modification

- Relevant only if tax deduction taken for donated portion of development rights sale
- **“Private Benefit Doctrine”**: Because the tax benefits to the individual are supplied by the public at large for *their* collective benefit - a modification of that benefit to advantage the taxpayer is not allowed
 - normally a threat to taxpayer (clawed back deduction) and to 501(c)(3) status of a land trust
 - Gentry, P. *Applying the Private Benefit Doctrine to Farmland Conservation Easements* (Duke Law J., 2013),

See [§ 1.170A-14 Qualified conservation contributions](#). No hard and fast rule found, but this example:

Example 3.

H owns Greenacre, a 900-acre parcel of woodland, rolling pasture, and orchards on the crest of a mountain. All of Greenacre is clearly visible from a nearby national park. Because of the strict enforcement of an applicable zoning plan, the highest and best use of Greenacre is as a subdivision of 40-acre tracts. H wishes to donate a scenic easement on Greenacre to a qualifying conservation organization, but **H would like to reserve the right to subdivide Greenacre** into 90-acre parcels with no more than one single-family home allowable on each parcel. Random building on the property, even as little as one home for each 90 acres, would destroy the scenic character of the view. Accordingly, no deduction would be allowable under this section.

Restriction on Subdivision (ADFPTF)

- From the ADFPTF Manual:

***Land Division:** Any parcel of land with an ADFP agricultural conservation easement will be limited to a **minimum division of 20 acres in size**. Any division of a land parcel must maintain agriculture, horticulture or forestry present use value status as designated by the State of North Carolina at the time of transfer. (Approved 12-09-08)*

- Subject to state statute limitation (see §106-744(b)(1) [next slide]
- Note: Funding preference to applicants with “Farm or Forest Transition Plans”

NC Statutory Limitation on Subdivision

§ 106-744. Purchase of agricultural conservation easements; establishment of North Carolina Agricultural Development and Farmland Preservation Trust Fund and Advisory Committee.

(a) A county may, with the voluntary consent of landowners, acquire by purchase agricultural conservation easements over qualifying farmland as defined by G.S. 106-737.

(b) For purposes of this section, "agricultural conservation easement" means a negative easement in gross restricting residential, commercial, and industrial development of land for the purpose of maintaining its agricultural production capability. Such easement:

(1) **May permit the creation of not more than three lots** that meet applicable county zoning and subdivision regulations;

(1a) May permit agricultural uses as necessary to promote agricultural development associated with the family farm; and

(2) Shall be perpetual in duration, provided that, at least 20 years after the purchase of an easement, **a county may agree to reconvey the easement to the owner of the land for consideration**, if the landowner can demonstrate to the satisfaction of the county that commercial agriculture is no longer practicable on the land in question.

Is this restriction limited to county-held conservation easements?

Subdivision NRCS Conservation Programs Manual

H. Subdivision

(1) The eligible entity **must address** the potential for future subdivision in each agricultural land easement deed by including provisions to prohibit subdivision of the easement area entirely or limit the subdivision of the easement area.

(2) In general, the agricultural land easement deed should prohibit future subdivision of the protected property. **If the landowner intends to subdivide a parcel in the future, individual applications should be submitted for the individual intended subdivided parcels and ranking conducted on the individual applications.** If the smaller parcels are individually eligible and rank high enough to be selected for funding, separate agricultural land easements may be purchased on the individual parcels.

(3) If the eligible entity includes provisions to prohibit subdivision of the easement area entirely, the provision may include an exception to address State or local regulations that explicitly require subdivision to construct residences for employees working on the agricultural land easement area.

(4) If the eligible entity instead of prohibiting future subdivision of the protected property wants to provide for the future subdivision of the protected property, then **the agricultural land easement deed must identify the maximum number of future parcels**, the terms required for the future conveyance of approved parcels, and identify the boundaries of the proposed subdivisions as follows—

(i) If Identified Prior to Closing.—Prior to closing, the eligible entity must provide NRCS a map of the proposed subdivision of the protected property. The individual parcels resulting from the proposed subdivision of the protected property must each meet the ACEP-ALE land eligibility requirements and

Subdivision Restrictions

(NRCS ALE Deed 2020)

(A) *Subdivision* – [Select Option 1, 2, or 3.] [Additionally, where required by State law the following may be inserted at the end of the selected option: Notwithstanding the foregoing, subdivision of the Protected Property is permissible when necessary to comply with State or local regulations that explicitly require subdivision to construct residences for employees working on the Protected Property. Grantor must provide written notice and evidence of such requirements to Grantee and the Chief of NRCS, or the Chief's authorized designee (Chief of NRCS), prior to division of the Protected Property in accordance with such State or local regulations.]

[Option 1] Separate conveyance of a portion of the Protected Property or division or subdivision of the Protected Property **is prohibited**.

[Option 2] The Protected Property must not be divided or subdivided into, or separately conveyed as, more than _____ separate parcels (_____ divisions allowed), the boundaries and the allocation of the impervious surface limitation of which have been identified in EXHIBIT _____, which is appended to and made a part of this ALE Deed. To protect the Purpose of the ALE, the boundaries of such divisions have been preapproved in writing by Grantee and the Chief of NRCS, or the Chief's authorized designee (Chief of NRCS). Deviations from the identified boundaries will not be allowed. Grantor must give Grantee and the Chief of NRCS written notice prior to subdividing, dividing, or separately conveying a parcel of the Protected Property.

Impervious Surface Restrictions

([NRCS ALE Deed 2020](#))

1. Limitation on Impervious Surfaces. Impervious surfaces will not exceed _____ percent **[Insert approved impervious surface percentage. Note: if greater than 2 percent, a written waiver from the Chief of NRCS or the Chief's authorized designee is required.]** of the Protected Property, excluding NRCS-approved conservation practices. Impervious surfaces are defined as material that does not allow water to percolate into the soil on the Protected Property, including, but not limited to, buildings with or without flooring, paved areas, and any other surfaces that are covered by asphalt, concrete, or roofs. This limitation does not include public roads or other roads owned and controlled by parties with rights superior to those rights conveyed to Grantee by this ALE Deed.

See [7 CFR § 1491.22](#): Director may waive to no more than 10%

[Include the following if limited subdivision is allowed below: In the event the Protected Property is subdivided as provided for in Section I, Paragraph (2)(A), the total cumulative impervious surface of the subdivided parcels must not exceed the impervious surface limitation referenced above. The Grantor, with Grantee approval, will allocate the impervious surface limit among the subdivided parcels and ensure said impervious surface limitation is clearly defined in each subdivided parcel's recorded instrument.]

Conveyance Restrictions in Standard NRCS Deed

- **K. Subsequent Conveyances.** The Landowner agrees to notify NRCS in writing of the names and addresses of any party to whom the property subject to this Easement Deed is to be transferred at or prior to the time the transfer is consummated. Landowner and its successors and assigns shall specifically refer to this Easement Deed in any subsequent lease, deed, or other instrument by which any interest in the property is conveyed.

Conservation Easement Deed should contain specific language allowing for transfer to entity or trust



THANKS FOR INVITING ME!

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