

*Farm Law for Producers and Landowners*

# Conservation Easements and Farm Succession

## Part III: The Impact of Conservation Easements on Real Property Transfer Decisions



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### News and Updates



**Conservation Easements: Save the Date for Three Part Series, September 7, 14, 21**

Please join this series of webinars on September 7, 14 and 21 at 1 p.m. for an update on ...


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**Farm Management: NCSFMRA Members Tour Shenandoah Valley Agriculture**

In the last week of July, members of the North Carolina Society of Farm Managers and Rural Appraisers (NCSFMRA) ...

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**Landowner Liability: Branan Presents Webinar on August 31**

The North Carolina Tree Farm Association – in collaboration with NC State Forestry Department – is hosting a lunch ...

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have a QUESTION

# So You Inherited a Farm

**Topics and Templates Concerning Transfer and Management of Interests in Farm and Forest Land**



[Landowner Liability Webinar \(on demand\)](#)  
(sponsored by NC Tree Farm Association)

# Conservation Easements 101

- Easement in gross (pr. grow)
- **Permanent** restriction of landowners' right to subdivide parcel
- Landowner paid for giving up right to subdivide/develop
- Landowner can donate the right to a third party
  - Donation amount is tax deduction under US tax code
  - Usually a combination of purchase and donation
- Third Party – e.g. non-profit land trust, S&WCD – ensures the terms of the easement are not violated by landowner
  - has right of access (and obligation) to monitor restrictions
- Value of CE = Highest value – restricted value



# Conservation Easement Concepts

- **“Highest and Best Use”** – an appraisal-supported valuation of the maximum market value of a property
  - Dependent on appraisal methods (certified appraiser)
  - Dependent on infrastructure, zoning, etc. supporting development
    - Residential: how many lots and houses can this parcel support with water, septic, etc.?
    - Industrial: will water, infrastructure, zoning for industrial use
- **“Restricted Use Value”** – the appraisal-supported value of the land without the right to subdivide or otherwise build on it
- **“Permanent”** – restriction must be permanent, last forever, have no termination date
  - No legal mechanism by which “stick” returns to bundle (but see
- **“Permeable Surface”** – minimum allowable surface impermeable to water (asphalt roads, barn roofs, etc.)
- **“Building Envelope”** – the location and size of additional structures allowed per the terms of the conservation easement deed

# Funding for Purchase of Development Rights

- Federal: **Agricultural Conservation Easement Program (ACEP)** (formerly Farm and Ranchlands Protection Program)
  - Funding amount authorized by Farm Bill (5 years)
  - Apportioned to states by NRCS (e.g. NC has \$X allocation of competitive funds)
- State of North Carolina:
  - **Agricultural Development and Farmland Preservation Trust Fund** (upland projects)
  - Land and Water Fund (formerly CWMTF) (riparian projects)
- **Private donations** of cash for purchase (wealthy donors cultivated by the Land Trust)
- Landowner donation
  - Cash for monitoring
  - Donation of value of land (see example)
    - Agree to take less than the value of the development right restricted by the easement

# Conservation Easement Example

- 100 acre parcel
  - Development Value: \$1,000,000
  - Value if could not develop: \$650,000
- Value of Easement:  $\$1\text{MM} - \$650\text{K} = \$350\text{K}$
- Funding for purchase of Easement
  - Federal ACEP: \$200K
  - State ADFPTF: \$100K
  - Other sources: \$10K
  - Donation of value: \$40K
    - Landowner may deduct \$40K from federal income tax
    - May carry unused portion forward for number of years (up to 10 if a “qualifying farmer”)

# 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...**

# IRC §2031(c) Reduction in Land Value Subject to Conservation Easement

## (c) Estate tax with respect to land subject to a qualified conservation easement

### (1) In general

If the executor makes the election described in paragraph (6), then, except as otherwise provided in this subsection, there shall be excluded from the gross estate the lesser of—

**(A)** the applicable percentage of the value of land subject to a qualified conservation easement, reduced by the amount of any deduction under section 2055(f) with respect to such land, or

**(B)** \$500,000.



# 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)

# “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](#)

# 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) **as a matter of right**
- plan building envelopes and impervious surface growth
  - financing for construction of allowed structure will encumber entire parcel unless subdivision allowed

# 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),



# Modification Example from Regs

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.

**RAB Comment: Note specificity of reason for denying subdivision. Similar situation with easement purpose focus on quality soils and water quality might have different result.**

**Subdivision decision would likely center on state law restrictions and impervious surface restrictions.**

# 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”

## CORRECTION ON PROPERTY ELIGIBILITY

To be eligible for a conservation easement through the ADFP Trust Fund's program, the property must be privately-owned, located within the borders of the State of North Carolina, and in working lands use (agriculture, horticulture, forestry). Minimum acreage requirements must follow the present-use value guidelines: Five acres for horticulture, 10 acres for agriculture (row crops or pasture), 20 acres for forestry, or a combination of working lands use. If there are existing easements that have removed the development rights from the property, those easement areas will be ineligible for the program and do not count towards the minimum acreage requirements.

Questions should be directed to Evan Davis, ADFP: [evan.davis@ncagr.gov](mailto:evan.davis@ncagr.gov), 919-707-3072

# 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?**



## CORRECTION ON SUBDIVISION

Conservation easements funded through the ADFP Trust Fund may not be subdivided once the conservation easement is recorded.

The subdivision restriction in the conservation easement is as follows: Separate conveyance of a portion of the Protected Property or division or subdivision of the Protected Property is prohibited. Grantor hereby waives any right to subdivide the protected property pursuant to North Carolina General Statute 106-744(b)(1). Even if the Protected Property consists of more than one parcel for real estate tax or any other purpose or if it was acquired previously as separate parcels, it will be considered one parcel for purposes of this ALE Deed, and the restrictions and covenants of this ALE Deed will apply to the Protected Property as a whole.

In accordance with G.S. 106-744(b)(1), before recording the conservation easement, the landowners can elect to create not more than three lots that meet applicable county zoning and subdivision regulations. These lots must be delineated on the recorded conservation easement survey and referenced in the conservation easement.

ADFP Trust Fund staff encourages county governments, land trusts, and landowners to consider the future disposition of property when determining the size and location of conservation easements. For example, one tax parcel can have more than one recorded conservation easement as long as the conservation easements meet the minimum acreage requirements. Noncontiguous parcels under the same ownership must be separate conservation easements.

Questions should be directed to Evan Davis, ADFP: [evan.davis@ncagr.gov](mailto:evan.davis@ncagr.gov), 919-707-3072

# Subdivision in NRCS Conservation Programs Manual (Part 528)

## 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—

## **Subdivision in NRCS Conservation Programs Manual (Part 528)... continued**

**(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 program purposes, as determined by NRCS. Both the approved number and boundaries of the proposed subdivided parcels as approved by the State conservationist prior to closing must be identified in the agricultural land easement deed. No further NRCS review is required at the time of future conveyance of the parcels as identified in the deed.

## Subdivision in NRCS Conservation Programs Manual (Part 528)... continued

(ii) **If Identified After Closing.**—The eligible entity must submit a request to the State conservationist for approval prior to authorizing a subdivision. The eligible entity must certify that the requested subdivision is required to keep all resulting farm or ranch parcels in production and viable for agricultural use. The State conservationist must determine that—

- Parcels resulting from the subdivision of the protected property will meet ACEP land eligibility requirements of 16 U.S.C. Section 3865 et seq. as enacted on the date the original parcel was enrolled in ACEP, including the **allocation of the impervious surface limitation** between the subdivided parcels.

- The resulting parcels **will not be below the median size of farms in the county** or parish as determined by USDA's most recent [National Agricultural Statistical Survey](#) (NASS).



# 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.

# Subdivision Restrictions

## (NRCS ALE Deed 2020)

**[Option 3]** The Protected Property must not be divided or subdivided into, or separately conveyed as, more than \_\_\_\_\_ separate parcels (\_\_\_\_\_ divisions allowed). To protect the Purpose of the ALE, the boundaries of such divisions must be approved in writing by Grantee and the Chief of NRCS, or the Chief's authorized designee (Chief of NRCS), before any such division, subdivision, or separate conveyance occurs. The Chief of NRCS may only approve the division, subdivision, or separate conveyance of the Protected Property into separately conveyable farm or ranch parcels when—

1. The Grantee requests the Chief of NRCS approval to subdivide the Protected Property into separate farm or ranch parcels, after receiving a request from the Grantor;
2. The Grantor certifies to the Chief of NRCS that the requested subdivision is required to keep all farm or ranch parcels in production and viable for agricultural use and that any new owners of the subdivided Protected Property farm or ranch parcels intend to use such parcels for agricultural operations; **and**
3. The Chief of NRCS determines that the—
  - a. Parcels resulting from the subdivision of the Protected Property will meet ACEP land eligibility requirements of 16 U.S.C. Section 3865 et seq. as enacted on the date the original parcel was enrolled in ACEP, including the allocation of the impervious surface limitation between the subdivided parcels, and
  - b. The resulting parcel will not be below the median size of farms in the county or parish as determined by the most recent United States Department of Agriculture's National Agricultural Statistical Survey (NASS).

# 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**

**Note: some entities have a “transfer fee”, consider language to except this fee for transfers to Trust or LLC or to lineal family members (defined)**



# Power of Trustee to Convey Development Rights (Conservation Easement)

## § 36C-8-816. Specific powers of trustee.

(8) With respect to an interest in real property, construct, or make ordinary or extraordinary repairs to, alterations to, or improvements in, buildings or other structures, demolish improvements, raze existing party walls or buildings or erect new party walls or buildings, subdivide or develop land, **dedicate land to public use or grant public or private easements**, and make or vacate plats and adjust boundaries, make contracts, licenses, leases, conveyances, or grants of every nature and kind with respect to crops, gravel, sand, oil, gas, timber and forest products, other usufructs or natural resources, and other benefits or incidents of the real property;

# Sample Trust Language

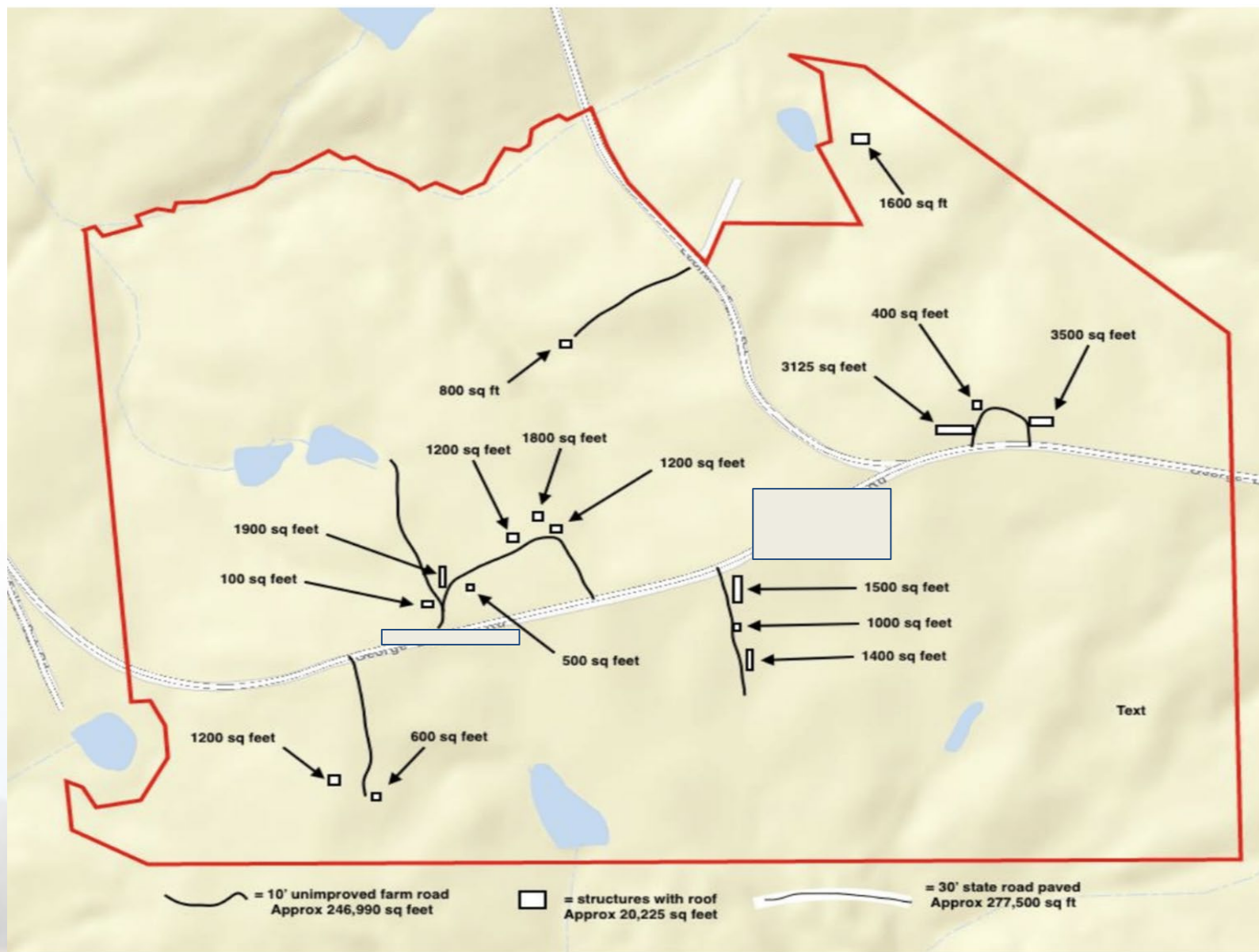
In trust Article Titled “Disposition of Real Property”

§ Qualified Conservation Easements. Pursuant to trustees powers over real property in §§ - Trustee may create a qualified conservation easement, as defined in Section 2031(c)(8)(A) of the Internal Revenue Code and NC General Statutes § 121-35 in any land held by the trust and may make the necessary election provided by Section 2031(c)(6).

May simply identify parcel: (e.g. “The Heron Farm”, PIN # 12345 comprised of 435 acres and described in Deed Book 1800 Page 100)

May place a time limit: “If within five (5) years of the death of surviving Grantor (of trust) Trustee is unable to create a qualified conservation on the property (identified in §§), Trustee shall subdivide property and distribute property to beneficiaries

- much more detail here... lot sizes, specifically to whom, trustee consult with beneficiaries on subdivision, but has ultimate authority if no agreement of who gets what



## EXHIBIT E-2

## EASEMENT IMPERVIOUS SURFACE CALCULATIONS

Total Square Footage of Easement Area: 18,974,636 square feet (435.60 acres)

30' Wide State Road Paved Surface: Approximately 9250 feet x 30w = 277,500 square feet (1.5% impervious surface)

Roofed Buildings (Barns, Dwellings, Greenhouse): Approximately 20,225 square feet (.1% impervious surface)

10' Wide Unimproved Farm Paths (Dirt Surface): Approximately 246,900 square feet (1.3% impervious surface)

TOTAL IMPERVIOUS SURFACE (including farm paths): 2.9% (without farm paths: 1.6%)

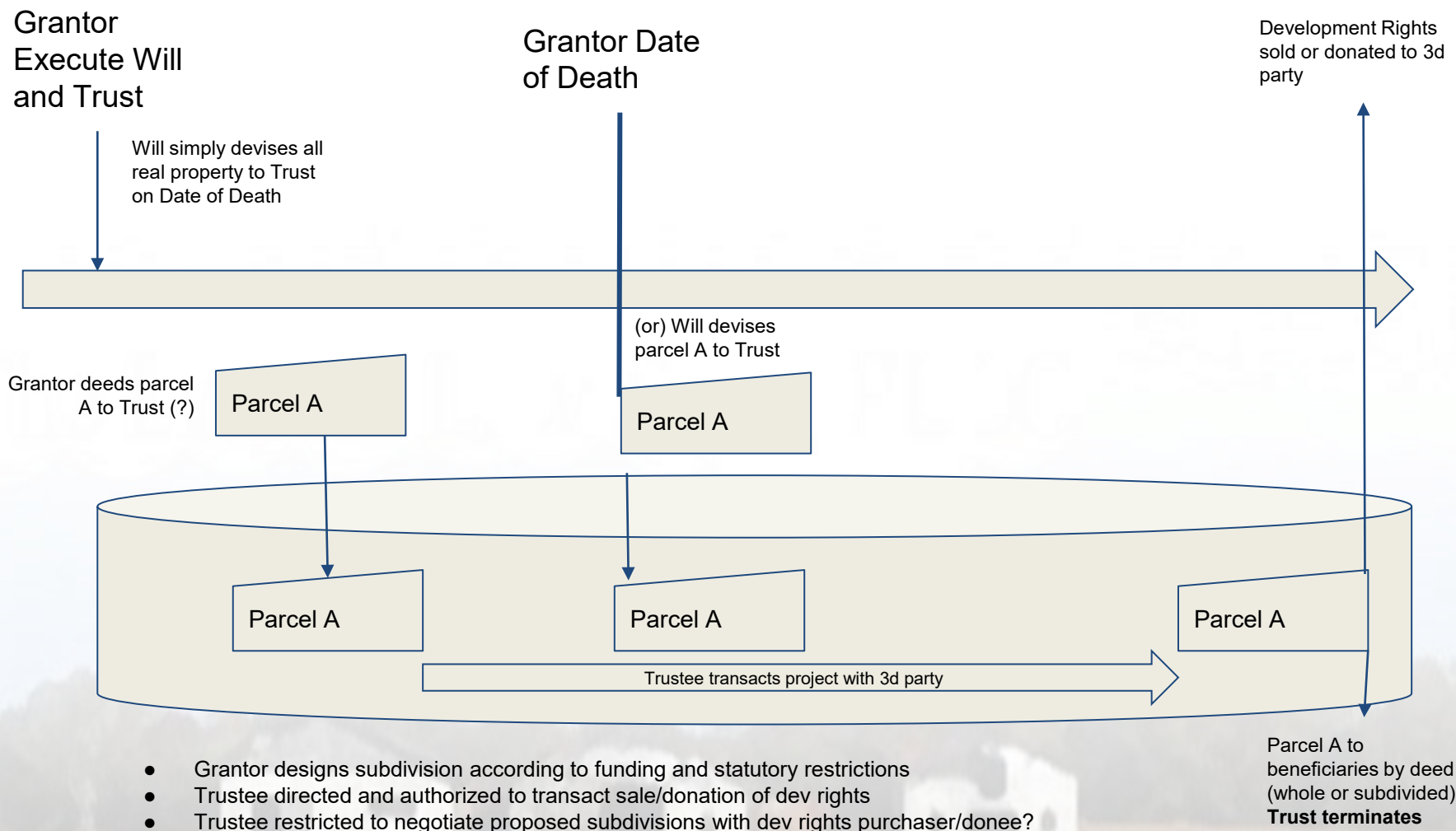




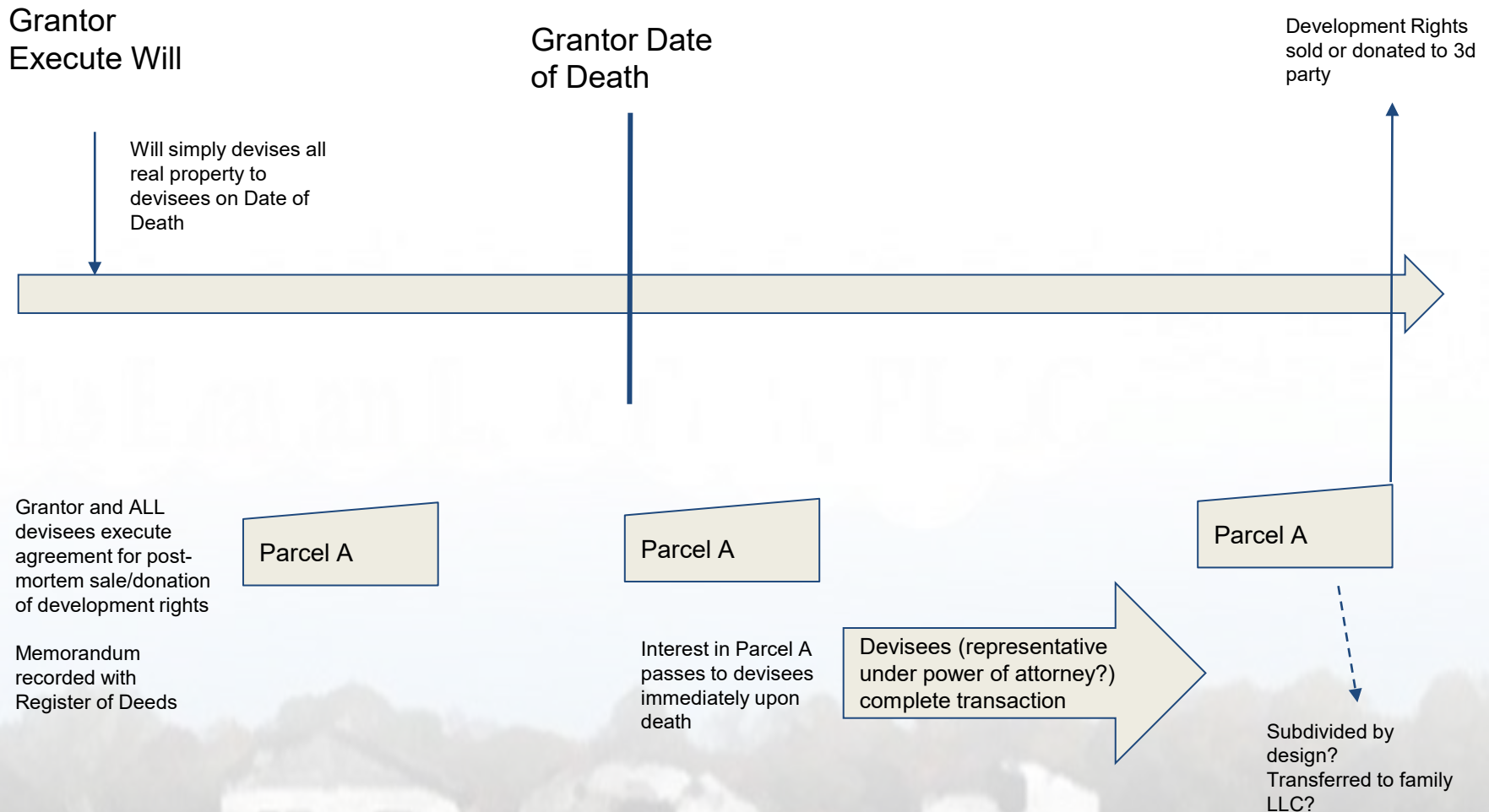




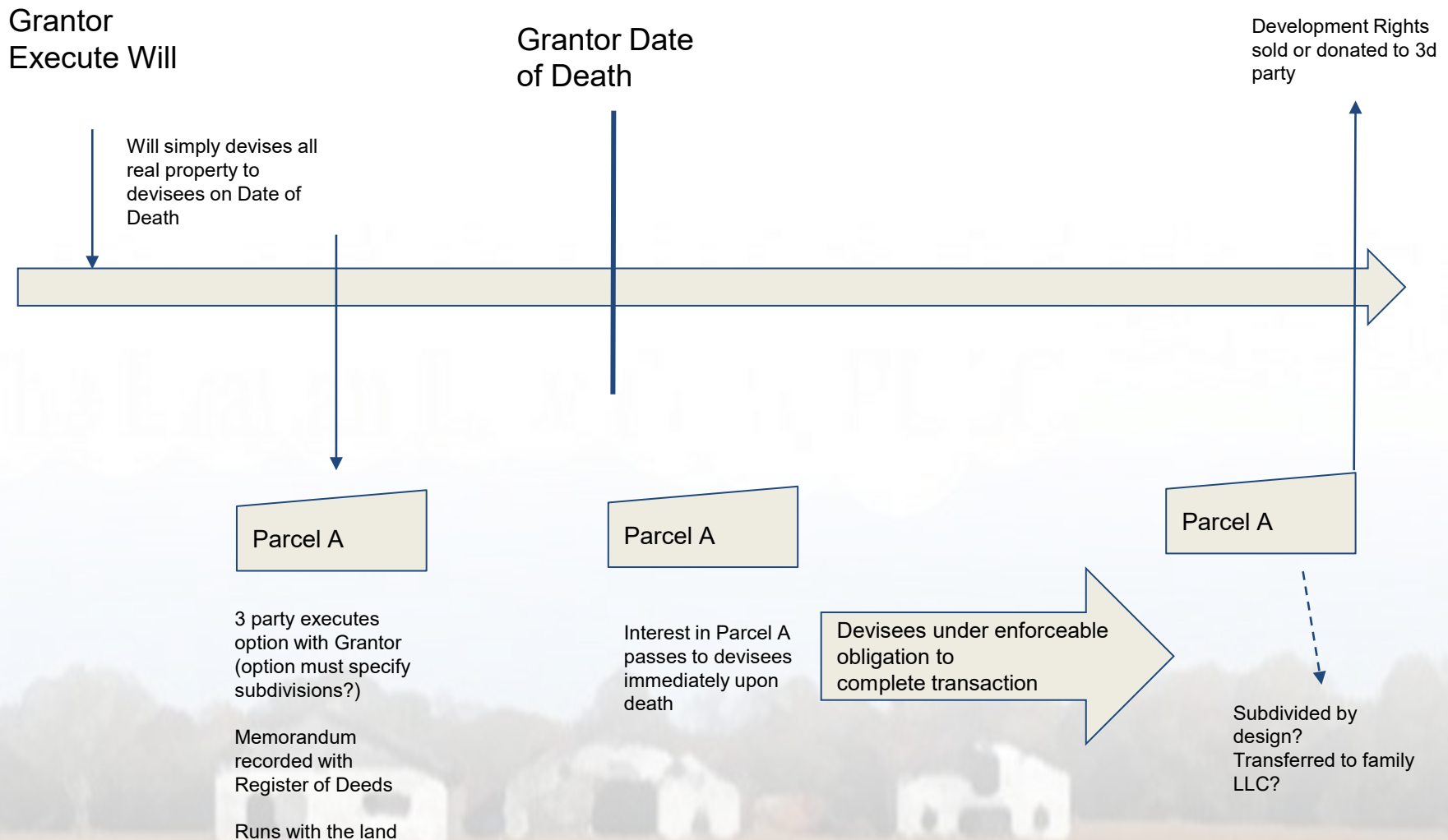
# Possible Timeline with Will and Trust



# Possible Timeline with Will only



# Possible Timeline with Option only





# THANKS FOR INVITING ME!



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