

The Basics of Combining Land Conservation & Planned Giving Techniques



**Myra Lenburg
Norman E. Rogers**

Note: Though this paper focuses on farmland, the same planned giving and conservation strategies can be used for protecting other threatened lands.

Protect Your Farm for the future ...Plan for Retirement Now

Keeping Farms Available for Farming: Some Elegant Solutions to a Familiar Problem

The story is a familiar one. A landowner is thinking about retirement but is concerned about his finances. With no children interested in buying the operation, he searches for the highest bidder. His farm is located in an area subject to increasing development pressure from nearby suburban sprawl. He can easily sell the farm - which has been in the family for three generations - for a large sum to a developer, but he really doesn't want to see it leave agriculture. Unfortunately, the value of the farm is well beyond the reach of most farmers. He laments the loss of productive farmland to development, and the large capital gains tax that would be due if he were simply to sell out.

But it doesn't have to be that way. Now there are alternatives that satisfy the farmer's wants and needs within American Farmland Trust's Farm Legacy Program.

American Farmland Trust (AFT), a national non-profit organization with regional offices throughout the U.S., is working with agricultural landowners and their financial advisors to structure innovative transactions that avoid selling the farm or ranch for development, and instead, achieve some or all of the following key benefits:

- Assure farmland and ranchland will be permanently protected from development and kept available for agriculture,
- Arrange for transition to another conservation minded agricultural family – perhaps a young farmer who could only afford a farm with a conservation easement,
- Provide potential capital gains, gift and income tax benefits,
- Potential income for the landowners, and
- Provide support for AFT's efforts to protect more farmland.

Using arrangements such as charitable gift annuities, charitable remainder trusts, bargain sales, and outright or retained life estate gifts, in combination with agricultural conservation easements, AFT, through its Farm Legacy Program, works with aging landowners and their professional advisers to develop creative alternatives to the conventional options.

Agricultural Conservation Easements: A Common Ingredient

Each of the transactions described in this fact sheet involve using an agricultural conservation easement (ACE), a deed restriction that keeps land available for agriculture. ACEs are voluntary, flexible agreements tailored to fit specific family and farm circumstances. In general ACEs limit subdivision, non-farm development and other uses of the land that are inconsistent with commercial agriculture. A landowner and a qualified conservation organization (such as AFT) or a public body creates the written document. Like all legal agreements affecting the chain of title, an easement must be recorded in the local land records and it runs with title to the land. It is enforced and monitored in perpetuity by the organization or public body that holds the easement.

After granting an ACE, landowners retain title to their property and can still restrict public access, farm, use the land as collateral for a loan or sell their property. Land subject to an easement remains on the local tax rolls. Landowners continue to be eligible for state and federal farm programs.

Donating an easement on farmland can provide immediate income tax savings for the landowner and reduce the value of the property for capital gains, gift and estate tax purposes. The difference between the value of the land with the development rights intact and the value of the land restricted by the conservation easement, as determined by qualified appraisal, can be taken as a charitable income tax deduction. The deduction can be used in the current year and carried forward and applied against as many as five subsequent year's income. Placing an easement on a property also reduces the value of the farmland for federal gift and estate tax purposes.

Options for Landowners

Landowners have many options to meet their financial and conservation objectives. All of the following options assume the use of an agricultural conservation easement.

- **Outright gift**

An outright gift of a property to AFT offers the landowner maximum immediate tax benefits – the landowner may receive the full market value of the property as a charitable tax deduction, and can avoid the capital gains tax that would be due from a sale. This simple solution also offers the landowner the ability to get out from under management headaches almost immediately, and the advantage of not becoming bogged down in drafting potentially complicated contracts or trust agreements.

- **Bargain sale**

A bargain sale is a sale of a property to a qualified non-profit organization, such as AFT, at a price below the fair market value of the property, with the difference

between sales price and market value representing a potential charitable deduction. AFT will then resell the property with an agricultural conservation easement in place. It makes sense to do a bargain sale when the landowner is ready to pass on management responsibilities for the property, doesn't need to cash-out to the maximum extent possible, has use for some tax deductions, and has some immediate cash needs. For tax planning or cash management purposes an installment bargain sale may be preferable. Here the seller elects to receive payments over a period of years, thus spreading out the tax consequences of the sale as well.

- **Charitable remainder trust**

A charitable remainder trust is an irrevocable trust that will provide lifetime income for the landowner and his or her

spouse or other beneficiary. The annual income may fluctuate year to year depending upon the structure of the trust, the ages of the landowner and other beneficiary, the value of the property funding the trust (subject to a conservation easement), and other factors. After an easement is placed on the farm, the owner transfers title to the farm to a charitable remainder trust and the Trustee sells the farm to another farmer. The sales proceeds are invested by the Trustee and used to generate annual income for the landowner. Upon the death of the landowner and any other beneficiary, any remaining assets in the trust pass to AFT.

The landowner receives a charitable deduction for the donation of the conservation easement, and upon creation of the charitable remainder trust, receives an additional charitable income tax deduction equal to the present value of the remainder interest that will pass to AFT at death. If the property has appreciated in value since it was originally acquired, the trust can sell the property free of any capital gains tax liability. Finally, because the remainder interest in the property passes to AFT at the landowner's death, no portion of the property is included in the landowner's taxable estate.

- Charitable gift annuity

A charitable gift annuity is created by transferring title to the farm to AFT. AFT then agrees to pay the landowner and spouse (or other beneficiary) a specified annual payment as long as they live. The amount of the annuity payment will depend upon the value of the farm (subject to a conservation easement), the age of the donor and other beneficiary, the annuity rate selected and the federal discount rate in effect at the time of the gift. AFT sells the farm to another farmer following creation of the gift annuity and uses the proceeds to fund the annuity. The landowner receives an immediate charitable income tax deduction equal to the present value of the remainder interest in the

annuity assets at death, avoids capital gains tax liability upon the sale of the farm and has the value of the farm excluded from his or her taxable estate at death. Assets not needed to fund projected annuity payments are available to AFT for uses agreed upon with the landowner. Some states do not allow using real estate to fund a CGA.

- Retained life estate

This planned giving technique allows the owner to continue to live on the land while he or she conveys title to the property to AFT. The life tenants must pay the property taxes, keep the premises insured and generally keep the land and buildings in good condition. If the property generates rental or other income during the landowners' lifetimes, the landowner may keep that income. Following the death of the life tenants, or sooner if they choose, the property passes to AFT. A conservation easement is placed on the farm either before or after creating the life tenancy arrangement. A landowner receives an immediate income tax deduction for the gift, limited to the present value of the remainder interest that is being given to the charity, which is determined based on actuarial tables published by the Internal Revenue Service.

- Unique solutions for unique situations

A strength of AFT's Farm Legacy Program is that it offers more than just pre-packaged financial options. Unique solutions can be designed to fit a landowner's particular circumstances. In several instances, this has led to a solution that doesn't fit neatly into the categories of traditional planned giving structures but fit the landowners needs better.

Combining Land Conservation and Planned Giving Techniques: Some AFT Case Studies
The following case studies illustrate how AFT has successfully combined planned giving techniques and agricultural conservation easements through the Farm Legacy Program:

The Refior Farm and a Charitable Gift Annuity

Betty Refior, age 78, owned a 79 acre farm and had four objectives for the property: 1) increase her annual income from the farm; 2) rid herself of the responsibilities and expenses associated with the operation; 3) remove the farm from her taxable estate and 4) conserve the property for long term agricultural use. To achieve these objectives, she deeded the farm to AFT, which in turn sold it to a younger farmer, subject to an ACE. The proceeds from the sale were used to establish a charitable gift annuity that paid Mrs. Refior considerably more income than she had previously received from the farming operation.

The Northrop Farm and a Charitable Remainder Trust

In 1992, the Northrops, ages 71 and 64, decided they were ready to part with their 46 acre farm, provided they could permanently protect the land. They wanted to avoid the large capital gains tax that would result from an outright sale of the property and also wished to take the proceeds from the sale of the farm as income payments for the rest of their lives. To achieve these objectives, the Northrops first donated an ACE on the property to AFT. Thereafter, with the help of AFT, the Northrops established a charitable remainder trust that was structured to pay them a lifetime income equal to the lesser of 8 percent of the trust's assets (recalculated each year), or the net income received by the trust. After title to the property was conveyed to the trust, the

These options should not be considered legal advice. Situations vary and you should consult with your legal and/or financial advisors about the best plan to meet your financial and conservation objectives.

trustee sold the conserved real estate and reinvested the proceeds to provide lifetime income for the Northrops. Upon the death of the second spouse, the assets funding the charitable remainder trust will pass to AFT who will use these funds to conserve other farm properties.

The Yeiser Farms and a Retained Life Estate

The Yeisers owned two farms with a total of 928 acres. Alarmed by the relentless march of urban sprawl in their community, they decided to permanently protect the farms, as their children had no interest in the properties. To assure that the farms would be protected from development and subdivision, and to provide for eventual disposition of the properties when they died, the Yeisers, aged 70 and 69, donated the farms to AFT, while retaining life estates in the properties. This was done with the understanding that AFT would, following the Yeiser's deaths, sell the farms to local farmers, subject to perpetual ACE's, and would use the sale proceeds to protect other farms in the Midwest.

Myra L. Lenburg (mmlenburg@farmland.org) is Director of Planned Giving and Norm Rogers (attorneyrogers@aol.com) in Farm Transition Advisor with American Farmland Trust. www.farmland.org