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# Conservation Easements: Wyoming Update

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## Increasing Incentives for Land Conservation in 2006 and 2007

In the summer of 2006, Congress passed a law<sup>2</sup> that makes conservation easements more attractive and the deductions associated with donated easements more available, especially for those engaged in active farming or ranching operations.

The new law includes increased tax incentives for conservation easements donated to land trusts or other nonprofit conservation organizations and that meet the “conservation purposes” requirement for federal tax deduction. They include:

- increasing the charitable deduction limit from 30 percent to 50 percent of adjusted gross income (AGI) for donations or bargain sales (sale for less than appraised value) of qualified conservation contributions;
- increasing the charitable deduction limit to 100 percent of AGI for eligible farmers and ranchers (i.e., those who receive more than 50 percent of their income from farming or ranching), so long as the contribution does not prevent future agricultural use; and
- allowing the taxpayer to carry forward the deduction for 15 years (rather than five years).<sup>3</sup>

The following fictional example illustrates the potential benefits of the new law. John and Mary Smith own a ranch in northeast Wyoming. The ranch is the Smith’s primary source of income, although John also has income from investments his father left to him. The Smith’s adjusted gross income from the ranch amounts to about \$80,000 a year and from the investments about \$60,000 a year.

John and Mary decide to donate a conservation easement on the ranch. They reserve the rights to hunt and fish, and reserve three home sites for future use or sale. They also provide that the land must always be available for ranching (although the easement doesn’t **require** ranching). The value of the ranch before the easement is \$2,500,000 and after the easement it is worth \$1,000,000. The easement deduction is, therefore, \$1,500,000.

1 This information is not intended to provide legal advice to individuals. Consult an attorney if interested in donating or selling a conservation easement.

2 Pension Protection Act of 2006, Section 1206: Encouragement of contributions of capital gain real property made for conservation purposes.

3 House Resolution 6 before the 109<sup>th</sup> Congress (2<sup>nd</sup> Session); Trust for Public Land. *Washington Watch* (August 15, 2006). Accessed at [www.tpl.org/tier3\\_cdl.cfm?content\\_item\\_id=20811&folder\\_id=2205#tax](http://www.tpl.org/tier3_cdl.cfm?content_item_id=20811&folder_id=2205#tax) on October 13, 2006.

Under the new tax law enacted as part of the 2006 Pension Reform Act, the Smiths may use this deduction against 100 percent of their AGI and carry forward to future tax years any part of the deduction not used, for a total of 16 years. Assuming the Smith's income does **not** change, they will not have to pay any federal income tax for more than 10 years thanks to the deduction. The benefit ends after 10 years in this example because, assuming that the Smith's income remains approximately \$140,000, they will have completely used up the \$1,500,000 deduction in 11 years. If the Smith's income were less, or the deduction were more, they would be able to spread the tax benefits over a longer period, up to a maximum of 16 years (including the year of the contribution).

Under the old law, the amount of the deduction was limited to 30 percent of the family's AGI (or 50 percent if they had owned the ranch for a year or less) and they could only carry unused portions forward for five years.

Even if the Smith's income was primarily from sources other than ranching, the new law would allow them to use the deduction against 50 percent of their income annually and carry any unused portion forward for 15 years.

These new rules are scheduled to expire at the end of 2007. While it is possible that the incentives will be extended beyond 2007, those who want to take advantage of them should be sure to make their gift before December 31, 2007.

More information about this new law and the tax benefits of conservation easements under the law can be found with most local or national land trusts including the Land Trust Alliance at [www.lta.org](http://www.lta.org).

## Wyoming Adopts the Uniform Conservation Easement Act

Creating and enforcing conservation easements in Wyoming recently became easier. In 2005, the Wyoming Legislature passed and Governor Freudenthal signed into law the Uniform Conservation Easement Act (UCEA).<sup>4</sup> Prior to passage, Wyoming was one of only two states that did not formally recognize conservation easements by statute. The law now contains

many provisions that clarify and simplify the use of conservation easements in the state. Here are some of the main provisions:

- **Wyoming land trusts can protect open space without owning a specific piece of property.** Prior to adoption of the UCEA, the organization holding the conservation easement was required to become the owner of property (usually one acre) adjacent to the land under easement for the provisions of the easement to be enforceable. Now, the law allows conservation easements to be held without requiring that the organization own an adjacent parcel.
- Easements created prior to the UCEA are validated. The act provides that any easement created prior to July 1, 2005 (the effective date of the act) is valid if the easement otherwise complies with the provisions of the act. This makes easements created prior to the act enforceable both under statute and common law.
- **Wyoming state property tax bases are protected.** To address concerns regarding the potential impact of conservation easements on Wyoming's property tax base, the Legislature provided that lands held in conservation easements are subject, at a minimum, to tax assessment values for agricultural use.
- **Mineral interests are protected.** The UCEA recognizes the primacy of the mineral estate, which is well established under state law. Specifically, conservation easements may not limit the right of mineral owners to make reasonable use of the surface estate for mineral exploration or development unless all such owners and lessees consent to the limitations of the easement.
- **Conservation easements are more easily enforced.** By providing a uniform set of provisions for the creation, termination, and modification of conservation easements, conservation easement will now be easier to enforce.

## Recent Questions on Conservation Easements

Since the publication of "Conservation Easements: an Introductory Review for Wyoming" in 2002 (University of Wyoming Cooperative Extension Bulletin B-1132)<sup>5</sup>, a number of related questions have arisen. Here are some answers.

<sup>4</sup> Wyoming Statute 34-1-201 through 34-1-207 (2005).

<sup>5</sup> Available online at [www.uwyo.edu/openspaces/content.html](http://www.uwyo.edu/openspaces/content.html).

## Conservation Easements: The Basics

Conservation easements are voluntary agreements that protect resources by limiting development of the land. They can be used to ensure continued agricultural production of the land, to protect wildlife habitat and natural areas, to protect historic structures, or to protect open spaces and views. Conservation easements can be for any length of time but usually are granted in perpetuity to ensure permanent protection of the land and to enable the landowner to qualify for federal tax benefits.

By donating or selling a conservation easement for full (or partial) value, the landowner may yield certain rights in order to protect the land. The landowner retains all other rights. Compensation to the landowner may consist of cash payments or federal tax benefits.

Conservation easements typically allow agricultural and other traditional uses of the land and generally limit or prohibit most commercial, industrial, and residential development. The activities prohibited by the easement are only those voluntarily agreed to by the landowner and the organization holding the easement.

Landowners may choose to either donate or sell a conservation easement to a land trust, other non-profit organization, or to a local, state, or federal government entity. The organization holding the easement provides managerial support and expertise and is responsible for ensuring terms of the easement are carried out. Each organization has its own mission and strategy for land protection. Priorities vary among agriculture, wildlife habitat, river corridors, community buffers, and greenway purposes, although many organizations enter into agreements for more than one primary purpose. Landowners choose the land trust or other organization whose mission best coincides with their own management goals.

### ***What is the relationship between conservation easements and mineral rights?***

Wyoming's adoption of the Uniform Conservation Easement Act ensures mineral rights are protected. To qualify for a federal tax deduction, the relationship between conservation easements and mineral rights depends upon who owns the mineral rights and the type of mining involved.

- If the mineral and surface rights are owned by different parties (severed), the mineral estate owner generally has the right to reasonable use of the surface estate to access and extract the minerals.<sup>6</sup> If the mineral extraction involves surface mining, the owner of the surface rights may not be eligible for a federal tax deduction for donating a conservation easement because the tax code requires surface mining be prohibited as a condition to receiving such a deduction. Conservation easements cannot affect minerals severed prior to conveyance of the easement unless the mineral owner consents.
- If the landowner owns both the mineral and surface estate, the landowner may be required to limit

surface mining on the property to benefit from federal tax deductions.<sup>7</sup> Regarding other forms of mining (which may include oil and gas development), federal tax law requires that mineral extraction not permanently harm the conservation value of the property.<sup>8</sup> For example, a deduction will not be denied where production facilities are concealed or compatible with existing topography and landscape and where surface alteration is to be restored to its original state.<sup>9</sup> A landowner may retain the mineral rights, recover those minerals, and still obtain a tax deduction for the easement donation or bargain sale provided the impact of such recovery complies with these provisions.

### ***How do conservation easements differ from purchases of development rights?***

In most cases, a conservation easement involves the donation of development rights by a landowner. When a conservation easement is paid for, and traded in a market between a willing buyer and a willing seller, it is sometimes referred to as a "purchase of development rights" or "PDR."

6 Mingo Oil Producers v. Kamp Cattle Co., 776 P.2d 736 (Wyo. 1989).

7 I.R.C. § 170(h)(5)(B) (2000), Treas. Reg. § 1.170A-14(g)(4)(i) (2004).

8 Treas. Reg. § 1.170A-14(g)(4)(i).

9 *Id.* § 1.170A-14(g)(4)(i).

***Can conservation easements be used to protect wildlife habitat?***

Yes. The donation of an easement to protect “significant relatively natural habitat” for fish, wildlife, or plants meets the “the conservation purposes test” for qualifying federal tax deductions.<sup>10</sup> Alteration of a habitat or environment to some extent by human activity will not result in denial of a deduction if the fish, wildlife, or plants continue to exist in a relatively natural state. For example, preservation of a lake formed by a man-made dam or a salt pond formed by a man-made dike would meet the conservation purposes test if the lake or pond were a natural feeding area for a wildlife community.

In addition, “significant habitats and ecosystems” are defined to include, but are not limited to, habitats for rare, endangered, or threatened species of animals,

fish, or plants; natural areas that represent high-quality examples of a terrestrial community or aquatic community.<sup>11</sup> A recent court decision reaffirmed the tax incentives available for conservation easement donations to protect wildlife habitat. The United States Tax Court opinion, *Glass v. Commissioner of Internal Revenue Service*,<sup>12</sup> held that conservation easements that protect viable habitat for rare, threatened, and endangered species meet Internal Revenue Service requirements for a tax deduction. Specifically, the court held that the “conservation purposes test” is met when the easement “protects a relatively natural habitat of wildlife and plants.” The court found the rather small portion of the donor’s property encumbered by the conservation easement was viable habitat for two endangered plant species and a known roosting site for bald eagles.

<sup>10</sup> *Id.* §1.170A-14(d)(3)(ii).

<sup>11</sup> *Id.* § 1.170A-14(d)(3)(ii).

<sup>12</sup> *Glass v. Comm’r. Of Internal Revenue*, 124 T.C. 258 (2005).

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