



**LANDOWNER GUIDE TO  
CONSERVATION EASEMENTS**

## Foreward

On August 17, 2006, President Bush signed into law the Pension Protection Act of 2006 providing new tax incentives designed to spur giving of conservation easements protecting family farms and other resource lands throughout the United States. This was the first major expansion of a tax incentive for conservation gifts in several decades, and it provides a very important opportunity for landowners in Leelanau County who want to protect their land, while making a prudent financial decision in the best long-term interests of family members.

Then, after two years of work by local land conservancies, and championed by Senator Michelle McManus and Representative David Palsrok, on December 7, 2006 the state of Michigan enacted Public Act 446. PA 446 provides a major new incentive to landowners for donating conservation easements which protect Michigan forests, farms, and lands which have a particular ecological signifi-

cance such as wetlands, shorelines, or streams .

The confluence of these two events presents a remarkable opportunity for landowners. Through the donation of a conservation easement on qualifying conservation land, property owners in Leelanau County can take advantage of significantly expanded federal tax deductions while making sure that their children or other succeeding property owners “lock in” a much lower property tax value than would otherwise be available.

This booklet is designed to explain in simple terms what a conservation easement is, how the new tax incentives apply to Leelanau County situations, and how to work with the Leelanau Conservancy. I hope you’ll consider this opportunity to protect your precious land for future generations.

— Brian Price  
Executive Director  
Leelanau Conservancy



## Introduction

As a Leelanau County property owner, you know that your land is special. Whether you own a farm or wetland, shoreline or dunes, the landscapes that give Leelanau its unique rural character are unlike any other.

Like many other landowners, you may be concerned about the future of your property. Will the next owner care for it the way you do? Can your children and grandchildren afford to keep the property?

The good news is that landowners now have the tools they need in the form of great tax breaks to protect forever the conservation values of the lands they love.

### Who We Are:

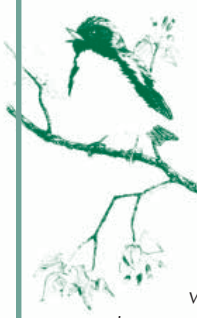
The Leelanau Conservancy is a 501 (c)(3) non-profit organization that was formed in 1988. Our mission is to Conserve the Land, Water and Scenic Character of Leelanau County. We achieve this mission by entering into conservation easement agreements with private property owners, accepting donations of property and by purchasing land.

We are a small, committed and highly professional staff with an office in Leland. We have a dedicated board of directors, an army of volunteers and 4,400 donors who care tremendously about protecting the places that make Leelanau County so unique. Together we have preserved land in each of our 11 townships—places like the Narrows on Lake Leelanau, Whaleback, Kehl Lake, the Crystal River, the DeYoung Farm and many more special locales. Over 5,400 acres and 9 ½ miles of shoreline have been protected since 1988, including 20 Natural Areas and Preserves that, collectively, represent so much of what we love about Leelanau. The Conservancy has also worked with over 100 private landowners to permanently protect the natural features of their land for future generations by creating individualized legal agreements that place certain development restrictions on the property called conservation easements. Conservation

easements can result in significant tax benefits for donors who then still enjoy private ownership of their property, including the right to prohibit public access.

### How We Save Land: Working Together to Find Solutions

The Conservancy believes in working together to find solutions and operates with this overarching goal: ***A good conservation transaction must be good for both the land and the people involved.*** We have the utmost respect for each landowner's individual goals for their property, their concerns and their privacy. The approach we take towards a property depends on the character of the land and individual donor's wishes. Although there are other land protection tools we employ, this booklet focuses primarily on the donation of conservation easements. Recent tax changes have presented an unprecedented opportunity for landowners who are willing to donate conservation easements.



*“Shortly after we purchased the 47 acres that became Charter Sanctuary, we stood at the top of the hill surveying the mix of habitats spread before us. I said, ‘Just think, after we’re gone, this will all belong to our birds.’ However, without someone to ensure that this place actually is preserved in the way we want it to be, it might not have always been there for the birds. And that someone is the Leelanau Conservancy, which, with every easement it signs, agrees to see that the terms of the agreement - which the owner stipulates - are carried out in perpetuity. Through our gift of a conservation easement, we have been provided with a way to keep our dream alive.”*

—Kay Charter, who with her husband, Jim, preserved 14 acres near Omena, known today as Saving Birds Thru Habitat.

# Learning More: A Quick Primer on the New Tax Rules

## Changes in Federal Tax Law : The “Pension Protection Act of 2006”

If you own land with important natural resources, voluntarily donating a conservation easement can be one of the smartest ways to conserve the land you love while maintaining your private property rights and realizing significant federal tax benefits.

These new incentives are the boldest change to conservation tax law in two decades. They allow modest income landowners, like working family farmers, to deduct much more than they could under the old rules, bringing increased fairness to the tax code. While the new provisions are set to expire in December of 2007, the coalition behind these incentives is working to make them permanent. However, there is no guarantee they will be available in 2008 or beyond. Now is the right time to consider donation of a conservation easement.

Among the changes, the new law:

1. Raises the deduction a landowner can take for donating a conservation easement from 30% of their adjusted gross income in any year to 50%;
2. Extends the carry-forward period for a donor to take tax deductions for a conservation easement from 5 to 15 years; and
3. Allows qualifying farmers, ranchers and forest landowners to deduct up to 100% of their taxable income (e.g., potentially pay no federal income tax).

As you read on in this booklet, we will provide specific examples from Leelanau County of how these tax law changes can benefit local landowners.

### Impact of Federal Tax Changes on Conservation Easement Donations

	<u>Old Law</u>	<u>New Law</u>
<b><u>Individuals</u></b>		
Adjusted Gross Income Limitation	30%	50%*
Carry-forward of Unused Contribution	5 years	15 years
<b><u>Corporations</u></b>		
Taxable Income Limitation	10%	50%*
Carry-forward of Unused Contribution	5 years	15 years

\*100% for qualified farms

Note that if your family land is in a corporation, the previous tax law made it very difficult to get the full value of the deduction from a conservation easement gift. That has changed. Under the Pension Protection Act of 2006 corporations are treated equally with individuals. Also, under the new law, qualified farms can offset up to 100% of annual adjusted gross income for the gift of a conservation easement. Lands held in a corporation or as part of a qualified family farm are special but important cases, and we encourage you to contact the Conservancy directly as well as to seek professional advice if you qualify under these rules.

# Learning More: A Quick Primer on the New Tax Rules

## Changes in State Tax Law: PA 446 – Elimination of the “Pop-up Tax” on Conservation Easement Land

When the State of Michigan reformed its school financing system in 1994, sweeping changes were made to the property tax system in the state. The changed property tax law included a provision that limited the rate of increase in real estate valuation on which an individual's property taxes are based to 5% per year or the annual rate of inflation, whichever is less.

However, Michigan Property Tax law states that the basic rate on which taxes are levied (the State Equalized Value or SEV) is to be set at 50% of the Fair Market Value (FMV) of the property. FMV is established based on sales of similar properties each year. So while Taxable Values cannot rise at a rate in excess of 5% per year, the State Equalized Value for a given parcel rises at a rate based on the local real estate market, usually well in excess of 5% each year. If you own land in Leelanau County, where market forces have been driving a rapid run-up in real estate values for several decades, the average Taxable Value of most parcels is just a fraction of their State Equalized Value.

What does this mean to you? First, if you've owned your property for many years, a look at your tax bill will undoubtedly show that your State Equalized Value is much higher than your Taxable Value. Your actual property taxes in a given year are based on multiplying the lower Taxable Value by the prevailing millage rate in your township. Now here comes the problem. When you transfer the land to a new owner, whether by sale or by a bequest or gift to your children, the property tax law states that the taxes must “pop-up” to the State Equalized Value, which is set at 50% of Fair Market Value. What it means for you as a property owner is that your heirs or whoever you may sell to will usually be paying 3 to 5 times the annual property taxes that you've been paying. This simple fact has created a log-jam of family lands that cannot be transferred from one generation to the next because the new owners simply cannot afford the

vastly increased property taxes. You may be one of these property owners.

Now to the point: PA 446 exempts from the “pop-up” tax lands subject to a qualified conservation easement. The law as previously written allowed certain types of transfers to be made without taxes popping-up. For instance, a husband could transfer land to his wife without the tax increasing. In 2000, in response to prodding from the Leelanau Agriculture Alliance and others, Senator George McManus introduced legislation that would exempt farmland from the pop-up tax. Now, with the passage of PA 446, a property owner can prevent property taxes from skyrocketing when land is passed down in the family by donating a conservation easement over qualifying land.

To understand what this might mean in your situation, simply consult your tax bills to check the difference between Taxable Value and your State Equalized Value. As you read on, we will give specific examples of the impact of this legislation, and how, especially when coupled with the new federal income tax provisions, it presents a great opportunity to lock-in both tax deductions and lower property taxes going forward.

### Definitions

**State Equalized Value (SEV):** by definition 50% of the Fair Market Value of your property. This number is based on comparable sales of similar land in your locale.

**Taxable Value (TV):** The State Equalized Value of land, since 1994 or the last date of transfer, plus annual adjustments for the rate of inflation or 5%, whichever is less. Your tax bill in a given year is based on this number.

**Millage Rate:** The rate at which local taxes are levied for various services such as schools, local and state government, and other extra-voted services. Taxable Value x Millage Rate = Annual Property Tax

## A Landowner's Story

### "A Vehicle for Us to Meet our Objectives"

**When Bob and Eleanor Miller bought their 160 acres in Centerville Township back in 1977, there were only a handful of people living year round in their neighborhood.** Bob, a psychiatrist, had just taken a job at the Traverse City State Hospital. Eleanor, who has a Masters in social work, had strong ties to the area; her family had carried on a tradition of summering in Leland that had begun with her ancestors in the early 1900s.

Although they considered themselves "city people," the Millers fell in love with the land and the idea of living just up the hill from South Lake Leelanau. They hoped for children eventually and viewed their 160 acres as a "quiet, safe place where kids could just be immersed in nature," says Eleanor. The weathered barn on the property was also a selling point: Eleanor had grown up with horses and wanted them in her life again.

They lived in a circa 1900s farmhouse on the property for eight years. A woodstove sufficed for heat; the house had no insulation. In time, they had a son, then a daughter, and built a simple, energy-efficient ranch house up a slight rise behind the farmhouse, but in a valley where it is protected from the winds. Eleanor got her horses, (there are now 11 in the barn) and began to volunteer as a 4-H leader. The old logging trails on the property made for good riding and wildflower hikes. Today, 4-H kids bunk in the old farmhouse for the week-long summer riding camps Eleanor hosts.

Among the land's other features: spectacular views of Lake Leelanau provided by many vantage points on their property, along with a mature and ecologically diverse northern beech-maple hardwood forest. A tributary of Rice Creek, which drains into South Lake Leelanau, runs through the Millers' northwestern corner. The creek provides valuable habitat for many species of plants and animals. "All of these features combined make it a significant contributor to the health of the Lake Leelanau Watershed," says Matt Heiman, Conservancy Land Protection Specialist.

The Millers' part of the county was so unpopulated when they first moved here that they weren't even on the school bus route. That would soon change. "All of a sudden Rosinski Road got developed and paved," says Eleanor. "Houses started going up and we saw how quickly and easily land can be divided and developed."

They knew from the start that they wanted most of



Bob and Eleanor Miller, who donated two conservation easements on 120 acres in Centerville Township.

their land to remain undisturbed forever. As time passed and they saw more land around them developed, the Millers knew they wanted to do something that would permanently protect a large portion of their land.

In 2001 they donated a conservation easement on 60 acres and donated a second 60-acre easement in 2005, "so we could take the tax benefits in phases," says Bob.

Though not the impetus for protecting their land, the tax benefits that come with giving up development rights were an added plus, says Bob. He adds that they are leaving 40 acres unrestricted to keep their options open.

"It was a no-brainer when the Conservancy emerged, and we realized we could have someone advocate for our wishes," says Bob. "When you are younger you think you are going to be here forever. But we're not, and we like that the Conservancy can provide a structure to protect the land long after we're gone. It became the vehicle for us to meet our objectives."

The Millers say they would be happy to talk to any landowner who wants to ask questions of someone who has done a conservation easement. "Our experience over the 10 years we have worked with the Conservancy is that they have been really flexible," says Bob. "The easement allows you to use the land in the way you want. What I'd like to see is a concerted effort of neighbors working together to protect large blocks of land. If we don't, this will all end up subdivided into a sea of houses."

# Getting Started: Understanding Conservation Easements

A conservation easement is a legal agreement between a landowner and the Leelanau Conservancy that permanently limits a property's uses in order to protect its conservation values. These agreements are not a new concept in property law, as similar agreements have been in force all across the United States since the late 1800's. However, conservation easements were a rarity in Michigan before 1990. They are not a rarity any longer, and the Leelanau Conservancy has received over 90 conservation easements since its founding in 1988.

## How Conservation Easements Work

When you own land, you also "own" many rights associated with it. These property rights include the right to harvest timber, build structures, grow crops, and so on (subject to zoning or other land use restrictions). When you grant a conservation easement to the Conservancy, you permanently give up some of those rights and retain others. For example, you might give up the right to build additional residences while retaining the right to grow crops or harvest timber. Future owners are also bound by the conservation easement's terms.

Conservation easements can be used to protect a wide variety of land including farms, forests, wildlife habitat, and properties with scenic views. Conservation easements are drafted in a detailed legal format that spells out the rights and restrictions on the owner's uses of the property as well as the rights and responsibilities of the Leelanau Conservancy.

*"I would recommend that anyone who is considering protecting their land should not hesitate to work with the Conservancy. They have a great staff and working with them has been a rewarding experience for us."*

—Roger Newton, who with his wife, Coco, protected 88 acres of farmland on Jelinek Road near Gills Pier that overlooks the Manitou Passage.

## Key Advantages of Conservation Easements

- Leaves the property in private ownership, and owners may continue to live on it, sell it, or pass it on to heirs.
- No public access.
- Flexible, can be written to meet the particular needs of the landowner while protecting the property's resources.
- Permanent, remaining in force when the land changes hands.
- Can provide very significant income tax, property tax, and estate tax benefits – often making the difference between families being able to retain land in their ownership, or being forced to sell because of high property and/or estate taxes

## Easements Are Flexible

The landowners and the Conservancy tailor the easement terms to protect the land's conservation values and to meet the needs of the landowner. Thus, each easement is a unique document. Generally, limitations are made on the number and location of structures and types of land use activities that can take place.

The Conservancy cannot accept an easement that does not meet our conservation standards. And, in order to receive the federal and state tax benefits from donation of a conservation easement, the gift must meet a "conservation purposes" test codified in federal law. The good news is that Conservancy acceptance criteria are developed to comply with the federal conservation purposes test, and the standards are met in different ways on different properties. For example, a farm might be protected by an easement that allows continued farming and additional clearing of woodlands for agriculture. For a property containing habitat for a rare species, an easement might prohibit development of any kind. Working forestland easements typically allow for sustainable timber harvesting under the guidance of a forest management plan.

The following are examples of common easement provisions.

### Commonly Reserved Rights

- The right to use the property for all purposes not inconsistent with the purposes of the easement.
- The right to sell, give or otherwise convey the property (subject to the easement).
- The right to replace or add on to the existing buildings.
- The right to construct specified and limited additional structures.
- The right to harvest timber under an approved forest management plan.

### Common Restrictions

- No buildings allowed except those specified above.
- Tree cutting restricted to removing dead, diseased or dangerous trees or exotic and nuisance species.
- No draining or filling of wetlands.
- No surface mining.
- No industrial or commercial use of the property. (In-home commercial use acceptable)
- No dumping trash or hazardous waste.
- No advertising billboards.
- No further division of the property (except under guidelines set out by the landowner).
- No motorized off-road vehicles (except under guidelines set out by the landowner).


A conservation easement can serve as a flexible tool in a family's financial planning. The easement may apply to just a portion of the entire property, and it can allow some building within the area under easement, if that is compatible with the easement's conservation objectives. More can be learned by consulting [www.theconservancy.com](http://www.theconservancy.com) and clicking on Preserving Your Own Land and the Commonly Asked Questions.

## Donating a Conservation Easement

Once a landowner has indicated an interest in conveying a conservation easement to the Leelanau Conservancy, a number of steps are required to complete the transaction. Some key steps are:

- Tour the property to determine whether an easement is appropriate.
- Conservancy staff and board conduct preliminary evaluation.
- Landowner advised to consult appropriate legal and tax counsel.
- Negotiate restrictions and draft conservation easement document.
- Obtain basic title and mortgage information.
- Prepare Baseline Documentation (a summary report on the condition of the property).
- Obtain a "qualified appraisal" to substantiate the value of the donation.
- Sign and record final version of conservation easement document.

All conservation easements require action by the Conservancy's Board of Directors. Generally, the whole process from initial contact to signing takes from two to six months. As the landowner you need to make key decisions, but the majority of the work is performed by Conservancy Staff.



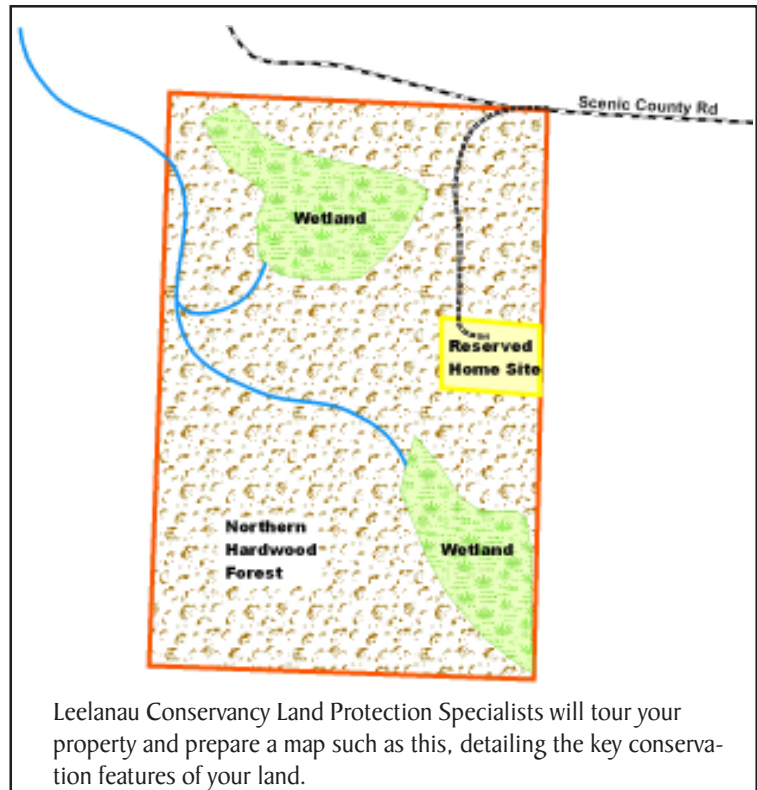
*"We have to recognize that wetlands are the most endangered type of land form in Michigan and throughout America. ...We have laws that are supposed to protect them in theory, but as individuals we need to do it ourselves. Tax relief wasn't my primary motivation, but (placing a conservation easement on our property) certainly turned out to be advantageous. Let's just say it made my tax accountant very happy."*

*--Phil VonVoigtlander, who with his wife, Barbara and neighbors Al and Betty Kohler, protected 30 acres of prime wetland near Northport.*

# Getting Started: Understanding Conservation Easements

## Qualifying for an Income Tax Deduction

The donation of a conservation easement must meet certain requirements of the tax code to qualify under the law as a tax-deductible gift. These requirements include a provision that the easement must be donated in perpetuity. It must also be donated to a qualified charitable organization, such as the Leelanau Conservancy. In addition, it must be donated exclusively for conservation purposes, such as the protection of natural habitat for wildlife or the preservation of farmland or forestland which provides a significant benefit to the public. In essence, the income tax deduction is reserved for the protection of significant conservation resources.



## The Size of the Income Tax Deduction

For income tax purposes the value of the easement is the difference between the value of the land “as is” and its value with the conservation easement restrictions, otherwise known as the “before” and “after” values. These values must be determined by a qualified real estate appraiser. When Congress passed the new legislation in 2006, providing for greatly expanded incentives for conservation easement gifts, it also tightened up the rules for appraisals. It is extremely important to have a highly qualified real estate appraiser establish the value of the gift and to thoroughly document the appraisal procedure. Fortunately, the Grand Traverse region has a number of experienced appraisers capable of valuing conservation easements. We would be happy to provide a list.

To understand how the new federal income tax incentives in the Pension Protection Act of 2006 and the new property tax limiting features of PA

446 might apply to any given situation you have to “run the numbers.” There is no substitute for detailed tax planning with professional help. However, it is quite possible to use examples from real life situations in Leelanau County to begin to get a grasp of how these tools can be used to protect your family land while saving money on taxes over many years.

*“The peace and beauty of the land is what attracted everyone to it, and made them want to preserve it. The magic was there; it was just waiting to happen. It was wonderful working with the Conservancy. (Director Brian Price) just never pushed but he was always available, and urged us to take our time. We feel like we have a very good easement plan.”*

—Carol Waters and friends, who preserved 109 acres in Kasson Township that includes most of Gilbert Lake.

## Case Study – Eighty Acre Woodlot

The Jacksons own eighty acres of forested land in Leelanau County which was purchased in 1975. Over the years the land has appreciated in value from the \$600-per-acre purchase price to a value of \$8,500 per acre today. The Jacksons live nearby, hunt in the fall, cut firewood from the woods, and carefully manage the property for selective harvest of timber every 15 years or so. Current property taxes are \$750 per year.

Now in their early 60's, the Jacksons have grown to love this family property and would like to pass it along to their three children. However, property taxes would be around \$6,000 per year if

the land is passed on to the children with all development rights intact. Harvest of timber from the property will help pay for some of the taxes, but there will be little if anything left over. In order to make sure that there is value in the land once it is transferred to the children, the Jacksons would always want to reserve one homesite.

The Jacksons looked at donating a conservation easement several years ago, but found that they would not be able to fully use the tax deduction available under the old rules. Is now the right time?

Below, you can see how these landowners benefit from the new tax law:

<b>Eighty Acre Woodlot - Impact of Conservation Easement Gift on Federal Income Tax</b>			
<b>Facts</b>			
Filing Status: Joint	<b>Value of Property:</b>		
Adjusted Gross Income (AGI): \$100,000	Highest & Best Use:	\$680,000	
Marginal Tax Rate: 25%	Conserved with One Home Site:	\$240,000	
Property Size: 80 Acres (Non-Farm)	Charitable Contribution:	\$440,000	
<b>Calculations</b>	<b>Old Law</b>	<b>New Law</b>	<b>Difference</b>
Adjusted Gross Income	100,000	100,000	0
Limitation on Charitable Cont	30% AGI (\$30,000)	50% AGI (\$50,000)	+20,000
Year 1 Contribution Deduction	30,000	50,000	+20,000
Year 2 Contribution Deduction	30,000	50,000	+20,000
Year 3 Contribution Deduction	30,000	50,000	+20,000
Year 4 Contribution Deduction	30,000	50,000	+20,000
Year 5 Contribution Deduction	30,000	50,000	+20,000
Year 6 Contribution Deduction	30,000	50,000	+20,000
Year 7 Contribution Deduction	not	50,000	+20,000
Year 8 Contribution Deduction	available	50,000	+20,000
Year 9 Contribution Deduction	<u>          </u>	<u>40,000</u>	<u>+40,000</u>
Total Deduction	180,000	440,000	+260,000*
Income Tax Rate	x	25%	
Tax Savings	<u><b>45,000</b></u>	<u><b>110,000</b></u>	<u><b>\$65,000 **</b></u>
* Old law: Unused Contribution = \$260,000 Deductions may be carried forward for only 5 years beyond the initial year			
New Law: Deduction maximized after 9 years. If needed, deductions could be taken for up to 16 years.			
<b>**Additional Tax Savings Under New Law \$65,000</b>			

## Case Study – Eighty Acre Woodlot (con't)

Note that under the old law a gift valued at \$440,000 would have generated \$65,000 in real tax savings, but \$260,000 in unused deduction was a major disincentive. Under the new law the gift is entirely deductible (even if the Jackson's income level declines) for an additional tax savings of \$65,000.

But lets not stop there. The biggest problem for the Jacksons in being able to transfer the property to their children is the fact that taxes will "pop-up" upon transfer to about five times the current rate. The children may not be able to afford to own the property without having to sell at least a portion if not all of the property to pay future taxes. PA 446 helps to solve this problem

because it allows a landowner – through the gift of a conservation easement – to "lock-in" future property taxes at the present rate plus the annual adjustment for inflation. In effect, the children (or any other subsequent owner) get the same tax treatment that the current owner enjoys.

How much is this worth? In effect it has the same value as an annuity or other income-generating instrument that would pay out \$5,250 per year. Accountants deal with this all time so we asked one to run the numbers, assuming an annual benefit of \$5,250 for 25 years.

Here is where PA 446 comes in. The following are real numbers, only slightly rounded off for simplicity:

### 80 Acre Woodlot - Impact of Conservation Easement Gift on Future Property Taxes

**Facts:**

Property Size: 80 Acres (Non-Farm)  
 Taxable Value: \$43,000  
 State Equalized Value (SEV): \$340,000  
 Current Property Taxes: \$750

	<i>Old Law</i>	<i>New Law</i>
Annual Property Taxes After Transfer	\$6,000	\$750
<b>Annual Savings from New Law:</b>	<b>\$ 5,250</b>	
<b>Property Tax Savings over 25 years:</b>	<b>\$140,000</b>	

Now lets put the two major tax incentives together.

- The Jacksons can expect to save about **\$110,000 in income taxes** from the gift of a conservation easement (see page II).
- The present value of **reduced property taxes** over 25 years is estimated to be about **\$140,000**.
- So the gift of a conservation easement which reduces the value of land by \$440,000 would generate **real tax savings of \$250,000**.

## A Landowner's Story: A Love Affair With the Tip

**The year was 1963.** Dick and Rosemary "Posy" Shuster were expecting their third child, and hadn't taken a vacation in seven years. "We didn't have a lot of money," says Dick, a retired judge from Hastings, Michigan. "A friend told us we ought to go on up to the Leelanau State Park, and said, 'Why, if you enjoy it, leave a contribution with George Anderson at the IGA there,'" adds Dick. "That sounded good to me."



The Shusters loved the peace and solitude at the tip of the Peninsula. Labor Day weekend, they went back, this time with a new baby and two other families in tow.

One afternoon, the men wandered off on a hike. They found themselves on a spectacular little peninsula, just a stone's throw from the then-operational Grand Traverse Lighthouse. The Fox Islands lay before them; to the east stretched miles of rocky shoreline, strewn with Petoskey stones. On their way to the beach they'd passed a hardwood forest filled with rare wildflowers and a coastal marsh flush with blue heron and songbirds. "It was like a little piece of heaven," says Dick.

On the way back to camp, the men spotted a for-sale sign. Dick was possessed with the thought of buying the land. He arrived at their tent and told Posie: "I've found something perfect for both of us."

"You can look at nothing but the lake," he told his wife, "and I can watch the island and the freighters going past." Later that day, Dick went to town to see about the property.

That was the beginning of a 40-year love affair with the land – a love affair that endures today. Over time, the Shusters would acquire 1,000 feet of shoreline, 23 acres – and two land contracts.

"I was a struggling young lawyer with three kids and a wife," says Dick, "trying to start a country law practice." When the land contract payments came due every year, inevitably he had to borrow the money. Somehow, they always managed

to pay the loan payments. "We did it a dollar at a time," says Posy.

What they got in return is decades of family memories spent camping on the land. Among them: digging a "bathtub" for the kids near the shore that would fill with lake water and be warmed by the sun, roasting fresh sweet corn

over a bonfire, making dribble castles with the kids on the narrow strip of sand at the water's edge, collecting Petoskey stones.

Even when the Shusters could afford to build a home there, it was never in their plans. "One of my least favorite things in life is keeping house," says Posy, "and I'm not about to do it on vacation!" She and Dick are adamant that the land be left just as they found it 40 years ago. "Our intention is for this place to remain natural for the critters and the plants and for our family to get away from an electronic world," says Posy.

In 1996, with the help of the Leelanau Conservancy, the Shusters put about a third of the property into a conservation easement. In 2001, they added another third. The rest of the land was permanently protected in 2003. The Shusters' easement specifies that no structures may ever be built on the property.

The tents of the old days have given way to a more comfortable motor home, and the Shusters come North with their kids and grandkids as often as they can. "We are so grateful to have the land," says Posy, "and to be able to protect it. More and more, we see all the places we enjoyed as children and they are no longer open spaces. That is just devastating to us. One of the problems of the world, I think, is that people need to get away and look at life from a little farther distance. They need to be able to get to a place like this where life isn't quite so instant."

## Case Study – Shoreline Property with Cottage

Tom and Ellen Spencer have a cottage on a smaller inland lake that has been in Ellen's family since the early 1900's. Originally part of a farm that stretched down to the water's edge, the cottage property still has 1,200 feet of shoreline on the lake. About half of this shoreline is wetlands under the law, but there are at least three potential lakefront homesites in addition to the one where the old cottage sits.

Tom and Ellen don't want to sell or develop any of the property. They have two children, and aren't sure whether the children will live close enough to the area to keep the cottage in the

family, or whether they will sell it. The Spencers enjoy fishing and sailing on the lake, and when they look back at ¼ mile of wild shoreline in their ownership, they get great satisfaction from knowing that they are protecting irreplaceable wildlife habitat and fish spawning areas. Now in their 50's, with an annual income of \$125,000 per year, the Spencers look forward to retirement when they can spend at least six months every year on the lake. But, can they afford to keep the land undeveloped? They wonder about whether it may be necessary to sell off more lots.

### Shoreline Property with Cottage Impact of Conservation Easement Gift on Federal Income Tax

#### Facts

Filing Status: Joint  
Adjusted Gross Income: \$125,000  
Marginal Tax Rate: 25%  
Property Size: 45 acres, including  
1,200 feet of shoreline

Value of Property:  
Before Easement Value: \$1,500,000  
Restricted to no further development :  
After Easement Value: \$500,000

#### Calculations

	<u>Old Law (30%)</u>	<u>New Law (50%)</u>
Year 1 AGI	\$125,000	\$125,000
Year 1 Contribution Deduction	37,500	62,500
Year 2 Contribution Deduction	37,500	62,500
Year 3 Contribution Deduction	37,500	62,500
Year 4 Contribution Deduction	37,500	62,500
Year 5 Contribution Deduction	37,500	62,500
Year 6 Contribution Deduction	37,500	62,500
Year 7-16 Contribution Deduction		625,000
Total Deduction	225,000	1,000,000
Tax Savings	56,250	<b>250,000</b>
Unused Contribution	775,000	-

**Additional Tax Savings Under New Law \$193,750**

## Case Study – Shoreline Property with Cottage (con't)

The first thing to note is that, under the old rules, the Spencers could not come even close to using the full value of their very large conservation easement deduction. But under the new rules the full deduction is used up over the course of the total of 16 years. The total tax savings is \$250,000.

As to the property taxes, the situation is not quite as simple as in the first example, where the land would be totally undeveloped at time of

transfer. PA 446 exempts from the “pop-up” in property taxes vacant land subject to a conservation easement, but not houses and other buildings. In this case, 1/3 of the fair Market Value of the property is attributed to the cottage, while the remaining 2/3 is attributed to the vacant land. After transfer, the cottage value “pops up”, while the vacant land taxable value remains capped. See how the numbers work out for the shoreline property owner below:

Shoreline Property with Cottage Impact of Conservation Easement Gift on Future Property Taxes		
<b>Facts:</b>		
Property Size: 45 acres, including 1,200 feet of shoreline		
Taxable Value: \$162,000		
SEV: \$660,000 (1/3 Allocated to Cottage, 2/3 to Vacant Land)		
Current Property Taxes: \$4,100		
	<u>Old Law</u>	<u>New Law</u>
Annual Property Taxes After Transfer		
Cottage	\$5,568	\$5,568
Land	\$11,136	\$2,733
Total	\$16,704	\$8,301
<b>Annual Savings from New Law</b>	<b>\$8,403</b>	
<b>Property tax savings over 25 years</b>	<b>\$158,000</b>	

Similar to Example I, but adding the value of the Income Tax Deductions to the Value of the limitation on property taxes, we can see that the gift of a conservation easement valued at \$1,000,000 will produce **real tax savings of approximately \$408,000.**



## Some other important factors in considering the Donation of a Conservation Easement

### Reduction in Estate Taxes

Throughout the 1980's and 1990's, estate taxes posed an enormous problem for landowners. It became a fact of life that simply passing land on from one generation to the next would prove impossible for many families. At the time, any land with development potential could drive up the value of an estate beyond the \$600,000 exclusion available to an individual, and trigger serious estate tax consequences.

Beginning in 2006 the individual exclusion has gone up, and at present, each individual can pass on \$2,000,000 without paying estate taxes. Now ownership of a valuable parcel of land might still trigger estate taxes, but it is less often an issue.

One way to reduce the value of land so transfer will not be subject to estate taxes is to place a conservation easement on the land, and many gifts of conservation easements were driven in whole or in part by the need to reduce estate taxes.

The good news is that fewer land transfers are affected by estate taxes. The bad news is that the current law is set to expire in 2010, and while everyone assumes that Congress will take action before then to either do away with the estate tax altogether or amend it in some way, there is no way to know at this time what Congress will do.

It is safe to say that, when land is part of a valuable estate that will be subject to estate tax, there is still a very good reason to donate a conservation easement. However, this area is complex and very uncertain, and if you think that estate taxes will play into a decision about land, you should seek good legal advice.

### Sales of Conservation Easements

Conservation easements customarily are donated by landowners who are motivated to protect land for its intrinsic value, and sometimes because they want future generations to enjoy the land and its wildlife as the donor has. However, a

conservation easement is an interest in real estate, and like other interests in real estate it can be purchased as well. There are several situations where conservation easements are often purchased rather than donated.

Farmland preservation programs generally buy conservation easements from willing farmers. This is most often called Purchase of Development Rights (PDR). These agricultural conservation easements are usually purchased because working farmers are seldom in a position to donate conservation easements, and yet communities find that there is great value in preserving working landscapes and a stable local food supply.

Watershed protection is another community goal where purchase of conservation easements may be employed. In these cases critical water supplies and natural waterways may be of such great importance to communities that it makes sense to buy easements to protect wetlands and groundwater recharge areas rather than have to replace water sources in the future or spend money on expanded water filtration plants. Locally, the Clean Michigan Initiative has provided money for the Leelanau Conservancy to purchase conservation easements on critical wetlands in the Lake Leelanau and Glen Lake watersheds.

*"Personally, I would have been sick if there had been 40 houses put on this land. There's a beautiful hillside on the north end where I like to plant my backside and watch the world go by. Because of my arrangement with the Conservancy, I'll still be able to do that. We'll just leave it alone, let the trees grow. If it's well managed, our sons will be able to come out here and have as much fun as I did when I was a kid. To be honest, I thought the Conservancy was just a bunch of tree huggers who want to lock down the land where you can't even use it. But the more I talked to Matt (Heiman, land protection specialist with the Leelanau Conservancy), I found out I can do what I want. I just can't develop it."*

—Dennis Buffum, who with his wife, Misty, protected 80 acres of old growth forest shading the headwaters of several small streams near Cedar.

## Bargain Sales of Conservation Easements

Easements can be purchased at fair market value, but they most often are purchased for less than market value – producing what is known as a bargain sale. For tax purposes a bargain sale is treated as a “part sale/part donation.” When a conservation easement is sold at less than fair market value it can combine the income producing benefit of a sale with the tax-reducing benefit of a donation. The difference between the conservation easement’s value as established by an appraisal and its sale price is considered a charitable donation and can be claimed as an income tax deduction.

The charitable donation component of the bargain sales of a conservation easement is treated exactly the same as an outright gift under federal income tax rules. Since whether by sale or donation land restricted by a conservation easement is not subject to the “pop-up tax” under PA 446, the property tax advantages are identical to an outright donation.

For a bargain sale to be completed, the Conservancy or a unit of government must have money dedicated to buy conservation easements for a specific purpose. When funding is available, these situations can be very attractive arrangements for a landowner, providing income while at the same time providing tax benefits to shelter the income.

## IRC Section 2031 (c)

The Taxpayer Relief Act, passed in 1997, added a significant incentive for the donation of conservation easements on family lands. Under Internal Revenue Code (IRC) Section 2031(c) a qualified conservation easement donation allows for an additional exclusion of up to 40% of the value of the protected land for estate tax purposes up to a cash value of \$500,000. It also provides the opportunity for a qualified conservation easement to be donated by the heirs after the death of a loved one, but before the estate tax return is filed. For complete information on all aspects of this IRC section, landowners should consult a qualified tax advisor.

## Conservation Buyers

Sometimes land is restricted by a conservation easement as part of, or in close proximity in terms of timing, to the sale of property. These transactions usually involve either a seller who wants to protect property from over-development even though he or she needs to transfer property for financial reasons, or a buyer who has identified property that he or she wants to own and protect because of its conservation values. On occasion, the Conservancy may step in to buy property (for instance, land adjacent to a Natural Area), and then re-sell it with a conservation easement so the land remains protected.

If you are considering selling or buying land that you feel should be protected by a conservation easement you are encouraged to contact the Conservancy to discuss how to structure such a transaction properly, and to confirm that the land and the contemplated conservation easement would meet established acceptance criteria.

## A Word About Donating Land

This booklet is dedicated to a thorough explanation of conservation easements and the new income tax and property tax incentives for landowners to consider. However, in some cases, an outright donation of the owner’s entire interest in the property (the Fee Title) may be more appropriate. Sometimes, with the agreement of the donor, land donated in fee can be restricted and resold by the Conservancy subject to an appropriate conservation easement which limits its future use. Once again, contacting the Conservancy and visiting directly with a Land Protection Specialist who can help you explore all the options is the suggested course of action.

*“We had a wonderful experience working with the Conservancy. The idea of having our property split up into five or six lots was just unacceptable. Even if we had no tax break we would have done it anyway. It should look like that forever.”—Vik Theiss, who with his wife, Susan, protected a 71-acre hillside near Glen Arbor.*

## Meet Our Land Protection Staff

If you would like to explore the possibilities of preserving the land you love, our seasoned land protection staff is here to serve you. Over the last several years, Matt Heiman and Tom Nelson have worked closely with dozens of landowners like you to help them navigate the ins and outs of conservation easement projects. They approach each project with a “no-pressure,” collegial attitude and a sincere desire to help you achieve your conservation goals for your land. Give them a call and they will be happy to walk your property with you and listen to how your vision for your land can fit with the array of options and incentives discussed in this Handbook.

### **Tom Nelson, Land Protection Specialist**

Tom’s interest in conservation began at an early age, spending uncounted hours and days in the woodlands around his boyhood home in Ohio near Lake Erie. As a young adult, he witnessed the nearly complete destruction of those woodlands by poorly planned development. Tom’s profound sense of loss propelled him into conservation work. Since joining the Leelanau Conservancy in 2004, Tom has worked with farmers and other landowners all over Leelanau County, helping them to preserve the natural features of their lands. Most recently, Tom wrote the grant to the Michigan Natural Resources Trust Fund that secured \$2 million in state funding to protect 1400 feet of shoreline and 51 acres at the Tip of the Peninsula that will be added to the Leelanau State Park.

Tom graduated magna cum laude with a Master of Laws in environmental law and policy from Vermont Law School. His background includes working as a social policy advocate in Ohio, Washington D.C. and Lansing. He lives at the Tip of the Peninsula and currently serves on the Leelanau Township Planning Commission and the M-22 Scenic Heritage Route Committee. Tom enjoys spending time outdoors with his black lab, Ellie May, hiking, canoeing, snowshoeing, sea kayaking and cross country skiing.

Contact Tom at [tnelson@theconservancy.com](mailto:tnelson@theconservancy.com).



### **Matt Heiman, Land Protection Specialist.**

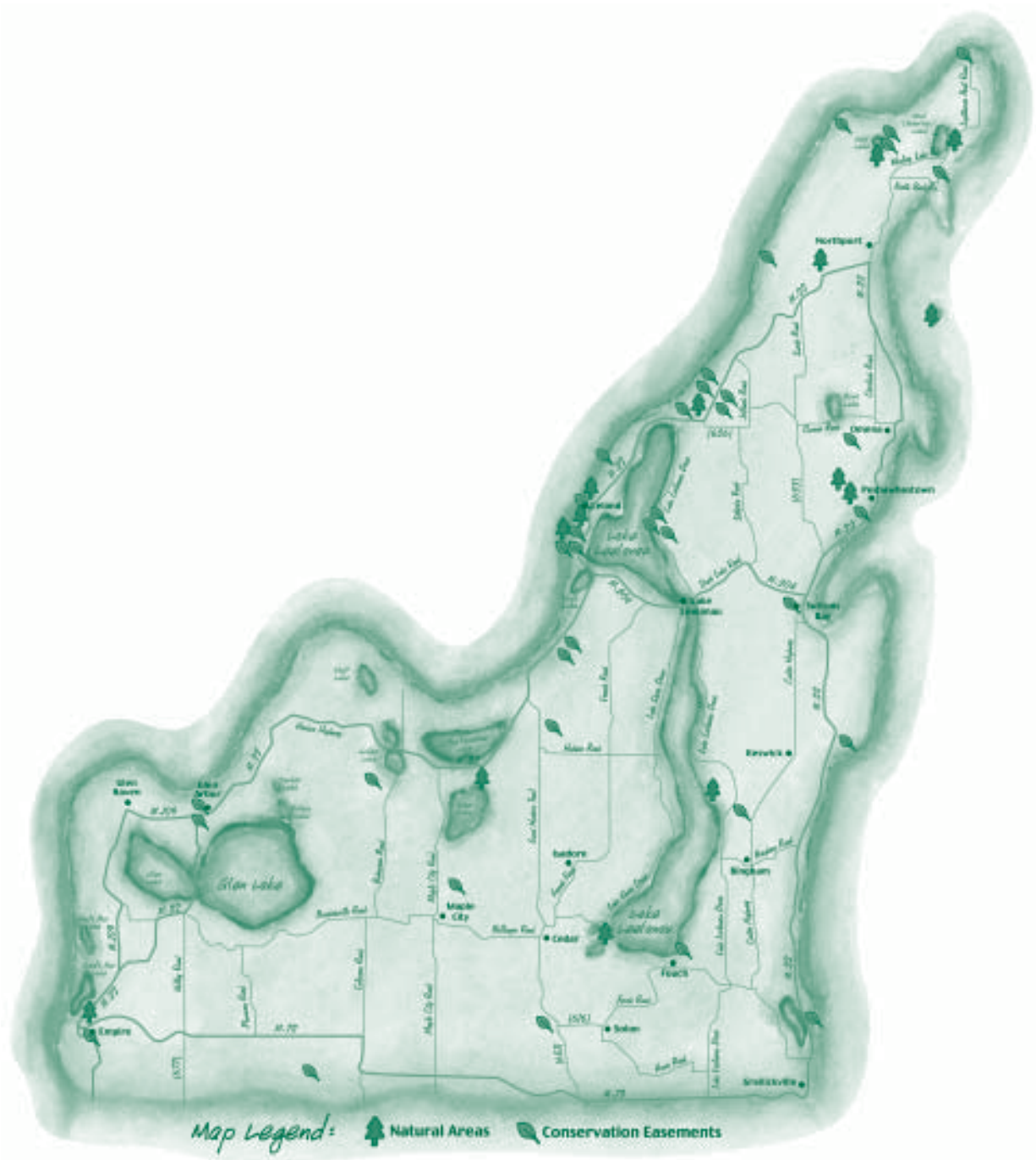
Matt’s passion for fishing drives his desire to see Leelanau’s most critical habitat and ecologically sensitive areas protected. His educational background in aquatic ecology (B.A. from Albion College (1994) and Master of Science candidate at CMU) helps him convey to landowners the value of their land from more than just a financial perspective. He joined the Conservancy in 2001 as a Land Protection Specialist and since then has completed several major land protection projects. Matt also co-wrote MDEQ-approved watershed management plans for the Lake Leelanau and Glen Lake/Crystal River watersheds, which have led to the Conservancy receiving over \$1,546,300 in Clean Michigan Initiative funds to purchase conservation easements over wetlands and forested areas critical to maintaining high water quality.

Prior to his work at the Conservancy, Matt worked as biological consultant performing stream restoration, fisheries population analysis, salmon spawning habitat restoration analysis, stream habitat mapping and macroinvertebrate studies in Michigan waters. He lives in Traverse City with his wife, son, daughter and two Polish lowland sheepdogs.

Contact Matt at [mheiman@theconservancy.com](mailto:mheiman@theconservancy.com)



“Migratory birds need habitat at both ends of their journey. We can’t do much to save the Rainforest, but we can save this. For us, this was a rare opportunity to be a part of such a vast system.”—*Ann McInnis, who with her husband Doug, and other neighbors nearby have protected 80 acres at the tip of the peninsula, helping to create large, safe-travel corridor for wildlife.*



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