Land Preservation Provides Estate Tax Benefits: Section 2031(c)

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I.
INTRODUCTION

In 1997, Congress created new estate tax benefits for landowners[1] who preserve land with a conservation easement. The new benefits allow for as much as a $500,000 exclusion from estate taxes. While private citizens and their beneficiaries will benefit from reduced estate taxes, the public stands to benefit the most from the new tax provision, because it provides incentive to preserve land for future generations. The 1997 Taxpayer Relief Act[2] added Section 2031(c)[3] to the Internal Revenue Code ("I.R.C."), providing for an estate tax exclusion for landowners who preserve their land with a conservation easement. A "conservation easement is a legal agreement a property owner makes to restrict the type and amount of development that may take place on his or her property. Each easement's restrictions are tailored to the particular property and to the interests of the individual owner."[4] This article first briefly provides an overview of conservation easements and their previous tax treatment. The article then focuses on a new section of the tax code, I.R.C. § 2031(c), its requirements and its administration.

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1. While most often thought of as benefiting non-commercial landowners, developers may also benefit from conservation easements. *See* Todd A. Etzler, *Conservation Easements in Real Estate Development,* 41-DEC RES GESTAE 24 (1997). *See also* Matthew J. Kiefer, *Creating Additional Tax Benefits from Qualified Conservation Easements*, 15 REAL EST. L.J. 136 (1986).

2. Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (codified as amended in scattered sections of 26 U.S.C.).

3. I.R.C. § 2031(c) (West Supp. 1998).

4. JANET DIEHL & THOMAS S. BARRETT, THE CONSERVATION EASEMENT HANDBOOK 5 (1988).

II.
CONSERVATION EASEMENT OVERVIEW

"Conservation easements are private land use restrictions designed to preserve open space and other environmentally significant resources."[5] Land preservation occurs when landowners voluntarily agree to place restrictions on their land, in the form of conservation easements. Such conservation easements are then donated to a governmental agency, foundation, or I.R.C. § 501(c)(3) organization.[6] Once a landowner donates the right to use the land in a certain manner, he or she has given up one of the proverbial sticks in his or her bundle of property rights. The donee organization then holds that stick in perpetuity. State statutes and the Uniform Conservation Easement Act have overcome traditional common law problems with conservation easements (e.g. ownership, enforcement, privity).[7] Because these common law impediments have been overcome, the benefits of conservation easements over traditional land preservation methods are numerous.

Several distinguishing characteristics make conservation easements improvements over traditional government land preservation. Conservation easements: (1) involve no government regulation; (2) are immune from the politics of open space legislation; (3) do not constitute a taking under the Fifth Amendment; (4) do not require fee simple purchase; (5) do not require maintenance or administration (e.g. parks); (6) are voluntary; (7) meet the needs of the private landowner; and (8) allow the landowner to retain ownership and control of the property.[8] The primary

5. John L. Hollingshead, *Conservation Easements: A Flexible Tool for Land Preservation*, 3 ENVTL. L. 319 (1997).

6. I.R.C. § 170(h)(3) (West Supp. 1998). I.R.C. § 170(h) describes the requirements for a property owner to receive favorable tax treatment for donating a conservation easement. *§ 501(c)(3) organizations are nonprofit organizations who have no stock, are prohibited from distributing profits to any interested individual and who may receive tax deductible charitable contributions. § 501(c)(3) organizations serve a variety of purposes; they promote the arts, health, education, science, religion, and charity.*

7. Hollingshead, *supra* note 5, at 335-36. The Hollingshead article provides a useful overview of the common law devices of easements, real covenants, and equitable servitudes. *Id.* at 326-32. The article also explains how state statutes and the Uniform Conservation Easement Act have overcome several common law impediments for land protection. *Id.* at 335-36.

8. *Id.* at 321-22.

cost to the government is decreased tax revenue, from reduced income, estate, gift, or property taxes.[9]

In some circumstances, placing a conservation easement on property provides for significant tax benefits. This article focuses on the charitable income tax deduction because it provides the foundation for exclusion under I.R.C. § 2031(c). The article also focuses on the estate tax provisions because it is these provisions of the tax code which have been changed to include the new I.R.C. § 2031(c) exclusion. While an owner may also receive real property tax[10] and gift tax benefits[11] for having a conservation easement placed on his or her property,[12] these tax benefits will not be discussed because they are not relevant to the new I.R.C. § 2031(c) estate tax exclusion.

A. *Charitable Income Tax Deduction*

Beginning in 1976, Congress enacted several tax provisions which allow a taxpayer to receive a charitable income tax deduction for donating a partial interest of land.[13] These provisions culminated in regulations issued by the Treasury Department in 1994.[14] The regulations provide valuable guidance in receiving a charitable deduction for those donating conservation easements.[15] Conservation easements qualify for favorable income

9. *Id.* at 323.

10. Jesse J. Richardson, Jr., *Maximizing Tax Benefits to Farmers and Ranchers Implementing Conservation and Environmental Plans*, 48 OKLA. L. REV. 449, 457-58 (1995).

11. JANET DIEHL & THOMAS S. BARRETT, *supra* note 4, at 57 (land with conservation easement has a lower value, and therefore lower gift tax rate). *See also* Hollingshead, *supra* note 5, at 357-58 (discussing gift tax of charitable donations of qualified conservation interests).

12. *See* JANET DIEHL & THOMAS S. BARRETT, *supra* note 4 at 51 (overview of tax benefits, appraisal procedures, and checklist for determining whether easement meets conservation purposes required by I.R.C. § 170(h). A cautionary note however, the book was published in 1988 and is therefore somewhat out of date). *See also* STEPHEN J. SMALL, THE FEDERAL TAX LAW OF CONSERVATION EASEMENTS (1986) (also out of date).

13. Michael C. Spata, *A Practical Approach to the Deductibility of a Charitable Contribution for a Qualified Conservation Easement*, 22 REAL EST. L.J. 132, 133-35 (1993) (overview of legislative history of deductibility of conservation easements).

14. *Id.* at 135. The regulations can be found at 1.170A-14. Treas. Reg. § 1.170A-14 (as amended in 1994).

15. Michael C. Spata, *supra* note 13, at 135. *See also* STEPHEN J. SMALL, *supra* note 12 (providing comprehensive, annotated commentary on each section and subsection of the 1.170A-14 regulations)

tax treatment if they meet the rigorous requirements of I.R.C. § 170(h).[16]

Section 170 allows the taxpayer a deduction for any charitable contribution.[17] Section 170(f)(3) disallows a deduction for the contribution of a partial interest in property,[18] except for a "qualified conservation contribution."[19] A qualified conservation contribution is defined in I.R.C. § 170(h) as a contribution: (1) of a qualified real property interest;[20] (2) to a qualified organization;[21] (3) exclusively for conservation purposes.[22] Thus, in order for a conservation easement to receive favorable tax treatment of any kind, the easement must first satisfy the requirements of I.R.C. § 170(h).[23] Once the conservation easement has satisfied the requirements of I.R.C. § 170(h), the landowner may receive an income tax deduction for the loss in value resulting from the restricted use.

B. *Estate Tax Reductions*

When the landowner dies, estate tax is generally calculated for land based on the "property's 'highest and best use'—the most profitable use at the time of the owner's death."[24] By creating a conservation easement, the "uses to which the property can be put are limited forever. This usually reduces the estate's value and thus reduces estate taxes."[25] Before I.R.C. § 2031(c) was enacted, there was "no estate tax exclusion for the value of land

16. I.R.C. § 170(h) (West Supp. 1998).

17. I.R.C. § 170(a)(1) (West Supp. 1998).

18. I.R.C. § 170(f)(3) (West Supp. 1998).

19. I.R.C. § 170(f)(3)(B)(iii) (West Supp. 1998).

20. I.R.C. § 170(h)(1)(A) (West Supp. 1998). Qualified real property interests include restrictions on use which are granted in perpetuity. I.R.C. § 170(h)(2)(C) (West Supp. 1998).

21. I.R.C. § 170(h)(1)(B) (West Supp. 1998). Qualified organizations include governmental units, § 501(c)(3) organizations, and foundations exempt under I.R.C. §§ 509(a)(2) and (a)(3). I.R.C. § 170(h)(3) (West Supp. 1998).

22. I.R.C. § 170(h)(1)(C) (West Supp. 1998). Conservation purposes include the preservation of land for outdoor recreation or the education of the public; protection of habitat or ecosystems; preservation of open space for scenic enjoyment or pursuant to a clearly delineated conservation policy; or "the preservation of an historically important land area or a certified historic structure." I.R.C. § 170(h)(4)(A) (West Supp. 1998).

23. Income tax deduction allowed pursuant to I.R.C. § 170(a)(1) (West Supp. 1998); estate tax deduction allowed pursuant to I.R.C. § 2055(f) (1994).

24. JANET DIEHL & THOMAS S. BARRETT, *supra* note 4, at 55.

25. *Id.* at 56.

subject to a qualified conservation easement."[26] I.R.C. § 2031(c) has added a potentially valuable estate tax exclusion for qualifying donees.

III.
I.R.C. SECTION 2031(c)

A. *Overview*

I.R.C. § 2031(c) was passed as part of the Taxpayer Relief Act of 1997.[27] In enacting the law, Congress hoped that "a reduction in estate taxes for land subject to a qualified conservation easement [would] ease existing pressures to develop or sell off open spaces in order to raise funds to pay estate taxes, and [would] thereby help to preserve environmentally significant land."[28] I.R.C. § 2031(c) says in short,

> [I]f you have land subject to a conservation easement that meets requirements of Section 170(h), and if you own that land when you die, and if you meet the additional requirements of this section [2031(c)], then you can exclude from your estate *a percentage of the value of that land in addition to* the reduction in value already attributable to the easement.[29]

This important new provision provides for tax benefits which should be part of estate planning and land conservation strategies. The remainder of this article focuses on the requirements, administration and benefits of the new provision.

B. *Requirements of I.R.C. § 2031(c)*

If the donee is to receive an estate tax exclusion, there must be a qualified conservation easement on his or her property.[30] A qualified conservation easement is very similar to an I.R.C. § 170(h) "qualified conservation contribution."[31] However, § 2031(c) adds more strict requirements than I.R.C. § 170(h) including: (1) the conservation easement may not be for preserva-

26. RESEARCH INSTITUTE OF AMERICA, TAXPAYER RELIEF ACT OF 1997 141 (Research Institute of America 1997).

27. Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (codified as amended in scattered sections of 26 U.S.C.).

28. RESEARCH INSTITUTE OF AMERICA, *supra* note 26, at 141.

29. Stephen J. Small & Timothy Lindstrom, *New Tax Act Incentives Make Easements More Attractive,* EXCHANGE, Fall 1997, at 14.

30. I.R.C. § 2031(c)(8)(B) (West Supp. 1998).

31. I.R.C. § 170(h) (West Supp. 1998).

tion of a historical area or historical structure;[32] (2) the donee may not retain more than the right to de minimis commercial recreational use;[33] and (3) the donee may retain mineral interests only if the probability of surface mining is so remote as to be negligible.[34]

In addition to the above requirements, there are very specific requirements about the location of land eligible for the exclusion. On the date of the decedent's death, the land must be located:[35] in or within twenty-five miles of an area which is a metropolitan area;[36] in or within twenty-five miles of a national park or wilderness area;[37]or in or within ten miles of an area which is an Urban National Forest.[38]

While this appears to be a stringent requirement, "it is believed that this covers about half of the land in the 48 contiguous states and almost all the land on the East and West Coasts!"[39] Furthermore, the land must have been "owned by the decedent or a member of the decedent's family at all times during the 3-year period ending on the date of the decedent's death . . . ."[40]

32. An I.R.C. § 2031(c) "qualified conservation easement" means a "qualified conservation contribution (as defined in § 170(h)(1)) of a qualified real property interest (as defined in § 170(h)(2)(C)), except that clause (iv) of section 170(h)(4)(A) shall not apply . . . ." I.R.C. § 2031(c)(8)(B) (West Supp. 1998). Clause (iv) provides for a charitable deduction for "preservation of an historically important land area or a certified historic structure." I.R.C. § 170(h)(4)(A)(iv) (West Supp. 1998).

33. A § 2031(c) "qualified conservation easement" means a "qualified conservation contribution (as defined in § 170(h)(1)) . . . and the restriction on the use of such interest described in § 170(h)(2)(C) shall include a prohibition on more than a de minimis use for a commercial recreational activity." I.R.C. § 2031(c)(8)(B) (West Supp. 1998).

34. I.R.C. § 170(h)(5)(B)(ii) was amended allowing for the retained negligible rights to mineral interests. I.R.C. § 170(h)(5)(B)(ii) (West Supp. 1998). Under prior law, a charitable deduction was only available if the mineral interests were separated from the land prior to June 13, 1976. RESEARCH INSTITUTE OF AMERICA, *supra* note 26 at 1959.

35. I.R.C. § 2031(c)(8)(A)(i) (West Supp. 1998).

36. I.R.C. § 2031(c)(8)(A)(i)(I) (West Supp. 1998).

37. I.R.C. § 2031(c)(8)(A)(i)(II) (West Supp. 1998).

38. I.R.C. § 2031(c)(8)(A)(i)(III) (West Supp. 1998).

39. Ronald D. Aucutt, *1997 Tax Law Changes: Selected Provisions of Interest to Estate Planners and Their Clients*, SC28 A.L.I.-A.B.A. 753, 781 (1997).

40. I.R.C. § 2031(c)(8)(A)(ii) (West Supp. 1998).

C. *Administration of I.R.C. § 2031(c)*

1. Overview

There are no regulations offering explanation of I.R.C. § 2031(c). The statute applies to estates of persons dying after December 31, 1997[41] and therefore should be considered in current estate planning. Those landowners who have donated a conservation easement in the past should also review their estate plans to assure compliance with and the maximum benefits from the new provision.[42] One of the costs of I.R.C. § 2031(c) is that planning after death has become much more complicated.[43] This section looks beyond the basic requirements of I.R.C. § 2031(c) and looks to what the statute requires for administration of the provision.

2. Exclusion Amount

After the death of the landowner, the executor elects to exclude the qualified conservation easement from the value of the estate on the estate tax return imposed by § 2001.[44] Once made, the election is irrevocable.[45] The election allows the executor to exclude the lesser of:[46] (1) the applicable percentage of the value of the land subject to a qualified conservation easement ("applicable percentage")[47] *or* (2) the exclusion limitation.[48]

To determine which amount will be excluded, the executor must determine whether the applicable percentage or the exclusion limitation is smaller; the smaller amount is the allowed exclusion. The applicable percentage is a complicated formula designed to discourage marginal easements which "don't reduce the value of [the] land very much."[49] The applicable percentage is determined through a series of three calculations. A hypothet-

41. H.R. CONF. REP. No. 105-220, at 403 (1997), *reprinted in* 1997 U.S.C.C.A.N. 1213, 1215.

42. Stephen J. Small & Timothy Lindstrom, *supra* note 29, at 14.

43. *Id.* at 18.

44. I.R.C. § 2031(c)(6) (West Supp. 1998).

45. *Id.*

46. I.R.C. § 2031(c)(1) (West Supp. 1998).

47. I.R.C. § 2031(c)(1)(A). The "applicable percentage" means "40 percent reduced (but not below 0) by 2 percentage points for each percentage point (or fraction thereof) by which the value of the qualified conservation easement is less than 30 percent of the value of the land (determined without regard to the value of such easement and reduced by the value of any retained development right . . . .)." I.R.C. § 2031(c)(1)(B) (West Supp. 1998).

48. I.R.C. § 2031(c)(1)(B) (West Supp. 1998).

49. Stephen J. Small & Timothy Lindstrom, *supra* note 29, at 15.

ical example will be used to illustrate each calculation. The first calculation determines the value of the land subject to the easement; the value is determined by including any reduction in value attributable to the easement.[50] For example, if a landowner has property worth one million dollars and donates a conservation easement worth $300,000 to the Nature Conservancy, restricting the right to develop wetlands on the property, the property would be worth $700,000 (1,000,000 - 300,000 = 700,000). Thus, the first figure in calculating the applicable percentage is $700,000.

The second calculation necessary to determine the applicable percentage requires adding back in to the first figure the value of any retained development right.[51] Because a landowner can craft the conservation easement to his or her liking, an owner may reserve development rights for the future. However, to the extent development rights are reserved, the value of any exclusion is reduced.[52] Using the previous example, if the landowner reserved the right to build five homes, this may increase the value of the land from $700,000 to $800,000.[53]

The third and final calculation for determining the applicable percentage is an actual determination of the percentage. The applicable percentage means "40 percent reduced (but not below zero) by 2 percentage points for each percentage point (or fraction thereof) by which the value of the qualified conservation easement is less than 30 percent of the value of the land (deter-

50. I.R.C. § 2031(c)(1)(A) (West Supp. 1998) (the value of the land subject to the easement, "reduced by the amount of any deduction under § 2055(f) with respect to such land"); I.R.C. § 2055(f) is the estate tax provision allowing the value of the conservation easement to be deducted from estate tax. I.R.C. § 2055(f) (1998).

51. I.R.C. § 2031(c)(2) (West Supp. 1998).

52. § 2031(c)(5)(A). "'Development right' means any right to use the land subject to the qualified conservation easement for any commercial purpose which is not subordinate to and directly supportive of the use of such land as a farm for farming purposes (within the meaning of § 2032A(e)(5))." I.R.C. §2031(c)(5)(D) (West Supp. 1998). Examples of use of the land as a farm for farming purposes include tree farming, ranching, viticulture, and the raising of other agricultural or horticultural commodities. H.R. CONF. REP. No. 105-220, at 402 (1997), *reprinted in* 1997 U.S.C.C.A.N. 1213, 1214.

53. Appraisal of land subject to an easement is an extremely complicated procedure. The figures used herein are not meant to be accurate, they merely illustrate the statutory principles. *See* Stephen J. Small and Timothy Lindstrom, supra note 12, at 17 (discussing valuation of easements). *See also* Kiefer, *supra* note 1, at 149-52 (discussing penalties imposed by § 6659 for overvaluation of a donated property, and several cases where the IRS found overvaluation).

mined without regard to the value of such easement and reduced by the value of any retained development right) . . . ."[54]

Returning to the example, this provision is applied as follows: an owner's land is worth $1 million without an easement, $700,000 with the easement, and $800,000 with the retained development right. The ultimate reduction in value is $200,000 ($1,000,000 - $800,000 = $200,000); this is a twenty percent reduction in value (200,000 ÷ 1,000,000 = .20 or 20%).

Because the reduction in value of the land is less than the thirty percent minimum reduction required by the statute, the exclusion is reduced, starting at forty percent, by two percentage points for each percentage point by which the value of qualified conservation easement is less than thirty percent of the value of the land.[55] Thus the exclusion is reduced from forty percent to twenty percent (30-20=10; 10 x 2=20; 40-20=20 percent excluded).[56] Consequently, the executor would be allowed to exclude twenty percent of $800,000, or $160,000.

Because of the reduction in the exclusion when the diminution in value to the land is less than thirty percent, if the reduction in value from the easement and retained development rights is less than eleven percent of the overall value of the land, there is no estate tax benefit.[57] Conversely, a maximum forty percent exclusion would be allowed if the easement reduced the value of the land more than thirty percent.[58] The executor must next determine if $160,000 is the lesser of the applicable percentage or the exclusion limitation.[59]

The exclusion limitation is a much simpler calculation designed to put a cap on the amount of the exclusion. The exclusion limitation will cap the benefit to landowners who have easements which greatly reduce the value of the land, or those owners who retain no development rights. The exclusion limitation will be phased in between 1998 and 2002.[60] In 1998, the limitation was $100,000; the limitation will increase by $100,000 every year until 2002 when it will be capped at $500,000.[61]

54. I.R.C. § 2031(c)(2) (West Supp. 1998).
55. *Id.*
56. Stephen J. Small & Timothy Lindstrom, *supra* note 29, at 15 (example of the applicable percentage calculation).
57. Ronald D. Aucutt, *supra* note 39, at 782.
58. I.R.C. § 2031(c)(2) (West Supp. 1998).
59. I.R.C. § 2031(c)(1) (West Supp. 1998).
60. I.R.C. § 2031(c)(3) (West Supp. 1998).
61. *Id.*

In the previous example, it was determined that under the applicable percentage calculation the landowner would be able to exclude $160,000 from his or her estate. The next step is to determine the lesser of the applicable percentage ($160,000) or the exclusion limitation. For example, if the decedent died in 1998, the applicable percentage is $160,000, and the exclusion limitation is $100,000,[62] then the executor will be able to exclude $100,000 from the decedent's estate. The $100,000 exclusion is correct because the statute allows for the exclusion of the lesser of the two amounts (applicable percentage-$160,000 or exclusion amount-$100,000). However, in 1999 and thereafter, $160,000 would be the lesser of the two amounts (the exclusion limitation is $200,000 in 1999 and increases in each of the following years).

3. Treatment of Certain Indebtedness

Generally, to the extent the land is debt-financed, the exclusion does not apply.[63] This does not mean that the estate is ineligible for the exclusion, rather, the amount of the debt is excluded from the overall value of the land. For example, if a one million dollar property is subject to an outstanding debt balance of $100,000, it is treated as if it were a $900,000 property that is not debt-financed.[64] Because debt-financed property is worth less, the percentage reduction in value is actually larger. Returning to the earlier example, a $900,000 property without an easement, that is worth $600,000 with an easement and worth $700,000 with a retained development right has a 22% reduction in value because of the easement (900,000 - 700,000 = 200,00; 200,000 ÷ 900,000 = .22 or 22%). Because twenty-two percent is closer than the twenty percent required for non-debt-financed property, debt-financed property may in have a larger estate tax exclusion (note that the exclusion would be the same if the $500,000 cap was reached).

62. *Id.*

63. I.R.C. § 2031(c)(4)(A) (West Supp. 1998). "Debt-financed property means any property with respect to which there is an acquisition indebtedness . . . on the date of the decedent's death." I.R.C. § 2031(c)(4)(B)(i) (West Supp. 1998).

64. H.R. CONF. REP. No. 105-220, at 403 (1997) *reprinted in* 1997 U.S.C.C.A.N. 1213, 1215.

4. Retained Development Rights

As previously mentioned,[65] to the extent development rights are retained, the exclusion is reduced.[66] Development rights include any right to "use the land subject to the qualified conservation easement for any commercial purpose which is not subordinate to and directly supportive of the use of such land as a farm for farming purposes . . . ."[67]

The statute provides a flexible provision allowing the donor to retain development rights. The beneficiaries can then extinguish some or all of those rights at the owner's death and the estate tax will be reduced accordingly.[68] If an agreement is made to extinguish the development rights, those rights must be extinguished within two years of the death of the decedent[69] or by the date of the sale of the land subject to the easement.[70] If the beneficiaries agree to extinguish the development rights and fail to do so, there will be a tax imposed equal to the amount which would have been due on the retained development rights.[71] The additional tax is due two years and six months after the death of the decedent,[72] or six months after the sale of the land subject to the easement.[73]

Returning to the previous example where the landowner retained the right to build five home sites, this reserved right increased the value of the property from $700,000 to $800,000. If the beneficiaries agreed, they could extinguish that right to build, and so long as they did so within the statutory time frame, they would not have to add back in the $100,000 attributed to the reserved development right.[74]

This would change the applicable percentage calculation because the reduction in value would be the 30 percent required by I.R.C. § 2031(c)(2). The executor can exclude the lesser of: (1)

65. See *supra* Part II, second calculation.
66. I.R.C. § 2031(c)(5)(A) (West Supp. 1998).
67. I.R.C. § 2031(c)(5)(D) (West Supp. 1998). The Committee Reports explain that the use of the land as a farm for farming purposes include tree farming, ranching, viticulture, and the raising of other agricultural or horticultural commodities. H.R. CONF. REP. No. 105-220 at 402 (1997) *reprinted in* 1997 U.S.C.C.A.N. 1213, 1214.
68. I.R.C. § 2031(c)(5)(B) (West Supp. 1998).
69. I.R.C. § 2031(c)(5)(C)(i) (West Supp. 1998).
70. I.R.C. § 2031(c)(5)(C)(ii) (West Supp. 1998).
71. I.R.C. § 2031(c)(5)(C) (West Supp. 1998).
72. I.R.C. § 2031(c)(5)(C)(i) (West Supp. 1998).
73. I.R.C. § 2031(c)(5)(C)(ii) (West Supp. 1998).
74. I.R.C. § 2031(c)(5)(B) (West Supp. 1998).

the applicable percentage[75] (now 40% of $700,000= $280,000) or (2) the exclusion limitation for the appropriate year.[76] For the 1998 example, the lesser amount is the exclusion limitation of $100,000. Ironically, in a statute intended to preserve environmentally significant land,[77] the beneficiaries can retain the development rights without forgoing any exclusionary amount. After January 1, 2000, when the exclusion limitation reaches $300,000 it would benefit the beneficiaries to extinguish the development right. Extinguishing the development right would allow the lesser exclusion of the applicable percentage amount of $280,000 rather than the $160,000 (the $300,000 exclusion limitation is greater than both of these figures; extinguishing the development rights allows the maximum exclusion from the lesser of the two applicable percentage figures).

5. Post Mortem Election

Prior to the new law, if a landowner died without having either donated an easement during his or her lifetime, or including an easement donation in his or her will, the land was subject to estate tax at its full, fair market value.[78] The new law allows an executor, trustee, or member of the decedent's family to elect to donate a qualified conservation easement after the death of the decedent.[79] The donation, even if made after the death of the decedent, will reduce the value of the land subject to estate tax and allow the estate to be eligible for the I.R.C. § 2031(c) exclusion.[80] "[T]he legal rules on when and under what circumstances an executor can make such a donation can vary widely from state to state, and may require changes in state law under some circumstances."[81] Of course, if there is a post-mortem election, the landowner loses the option of also receiving a charitable income tax deduction.

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75. I.R.C. § 2031(c)(1)(A) (West Supp. 1998).

76. I.R.C. § 2031(c)(1)(B) (West Supp. 1998).

77. RESEARCH INSTITUTE OF AMERICA, *supra* note 26, at 141.

78. Stephen J. Small & Timothy Lindstrom, *supra* note 29, at 16.

79. I.R.C. § 2031(c)(8)(A)(iii) (West Supp. 1998) (qualified conservation easement made by an individual); I.R.C. § 2031(c)(8)(C) (West Supp. 1998) (describing individual as decedent, member of decedent's family, executor, and trustee). *See also* H.R. CONF. REP. NO.,220, 105th Cong., 1st Sess. 401, 403 (1997) *reprinted in* 1997 U.S.C.C.A.N. 1213, 1215.

80. Stephen J. Small & Timothy Lindstrom, *supra* note 29 at 16.

81. *Id.* at 17.

6. Carryover Basis

To the extent that land is subject to a qualified conservation easement, and is included in the gross estate, the basis of the land acquired at death is the basis in the hands of the decedent.[82] This means that the basis is a carryover basis, and is not stepped up to the fair market value at death.[83] Generally, property acquired at death is stepped up to its fair market value.[84] The disallowance of the stepped-up basis could result in a significant cost to the transferee upon a future disposition. However, "keep in mind that the lowest tax rate on long-term capital gains is now 20 percent, while the top estate tax rate is 55 percent."[85] Therefore, by placing a conservation easement on a property, both reducing its value and qualifying for the I.R.C. § 2031(c) exclusion, the resulting smaller amount subject to estate tax may offset the later increase in the amount realized from the sale of the property with the lower carryover basis (the gain from the sale of property is the difference between the amount realized and the adjusted basis[86]).

IV.
CONCLUSION

Determining whether to subject land to a conservation easement is a personal decision for a landowner. The new law allows the landowner to make a decision to create a conservation easement during his or her lifetime, generating the maximum income, estate, gift and potential property tax benefits. The landowner may also provide for a conservation easement in a will, resulting in the loss of possible income tax and gift tax benefits but retaining the estate tax exclusion and other tax benefits for the landowners' beneficiaries. The flexibility of the new law also allows the beneficiaries to subject the land to an easement once the original owner is deceased. This flexibility will aid in both the preservation of land and in the ability of beneficiaries to continue to own the land, reducing the chance that the land will have to be sold to pay estate taxes.

82. H.R. CONF. REP. No. 105-220, at 402 (1997), *reprinted in* 1997 U.S.C.C.A.N. 1213, 1214; *see* I.R.C. § 1014(a)(4) (West Supp. 1998).

83. H.R. CONF. REP. No. 105-220, at 402 (1997), *reprinted in* 1997 U.S.C.C.A.N. 1213, 1214.

84. I.R.C. § 1014(a)(1) (West Supp. 1998).

85. Stephen J. Small & Timothy Lindstrom, *supra* note 29, at 15.

86. I.R.C § 1001(a) (West Supp. 1998).

A landowner creating a conservation easement during his or her lifetime, or in a will, gains tax benefits as well as preserves land for the future. Although beneficiaries may be more motivated by decreased estate taxes, the public also benefits through the preservation of habitat, open-space, recreational and educational opportunities. These benefits are significant in long-term preservation of America's special places.