



Conservation Easements, Water Law & Other Issues Facing Rural Texas

JAMES D. BRADBURY
AUSTIN AREA RANCHERS ASSEMBLY

AUSTIN, TEXAS

OCTOBER 23, 2018



Conservation Easements

What is a Conservation Easement?

A **voluntary** legal agreement, between a landowner and a qualified holder, that allows a **landowner** to permanently limit the type or amount of development on their property in order to protect the property's conservation and agricultural values while retaining private ownership of the land.



What is a Conservation Easement?

- A real property interest
- Filed at the courthouse
- Runs with the land



What is a Conservation Easement?

- ▶ Mortgaged Property
 - ▶ Mortgage is “subordinated” to the conservation easement
 - ▶ Lender agrees to allow CE to remain after foreclosure

What is a Conservation Easement?

- ▶ Part of the title of the land
- ▶ Land can be sold or gifted
- ▶ Will be binding on all future owners
- ▶ Selectively removes rights from the title of the land
- ▶ Very little is required
- ▶ Each easement is individually tailored



Jackson Nature Park

What is a Conservation Easement?

- ▶ Provided for in the state law by Texas Natural Resources Code Section 183



Purpose of CEs – 170(h) IRC

- ▶ Conservation easements have different purposes
 - ▶ Protection of significant natural resources including water and/or endangered species and their habitats
 - ▶ Protection of historical resources
 - ▶ Public access, for recreation and/or education
 - ▶ Open Space

Types of Conservation Easements

- ▶ Donated easements, governed by IRS regulations – must be perpetual to qualify for a deduction (Section 170(h) IRC)
- ▶ Purchased easements (a.k.a Purchase of Development Rights – PDR; or Purchase of Agricultural Conservation Easement – PACE), governed by the rules of the organization making the purchase; depending on the funder, can be for a term of years
- ▶ Bargain Sale, or a combination of a donated and purchased easement, most commonly used to offset tax considerations

Conservation Easement Process

- ▶ The process is essentially the same for donated and purchased easements
- ▶ Determine reserved rights (how many partitions will be allowed, how many “building envelopes”, etc.)
- ▶ Get an appraisal, preferably from an appraiser who has experience appraising conservation easements
- ▶ Develop a “baseline report” that documents the condition of the property at the time of the transaction

Terms of the Conservation Easement Agreement

- ▶ Purpose Clause
- ▶ State Conservation Values
- ▶ Restrictions & Reserved Rights
- ▶ Administrative Sections

Terms of the Conservation Easement Agreement

Restrictions & Reserved Rights

- ▶ Subdivision of the property
- ▶ Construction on the property
- ▶ Surface Alteration
- ▶ Vegetation Management
- ▶ Land Uses
 - ▶ Agriculture/crops
 - ▶ Grazing
 - ▶ Hunting
 - ▶ Surface mining
 - ▶ Oil & gas development
 - ▶ Water extraction

Terms of the Agreement

Administrative Sections

- ▶ Gives the Land Trust right of entry to monitor compliance
- ▶ Gives the Land Trust the right to enforce terms of the Agreement

Limitations Regarding Minerals

- ▶ Surface Mining is Prohibited
- ▶ Required by the IRC



Other Considerations

- ▶ Term or perpetual
- ▶ Condemnation
- ▶ Termination



The Easement Holder

- ▶ A non-profit land trust whose mission is land conservation; or a governmental entity
- ▶ Has the right to monitor and enforce the easement
- ▶ Typically visits the property once a year to ensure that the terms of the easement are being upheld
- ▶ 30 Texas land trusts, each with a specific mission

Conservation Easements: Donor Profile

- ▶ Conservation-minded
- ▶ Interest in passing land on in the family
- ▶ Sufficient income to benefit from the deduction
- ▶ Diverse income sources, beyond the property
- ▶ Post-mortem can work

Ground Water Restrictions

- ▶ The terms of conservation easement agreements typically prohibit the property's ground water from being transported off-site.
- ▶ But most agreements do not restrict the use of ground water on the property itself.





Photo by Tave Doty

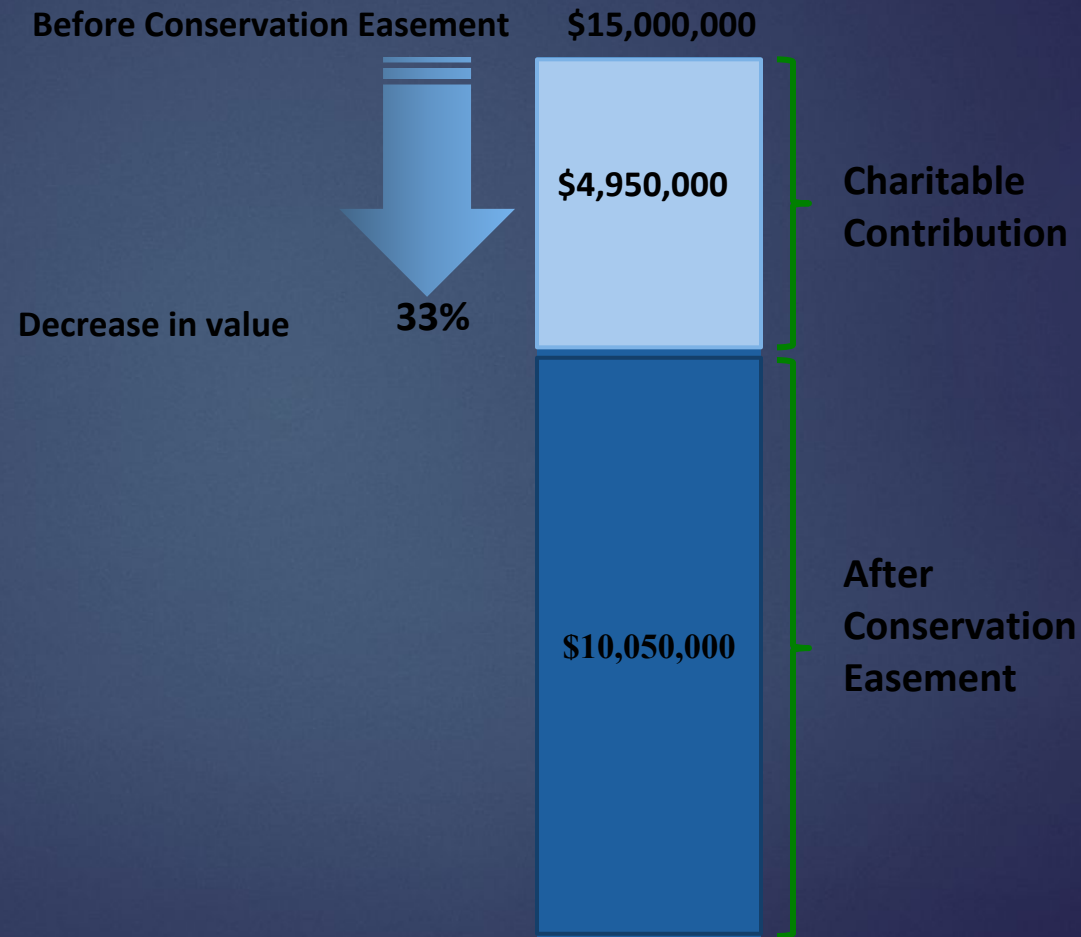
Financial Incentives and Implications

James D. Bradbury, PLLC

Tax Savings: An Overview

- ▶ How a CE provides tax savings:
 - ▶ Income tax deduction when donated
 - ▶ Lower appraised value in estate
 - ▶ May impact property taxes

Valuation of Conservation Easements



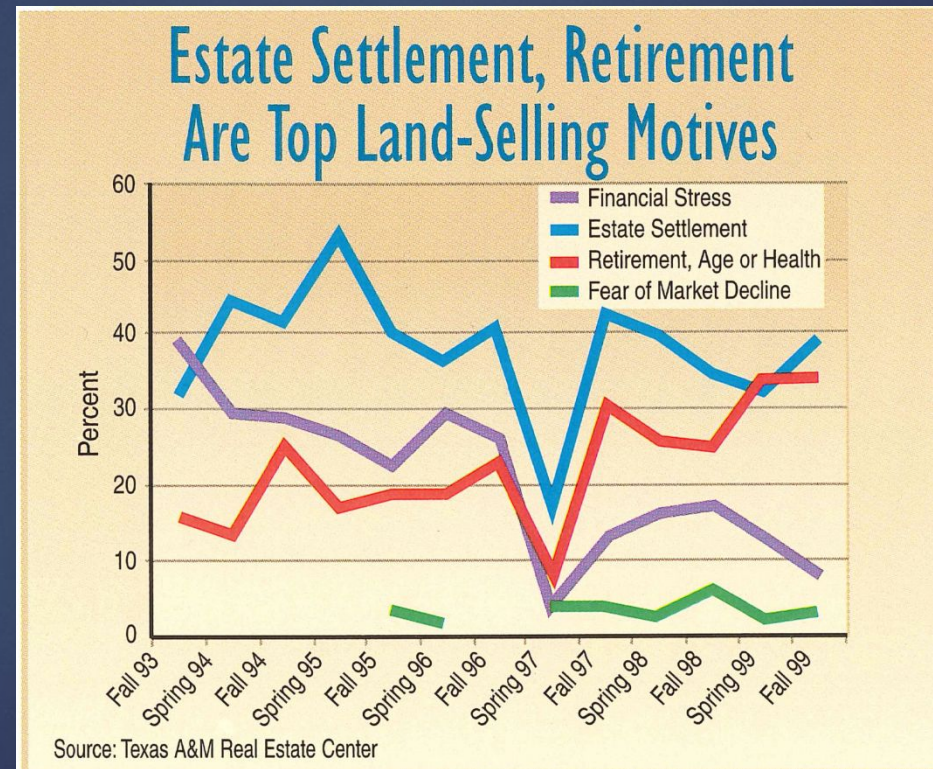
Tax Incentives

- ▶ Donated Easements
 - ▶ Can deduct donation against 50% of adjusted gross income (AGI)
 - ▶ Carry-forward = In addition to the year of the donation,
15 years
 - ▶ A qualified farmer or rancher can deduct up to 100% of his or her AGI

Tax Deduction: How it Works

- ▶ Let's assume that the landowner's annual adjusted gross income for income tax purposes is \$150,000 which remains constant.
- ▶ The deduction resulting from the easement is as follows:
 - ▶ (50 percent of \$150,000 = \$75,000)
 - ▶ Year of Contribution \$75,000
 - ▶ Carry-forward to Year 1 \$75,000
 - ▶ Carry-forward to Year 2 \$75,000
 - ▶ Carry-forward to Years 3-15 \$975,000
 - ▶ TOTAL DEDUCTION \$1,200,000

Estate Tax Considerations



Estate Tax Considerations

\$17 Million



Jones Ranch

~~\$17~~ 9 Million



Smith Ranch

Estate Tax Considerations

\$17 Million



Jones Ranch

~~\$17~~ 9 Million



Smith Ranch

FET/ Sales to pay taxes/ divisions for heirs

Purchased – Conservation Easements

- ▶ Federal (Purchase of Development Rights)
 - ▶ Agricultural Conservation Easement Program (formerly known as the NRCS Grasslands Reserve Program and the Farm & Ranch Protection Program)
 - ▶ Passed within the 2014 Farm Bill
 - ▶ 2014 USDA announced \$386 Million for ACEP
 - ▶ 2015 USDA announced \$332 Million for ACEP

Purchased –Agricultural Conservation Easements

- ▶ State
- ▶ Texas Farm & Ranch Lands Conservation Program
 - ▶ Managed by Texas Parks & Wildlife Department
 - ▶ Oversight board = representatives from statewide agricultural organizations
 - ▶ \$2M in funding allocated in the last legislative session
- ▶ Local / Resource Specific
 - ▶ City of San Antonio \$300 million Aquifer Protection Initiative, 2000, 2005, 2010, 2015 – to protect the Edwards Aquifer
 - ▶ City of Austin / County of Travis / County of Hays \$120 million – to protect water quality and quantity
 - ▶ REPI / ACUB Programs – to create open space buffers around military installations

Financial Implications: Benefits

- ▶ A voluntary mechanism to protect property from fragmentation or development – fits family's long-term stewardship goals for the farm or ranch
- ▶ Income tax deduction
- ▶ Estate tax benefits/facilitates inter-generational transfer
- ▶ Convert property equity to cash or tax savings
- ▶ Accomplishes the objectives of some landowners

Financial Implications: Drawbacks

- ▶ Projects are expensive
- ▶ Cash match isn't always available
- ▶ Take a long time to complete
- ▶ Do not ensure that the land will continue to be farmed, ranched or managed for wildlife-only that the land will be available for agriculture and hunting
- ▶ Sale of conservation easement is subject to capital gains tax
- ▶ Tax benefits are generally only available to the first generation of easement donors
- ▶ Use of property is limited for the future
- ▶ Value of the property is reduced by the conservation easement



Texas Farm & Ranch Lands Conservation Program

James D. Bradbury, PLLC

Overview of Applications

- ▶ Fifteen (15) applications received
- ▶ Eight (8) different organizations submitted applications
- ▶ Projects range in size from 24 to 9,500 acres, across thirteen (13) counties
- ▶ Total TFRLCP request: \$ 5,343,585; total acreage: 34,683; and, total project value: \$ 44,267,628
- ▶ Projects include working cattle ranches, crop lands, timber operations and wildlife management lands
- ▶ Habitats include south Texas brush, coastal marshes, prairies and forest, pine forest, oak forest, oak-juniper woodland and grassland

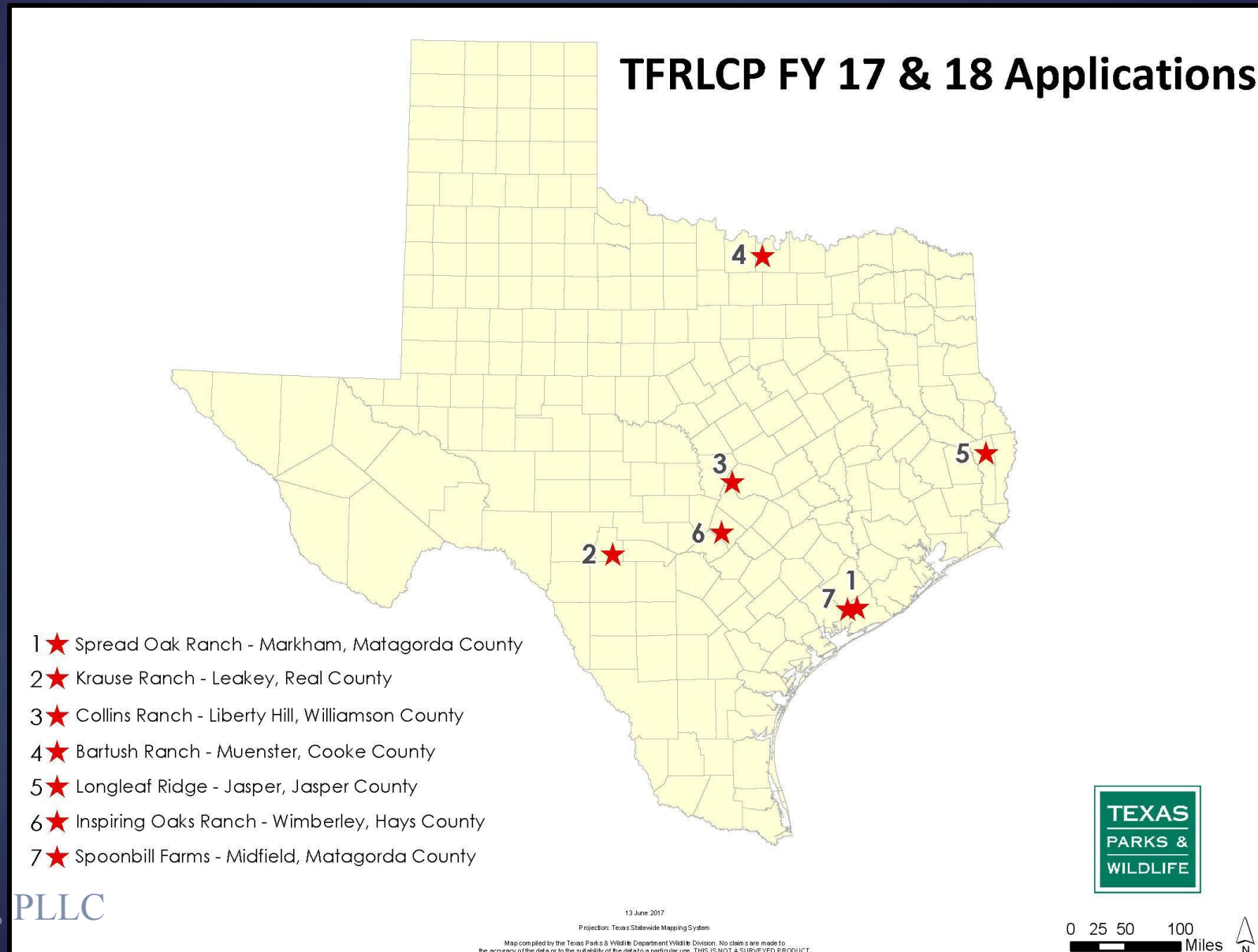


Selection Criteria

- ▶ Threat of development or other conversion to productive working lands (20 pts)
- ▶ Value (20 pts)
- ▶ Watershed value (20 pts)
- ▶ Fish and wildlife value (20 pts)
- ▶ Contribution to a conservation landscape (10 pts)
- ▶ Terms of the conservation easement (10 pts)



Recommended Projects



Recommended Project Summary

- ▶ 7 projects recommended for funding
 - ▶ 6 projects for full funding; 1 project for partial funding
 - ▶ Combined project area = **16,009 acres**
 - ▶ Combined project value = **\$ 16,468,800**
- ▶ Staff recommends awarding \$ 1,800,700
 - ▶ Fund balance of \$ 199,300 for operating costs
 - ▶ TFRLCP proposed funding leverage = **9.15 to 1**



TFRLCP Value

- ▶ FY16-17 biennium: program appropriated \$ 2 million
 - ▶ \$ 1.84 million awarded to 7 projects in 6 counties protecting 10,373 acres
 - ▶ Project value: \$ 13.4 million for a leverage of 7:1
- ▶ FY18-19 biennium: program appropriated \$ 2 million
 - ▶ Staff recommends awarding \$ 1.80 million to 7 projects in 6 counties protecting 16,009 acres
 - ▶ Projects valued at \$ 16.5 million for a leverage of 9:1
- ▶ *Average cost of conservation: \$ 138/acre*
- ▶ In December 2016, Texas A&M's Institute of Renewable Natural Resources conducted a Return on Investment analysis of the Legislature's \$2m appropriation to the Texas Farm & Ranch Lands Conservation Program. The state's \$2m investment funded seven perpetual conservation easements, representing 10,500 acres. The use of 1.8MM in state program dollars leveraged purchases of 14MM, which cumulatively protect on an annual basis \$11.5m in water resources.



James D. Bradbury, PLLC



Fort Worth • Austin