Building Envelopes in Conservation Easements: Drafting for Perpetuity

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Learning Objectives

• Federal tax law relating to building envelopes

• Achieving flexibility and protection of conservation purposes in perpetuity

• Drafting tips
• IRS Provisions and Case Law
• LTA Standards and Practices
• Discussion Questions and Drafting Tips
• Sample Provisions
• Case Studies and Discussion
IRS §170(h)(1) – Qualified Conservation Contribution

- Qualified real property interest
- Donated to a qualified organization
- Exclusively for conservation purpose
Perpetuity

- IRS §170(h)(2) Qualified real property interest
  - Restriction (granted in perpetuity) on the use which may be made of real property

- IRS §170(h)(5) Exclusively for conservation purpose
  - Conservation purpose protected in perpetuity
Floating Easement - Potential Split in Circuits

*Belk v. Comm’r - 4th Circuit (2014)*

- Static piece of real property
- Not qualified real property interest: not “granted in perpetuity”
- Distinguished from “protected in perpetuity”
- Baseline fails
- Appraisal fails
Bosque Canyon - 5th Circuit (August 2017)

Holes in the swiss cheese could be relocated

Distinguished from Belk

- No change in outer perimeter
- Each new exclusion must be 5 acres – no change in acres
- Holder’s consent – no material adverse effect
- No appraisal issues
Bosque Canyon

- Facts and circumstances - evaluation of perpetuity
- CE may be modified to address changing and unforeseen conditions
  - Flexibility is a benefit
- Standard of review
  - “Ordinary standard for statutory construction”
  - Not “strict construction”
Building Envelopes

• Do reserved rights still allow for protection in perpetuity of conservation purposes - IRS §170(h)(5)

➢ Treasury Regulation - §1.170A-14(a)
  o Impermissible “checkerboard”
  o Permissible “cluster”
• *Glass* - 6th Circuit (2006) - Uses that don’t impair conservation purposes are permissible

  - Building construction done in a manner and location to minimize interference with the identified plant and wildlife habitat
  - Right is subject to holder’s right to say no if inconsistent with conservation purposes
• **Butler v. Comm’r, T.C. Memo 2012-72 (2012)**
  
  ➢ If property is developed as fully permitted under CE, would the conservation purposes still be protected?
  
  ➢ CE allowed “reconfiguration” of building sites
LTA Standards and Practices  
Standard 9: Ensuring Sounds Transactions  

Practice 9D: Determining Property Boundaries  

1. Determine both the legal description and physical boundaries of each property or conservation easement.  

2. If a conservation easement contains restrictions or permitted rights that are specific to certain zones or areas within the property, include the locations of these areas in the easement document so that they can be identified in the field.
Practice 9E: Conservation Easement Drafting

1. For every conservation easement,
   a. Individually tailor it to the specific property;
   b. Identify the conservation values being protected;
   c. Allow only uses and permitted rights that are not inconsistent with the conservation purposes and that will not significantly impair the protected conservation values;
   d. Avoid restrictions and permitted rights that the land trust cannot monitor and enforce; and
   e. Include all necessary and appropriate provisions to ensure it is legally enforceable.
Practice 9E: Conservation Easement Drafting

2. Review, on the land trusts own behalf, each potentially tax-deductible conservation easement for consistency with the Treasury Department regulations (U.S.C. § 1.170A-14), especially the conservation purposes test of I.R.C. § 170(h).
Critical Information for Drafting

Conservation purposes!!

Current uses of the property/
sources of income
  • Agricultural
  • Recreational
  • Commercial

Any additional desired
future uses?
• Title commitment, which might show rights of third parties on the property
  > Access roads, ditches, severed minerals
Existing/Future Structures
- Houses, garages
- Other residential structures
- Cabins, hunting blinds
- Other recreational structures
- Barns, sheds
- Other agricultural structures
- Any commercial structures

Existing/Future Infrastructure
- Roads, trails
- Wells, septic systems
- Fences
- Ditches, irrigation systems
- Stock ponds
Discussion Question

Why not just exclude the building areas from the CE?

• Benefits of exclusion
  ➢ No monitoring
  ➢ Will not jeopardize conservation purposes
  ➢ Eliminates the building envelope challenge

• However
  ➢ Risk of carving out the wrong property (see Bosque Canyon)
  ➢ Risk of leaving the CE property with no economic viability
  ➢ Unrestricted adjacent uses may harm conservation values
Discussion Question

• What guidelines are there to determine how many building envelopes (and what size) to allow based on size of the property or sensitive habitat factors, scenic view or other factors?
Drafting Tips

• Only reserved rights and permitted uses that are not inconsistent with conservation purposes
• Before you draft - detailed description of the conservation values
• Location, number and size of building envelopes
• Right to monitor and enforce
• Blanket prohibition of inconsistent activity
Discussion Question

• How to draft to demonstrate certainty of perpetual protection of the conservation purposes but also allow flexibility to allow landowner to reasonably carry out their goals
Drafting Tips

• Flexibility in description of building envelope
• Don’t make the building envelopes too small
• Make allowances for utility and sewer
• Require holder notification/approval of final plans BEFORE construction
• Know the property and address unrealistic expectations
Discussion Questions

• Should the CE specifically permit relocation of the building envelopes?

• If not specifically permitted by the CE, can the building envelopes be relocated without an amendment?
Drafting Tips

• Holder approval of any adjustments to existing building envelopes. Adjustments should include only property already within the easement. *(But see Bosque Canyon II)*

• Don’t rely on “savings clause”. Specific provisions prevail over a savings clause.
Discussion Question

• How do you document the location of a building envelope in the conservation easement?
Drafting Tips

• Surveyed and monumented legal description is the best option – before or after?
• GPS coordinates of the corners of the building envelope
• Lines drawn on a properly scaled topographic map
• Other ideas?

• Regardless of method chosen, the documentation must be contained within the actual conservation easement document

  *Butler v. Comm’r, T.C. Memo 2012-72 (2012)*
Discussion Question

• If the location of a building envelope has not been determined, how do you provide for its location in the conservation easement in compliance with the perpetuity requirements?
Drafting Tips

Location must be chosen in a manner that is not harmful to the conservation purposes

- Development zones
  - Identify specific area within which the building envelope must be located
  - Identify single GPS point and provide that the building envelope must contain the GPS point

- Multiple Options
  - Identify multiple potential building envelopes and provide that only one may be chosen

- Exclusion zones
  - Identify specific areas where the building envelope cannot be located
Discussion Questions

• Do you need a building envelope for existing buildings?

• What restrictions should apply to existing buildings?
Drafting Tips

• Typically placed in a building envelope that surrounds the existing buildings with sufficient space for additional desired buildings
• Should permit repair and maintenance of existing buildings
• Document the square footage of the buildings in the conservation easement
• Include reasonable height restrictions
• Provide for the buildings to be replaced and enlarged unless square footage is limited
• Provide for buildings to be relocated within the building envelope
• Specify how the buildings can be used?
Discussion Questions

• If landowner wants to reserve the right to construct future buildings, what restrictions should apply?

• Should you restrict square footage and building materials?
Drafting Tips

• Always within building envelope with limited exceptions for minor agricultural buildings or hunting blinds
• Importance of square footage limitations
  > Include a measurement standard
  > Total square footage or footprint?
  > Limitations on each building or limit only the cumulative total within the envelope?
  > Other options?
• Include reasonable height restrictions
• Specification of building materials for scenic easements
• Specify how the buildings can be used
Discussion Question

• Should all infrastructure be placed within the building envelope?
Drafting Tips

• Ideally all infrastructure is located within the building envelope
• What about utilities?
  • Power lines
  • Solar and wind generation
• Other Items that might be located outside the building envelope
  > Road to building envelope
  > Well
  > Septic system
  > Fences
Discussion Question

- Do you need to define the terms you use to describe the types of buildings and uses?
Drafting Tips

• Define terms wherever possible
  • Use definitions in land use regulations
  • Rely on common usage – courts will look to customary meanings of words
  • Use terms that are capable of being understood 100 years from now
  • Think about how a reasonable person would understand the words used
Commercial Uses

Balance between permitting sources of income and allowing scope and intensity of commercial use to damage the conservation purposes

- Dude Ranch
- Eco Lodge
- Bed and Breakfast
- Wedding Venue
- Conference Center
- Paint Ball Course
- Horseback Riding
- Wagon Rides/Jeep Trails
- Snowmobiles and ATVs
Case Study – Casa Grande Ranch

• 1,500 acres subject to conservation easement

• Three building areas
  > Ranch Headquarters Building Area
    o Contains agricultural buildings
  > Main House Building Area
    o Contains 14,000 square foot 3 bedroom house
    o Adjacent barn
  > Additional Building Area

• Originally operated as a working cattle ranch

• Now operated as a cattle ranch and wedding venue
• Structures Permitted in Main House Building Area. Within the Main House Building Area, the Grantor may construct, maintain, repair, enlarge and/or replace one (1) single-family residence (which may be converted into a bed and breakfast or other similar short-term overnight accommodations), improvements and uses accessory thereto, including a greenhouse, windmills, access drives and related improvements, fish ponds, landscape structures, gardens, a guest house, garages, a barn, a meeting venue, livestock pens, accessory structures and recreational structures including without limitation, a garage, a small barn, indoor and outdoor tennis courts, tower and swimming pools. No such structure shall exceed 50 feet in height. At the time of construction of any such improvements, Grantor shall notify Grantee so it can update its records.
Commercial or Industrial Activity; Nuisances. No industrial uses shall be conducted on the Property. Grantor shall not conduct commercial uses of the Property that are inconsistent with the preservation and protection of the Conservation Values. Examples of such prohibited uses are: commercial feedlots, meat or poultry processing facilities, commercial greenhouses, commercial nurseries, tree farms, sawmills or logging operations or facilities, agricultural products wholesale or retail outlets, concentrated animal feeding operations and other similar intensive agricultural uses, and commercial recreational uses. Provided they are not inconsistent with the preservation and protection of the Conservation Values, within the Building Areas, Grantor may hold competitions for horses or cattle, barrel races, cattle or horse shows, cattle or horse auctions and sales. Ranching, ranching activities, breeding, boarding and training of animals are permitted on the Property. Home-based uses are also permitted. Within the Main House Building Area, Grantor may conduct weddings, meetings, conferences, seminars, and workshops, including short-term overnight accommodations, provided such uses do not cause a material adverse impact to the Conservation Values. Within the Ranch Headquarters Building Area and on existing trails and access roads, Grantor may conduct horseback rides and hay rides, provided such uses do not cause a material adverse impact to the Conservation Values.
Discussion Questions

• Are the structures adequately defined?
  > Meeting venue?
  > Guest house?
  > Tower?

• Are the commercial uses clear and understandable?

• Would you allow other similar commercial uses within the Main House Building Area?

• Can this be salvaged with a commercial operations plan?
QUESTIONS?