An Overview of Financial Alternatives for Land Conservation Transactions

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Clearly, the motivation for a land conservation transaction is often the desire of the landowner to safeguard the property. However, this objective must be balanced with the need to maximize the return to the landowner. The general perception is that the highest return will be realized from a sale to a developer. Yet, that is sometimes not the case. Working with a team of professional advisors, a land trust is well positioned to demonstrate this point. Once financial, tax and estate planning impacts are calculated, a land conservation transaction can often offer the greatest financial as well as philanthropic benefits. In fact, a key selling point for land preservation is that these cases typically result in benefits for all the parties involved, which is the objective of the teamwork between professional advisors, the land trust and the landowner.

Land trusts are quite effective at identifying properties and landowners with an inclination to consider a preservation opportunity. However, many land trust organizations lack the staff with financial and legal expertise to design, define and compare land conservation scenarios with a development offer. As a result, it may be difficult for a land trust to illustrate to a landowner that the preservation opportunity (with what appears to be a smaller dollar value offer) can have the more financially beneficial result. A very effective way to complete preservation cases is to approach the case from the beginning with a team of professional advisors consisting of the land trust and financial advisor supplemented by an attorney and tax accountant.

So, how does this process work? Typically, the land trust holds initial meetings with the landowner. This is to primarily understand the scope and zoning implications of the property, and to obtain an initial sense of the landowner's key needs and interests. The land trust then calls in the financial advisor to meet with the landowner and discuss financial and estate planning considerations. They would then address issues including:

- Is the financial priority income generation or tax minimization, or a combination?
- How does this transaction fit into broader financial and estate planning considerations?

> ***Wade Martin,***
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> Delaware & Raritan Greenway (NJ) and
> ***David Epstein,***
> Morris Land Conservancy (NJ) will present:
> **"Alternative Financial Strategies: Leveraging Every Dollar for the Land Trust and the Landowner"**
> on Saturday, October 30, from 10:30 to 12:00 at the National Land Conservation Conference.

■ What will be the impact on other family members?

■ What are the financial and tax implications of a charitable donation versus outright sale?

■ Have trust and insurance/annuity solutions been researched to potentially maximize the liquid assets once the land is transferred?

The land trust and the financial advisor work together to present initial ideas for land preservation and investment scenarios. The next step is to involve an attorney and tax accountant, retained by the landowner, who provide counsel and specific details about the tax and transactional implications of the proposed scenarios—which are unique to each state and to the individual financial circumstances of the landowner.

Even if the landowner already works with a financial advisor, attorney and accountant for other business matters, those advisors may not be attuned to all of the ramifications and nuances of a land deal. Land trusts have indicated that a key barrier to the completion of a land conservation transaction can be the absence of creative solutions presented by professional advisors. Thus, the involvement of professional advisors who are experienced in this area improves the efficiency and effectiveness of land conservation activities.

The role of the financial advisor throughout the process is multi-faceted. Generally, the financial advisor is the facilitator of the transaction—providing guidance to the land trust on how to structure the transaction to meet the financial objectives of the landowner, and helping the landowner to understand and compare the financial implications of the land sale alternatives. Because the financial advisor is not formally retained or compensated throughout the design portion of the process, and does not provide legal or tax advice, the financial advisor is a neutral third party whose "pro-bono" input benefits all parties involved. The financial advisor is only "retained" and compensated if either the land trust or landowner chooses to purchase a product from the financial advisor or has the financial advisor act as an ongoing investment advisor for the proceeds of the transaction. The specific legal and tax advice provided to the land trust and the landowner to complete the transaction is provided separately by professionals who are uniquely retained by those parties.

The following case studies offer insights into the way this partnership can answer a variety of landowner needs.

Case 1. *How Your Land Can Provide the Income You're Looking For*

A key factor, often overlooked, is that many individuals who are land-rich may not consider the domino effect of income, investment, and tax and estate considerations that come from the receipt of cash from a sale to a developer. One of the most frequent land preservation opportunities involves the multi-generational farming family with a high net worth due to the land value, but little in the way of liquid assets. In this case, the landowner needed income, but she and her family didn't want to leave their land, and she certainly did not want more housing developed in the area. In

Teamwork in Action . . .
*D&R Greenway and UBS Financial Services Inc.**

The Delaware & Raritan Greenway (D&R Greenway) land trust in Princeton, New Jersey, presents a prime example of how a land trust and a financial advisory team can work together to develop many successful and creative preservation solutions. The relationship between D&R Greenway and Financial Advisor Wade Martin of UBS Financial Services Inc. developed from a seminar hosted by the land trust that featured a nationally renowned land preservation attorney. The attorney emphasized the importance of estate planning in determining the net financial benefit of land transactions.

Martin recognized that many of his clients with significant land holdings had not ever considered land preservation as a financial or estate planning tool. He approached D&R Greenway to recommend some of his clients for potential preservation transactions, and those initial discussions grew into an ongoing relationship. Together, they have accomplished more than a dozen successful transactions.

Linda Mead, D&R Greenway's executive director, is enthusiastic about the results and the continuing opportunities. "Our relationship with UBS Financial Services Inc. has allowed D&R Greenway to meet our aggressive goals for land preservation in a state that is the most densely populated in the nation. When we are dealing with a finite resource such as land, we need to be smart and sophisticated in our approach," says Mead. "This enterprise has led to a number of transactions where landowners have chosen land preservation rather than a direct development offer. We firmly believe that others can benefit from our example."

**UBS Financial Services Inc. does not provide tax or legal advice. Landowners are advised to consult their tax or legal advisors with regard to their individual situations.*

Exhibit One

Comparison of Implications for a Property Sale *(illustrative)*

When presenting a preservation scenario to a landowner,
make sure that you have addressed these financial and procedural considerations:

Sale to Developer

FINANCIAL

- 15% capital gains tax
- State income tax
- Rollback taxes—if applicable by state (e.g., average of past three years of property taxes based on the sale value of the land)
- Realty transfer tax
- Real estate commission

PROCEDURAL

- Contingencies based on permits, approvals and variances—which contribute to the risk and length of time to close the deal

Sale to Land Trust

FINANCIAL

- Defer taxes on lump sum of proceeds by having land trust purchase annuity for landowner
- Itemized deduction for the charitable donation of the bargain sale (i.e., difference between full market value and sale price)
- No rollback taxes
- No realty transfer tax
- Time value of money due to a quicker time to close the sale

PROCEDURAL

- Quicker time to close deal
- Can split the land for various uses
- Need additional appraisal and multiple signatures on tax forms

fact, she was more inclined to accept less money from a land trust rather than to sell to a developer. Creative partnering between the land trust and team of professional advisors resulted in the design of a transaction that enabled the landowner to protect the land from developers, gain income and continue living on the farm.

The landowner sold a conservation easement to the land trust. Part of the proceeds from the sale went directly to the landowner as a lump sum, thereby enabling her to address her immediate financial needs. The remainder of the proceeds were treated as an installment sale funded by an annuity purchased by the land trust with the landowner named as beneficiary. This solution enabled the landowner to defer taxes by taking the money over time, and to guarantee an income stream from the annuity payments for the rest of the landowner's life. An added benefit was the relationship that developed between the land trust and the landowner, which recently led to a second transaction that will preserve additional family lands.

Case 2. *Look Carefully at the Bottom Line When Comparing Land Preservation Versus Developer Offers*

This case demonstrates how the net financial end result of an offer from a developer versus a land trust can be quite similar, even though the dollar value of the initial offers from the two parties are so divergent. The challenge in this case was for the land trust to make an offer that would have a comparable financial result to the multi-million dollar development offer that would have transformed a 200-acre family farm into 200 houses.

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The family had decided to discontinue farming, and wanted to cash in the value of their property. Though they didn't want to sell to a developer, they did not believe there would be options more attractive than the $23.7 million offer from the developer. With encouragement from the mayor of the town (in which this was the last large open space parcel) and the State Green Acres program, the landowners agreed to consider a land conservation transaction.

After nine months of discussions, the land trust and financial advisory team were able to clearly illustrate to the landowner that after taxes, the sale to the developer would result in $16.1 million of investable proceeds (see Exhibit One for a sample comparison of financial and tax considerations between development and conservation scenarios). Therefore, the town's offer that would net the landowners $16.1 million would keep the landowners financially whole and enable them to fulfill their desire to protect the land. The town structured an offer that included a bargain sale, a charitable donation, and a 1031 exchange, which provides tax benefits by using the proceeds from the original transaction to purchase income-producing properties in other states.

Case 3. *A Solution That Addresses Differing Family Objectives*

This case demonstrates three dimensions of complexity of land deals: personal, legal and transactional. When six siblings inherited their family's land, a developer immediately offered $2.4 million for the entire property. The siblings were split in their desire to sell to a developer or to preserve the land, and the dispute ended up in court. Fortunately, the resolution benefited all. As a first step, the six siblings as a unit sold the development rights to the town for $1.2 million. As a second step, the three siblings who wanted to preserve the land used their half of the proceeds from the sale of the development rights to purchase the deed-restricted land outright from the other three siblings. Ultimately, the three conservation-minded siblings ended up with the entire plot of deed-restricted land, and the development-minded siblings ended up with two separate lump sum payments that were comparable to the net result of their share of the offer from the developer.

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Case 4. *Potentially Realizing Tax and Charitable Benefits From Your Land*

This case represents a common scenario presented to financial advisors: a wealthy landowner with a low-cost-basis land position was looking for ways to reduce his income tax and/or estate tax bill. Preservation didn't initially hit the radar screen, since the landowner's traditional financial, legal and tax advisors were not experienced with land conservation. Further, the landowner, who wasn't looking for a philanthropic outlet, was reluctant to part with net worth in his estate. The following solution addressed financial and estate planning needs, and opened up a previously unidentified opportunity for land preservation:

■ The landowner donated the property to a Charitable Remainder Trust (CRT). The landowner took a charitable contribution deduction in the first year that was equal to 30 percent of his gross income, and was able to carry over the remainder for up to five years.

■ The trustee of the CRT sold the property to a land trust (which was named as the remainder beneficiary in the CRT, providing an added conservation benefit through support of the land trust's activities). The trustee invested 100 percent of the proceeds (as no taxes apply to the trust) to provide an income stream for the lifetime of the donor/landowner.

■ The donor/landowner used the income received from the trust to purchase an insurance policy through an irrevocable insurance trust. This enabled the landowner to replace the "loss of wealth" caused by the donation of the land. Further, since the irrevocable insurance trust is not part of the landowner's estate, the beneficiaries of the trust receive the insurance benefit tax free.

Strategize for Success

These cases highlight a number of scenarios aimed at pursuing each landowner's specific needs. However, the process involved in obtaining those successes isn't usually quick or easy. Often, the initial—and biggest—challenge is the skepticism of the landowner. Many are skeptical of the net results or are not aware of alternative strategies. Given this, a significant portion of time put into these cases involves gaining confidence and educating landowners and other advisors on the process and the details of the financial implications. Time is an important issue: the elapsed time needed to complete a preservation case often averages 9-12 months. While this is typically faster than closing a development deal, it is long enough to require the financial and other professional advisors to exercise extreme patience and sensitivity with both landowners and land trusts. Advisors cannot force the issue; instead they must patiently present multiple alternatives and develop a personal rapport.

Finally, successful closure of preservation deals requires focus and passion from all parties. Clearly, there must be a commitment from the landowner to achieve specific philanthropic as well as financial goals. The land trust must have focused, prioritized land preservation goals and a comprehensive strategy to pursue those goals, as well as an appreciation of the value that a financial partner brings to the process. Landowners must always be represented by their own tax and legal counsel. And the professional advisors need to love this type of work: they need to be passionate about preserving the land, and about helping landowners use their land to pursue their dreams.

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