



TESTIMONY OF RAND WENTWORTH
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SENATE FINANCE COMMITTEE HEARING
“The Tax Code and Land Conservation:
Report on Investigations and Proposals for Reform”
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Mr. Chairman, Senator Baucus, and Members of the Committee:

I am the President of the Land Trust Alliance, the national 501(c)(3) organization that provides training, research and standards for the 1500 land trusts in America. We were formed 23 years ago by land trust leaders to help improve the skills and practices of land trusts throughout the country. Land trusts are publicly supported charities that conserve land for public benefit, and they count on charitable gifts of land or conservation easements to accomplish their mission. The Land Trust Alliance is a non-partisan organization that does not engage in real estate transactions, own land, or hold easements.

Thank you for the opportunity to testify on the conservation donations which make the work of these charities possible. I also want to thank Dean Zerbe and Jonathan Selib of the committee staff for taking the time over the past year and a half to discuss a host of ideas about how to improve the laws governing conservation donations. They have studied this from every angle, and, while they have challenged virtually every aspect of our members’ operations, they have also been responsive to our suggestions for more practical ways to address their concerns.

A TAX POLICY SUCCESS

Encouraging landowners to donate conservation lands is a stunning success story of tax policy. Private landowners hold 70 percent of the undeveloped land in America and they are essential for the conservation of Americas’ natural heritage. The Congress enacted the current law governing tax deductions for donations of conservation easements 25 years ago. Under that law, land owners can donate the development rights to their land to protect resources important to the public, through a legal tool known as a conservation easement.

A conservation easement keeps land in private hands, supports rural economies, and keeps land on the tax rolls. It is politically attractive because it is voluntary, non-regulatory and respects private property rights, and it is only possible because of generous private landowners who have been good stewards of their land and have made extraordinary charitable gifts to provide public conservation benefits.

Since Congress enabled tax deductions for those donations, land trusts have protected more than 9 million acres of important wildlife habitat, farms, ranches, and forests with this tool. In combination with other tools, including the acquisition and management of preserves, partnerships with government conservation agencies, and a host of other means, land trusts have protected a total of 34 million acres in the US. This is an extraordinary legacy of land, more than the National Park Service holds in the lower 48 states, an area larger than Pennsylvania. It represents the commitment of more than 3 million Americans who support these nonprofits with their memberships and donations.

I would like to briefly recount two stories about conservation easement gifts.

Sinclair Farm, Lancaster County, Pennsylvania:

In Drumore Township, Pennsylvania, Joseph Sinclair donated a conservation easement on his land to the Lancaster Farmland Trust to preserve a significant component of the region's historical and natural legacy.

The 133-acre farm, which Mr. Sinclair works with his grandson, is a famous Underground Railroad station that protected escaped slaves in the mid-nineteenth century. Mr. Sinclair and his grandson offer tours to school and community groups of the stone vault where escapees once stayed, and are proud that the scenic farm will remain in agricultural use in perpetuity.

Hass Ranch, Las Animas County, Colorado:

Tony and Connie Hass purchased their 5,500 acre ranch in southeastern Colorado in the early 1990's when Tony retired from professional rodeo. Their ranch includes several miles of Timpas Creek, an oasis for wildlife in the area, including wild turkey, pronghorn antelope, swift fox, and trophy mule deer. In addition, the historic "Hole in the Wall" stop on the Santa Fe Trail is on the property and remnants of the thousands of wagons that crossed the plains in the 19th century are still visible.

Poor cattle prices and crippling drought tested Tony and Connie, who are raising their two children on the ranch. The ranch income is supplemented by Connie's job as a school teacher in town. In 2002, the family began to explore conservation easements as a way to help them stay on the ranch and avoid selling it to a developer. In 2003, they placed 1,600 acres into an easement held by the Colorado Cattlemen's Agricultural Land Trust – one of a number of land trusts associated with their states' cattle growers associations. In 2004 they added another 1,500 acres to the easement. Their intent is to protect the entire ranch.

The tax incentives have allowed them to reduce debt on the property and purchase a nearby hay farm which allowed them to expand their cattle operation.

There are thousands of stories like these, stories of valuable resources that have been protected for the long-term benefit of the public by private landowners working with a land trust.

The tax incentives that Congress has provided for gifts like these have leveraged extraordinary charitable giving, worth more than \$1 billion each year. The value of these gifts to the public will rise each year as land values increase and as development moves further and further into the countryside. As our nation builds and grows, we need to set aside land before it is too late to provide a legacy of wildlife habitat, clean water, working farms, and quality of life for the future.

ADDRESSING THE PROBLEMS

In the 25 years since Congress enacted section 170(h) of the Internal Revenue Code, conservation transactions have grown in size and complexity. It would be surprising if a close examination did not reveal a need for changes. While the vast majority of conservation transactions are properly structured, there are problems that require immediate attention, especially improper appraisals and transactions that do not have a legitimate conservation purpose.

These problems come from two distinct sources. One is caused by well-intentioned people with limited resources, trying to do as much as they can for a good cause – and not paying careful enough attention to the rules as they go. With two new land trusts being formed every week in America, some land trusts have not yet instituted strong policies and ethical safeguards. This is something we believe that we, in the private sector, can and must take primary responsibility for fixing. The second source of problems comes from people abusing conservation tax incentives to maximize personal gain, a problem that requires government action.

We were taken aback by the approach the Joint Committee on Taxation took to solving these problems in its report JCS-02-05, because they basically took the approach of stopping this program, rather than examining specific problems and tailoring solutions. I want to thank those Senators on the Committee who have expressed concern about the Joint Committee on Taxation recommendations to deny deductions for most conservation easement donations, and to reduce deductions for those donating land from the land's fair market value to the landowner's basis in that land. If these proposals were enacted into law, they would virtually stop all conservation donations, and would bring an end to this great success story.

There are solutions that will correct and prevent the problems we have seen in conservation donations without undermining the incentives for legitimate donations.

Those solutions require a coordinated approach between the government and the private sector with three clear steps:

- 1) Strong private sector standards, training, and accreditation;
- 2) Strong enforcement; and,
- 3) Strong reform legislation.

STANDARDS, TRAINING AND ACCREDITATION

The Land Trust Alliance has been concerned with these problems for many years. We first developed the *Land Trust Standards and Practices* in 1987 and later published a 564 page manual providing detailed guidance on legal, ethical and governance issues. Recognizing the rapid change in conservation practices and the law, the Land Trust Alliance initiated in 2003 an extensive public participation process to completely rewrite the standards. These new standards set a high bar for ethical and professional practices, and directly address the issues raised by the Senate Finance Committee staff at this hearing. The Board of the Land Trust Alliance approved these standards in October 2004 and now requires each of our member land trust to adopt the new *Land Trust Standards and Practices* as their guiding principles. Recognizing the concerns about proper conservation easement practices, the Land Trust Alliance - in partnership with the Trust for Public Land - recently published *The Conservation Easement Handbook*, a comprehensive resource on the design and management of conservation easements.

We are now designing an accreditation program to provide objective, third-party verification of ethical practices. Our goal is to encourage and recognize excellence in conservation practices and to give the public a “seal of approval” that clearly indicates those groups that meet rigorous standards. We have just completed an extensive series of meetings and surveys to solicit comments from our members. When asked if a land trust would apply for accreditation if an acceptable program were offered, 94 percent said yes. This is clearly a community that is committed to ethical practices and ensuring the public trust.

We believe that accreditation should be managed by the private sector and we are grateful for grants from the Doris Duke Charitable Foundation, the National Fish and Wildlife Foundation, the Surdna Foundation and many other funders for their support for our work on this. For the past six months, a 19-member committee of land trust leaders has worked on the design of the program and we expect to have the business plan complete by September 2005. It will take time to assess hundreds of organizations, but, assuming we can identify the necessary funds, we could begin the process as early as 2007.

To help land trusts prepare for accreditation, we are creating a comprehensive core curriculum based on the *Land Trust Standards and Practices*. We are also developing books, articles, sample policies, model documents, and an online database to help land trusts improve their practices. Once we have launched an accreditation program, the Land Trust Alliance plans to offer professional certification for individuals who have completed the core curriculum and demonstrate broad competence in land conservation.

THE IMPORTANCE OF ENFORCEMENT

Government enforcement is simply essential to discourage unwarranted tax deductions. In his testimony to this Committee on April 5th, Internal Revenue Service (IRS) Commissioner Everson acknowledged that his agency had not paid much attention to this and related areas of the law over a period of 6-8 years. That has had real consequences, including a growth in exaggerated appraisals and claims for gifts that were never actually made.

Commissioner Everson has demonstrated strong leadership in focusing investigative and enforcement resources on improper deductions for land conservation donations. He testified that more than 400 conservation easement donations were under review by his staff, and that 48 easement donations were already under audit. The IRS issued a formal Notice 2004-41 a year ago, informing both taxpayers and their own personnel about their concerns in this area. The agency conducted a training session for their personnel from around the country, and they are boosting their expertise in real estate appraisals.

We in the private sector can help, by providing greater transparency and information to the IRS and the states, and we are very willing to do that through additions to the Forms 8283 and 990. Over the past year, we have met with Commissioner Steven Miller and his staff to discuss appraisal standards, easement amendments, and increased enforcement. We invited IRS personnel to our national conference last year, both to present and to learn, and their participation was greatly appreciated by our members. This partnership is now being expanded to advance additional training programs.

The states can also play a major role in education and enforcement, as Director Maybank is demonstrating in South Carolina. He has audited every land trust doing business in his state – but he is a true friend of conservation. He believes that the long term success of conservation depends on land trusts playing by the rules, and he has published a text on conservation donations to help land trusts and easement donors comply with the law.

We think that this new enforcement activity will have a major effect on discouraging future abuses. There is no question that, whatever the rules are, they will require enforcement.

REFORM LEGISLATION

Given the success of the current tax incentives, we are understandably cautious about changing the rules. This represents a risk for us, because the current rules have worked reasonably well over the past 25 years. But we cannot turn a blind eye to abuses that, while limited, threaten the credibility of a successful tax policy that has a record of providing valuable conservation, and that holds the promise of doing so much more in the years to come.

After careful consideration, the Land Trust Alliance has decided to support reform legislation provided that it:

- Targets the worst abuses
- Is cost-effective for small, all-volunteer charities
- Protects the incentives for legitimate gifts;
- Clarifies rules, rather than complicates them; and
- Complements what the private sector and state governments can do to prevent abuses.

After discussions with many in the land trust community, we propose the following changes in federal law. In short, we believe that we must stop improper appraisals and easements that lack true conservation value, especially those on golf courses and back yards.

Strict rules that establish minimum qualifications for appraisers and appraisals.

1. Require the appraiser to be state licensed as a “general certified real estate appraiser” under the licensing required by Title XI of the Financial Institutions Reform Recovery and Enforcement Act of 1989 (FIRREA). To protect the banking industry from overvaluation of mortgages, the Congress required the states to license appraisers. That licensing system is in every state. “General certified real estate appraisers” are the highest license level, qualified by training and experience to appraise any type of real estate.
2. Require the appraiser to certify that he or she has not been subject to disbarment from practice before the IRS by the Secretary of the Treasury pursuant to 31 U.S.C. sec. 330(c).
3. Require that appraisals meet the Uniform Standards of Professional Appraisal Practice (USPAP) as required for federally-related real estate appraisals by Title XI of FIRREA. Virtually every agency in the federal government other than the IRS requires that real estate appraisers and appraisals comply with the Uniform Standards of Professional Appraisal Practice, which were created under the direction of Congress. These standards are also the standards enforced by state licensing authorities – so that requiring compliance with these standards brings state licensing authorities into action as well.
4. Request the Appraisal Standards Board and the Appraisal Foundation to establish standards for conservation easement appraisals.
5. Require that the appraiser certify in the appraisal that (1) the specific restrictions and obligations imposed by the easement and (2) the effect of existing zoning and other local ordinances, including local historic preservation ordinances, if any, have been expressly disclosed and taken into account in the valuation.

Stricter penalties for inflated appraisals.

1. Cut the thresholds for valuation misstatement penalties for charitable easement donations. Currently, under code section 6662(e)(1)(B)(i) a substantial valuation misstatement penalty applies if the deduction claimed is 100% greater than the amount determined to be correct. Under code section 6662(h) a gross valuation misstatement penalty applies if the value claimed is more than 300% greater than the amount determined to be correct. Under this proposal, the substantial valuation misstatement penalty would apply if the charitable deduction claimed is more than 50% greater than the correct amount and the gross valuation misstatement penalty would apply if the charitable deduction claimed is more than 100% greater than the correct amount.
2. Require the IRS to report all appraisals where a gross or substantial valuation misstatement is determined to the appraiser's state certification board.
3. Provide the Secretary of the Treasury with the authority, after notice and a hearing, to bar an appraiser from practice before the Department of the Treasury under 31 U.S.C. sec. 330(c) when the appraiser has issued three or more appraisals determined to be subject to substantial or gross valuation misstatements.
4. Increase the penalty for aiding and abetting understatement of tax liability under IRC 6701(b) from \$1,000 to \$10,000.

Prohibit deductions for donations most subject to abuse.

1. Prohibit deductions for the donation of a conservation restriction on a golf course or similar properties. This would cover similar commercial recreational areas, such as batting cages, miniature golf courses, driving ranges, etc.

Numerous reputable conservation organizations hold conservation easements on golf courses, protecting important conservation values other than outdoor recreation. But recently, we have seen golf course industry consultants recommending that every golf course owner should donate an easement on their property, without reference to any special values. We do not believe that the drafters of section 170(h) had golf in mind when they made outdoor recreation for the public a qualifying conservation purpose for conservation donations.

2. Prohibit deductions for the donation of a conservation easement on a backyard or other very small property unless it meets additional tests of its public benefit.

The committee staff have indicated their concern that easements can be placed on an ordinary back yard. We do not think that such an easement would qualify under the current law and regulations, because it lacks a clear conservation purpose.

We put this proposal forward very reluctantly, and believe that the details of the legislation need to be carefully drafted. There are hundreds of land trusts across the

country operating in jurisdictions in which most if not all land ownerships are less than 10 acres, and where the landscape is changing in front of people's eyes. Local, community-based land trusts may be the best hope for land conservation there, and we urge the committee not to propose a minimum size for easements without exclusions. We are very open to discussing specific conditions that would better ensure that smaller easements are, in fact, serving an important public purpose.

Make the tax code fair for working farmers and ranchers.

1. Encourage conservation donations by working farmers and ranchers by allowing deductions to be a higher percentage of their adjusted gross income over a longer period of years, so that deductions from these donors are not unduly restricted by their modest incomes (as in section 106 of S. 476 in 2003, as approved by this Committee and the full Senate). We are grateful that the committee approved these provisions in the past, and want to particularly thank Senator Baucus for his leadership on this.

The current code is structured to prevent people from using deductions to entirely avoid paying taxes. But that same structure – limiting deductions to a percentage of the donor's annual gross income – unfairly reduces the deductions available to moderate income farmers and ranchers. For land rich, cash poor farmers and ranchers, a gift of development rights may be worth ten or twenty times their annual income. These landowners are making extraordinary donations, and deserve fair treatment. Increasing the percentage of gross income such a taxpayer can take as a deduction in any one year, and extending the number of years they can carry over unused deductions, allows such donors to get a tax benefit that, while still far less than the value of their gift, is at least proportional to the gift.

2. We support the President's proposal to provide capital gains tax relief to landowners selling their land to a charity or government agency that will hold it for conservation purposes. This would help a great many local and state government conservation programs, which will always be strapped for cash, to deliver a fairer return to those landowners. We want to thank the Administration for advancing this idea, and recommend that you adopt it. This committee and the Senate approved a version of this proposal as section 107 of S. 476 in 2003.

THE NATURE CONSERVANCY

Since this hearing has considered the activities of the Nature Conservancy, it is appropriate for me to comment on their role in the larger land trust community. The Nature Conservancy is a member of the Land Trust Alliance and is widely respected as the largest holder of conservation easements in the country, managing easements on over 2 million acres of biologically significant lands and helping land trust partners and government agencies conserve another 1.3 million acres with easements. In response to the concerns raised by this committee, they commissioned outside experts to conduct an unbiased assessment of their policies on ethics, governance and transactions, and they have implemented a wide range of internal reforms. The Conservancy has been very

supportive of the new *Land Trust Standards and Practices* and our accreditation program. They have submitted to the Senate Finance Committee a very thoughtful proposal for potential reforms which demonstrates their commitment to proper conservation easement practices. From my conversations with both board members and staff, I believe that the Nature Conservancy is committed to genuine reforms.

CONCLUSION

Two decades ago, Congress passed a far-sighted bill to encourage private landowners to donate their land for public conservation purposes. This program has worked well thanks to the generosity of thousands of landowners and the hard work of 1500 land trusts throughout America. We can not allow a few bad apples to spoil a highly successful program, and we will do our part by implementing a strong program of standards, training and accreditation. In addition, we support strong reform legislation targeted at the worst abuses and consistent IRS enforcement.

In closing, I want to thank the committee for holding this hearing, for paying attention to these important issues, and for helping to encourage reforms that will ensure the public confidence in the work of land trusts. America is a vast and beautiful land, and the measures we have discussed today will help conserve this natural legacy for the future generations.

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