PRESENT LAW AND DESCRIPTION OF PROPOSALS RELATING TO FEDERAL INCOME AND ESTATE TAX PROVISIONS THAT IMPACT LAND USE CONSERVATION AND PRESERVATION

Scheduled for a Hearing
Before the
Senate Committee on Finance
on June 12, 2001

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION

June 11, 2001
JCX-53-01

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INTRODUCTION

The Senate Committee on Finance has scheduled a public hearing on June 12, 2001, on issues relating to the impact of Federal tax law on land use conservation and preservation. This document,[1] prepared by the staff of the Joint Committee on Taxation, describes selected Federal income and estate tax law provisions that affect land use conservation and preservation. Part II of this pamphlet describes a number of legislative tax proposals that relate to land use conservation and preservation.

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[1] This document may be cited as follows: Joint Committee on Taxation, *Present Law and Description of Proposals Relating to Federal Income and Estate Tax Provisions That Impact Land Use Conservation and Preservation* (JCX-53-01), June 11, 2001.

I. INCOME AND ESTATE TAX RULES RELATING TO LAND USE CONSERVATION AND PRESERVATION

A. Cost Recovery

In general

A taxpayer generally must capitalize the cost of certain property used in a trade or business. The capitalized cost of business property that is subject to exhaustion, wear, tear, or obsolescence may be recovered over time through allowances for depreciation (sec. 167). Depreciation allowances for tangible property placed in service after 1986 generally are determined under the Modified Accelerated Cost Recovery System ("MACRS") of section 168, which provides that depreciation is computed by applying specific recovery periods, placed-in-service conventions, and depreciation methods to the cost of various types of depreciable property. Intangible property acquired after July 25, 1991, generally is amortized under section 197, which provides a 15-year recovery period and applies the straight-line method to the cost of applicable property.

Under MACRS, depreciable personal and real property is divided into ten classes (3-year property, 5-year property, 7-year property, 10-year property, 15-year property, 20-year property, 25-year water utility property, 27.5-year residential rental property, 39-year nonresidential real property, and 50-year railroad grading or tunnel bores). Personal property generally is included in a property class based upon its class life. The class life of certain property is specifically provided by statute. The class life of other personal property is determined by reference to the generally applicable class lives. The 200-percent declining balance method of depreciation is used for 3-year, 5-year, 7-year, and 10-year property; the 150-percent declining balance method is used for 15-year and 20-year property and any property used in a farming business; and the straight-line method is used for other property, including most depreciable real property.

Treatment of land

The cost of land generally may not be depreciated, even if the taxpayer's use of the land may result in its erosion or other type of wear or tear (e.g., in the case of certain farming practices). An interest in land may not be amortized under section 197 (sec. 197(e)(2)). When a taxpayer acquires both land and improvements on the land in a single transaction (e.g., the purchase of an apartment building and the underlying land), the acquisition cost must be allocated between the nondepreciable land and depreciable improvements.

Certain types of improvements to land (such as sidewalks, roads, landscaping, etc.) may be depreciated. However, certain other land improvements may be so "inextricably associated" with the land as to be nondepreciable. Examples of nondepreciable land improvements include certain clearing and grading costs associated with land and golf course improvements. The cost of demolishing any structure generally must be charged to the capital account with respect to the land on which the demolished structure was located (sec. 280B).

The cost of extracting minerals and other natural resources imbedded in land are recoverable through depletion allowances (sec. 611).

B. Income Tax Treatment of Dispositions of Land

Capital gains treatment

In general, gain or loss reflected in the value of an asset is recognized for income tax purposes at the time the taxpayer disposes of the property. On the sale or exchange of capital assets held for more than one year, gain generally is taxed to an individual taxpayer at a maximum marginal rate of 20 percent. However, gain attributable to real estate depreciation deductions that were previously claimed against ordinary income is taxed at a maximum marginal rate of 25 percent. Losses from the sale or exchange of capital assets are deductible only the extent of the gains from the sale or exchange of other capital assets, plus, in the case of individuals, $3,000.

Land is a capital asset, unless it is held primarily for sale to customers in the ordinary course of the taxpayer's trade or business, or it is used in the taxpayer's trade or business. In addition, if the gains from property, including land, used in a taxpayer's trade or business exceeds the losses from such property, the gains and losses are treated as capital gains.

Deferral of gain or loss

Several provisions allow a taxpayer to defer gain when property, including land, is disposed of. For example, gain or loss is deferred if land held for investment or business use is exchanged for property of a like kind (generally defined to include other real estate) (sec. 1031). Likewise, gain or loss is deferred if land is condemned and replaced with other property of a like kind (sec. 1033(g)).

C. Rehabilitation Expenditures

In general

An income tax credit is provided for a portion of certain expenditures incurred in the rehabilitation of certified historic structures and certain other buildings first placed in service before 1936. The amount of the credit is equal to 20 percent of the qualified rehabilitation expenditures for a certified historic structure and 10 percent of the qualified rehabilitation expenditures for a qualified rehabilitated building other than a certified historic structure.

In order for a rehabilitation expenditure to qualify for the credit applicable to certified historic structures, the rehabilitated building must be listed in the National Register of Historic Places or be located in a registered historic district and certified by the Secretary of the Interior as being of historic significance to the district. In addition, the Secretary of the Interior must certify that the rehabilitation is consistent with the historic character of the building or the historic district in which the building is located.

In the case of other rehabilitations, a building (or its structural components) is a qualified rehabilitated building if: (1) the building is substantially rehabilitated; (2) the building was placed in service before the beginning of the rehabilitation; (3) the rehabilitation meets a 75-percent retention test; (4) depreciation is allowable with respect to the building; and (5) the building was first placed in service before 1936.

A building is substantially rehabilitated if the qualified rehabilitation expenditures incurred during the 24-month period selected by the taxpayer exceed the greater of: (1) the adjusted basis of the building (and its structural components) as of the beginning of the period (or as of the holding of the building, if later); or (2) $5,000.

The 75-percent retention test requires the retention, in place, of (1) at least 75 percent of the building's existing external walls (including at least 50 percent as external walls) and (2) at least 75 percent of the building's internal structural framework. In general, a building's internal structural framework includes all load-bearing internal walls and any other structural supports, including the columns, girders, beams, trusses, spandrels, and all other items that are essential to the stability of the building.

Qualified rehabilitation expenditures generally include any amounts properly chargeable to capital account in connection with the rehabilitation of a building, but do not include the cost of: (1) acquiring the building or any interest in the building; (2) facilities related to a building (e.g., a parking lot); (3) enlarging an existing building; or (4) rehabilitations allocable to a portion of a building that is (or is reasonably expected to be) tax-exempt use property.

Other rules

The rehabilitation credit is part of the investment credit, which, in turn, is part of the general business credit. The general business credit may offset the first $25,000 of a taxpayer's regular tax liability, plus 75 percent of the taxpayer's regular tax liability in excess of $25,000. The general business credit is not allowed to offset a taxpayer's minimum tax liability.

Taxpayers claiming the credit must reduce their adjusted basis in the building by the amount of the credit. Capitalized rehabilitation expenditures must be depreciated using a straight-line method.

The credit is subject to recapture if the rehabilitated building is disposed of, or otherwise ceases to be a qualified property, within five years after the property is placed in service.

D. Environmental Remediation Expenditures

Taxpayers can elect to treat certain environmental remediation expenditures that would otherwise be chargeable to the taxpayer=s capital account as deductible in the year paid or incurred (sec. 198). The deduction applies for both regular and alternative minimum tax purposes. The expenditure must be incurred in connection with the abatement or control of hazardous substances at a qualified contaminated site. Eligible expenditures are those paid or incurred before January 1, 2004.

In general, any expenditure for the acquisition of depreciable property used in connection with the abatement or control of hazardous substances at a qualified contaminated site does not constitute a qualified environmental remediation expenditure. However, depreciation deductions allowable for such property, which would otherwise be allocated to the site under the principles set forth in *Commissioner v. Idaho Power Co.*[2] and section 263A, are treated as qualified environmental remediation expenditures.

A Aqualified contaminated site@ generally is any property that: (1) is held for use in a trade or business, for the production of income, or as inventory; and (2) is certified by the appropriate State environmental agency to contain (or potentially contain) a hazardous substance (so-called Abrownfields@). However, sites that are identified on the national priorities list under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 cannot qualify as targeted areas. Hazardous substances are those substances so designated under sections 101(14) and 102 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, but does not include substances the removal or remediation of which is not permitted under section 104 of the Act by reason of subsection (a)(3).

In the case of property with respect to which a qualified environmental remediation expenditure otherwise would have been capitalized, any deduction allowed under section 198 is treated as a depreciation deduction and the property is treated as section 1245 property. Thus, deductions for qualified environmental remediation expenditures are subject to recapture as ordinary income upon sale or other disposition of the property.

E. Reforestation Expenditures

1. Amortization of reforestation costs

A taxpayer may elect to amortize up to $10,000 ($5,000 in the case of a separate return filed by a married individual) of qualifying reforestation expenditures incurred during the taxable year with respect to qualifying timber property (sec. 194). Amortization is taken over 84 months (7 years) and is subject to a mandatory half-year convention.[3] In the case of an individual, the amortization deduction is allowed for purposes of determining adjusted gross income (an above-the-line deduction) rather than as an itemized deduction.

Qualifying reforestation expenditures include the direct costs that a taxpayer incurs in connection with the forestation or reforestation of a site by planting or seeding, and include the costs for the preparation of the site, the cost of the seed or seedlings, and the cost of the labor and tools (including depreciation of long-lived assets such as tractors and other machinery) used in reforestation activities. Qualifying reforestation expenditures do not include expenditures that would otherwise be deductible and do not include costs for which the taxpayer has been

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[2] 418 U.S. 1 (1974), holding that equipment depreciation allocable to the taxpayer=s construction of capital facilities must be capitalized under section 263(a)(1).

[3] Under the half-year convention, all reforestation expenditures are considered to be incurred on the first day of the first month of the second half of the taxable year. Thus, an amortization deduction equal to 6/84 of the expenditures for the year is allowed in the first and eighth years and an amortization deduction equal to 1/7 (12/84) of such expenditures is allowed in the second through seventh years.

reimbursed under a governmental cost sharing program, unless the amount of the reimbursement is also included in the taxpayer's gross income.

Qualifying timber property includes any woodlot or other site that is located in the United States that will contain trees in significant commercial quantities and that is held by the taxpayer for the planting, cultivating, caring for, and cutting of trees for sale or use in the commercial production of timber products. Treasury regulations require that the site consist of at least one acre that is devoted to such activities. A taxpayer may hold qualifying timber property in fee or by lease. Where the property is held by one person for life with the remainder to another person, the life tenant is considered the owner of the property for this purpose.

Reforestation amortization is subject to recapture as ordinary income on the sale of qualifying timber property within 10 years of the year in which the qualifying reforestation expenditures were incurred.

2. Reforestation tax credit

A tax credit is allowed in an amount equal to 10 percent of the reforestation expenditures incurred during the year that are properly elected to be amortized under sec. 194 (sec. 48(b)). The amount that is allowed for amortization under sec. 194 is reduced by 50 percent of the amount of credit claimed. The amount that is allowed as a credit is subject to recapture if the qualifying timber property to which the expenditure relates is disposed of within 5 years.

F. Tax-Exempt Bonds and Tax-Credit Bonds

1. Tax-exempt bonds

<u>In general</u>

Interest on debt issued by States or local governments is excluded from income if the proceeds of the borrowing are used to carry out governmental functions of those entities or the debt is repaid with governmental funds (sec. 103). Like other activities carried out or paid for by States and local governments, the construction, renovation, and operation of governmental transportation infrastructure projects such as public highways or governmental mass commuting (rail and bus) systems are eligible for this financing.

Interest on bonds that nominally are issued by States or local governments, the proceeds of which, however, are used (directly or indirectly) by a private person and payment of which is derived from funds of such a private person, is taxable, unless the purpose of the borrowing is approved specifically in the Code or in a non-Code provision of a revenue Act. These bonds are called "private activity bonds." The term "private person" includes the Federal Government and all other individuals and entities other than States or local governments.

Private activities eligible for financing with tax-exempt private activity bonds

The Code includes several exceptions permitting States or local governments to act as conduits providing tax-exempt financing for private activities.

States or local governments may issue tax-exempt "exempt-facility bonds" to finance property for certain private businesses. Property eligible for this financing includes transportation (airports, ports, local mass commuting, and high speed intercity rail facilities); privately owned and/or privately operated public works facilities (sewage, solid waste disposal, local district heating or cooling, and hazardous waste disposal facilities); privately-owned and/or privately operated low-income rental housing; and certain private facilities for the local furnishing of electricity or gas. A further provision allows tax-exempt financing for "environmental enhancements of hydro-electric generating facilities." Tax-exempt financing also is authorized for capital expenditures for small manufacturing facilities and land and equipment for first-time farmers ("qualified small-issue bonds"), local redevelopment activities ("qualified redevelopment bonds"), and eligible empowerment zone and enterprise community businesses.

Both capital expenditures and limited working capital expenditures of charitable organizations described in section 501(c)(3) of the Code may be financed with tax-exempt private activity bonds ("qualified 501(c)(3) bonds"). Qualified 501(c)(3) bonds may be issued only to finance exempt, as opposed to unrelated business, activities of these organizations. However, if the bonds are issued to finance property which is intended to be, or is in fact, sold to a private business while the bonds are outstanding, bond interest may be taxable. An example of such an issue would be qualified 501(c)(3) bonds issued to finance the purchase of land and standing timber, when the timber was to be sold.

As is true of other private activities receiving tax-exempt financing, beneficiaries of qualified 501(c)(3) bonds are restricted in the arrangements they may have with private businesses relating to control and use of bond-financed property.

Finally, tax-exempt private activity bonds may be issued to finance limited non-business purposes: student loans and mortgage loans for owner-occupied housing ("qualified mortgage bonds" and "qualified veterans' mortgage bonds").

General restrictions on State and local government bond financing for private activities

Like many Federal direct spending programs, issuance of State and local government private activity bonds is subject to general restrictions on amount and use. The following discussion illustrates some of the major restrictions.

State volume limitations.--Issuance of most tax-exempt private activity bonds is subject to annual per-State volume limitations. Each State (including local governments within the State) is allowed to issue an annual amount of these bonds not exceeding the greater of $62.50 per resident of the State or $187.5 million in calendar year 2001. These volume limits are scheduled to increase to $75 per resident of the State or $225 million beginning in calendar year 2002. Beginning in calendar year 2003, the volume limit will be adjusted annually for inflation. States may elect to carryover their unused private activity bond volume authority for designated activities for a period of up to three years. Bond authority that is not used within the carryforward period lapses.

The State volume limits do not apply to State and local government bonds for section 501(c)(3) organizations, for airports and ports, for governmentally owned (but privately operated) solid waste disposal facilities, for environmental enhancements of hydro-electric generating facilities, for governmentally owned (but privately operated) high-speed intercity rail facilities,[4] for qualified veterans' mortgage loans,[5] and for financing property in empowerment zones.

Other restrictions on private activity bonds.--Among the other Federal restrictions applicable to private activity (but not to governmental) State and local government bonds are the following:

- A requirement that public notice be given and a hearing held before issuance of the bonds;
- A restriction on the costs of issuance (e.g., bond attorney and underwriter fees) that may be financed with bond proceeds to an amount not exceeding two percent of the bond issue;
- A minimum rehabilitation requirement for existing property that is acquired with State and local government bond proceeds;
- A limit on the amount of land that may be financed with any single bond issue;
- A limit on the maximum maturity of the bonds, determined by reference to the economic life of the property being financed; and
- Loss of interest deductions for private borrowers receiving bond proceeds if the bond-financed property ceases to be used in a qualifying use.

Arbitrage restrictions on tax-exempt bonds

The Federal income tax does not apply to income of States and local governments that is derived from the exercise of an essential governmental function. To prevent these tax-exempt entities from issuing more Federally subsidized tax-exempt bonds than is necessary for the activity being financed or from issuing such bonds earlier than necessary, the Code includes arbitrage restrictions limiting the ability to profit from investment of tax-exempt bond proceeds. In general, arbitrage profits may be earned only during specified periods (e.g., defined “temporary periods”) before funds are needed for the purpose of the borrowing or on specified types of investments (e.g., “reasonably required reserve or replacement funds”). Subject to limited exceptions, investment profits that are earned during these periods or on such investments must be rebated to the Federal Government.

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[4] Bonds for privately owned high-speed intercity rail facilities must receive a State volume limit allocation equal to 25 percent of the bond amount.

[5] Qualified veteran’s mortgage bonds are subject to separate limits based on historical State issuance as part of the 1984-enacted phase-out of that program.

The Code includes three exceptions applicable to bonds for transportation infrastructure facilities. First, issuers of all types of tax-exempt bonds are not required to rebate arbitrage profits if all of the proceeds of the bonds are spent for the purpose of the borrowing within six months after issuance. In the case of governmental bonds (including bonds to finance public highways) the six-month expenditure exception is treated as satisfied if at least 95 percent of the proceeds is spent within six months and the remaining five percent is spent within 12 months after the bonds are issued.

Second, in the case of bonds to finance certain construction activities, including governmentally owned transportation infrastructure facilities, the six-month period is extended to 24 months for construction proceeds. Arbitrage profits earned on construction proceeds are not required to be rebated if all such proceeds (other than certain retainage amounts) are spent by the end of the 24-month period and prescribed intermediate spending percentages are satisfied.

Third, governmental bonds issued by “small” governments are not subject to the rebate requirement. Small governments are defined as general purpose governmental units that issue no more than $5 million of tax-exempt governmental bonds in a calendar year. The $5 million limit is increased to $15 million if at least $10 million of the bonds are used to finance public schools.

2. Tax credit bonds for qualified zone academies

A nonrefundable income tax credit in an amount equal to a credit rate (set by the Treasury Department) multiplied by the face amount of certain qualified zone academy bonds is allowed to certain financial institutions (i.e., banks, insurance companies, and corporations actively engaged in the business of lending money) (sec. 1397E). A taxpayer holding a qualified zone academy bond on the credit allowance date (i.e., the annual anniversary of the bond’s issuance) is entitled to a credit. The credit is includible in gross income (as if it were an interest payment on the bond), and may be claimed against regular income tax liability and alternative minimum tax liability.

A qualified zone academy bond is defined as any bond issued by a State or local government, provided that: (1) at least 95 percent of the proceeds are used for the purpose of renovating, providing equipment to, developing course materials for use at, or training teachers and other school personnel in a “qualified zone academy”; and (2) private entities have promised to contribute to the qualified zone academy certain equipment, technical assistance or training, employee services, or other property or services with a value equal to at least 10 percent of the bond proceeds.

Issuance of qualified zone academy bonds is subject to an annual national limitation of $400 million for 1998 through 2001, and zero thereafter. The national limitation for a calendar year is allocated by the Secretary of the Treasury among the States based on their respective populations of individuals below the poverty line. This limitation is then allocated by the State education agency to qualified zone academies within such State.

G. Contributions of Capital Gain Property and Qualified Conservation Interests

1. Income tax provisions

Charitable contributions generally

In general, a deduction is permitted for charitable contributions, subject to certain limitations that depend on the type of taxpayer, the property contributed, and the donee organization. The amount of deduction generally equals the fair market value of the contributed property on the date of the contribution. Charitable deductions are provided for income, estate, and gift tax purposes (secs. 170, 2055, and 2522 respectively).

In general, in any taxable year, charitable contributions by a corporation are not deductible to the extent the aggregate contributions exceed 10 percent of the corporation's taxable income computed without regard to net operating or capital loss carrybacks. For individuals, the amount deductible is a percentage of the taxpayer's contribution base, which is the taxpayer's adjusted gross income computed without regard to any net operating loss carryback. The applicable percentage of the contribution base varies depending on the type of donee organization and property contributed.

Gifts of certain types of property interests are subject to special restrictions, either as to the amount deductible or as to the types of property interests for which a deduction is permitted. For example, a contribution of less than the donor's entire interest in property generally is not allowable as a charitable deduction unless the gift takes the form of an interest in a unitrust, annuity trust, or a pooled income fund.

Capital gain property

Capital gain property is property, which if sold at fair market value at the time of contribution, would have resulted in gain that would have been long-term capital gain. Contributions of capital gain property to a qualified charity are deductible at fair market value within certain limitations. Contributions of capital gain property to charitable organizations described in section 170(b)(1)(A) (e.g., public charities, private foundations other than private non-operating foundations, and certain governmental units) generally are deductible up to 30 percent of the taxpayer's contribution base. Contributions of capital gain property to charitable organizations described in section 170(b)(1)(B) (e.g., private non-operating foundations) are deductible up to 20 percent of the taxpayer's contribution base.

For purposes of determining whether a taxpayer's aggregate charitable contributions in a taxable year exceed the applicable percentage limitation, contributions of capital gain property are taken into account after other charitable contributions. Contributions of capital gain property that exceed the percentage limitation may be carried forward for five years.

Qualified conservation contributions

Qualified conservation contributions are not subject to the "partial interest" rule, which generally bars deductions for charitable contributions of partial interests in property. A qualified conservation contribution is a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. A qualified real property interest is defined as: (1) the entire interest of the donor other than a qualified mineral interest; (2) a remainder interest; or (3) a restriction (granted in perpetuity) on the use that may be made of the real property. Qualified organizations include certain governmental units, public charities that meet certain public support tests, and certain supporting organizations. Conservation purposes include: (1) the preservation of land areas for outdoor recreation by, or for the education of, the general public; (2) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem; (3) the preservation of open space (including farmland and forest land) where such preservation will yield a significant public benefit and is either for the scenic enjoyment of the general public or pursuant to a clearly delineated Federal, State, or local governmental conservation policy; and (4) the preservation of a historically important land area or a certified historic structure.

Qualified conservation contributions of capital gain property are subject to the same limitations and carryforward rules of other charitable contributions of capital gain property.

2. Estate tax provisions[6]

Estate tax exclusion for land subject to permanent conservation easement

An executor may elect to exclude, for Federal estate tax purposes, 40 percent of the value of any land subject to a qualified conservation easement, up to a maximum exclusion of $400,000 in 2001, and $500,000 in 2002 and thereafter (sec. 2031(c)). If the value of the conservation easement is less than 30 percent of the value of the land without the easement (reduced by the value of any retained development rights), then the exclusion percentage is reduced 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.

A qualified conservation easement is one that meets the following requirements: (1) the land has been owned by the decedent or a member of the decedent's family at all times during the three-year period ending on the date of the decedent's death; and (2) a qualified conservation contribution (within the meaning of sec. 170(h)) of a qualified real property interest (as generally defined in sec. 170(h)(2)(C)) was granted by the decedent or a member of his or her family.[7] For

[6] The Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16 ("2001 Act"), signed into law on June 7, 2001, repeals the estate tax for decedents dying after December 31, 2009. All provisions in title V of the 2001 Act (which includes the provisions regarding repeal of the estate tax) cease to apply to estates of decedents dying after December 31, 2010 (Sec. 901 of the 2001 Act).

[7] Sec. 551 of the 2001 Act eliminates the requirement that the land be located within 25 miles of a metropolitan area (as defined by the Office of Management and Budget), national park, wilderness area, or within 10 miles of an Urban National Forest (as designated by the Forest Service of the Department of Agriculture), effective for estates of decedents dying after December 31, 2000. Thus, a qualified conservation easement exclusion may be claimed with respect to any property that is located in the United States or its possessions. All provisions in title V of the 2001 Act (which includes the provision that eliminates the distance requirement in

purposes of the provision, preservation of a historically important land area or a certified historic structure does not qualify as a conservation purpose.

In order to qualify for the exclusion, a qualifying easement must have been granted by the decedent, a member of the decedent's family, the executor of the decedent's estate, or the trustee of a trust holding the land, no later than the date of the election. To the extent that the value of such land is excluded from the gross estate, the property is not stepped up to its fair market value on the date of the decedent's death. The basis of such land acquired from a decedent's estate is the same as in the hands of the decedent before death (i.e., a carryover basis). Property financed with acquisition indebtedness is eligible for this provision only to the extent of the net equity in the property. The exclusion from estate taxes does not extend to the value of any development rights retained by the decedent or donor.

H. Self-Employment Taxes on Conservation Reserve Program Payments

Generally, employment taxes under the Self-Employment Contributions Act ("SECA tax") are imposed on an individual's self-employment income within the Social Security wage base. Net earnings from self-employment generally means gross income (including the individual's net distributive share of partnership income) derived by an individual from any trade or business carried on by the individual less applicable deductions. A recent court decision held that payments made under the Department of Agriculture's conservation reserve program established pursuant to the Food Security Act of 1985 are includible in an individual's self-employment income for purposes of SECA tax.[8]

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section 2031(c)) cease to apply to estates of decedents dying after December 31, 2010 (Sec. 901 of the 2001 Act).

[8] *Wuebker v. Commissioner*, 205 F.3d 897 (6th Cir. 2000), *rev'g* 110 T.C. 431 (1998).

II. PROPOSALS RELATING TO LAND USE CONSERVATION AND PRESERVATION

A. S. 808 (introduced by Senator Jeffords and others on April 15, 1999)

S. 808 would provide a 50-percent exclusion of the gain on the sales of land or interests in land or water to eligible entities for conservation purposes. The land or interest in land or water must have been owned by the taxpayer or a member of the taxpayer's family at all times during the 3-year period ending on the date of the sale. An eligible entity would be: (1) any agency of the United States or of any State or local government, or (2) any other organization described in section 501(c)(3) and exempt from tax under section 501(a) that is organized and at all times operated principally for one or more specified conservation purposes as described in the proposal.

B. S. 1392 (introduced by Senator Baucus on July 19, 1999)

S. 1392 would provide incentives for the voluntary conservation of endangered or threatened species by: (1) providing an exclusion for income tax purposes for cost-sharing payments under the Partners for Fish and Wildlife Program; (2) expanding the availability of the income tax deduction for qualified conservation contributions; and (3) providing a maximum $10 million estate tax exclusion for certain land subject to an endangered species conservation agreement.[9]

C. S. 1558 (introduced by Senators Baucus and Hatch on August 5, 1999)

S. 1558 would provide a new income tax credit for holders of "Community Open Space" bonds, which would be bonds, 95 percent or more of the proceeds of which must be used for a "qualified environmental infrastructure project." A qualified environmental infrastructure project would include acquisition of qualified property for use as open space, wetlands, public parks, or greenways, or to improve access to public lands by non-motorized means. A qualified environmental infrastructure project also may include the construction, rehabilitation, or repair of a visitor's facility in connection with qualified property including nature centers, campgrounds, or hiking and biking trails.

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[9] S. 1392 also contains a provision that would eliminate the requirement that land be located within a certain distance from a metropolitan area, national park, wilderness area, or Urban National Forest to be eligible for the estate tax exclusion. Sec. 551 of the 2001 Act eliminated this requirement, effective for estates of decedents dying after December 31, 2000. Thus, a qualified conservation easement exclusion may be claimed with respect to any property that is located in the United States or its possessions.

The 2001 Act repeals the estate tax for decedents dying after December 31, 2009. All provisions in title V of the 2001 Act (which includes the provisions that repeal the estate tax and eliminate the distance requirement in section 2031(c)) cease to apply to estates of decedents dying after December 31, 2010 (Sec. 901 of the 2001 Act).

D. Section 4 of S. 312 (introduced by Senators Grassley, Baucus, Conrad, Lincoln, and others on February 13, 2001) and S. 315 (introduced by Senators Brownback, Daschle, Jeffords, Baucus, and others on February 13, 2001)

Section 4 of S.312 and S. 315 would provide that for purposes of the tax imposed under the Self-Employment Contributions Act of 1954 ("SECA"), net earnings from self-employment would not include conservation reserve program payments under section 1233(2) of the Food Security Act of 1985, which includes annual rental payments in an amount necessary to compensate for: (1) the conversion of highly erodible cropland normally devoted to the production of an agricultural commodity on a farm or ranch to a less intensive use, and (2) the retirement of any cropland base and allotment history that the owner or operator agrees to retire permanently.

E. S. 701 (introduced by Senator Baucus on April 5, 2001)

Section 2

Section 2 of S.701 would provide that charitable contributions of capital gain property by an eligible farmer or rancher would be deductible up to 100 percent of the taxpayer's contribution base. Such contributions would be taken into account after all other charitable contributions.

The proposal defines an eligible farmer or rancher as a taxpayer whose gross income from the trade or business of farming is at least 51 percent of the taxpayer's gross income for the taxable year, and, if the taxpayer is a C corporation, the taxpayer's stock is not publicly traded on a recognized exchange.

The increased percentage limitation would be available only if the taxpayer elects to take the deduction for capital gain property for a 15-consecutive-taxable-year period. A taxpayer may make only one election per contribution of capital gain property, which shall be irrevocable.

Section 3

Section 3 of S.701 would eliminate the 30 percent limitation for qualified conservation contributions of capital gain property to organizations described in section 170(b)(1)(A). Elimination of the 30 percent limitation would mean that the 50 percent limitation generally applicable for non-capital gain property contributions by individuals to section 170(b)(1)(A) organizations would apply. However, if such contributions are made by eligible farmers or ranchers that make an election (as described above), then the 100 percent limitation would apply.

The proposal would provide that the five-year carryforward rule would not apply to a qualified conservation contribution of capital gain property. The proposal instead would provide for an unlimited carryforward to the extent of the excess of the qualified conservation contribution over the taxpayer's contribution base.

<u>Section 4</u>

Section 4 of S.701 would treat eligible farmers and ranchers (as defined above) that are corporations as individuals for purposes of section 170, but only with respect to qualified conservation contributions. Accordingly, the percentage limitations and carryforward rules that apply to individuals would apply to qualified conservation contributions by eligible corporate farmers and ranchers.

F. S. 822 (introduced by Senators Murray, Daschle, and others on May 3, 2001)

S. 822 would modify the rules governing issuance of qualified 501(c)(3) bonds to permit issuance of long-term bonds for the acquisition of timber land by organizations a principal purpose of which is conservation of that land as timber land. Under the bill, these bonds would not have to be repaid (to avoid loss of tax-exemption on interest) when the timber is harvested and sold. In addition, the bill would allow these section 501(c)(3) organizations to enter into certain otherwise prohibited timber management arrangements with private businesses without losing tax-exemption on bonds used to finance the property and timber.