



SUMMARY REPORT

Agenda Date: 8/6/2019

To: Board of Directors of the Sonoma County Agricultural Preservation and Open Space District
Department or Agency Name(s): Sonoma County Agricultural Preservation and Open Space District
Staff Name and Phone Number: Sheri Emerson, 565-7358
Vote Requirement: Majority
Supervisory District(s): Fifth

Title:

First Amendment to Howlett Forest Conservation Easement

Recommended Action:

- A) Adopt a Resolution making certain findings and authorizing the President to execute a First Amendment to the Conservation Easement as requested by the Howlett Family Partnership to support its eligibility for a charitable tax deduction. (Fifth District)
- B) Delegate authority to the General Manager to execute similar amendments to other conservation easements held by the Sonoma County Agricultural Preservation and Open Space District if requested by a landowner under similar circumstances.

Executive Summary:

Sonoma County Agricultural and Open Space District staff requests the Board approve an amendment to the Howlett Forest Conservation Easement to modify a provision that governs the allocation of proceeds as between the landowner and the Sonoma County Agricultural and Open Space District in the unlikely event that another public agency condemns the property. The Howlett Family Partnership has requested this change to support its eligibility for a charitable tax deduction. The proposed amendment does not change any of the resource protections established by the easement. The amendment merely protects the minimum compensation due to the Sonoma County Agricultural and Open Space District in the unlikely case of condemnation.

Discussion:

In April 2017, the Sonoma County Agricultural and Open Space District (Ag + Open Space) acquired a conservation easement over the 1,380-acre Howlett Forest property northwest of Lake Sonoma. Because the landowners donated a portion of the easement value to Ag + Open Space, they may be eligible for a federal tax deduction under Internal Revenue Code § 170(h).

Language in the Howlett Forest Easement permits the deduction of the value of improvements made by the landowner from the proceeds received from a condemning agency before calculating Ag + Open Space's share. This language is common in conservation easements across the country, as it reflects many landowners' expectations of fairness.

However, this language has been subject to recent scrutiny by the Internal Revenue Service (IRS). The IRS asserts that, by allowing a landowner to be compensated for the value of improvements made after the donation, the amount of residual proceeds available for the donee may fall below the minimum prescribed by the IRS's regulations. (26 C.F.R. § 1.170A-14(g)(6).) The IRS interprets the applicable regulations to require that the parties' respective interests in the proceeds of a condemnation action remain fixed over time, based on the ratio of the value of the conservation easement at the time of the gift, divided by the value of the property as a whole at that time. (26 C.F.R. § 1.170A14(g)(6)(ii).) This interpretation has been the subject of some controversy, in no small part because it deviates from prior IRS advisory rulings, and because it could have a chilling effect on donor activity. Nonetheless, in August of 2018, the IRS prevailed in a case challenging this interpretation of the applicable regulations. (*PBBM-Rose Hill, Ltd. v. Comm'r*, 900 F.3d 193 (2018).) As a result, landowners may reasonably anticipate the potential that the IRS will deny their tax deduction based on the wording of the extinguishment clause in their donated conservation easement. This court decision is what prompted the Howlett Family Partnership to approach Ag + Open Space with a request to modify their conservation easement.

Modifying the language at issue, as shown in the redline on file with the Clerk, will result in Ag + Open Space recovering a portion of the improvement value in the unlikely case of condemnation. The proposed changes also require each party to bear their own costs in connection with any legal actions to respond to a condemnation, rather than using the proceeds recovered from the condemning agency to cover all such costs before the remainder is divided as between the parties in proportion to their interests. Both of these changes are made in an effort to conform the easement to the IRS's current application of 26 C.F.R. § 1.170A14(g)(6)(ii). The proposed amendment would not impact conservation values and would not convey back any rights expressly extinguished. Therefore, the proposed amendment is consistent with Ag + Open Space's Easement Amendment Policy, as further described in the attached resolution, which staff requests the Board to adopt.

Because the proposed amendment clearly does not convey any real property interest to the landowner, nor does it impair any of Ag + Open Space's contractual rights under the easement, staff did not take this item to the Fiscal Oversight Commission for review as to the adequacy of the consideration provided to Ag + Open Space for this transaction. The General Manager proposes to split the costs of the proposed amendment with the landowner, as an exception to Ag + Open Space policy requiring landowners to pay all costs for any amendment they initiate.

Staff recommends that the Board adopt the attached resolution making findings necessary under the Ag + Open Space Easement Amendment Policy, authorizing the President to execute a First Amendment to the Conservation Easement with the Howlett Family Partnership, and delegating authority to the General Manager, with prior review and approval from County Counsel, to execute similar amendments to other conservation easements if requested by a landowner under similar circumstances. The requested delegation to the General Manager would streamline the process, save taxpayer money, and support tax deductions intended by landowners, without any negative impacts to the land or Ag + Open Space's rights under the conservation easements that may prompt this concern.

Prior Board Actions:

17-0095 2/21/2017: Approving Acquisition of Conservation Easement

FISCAL SUMMARY

Expenditures	FY 19-20 Adopted	FY20-21 Projected	FY 21-22 Projected
Budgeted Expenses	5,000	0	0
Additional Appropriation Requested	0	0	0
Total Expenditures	5,000	0	0
Funding Sources			
General Fund/WA GF			
State/Federal			
Fees/Other	5,000		
Use of Fund Balance			
Contingencies			
Total Sources	5,000		

Narrative Explanation of Fiscal Impacts:

This amount is appropriated in the FY 2019-2020 budget and will be incorporated in the projected year's budgets. The \$5,000 represents half of the total Ag + Open Space estimated cost of processing the amendment to the easement, which will be wholly expended in FY 2019-2020. O&M would fund the cost of processing similar amendments, at the discretion of the General Manager, if exceptions are granted to landowners in the future.

Staffing Impacts:			
Position Title (Payroll Classification)	Monthly Salary Range (A-I Step)	Additions (Number)	Deletions (Number)

Narrative Explanation of Staffing Impacts (If Required):

No additional appropriations are needed.

Attachments:

1. First Amendment to Conservation Easement
2. Resolution

Related Items "On File" with the Clerk of the Board:

1. Redline Changes to Conservation Easement
2. Conservation Easement
3. Cost Recovery Agreement

