

NewsLinks

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Conservation Easements on Golf Courses, Part I

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Conservation easements are an increasingly common tool used in estate planning, income tax planning and land preservation by individuals who own substantial pieces of land. For many years, conservation organizations have solicited donations of conservation easements in order to meet their environmental preservation goals. More recently, with the heightened nationwide interest in promoting environmentally sound practices in the design and management of golf courses as well as more sophisticated income and estate tax planning among golf course owners, we are seeing an increasing number of golf course owners, including individuals, partnerships or limited liability companies, placing conservation easements on golf courses and surrounding environmentally significant land.

If you have never had the opportunity to consider conservation easements, here are some of the most commonly asked questions about conservation easements, what they are, how they work and why they may be useful to you.

What is a conservation easement? A conservation easement is a written agreement between a landowner and a qualified, non-profit conservation organization or a governmental agency in which the landowner agrees to restrict the future use of his land. This may mean agreeing not to further develop the land or only to develop the land to a limited extent that does not compromise the conservation purposes of the conservation easement. It will also prohibit specific activities that would degrade the environmental or scenic attributes of the property, such as mineral extraction, stream diversion and clear cut logging. The conservation organization or government entity that enters into the conservation easement with the land owner is given the power to enforce these restrictions. In this way the agreement functions like a donation of the development rights that the land owner would otherwise have as owner of the land.

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A conservation easement will ordinarily be a perpetual agreement – and must be in order to be eligible for tax benefits – it will be binding on future owners of the land and would be recorded in the public office where deeds are recorded in the county in which the land is located.

What may I do with my land after I have imposed a conservation easement?

This depends upon the terms of the conservation easement agreement. The conservation easement restricts uses and activities that will infringe upon the highest and best use of the land. This usually entails a substantial reduction of the future development potential of the land. The conservation easement does not, however, transfer legal ownership. The land owner keeps legal ownership of the land and may use the land for anything that is not prohibited by the easement document. For example, a conservation easement might permit agricultural activities on the land, it may permit certain outdoor recreation uses or it may permit a limited number of dwellings or other buildings in locations carefully selected and controlled consistent with the purposes of the conservation easement.

A little known fact is that, with proper planning, conservation easements may allow the owner to reserve certain development rights in the land, provided that those reserved rights do not compromise the purposes of the conservation easement. This requires a careful assessment of, among other things, the ecological and scenic values of the property. Properly done, retaining limited reserved rights will not jeopardize the ability to use the tax and estate planning benefits of a conservation easement.

Do I have to allow the public to use my land? It is not necessary to allow public access to your land to qualify for the tax benefits of a conservation easement. Although some easements do require public access and do qualify for the tax benefits under the IRS regulations on that basis,

there are provisions in the IRS regulations that allow a conservation easement to qualify for tax benefits without requiring public access. Among these are conservation easements that have a scenic purpose or a purpose of protecting a natural habitat. However, certain golf course easements do qualify for tax benefits on the basis that they require the land, or a part of the land, to be made available for outdoor recreation or education of the general public.

Do I have to restrict all of my land under a conservation easement? No. A landowner may subject any part of his or her land to a conservation easement. However, in order to qualify for tax benefits, it will be necessary that the land covered by the conservation easement have conservation value and meet the conservation purpose standards of the IRS regulations. For this purpose, the advice an experienced conservation organization or conservation planner is recommended.

How can I reduce my income taxes by using a conservation easement? A conservation easement that meets the requirements of the IRS regulations affords to the owner an income tax deduction for the charitable contribution of the development recording a perpetual conservation easement. The amount of that tax deduction can be rights that are given up by signing and generally described as the difference between the value of the land before restriction by the conservation easement and the value of the land after imposition of the conservation easement on the land, which requires a "before and after" appraisal. It should be noted that the benefit of the tax deduction to a "before and after" appraisal.

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Linking Up

The Golf Course Market As I See It

– September, 2003

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These are interesting times in the golf course business. First, earlier this year the biggest portfolio in the business (National Golf Properties) was sold to investors. However, this has NOT started a flurry of transactions. Golf courses are still a challenge to sell and I still observe a gap between buyers and sellers based on acceptable capitalization rates. Buyers are looking for bargains (12%+ cap rates) and sellers are still hopeful of selling for top dollar (10% cap rates). All this being said, I do sense increased activity in the marketplace, which should settle somewhere in between the above mentioned rates.

One of the most significant things I've seen is that some courses are considering alternative uses (other than golf) for their properties. A look back into history shows that many golf courses have been redeveloped through the years as their locations become too valuable for golf. Some become shopping centers, some become housing developments and we have just received an assignment for one that has the ability to be redeveloped into a large office complex.

There are several considerations that go into such a decision:

- The competitive golf market
- The evolution of community development
- The development rights and zoning

Let's discuss each:

Competitive Golf Market – This is the primary motivation for any decision by a golf course to close up shop. With the addition of much competition in the recent past, some courses are forced to consider lowering prices, repositioning themselves in the market, making expensive improvements or even going out of business.

Evolution of Community Development

– One of the fundamental concepts for golf development through the years has been to identify and locate sites that are not only large enough with adequate resources and physical characteristics, but are also located with adequate proximity to players. Accordingly, many courses were built on the perimeter of then existing community boundaries. As population has grown and communities have spread outward land has become scarcer and thus more valuable. In many communities, the golf courses represent the last large parcels of open space. As a result, they become too valuable for golf (especially in a sluggish golf market) and may be sold to developers of other property types. This has occurred for years in the golf course industry and I sense that it is occurring again.

Development Rights and Zoning –

One of the key elements of this equation is whether a golf course CAN be developed for an alternative use. Many projects (especially those designed as an amenity for housing) gave up such rights in the entitlement process and must remain as open space if not continued to be operated as a golf course. Other courses have conveyed open space conservation easements to take advantage of the tax benefits therein and later found that through increased competition or some other reason that they might not prefer to stay in the golf business.

What does all this mean? In general, I do sense that the market is beginning to "correct" itself in those markets that are oversupplied. It is only to be expected that more desirable courses will be stronger competitors and that the less attractive ones (although not always) will be candidates

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It should be noted that the benefit of the tax deduction to a particular taxpayer is based upon the amount of the taxpayer's adjusted gross income ("AGI"), the method of valuing the development rights and other factors beyond the scope of this article, and the advice of an experienced tax attorney or accountant is encouraged.

A taxpayer may claim a tax deduction for the contribution up to 30% of his or her AGI in any given year. If the deduction exceeds 30% of the taxpayer's AGI, the excess may be carried forward for up to five years.

How can I reduce my estate taxes by using a conservation easement? Estate taxes are imposed upon the fair market value of property included in a person's estate at the time of death. In determining the fair market value of the land, the land's development potential is a significant factor. Value based on development potential will be much greater than the value of undeveloped land held by the owner at the time of death. One way to reduce the fair market value for determining the estate tax, and thus help to keep the land in the family for additional generations, is to reduce its value through creating a conservation easement on the land. Because land is less valuable with restrictions on it, the estate tax on the land will be greatly reduced. Additionally, a further tax deduction against federal estate tax may be available for certain land protected by a conservation easement. Sometimes, advance planning that leads to a conservation easement can make the difference in the ability of an owner to pass his land on to the next generation.

Will the conservation organization maintain the land, chase off trespassers, prosecute illegal dumping, and the like? Ordinarily, the conservation organization which accepts the conservation easement assumes no obligation to maintain the land. Remember, a conservation easement does not transfer ownership or broad rights of use of the land to the conservation organization. The donor remains the owner of the land and will ultimately be responsible for its maintenance. However, this is a very

important consideration for landowners. Other methods, used in conjunction with a conservation easement, can provide for long term or perpetual maintenance of the land.

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Hirsh Speaks

GPA president Laurence A. Hirsh will be speaking at several upcoming events this fall. On October 10th, he will be addressing the Burlington County Assessors Association in New Jersey on the topic of golf course assessment. On November 1st he will be speaking at the Urban Land Institute Fall meetings in San Francisco, California.

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2003 Golf Course Investor Survey

Again this year, Golf Property Analysts (GPA) distributed a survey questionnaire to frequent investors in the golf course industry. Nearly 200 surveys were selectively distributed. Many of the respondents were multi-course management firms with some smaller investors who possessed a regional or local focus. With limited activity there have been a limited number of transactions.

The primary feedback from the majority of traditional golf buyers was that they are not buying right now.

We asked our respondents for desired beginning cap rates, which have remained steady since 2002, and are between 11% and 16%. While many sellers are seeking cap rates of 10% for their courses, the result has been that limited transactions have occurred. Desired internal rates of return (IRR) are high, with many investors seeking rates in the 18% and up range. Traditionally, other forms of real estate have commanded IRR's in the low to mid 20's, while golf's "sex appeal" and ability to attract investors at lower rates still exists, investors are inching closer to the rates required in other types of real estate.

Like last year, our respondents predominantly perceived values of golf

which shows a more individualistic approach to analyzing golf properties.

With respect to golf property financing, the responses were about equally split between commercial banks and golf finance companies, with many using both. The typical loan size was in the \$3 to \$5 million range with an overwhelming percentage (90+%) of the respondents reporting loan to value ratios between 60% and 75%. Interest rates for loans were predominantly less than 8% and as low as 6% with loan amortization terms typically 15-25 years.

Generally, it is concluded that despite lower interest rates, the supply/demand imbalance in several markets and the economy are causing many buyers to sit on the sidelines and seek the bottom of the market, which some perceive is here. Another consideration, discussed at greater length in *Linking Up*, is the potential for some golf courses to be put to alternative uses.

We invite your comments on our survey, to be conducted annually and welcome any suggestions to include additional information.

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for alternative uses. There is considerable interest in buying golf courses (at the right price) and fewer are being developed. Given this generalization, let me be the first to caution that we are talking about a series of markets (not one) and that all have different characteristics. Does this mean values are stabilized or back on the way up? I don't think so. That will take some time but all industries have cycles and we are no exception.



properties as **declining**. However, this year we have begun hearing from a few that the market is "at bottom". In past surveys, most investors indicated desirability for larger markets; this year many indicated a willingness to consider smaller markets,

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- ◆ **Bank of America** recently retained GPA to provide appraisal services for **South Riding Golfers' Club** in South Riding, VA and **Pleasant Valley Golfers' Club** in Chantilly, VA.
- ◆ The **Mashantucket Pequot Tribal Nation** recently retained GPA to provide a market value appraisal of **Bolder Hill Golf and Country Club** in Richmond, RI.
- ◆ GPA has recently completed the appraisal of the **Linkscorp Portfolio**. The portfolio included appraisals on 22 courses located in Tennessee, Florida, Alabama, Mississippi, Arkansas, Louisiana, North Carolina, Virginia and South Carolina.
- ◆ GPA has recently worked with CB Richard Ellis to complete the appraisals of the **National Golf Properties** portfolio. The 70 courses appraised by GPA were located in Minnesota, Missouri, Kansas, Virginia, Maryland, Illinois, Connecticut, New Jersey, New York, Pennsylvania, Oklahoma, Colorado, North Carolina, South Carolina, Tennessee, Louisiana, Ohio and Michigan.
- ◆ The **State of West Virginia** recently retained GPA to provide a market value and historic value appraisal of the 1884 **Oakhurst Links** in White Sulphur Springs, WV. This facility is recognized as the "first golf club in the United States."
- ◆ GPA was recently retained by the law firm of **Riley, Ripa, Hollin and Colagreco** to provide tax assessment evaluation and appraisal services for **Stonewall Golf Club** in Elverson, PA.