COLORADO COALITION OF LAND TRUSTS

Advice for Colorado Land Trusts and Local Governments Regarding the Colorado Income Tax Credit

The Board of Directors and staff of Colorado Coalition of Land Trusts (“CCLT”) wants to advise land trusts operating in Colorado and Colorado local governments that they are concerned about potential abuse of the conservation easement tax credit. Several transactions in the planning stage have been brought to the attention of the CCLT board and staff that appear to be potentially abusive.

Phasing of conservation easements is not a new idea. Before there was a state tax credit, landowners planned conservation easements in a number of phases, usually two, so that they would not generate a larger federal charitable income tax deduction than they could use under the six-year period allowed under the Internal Revenue Code.

Still, there are a number of reasons that CCLT is concerned about phasing and the tax credit. The Colorado tax credit is the most favorable incentive for donation of conservation easements at the state level in the nation. CCLT believes that the land trust and local government community should carefully guard this generous incentive. The tax credit, currently a maximum of $260,000 per transaction, has the potential to be very successful in encouraging the donation of conservation easements. Currently, the Colorado legislature is facing an extremely large budget deficit, and is looking for ways to reduce the deficit. If conservation easements which do not meet the federal conservation purposes test, particularly those which result in multiple tax credits, are added to the fiscal impact of valid conservation easements, the result could be a significant financial detriment to the state. Already we have seen one proposal to eliminate the conservation easement tax credit as a measure of fiscal austerity. Another reason to avoid transactions which do not meet the federal conservation purposes test is to avoid negative publicity for the land trusts and local government community as well as for conservation easements in general.

The conservation easement tax credit was enacted by the Colorado legislature in 1999. Originally limited to $100,000, the tax credit was broadened in 2001 to $100,000 plus 40% of the value of the conservation easement in excess of $100,000 subject to a cap of $260,000 per donation. In 2002, the tax credit law was amended by House Bill 02-1098 to require that the credit is only allowed “… for a donation that is eligible to qualify as a qualified conservation contribution pursuant to section 170(h) of the Internal Revenue Code, as amended, and any federal regulations promulgated in connection with such section.” One of the effects of this law was to incorporate the federal conservation purposes test into the requirements for eligibility for the Colorado income tax credit.

The Colorado income tax credit is a generous financial inducement for the donation of conservation easements. Despite this generous benefit, many landowners are asking land trusts, local governments, and advisors how many tax credits a landowner may generate from one piece of land. In order to give land trusts and local governments advice and guidance in answering these questions, CCLT is suggesting the following best practices.
Best Practices

1. Each land trust and local government shall adopt or review their criteria for the acceptance of conservation easements.

2. The acceptance criteria should take into account the federal conservation purposes test, which includes, in part:
   a) The protection of a relatively natural habitat of fish, wildlife, or plants or similar ecosystem (IRC § 170(h)(4)(A)(ii)).
   b) The preservation of open space (including farmland and forest land) where such preservation is:
      (I) For the scenic enjoyment of the general public, or
      (II) Pursuant to a clearly delineated Federal, State, or local governmental conservation policy,

      And will yield a significant public benefit. (IRC §170(h)(4)(A)(iii)). See also, Treasury Regulation § 1.170A-14.

3. Do not change the criteria for acceptance of conservation easements in order to accommodate multiple tax credits from a single piece of land.

4. Adopt a multiple easement/phasing policy for single properties which grantors intend to encumber with multiple easements.

5. A policy for multiple conservation easements can include a requirement for a phasing plan (a map on which the boundaries of the proposed multiple easements are shown).

6. Every conservation easement, including any single part of a multiple easement transaction, must be evaluated independently on its own merits in accordance with the previously adopted acceptance criteria. (See item #2).

7. Determine that the first, and each successive, phase of a multiple easement project will be successful if the land trust or local government does not receive future phases of conservation easements.

8. Consider the effect on the land if multiple conservation easements could result in multiple owners. Ask the question: is this project within our mission, does it meet our criteria, and is it good conservation?

9. Do not give tax advice to the landowner. Instead, educate the landowner about the requirements for obtaining a tax credit and urge the landowner to obtain sound legal and accounting advice.
10. While not giving tax advice to the landowner, appreciate that if a tax credit is disallowed because the donation does not meet the federal conservation purposes test the land trust will not avoid blame and consequences. Compare this situation to other violations of the federal requirements such as a failure to obtain subordination of a mortgage of deed of trust to the conservation easement or failure to deal with a severed mineral estate.

11. Be extra cautious about transactions where title to land is being “lent” to investors for the purpose of the investors obtaining tax credits. Think of the land as Humpty Dumpty. Are the investors taking Humpty Dumpty apart just for the tax credits and then putting Humpty Dumpty together again?

12. Strongly consider requesting that a landowner, who divides his or her parcel of land into multiple parcels for the purpose of multiple conservation easements, reassemble the land into a single ownership parcel as multiple conservation easements are completed. For example, a conservation easement may be amended to add a second parcel of land and both parcels of land would be subject to the prohibition against subdivision.

13. Be aware that the Colorado Department of Revenue has adopted a regulation that states “A taxpayer cannot earn multiple credits in one year from multiple donations even if the donations are made by different pass-through entities.” The final regulations can be found under “Final Income and Withholding Tax Regulations” on the Department of Revenue website at www.revenue.state.co.us.

In summary, if you pursue your mission using good, sound land conservation practices, the tax credit for conservation easements should take care of itself.

APPROVED BY CCLT BOARD OF DIRECTORS
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