

# **A Conservation Easement Guide For Landowners**



*La Plata Open Space Conservancy*

*2006*

# La Plata Open Space Conservancy

*Because they're not making land anymore...*

## About LPOSC

La Plata Open Space Conservancy (LPOSC) incorporated as a nonprofit land trust in 1992. Its mission is to protect open lands in Southwest Colorado that have important agricultural, wildlife, scenic, historical, archaeological, and/or recreational value, for the benefit of the public. LPOSC has worked alone, and with other private and public entities, to protect farms and ranches, natural wildlife habitat, watersheds, archaeological sites, scenic views, and parks for active and passive recreation. LPOSC has saved many thousands of acres of land in La Plata, Montezuma, Dolores, Archuleta, and Ouray Counties that would otherwise have been lost forever.

LPOSC is governed by a volunteer Board of Directors and funded by membership donations, proceeds from special events, and grants.

Through its programs, LPOSC builds public awareness of the need for land protection and of land conservation options, negotiates land protection agreements, and monitors and enforces those agreements to ensure permanent land protection.

## Land: It's Not Just Another Pretty Space

Open land is nice to look at. And it is much, much more. Land is life. It provides food and fiber; it recharges vital aquifers and controls flood waters; it feeds and shelters wildlife, and yields myriad recreation opportunities, to name just a few quantifiable benefits.

Colorado's open land is fast disappearing, succumbing not just to growth but to the way we are growing. Federal, state, and local agencies all work to protect land, but due to budgetary and/or bureaucratic constraints, they are often unable to save critical private land. Fortunately land trusts are working with confidentiality, flexibility, and speed to meet landowners' needs and to protect private land for public benefit, at little or no cost to taxpayers.

## Conservation Easements

La Plata Open Space Conservancy uses several different methods, alone or in combination, to protect land and meet landowner and community needs. However, the Conservancy's most common method of land protection is the conservation easement, where a landowner gives up (donates or sells) certain property rights to the land trust in order to protect specific resources. All of LPOSC's conservation easements have been donated, and most have resulted in significant tax benefits for the donors.

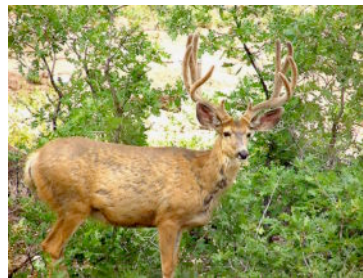


# **Summary:**

## **A Conservation Easement Guide for Landowners**

### **Conservation Easement Facts**

- A conservation easement is a legal, binding agreement made between a landowner and a conservation organization that protects land with conservation values – agricultural, wildlife, scenic open space, and/or historical/archaeological values -- that are important to the public.
- Each easement is unique to the parcel it is designed to protect and to the needs of the landowner donating the easement.
- A conservation easement does not require a landowner to open his property to the public.
- A conservation easement is designed to last forever, and it runs with the land, binding not only the landowner who gives the easement, but all future owners as well.
- Any landowner may give an easement, provided his property has conservation values that meet federal and state criteria for conservation purposes and public benefit.
- A conservation easement may be conveyed to a public agency, or to a conservation organization that qualifies as a public charity under Internal Revenue Code 501(c)(3).
- The easement holder is responsible for enforcing the restrictions of the easement.
- A conservation easement can help reduce income, estate, and property taxes.
- The value of a conservation easement can be determined by a qualified appraiser.



### **Steps for Giving a Conservation Easement**

- Determine whether the land has qualifying conservation values.
- Choose a qualified conservation organization to hold the easement.
- Obtain professional legal and financial/tax advice.
- Determine which conservation values to protect.
- Draft the conservation easement document.
- Document the conservation values and condition of the property.
- Obtain mortgage subordination.
- Obtain a qualified appraisal in order to claim tax benefits.
- Sign and record the conservation easement.



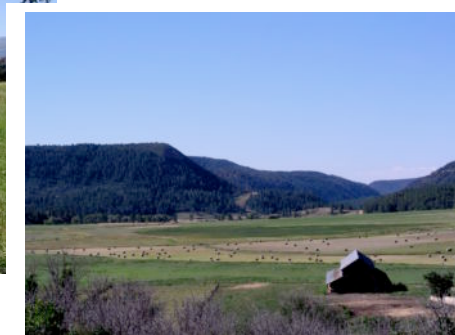
## **Conservation Easement Costs**

- Legal/financial advice to ensure proper structuring of the easement.
- Survey (sometimes, but not always, required) to determine boundaries of the conservation easement.
- Baseline documentation to verify conservation values and establish the condition of the property.
- Appraisal to establish easement value in order to claim tax benefits.
- Stewardship endowment to enable the land trust to monitor and enforce the easement.

## **Conservation Easement Tax Benefits**

A landowner who gives a conservation easement in perpetuity and exclusively for conservation purposes to a qualified organization may be eligible for the following tax benefits:

- Federal Income Tax Deduction.
- State Income Tax Credit.
- Federal Estate Tax Deduction and Exclusion.
- State Property Tax Benefit.





## **Part I. Conservation Easement Facts**

### ***What is a Conservation Easement?***

A conservation easement is a legal, binding agreement made between a landowner and a conservation organization that protects land with conservation values – agricultural, wildlife, scenic open space, recreation, and/or historical/archaeological values -- that are important to the public. Owning land is like owning a bundle of rights. A landowner can give up (by donation, sale, or other method of transfer) the whole bundle, or just a few of those rights. To protect land with a conservation easement, a landowner retains most of his rights, but gives up certain rights that, if exercised, would harm the land's conservation values. The rights he keeps and the rights he gives up are spelled out in a legal deed of conservation easement. The rights that are "given up" are conveyed to a qualified conservation organization - either a public agency or a nonprofit land trust - that is bound by law to hold the rights and to enforce the terms of the conservation easement. While a landowner can sell a conservation easement, most easements are donated. A landowner donating a conservation easement can be sure that his land will be protected forever, according to his wishes, and he may be eligible for substantial income and estate tax benefits as a result of his gift.

### ***How Restrictive Is a Conservation Easement?***

A conservation easement restricts development as necessary to protect specific conservation values. Each easement is unique to the parcel it is designed to protect and to the needs of the landowner donating the easement. Some easements are very restrictive and others are not. Even the most restrictive easements generally permit the continuation of historical uses of the land.

### ***Does a Conservation Easement Allow Public Access?***

A conservation easement generally does not require a landowner to open his property to the public. However, an easement granted to protect scenic open space must allow visual access (i.e. from a public roadway). Some landowners convey certain public access rights, such as fishing or hiking in specified locations. Others do not.

### ***How Long Does a Conservation Easement Last?***

A conservation easement can be designed to last forever (a perpetual easement) or, where state law allows, for a period of years (a term easement). However, only gifts of perpetual easements, qualify for income and estate tax benefits, and conservation organizations typically require perpetual easements. A conservation easement runs with the land, binding not only the landowner who gives the easement, but all future owners as well. The easement is recorded in the county's land records, so that future owners and lenders will learn about the restrictions when they obtain title reports.

### ***Who May Give, and Who May Accept a Conservation Easement?***

Any landowner may give an easement, provided his property has conservation values that meet federal and state criteria for conservation purposes and public benefit. If the land is owned jointly or partially, all owners must consent to placing an easement on the land. If the property is mortgaged, the landowner may need to obtain an agreement from the lender to subordinate its

interests to those of the easement holder. A conservation easement may be conveyed to a public agency, or to a conservation organization that qualifies as a public charity under Internal Revenue Code 501(c)(3). The recipient organization is required to have adequate resources to enforce the terms of the easement in perpetuity.

### ***What is the Responsibility of the Land Trust?***

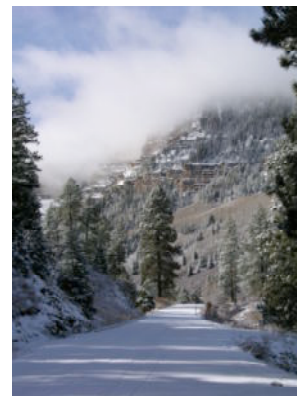
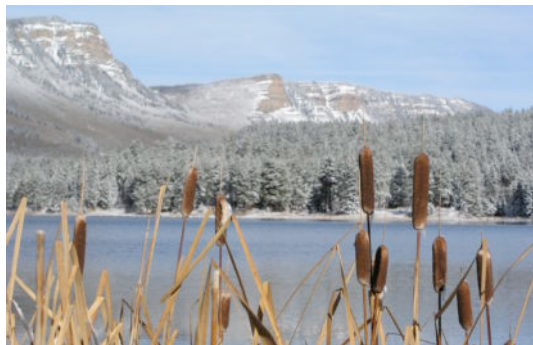
The land trust is responsible for enforcing the restrictions that the easement document spells out. Land trust personnel inspect or “monitor” the property on a regular basis – generally once a year – to ensure that the land remains in the condition prescribed by the easement. If a visit reveals that the easement has been violated, the land trust must require the landowner to cure the violation, and restore the property to its original condition.

### ***How Can Giving an Easement Reduce Taxes?***

To qualify for federal and state tax benefits, a conservation easement must be donated in perpetuity to a qualified conservation organization “exclusively for conservation purposes.” Lands that satisfy the “conservation purposes” requirement for conservation easements are outdoor recreational areas, relatively natural habitats of fish, wildlife, plants or similar ecosystems, open space (including farmland or forest land) protected for scenic enjoyment or in pursuance of an adopted governmental conservation policy, and historically or archaeologically important land areas. The value of a qualifying conservation easement can be deducted from federal income and used as a credit against Colorado income tax. The easement can also result in an estate tax reduction and an estate tax exclusion. Conservation easements can reduce property taxes as well. (For specific tax information, see Tax Benefits of Conservation Easements below.)

### ***How is the Value of a Conservation Easement Determined?***

The value of a conservation easement is the difference between the fair market value of the property unencumbered (“before”) and the fair market value of the property subject to the easement restrictions (“after”), as determined by a qualified appraiser. For example, the “before” fair market value of a highly developable property is the amount a person would pay for the property with the intent of developing it under existing and/or likely market conditions. (Note that “before” value is not the sale price of the developed lots.) The “after” fair market value is the amount a person would pay for the property, knowing that it is permanently restricted from some or all development. There is usually (but not always) a substantial difference between the before and after values, and the difference is the value of the conservation easement.



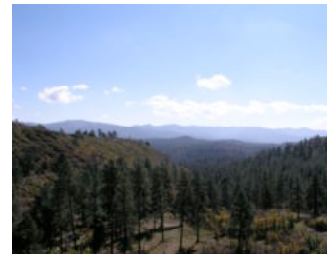
## Part II. Steps for Giving a Conservation Easement

*To give a conservation easement, a landowner should take the following steps:*

- **Determine whether the land has qualifying conservation values.** A property must meet the “conservation purposes” requirement to qualify for a conservation easement.
- **Talk with qualified conservation organizations.** Determine whether a conservation easement is the best way to protect the specific property. Then choose a qualified land trust to draft, hold, and steward the conservation easement.
- **Discuss the conservation easement with an attorney and/or tax advisor who is experienced in conservation easements.** A conservation easement is legally binding and restricts the use of land forever. A landowner should make sure his anticipated easement will effectively protect his land and anticipate future needs. Additionally, a landowner should make sure his anticipated easement is structured properly so that he can qualify for and maximize tax benefits.
- **Determine which conservation values to protect.** Most easement-restricted properties have more than one conservation value. While it is important to protect as many conservation values as possible, sometimes the protection of one value jeopardizes another. For example, certain agricultural operations may compromise wildlife habitat, but certain restrictions to protect habitat may hinder agricultural operations. For this reason, it is desirable to prioritize the property’s conservation values and design the conservation easement accordingly.
- **Work with the land trust to draft the conservation easement document.** LPOSC uses a nationally accepted model conservation easement that can be modified to protect specific conservation values and to meet the needs of individual landowners.
- **Document the conservation values and condition of the property.** LPOSC will prepare a “baseline inventory,” including deeds, title report, mortgages, status of mineral interests, maps, photos, professional evaluations of conservation values, and other data to document the legal status and condition of the property at the time of the easement. The baseline inventory is later used in monitoring compliance with the conservation easement and evaluating changes in use of the property.
- **Obtain Mortgage Subordination.** Because foreclosure on a mortgaged property may extinguish a conservation easement, it is necessary that the lender subordinate, by legal agreement, its rights in the property to the rights of the easement holder.
- **Obtain a qualified appraisal.** A “qualified” conservation easement appraisal, completed by a “qualified” appraiser, is required in order to claim income tax deductions and credits. A conservation easement appraisal is more complicated than an ordinary real estate appraisal, and it is very important to choose an experienced appraiser who understands and works in accordance with the regulations for conservation easement appraisals, as stated in Section 1.170A of the federal regulations. Poorly structured appraisal reports and/or overstated estimates of value can result in both rejection of tax benefit claims and penalties. Selection of a qualified appraiser is the responsibility of the landowner. As part of the selection process the landowner should ask what license an appraiser holds (a “Certified General” license, while not required, may be preferred) and what other special designations he has attained. The landowner should also ask about the appraiser’s experience in general, his experience in appraising conservation easements, his experience appraising easements locally and on similar properties, and his experience,

if any, with the Internal Revenue Service in defending easement appraisals. If the landowner elects to hire an appraiser without significant experience, he may want to arrange for a review of the appraisal by a more experienced appraiser. While LPOSC does not recommend one appraiser over another, it can provide contact information for independent, experienced conservation easement appraisers in southwest Colorado.

- **Sign and record the conservation easement.** The landowner (“Grantor”) signs the easement document to convey the easement, and the land trust (“Grantee”) signs to accept it. The document is then recorded in the official county real estate records.



## Part III. Conservation Easement Costs

*The landowner bears certain costs of completing a conservation easement, including:*

- **Legal/Financial Advice.** It is recommended that a landowner obtain legal and financial advice from independent, experienced professionals to ensure proper structuring of the easement for land protection and tax purposes.
- **Survey.** A survey is sometimes, but not always, required to determine the exact boundaries of a conservation easement and/or to determine the boundaries of building areas within an easement.
- **Baseline Documentation.** Baseline documentation is required to verify conservation values and establish the condition of the property. The cost of a baseline inventory varies with the purposes and complexity of the easement.
- **Conservation Easement Appraisal.** An appraisal by a qualified conservation easement appraiser is required in order to claim federal and state income tax benefits for a gift of conservation easement. Appraisal costs vary, but an easement appraisal costs more than an ordinary real estate appraisal because it requires appraisal of both the “before” and “after” values.
- **Stewardship Endowment.** The land trust is required by law not only to monitor and enforce its conservation easements in perpetuity, but also to have the resources to do so. Thus, the land trust asks the landowner to “endow” the conservation easement with a contribution large enough to earn adequate funds each year to support the land trust’s



stewardship obligations. LPOSC calculates the amount of stewardship endowment necessary, based on the anticipated cost of annual monitoring and the perceived risk of violation of the easement. Stewardship endowments given to LPOSC are tax-deductible transaction costs. LPOSC's Stewardship Endowment Fund is a restricted fund used only for stewardship purposes.

The landowner's costs of completing a conservation easement are usually more than offset by his tax benefits resulting from the gift. In cases where important land is at risk because the landowner cannot afford the costs of the transaction, LPOSC may be able to assist with funds from its grant-supported Transaction Assistance Fund.

## **Part IV. Conservation Easement Tax Benefits**

*The following is general tax information and may not apply in each specific situation. La Plata Open Space Conservancy recommends consultation with professional tax advisors during the course of creating a conservation easement.*

Conservation easements protect important open lands in perpetuity. Recognizing the importance of voluntary land protection, the federal government and the State of Colorado have created a number of important tax incentives that can help make private land conservation attractive and affordable. In order to qualify for tax benefits, an easement must be perpetual, and must be granted exclusively for conservation purposes to a qualified conservation organization, and its value must be established by a qualified appraisal. Tax benefits include:

### ***Federal Income Tax Deduction:***

The federal government allows taxpayers to claim a charitable gift deduction against federal income for the full value of a donated conservation easement. The deduction can be taken at the rate of 30% of the taxpayer's Adjusted Gross Income (AGI) in the year of the donation, and may be carried forward at that rate for up to five additional years.

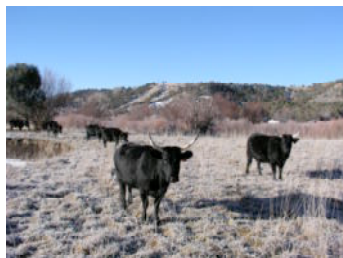
Recognizing that existing limits on the use of the tax deduction may discourage lower income landowners from giving conservation easements, Congress is considering raising the percentage of AGI that can be deducted each year, and increasing the carry forward period.



### ***State Income Tax Credit:***

The Colorado Legislature has created a tax credit against Colorado income tax for the donation of a conservation easement. The credit represents a dollar-for-dollar reduction of income tax. The credit is allowed for qualified conservation easements that meet federal regulations, and is subject to the following limitations.

- The tax credit is in the amount equal to the fair market value of the conservation easement for the first \$100,000, plus 40% of the remaining value of the easement, to a maximum credit of \$260,000. (Beginning in 2007, the credit will be calculated at 50% of the fair market value of the easement up to \$750,000, for a maximum credit of \$375,000.)
- Credit not used in the year of the easement donation may be carried forward for up to 20 succeeding income tax years. Credit not used during that time is not refundable.
- A summary of a qualified conservation easement appraisal verifying the value of the easement must be filed with the donor's tax return.
- A taxpayer may claim only one conservation easement tax credit per year. A taxpayer who carries forward any unused portion of a tax credit may not claim credits for additional donations in years to which unused credit is carried forward.
- A taxpayer may transfer (give or sell) all or part of his credit to one or more other taxpayers (transferees) to be used against the transferees' Colorado income tax. The transferee(s) of the credit may not claim a cash refund of the credit.
- Both the taxpayer and the transferee(s) must specify the amount transferred in written statements filed with their income tax returns.
- A taxpayer may claim a refund of any unused portion of the tax credit from the State of Colorado in years when there is a state revenue surplus (fiscal years when state revenues exceed state spending limitations). The refund (like the tax credit itself) may only be claimed for one conservation easement donation in a given year. Whether or not there will be a surplus in any given year is determined by the Treasurer after the end of the state's fiscal year in September.
- A taxpayer may use the credit against his taxes and claim a refund of the unused portion of the credit, so long as the total amount of credit used and refund claimed in a given tax year does not exceed \$50,000. (However, a taxpayer may use more than \$50,000 of credit to offset taxes in a given year, as long as he does not also claim a refund in that year.
- The state income tax credit is available only to "resident individuals" or "domestic or foreign corporations subject to the provisions" of the Colorado income tax statutory provisions applicable to corporations. Conservation easement donors whose primary residence is not in Colorado should check with an experienced advisor to see if they can qualify for the credit. For easement donors wishing to transfer tax credits, organizations exist that will, for a reasonable fee, find buyers and broker the sale of the credits. LPOSC maintains a list of these organizations.



### ***Federal Estate Tax Deduction and Exclusion:***

Because a conservation easement limits future uses of land, it also limits the value that can be assigned to property for estate tax purposes. This estate tax “deduction” can lower estate taxes significantly, and can help heirs to keep family land rather than sell it to pay the estate tax. The federal Taxpayer Relief Act of 1997 created additional estate tax benefits for donors of conservation easements, including:

- An exclusion from estate tax of up to 40% of the value of land subject to a qualified conservation easement, up to \$500,000. The exclusion can be taken in addition to the estate tax deduction described above, and it can be taken by each succeeding generation of heirs of the original easement donor as long as the land remains in the family. It can also be taken in addition to the estate tax exclusion for family-owned businesses.
- A post mortem election whereby the heirs or executor of an estate may grant a conservation easement following the death of the landowner, in order to take advantage the estate tax deduction.

### ***State Property Tax Benefit:***

In Colorado agricultural land that is taken out of production is reclassified as “vacant land,” causing property taxes to increase astronomically. High property taxes on vacant land have forced many landowners to sell their land for development.

In 1995 the Colorado Legislature passed House Bill 1268, modifying property tax law to encourage land conservation. HB 1268 allows farmers and ranchers who have protected their land from development with a permanent conservation easement to take their land out of production without losing their favorable agricultural property tax classification. The law does not encourage cessation of agriculture. Instead, it enables the preservation of precious farm and ranch land by giving farmers and ranchers an option they did not previously have -- the option to retire or to suspend an operation due to market, natural, or other conditions. The law does not adversely impact other taxpayers, since it does not take land off the tax rolls or reduce tax revenue from affected lands. To qualify for the agricultural property tax benefit, the subject property must be 80 acres or larger (smaller if there are no structural improvements) and must be classified as agricultural at the time of the gift of easement.

Nonagricultural lands protected by conservation easement may qualify for reduced property taxes as well, since the easement restrictions generally reduce land value. This is not always the case, however, and an easement donor’s tax bill will ultimately depend upon the local tax assessor’s judgment of the diminution in value caused by the easement restrictions.



**For additional information, please contact:**

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