

CONSERVATION ALERT

TO: Friends and Clients

FROM: Isaacson Rosenbaum, P.C.

DATE: June 12, 2008

RE: State and Federal Developments Affecting Conservation in Colorado

Introduction

Recently, both Congress and the Colorado General Assembly enacted legislation with significant implications for conservation. Congress recently overrode President Bush's veto to enact the Food, Conservation and Energy Act of 2008 (the "Farm Bill"), which extends important federal conservation tax incentives and funds federal conservation programs.

Colorado House Bill 08-1353 ("HB 1353") creates new reporting and submission requirements for appraisers, and new review and enforcement duties in the Department of Revenue (the "DOR"), Division of Real Estate (the "Division"), and the Board of Real Estate Appraisers (the "Board"). The bill also creates a new Conservation Easement Oversight Commission to oversee conservation easement transactions for which a Colorado conservation tax credit is claimed. Land trusts accepting conservation easements for which a tax credit is claimed must complete a conservation easement holder certification process. Finally, HB 1353 imposes a new tax basis limitation on conservation tax credits for property held for less than one year, aligning the state program with federal tax requirements.

2008 FEDERAL FARM BILL EXTENDS CONSERVATION INCENTIVES

The Farm Bill extends the expanded tax incentives for charitable contributions of qualified conservation easements from the Pension Protection Act of 2006 (the "Pension Act"). Retroactive from January 1, 2008 through December 31, 2009, the Farm Bill extended the Pension Act's expansion of the amount of the deduction available for donations of qualified conservation contributions from 30% to 50% of adjusted gross income ("AGI"), and up to 100% of AGI for farmers and ranchers. The Farm Bill also extended the expansion of the deduction's lifetime, or its "carryforward" period, from five to fifteen years. Finally, the Farm Bill included \$733 million in funding over five years for the Farmland Protection Program, and re-established the Grasslands

Reserve Program, targeting 1.22 million acres for protection with an estimated \$300 million in funding.

COLORADO HB 1353

Background

From its inception in 1999, Colorado's conservation easement tax credit program has been a national model for state conservation incentive programs. The program has grown tremendously, with expanded use of the tax credits and periodic expansion of the tax credit benefits available to Colorado landowners. As the program grew, Colorado's conservation community and the state's General Assembly became increasingly concerned that unscrupulous citizens could abuse the tax credit system for personal gain, and thus threaten the integrity of the highly regarded program.

In 2007, State Representative Alice Madden and State Senator Jim Isgar convened the Conservation Easement Tax Credit Task Force to develop recommendations to the General Assembly for legislative and administrative improvements to the tax credit program. The task force, which was chaired by Larry Kueter of Isaacson Rosenbaum's Conservation Practice Group, included more than two dozen Colorado legislators, state and local government officials, land trust representatives and other conservation professionals. This diverse group reached a consensus to make wide-ranging recommendations for improving the state tax credit program, ensuring that it will continue to encourage land conservation in Colorado, while mandating the cost-efficient use of state resources to do so. The end result of this process was HB 1353, which Governor Ritter signed into law on June 5, 2008.

Appraiser Reporting, Submission, and Education Requirements

Perhaps the biggest change in HB 1353 is the new requirement that appraisers must submit a copy of the conservation easement appraisal to the Division. This requirement has three main components. First, whenever a taxpayer intends to claim a conservation tax credit, the appraiser must submit the underlying appraisal to the Division within thirty days of "completion" of the appraisal. "Completion" is defined as the point at which the appraiser has signed the appraisal certification page and delivered the appraisal to the client.

Second, the appraiser must also submit a fee to the Division. The fee will create the Conservation Easement Appraisal Review Fund to support the Division's administration of the new appraisal requirements. The Division must set the amount of the fee prior to January 1 of each year (the Division must establish the initial amount of the fee prior to January 1, 2009), but the fee is capped at \$600 per appraisal.

Third, the appraiser must submit an affidavit to the Division which includes and expands upon the appraisal information currently reported on form DR 1303. The expanded affidavit must report:

- the value of the unencumbered property, the value of the conservation easement, and the methods used to determine each value;

- whether the appraisal separately values sand and gravel, mineral rights, water rights or improvements, and if so the before and after values of each;
- whether the appraiser used subdivision analysis to value the conservation easement;
- whether the landowner or "family members" (as defined under the Internal Revenue Code) own contiguous property, and whether the landowner or a "related party" (as defined by the Internal Revenue Code) owns nearby property, the value of which could be enhanced by the conservation easement – this requirement mirrors the requirement found in U.S. Treasury Regulation 1.170A-14(h);
- how the appraiser satisfies the qualified appraiser and licensing requirements established in the C.R.S. Section 39-22-522(3.3);
- the date of and method by which the appraiser has satisfied the new classroom education requirements established by HB 1353 (see below for the requirements); and
- the number of conservation easement appraisals the appraiser has previously completed.

The affidavit will be on a form that is yet to be developed by the Board. HB 1353 also gives the Board authority to promulgate rules concerning the affidavit.

The Board is also charged with establishing classroom education and experience requirements for appraisers "to ensure that appraisers have a sufficient amount of training and expertise to accurately prepare appraisals that comply with USPAP and any other provision of law related to the appraisal of conservation easements." It is important to note that a conservation tax credit will not be allowed unless the appraiser who completed the conservation easement appraisal complied with the classroom education and experience requirements at the time the appraisal was completed.

State Agency Review and Enforcement Functions

HB 1353 also greatly expands the ability and powers of state agencies to oversee and enforce the conservation tax credit program.

First, HB 1353 provides that the Division review appraiser affidavits and maintain an electronic database of them, and that the Division may share the affidavits with the DOR. The bill prohibits the Division from publicly disclosing the affidavits for inspection, unless the Division files a notice of charges based on the information they contain.

Second, HB 1353 states that the Board may investigate or, upon receipt of a written complaint, shall investigate appraisers who submit affidavits to ensure compliance with the Uniform Standards of Professional Appraisal Practice ("USPAP") and other legal requirements. The Board may cooperate with the Division during such investigations, and if the Board determines that a material violation of USPAP or a substantial misstatement of value has occurred, the Board shall notify DOR and provide DOR with a copy of the subject appraisal and a summary of its investigative findings. The Board is authorized to take disciplinary action against any appraiser who fails to submit an appraisal, affidavit, or other information required by law.

The Board is charged with establishing classroom education and experience requirements for appraisers "to ensure that appraisers have a sufficient amount of training and expertise to accurately prepare appraisals that comply with USPAP and any other provision of law related to the appraisal of conservation easements." It is important to note that a conservation tax credit will not be allowed unless the appraiser who completed the conservation easement appraisal complied with the classroom education and experience requirements at the time the appraisal was completed.

Third, HB 1353 amends Section 39-22-522 of the Colorado tax code to enable DOR to share copies of appraisals and other information with the Division and the new Conservation Easement Oversight Commission discussed below, as well as to file complaints against appraisers with the Division. HB 1353 appropriates funds to hire new staff members within both DOR and the Division to implement these new requirements.

Implications for State Tax Reporting and Tax Forms

The appraiser affidavit described above reports all of the information, and more, that is currently reported by appraisers on the state form DR 1303. HB 1353 amends the reporting requirements for conservation tax credits, so it is anticipated that DOR will revise the state tax forms sometime during 2008.

Conservation Easement Oversight Commission

HB 1353 creates the Conservation Easement Oversight Commission (the "Commission") within the Division of Real Estate. The purpose of the Commission is to advise the Division and the DOR regarding the integrity and accuracy of conservation easement transactions for which a tax credit is claimed and to review certification applications for conservation easement holders.

The Commission will have nine members:

- Great Outdoors Colorado, Department of Natural Resources, and the Department of Agriculture will each appoint one member from their respective entity to the Committee.
- The Governor will appoint six members, including at least one member with the following qualifications or representing the following interests:
 - a local land trust;
 - a statewide or national land trust;
 - a local government open space or land conservation agency;
 - an historic preservation organization with experience in easements on historical properties;
 - a certified general appraiser with experience in conservation easements; and
 - a landowner that has donated a conservation easement in Colorado.

Certification Process for Holders of Conservation Easements

In an effort to prevent fraudulent or unqualified organizations from holding conservation easements for which tax credits are claimed, HB 1353 establishes a certification requirement for all entities that

hold such conservation easements. Beginning one year after the Division starts accepting certification applications, as described below, a tax credit may only be claimed for a conservation easement donation if the easement holder was certified at the time of the donation.

The certification requirement applies to nonprofit and governmental entities that hold easements on property with conservation values relating to recreation or education, protection of environmental systems, preservation of open space, or historical preservation. The Division may allow for expedited or automatic certification of an entity that is accredited by national land conservation organizations.

To become certified to hold conservation easements, an organization must submit an application to the Commission with an application fee. The application requirements and the amount of the fee will be determined by the Division prior to January 1, 2009, however the fee will not exceed \$5,810. The Commission will review the application and make a recommendation to grant or deny the application to the Division. The Division will make the final determination. The Commission and the Division may consider the following factors during the review process:

- the applicant's process for reviewing, selecting and approving a potential conservation easement;
- the applicant's stewardship practices and capacity;
- an audit of the applicant's financial records;
- the applicant's system of governance and ethics regarding conflicts of interest and transactions with related parties, as described in Section 267(b) of the Internal Revenue Code, donors, board members, and "insiders," which is defined as board and staff members, substantial contributors, those who have an ability to influence decisions of the organization, and those with access to information not available to the general public;
- the unique circumstances of the different entities to which this certification applies; and
- any other information deemed relevant by the Division or the Commission.

If the application is approved, the organization will be certified to hold conservation easements for which a tax credit is claimed for three years. If the application is denied, the organization may request a hearing on the determination and/or reapply. The Division can suspend or revoke an organization's certification, or impose fines, for violating requirements of certification or other rules to be established by the Division.

The Division will maintain an online list of organizations that have applied for certification and whether each has been certified, rejected for certification, or had its certification revoked or suspended.

The Commission has a statutory obligation to begin accepting applications for certification no later than January 1, 2009. Land Trusts must be certified to hold conservation easements, for which a tax credit is claimed, by January 1, 2010, which is one year after the Commission begins accepting applications. Governmental entities and nonprofit entities that hold easements on property for historic preservation will need to be certified by January 1, 2010 or January 1, 2011, depending on

whether the Division begins accepting certification applications for these types of entities on January 1, 2009, or January 1, 2010.

Tax Basis Limitation

HB 1353 amends Section 39-22-522 of the Colorado tax code to limit the amount of the conservation tax credit available to landowners who donate a conservation easement over land they have owned for less than one year. For the purpose of calculating the amount of the available credit, the value of the conservation easement will be reduced to the taxpayer's adjusted tax basis in the property. This change aligns the state tax credit program with Internal Revenue Code limitations.

Practical Guidance

HB 1353 will take effect on July 1, 2008. It is difficult to offer detailed guidance on how to comply with HB 1353 at this time, or to predict when state agencies will promulgate some of the rules and procedures called for in HB 1353, such as appraiser education or easement holder certification requirements. In the near future, some of these requirements may be difficult to comply with until the Commission is created and all of the state agencies develop the staff and processes to implement them. However, landowners and conservation professionals can begin to plan existing and imminent conservation transactions around the new requirements and attempt to comply with as many of HB 1353's provisions as possible.

For example, landowners, appraisers, land trusts and other advisors (i.e., attorneys, accountants and tax credit brokers) should begin to coordinate the preparation of conservation easements, appraisals and other documents as early in the transaction as possible, and then attempt to arrive at an appraisal that is as close to being "complete" as possible, in order to avoid the potential of submitting and re-submitting an appraisal to the state and incurring additional fees, delays and expenses.

If you have any questions regarding this legislation or your individual situation, please call Larry Kueter, Bill Silberstein, Allison Ulmer, or Chris Jensen in our Conservation Practice Group at (303) 292-5656. Also, to view previous editions of this Conservation Alert, go to the Conservation Law Library on our website at www.ir-law.com.

This memo is intended as a summary of the above-described legislative changes and proposals. It is not to be treated as legal advice.