

## Income 39: Gross Conservation Easement Credit

An income tax credit is available for tax years beginning on or after January 1, 2000, for the donation of a perpetual conservation easement in gross on real property in Colorado. In general, a conservation easement is a right in the owner of the easement to prohibit or require certain acts on, or with respect to, a land or water area for conservation purposes. "Conservation easement in gross" is further defined in section 38-30.5-102, C.R.S. In order to qualify for the credit, the donation must meet the requirements of §§38-30.5-101, et seq., and 39-22-522 C.R.S., Internal Revenue Code §170(h), and their associated regulations.

### CREDIT QUALIFICATIONS

A taxpayer must meet statutory requirements to claim a conservation easement credit and comply with limits on the amount and number of credits allowable for a given year.

#### Eligible taxpayers

Taxpayers eligible to claim a conservation easement credit are:

- Colorado resident individuals,
- C corporations,
- trusts,
- estates,
- members of a pass-through entity who receive the credit from the entity's donation, regardless of whether such members are Colorado residents.

A limited liability company with only one member will generally be disregarded for federal tax purposes (IRS Regulation §301.7701-3) as well as for state tax purposes. Therefore, a sole member is not a "member of a pass-through entity" and does not qualify as a "taxpayer" for the credit unless they otherwise meet the definition of a "taxpayer". [§39-22-522(1), C.R.S.]

Nonresident individuals are not eligible to claim credits for conservation easement donations they make individually. However, a Colorado resident who claims a credit and subsequently moves to another state may use any remaining carryforward credit or transfer such remaining credit to another taxpayer. A part-year resident is eligible to claim a credit for a conservation easement donation only if the donation was made while they were a Colorado resident.

#### Certificate application and annual limit

A taxpayer donating a conservation easement on or after January 1, 2011 must apply to the Department of Regulatory Agencies and receive a tax credit certificate. Each certificate indicates the amount of credit and the designated tax year for which the amount may first be claimed and used on a tax return. The aggregate total of credits that the Department of Regulatory Agencies can certify each year is limited (capped). If the cap has been reached for the donation year, the Department of Regulatory Agencies may "waitlist" the credit and issue a tax credit certificate for a subsequent year. [§39-22-522(2.5) C.R.S.]

#### Multiple donations

Only one credit may be claimed each year by each donor of a new easement.

- A taxpayer cannot claim multiple credits for separate donations they make in the same tax year, even if the donations are made by different pass-through entities of which the taxpayer is a member, or if one or more of the credits are transferred to other taxpayers.
- A taxpayer cannot purchase additional credits for any year in which they claim a credit from a new donation.
- A taxpayer cannot claim a credit for a donated easement if any credit from a previous donation made by the taxpayer prior to January 1, 2014 has been carried forward to the tax year in which the new donation is made, by either the taxpayer or a transferee. The donor also cannot acquire by transfer any credit for such tax year.

For a waitlisted credit claim, the above rules will be applied to both the year of the donation and the year of the tax credit certificate. The carry forward period will be applied based on the year of the tax credit certificate.

**Example:** A taxpayer donates a conservation easement in 2016, and their first tax credit certificate allows the credit to be claimed on their 2017 tax return. The taxpayer must not have claimed any other new credits in 2016 or 2017, either on a tax return or on an application to the Department of Regulatory Agencies. If the taxpayer donates another conservation easement in 2017, a credit would not be allowed for that donation, even if the Department of Regulatory Agencies would have waitlisted the credit to 2018. If the credit is not fully used on the 2017 return, the remaining credit can be carried forward for up to 20 years, through 2037.



## CREDIT COMPUTATION

The credit calculation depends on the year in which the qualifying donation is made and is generally based on the fair market value (FMV) of the donation, excluding any amount received by the donor as part of a bargain sale for the easement. Additionally, if the taxpayer holds the property encumbered by the easement for less than one year prior to donating the easement, the value of the easement for the purpose of calculating the credit is limited to the taxpayer's basis in the donated easement as determined pursuant to IRC §§ 170(e) and (h). [§§39-22-522(3.7) and (4)(a), C.R.S.] The following table outlines the calculation of the credit and the maximum allowable credit based on the date of the donation.

Year of donation	Credit calculation	Maximum allowable credit
2015 or later	75% of the first \$100,000 of FMV or basis, plus 50% of FMV or basis in excess of \$100,000	\$5,000,000, in maximum increments of \$1,500,000 per year
2007-2014	50% of FMV or basis	\$375,000
2003-2006	100% of the first \$100,000 of FMV or basis, plus 40% of FMV or basis in excess of \$100,000	\$260,000
2000-2002	100% of the first \$100,000 of FMV or basis	\$100,000

When a donation is made collectively by multiple taxpayers, the credit calculation and the maximum allowable credit from the preceding table apply to the donation as a whole. Donations made collectively by multiple taxpayers include those made by:

- a married couple, regardless of whether they file jointly or separately;
- all members of a pass-through entity that makes a donation; and
- all tenants in common, joint tenants, or other similar ownership groups that donate a conservation easement on jointly owned land.

The credit resulting from the donation and any associated income are allocated to the owners, partners, shareholders, or members in proportion to their distributive shares of income or ownership from the entity or group. [§39-22-522(4)(b), C.R.S.]

## CREDIT USE, CARRY-FORWARD, REFUND, AND TRANSFER

In general, the amount of credit a taxpayer can use is limited to their net tax liability. If a taxpayer's credit exceeds their tax liability, the excess credit may be carried forward for up to 20 years after the first year it was eligible to be claimed. The credit may not be carried back to a prior tax year.

Credit for a donation made by a pass-through entity is allocated and allowed to the pass-through entity's members, rather than to the pass-through entity itself. If certain conditions are met, the pass-through entity may transfer the credit directly on behalf of its members (see *Transfer of credit: pass-through entities* on the following page). If the full amount of the credit allocated to a member has not been transferred, refunded, or applied toward the member's tax liability, the member may carry forward the remaining credit to the following tax year.

### Refundable credit

Under certain conditions, a taxpayer who donated a conservation easement may elect to receive a limited refund of the credit. First, the State Controller must certify that state revenues are in excess of certain thresholds. This condition was met for tax years commencing in 2000, 2001, 2005, 2015, 2018, and 2019.

Second, if any part of a credit is to be refunded, the total credit used from that donation for that tax year by all taxpayers, both to offset tax and to claim refunds, is limited. For donations made in tax years beginning on or after January 1, 2000, but before January 1, 2003, the limit is \$20,000. The limit increases to \$50,000 for donations made in tax years beginning on or after January 1, 2003. This aggregate limit applies collectively to all of the following groups with credit from the same donation:

- A married couple, regardless of whether they file jointly or separately,
- All members of a pass-through entity that makes a donation,
- All tenants in common, joint tenants, or other similar ownership groups that donate a conservation easement on jointly owned land, and
- All taxpayers who donate the conservation easement and all transferees of that credit.

Taxpayers in such groups who want to claim a refund for any of the credit should coordinate their use of the credit so they do not exceed this limit. However, if no refund is claimed for any of the credit, then this limit does not apply, and each taxpayer may use their portion of the credit up to their net tax liability.



## Transfer of credit

A conservation easement donor can transfer all or part of their unused credit to a "transferee" who meets the definition of a taxpayer who can claim the credit. [§§39-22-522(2), (2.7), and (7), C.R.S.] For tax years beginning on or after January 1, 2003, there is no limit on the increment per transfer or the number of transferred credits a transferee can have each year. For transfers made on or after June 7, 2005, but before May 29, 2018, a transferee must receive the credit by the due date of the income tax return, not including extensions, on which the credit will be used. Beginning May 29, 2018, a transferee must receive the credit by the due date of the income tax return, including extensions, on which the credit will be used. [§39-22-522(7)(g), C.R.S.] A transferee cannot transfer a credit to another taxpayer.

### *Transfer of credit: pass-through entities*

A pass-through entity cannot purchase a credit for use by itself or its members. A pass-through entity that makes a donation may directly transfer the credit to other taxpayers on its members' behalf, but only if all of the following conditions are met:

- Each partner, shareholder, or member consents to the transfer.
- Each partner, shareholder, or member could, under the restrictions of the law, have claimed and transferred their pro rata share of the credit directly. [§39-22-522(4)(b), C.R.S.]
- The partners, shareholders or members have not yet transferred any of the credit to another taxpayer, used any of the credit either to offset their tax or to claim a refund, or carried forward any of the credit on their own returns. If a partner, shareholder, or member has taken any of these actions, the pass-through entity cannot directly transfer any part of the credit on its members' behalf.

### *Transfer of credit: disallowance of a transferred credit*

If a credit that has been transferred is disallowed, the transferee will be held liable for the tax otherwise offset by the disallowed credit, including any applicable penalty and interest. [§39-22-522(9), C.R.S.] All protest rights regarding a transfer item adjustment reside with the donor of the easement or the transferor of the credit, who is considered the tax matters representative in all matters with respect to the credit. For additional information regarding the tax matters representative, see Department Rule 39-22-522(3)(h) and §39-22-522(7)(i), C.R.S.

### *Transfer of credit: income from the sale*

The Federal Tax Court determined that this credit is a capital asset with no basis, and that the holding period begins when the credit is granted. Therefore, the gain from the sale of the credit must be included in federal taxable income, which is then subject to Colorado income tax. A part-year resident or nonresident individual must include such income on Colorado form DR 0104PN.

## Deceased taxpayer

Upon the death of a taxpayer the credit passes to the decedent's estate. If the decedent is a donor of the easement, the estate may use the credit to offset income tax owed by the estate or may transfer some or all of the credit according to the transfer rules. If the decedent is a transferee, the estate may use the credit to offset income tax owed by the estate, but may not transfer the credit. [§39-22-522(7)(h), C.R.S.]

## FEDERAL DEDUCTION ADBACK

Any taxpayer who claims a conservation easement credit and a federal charitable contribution deduction for the same donation must make an addition to taxable income (an "addback") on their Colorado income tax return in the amount of the deduction used each year. [§§39-22-104(3)(g) and 39-22-304(2)(f), C.R.S.] However, a pass-through entity should not include this deduction or addback on its Colorado income tax return.

The addback must begin the first year the deduction is claimed, even if the credit is waitlisted by the Department of Regulatory Agencies, transferred to another taxpayer, or carried forward to a subsequent tax year. Any contribution carryover from a conservation easement that is deducted in a subsequent tax year must be added back on that year's Colorado income tax return. The aggregate addback for all donors of each conservation easement is limited to the donation amount needed to generate the credit, as allocated to each donor. For donations made on or after January 1, 2015, the maximum aggregate addback is \$9,950,000.

## High income taxpayers

If a taxpayer's itemized deductions are reduced because their federal adjusted gross income (AGI) is above the annual limit, then the required addback on their Colorado return is reduced by the same proportion.



## DOCUMENTATION

Any taxpayer engaging in a conservation easement credit activity for the tax year must file a Colorado income tax return with all applicable parts of form DR 1305, Gross Conservation Easement Credit Schedules. A taxpayer who does not file a return as required will have any subsequent claims of their share of the credit disallowed.

Conservation easement credit activity includes:

- Receiving a tax credit certificate from the Department of Regulatory Agencies, either directly or as a member of a pass through entity that made a conservation easement donation, and claiming the new credit;
- Receiving a credit transfer;
- Using credit to offset tax liability or claim a direct refund;
- Carrying credit forward to the following year; and
- Transferring credit to another taxpayer. For example, credit transferred October 10, 2019 can be used on the transferee's 2018 return, so the donor must report the transfer on their form DR 1305 for 2018, not 2019.

## FURTHER READING

- State law and regulation
  - § 39-22-522, C.R.S. and Dept. Rule 39-22-522
  - § 39-22-522.5, C.R.S. (dispute resolution for disallowed credit claims)
  - § 39-22-104(3)(g) and Dept. Rule 39-22-104(3)(g) (addback for individuals, estates, and trusts)
  - § 39-22-304(2)(f) and Dept. Rule 39-22-304(2)(f) (addback for corporations)
- Federal law and regulation
  - 26 U.S.C. § 170 (regarding charitable contribution deductions)
  - 26 CFR § 1.170A
- Court cases
  - *Huber v. Kenna*, 205 P.3d 1158, 1161 (Colo. 2009)
  - *Tempel v. Commissioner*, 136 T.C. 341, 351 n.19 (2011)
  - *Kowalchik v. Brohl*, 2012 COA 49, 277 P.3d 885
  - *Carpenter v. Commissioner*, T.C. Memo 2013-172
  - *Esgar Corp. v. Commissioner*, 744 F.3d 649 (10th Cir. 2014)
  - *Markus v. Brohl*, 2014 COA 146, 412 P.3d 647
  - *State v. Medved*, 2019 CO 1, 433 P.3d 33
- Other guidance and reports
  - [www.colorado.gov/pacific/tax/gross-conservation-easement-gce](http://www.colorado.gov/pacific/tax/gross-conservation-easement-gce) (including reports of 2000-2013 conservation easement donations)
  - [www.irs.gov/pub/irs-wd/0126005.pdf](http://www.irs.gov/pub/irs-wd/0126005.pdf) (regarding state income tax deductions allowed to transferees)
  - [IRS Form 8283 and related publications](#) (regarding charitable contributions)

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FYIs represent a good faith effort to provide general information concerning a variety of Colorado tax topics in simple and straightforward language. By their nature, however, FYIs cannot and do not address all taxpayer situations nor do they provide a comprehensive overview of Colorado's tax laws. For this reason, FYIs are not binding on the Colorado Department of Revenue, nor do they replace, alter, or supersede Colorado law and regulations.

A taxpayer seeking additional guidance regarding the tax consequences of a particular transaction or factual scenario can request a Private Letter Ruling (PLR) or General Information Letter (GIL). Requests for PLRs and GILs must comply with certain requirements, which are currently set forth at 1 Code of Colorado Regulations 201-1, Rule 24-35-103.5. PLRs are binding upon the Department only with respect to the specific taxpayer that requested the PLR. GILs are for informational purposes only and are not binding on the Department.