



What Do I Do With My Conservation Easement Tax Credits?

By: Lyle Hood

Now that you've received your tax credit certificate, you must decide what to do with your credits. You have several choices:

1. Use it to pay your Colorado income tax. Any credit unused may be carried forward for 20 years to offset future Colorado income taxes. You get a dollar for dollar benefit with this option.
2. Transfer/sell your credits to another taxpayer. You will realize approximately 85% of the face value of the credits transferred.
3. Refunds from the state of up to \$50,000. This option is contingent upon the state controller certifying that state revenues are above certain thresholds. That was the case in 2015, but historically has been fairly rare.

CONSIDERATIONS: The sale or refund of credits is an income taxable event. The courts have determined that the tax credit is a capital asset. Therefore, any receipts are taxable as a capital gain. The courts have likewise determined that the tax credit has a zero basis, meaning that 100% of the proceeds are taxable. Since the credits are a capital asset, it's very important to distinguish between short term and long term gains. To be long term, the credit has to be held for more than a year. The first day of the holding period is the date the tax credit certificate was issued, not the date you donated your easement. Short term gains are generally taxed as 'ordinary income', thus potentially at the highest rates. Long term gains on the other hand offer very favorable tax rates-0%, 15% and 20% (maximum rate), depending on your other income. For example, a married couple could have income up to \$77,400 and actually pay 0% on the gain.

However, if you need the money, an immediate sale is frequently the best option. The generally sizable charitable donation deduction for your easement contribution should help mitigate any taxes on the sale. This is true for short or long term gains. Regardless, always retain enough credits to pay your Colorado income tax bill.

One strategy would be to sell/parcel out your credits over multiple years to manage and keep your taxable income at the most desirable levels.

PASS THROUGH ENTITIES: If you are a member of a pass through entity such as an "S" corporation, partnership, or LLC which donates a conservation easement, the tax credit is issued to the entity. The entity may transfer the credit or pass it through to its members. To transfer the credit requires approval from 100% of the members. Also, if the entity does not transfer the credit in the first year, it **MUST** distribute the credit to its members based on their pro rata share of the entity. They then individually decide how to utilize their credit.

CONCLUSION: The decision of when to sell or utilize and how much to sell is a complex one. You should carefully review the options and consequences with your accountant to achieve the most favorable results.

Lyle retired in 2017 after 44 years of practice as a Certified Public Accountant and has spent many years working on conservation easements in an advisory and compliance capacity. He served on the Conservation Easement Oversight Commission and currently serves on the board of the Rio Grande Headwaters Land Trust.

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