



NOVA SCOTIA NATURE TRUST

## Cross-Border Conservation Gifts: Fact Sheet for Appraisers

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## **Purpose**

Canadian land trusts are increasingly working with U.S. residents to protect important natural areas owned in Canada. Such “cross-border” conservation gifts present some unique challenges and complexities, including specific appraisal requirements. Because the donors are U.S. residents, and the land is in Canada, the appraisal must meet both Canadian and U.S. tax law requirements.

**This fact sheet is not intended to provide appraisal, legal, financial or other advice.** Its purpose is to provide appraisers with a basic overview of appraisal requirements for cross-border gifts of conservation land or interests in land, such as conservation easements (i.e. restrictions registered on title for conservation purposes) or remainder interests. It also highlights some of the available resources and reference materials. Since it is assumed that most appraisers reviewing this fact sheet will be based in Canada, the primary focus will be on U.S. appraisal standards that apply to such gifts, and more specifically, Internal Revenue Code (IRC) requirements, since these are likely less familiar to Canadian appraisers.

## **General Appraisal Standards**

All appraisals should conform to the requirements of the Canadian Uniform Standards of Professional Appraisal Practices, or in Quebec, Les Normes De Pratique Professionnelle Des Evaluateurs Agrees. Depending on how the cross-border conservation gifting is pursued, there may be two Canadian and one U.S. agency involved in establishing and administering appraisal criteria and in reviewing appraisals: the Canada Revenue Agency (CRA), the Ecological Gifts Program of Environment Canada, and the Internal Revenue Service of the U.S. Department of Treasury (IRS). The IRS administers very specific requirements for appraisals, particularly for conservation easement donations. In Canada, the requirements are not as specific, except for appraisals for donations made through the federal Ecological Gifts Program.

Because of the complexity of cross-border conservation gifts, and the potential tax implications on both sides of the border, it is recommended to use an appraiser with designation as an Accredited Appraiser Canadian Institute (AACI) from the Appraisal Institute of Canada, and one who has taken appraisal training through the Ecological Gifts Program. It would also be prudent to address the key appraisal requirements of both the IRS and the Ecological Gifts Program for all cross-border conservation gift appraisals. Resources and references for related statutes, regulations and other documents are listed under *Additional Resources* at the end of this document.

## **U.S. Appraisal Standards**

U.S. tax law requires a “qualified appraisal” whenever a taxpayer claims a U.S. federal income tax deduction for charitable gifts having a value of five thousand dollars (\$5,000) or more. A qualified appraisal means an appraisal that is: treated as a qualified appraisal under regulations or other guidance prescribed by the IRS; and conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance prescribed by the IRS.

A qualified appraiser must meet the following general criteria:

1. The individual performs appraisal work for the public as a profession (and is compensated);
2. He or she demonstrates verifiable education and experience in performing appraisals of the type of property being appraised (i.e. conservation easements or gifts of conservation land);
3. He or she has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the IRS;
4. The appraiser must be “independent”, meaning he or she may not have any personal or financial interest in the property being appraised nor have any personal or business relationship with the prospective donor or donee other than the contracted appraisal assignment. Additionally, the appraiser's fee may not be based upon a percentage of appraised value or upon the donor’s tax deduction amount; and
5. He or she must not be prohibited from practicing before the IRS under Section 330 of Title 31 of the IRC at any time during the 3-year period ending on the date of the appraisal.

It is important to note that in 2006, changes to U.S. tax law gives the IRS the power to issue new regulations on appraiser qualifications. As such, appraisers will have to show donors that they are qualified under the new law and any new Treasury regulations or guidance that may follow from it, in addition to meeting existing regulation requirements.

### **Penalty Provisions**

Significant IRS penalties exist for appraisers, donors and charities involved in misstatements of appraised value. Section 1219 of the Pension Protection Act adds new penalty provisions as of 2006. If the claimed value of property based on an appraisal results in a substantial or gross valuation misstatement, a penalty is imposed on any person who prepared the appraisal and who knew, or reasonably should have known, the appraisal would be used in connection with a return or claim for refund. There are also penalties for a donor who underpays taxes as a result.

## **Appraisal Contents**

Both Canadian and U.S. tax law requires appraisals to support most conservation gifts. The appraisal should include consideration of the following factors: cost or selling price, comparable sales, replacement cost and/or opinions of experts. To ensure tax deductibility for the donor, the IRS requires that ***the appraisal must be commissioned by the donor, not the donee.***

In most cases, a cross-border conservation gift should be supported by a full-narrative appraisal. The appraisal may not contain any unsupported assumptions or conclusions. Hypothetical conditions must be identified, and are only accepted where necessary for a reasonable analysis of the property.

To meet both Canadian and U.S. appraisal requirements, a qualified appraisal should include the following components:

1. Description of the property (location, physical features, condition, dimensions, property use, zoning and permitted uses, potential use for other higher and better uses, name and address of present owners, legal description, declaration of the interest(s) being valued);
2. Purpose and scope;
3. Terms of any agreement or understanding which restricts the donee's use or disposal of the property, such as a copy of the conservation easement (or equivalent document).  
*Note: the document does not have to be registered at the time of the valuation;*
4. Terms of any agreement or governmental control relating to use, sale or disposition of the donated property;
5. Methods of valuation and process used to determine the fair market value;
6. Specific basis for the valuation, such as specific comparable sales transactions or statistical sampling;
7. Copy of title to the property;
8. Information about the appraiser and his or her qualifications (name, address, type of business, tax ID number (U.S), background, experience, education, membership in professional associations);
9. The appraiser's conclusions, with references to attached exhibits and appendices;
10. Definition of fair market value;
11. Statement that the appraisal was prepared for income tax purposes;
12. Appraised fair market value of the property on the date (or expected date) of contribution;
13. Effective date of the appraisal;
14. Appraiser's signature.

Note: For cross-border conservation gifts being donated through the Canadian federal Ecological Gifts Program, all appraisals must be reviewed by a national appraisal review panel,

and the value substantiated by the federal Minister of the Environment. Additional documentation is required in the application. See guidelines listed under *Additional Resources*.

### **Special Considerations for Conservation Easement Appraisals**

Gifts of conservation easements and conservation remainder interests in Canada by U.S. residents will most likely be structured to meet requirements of a *qualified conservation contribution* under the IRC to ensure proper tax benefits for the donor. Sections 170(h) of the IRS Code and U.S. Treasury Regulations 1.170A(14) provide background on such gifts and related appraisal considerations.

In cases where there are substantial sales of restricted land or comparable easements, the value of the conservation easement may be substantiated with such sales. Otherwise, conservation easements are appraised on a “before and after” basis. The general rule is that the value of a conservation easement is the difference between the fair market value of the property it encumbers (“before” value), and the fair market value of the property after the conservation easement is in place (“after” value). In other words, the fair market value of the conservation easement is the difference between what the property would sell for if it were put to the most valuable economic use possible, without the easement restrictions in place, and what it would sell for when certain uses are restricted. However, each appraisal problem and assignment has unique circumstances that have to be considered on an individual basis.

If a conservation easement covers a portion of a contiguous property, again, the value is the difference between the fair market value of the entire property before and after the conservation easement. If the conservation easement increases the value of any other property (contiguous or not) owned by the donor or related persons, the amount of the tax deduction is reduced by the increase in the value of the other property.

The objective assessment of the “before” value of the property must take into consideration both the current use of the property and the likelihood (whether remote or immediate) that the property may be developed in the future. Further consideration must also be given to any effect from zoning, conservation, historic preservation or other laws that already restrict the potential use of the property. If the conservation easement has no material effect on the value of the property, or if it increases the value of the property, then no tax deduction is permitted.

If a conservation easement allows for any development, any objective assessment of the “after” value of the property (e.g. the value of the property *after* the easement is put in place) must take into account the effect of the development. In some cases, an easement permitting development might allow for higher use than is currently available on the property, but is less than the potential highest and best use of the property.

The value of a conservation easement is not reduced because of special requirements for transferring of the easement (i.e. if the easement must be transferred to an *eligible donor* as defined by Section 170(h) of the IRC). Such restrictions are intended solely to ensure that the easement will remain dedicated to conservation purposes, and thus further the rationale behind a *qualified conservation contribution*.

### **Adjusted Cost Base of the Conservation Easement**

In most cases, the CRA will require verification of the conservation easement's adjusted cost base (as well as fair market value) as part of the cross-border conservation gift process. The adjusted cost base is essentially the cost of acquiring the property (typically purchase price and certain acquisition expenses).

Determining the adjusted cost base of land may be simple and can be supported by documents such as deeds, purchase and sale agreements, real estate or tax records. However, such determination is not simple where an easement has been placed on the property. It may be difficult to place a value on what an easement may have been worth in the past when the property was acquired (i.e. the adjusted cost base of the easement itself).

Recognizing this challenge, the CRA may accept a proportional value method for the conservation easement valuation. The appraiser determines the current fair market value of the entire property and of the conservation easement. The proportionate value of the conservation easement is then determined. In other words, if the conservation easement today is determined to be worth 1/3 of the fair market value of the property, then the conservation easement's adjusted cost base can be considered to be 1/3 of the land's adjusted cost base. The donor and donee should assess this proportional value and be sure it seems reasonable. Ultimately, the CRA determines whether to accept this value or not. Alternatively, the conservation easement can be appraised as of the time the land was purchased, but this can be more challenging for an appraiser and may cost more, particularly where the property was acquired many years prior.

### **Valuation of Remainder Interests**

With a gift of remainder interest, even though the gift of interest in land is made currently, the donee's full enjoyment of the gift is postponed until a later date, when the person with a life interest dies. When they die, their remaining interest in the land becomes the property of the donee. Under U.S. tax law, the value of the remainder interest for income tax purposes is determined by taking the current fair market value of the interest and reducing or discounting it based on life-expectancy tables and interest-rate-assumption tables. More specifically, according to IRC Section 170(f)(4) and Treasury Regulations 1.170A-12, to determine the value of a remainder interest in real property, depreciation (computed on the straight line method) and depletion of such property must be taken into account. Multiply the fair market value of the property on the date of the gift by the appropriate factor (see Publications 1457 and 1458). Make an adjustment for depreciation or depletion using factors shown in Publication 1459.

For a remainder interest for conservation purposes, the current fair market value of the property (against which the limitations of Section 1.170A-12 are applied) must take into account any pre-existing or contemporaneously recorded rights that limit, for conservation purposes, the use to which the subject property may be put.

Good sources on valuation of conservation easements and remainder interests include *Appraising Easements* by the Land Trust Alliance, the *Internal Revenue Service Publication 526: Charitable Contributions*, and *Publication 561: Determining the Value of Donated Property*.

### **Appraisal Timing**

U.S. tax law requires that the appraisal and IRS Form 8283 (see below) be completed within the period between 60 days prior to the date of contribution and the filing of the donor's federal income tax returns for the year in which the charitable contribution is made. CRA advises that the appraisal should be completed no more than six months before the effective date of the donation for Canadian tax purposes.

For Ecological Gifts, an appraisal review (by the national Ecological Gifts Program appraisal review panel) is required before the gift is accepted into the program. Where the donor submits an *Application for Appraisal Review and Determination* to Environment Canada before making the gift, the appraisal's effective date may not be more than six months prior to application. If the donor has already made a gift, the donor has three years to request a valuation.

If any of these timing requirements are not met, the appraiser must verify in writing that there has been no material change in use of the property, and no material change to the market value. Alternatively, a new appraisal may need to be completed, or the appraisal updated. The written confirmation or updated or new appraisal must be submitted with the Ecological Gifts application or any tax return filing.

### **IRS Form 8283**

IRS Form 8283 is a summary form filed with the donor's federal income tax. Its purpose is to document that a noncash charitable contribution has been made, the details of which are included in a full narrative appraisal. It must be signed by the donor, the appraiser and donee organization (indicating that the donee has received the gift). For gifts worth more than \$500,000, the entire appraisal must be attached to the donor's U.S. tax return.

Key components of Form 8283 include the following:

#### Section B (for Donated Property over \$5,000). Part I Information on Donated Property

1. Name and taxpayer identification number of the donor (social security number if donor is an individual or employee identification number if donor is a partnership or corporation);
2. Description of the property;
3. Brief summary of the physical condition of the property;
4. Appraised fair market value of the property interest on the date of contribution;
5. Manner of donor's acquisition of the property (purchase, gift, etc.) and the date of donor's acquisition;
6. Donor's cost or adjusted basis (adjusted cost base) in the property;
7. For bargain sales, the amount of consideration received by the donor;
8. Amount claimed as a deduction; and
9. Date the donee received the property or interest in property.

### Part III Declaration of Appraiser

1. Name, address and tax identification number of the appraiser;
2. Declarations by the appraiser pertaining to interests in the transaction and the fee arrangement (with signature, business address and identifying number):
  - a. The appraiser is not the donor, donee, a party to the transaction, employed by or related to the donor or donee. If regularly used by any of the foregoing parties, he or she performed most appraisals for other persons during the tax year;
  - b. The appraiser holds him or herself out to the public as an appraiser or performs appraisals on a regular basis;
  - c. Because of his or her qualifications (as described in the appraisal), the appraiser is qualified to make appraisals of the type of property being valued;
  - d. The appraisal fees were not based on a percentage of the appraised property value or amount of donor's deduction;
  - e. He or she understands that a false or fraudulent overstatement of the property value may subject him or her to the penalty under IRC section 6701(a) (aiding and abetting the understatement of tax liability); and
  - f. The appraiser is not barred from presenting evidence or testimony by the Office of Professional Responsibility.

### Part IV Donee Acknowledgement

1. Name, address and tax identification number of the donee;
2. Signature of donee, acknowledging receipt of the gifted property and making certain declarations (acknowledgement does not mean the donee agrees with the claimed fair market value):
  - a. It is a qualified organization under IRC Section 170(c) and that it received the donated property (including date of donation)
  - b. If it sells, exchanges or otherwise disposes of the property within 2 years, it will file Form 8282 and give donor a copy.
  - c. It does not intend to use the property for unrelated use

Donor Attachment to Form 8283: The donor must attach a statement that:

- d. Identifies the conservation purposes further by the donation;
- e. Shows, if before and after valuation is used, the fair market value of the underlying property before and after the gift;
- f. States whether the donor made the donation in order to get a permit or other approval from a local or other governing authority and whether the donation was required by a contract; and
- g. If the donor (or related person) has any interest in other property nearby, and if so, a description of that interest.

### **Additional Resources**

*A Guide to Cross-Border Conservation Gifts by U.S. Residents*, Bonnie Sutherland. Nova Scotia Nature Trust, 2006. Available at [www.nsnt.ca](http://www.nsnt.ca) or (902) 425-5263.

*Ecological Gifts Program. Guidelines for Appraisers*, Environment Canada, Canadian Wildlife Service. [www.cws-scf.ec.gc.ca/egp-pde/](http://www.cws-scf.ec.gc.ca/egp-pde/)

*Appraising Easements*, Land Trust Alliance. 1999.

*Land Trust Standards and Practices*, Land Trust Alliance, 2004.

*Actuarial Values. Publications 1457, 1458 and 1459 (for valuing remainder interest)* U.S. Treasury Department.

*Charitable Contributions*, Publication 526, U.S. Treasury Department.

*Determining the Value of Donated Property*, Publication 561, U.S. Treasury Department.

*Notice 4002-41*. U.S. Treasury Department.

*Notice 2006-96, Guidance Regarding Appraisal Requirements for Noncash Charitable Contributions*, U.S. Treasury Department.

### **Relevant Statutes and Regulations**

#### Internal Revenue Code

Section 170(f)(4) (2004). (*Valuation for Remainder Interests*)

Section 170(f)(11) (2004). (*Appraisers and Appraisals, Reporting/Substantiation*)

Section 170(h) (2004). (*Qualified Conservation Contributions/Conservation Easements*)

Sections 6662, 6695, 6700, 6701, 6694. (*Valuation Misstatements and Penalties*)

#### U.S. Treasury Regulations

1.170A-12. (*Remainder Interests and Conservation Valuation*)

1.170A-13 (2003). (*Appraisal Requirements*)

1.170A-14 (2003). (*Qualified Conservation Contributions/Conservation Easements*)

Pension Protection Act (2006) (Section 1219) (*Valuation Misstatements and Penalties*)

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