



NOVA SCOTIA **NATURE** TRUST

**Cross-Border Conservation Gifts:
Fact Sheet for Donors**

October 2006

Bonnie Sutherland
Nova Scotia Nature Trust
PO Box 2202 Halifax, NS B3J 3C4
(902) 425-5263
nature@nsnt.ca www.nsnt.ca

Version 1.000 06-10-31

Introduction

More and more U.S. residents are interested in protecting conservation lands in Canada. While the primary motivation is protecting outstanding natural areas, most donors also hope for tax benefits in recognition of the significant natural legacy they have created to benefit generations to come. Many donors expect a conservation gift in Canada to essentially work the same as it would for protecting land in his or her home state in the U.S. Unfortunately, “cross-border” conservation gifts involve complex legal and tax issues and additional procedures beyond typical conservation gifts.

The purpose of this document is to provide some general background information for potential donors of cross-border conservation gifts. This document does not provide tax, legal, estate planning or other advice. **It is essential for donors to obtain independent advice from professional advisors who understand these issues on both sides of the border.**

Conservation Partners

A U.S. donor may work with a Canadian land trust or government agency to complete a cross-border conservation gift. Others may partner with a U.S. land trust, or combination of both. The income, estate and gift tax consequences will vary significantly depending on the “donee” (i.e. the organization that receives the conservation gift). For example, if a conservation gift is donated to most U.S. land trusts, the donor will receive an income tax deduction against U.S. income, but may have to pay capital gains tax on the gift in Canada. Conversely, with a Canadian donee, the donor can avoid paying the capital gains tax, but will only be able to use the tax benefit against Canadian-source income.

A new U.S. organization is currently being created, the *American Friends of Canadian Land Trusts*. Its mission is to support Canadian land trusts and U.S. donors in completing cross-border conservation gifts. The organization is developing a national program to support and facilitate cross-border gifts. It is hoped that this new organization will be able to offer the most favourable tax outcome for cross-border gifts—an income tax deduction against U.S.-source income, and avoidance of Canadian capital gains.

Conservation Gifts Defined

There are a number of different conservation options for protecting important conservation lands in Canada. While many are similar to those available for protecting conservation land within the U.S., there are some important considerations when the gift is cross-border in nature.

Gift of Land: A donation of fee simple interest (or full ownership) in land.

Gift of Conservation Easement: A voluntary, legal agreement between a landowner and a qualified conservation organization that restricts the future uses of land pursuant to a defined set of conservation purposes. The conservation easement is registered on title for the property and is binding against future owners.

Conservation easement law varies across Canada, and cross-border easements must address specific language and content requirements for the respective jurisdiction where the land is located. At the same time, to address significant U.S. income, gift and estate tax considerations, cross-border conservation easements should also address the many U.S. tax law requirements for tax deductible conservation easements (see further discussion below).

Canadian land trusts planning to accept a conservation easement from a U.S. donor should also take certain steps to qualify with the IRS as a *publicly-supported charity* (again, see discussion below). U.S. organizations planning to accept a cross-border conservation easement in Canada may also need to take certain steps to become eligible to hold easements in a specific province or territory.

Gift of Remainder Interest: A donation of interest in land in which the donor retains the right to use the property during his or her lifetime, after which the remainder interest in land passes to the donee organization.

Testamentary Gift: A donation of land or conservation easement (or cash or other assets) donated through a will. Testamentary gifts to Canadian charities should provide the same estate tax benefits as gifts to a U.S. charity. For conservation easements, special considerations apply with regards to ensuring that the easement meets U.S. tax law requirements, and that the Canadian charity meets certain Internal Revenue Service requirements (see below).

“Bargain Sale” (known as a Split-Receipt Donation in Canada): A landowner may choose to sell land for an amount less than full fair market value. The difference between the donor’s sale price and the fair market value of the property is considered a gift for income tax purposes. Such gifts are subject to specific rules and limitations in Canada.

Conservation Gifts and Financial Incentives

Generally speaking, landowners who wish to make gifts for conservation purposes are first and foremost motivated by their love of the landscape and their desire to see a particular natural landscape remain intact. Whether one acts on his or her inclination to conserve land is often motivated, in part, by financial incentives. Such incentives include charitable tax deductions, capital gains tax avoidance, reducing estate tax liability and in some cases reducing the ongoing costs of property ownership.

Needless to say, the financial incentives that often drive conservation transactions are complex on either side of the border. They become even more complex for a U.S. resident with land holdings in Canada. For this reason we reiterate the need for legal and tax counsel that is experienced in cross-border conservation transactions.

Tax Issues Associated with Cross-Border Conservation Gifts

The following is a brief summary of various issues to be considered in planning a cross-border conservation gift.

Canadian capital gains tax

A conservation gift, such as a gift of land, conservation easement, or remainder interest, is subject to capital gain (and therefore a potential capital gains tax) in Canada, just as if the land or interest in land was sold. The capital gain is based on the difference between the fair market value of the property and the adjusted cost base of the property (the costs for acquiring the land, as well as certain documented expenses). The tax liability is generally calculated on 50% of the capital gain (i.e. the donor pays tax on 50% of the capital gain, at his or her marginal tax rate).

A donor may be able to reduce the capital gains tax, depending on the donee. One option is to donate the gift through the Canadian Ecological Gifts Program. This is possible if the donee is a Canadian charity or government agency, and an eligible Ecological Gifts recipient, and if the gift meets certain ecological criteria.

A second option is to reduce or eliminate the capital gains through a special “election” under the Canadian Income Tax Act. This option is only available if the donee is a Canadian charity, government agency or a U.S. charity with special status in Canada as a *prescribed donee*. Note: while there are currently no *prescribed donees* actively involved in cross-border conservation, it is hoped that the *American Friends of Canadian Land Trusts* will be able to obtain both U.S. *publicly-supported charity* status, and *prescribed donee* status in Canada. It would then be able to provide an ideal tax scenario for donors: elimination of the Canadian capital gains tax, and provision of a tax deduction against U.S. income). If the gift is to any other U.S. charity, capital gains taxes often can not be avoided or reduced and usually will be taxed.

U.S. federal and state income tax deduction

A cross-border charitable gift may be tax deductible at the state and federal levels. Deductibility at the state level varies in accordance with state law and is beyond the scope of this summary.

For gifts of conservation easements or remainder interests, deductibility at the federal level requires strict adherence to Internal Revenue Code guidelines for *qualified conservation contributions*. That means that even though the land is in Canada, and even if the donee is a Canadian charity, the conservation easement or remainder interest should meet all the same criteria as those in the U.S. to ensure deductibility. Such requirements range from very specific wording and restrictions in the easement document, to issues related to mortgages on the property, mineral interests and the type of organization to which the easement can be transferred. Meeting U.S. *qualified conservation contribution* criteria is essential to provide income tax deductions against the donor’s U.S. income (if donee is a U.S.-based charity) or against the donor’s Canadian income (if the donee is a Canadian charity).

Under a tax treaty between the U.S. and Canada, gifts to Canadian charities may provide an income tax deduction on Canadian-source income. To maximize the deductibility, the Canadian land trust can take steps to be recognized as a *publicly-supported charity* in the U.S. (as opposed to being considered a *private foundation* which is the default classification). Typical U.S. income tax deduction limits would be applied to the Canadian-source income. With recognition as a *publicly-supported charity*, the deduction limit for gifts of cash or qualified conservation easements (at least during 2006 and 2007*) would be 50% of the donor’s adjusted gross income, and 30% for gifts of land, or appreciated securities. Without such recognition, deduction limits for cash would generally be reduced to 30% and for land and appreciated securities to 20%.

Gifts of conservation easements to private foundations (including Canadian land trusts that have not made this application) are not deductible because they do not meet U.S. tax law requirements for *qualified conservation contributions*.

*(*note: Current U.S. tax law as of August 2006 provides enhanced deductions for conservation easements completed during 2006 and 2007 only. The deduction ceiling is raised from 30% to 50% for qualified conservation easements given to publicly-supported charities, and the unused benefit can be carried forward for fifteen years, rather than the usual five years).*

U.S. state and federal gift taxes

Gifts of cash or real property interests exceeding certain values have the potential to trigger gift tax liability for the donor. Properly sequenced and managed conservation transactions may avoid triggering this tax. The tax might apply if a conservation easement is granted to a charity that is not deemed to be a *publicly-supported charity* or if the easement conditions and wording do not meet U.S. tax law requirements as a *qualified conservation contribution*, as discussed above.

U.S. estate tax benefits

A charitable gift of land, conservation easement or remainder interest may provide significant estate tax benefits. The value of the gift may be exempted from calculation of the donor's estate, and significantly reduce the estate tax liability.

Typically, state and federal estate tax liability can range from 40 to 55% of the estate's total value. This liability is due and payable within nine months. By making a charitable gift of land or interest in land, the estate's value, and thereby the potential estate tax liability, is correspondingly reduced. This reduction in value may be significant, particularly if the value of the estate is reduced below certain thresholds that trigger estate tax liability. A conservation easement can make the difference between land being passed successfully to the next generation, and a disastrous situation where heirs are forced to sell property to pay the associated estate taxes.

For conservation easements, it is essential for the donee to apply for recognition as a *publicly-supported charity* and for the conservation easement to meet all the U.S. tax law criteria mentioned above. These requirements apply even if the donee is a Canadian land trust, and the land is in Canada. Otherwise the gift may not be deductible and the major estate tax problems could arise for heirs, in that the land is valued, for estate tax purposes, as if there are no restrictions in place. The estate tax on the land could be so high that heirs have to sell the cherished family land.

Additional Steps for Cross-Border Conservation

There are several specific additional steps required for a cross-border conservation gift above and beyond those required for typical conservation gifts. Examples include applying to the Canada Revenue Agency for a certificate of compliance for a non-resident disposition of land in Canada, applying to reduce or eliminate capital gains tax on the gift (depending on the donee) and filing both a Canadian and U.S. income tax return and associated documents. The appraisal should meet both

Canadian and U.S. appraisal requirements. A U.S. donee organization may need to amend provincial conservation legislation or go through an application process to be eligible to hold land or a conservation easement in a particular province. The donor needs to provide certain documentation on the property (such as maps and photographs) to create baseline documentation of the property, to meet U.S. tax law requirements. Conservation easements need to be carefully crafted to address both Canadian conservation easement and tax law, and U.S. tax law for *qualified conservation contributions*.

A word of caution. It is important to recognize that cross-border conservation gifts are complex, and will likely involve time and resources beyond those typical for gifts within the U.S. Cross-border conservation gifts also have serious potential tax consequences if not carried out properly. Such consequences range from significant tax savings lost, or a hefty and unanticipated Canadian capital gains tax on the gift, to U.S. tax law failing to recognize the value of an easement for estate tax purposes (resulting in an unexpected and large estate tax, making it difficult to pass the property on to heirs). Professional advice is critical.

There is a growing body of resources (listed below) available to provide background and reference material for donors, land trusts, appraisers and professional advisors to assist in ensuring a smooth process for a cross-border conservation gift. For current information on the development of the *American Friends of Canadian Land Trusts*, and a program to support cross-border conservation gifts in Canada, please visit www.nsnt.ca.

Additional Resources

Cross-Border Conservation Tool Kit. Bonnie Sutherland. Nova Scotia Nature Trust, 2006.
(available at nature@nsnt.ca or (902) 425-5263, www.nsnt.ca)

A Guide to Cross-Border Conservation Gifts by U.S. Residents.

Cross-Border Conservation Gifts by U.S. Residents: Fact Sheet for Appraisers.

Cross-Border Conservation Gifts by U.S. Residents. Fact Sheet for Donor Advisors.

Cross-Border Conservation Gifts by U.S. Residents: Fact Sheet for Canadian Land Trusts.

Cross Border Conservation Easement Template.

The Canadian Ecological Gifts Program Handbook. Environment Canada Ecological Gifts Program.
www.cws-scf.ec.gc.ca/egp-pde/

Preserving Family Lands: Book I (Essential Tax Strategies for the Landowner), 3d ed. Stephen J. Small.
(Boston, M.A.: Landowner Planning Centre, 1998).

Preserving Family Lands: Book II (More Planning Strategies for the Future), Stephen J. Small. (Boston, M.A.:
Landowner Planning Centre, 1997).

Preserving Family Lands: Book III (New Tax Rules and Strategies and a Checklist), Stephen J. Small.
(Boston, M.A. Landowner Planning Centre, 2002).

Funding for this cross-border conservation resource was generously provided by:

The Davis Conservation Foundation, Donner Canadian Foundation, EJLB Foundation, Environment Canada's
EcoAction Community Funding Program and Ecological Gifts Program, George Cedric Metcalf Charitable
Foundation, Norcross Wildlife Foundation, and the Salamander Foundation