South Carolina Conservation Incentives Act
An Innovative Approach to Conservation

By Scott Barnes and Chip Campsen

The South Carolina Conservation Incentives Act (H3782, Act 283) is an innovative conservation incentive with which tax and real estate practitioners should become familiar. With certain limitations, the Act provides a state income tax credit for voluntary donations of land for conservation and for conservation easements that qualify as charitable deductions under federal tax law. Signed into law on May 19, the Act becomes effective on June 1, 2001.

Donations of land for conservation and conservation easements are typically made to nonprofit conservation organizations such as The Nature Conservancy, Ducks Unlimited (Wetlands America Trust) and the Lowcountry Open Land Trust. A conservation easement is a type of negative easement that prohibits the land upon which the easement is placed (the servient estate) from being developed in a fashion that is inconsistent with the terms of the easement. Conservation easements are enforceable by the nonprofit organizations to which they are conveyed and typically permit continuation of traditional rural land uses such as farming, timbering, hunting, fishing and game management. Their conservation effect is accomplished through prohibitions or limitations on subdivision and development.

Current federal and state tax law allows a deduction for donations of land for conservation and qualifying conservation easements as charitable contributions to nonprofit organizations. The amount of the deduction is the value of the donation as established by an appraisal. The tax credit provided for by the Conservation Incentives Act is in addition to this deduction and is equal to 25 percent of the value of the donation. An important aspect of the tax credit is its transferability. This transferability enables donors to realize the credit provided for by the Act and then either recognize the credit on their own returns or sell the credit if they so desire.

Donations of land for conservation and conservation easements have typically been made by higher income taxpayers who quickly recognize benefits of large deductions for charitable contributions as offsets to taxable income. The tax credit established by the Conservation Incentives Act is an additional and powerful incentive for all owners of rural land to voluntarily place easements on their property. However, the transferability of the new tax credit creates an incentive for a whole new class of property owners—those who are land rich and cash poor. Instead of carrying forward unused portions of the tax credit over many years, donors can sell the credit to receive an immediate benefit from their gift. This feature should be particularly attractive to lower income taxpayers who otherwise would have to spread the tax credit over many years of taxable income.

As it moved through the General Assembly, the Conservation Incentives Act garnered support from a unique coalition of environmental and business groups that usually find themselves at odds with one another over conservation issues. This broad-based support is due to the Act’s incentive-based approach. Rather than regulating land use, which is ripe with acrimony and litigation, it provides an incentive for voluntary conservation. The Act is expected to preserve tens of thousands of acres of undeveloped land, while fully respecting property rights—a paradigm upon which both environmentalists and property rights advocates can agree.
Technical Aspects of the Conservation Incentives Act

Under Section 170(h) of the Internal Revenue Code of 1986, "qualified conservation contributions" of "qualified real property interests" to "qualified organizations" create a federal income tax deduction. The size and type of deduction depends, among other things, on the length of time the property has been held by the donor and the character of the property being contributed. The term "qualified conservation contribution" includes a restriction (granted in perpetuity) on the use that may be made of real property, commonly referred to as a "conservation easement." As a general rule, an individual placing a conservation easement on real property will be entitled to a deduction equal to the difference between the fair market value of the property before the easement is placed on the property and the fair market value of the property after the easement has been placed on the property as determined by a qualified appraisal.

South Carolina follows federal law, and South Carolina taxpayers are entitled to both a federal and state income tax deduction for "qualified conservation contributions."

After May 31, 2001, South Carolina taxpayers will be entitled to both a state income tax deduction and a credit against South Carolina income taxes. To obtain the credit, a South Carolina taxpayer must have qualified for and claimed on his or her federal income tax return a charitable deduction for either a gift of land for conservation or for a qualified conservation contribution. The donation must have been made after May 31, 2001 on a qualified real property interest located in the state of South Carolina. If a taxpayer so elects, he or she may claim a credit, with certain limitations as discussed below, in an amount equal to 25 percent of the total amount of the deduction attributable to either a gift in land for conservation or a qualified conservation contribution of real property located in the state of South Carolina. To the extent the credit is unavailable for use by the taxpayer in a particular year, it may be carried forward to succeeding tax years until all of the credit is claimed. In addition, all or a portion of the credit may be transferred, devised or distributed, with or without consideration, to a third party. Thus to the extent a taxpayer cannot use the credit, he or she has the right under the Act to sell it to one or more third parties. To be effective, the sale, transfer, devise or distribution requires written notification to and approval by the Department of Revenue. (It is anticipated that the Department of Revenue will issue some form of announcement to taxpayers establishing the notification and approval procedure for taxpayers who wish to transfer the credit to a third party.)

The amount of credit that can be used by a taxpayer is subject to certain limitations. The credit, along with any other state income tax credits of a tax-payer, cannot exceed the taxpayer’s total income tax liability for any taxable year. In addition, the credit is subject to a per acre cap of $250 per acre and an annual cap of $52,500. In determining the acreage to be included in calculating the $250 per acre cap, all upland and wetlands subject to a qualified conservation contribution are included other than property lying within the intertidal zone. Wetlands including ponds, impoundments, bottoms and Carolina Bays can be included in the acreage computation. As mentioned earlier, a taxpayer may not use more than $52,500 of credit in any one taxable year. Any unused credit may be transferred to a third party with or without consideration and/or may be carried forward to a subsequent year. While the Act contains no specific language, it seems reasonably clear a taxpayer has the right to choose when to use the credit and the amount of credit to be used, subject of course to the caps discussed above. The mathematical application of the caps and the sale of the credit can be better understood by the following examples:
A. A plantation owner placed a conservation easement on her 4500 acre plantation located in Berkeley County. Based on a qualified appraisal the value of the easement is determined to be $1,800,000 for federal income tax purposes. The South Carolina income tax credit is $450,000, which may be utilized by the plantation owner or sold to one or more third parties. The maximum amount of credit that may be utilized by the plantation owner in any one year to offset South Carolina income tax is $52,500.

B. A husband and wife own a vacation home and 20 acres on Edisto Island. They place a conservation easement on the property, which is valued at $45,000 for federal income tax purposes. The South Carolina income tax credit is $11,250 but the $250 per acre cap reduces the credit to $5,000.

C. A farmer on Wadmalaw Island owns 500 acres of farm land and raises vegetables and cut flowers. He places a conservation easement on the farm and is advised by a qualified appraiser that the value of the easement is $1,500,000. The available South Carolina income tax credit is $375,000 of which $125,000 is available for use as a result of the $250 per acre cap. The farmer, because his South Carolina tax liability averages $5,000 per year, decides to sell $100,000 of the credit to two of his neighbors for $80,000 with each neighbor purchasing $40,000 of credit. The farmer notifies the South Carolina Department of Revenue of the proposed sale and receives written consent from the Department authorizing the transaction. The farmer pays federal and state income taxes on the income derived from the sale of the credit.

The Act also contains a safe harbor provision for properties utilizing forestry and silva culture practices that may preclude an income deduction under Section 170(h) of the Internal Revenue Code of 1986. In such a case, a state income tax credit is allowable even though no state income tax deduction is permitted if (i) the forestry and silva culture practices permitted by the easement conform to Best Management Practices established by the South Carolina Forestry Commission at the time the easement was made or the practice was undertaken; (ii) the easement in all other respects conforms to the requirements of Section 170(h) of the Internal Revenue Code and the applicable regulations established for "qualified conservation contributions" of "qualified real property interests;" and (iii) the taxpayer provides the Department of Revenue with information that the department considers necessary to determine the taxpayer would otherwise be eligible for the deduction allowed under this Section 170(h).

Finally, the Act amends Article 3 of the Probate Code to provide that a personal representative of an estate or a trustee of a trust has the authority if certain procedural safeguards are met to grant a conservation easement or a fee simple gift of land for conservation purposes. The personal representative or trustee must have the written consent of all of the heirs, beneficiaries and devisees whose interests are affected by the donation and a guardian ad litem must be appointed to represent the interests of any unborn, unascertained or incapacitated persons. While this provision should prove to be helpful for personal representatives of an estate who seek to generate an estate tax deduction through the creation of a qualified conservation contribution, it is of little benefit to an estate or trust for federal or state income tax purposes since an estate or trust is not entitled to an income tax deduction for a qualified conservation contribution. See, Treas. Reg. § 1.642(c)-1.

Conclusion
The South Carolina Conservation Incentives Act will provide property owners in this state with the ability to preserve and protect significant historic and rural property in this state by providing an option to either decrease state income tax liabilities or generate additional cash flow through the sale of the credit to a third party.