

LAND TRUST RISK MANAGEMENT OF LEGAL DEFENSE AND ENFORCEMENT OF CONSERVATION EASEMENTS: POTENTIAL SOLUTIONS

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INTRODUCTION

As the dawn of the next century approaches, the private land conservation movement in this country must prepare to face a daunting opponent—landowners and their challenges to the restrictions placed on their land. These challenges are apt to take the form of legal scrutiny of one of the most popular land preservation devices currently in use, the conservation easement, and of the custodians of the conservation easement, the nonprofit land trust organizations. This

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article seeks to examine the complex interplay between land trusts, landowners, and the tie that binds them, the conservation easement. This article also proposes options for land trusts to protect against the inevitable legal challenges that await them in the next century by both present and future generations of landowners. Parts I, II, and III define and examine the roles of the land trust, conservation easement, and landowner. Part IV presents potential solutions for the individual land trust ranging from insurance solutions to options available for nonprofit entities, and Part V presents potential solutions for the land trust community as a whole, ranging from insurance solutions to nonprofit entity possibilities.

I. LAND TRUSTS

Land trusts are nonprofit organizations that, as all or part of their mission, work to conserve land.¹ By virtue of their nonprofit status as 501(c)(3) tax-exempt, charitable organizations,² among other characteristics, land trusts are qualified to accept qualified conservation contributions of real property interests, such as conservation easements.³ Land trusts may accept a qualified conservation contribution in the form of a conservation easement for exclusive conservation purposes, including the preservation of land for outdoor public recreation, protection of wildlife habitat, preservation of open space, and preservation of historically important areas.⁴

¹ See LAND TRUST ALLIANCE, 1998 NATIONAL LAND TRUST CENSUS (1998)(*Hereinafter* LTA CENSUS). See also John A. McVickar, *Land Trust: A Growing Conservation Institution*, 21-Oct Vt. B.J. & L. Dig. 33, 33 (1995). “Non profit” does not refer to an organization that is prohibited from earning a profit, rather it refers to an organization that is not permitted to distribute its profits, or benefits, to those who control it, or to any other than the general public. I.R.C. 501(c)(3); See BRUCE R. HOPKINS, THE LAW OF TAX-EXEMPT ORGANIZATIONS 4-5 (1998) (for discussion of definitions and private inurement, private benefit, excess benefit).

² I.R.C. § 501(c)(3). Land trusts are “tax-exempt” organizations and a subset of nonprofits because they are eligible to attract deductible, charitable gifts. See HOPKINS at 6.

³ A conservation easement is a legal agreement that permanently restricts the development and use of land to ensure protection of its conservation values. See LTA CENSUS *supra* note 2. See also discussion *infra* Part II.

⁴ Land trusts have been approved under the U.S. Internal Revenue Code and Regulations as

Land trusts protect a variety of land types, such as wetlands, watersheds, forests, river corridors, scenic views, ranches and farmland, wildlife habitat, trails, greenways, and urban lands.⁵ In addition to protecting land, land trusts also maintain land for recreation and public access, environmental education, land use planning, biological monitoring and research, ecological restoration, and management for rare and endangered species.⁶

Land trusts protect land in a variety of ways, including: undertaking or assisting direct land transactions through the purchase of land or acceptance of donations of conservation easements, transferring land to governmental agencies and other nonprofit organizations, acquiring land from governmental agencies and other nonprofit organization, raising funds for land acquisition on behalf of other organizations, identifying and encouraging conservation buyers,⁷ and conducting negotiations for land acquisitions by public agencies.⁸

charitable organizations devoted to conservation qualified to accept charitable conservation donations. I.R.C. § 501(c)(3) (1997); *See* *McVickar supra* note 1. Specifically, the above mentioned conservation purposes include:

- (i) The preservation of land areas for outdoor recreation by, or the education of, the general public,
- (ii) The protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystems,
- (iii) The preservation of open space (including farmland and forest land) where such preservation is
 - (I) for the scenic enjoyment of the general public, or
 - (II) pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or
- (iv) the preservation of an historically important land area or land area which
 - (i) is listed in the National Register, or
 - (ii) is located in a registered historic district.

I.R.C. § 170(h)(4)(A); see *Treas. Reg. § 1.170A-14(d)*(as amended in 1994) for further discussion of these conservation values.

⁵ *See id.*

⁶ *See id.*

⁷ Conservation buyers are conservation-minded individuals who are willing to invest in property to promote its ultimate and permanent protection as open space. *See LTA CENSUS supra* note 1. *See also* discussion *infra* Part III.

⁸ *See id.* The largest number of land trusts exists in New England (Connecticut, Massachusetts,

The most common methods of protection used by land trusts are land donations, conservation easement donations, and land purchase.⁹ When a land trust accepts a conservation easement from a landowner on the landowner's property, the land trust becomes responsible for enforcing the restrictions the landowner is agreeing to within that easement document.¹⁰ To enforce the terms of the easement, the land trust must monitor the eased property on a regular basis by visiting the property, and must maintain written records of the monitoring visits.¹¹ If the land trust learns that the terms of the conservation easement have been violated by the landowner, the land trust has a duty to require the owner to correct the violation and restore the property to its prior condition.¹²

Accepting or "holding" a conservation easement is a great responsibility for a land trust, requiring large amounts of time and resources, and when accepting such a responsibility, a land

Maine, New Hampshire, Rhode Island, and Vermont) with 419, where the first trusts originated and where it is touted that the conservation movement was born. *See id.* The largest increases regionally over the last decade have been in the Rocky Mountains (Colorado, Idaho, Montana, Utah, and Wyoming), the Southwest (Arizona, New Mexico, Oklahoma, and Texas), and the South (Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, South Carolina, Tennessee, Virginia, and West Virginia). *See id.* The Rocky Mountain Region increased from twenty to fifty-two land trusts, a 160 percent increase; the Southwest increased from fifteen to thirty-seven land trusts, a 147 percent increase, and the South increased from sixty-five to one hundred forty-two land trusts, a 118 percent increase. *See id.* States that as of 1988 had no land trusts, Arkansas, Hawaii, Mississippi, Nevada, and Utah, are now served by at least one land trust, and even the Virgin Islands is now serviced by one land trust. *See id.*

Land trusts have developed on three levels—nationally, such as The Nature Conservancy and the American Farmland Trust, regionally or statewide, such as Colorado Open Lands and the Vermont Land Trust, and locally, such as the Mountain Area Land Trust in Evergreen, Colorado and the Nantucket Land Council. *See* McVickar, *supra* note 1.

⁹ *See id.* Sixty-eight percent of land trusts use land donation as a common method of protection, sixty-two percent use conservation easements, and fifty percent use land purchase as a tool to protect land. *See id.*

¹⁰ JANET DIEHL & THOMAS S. BARRETT, THE CONSERVATION EASEMENT HANDBOOK 7 (1988) (*hereinafter* HANDBOOK).

¹¹ *See id.*

¹² *See id.* For those who doubt that easements will be violated, see Andrew C. Dana, *The Silent Partner in Conservation Easements: Drafting for the Courts*, THE BACK FORTY, Vol. 8, No. 1, at 1 (Jan./Feb. 1999) ("This article considers the importance of drafting conservation easements with the expectation that *every easement is likely to be violated at one time or another, so*

trust typically solicits a donation from the landowner in order to offset some of these costs.¹³ Improper use of funds, private inurement, and inability to monitor might all jeopardize a land trust's nonprofit, tax-exempt status.¹⁴ However, the responsibilities that accompany holding conservation easements have not curbed the growth in number or size of this country's land trusts.

As of 1998, more than 1,213 land trusts were operating within communities spread across the United States.¹⁵ Between 1989 and 1998, local and regional land trusts saved more than 4.7 million acres of land, and held more than 7000 conservation easements on 1.4 million acres.¹⁶

These numbers are likely to continue to grow. As part of the Clinton Administration's legacy to the environment and to Al Gore, President Clinton has included a new "Lands Legacy Initiative" in his Fiscal Year 2000 budget that will include \$150 million in matching grants for states, local governments and land trusts for land protection and acquisition achieved through a competitive grants program,¹⁷ and \$50 million in grants to states to develop open space plans and

conservation easements should be drafted in anticipation of a court defense of easement terms").

¹³ *See id.* at 6.

¹⁴ A nonprofit organization must be organized and operated to avoid private inurement so that "no part of . . . its net earnings . . . inures to the benefit of any private shareholder or individual." I.R.C. § 501(c)(3); *see HOPKINS* at 6.

¹⁵ *See id.* This is a sixty-three percent increase from 1988. *See id.* Jean Hocker, the President of the Land Trust Alliance attributes the increasing popularity of land trusts to two factors: first, people are realizing that open space is a finite resource that once lost can never be regained, and second, people are discovering that they can make a direct, lasting difference in their community and the world they leave their children and grandchildren through land trusts. *See id.*

¹⁶ *Id.* The amount of acres of land protected has increased from 2 million acres before 1989, a 135 percent increase in ten years, while the amount of land protected by conservation easements has increased by over 400 percent in the same time. *See id.*

¹⁷ *See* President's Lands Legacy Initiative, Fiscal Year 2000 Budget; *See* LAND TRUST ALLIANCE, LEGISLATIVE PROPOSALS FOR PERMANENT FEDERAL LAND PROTECTION FUNDING (1999)(*Herinafter* LEGISLATIVE PROPOSALS). The President has committed to seek legislation providing *permanent* funding for these programs. *See id.* Since there are very few federal programs that allow for direct grants to land trusts, this is the next best way to provide such funds. *See id.*

“smart growth” (anti-sprawl) initiatives.¹⁸ The Lands Legacy Initiative also provides for \$440 million for acquisition of federal lands, \$4 million for grants to cities to maintain, improve, and purchase parks and recreation facilities through an Urban Parks and Recreation Recovery Act, \$50 million for matching grants to states, communities, and Native American tribes for purchase of conservation easements on farmland, matching grants for states to purchase conservation easements on forest lands through the Forest Legacy Program in the amount of \$50 million, \$80 million for state and federal habitat conservation programs, and coastal restoration funds in the amount of \$200 million.¹⁹

In furtherance of the goal of private land conservation, Congress is actively considering legislation for which there is strong, bipartisan support that would devote more than \$1 billion and \$2 billion a year for land protection.²⁰ These bills include the Conservation and Reinvestment Act of 1999 sponsored in the House of Representatives by Representatives Don Young (Republican from Alaska) and John Dingell (Democrat from Michigan) through H.R. 701, and in the Senate by Senators Mary Landrieu (Democrat from Louisiana) and Frank Murkowski (Republican from Alaska) through S. 25,²¹ the Resources 200 Act, sponsored by

¹⁸ *See id.* These initiatives are to be paid for within the existing budget caps, not from the current budget surplus, and therefore, the Administration aims to acquire these funds through the legislative appropriations process in 1999. *See* LAND TRUST ALLIANCE, LEGISLATIVE UPDATE: LEGISLATION TO PROVIDE FEDERAL FUNDS FOR LAND PROTECTION (1999)(*Herinafter* LEGISLATIVE UPDATE). *See id.* President Clinton also expressed a commitment to legislation that would enable permanent funding for the initiatives. *See id.* One such initiative is the “Livable Communities Initiative” to help communities develop planned growth strategies to enhance their quality of life through funding in part provided by the “Better America Bonds” program. *See* LEGISLATIVE PROPOSALS *supra* note 17. The “Better America Bonds” program aims to create \$700 million in tax credits over five years to be used in lieu of interest payments for bonds in support of land acquisition, brownfield development, and park restoration, among other things. *See id.* Purchaser of the bonds receive the equivalent of their value in tax credits—a value in credits thought to be enough to support as much as \$9.5 billion in bond authority. *See id.*

¹⁹ *See* LEGISLATIVE PROPOSALS *supra* note 17.

²⁰ *See* LEGISLATIVE UPDATE *supra* note 18.

²¹ The Conservation and Reinvestment Act proposes to provide permanent funding from offshore

Representative George Miller (Democrat from California) as H.R. 798 and Senator Barbara Boxer (Democrat from California) as S. 446,²² and the Public Land and Recreation Investment Act of 1999, sponsored by Senator Dianne Feinstein (Democrat from California) through S.532.²³

These proposed initiatives and proposed legislation indicate the current trend of the administration and the legislature to embrace a government role in providing means to protect land, including encouraging those tools used by land trusts to protect private property. The most unique tool used for protecting private property, and that through which land trusts expose themselves to the most liability, is the conservation easement.

oil and gas drilling revenues through funding to the Land and Water Conservation Fund of \$378 million, matching funds to the Land and Water Conservation Fund of \$378 million to states allocated based on a state's size and population, \$144 million to the Urban Parks and Recreation Recovery Act for grants to cities to maintain, improve, and purchase parks and recreation facilities, \$1.24 billion in the form of "Impact Aid" for coastal states to offset the impacts of offshore drilling payments in lieu of taxes for counties with federal lands in the amount of \$70 million, and aid to state fish and wildlife agencies distributed to the states in the amount of \$440 million. *See* LEGISLATIVE PROPOSALS *supra* note 17. Unfortunately, at present and as introduced, this bill has no specific funding for land trusts or the purchase of conservation easements. *See id.*

²² *See* LEGISLATIVE PROPOSALS *supra* note 17. These bills propose to provide *permanent* annual funding from offshore oil and gas drilling revenues in the amounts of \$450 million to the Land and Water Conservation Fund for acquisition of federal lands, \$450 million for matching grants to the Land and Water Conservation Fund to be allocated by formula and competitive grant applications in two-thirds and one-third amounts respectively, \$100 million to the Urban Parks and Recreation Recovery Act for grants to cities to maintain, improve, and purchase parks and recreation facilities, \$50 million apiece for matching grants to states, Native American tribes *or land trusts* for purchase of conservation easements on farmland through the Farmland Protection Program, for purchase of conservation easements on ranchland through the Ranchland Conservation Program, and for purchase of conservation easements on forest lands through the Forest Legacy Program. *See* LEGISLATIVE PROPOSALS *supra* note 17. These bills also propose \$150 million in funding for the Historic Preservation Fund, \$300 million for programs conserving and managing ocean fish and wildlife, and \$300 million in grants to states for development and implementation of state wildlife conservation plans for non-game species under the Fish and Wildlife Conservation Act.

²³ *See* LEGISLATIVE PROPOSALS *supra* note 17. This Senate bill aims to *permanently* fund \$450 million to the Land and Water Conservation Fund for acquisition of federal lands, \$350 to the LWCF for matching grants to states and Native American tribes, and \$90 million to the Urban Parks and Recreation Recovery Act for grants to cities to maintain, improve, and purchase parks

II. CONSERVATION EASEMENTS

Conservation easements are unique, dynamic tools used by private landowners and land trusts to preserve private lands.²⁴ Plainly, a conservation easement is a voluntary contract between a landowner and a land trust, or government entity, that usually contains permanent, perpetual restrictions on the use and development of the landowner's property.²⁵

Those who describe property rights often use the example of a landowner possessing a bundle of sticks, each stick representing a property right held by the owner of the property.²⁶ Without a conservation easement, a landowner may have the right to construct buildings, subdivide his or her property, restrict access to the property, harvest timber, sell water rights, build ponds, and graze cattle on his or her property.²⁷ When a landowner enters into a conservation easement, he or she relinquishes some of these rights, or sticks, from his or her bundle of rights, such as the right to build additional buildings in a scenic vista, or the right to graze animals in sensitive wildlife habitat.²⁸ Because each landowner negotiates different restrictions for his or her property, and each piece of property is distinct from another, each conservation easement is a unique document, drafted to fit the particular property and the

and recreational facilities. *See id.*

²⁴ The author believes conservation easements are unique and dynamic for several reasons: first, because they are voluntary contracts, as opposed to government mandated controls; second, because they are designed for private property owners and their private property; third, no two are alike; and fourth, they are designed to be perpetual.

²⁵ William M. Silberstein, *Conservation Easements*, Isaacson, Rosenbaum, Woods & Levy, P.C. 1 (April 25, 1999); David J. Dietrich, *Conservation Easements*, 1 November/December (1998). *See* § 170(f)(3)(B), (h), 94 Stat. at 3206 (1980); HANDBOOK at 5; John L. Hollingshead, *Conservation Easements: A Flexible Tool for Land Preservation*, 3 ENV'T'L. LAW. 319, 321 (1997).

²⁶ *See* HANDBOOK at 5.

²⁷ *See id.* Landowners do not typically give up the right to prevent public access on their land, and usually retain the right of limited additional homebuilding, or agricultural building. *See also* Silberstein *supra* note 25, at 1.

²⁸ *See id.*

interests of its owner.²⁹

The specific rights, or sticks, a landowner relinquishes are described in detail within the conservation easement document itself.³⁰ The promises made by the landowner in the conservation easement run with the land to bind future landowners, usually perpetually, if the landowner is seeking a charitable deduction under the income tax code.³¹ A perpetual easement granted by a landowner as a charitable gift to a land trust may qualify that landowner for income, estate, and property tax benefits, since the tax code provides deductions and estate tax incentives to individuals and entities making conservation donations, providing that the donation meets certain statutory requirements.³²

Section 170(h) of the Internal Revenue Code provides the framework for the deductibility of charitable contributions of conservation easements by allowing an income tax deduction for a “qualified conservation contribution.”³³ The term “qualified conservation contribution” is defined in § 170(h)(1) as a contribution that is a “qualified real property interest” granted to a “qualified organization” that is exclusively for conservation purposes.³⁴ A “qualified real property interest” includes the entire interest of the donor in real property, other than a qualified

²⁹ *See id.*

³⁰ *See id.*

³¹ *See id.* at 7.

³² § 170(f)(3)(B), (h), 94 Stat. at 3206 (1980). The IRS ruled for the first time in 1964 that a taxpayer could deduct for income tax purposes the fair market value of a perpetual conservation easement. *See Rev. Rul. 64-205, 1964-2 C.B. 62.* Although the Tax Reform Act of 1969 appeared to reverse this ruling and prohibited deductions for contributions of conservation easements by enacting I.R.C. § 170(f)(3)(A), Pub. L. No. 91-172, 83 Stat. 556 (1969)(codified at I.R.C. § 170 (1994)), the Tax Reform Act of 1976 resolved this ambiguity by adding a clause (iii) to Section 170(f)(3)(B) to specifically allow deductions for easements on real property of not less than thirty years’ duration granted to a qualified organization exclusively for conservation purposes. The Tax Treatment Extension Act of 1980 provides the current framework for the deductibility of charitable contributions of conservation easements and retains the § 170(f)(3)(B)(iii) exception permitting a deduction for a qualified conservation contribution. Pub. L. No. 96-541, sec. 6, § 170(f)(3)(B), (h), 94 Stat. At 3206 (1980); sec. 6(a), § 170(f)(3)(B)(iii), 94 Stat. At 3206; *See Hollingshead supra* note 25, at 337-339.

³³ § 170(f)(3)(B)(iii), 94 Stat. at 3206.

mineral interest.³⁵ A “qualified organization” includes the following entities: the United States, a state, a political subdivision of the United States or a state, a state or federally chartered corporation, trust, community chest, fund or foundation that is organized and operated for a specified conservation purpose, and certain §501(c)(3) organizations, including land trusts.³⁶

When a landowner grants and conveys his or her rights to a qualified organization, such as a land trust, that entity then bears the responsibility of monitoring and enforcing the terms of the easement to ensure that the landowner is upholding his or her end of the conservation easement bargain.³⁷ A variety of organizations hold conservation easements aside from land trusts, including local entities such as towns, conservation commissions, state divisions of wildlife, watershed associations, and historic preservation organizations. Each organization must be prepared to monitor, enforce, and in some cases, defend its easements.

Conservation easements are not only defined by federal statutes and regulations, but also by state conservation easement acts.³⁸ The Uniform Conservation Easement Act approved by the National Conference of Commissioners on Uniform State Laws also provides some guidance as to how the conservation easement document should evolve.³⁹ The conservation easement

³⁴ § 170(h), 94 Stat. at 3206; Treas. Reg. §1.170A-14(b).

³⁵ As recently borne out by the Nekoosa case, the United States Court of Federal Claims denied a charitable income tax deduction claimed by Great Northern Nekoosa Corp. for the contribution of two conservation easements because the corporation had retained the right to mine gravel by surface mining methods. *Great Northern Nekoosa Corp v. United States*, 38 Fed. Cl. 645 (1997).

³⁶ HANDBOOK at 6.

³⁷ *See id.* at 7. The conservation easement has become an arguably more popular device to protect private property than purchasing private property in fee, because it is less costly at the outset than outright purchase of property, and allows eased property to remain on local communities’ tax roles. However, after the rush to protect land through easements has subsided, easement holders must face the fact that just placing the land under easement is not the end of the easement holder’s responsibility--this tool comes with the perpetual responsibility of monitoring and enforcement of that document and the promises contained therein.

³⁸ *See* Frederico Cheever, *Public Good and Private Magic in the Law of Land Trusts and Conservation Easements: A Happy Present and a Troubled Future*, 73 DENV. U. LAW REV. 1077, 1080 (1996).

³⁹ *See id.* HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE

document, like many contracts, is comprised of a title, names of the parties involved in granting and receiving the easement, recitals providing background about the property and its qualifying characteristics, title and legal description of the property.⁴⁰ It also describes attributes unique to a conservation easement, such as the conservation values of the property, a qualitative description of the property, a baseline inventory of the condition of the property, prohibited and permitted uses under the easement, remedies, enforcement, access, and amendment to the easement, among other things.⁴¹ Because each one of these sections within the easement document impacts the rights and obligations of the grantor landowner and the grantor land trust, the conservation easement should be negotiated on equal footing with attorneys on either side of the negotiation, so that those rights involved are adequately represented.⁴²

Giving away rights, such as the right to develop, reduces the value of a landowner's property, and the Internal Revenue Code rewards those landowners who gives up such rights by giving the landowner the value of the reduction in land as a charitable deduction against income.⁴³ The landowner is allowed to deduct an amount equal to thirty percent of his or her adjusted gross income each year for six years, or until the value of the gift has been depleted,

LAWS AND PROCEEDINGS OF THE ANNUAL CONFERENCE MEETING IN ITS NINETIETH YEAR, 117-124 (1981).

⁴⁰ See HANDBOOK at 166-208. Other sections typically occurring in land contracts include sections covering costs and liabilities, taxes, proceeds, condemnation, assignment, transfers, estoppel, notices, recordation, general provision, habendum clause, signature, acknowledgments, and exhibits, supplementary provisions, arbitration clauses, executory limitation, and subordination clauses. *See id.*

⁴¹ *See id.* Other important and unique sections within a conservation easement include the extinguishment, the affirmative purpose, the qualifications of the grantee, the grantee's commitment, the grant, the rights of the grantee, waiver, acts of beyond grantor's control, costs and liabilities, taxes, extinguishment, proceeds, condemnation, assignment, transfers, estoppel, notices, recordation, general provision, habendum clause, signature, acknowledgments, and exhibits, supplementary provisions, arbitration clauses, executory limitation, and subordination clauses. *See id.* and *see also* 156-165 for an example of a model conservation easement.

⁴² *See id.* at 66. *See also* Marlene Post, *Independent Attorney Representation in a Conservation Easement . . . How Important Is It?*, THE BACK FORTY, Vol. 7, No. 2, Nov./Dec. (1992).

⁴³ *See id.* at 8.

whichever comes first.⁴⁴ State income tax codes are also beginning to track the federal income tax provisions, and therefore provide a landowner for a double opportunity to reap income tax benefits, at both the federal and state level.⁴⁵

By reducing the value of the property, conservation easements also yield estate tax benefits by restricting the value to be placed on property at a landowner's death.⁴⁶ To the extent that the value of the property is reduced through the conservation easement restrictions, the estate tax burden shared by the heirs of the property is reduced.⁴⁷ Rather than making a gift of a conservation easement during his or her lifetime, a landowner could choose to bequest to a qualifying organization an easement in his or her will.⁴⁸ Such a gift would also cause the value of the easement to be deducted from the estate, and thereby reduce the estate taxes.⁴⁹

Further, if the easement qualifies under the 1997 Taxpayer Relief Act, forty percent of the value of the property remaining after the grant of the easement is excluded from the value of the estate, yielding a maximum exclusion of up to \$200,000 in 1999, and increasing by \$100,000 each year until reaching a maximum exclusion of \$500,000 in 2002.⁵⁰ Two of the unique features of the Taxpayer Relief Act are first, that it allows the deceased landowner, a member of the deceased landowner's family, the executor of the deceased landowner's estate, or the trustee of a trust including the landowner's land, to grant the conservation easement on the landowner's behalf, and second, that the grant of the easement can be made *after* the date of the landowner's

⁴⁴ *See id.*; I.R.C. § 170(b)(1)(B), (D).

⁴⁵ *See* HANDBOOK at 8.

⁴⁶ *See id.* at 9.

⁴⁷ *See id.*

⁴⁸ *See id.*

⁴⁹ *See id.*

⁵⁰ I.R.C. § 2031(c): some qualifying characteristics include the requirement that the property subject to the easement be located in or within twenty-five miles of a metropolitan area, in or within twenty-five miles a national park or wilderness area designated as part of the National Wilderness Preservation System, or in or within ten miles of an area which is an Urban National Forest. I.R.C. § 2031(c)(8)(A). The property must also have been owned by the decedent or a

death.⁵¹

Last, because state property taxes are generally based on a property's market value, placing a conservation easement on property to remove development value may reduce the level of property tax assessment and the landowner's property taxes.⁵² Therefore, by donating a conservation easement, a landowner stands to benefit substantially from income tax, estate tax, and property tax reductions. However, the benefits yielded by a conservation easement vary as much as the landowners who create them, and the landowners who inherit or buy properties encumbered by them.

III. LANDOWNERS

Landowners who grant conservation easements to conservation organizations such as land trusts usually do so for one of several reasons. Landowners may be genuinely motivated to protect their environmentally unique property and be devoted to the promise to perpetually preserve their land in its present state. Or landowners may want to obtain a charitable income tax deduction, reduce the taxable estate burden on their children, and reduce their property taxes. Or the landowner may be motivated by a combination of all of the above.

Certain land-rich, but cash-poor landowners, such as ranchers and farmers, who do not draw substantial incomes needing to be offset by income tax deductions, but who have an extremely valuable and highly taxed piece of property, are attracted to the opportunities provided to reduce estate taxes through conservation easements.⁵³ In particular, these landowners are usually seeking ways to enable their continued way of life and use of property within the next few generations of their family. Faced by enormous estate taxes on appreciated property values, the children of farmers and ranchers are often forced to sell off their extremely valuable property

member of the decedent's family for the three years prior to the decedent's death. *Id.*

⁵¹ I.R.C. § 2031(c)(8)(C), (9).

⁵² *See* HANDBOOK at 9.

just to cover the tax burden at the time of death of their parents.⁵⁴

In contrast, another landowner attracted to the conservation easement is the land-rich and cash-rich landowner who draws a large income and is motivated by the opportunity for a charitable deduction by donating a conservation easement on their valuable property. The CEO of a wealthy corporation who buys as an investment property and fun place to visit, a 5000 acre ranch in Wyoming, or a 250 acre horse farm in upstate New York, can be highly motivated to place a conservation easement on her property to offset her income taxes and reduce her property taxes, while at the same time, protecting her prized property perpetually.

As you can see, the two prospective conservation easement grantors could not be more different, and yet they can both make use of the same conservation easement tool to better their financial situations and effect the same result, perpetual protection of their private property. It has not been land trusts' experience that the first generation landowners, the ones who grant the conservation easements, have presented the biggest problems for the land trust. Rather, it is those landowners that inherit or purchase the encumbered property after the first generation that are proving to dislike the restrictions on their land, and it is not unforeseeable why these

⁵³ *See id.* at 51.

⁵⁴ STEPHEN J. SMALL, PRESERVING FAMILY LANDS: BOOK II: MORE PLANNING STRATEGIES FOR THE FUTURE 2-3 (1997):

Sue Ranchowner owns Diamond Ranch, 500 acres that her late husband's father bought in the late 1940s for \$50 an acre; Diamond Ranch has been owned by the family since that time. All of the family's energy and almost all of the family's cash, has been poured into the ranch. Sue's husband Bob died a few years ago. . . . It has saddened [the family] . . . to see other ranches and farms in the area sold off and subdivided. . . . It gives them a real sense of satisfaction to know that they have been able to keep Diamond Ranch intact. Diamond Ranch is prime ranching and agricultural land on the urban fringe. . . . Because of increasing development pressure in the area Diamond Ranch is now worth \$1,700,000. . . . Sue has an estate value of \$1,850,000. . . . [At the time of Sue's death], it is absolutely clear to Sue that Diamond Ranch will have to be sold to pay the estate tax [of at least \$500,000].

Id.

landowners might be disgruntled.⁵⁵

Conservation easements create long-term relationships between parties, the land trust and the landowner, having a legal interest in the same piece of property, and because of the longevity of the easement agreement, future parties having no involvement in the original transaction are bound to share concurrent interests in that property.⁵⁶ It is both likely and foreseeable that the goals of the future members of the land trust and the future owners of the encumbered property may diverge over time.⁵⁷

First, those families attempting to protect their way of life, be it ranching or farming, for the next generation of their family usually count on their children to follow in their footsteps and continue to ranch or farm, or they would not (should not) grant the conservation easement in the first place.⁵⁸ However, the likelihood that the children's children, or the grantors' grandchildren, will share the same objectives, or the same conservation ethic, as their parents or grandparents is much less predictable.⁵⁹

Second, the benefits of the easement transaction lessen over time; the later owners of the eased property do not reap the immediate benefits of an income tax deduction, nor do they necessarily benefit from the estate tax reduction after several generations.⁶⁰ The original donor of an *inter vivos* gift of a conservation easement will have experienced the rewards and satisfaction of donating a generous gift for a good cause.⁶¹ However, successive generations of landowners may not experience this same personal benefit, and may focus instead on the burdens

⁵⁵ See HANDBOOK at 143-44;

⁵⁶ See *id.*

⁵⁷ See *id.*

⁵⁸ See *id.*

⁵⁹ See *id.* See also Cheever, *supra* note 38, at 1092 (“As the ranch passes down to the next generation or the one after, perceptions of the nature of the transaction may change. . . . [T]he nature of the arrangement will seem more and more like the most despised aspect of government: regulation.”).

⁶⁰ See HANDBOOK at 144.

imposed by the easement and the benefits provided if it did not exist.⁶²

Many conservation easement properties are currently in the hands of the original donors, and the land trust community is without the experience of several generations of use under these easements to predict the future, but the community is armed with the knowledge that both the use of conservation easements and the creation of land trusts are increasing drastically at least some future landowners are likely to resent the easement restrictions placed on their property.⁶³ It is critical, therefore, for land trusts to troubleshoot potential skirmishes with future landowners now.

For those who question the likelihood that future, or even present landowners, will dislike or have a change of heart regarding the encumbrance on their property, look at the example presented by the French and Pickering Creeks Conservation Trust in Pennsylvania, which fought for more than nine years in state court and spent \$100,000 in legal fees to have a non-permitted house built on easement property demolished.⁶⁴ Imagine if another landowner for which the French and Pickering Land Trust held an easement also violated its easement during this time period, or worse, brought an action against the land trust itself.^{64.5} Considering these scenarios challenges the community to create ways to ensure continued viability of land trusts during times

⁶¹ *See id.*

⁶² *See id.* *See also* Cheever, at 1092-93 (“Ranching is now less common in the area and a buyer who intends to ranch might be hard to find. However, if the easement did not exist, the ranch would be worth \$15 million for development.”).

⁶³ *See* HANDBOOK at 144.

⁶⁴ *See* EXCHANGE: THE JOURNAL OF THE LAND TRUST ALLIANCE, Vol. 18, No 1, Winter 1999, p. 18. French and Pickering Creeks Conservation Trust opposed construction of the house from the outset in 1989 when it requested that the county court block its construction. The county court refused, and the land trust appealed to the court of appeals, which ruled that the house violated the conservation easement. The landowner then appealed the decision of the court of appeals to the Pennsylvania Supreme Court, which remanded the case back to county court for a resolution. The land trust eventually won the right to have the house removed, but had to pay for the removal itself and is still seeking reimbursement from the landowner. In the midst of this case, the landowner also attempted to sue the land trust in federal court. *See id.*

^{64.5} Consider also that new data reveals that over 100 easement violations have been reported by

of enforcement and legal defense actions of landowners, in anticipation of the stark reality and likelihood of such actions.

When aiming to protect land trust conservation easement holders from financial devastation resulting from multiple enforcement actions or defense of easement actions, the goal must be to identify and utilize mechanisms to transfer risk away from the land trust. Although many conservation easements provide for the use of dispute resolution tools such as mediation and arbitration before resorting to legal action, conservation easement holders must also be prepared for the possibility of bringing and defending lawsuits stemming from the conservation easements they hold.

This article proposes mechanisms to ensure adequate protection for individual land trusts and the land trust community as a whole when defending and enforcing conservation easements, based on the evaluation of possible risk management strategies. The inquiry here begins with potential solutions for individual land trusts and graduates to an examination of solutions for the land trust community as a whole.

IV. SOLUTIONS FOR THE INDIVIDUAL LAND TRUST

A. Insurance Solutions for the Individual Land Trust

The most obvious method of transferring risk from the individual land trust is through insurance. However, providing recommendations in the area of insurance can be difficult due to the variation in insurance laws from state to state. What follows is an overview of general insurance solutions that makes reference to specific examples of state law.

1. Status Quo: D&O and CGL Policies

The first step in the individual land trust's risk-management inquiry is for the individual land trust to look inward at its own insurance policies and examine the current scope of coverage

land trusts alone as having occurred. *See LTA CENSUS supra* note 2.

provided by existing Commercial General Liability (CGL) and/or Director and Officer Liability (D&O) insurance policies. This assumes, of course, that the land trust has one or both of the CGL and D&O coverage provided by its own insurance carrier or through the Land Trust Alliance's "Conserve-a-Nation" insurance program.⁶⁵ If a land trust is not yet insured, the trust should consider that land trust directors and volunteers engage in a variety of agreements and decisions that foreseeably expose them to liability, including: land purchases, conservation easements, land exchanges, bargain-sales for conservation easements, money management, fundraising, money investment, loans, and consulting payments.⁶⁶ However, land trusts are also vulnerable to less obvious liability, such as that resulting from bodily injury, property damage, personal injury, poor business judgment, breach of duty, interference with another's business, and discrimination.⁶⁷ For these reasons, insurance is necessary for every land trust that intends to protect its assets.⁶⁸

Individuals can file lawsuits against land trusts for damage or injury caused by the land trust's alleged negligence or "wrongful acts,"⁶⁹ and an allegedly injured party can sue the person

⁶⁵ If the land trust does not have insurance coverage, the author encourages the land trust to begin researching the availability and benefits of such policies. For more information, see *Is D and O Insurance Really Necessary?* LAND TRUST NEWS, Spring 1996, Vol.1, No. 1, at 1 ("D & O needs to be considered a fundamental operating expense of every land trust"). The Land Trust Alliance has found that one of the "major tangible needs of land trusts across the country is low-cost general liability and related insurance coverage" and as such, has worked together with Franey, Parr and Muha, Inc. with Chubb Group of Insurance Companies as an underwriter, to provide the "Conserve-a-Nation" insurance program to land trusts and other land trust organizations. LTA INSURANCE PROGRAM, LAND TRUST ALLIANCE (1999). Over 400 land conservation organizations currently use this insurance, which includes a Commercial Package Policy and an Umbrella Policy, including CGL coverage, and a Volunteer Accident Policy. D&O Liability insurance is offered as optional additional insurance. LTA INSURANCE PROGRAM, LAND TRUST ALLIANCE (1999).

⁶⁶ THE STANDARDS AND PRACTICES GUIDEBOOK: AN OPERATING MANUAL FOR LAND TRUSTS, LAND TRUST ALLIANCE 6-43 (1993) (*hereinafter*, STANDARDS AND PRACTICES).

⁶⁷ *See id.* at 6-48, 6-49.

⁶⁸ *See id.* at 6-37, 6-47.

⁶⁹ Negligence is defined as the failure to use the care of a reasonably prudent and careful person under similar circumstances, or the doing of some act which as person of ordinary prudence

responsible for the injury, such as the land trust employee or any person acting on behalf of the land trust, paid or unpaid, as well as the land trust itself, for carelessly selecting or supervising that person.⁷⁰ Because the individual has the right to hold a land trust accountable for its allegedly negligent acts, it is foreseeable that a landowner seeking to extricate his or her land from the encumbrance of a conservation easement may allege negligence on the part of the land trust as a means to attack, invalidate, and “break” the conservation easement contract.⁷¹

Because land trust assets are at risk, including the conservation easement itself, and a defending land trust incurs the costs of defense of an easement or against claims of negligence related to an easement whether or not the land trust was negligent or responsible for the alleged injury, land trusts should determine whether their existing insurance coverage includes defense of easements or negligence tied to easements. CGL and D&O policies provide the most promising avenues for potential coverage of land trusts in defense of negligent acts associated with conservation easements.

would not have done under similar circumstances, or the failure to do what a person of ordinary prudence would have done under similar circumstances. BLACK’S LAW DICTIONARY 1032 (1990). “Wrongful Act” is a term of art used by insurance companies and is defined by each policy. An example from a Chubb policy states:

A Wrongful Act means any error, misstatement or misleading statement, act or omission, or neglect or breach of duty committed, attempted or allegedly committed or attempted by any insured individually or otherwise, in the discharge of his duties to the Association, or any matter claimed against him solely by reason of his serving in such capacity. All such casually connected errors, statements, acts, omissions, neglects, or breaches of duty or other such matters committed or attempted by, allegedly committed or attempted by or claimed against one or more of the insureds shall be deemed interrelated Wrongful Acts.

Chubb D&O Liability Insurance Policy (on file with the author). *See* discussion *infra* Part III.

⁷⁰ PAMELA J. RYPKEMA, NONPROFITS’ ESSENTIAL HANDBOOK ON INSURANCE, (Nonprofit Risk Center) (1996)(*Hereinafter* ESSENTIAL HANDBOOK).

⁷¹ *See* Cheever, at 1093: (At this point, [the landowner] may decide . . . to cast the dice, venturing a significant sum in litigation fees in an attempt to “break” the easement in the hope of recouping a much greater sum by selling or developing the unburdened ranch. Assume the die is cast, [the landowner] returns to her lawyer and, suddenly, many of the elements which made the original transaction such a happy marriage . . . now may aid in the frustration of the public goal). *See*

CGL policies provide the broadest coverage, usually requiring an insurance carrier to “defend any ‘suit’ seeking damages,”⁷² and, therefore, may protect a land trust and its paid staff⁷³ against many lawsuits filed by landowner clients and the general public.⁷⁴ Such lawsuits could include allegations against the land trust of bodily injury, personal injury, or property damage, because the land trust has a duty of reasonable care to manage its property and its actions so as not to injure others.⁷⁵ Bodily injury could result from a “slip and fall” on the land trust’s property, food poisoning from a meal served by the land trust, or even an intoxicated guest to whom a land trust employee or volunteer served alcohol at a fundraiser.⁷⁶ Personal injury could include a land trust’s libel, slander, invasion of privacy, and interference with the business of another a member of the general public.⁷⁷ Damage to property may result from vandalism, fire, flood, or rockslides attributed to, or occurring on, the land trust’s property.⁷⁸

In the context of a conservation easement, a landowner may point the finger at the land trust holding a conservation easement on his or her property and allege negligence on the part of the land trust in its monitoring or enforcement of the easement. Negligence related to a conservation easement may include claims that a land trust failed to monitor the subject property,

discussion *supra* at Part III.

⁷² Daniel J. Callahan & Kathleen Dunham, *PRPs Can Avoid Some Pollution Exclusion Barriers: Savvy PRPs Manage CGL Coverage*, THE NATIONAL LAW JOURNAL, Jan. 25, 1999, at C3.

⁷³ See ESSENTIAL HANDBOOK, *supra* note 70, at 18. Generally, volunteers are not covered by standard CGL policies, although CGLs do cover the land trust for its liability for claims arising from its volunteers’ activities. *See id.* Even if the volunteers, including volunteer staff and board members, are not covered by the CGL policy, such individuals may have coverage in place under their personal homeowner’s, renter’s, or umbrella insurance policies. *See id.* The land trust may also specifically request that coverage be provided for volunteers under the CGL policy as the volunteers are acting as “agents” for the land trust. *See id.* The land trust could also obtain separate coverage through Volunteer Liability Insurance for volunteers only. *See id.*

⁷⁴ *See id.*

⁷⁵ *See id.*

⁷⁶ *See id.*

⁷⁷ *See id.*

⁷⁸ *See id.* at 17.

or failed in aspects of due diligence relating to the conservation easement.⁷⁹

Nonprofit Association Liability, or Director and Officer Liability Insurance (D&O) coverage is supplemental to the CGL insurance and affords protection against liability claims for “wrongful acts” and poor business decisions of the directors, officers, employees, or the organization itself.⁸⁰ Wrongful acts typically include actual or alleged error, misleading statements, and neglect or breach of duty as defined and narrowed by a list of limitations and exclusions.⁸¹

Generally, a D&O policy covers claims arising from governance and management issues such as wrongful termination, waste or ill-advised use of charitable assets, political or partisan activities, failure to insure, failure to prevent misappropriation of funds, and errors in newsletters or publications.⁸² Nonprofit directors’ and officers’ liability arises out of state law fiduciary standards of care and loyalty ranging from the duty not to steal from the organization, to avoiding conduct that could be viewed as a conflict of interest⁸³

In the context a conservation easement, a landowner might allege that the land trust was political, or partisan, or made up of directors and officers who manipulated the conservation easement tool for their own personal and financial gain, ignored their fiduciary duties, and used a private land use control to use control to achieve private ends.⁸⁴

Whether a land trust is covered to defend a conservation easement attack such as those

⁷⁹ Cheever, at 1097-1098.

⁸⁰ See ESSENTIAL HANDBOOK, *supra* note 70, at 20. Sometimes these policies only protect individual directors and officers, and sometimes they extend coverage to the nonprofit entity and its employees. See *id.* at 21. Volunteer board members may already be covered personally or under an Outside-Directorship Policy for volunteer board activities with charitable organizations. See *id.*

⁸¹ See *id.*

⁸² See *id.*

⁸³ Wayne A. Wolff, *Personal Liability of Nonprofit Directors and Officers*, THE BACK FORTY, Vol. 2, No. 9, May/June (1992).

⁸⁴ Cheever, at 1095. Such allegations would also raise a whole host of private inurement

described above hinges on the scope and language of the D&O and CGL policies themselves, specifically, on the definitions of “insured” and “wrongful act.”⁸⁵ “Insured” may be defined in a variety of ways, but some typical language includes:

The association/organization and any natural person who has been, now is or shall become a duly elected director or trustee, a duly elected or appointed officer, an employee, or committee member, whether or not they are salaried, and any other person acting on behalf of the association/organization or at the specific direction of an officer or board of directors of the association/organization.⁸⁶

Typical “Wrongful Act” language includes:

A Wrongful Act means any error, misstatement or misleading statement, act or omission, or neglect or breach of duty committed, attempted or allegedly committed or attempted by any insured individually or otherwise, in the discharge of his duties to the Association, or any matter claimed against him solely by reason of his serving in such capacity. All such casually connected errors, statements, acts, omissions, neglects, or breaches of duty or other such matters committed or attempted by, allegedly committed or attempted by or claimed against one or more of the insureds shall be deemed interrelated Wrongful Acts.⁸⁷

The broader the definitions, the more likely a land trust may be covered in defending a conservation easement.⁸⁸ To identify the scope of their D&O and CGL policy coverage, land trusts should raise the following questions with their insurance carriers:

- Who is insured under the policy--the directors, officers, committee members, volunteers, the organization itself, and or any affiliates or subsidiaries?
- If key risks are excluded from coverage, can coverage be added or is there a specialized insurance policy which might cover such exposure?
- Does the policy protect against liability at the land trust’s every location, and/or on its different properties?

questions.

⁸⁵ Letter from John L. Dana, Vice President, O’Gorman and Young, Inc., to the author (November 4, 1998)(on file with the author).

⁸⁶ Chubb D&O Liability Insurance Policy, *supra* note 69; LTA INSURANCE *supra* note 65.

⁸⁷ Chubb D&O Liability Insurance Policy, *supra* note 69.

⁸⁸ Telephone Interview with John L. Dana, Vice President of O’Gorman & Young, Inc., (Oct.

- What invokes coverage: the occurrence of an accident or event (occurrence coverage: suit may occur years or decades after the incident giving rise to the claim) or a claim filed seeking compensation (claims-made coverage: the wrongful act and the claim must be made in the same policy period)?
- Is the land trust entitled to a defense when a claim is filed, or must it finance the litigation, resolve the claim, and seek reimbursement from the insurer?
- Can the land trust seek reimbursement from the insurer?
- Can the land trust select its own defense counsel, or must it defer to the insurer's choice or own attorneys?
- Are defense costs and attorney fees included within the limit of liability under the policy, or are they in addition to the policy limits?⁸⁹

If it appears through conversations with the insurance carrier that the land trust may be covered for liability stemming from poor diligence of conservation easements or other negligence stemming from the conservation easement, the land trust should identify whether it has claims-made or occurrence coverage.⁹⁰

Claims-made coverage applies only to those actions and claims made within the policy year.⁹¹ For instance, if a land trust fails to inspect an easement property and the landowner is trying to break the easement and files a claim that same year, the action, or here inaction, occurred in the same year and would probably be covered. However, if the landowner sues the land trust two or three years after the allegedly negligent action, that claim would not be covered.

Occurrence coverage, by contrast, applies to the occurrence of negligence by the land trust itself, *no matter when the claim is made*, and often costs much, much more due to its

1998).

⁸⁹ See ESSENTIAL HANDBOOK, *supra* note 70, at 19, 21.

⁹⁰ See *id.* at 21.

broader coverage.⁹² For instance, if a landowner were to allege an injury stemming from an action of the land trust that took place ten years prior to the discovery of the injury, such as the development of a disease related to an asbestos dump on a land trust property, the land trust would still be insured for any negligence under its occurrence coverage.

In addition, if it appears that the land trust is in fact insured for its defense of easements, the land trust should determine who would represent the land trust in any action: the insurance company's attorneys, or attorneys of the land trust's choosing, and who has the authority to settle claims: the insurance company or the land trust.⁹³ One can anticipate why it might be beneficial to the land trust to retain some authority in its own representation to recommend attorneys with expertise in the field of conservation law, and also to prevent premature and potentially damaging settlements.⁹⁴

Unfortunately, because D&O and CGL coverage applies primarily to the negligent acts of the land trust, actions by the land trust to *enforce* an easement are not likely to be covered by D&O and CGL policies. A land trust should inquire as to whether it would be covered for enforcement actions, and if it is not, the land trust should ask if it is possible to receive such coverage. And, land trusts should continue to examine other possibilities for coverage of their potential defense and enforcement actions, such as the possibility of self-insuring.

2. Self-Insurance for the Individual Land Trust

Because it is foreseeable that typical insurance policies such as D&O and CGL coverage will not apply to enforcement actions, and may not even cover defense actions, a land trust may

⁹¹ *See id.*

⁹² *See id.*

⁹³ *See id.* at 19, 21.

⁹⁴ For instance, if an insurance carrier wanted to resolve a claim against the land trust involving a conservation easement without any aid from the land trust, the insurance company's attorneys might unwittingly agree to a settlement that negatively impacts the conservation values of the subject property, such as permitting building in an ecologically sensitive area, or in a wildlife

consider the possibility of providing its own insurance, or self-insuring. The responsibility of enforcing the terms of a conservation easement falls on the land trust, and the land trust may have a small fraction of the financial resources available to a landowner willing to spend these resources in litigation against the land trust.⁹⁵ Furthermore, in order for land trusts to function as nonprofit organizations that can accept and defend tax-deductible conservation easements, they *must* have the resources to enforce the restrictions they place on land.⁹⁶ Therefore, a land trust without broad insurance coverage should find ways to generate and store funds in anticipation of both enforcement and legal defense actions. These anticipated costs can be folded into the land trust's management of its stewardship funds, or they may be offset by third party involvement in defense and enforcement actions.

a. Stewardship Funds: Fiscal Solicitation, Conservation, and Co-Holding Easements

Before a land trust endeavors to accept a conservation easement, it must consider the financial implications of the stewardship, enforcement, and defense of easements.⁹⁷ Self-insurance, also known as self-retention or contingency insurance, is a program of insurance financed entirely by an individual organization itself, as opposed to the organization's purchase of insurance from a commercial carrier.⁹⁸ Through self-insurance, a land trust can designate

corridor, in exchange for the landowner's agreement to drop the lawsuit against the land trust.

⁹⁵ Cheever, *supra* note 38, at 1100. Cheever states:

How can a land trust with an annual budget of \$10,000 a year and no paid staff members hope to defend its rights created by a conservation easement from an attack by a landowner who may have tens of millions of dollars to gain by developing the servient land? The scales tilt even more when the land trust [finds] itself challenged by more than one such landowner.

⁹⁶ Dale Bonar, *Growing Pains and Stewardship Funds: The Northwest Experience*, EXCHANGE: THE JOURNAL OF THE LAND TRUST ALLIANCE, Vol. 16, No 4., Fall 1997, p. 8. It is a sign of a maturing organization to recognize the importance of having sufficient resources to adequately steward the property. *See id.*

⁹⁷ *See* STANDARDS AND PRACTICES, *supra* note 66, at 14-4. Stewardship must anticipate the land trust's obligation to monitor the terms of the easement of which it is the holder, and requires a commitment of time, money, and other resources. *See id.*

⁹⁸ *Insurance News Network* (visited December, 1998) <<http://www.insure.com/glossary/terms>

funds for stewardship, and for the risk management of liabilities arising out defending or enforcing a conservation easement and the performance of land trust duties by any trustee, employee, director, or volunteer of the organization.

Regulation of self-insurance or self-retention of funds varies from state to state, but in Colorado, land trusts are not regulated for self-insuring.⁹⁹ The option of self-insuring is appealing not only because it is unregulated, but also because it can be crafted by the land trust to meet its individual needs and can grow out of the management of stewardship funds.¹⁰⁰

Stewardship funds and funds to self-insure can be solicited in many ways: a trust could solicit funds per easement from the grantor in anticipation of such actions, or could raise funds for insurance, or could carve out part of the trust's endowment to protect easements.¹⁰¹ Such funds could also be designated or dedicated in many ways: a single fund could be developed to cover both monitoring and legal defense costs of all the land trust's easements, or a trust might

[/selfinsure.html](#)>.

⁹⁹ COLO. REV. STAT. § 24-30-1512 (1998); Risk Management Fund and Self-Insured Property Fund Not Subject to Insurance Laws:

The setting aside of reserves for self-insurance purposes in the risk management fund . . . [or] in the self-insured property fund . . . shall not be construed to be creating an insurance company, nor shall the risk management fund of the self-insured property fund otherwise be subject to the provisions of the laws of this state regulating insurance or insurance companies.

Id. However, land trusts in Colorado cannot work *together* to provide self-insurance without being regulated as an “inter-insurance exchange,” a highly regulated form of insurance. COLO. REV. STAT. §§ 10-31-101 to 10-14-705 (1998). Therefore, in states like Colorado, trusts are better off insuring themselves, and only themselves, and avoiding regulation.

¹⁰⁰ *See id.*

¹⁰¹ *See* STANDARDS AND PRACTICES *supra* note 66, at 14-5, 14-6. The Land Trust Alliance recommends that a land trust set up a stewardship fund that is managed separately from the trust's operating budget and that is created by depositing an appropriate amount of money into the fund each time an easement is acquired. *See id.* at 14-5. Since a land trust usually solicits funds from the donor of a conservation easement for monitoring and enforcement of that easement, the trust could use these funds as to defend as well. *See id.* at 14-6. However, determining the “appropriate amount” can be a difficult task. The few land trusts throughout the country that have set policies to determine the size of the estimated stewardship funding necessary to support their activities do not report a calculated basis that took into account the actual costs of monitoring or defending the conservation easement properties. *See Bonar supra*

create separate stewardship and legal defense funds, or stewardship and defense funds may be developed individually for each easement.¹⁰²

At the same time a land trust develops a system to acquire and designate funds for its own protection and the protection of its easements, it should also create a system for how such funds should continue to grow and be accessed when needed. For instance, the land trust could determine that the funds taken for monitoring conservation easements should be invested aggressively in mutual funds, or placed in an interest-bearing bank account.

Through the solicitation, dedication, and growing of such funds, a land trust might be able to amass a secure amount of money for the stewardship, enforcement, and defense of its easements. Unfortunately, self-insuring remains a challenge for most land trusts because of the difficulty of raising, designating, and setting aside funds in a timely manner. Land trusts may already be attempting to self-insure against defense and enforcement actions while at the same time providing for stewardship costs, but they either underestimate the amount of funds needed to engage in the enforcement or defense of an easement, or are unable to acquire the necessary sums. Those trusts with substantial endowments, or those that solicit large amounts for monitoring of easements at the time of donation, are the best suited for a system of self-insurance. Vermont Land Trust, for instance, solicits stewardship grant awards from easement donors on a sliding scale of \$2000 to \$7400 per project, and receives \$5000 to \$7000 when purchasing a conservation easement.¹⁰³ However, with a current stewardship fund of \$1.6 million and over 600 easements, the average amount available per easement is less than \$3000. Vermont Land Trust attributes this low per-easement figure to the failure to solicit funds during early projects, waiver of donation of funds, and installment payment plans, among other

note 96, at 9.

¹⁰² *See id.* at 10.

¹⁰³ Preston Bristow, *The Vermont Land Trust Approach*, EXCHANGE: THE JOURNAL OF THE LAND

factors.¹⁰⁴

This substantial stewardship endowment of over a million dollars is invested not by the land trust itself, but by the Vermont Community Foundation, a donor-restricted trust which is a separate creation of the land trust, in an attempt to remove the funds from the reach of creditors and third-party attacks.¹⁰⁵ In addition to its stewardship funds, Vermont Land Trust has also dedicated \$300,000 to a separate interest-bearing account in anticipation of legal defense and enforcement actions.¹⁰⁶

Aside from this accumulation of funds, Vermont Land Trust possesses yet another layer of security against financial devastation linked to enforcement and defense of their conservation easements in what is perhaps the best form of self-insurance, free access to lawyers. Because the trust co-holds approximately 300 of its 600 easements with the State of Vermont, the trust is entitled to legal assistance and state resources from the Vermont Attorney General's Office in anticipation of enforcement actions.¹⁰⁷ Vermont is not the only state to provide legal assistance to land trusts and access to private funding and assistance of a state's attorney general must also be considered a form of self-insurance available to land trusts.

b. Support Systems: The Attorney General, In-House Counsel, and Third Party Assistance

Another layer of self-insurance is added to a land trust when the state in which it

TRUST ALLIANCE, Vol. 16, No 4., Fall 1997, p. 11.

¹⁰⁴ See *id.* Bristow also attributes the low per easement funds saved to reductions for multiple easement conveyances and reductions for easements held on public land. See also Letter from Leslie Ratley-Beach, Project Counsel, Vermont Land Trust, to the author (Sept. 14, 1998) (on file with the author). Ratley-Beach estimates that the annual payments out of the stewardship fund meet about forty-five percent of the trust's budgeted expenses and the trust hopes to increase that to one-hundred percent sometime in the future.

¹⁰⁵ See Ratley-Beach Letter, *supra* note 104. For more information on the creation of a separate entity to handle funds, see discussion *infra* Part IV, B., 3, and Part V, B., 1.

¹⁰⁶ See *id.*

¹⁰⁷ See *id.* Co-holding is a practice involving more than one donee for the conservation easement which reflects a shared responsibility and liability by virtue of doubling the parties involved in the transaction. Whether or not the A.G. also provides assistance in a land trust's defense actions

conducts business requires government approval before an conservation easement is accepted, and in return, offers legal assistance in from the Attorney General. Massachusetts is one such state.¹⁰⁸

Conservation easements proposed in Massachusetts must have local and state approval before being accepted by a land trust there.¹⁰⁹ State involvement in the acquisition of conservation easements and the easement process enables land trusts such as the Trustees of Reservations, the Nantucket Land Council, and the Vermont Land Trust to rely on the attorneys from the state's Attorney General's Office to enforce and possibly even defend their conservation easements.¹¹⁰

Such ready access to attorneys strongly supports the notion that attorney fees may not be an issue for land trusts trying to self-insure by virtue of the fact that the state attorney general could conceivably step in and litigate a case on a land trust's behalf.¹¹¹ Massachusetts prepared to step into its first enforcement action in 1997, when the Attorney General wrote to landowners violating their conservation easement and indicated the A.G.'s intent to become involved in the case.¹¹² The landowners settled out of court shortly thereafter and it is thought that the perceived threat of government involvement in the enforcement action was enough to encourage these

has not yet been tested or queried in Vermont.

¹⁰⁸ *Gleanings*, EXCHANGE: THE JOURNAL OF THE LAND TRUST ALLIANCE, Vol. 16, No 4., Fall 1997, p. 17.

¹⁰⁹ *See id.*

¹¹⁰ Like Vermont, the ability and willingness of the Attorney General to step forward and help defend and land trust or conservation easement has not yet been tested in Massachusetts, but the government's involvement in the conservation easement approval process lends strong support to the government's involvement during defense and enforcement actions: "The fact that we must have government approval is a solid reason for the attorney general to act . . . because [the attorney general's involvement] indicated that [the attorney general] was ready to intervene in the case, I am certain that we saved a lot of money in legal fees" when the case settled just weeks after the attorney general wrote to the landowners. *Id.* Statement of Lyn White, chair of the Natural Resources Trust in Easton, Massachusetts, the land trust holding the easement being enforced. *See id.*

¹¹¹ *See id.*

landowners to resolve the issue out of court.¹¹³

The chair of the land trust involved in the Massachusetts action urges other land trusts and states to examine more government involvement in the conservation easement field: “I hope this causes other land trusts to evaluate how important government approval of conservation [easements] is . . . It’s an extra layer of defense.”¹¹⁴ Vermont Land Trust, as part of its legal defense mechanism, relies upon the State Attorney General for assistance with the 300 easements the State of Vermont co-holds with the Vermont Land Trust.¹¹⁵ The creation of a government right and duty to defend and enforce conservation easements on behalf of land trusts may be the most effective way to match a landowner with limitless resources attempting to break an easement, and may even create a voice for the public value of the easement.¹¹⁶ However, such government involvement may scare landowners who view it as intrusive, overreaching, and threatening to what is touted as a private transaction between a landowner and a nonprofit. To keep the transaction private, and devoid of government involvement, the larger nonprofits have developed their own form of self-insurance.

The Nature Conservancy, Land and Water Fund, EarthLaw, National Wildlife Federation, and Trust for Preservation of Historic Places, and other large nonprofits, have a unique form of self-insurance. Rather than setting aside funds for defense and enforcement actions, or relying on assistance in the form of attorney general litigators through co-holding easements or government approval, these nonprofits ensure that they will be able to defend and enforce actions without the accumulation of funds or outside assistance. These entities rely on their own in-house attorneys, whose sole purpose is to protect the nonprofit and its goals. Those nonprofits

¹¹² *See id.*

¹¹³ *See id.*

¹¹⁴ *See id.*

¹¹⁵ *See* Ratley-Beach Letter, *supra* note 104.

¹¹⁶ *See* Cheever *supra* note 38, at 1101-1102.

with attorneys on their staffs worry little about legal fees, but only paying their in-house attorneys' salaries. For most land trusts, the ability to maintain full-time attorneys as staff members is not feasible, even though many may have attorneys on their boards.^{116.5} However, the older, more well-established and well-endowed land trusts, such as Vermont Land Trust, do have their own attorneys on staff, so the possibility of a land trust's eventually possessing its own, in-house counsel is not completely unforeseeable. Until that time, land trusts must continue to search for ways to protect themselves, even if it means turning to third-party beneficiaries.

Private parties, including individuals, corporations, and foundations, who are seeking opportunities to make charitable donations in order to offset income taxation, or have it as part of their mission to give grants, may be attracted to the possibility of providing funding for a land trust's security against legal defense and enforcement actions. When researching these issues for this article, the author was approached by one private organization interested in the opportunity to make donations or set up another foundation for the benefit of the land trust community's legal defense which would be out of reach of landowners and potential litigants.¹¹⁷ The potential for involvement by wealthy donors, large foundations, or grant-making organizations should not be overlooked during a land trust's mission for conservation. Such opportunities may only surface but once in a lifetime, and could provide a blanket of security to smother concerns about defense and enforcement actions.

Unfortunately, the newer, perhaps smaller, land trusts without large stewardship funds, that work in states that do not provide attorney general assistance, that cannot afford in-house

^{116.5} Board members who happen to be attorneys should not be confused with staff attorneys, nor should boards with attorneys be lulled into a false sense of security. While attorney-board members may be able to provide the occasional pro bono assistance, board member attorneys may not have the proper training, nor be ethically permitted by canons and codes of ethical responsibility, to provide specific enforcement and defense legal assistance. Therefore, it is important to remember that merely having an attorney on a land trust board does not automatically resolve all the land trust's legal problems.

counsel, and that have not had the fortuity of meeting that once in a lifetime extremely generous donor, probably do not have the luxury of being able to self-insure, and must continue to examine other ways to provide for their defense and enforcement of conservation easements. One such way may be to seek out insurance that is specifically tailored to meet their needs.

3. Surplus Lines and the Individual Land Trust

Surplus lines insurance is coverage placed with an approved, but nonadmitted insurance provider, or those insurers not having a certificate of authority to transact business in the state.¹¹⁸ Probably because this type of insurance is not regulated very rigorously, these insurance companies tend to insure more unique situations and scenarios, that for reasons of expertise or capacity cannot be insured by local companies.¹¹⁹

Lloyd's of London is probably the most familiar surplus lines provider due to its willingness to cover the largest, as well as the most technically challenging, risks.¹²⁰ Lloyd's describes itself as a market comprising 155 underwriting syndicates transacting a wide variety of classes of business and a vast array of risks, including: a professional football team signing a star player and protecting themselves with disability insurance; a law firm wishing to protect its business against the losses related to the death of its senior partner by securing "keyman" insurance; a snowmobile rental company wanting to insure its vehicles; and, a racehorse breeder insuring against the infertility of a prize stallion.¹²¹ Lloyd's also insures a wide variety of smaller risks for individuals, such as: jewelers and their stock, bankers and their security, art collectors and their collections, and bar owners against actions of customers who have had too

¹¹⁷ Letter on file with author.

¹¹⁸ COLO. STAT. REV. § 10-5-101.2 (1998); COLO. CODE REGS. § 2-4-1 (1998);

¹¹⁹ Lloyd's America, <<http://www.lloydsamerica.com.html>>.

¹²⁰ *See id.*

¹²¹ *See id.*

much to drink.¹²²

Because Lloyd's underwriters, and other surplus lines insurers, pride themselves on their ability to respond to the needs of their clients through innovative solutions, there is a potential in the surplus lines market for a land trust to obtain coverage to protect against enforcement and defense actions relating to its conservation easements.¹²³ Just as it is important to research present coverage under D&O and CGL policies, it may also be helpful for land trusts to examine better avenues for insurance coverage, by contacting a surplus lines insurer and asking the same questions of the surplus lines carrier that must be asked of the D&O and CGL provider.¹²⁴ The potential to mold a specific policy to a very specific risk may turn out to be an appealing, though possibly expensive, option for a land trust. Another non-traditional, but popular tool in the insurance industry that is worthwhile to examine is the potential for surety coverage.

4. Suretyship for the Individual Land Trust

Suretyship is a specialized line of insurance that is created whenever one party guarantees performance of an obligation of another party.¹²⁵ There are three parts to a surety agreement: the principal, or the party that undertakes the obligation, the surety, or the guaranty, that the obligation will be performed, and the obligee, or the party who receives the benefit of the surety bond.¹²⁶ A surety bond is a written instrument that usually provides for monetary compensation in case the principal fails to perform acts as promised.¹²⁷

Suretyship is like more common forms of insurance because both insurance and surety transfer risk, are regulated by state insurance commissioners, and provide for financial loss.¹²⁸

¹²² *See id.*

¹²³ *See id.*

¹²⁴ *See discussion supra* Part IV, A.,1.

¹²⁵ *What is Suretyship?* <<http://www.surety.org/surwhati.html>>.

¹²⁶ *See id.*

¹²⁷ *See id.*

¹²⁸ *See id.*

Surety differs from insurance, however, because instead of transferring risk to the insurance company, the risk remains with the principal and the protection of the bond is for the obligee.¹²⁹ Also, in the traditional insurance setting, the insurance company takes into consideration that a certain amount of the premium for the policy will be paid out in losses.¹³⁰ Through suretyship, the premiums are “service fees” charged for the use of the surety company’s financial backing and guarantee.¹³¹ Further, in underwriting traditional insurance products, the goal is to spread the risk, where as in suretyship, surety professionals view their underwriting as a form of credit, so the emphasis is on prequalification and selection.¹³²

Most large property and casualty insurance companies have surety departments, and some companies focus solely on surety.¹³³ In either case, the company writing the surety bond must be licensed by the insurance division of the state in which it is doing business.¹³⁴

Surety is an expensive alternative to insurance, but it provides an interesting opportunity to protect a land trust’s investment in a conservation easement. If no insurance company will adequately address the needs of the land trust or land trust community through traditional forms of insurance, it is worth investigating whether a surety company would consider creating a bond for each individual easement a land trust holds, or a bond for the land trust itself. The bond would guarantee, or back the continued performance of the conservation easement, the performance of the land trust, and perhaps even of the landowner, depending on who purchased the bond. Should the land trust need to defend an easement, or enforce an easement, the surety bond would be lurking in the shadows to help pay for, or guarantee, that those costs would be covered.

¹²⁹ *See id.*

¹³⁰ *See id.*

¹³¹ *See id.*

¹³² *See id.*

¹³³ *See id.*

Surety may seem an unlikely mechanism to transfer risk for a land trust because surety bonds are the preferred method of guaranteeing the performance of financial obligations of others in contract and commercial situations largely associated with building and construction contracts.¹³⁵ However, more and more corporations, public officials, and individuals are turning to surety bonds to protect their interests.¹³⁶

When considering whether or not to underwrite a risk, a surety company will generally examine the capacity of the applicant to perform the obligation behind the bond, the capital, or financial condition of the applicant, and the likelihood of the applicant to perform the obligation.¹³⁷ In terms of a conservation easement, this may mean examination of the trust's reputation and past history in monitoring its easements, in order to project the likelihood that the land trust will perform its end of the conservation easement bargain. If the surety company believes the land trust is a good risk to ensure, there is the potential for the surety to back up that easement in perpetuity.

Like individual insurance coverage, if a surety bond could be designed to protect an easement, that backing might not only encourage due diligence on the part of the land trust in its monitoring and enforcement, but also, guaranty coverage for the land trust if a landowner attempts to break an easement. A land trust interested in this type of coverage should inquire further with a knowledgeable and nontraditional surety provider.

¹³⁴ *See id.*

¹³⁵ *See id.*

¹³⁶ *See id.*

¹³⁷ *See id.*

5. Captive Insurance and the Individual Land Trust

Land trusts that have the resources to self-insure, purchase surplus lines, or purchase surety bonds, may instead want to consider providing their own insurance through a captive insurance company. A captive insurance company is an insurance company created by a parent entity for the purpose of providing insurance and reinsurance for the risks, hazards, and liabilities of the parent.¹³⁸ A captive insurance company may also issue surety coverage, or provide loans for its parent.¹³⁹

Captives are becoming an increasingly popular alternative to conventional insurance in the United States due to a more favorable regulatory climate.¹⁴⁰ It used to be that United States entities wanting to create their own captives had to turn to offshore, or to foreign insurance companies for assistance.¹⁴¹ But in 1972, Colorado passed the first law enabling domestic captives, and today thirteen states in this country now permit domestic captive insurance.¹⁴²

Furthermore, the category of entities eligible to form captives is also broadening; parents now include groups and associations such as individual and groups of land trusts.¹⁴³ With captive insurance, a land trust could create its own insurance company and formally provide itself insurance, while at the same time, shift the risk of liability away from itself and to a third party (the captive insurer).¹⁴⁴ Captives do not work completely alone, however; they are almost always paired with a “fronting insurer” that issues a primary policy to underwrite, calculate the premium, and handle state regulatory compliance, since this form of insurance is subject to all of

¹³⁸ David Jacoby & Judith S. Roth, *Captives Represent Attractive Alternatives*, THE NATIONAL LAW JOURNAL, Jan. 25, 1999, at C1.

¹³⁹ *See id.*

¹⁴⁰ *See id.*

¹⁴¹ *See id.*

¹⁴² *See id.* Colorado, Delaware, Georgia, Hawaii, Illinois, Maine, New York, Rhode Island, South Dakota, Tennessee, Vermont, U.S. Virgin Islands, and Virginia all permit domestic captive insurance. *See id.* at C11.

¹⁴³ *See id.* at C1. Group captives are discussed *supra* Part V, A., 4.

the state regulations of any other insurance company.¹⁴⁵ And, if a land trust did not possess the capital or wherewithal to create its own captive company, it could choose to “rent” the services of a captive from an existing provider.¹⁴⁶

Like self-insurance, the captive insurance company provides coverage solely for its parent corporation, and no other entity.¹⁴⁷ Such a company requires independent management and is strictly governed by statutes, regulations, and a state’s division of insurance.¹⁴⁸

By way of example, applicants for a certificate of authority for a captive insurance company in Colorado file a detailed plan of operation, feasibility study, and any other information deemed relevant to the Commissioner of Insurance to ascertain whether the proposed company will be able to meet its policy obligations.¹⁴⁹ No captive insurance company in Colorado can be approved without a total capital and surplus of less than \$500,000.¹⁵⁰

Once approved and issued a certificate of authority, the business of each captive insurance company within Colorado must be managed by a board of directors or other governing body of not less than three persons which must provide the insurance commissioner with a report of the company’s financial condition at the end of each fiscal year.¹⁵¹ However, the captive insurance company is not subject to any restrictions on its investments whatsoever, except that the insurance commissioner may prohibit or limit investment if it is not made within the

¹⁴⁴ *See id.*

¹⁴⁵ *Id.* A “fronting insurer” is a United States licensed insurer that issues the primary policy for the captive. *Id.*

¹⁴⁶ *See id.* at C9.

¹⁴⁷ *See id.* at C1.

¹⁴⁸ *See id.* See for example, Colorado’s statutes at COLO. REV. STAT. §§ 10-6-101 *et seq.* (1998); regulations at, 3 COLO. CODE REGS. § 702-2; amended regs. § 2-3-1 *et seq.* (1998); and the Division of Insurance, <<http://www.dora.state.co.us/insurance>>.

¹⁴⁹ COLO. REV. STAT. § 10-6-107 (1998).

¹⁵⁰ COLO. REV. STAT. § 10-6-116 (1998).

¹⁵¹ COLO. REV. STAT. § 10-6-108 (1998).

approved plan of operation.¹⁵²

Finally, captive insurance companies in Colorado pay an annual tax on the gross amount of all premiums collected, on policies or contracts covering property or risks in and out of the state, which is at least \$5000.¹⁵³

While all this regulation seems burdensome, the main attraction of a land trust owning its own insurance company is that the trust can insure whatever liability it wants, including possibly enforcement and defense actions. Captives not only have a “high profile regarding unusual risks,” such as defense and enforcement of conservation easements, they give the parent more control over their claims management than traditional insurance companies, allow the parent to invest its funds any way it chooses, and may even turn a profit through investment income and underwriting.¹⁵⁴ However, most of these same attractions are inherent in the self-insurance model, without the burden of state regulation.

Aside from the obvious drawbacks of going into the insurance business, and the difficulty of maintaining a surplus of no less than \$500,000, captive insurance companies present another potential problem for implementation by the average land trust. While an organization that is exempt from federal taxation may establish a separate fund or entity that is itself an exempt organization, the tax code states and tax courts uphold that an otherwise tax-exempt organization will lose or be denied tax exemption if a substantial part of its activities consists of “the provision of commercial-type insurance.”¹⁵⁵

The goal of captive insurance companies is to provide just that, commercial-type

¹⁵² COLO. REV. STAT. § 10-6-121 (1998).

¹⁵³ COLO. REV. STAT. § 10-6-128 (1998).

¹⁵⁴ See Jacoby & Roth *supra* note 138, at C9.

¹⁵⁵ I.R.C. § 509(a); I.R.C. § 501(m); *Paratransit Ins. Corp. v. Comm’r*, 102 T.C. 745 (1994); BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 523 (1998) (The activity of providing commercial-type insurance is treated as the conduct of an unrelated trade or business and its income is taxed as income from taxable insurance companies).

insurance coverage for its parent company, the land trust. Therefore, any land trust exempt from federal taxation under 501(c)(3) wishing to create a captive insurance program would probably have to meet the tax code test head on, and attempt to prove that providing commercial-type insurance is not a substantial part of the captive's activities--that is, if they want that entity to remain tax-exempt.

Although it may seem an insurmountable task to prove that a captive insurance company is not providing commercial-type insurance for a tax-exempt land trust, the tax courts' rulings on tax-exempt status have been somewhat supplanted by statutory law providing tax-exempt status for charitable risk pools.¹⁵⁶ Further, the tax code provides that a separate tax-exempt entity that is an association can become involved in a variety of insurance programs by managing a program of insurance for its members, or by operating an insurance fund to cover the liability of its members.¹⁵⁷ By analogy, if not direct application, this provision of insurance by the association parallels that of a captive insurance company for its parent land trust.

If a land trust has the funds and perseverance to create a captive insurance company, or even rent from a captive provider, it must consider how to implement this type of insurance without jeopardizing the trust's and captive's tax-exempt status.

B. Solutions for the Individual, Tax-Exempt, Nonprofit Land Trust

1. The Individual 501(c)(3) Land Trust with a Separate Entity

The income tax code provides that an organization already exempt from federal taxation may establish a separate fund or like entity that is itself an exempt organization.¹⁵⁸ A land trust

¹⁵⁶ See discussion *supra* at Part V, B., 1. I.R.C. 501(n)(1)(B). See also HOPKINS at 526: "The rule that a charitable organization cannot be exempt from tax if a substantial part of its activities consists of providing commercial-type insurance is not applicable to charitable risk pools" and "[t]his body of law overrides otherwise applicable caselaw denying tax-exempt status to eligible charitable risk pools." HOPKINS at 238.

¹⁵⁷ Rev. Rul. 66-151; HOPKINS at 690.

¹⁵⁸ I.R.C. § 509(a); HOPKINS at 52.

may therefore establish a separate entity that helps the land trust or trusts in some way, and is also tax-exempt. An organization that functions as an integral part of the exempt activities of a related entity or entities may itself be tax-exempt.¹⁵⁹ Tax exemption of this nature is known as derivative or vicarious exemption and permits exemption on the basis that the subsidiary organization's activities are an integral part of the activities of the parent organization.¹⁶⁰

An entity seeking tax exemption as an integral part of another entity or entities cannot primarily be engaged in an activity that would generate “more than insubstantial unrelated business income for the other entity.”¹⁶¹ However, barring that restriction, this opportunity to create another entity for the purpose of guiding and funding defense and enforcement actions presents an interesting possibility for individual land trusts.

For instance, Vermont Land Trust created a separate foundation to oversee its due diligence and monitoring. Colorado Open Lands, too has a separate foundation affiliated with its statewide land trust. These separate entities provide protection of funds and resources from the reach of potential litigants and while they operate as a form of self-insurance, these entities are distinct from self-insurance because they separate and insulate the land trust assets.

As long as it does not generate *unrelated* income, the separate entity would be in compliance with federal regulations. Because any income generated by the separate entity in relation to providing resources for defense and enforcement of easements for a land trust is likely to be considered related to the land trust, these types of entities should be compliant.

For instance, a separate entity could be created with a decisionmaking apparatus to oversee the potential cases arising from enforcement and defense of conservation easements. Such an entity could create a board comprised of lawyers and land trust directors involved in the

¹⁵⁹ Reg. § 502-1(b); HOPKINS at 552.

¹⁶⁰ See HOPKINS at 552.

¹⁶¹ Reg. § 1.502-1(b); HOPKINS at 552.

land trust community to evaluate membership issues and fundraising for legal actions.

Such security, or protection, would be distinct from any insurance reliance, where an insurance company underwriting liability might be able to force a land trust to use the insurance company's own attorneys, or even more troubling, force or accept a settlement of a claim without any land trust involvement at all. Here, the autonomy of a separate nonprofit entity to choose its own battles, its own attorneys, and control the potential lawsuit, might prove to be its most appealing aspect.

Another appealing aspect of a separate nonprofit is that such an entity would provide continuing support, guidance, and legal advice in a preventative manner *before* situations reached the stage of a lawsuit. The separate entity could assist a land trust to understand its role and responsibilities with regard to due diligence of conservation easements throughout the monitoring process. Such assistance may be the key to avoiding *ever* having to defend or enforce an easement.

Compared to the prospect of obtaining or creating some form of insurance or surety for defense, the option of creating a separate nonprofit to protect easements seems fairly feasible, perhaps only because creating a nonprofit is a familiar process. The process of creating a separate entity is not dissimilar from creating a separate law firm, an option which may have benefits of its own for the individual land trust.

2. The Individual 501(c)(3) Land Trust with a Public Interest Law Firm

A public interest law firm is a separate entity that provides a charitable service that is of benefit to the community as a whole--legal representation for important but under-represented citizen interests.¹⁶² Litigation is considered to be in representation of a broad public interest if it

¹⁶² Rev. Rul. 75-74; HOPKINS at 163.

is designed to present a position on behalf of the public at large on matters of public interest.¹⁶³

A public interest law firm that provides representation in cases it selects as having significant public interest and for which representation by traditional law firms is not economically feasible is considered to be operated exclusively for charitable purposes and therefore is tax exempt under I.R.C. § 501(c)(3).¹⁶⁴

Guidelines for public interest law firms strictly regulate these entities: such a firm may accept fees for services rendered in accordance with specific IRS procedures; may not have a program of disruption of the judicial system, illegal activity, or violation of the applicable canons of ethics; must file with its annual information return a description of cases litigated and the rationale for the determination that they would benefit the public; must have policies and programs that are the responsibility of a board or committee representative of the public interest not controlled by its employees or those who litigate on its behalf; may not operate so as to create identification or confusion with a particular private law firm; and may not have an arrangement to provide, directly or indirectly, a deduction for the cost of litigation which is for the private benefit of the donor.¹⁶⁵

IRS procedures for the acceptance of fees by these firms forbid a firm from soliciting fees from clients, permit acceptance of fees where paid by opposing parties under court or agency award, require the firm to use awarded fees to defray normal operating expenses, and require the firm to file with its annual information return a report of all fees sought and recovered.¹⁶⁶ A public interest law firm will lose its tax exemption if it enters into a fee-sharing arrangement with a private lawyer who keeps a portion of a court-awarded fee that exceeds the amount paid by the

¹⁶³ Reg. § 1.501(c)(3)-1(f); Rev. Proc. 92-59.

¹⁶⁴ Rev. Rul. 75-76, 1975-1 C.B. 154, amplified by Rev. Proc. 92-59, 1992-2 C.B. 411.

¹⁶⁵ Rev. Proc. 71-39, 1971-1, C.B. 575; HOPKINS at 163-64.

¹⁶⁶ Rev. Proc. 75-13, 1975-1 C.B. 662; HOPKINS at 164.

firm to the lawyer for services.¹⁶⁷

Organizations such as the Earthjustice Legal Defense Fund and the Environmental Defense Fund are entities institutionally separate from the other organizations that utilize their legal services in the pursuit of public interest legal justice. Creation of a separate entity to provide for legal assistance would guarantee a land trust a way to defray legal costs and create an epicenter for legal knowledge of and experience with defending and enforcing conservation easements. What such an endeavor might cost is unknown, since it basically requires the creation of a law firm of sorts.

The most important facets of creating a public interest law firm would be in the provision of lawyers and legal assistance for every need of the land trust, including assisting in mediations and arbitrations before conflicts reach the stage of lawsuits,^{167.5} in warehousing legal knowledge in one place, and hopefully, in giving advice early and consistently throughout the easement process, so that the land trust might ultimately avoid legal problems altogether.

The best approach to the public interest law firm might be to create a separate entity to oversee the land trust community's legal issues, such as that described previously, and when it becomes apparent that there is a great need and demand for it, turn that entity into a public interest law firm, or allow it to authorize the creation of a public interest law firm. That way, the separate entity could start out on a small scale, with perhaps just one lawyer to begin with, warehousing information and giving assistance. As the land trust's need for more assistance, or dependence on such assistance grows, so to could the public interest law firm grow.

Paying one person or even just a few person's salaries might eventually save hundreds of

¹⁶⁷ Rev. Rul. 75-75, 1975, C.B. 154; HOPKINS at 164.

^{167.5} Because many conservation easements include provisions for resolution of conflict through mediation and arbitration, lawyers with experience in these methods of dispute resolution would be able to provide invaluable assistance early on to prevent a lawsuit, or to attempt to resolve the conflict before either party opts for a lawsuit.

thousands of dollars otherwise paid to insurance companies or surety agencies when there might not ever even be any claims against the land trust, or an independent law firm when there is. Having just one individual or firm available to help with legal advice might make the public interest law firm all worthwhile. In fact, having such a firm may be more useful to the community as a whole, than to just an individual trust, and will be explored more fully under the community solutions, Part V, B., 2.

3. The Individual 501(c)(3) Land Trust with a Charitable Risk Pool

A qualified charitable risk pool is a separate entity that is organized and operated solely to pool insurable risks of its members (other than medical malpractice risks) and to provide information to its members with respect to loss control and risk management.¹⁶⁸ No profit or other benefit may be accorded to any member of the organization creating the charitable risk pool other than through the provision of insurance to its members.¹⁶⁹

The pool is required to be organized as a nonprofit organization under state law authorizing risk pooling for charitable organizations, required to be exempt from state income tax, and required to obtain at least \$1 million in start-up capital from member charitable organizations.¹⁷⁰ Start-up capital means any capital contributed to, and any program-related investments made in the risk pool before the pool commences operations.¹⁷¹

The pool must be controlled by a board of directors elected by its members, and must provide three elements in its organizational documents indicating that members must be tax-exempt charitable organizations at all times, that if a member loses its tax-exempt status it immediately notify the organization, and that no insurance coverage apply to a member after the

¹⁶⁸ I.R.C. § 501(n)(2)(A); HOPKINS at 238.

¹⁶⁹ H.R. Rep. No. 737, 104th Cong. 2d Sess. 189 (1996); HOPKINS at 238.

¹⁷⁰ I.R.C. § 501(n)(4)(A); HOPKINS at 238.

¹⁷¹ I.R.C. § 501(n)(4)(A); HOPKINS at n.68.

determination that the member no longer qualifies as a tax-exempt organization.¹⁷²

The rule that a charitable organization cannot be exempt from taxation if a substantial part of its activities consists of providing commercial-type insurance is not applicable to charitable risk pools.¹⁷³ The charitable risk pool body of statutory law overrides otherwise applicable caselaw denying tax-exempt status to eligible charitable risk pools.¹⁷⁴ Because this category of tax exemption is based on qualification as a charitable organization, a charitable risk pool must meet all of the other requirements to maintain its tax-exempt status.¹⁷⁵

Creation of a charitable risk pool for land trusts could be an individual effort. For instance, an individual land trust could create its own risk pool to provide for its own insurance for defense and enforcement of easements. Of course, once created, the risk pool basically becomes a form of self-insurance, and though not governed as such, would be fraught with all the same concerns of any insurance company trying to protect a pool of funds.

However, not being governed as an insurance company would presumably provide the land trust, pool, and board of directors more flexibility in crafting their coverage within the pool. Unfortunately, the start-up capital required for this pool is extraordinary, at \$1million, and this cost largely eliminates this option for the individual land trust.

Even if the qualifying costs were not so high, state law governing this type pooling mechanism may prevent it in some states, as discussed below under the self-assessment option.¹⁷⁶ Because of the start-up costs and potential state law conflicts, the charitable risk pool option should only be considered as a possibility for the land trust community as a whole.

V. SOLUTIONS FOR THE LAND TRUST COMMUNITY

¹⁷² I.R.C. §§ 501(n)(4)(B); 501(n)(2)(C); 501(n)(C)(3); HOPKINS at 238-39.

¹⁷³ I.R.C. § 501(n)(1)(B); HOPKINS at 239.

¹⁷⁴ See HOPKINS at 238, 526.

¹⁷⁵ See *id.* at 239.

¹⁷⁶ See discussion *infra* Part V, A., 2.

Although there is a ground swell of support for community solutions in the land trust community, there is also a profound sense of hesitancy to engage in what is perceived to be a tying of one's fate to that of another.¹⁷⁷ Taking this reluctance into account, the models presented for the land trust community attempt to provide broad-based solutions without directly linking the fates of land trusts to one another.

A. Insurance Solutions for the Land Trust Community

These insurance solutions seek to link land trusts only through the same insurance legal defense mechanisms for each individual land trust. The fate of each land trust defending or enforcing a conservation easement would be independent from the rest of the community, and would not involve the rest of the community, except that each trust would share a safety net of insurance coverage.

1. Interinsurance Exchange within the Land Trust Community

Instead of trying to provide risk management for itself independently, a land trust may consider working in conjunction with other land trusts to provide insurance coverage. Reciprocal, or interinsurance, exchange means any aggregation of persons, known as "subscribers," who, under a common name, engage in the business of exchanging contracts of insurance through an attorney-in-fact having the authority to obligate the subscribers on contracts of insurance made with other subscribers.¹⁷⁸

By way of example, under Colorado state law, individuals, partnerships, and corporations, as subscribers, are authorized to exchange reciprocal or interinsurance contracts with each other, or with individuals, partnerships, and corporations of other states and countries,

¹⁷⁷ See Land Trust List Serve Dialogue, responses to questions posed by author (September 29, 1989-October 12, 1998)(on file with the author).

¹⁷⁸ COLO. REV. STAT. § 10-13-101 *et seq.* (1998); COLO. CODE REGS. § 2-6-1 (1998).

to provide indemnity among themselves from any loss which may be insured against.¹⁷⁹ In addition to the rights, powers, and franchises specified in its articles of incorporation, any corporation organized under the laws of the state has full power to exchange insurance contracts with subscribers in a reciprocal exchange.¹⁸⁰

However, to qualify for the authority to transact in the insurance business, every interinsurance exchange (composed of the member land trust subscribers) must possess and maintain an unencumbered surplus in an amount of not less than \$300,000.¹⁸¹ In addition, subscribers, through their attorneys, attorneys-in-fact, agents, or other representatives, must deposit and maintain on deposit with the commission of insurance moneys or securities of the value of \$50,000 as security for the performance of all such contracts issued by the subscribers.¹⁸²

An attorney, attorney-in-fact, agent, or other representative duly authorized to act for the subscribers must execute the contracts for insurance.¹⁸³ The authority of the attorney to manage the affairs of the reciprocal derives from the subscribers' agreement executed by each subscriber providing for the subscribers' advisory committee composed of at least nine individuals elected by the subscribers.¹⁸⁴

The attorney, under the direction of the subscribers' advisory committee, files with the commissioner: a declaration of the name or title of the office at which the subscribers propose to exchange indemnity contracts; a description of the kind of insurance to be effected or exchanged; a copy of the form of policy contract and the form of power of attorney; an application for indemnity upon at least one hundred separate risks, aggregating not less than one and one-half

¹⁷⁹ COLO. REV. STAT. § 10-13-101.

¹⁸⁰ COLO. REV. STAT. § 10-13-109.

¹⁸¹ COLO. REV. STAT. § 10-13-106(2).

¹⁸² COLO. REV. STAT. § 10-13-101.

¹⁸³ COLO. REV. STAT. § 10-13-102.

million dollars; and a financial statement.¹⁸⁵

Once certified by the commissioner to do business as an interinsurance exchange, all assets of the reciprocal and its subscribers can then be invested in accordance with the investment guidelines approved by the subscribers' advisory committee.¹⁸⁶

The most interesting feature of the interinsurance exchange program is that the exchange *itself* may, in its own name, purchase, take, receive, lease, or otherwise acquire, own, hold, improve, use, and otherwise deal in, and with real property, or have an interest in real property, wherever situated, and may sell, convey, assign, encumber, mortgage, pledge, lease, exchange, transfer, and otherwise dispose of all or any part of such real property interest.¹⁸⁷ It is conceivable then, that the interinsurance exchange *itself* could ultimately place conservation easements on property, and be fully insured for the enforcement and liability actions which may result therefrom.

In addition to the ability to deal in conservation easements, the exchange, and its member subsidiaries, could presumably craft whatever sort of risk protection it wanted in the individual contracts for exchange, including potentially, insurance for easement enforcement and defense of easements actions.

Whether the exchange would qualify as an exempt, nonprofit organization is the pivotal question, as with the captive insurance.¹⁸⁸ As previously noted under the captive insurance section, federal tax courts have stated that an otherwise tax-exempt organization will lose or be denied tax exemption if a substantial part of its activities consists of the provision of

¹⁸⁴ COLO. REV. STAT. § 10-13-102.

¹⁸⁵ COLO. REV. STAT. § 10-13-103.

¹⁸⁶ COLO. REV. STAT. § 10-13-109.5.

¹⁸⁷ COLO. REV. STAT. § 10-13-109.5.

¹⁸⁸ See discussion *supra* Part IV, B., 5.

commercial-type insurance.¹⁸⁹ Like captive insurance, the goal of an interinsurance exchange is to provide commercial-type insurance coverage for its subscriber-land trusts.¹⁹⁰ Therefore, land trusts exempt from federal taxation under 501(c)(3) wishing to create an interinsurance exchange would probably also have to prove that providing commercial-type insurance is not a substantial part of the interinsurance exchange. However, it is important to remember that the tax courts' rulings on tax-exempt status have been overshadowed by statutory law providing tax-exempt status for charitable risk pools, a concept to be discussed in Part V, B., 1. In both the captive and interinsurance exchange, it may prove worthwhile to solicit a treasury ruling from the IRS to determine the status of such organization.

Also, as with the captive insurance model, entering into the interinsurance business requires a fair amount of start-up capital: at least \$300,000 at the outset and then an additional \$50,000. for the reciprocal contracts.¹⁹¹ However, when keeping in mind that the older, more-established land trusts, such as Vermont Land Trust, have already set aside that same amount for a litigation fund, the benefits of insuring each other's land trusts, and in essence, each other's easements, may far outweigh any start-up costs.¹⁹²

But what, exactly, does reciprocal insuring mean, and how does it work? Basically, each land trust in the exchange would be underwriting the liabilities of the other land trusts. The exchange is not a pooling mechanism; it is the creation of an entity separate from the land trusts to insure not only one land trust's liability, but every member land trust's liability, while at the same time, investing securities, and managing the assets of the member land trusts. The members of the exchange could presumably dictate what could be covered, and how, and this power might turn the interinsurance exchange into one of the best arrows in the land trust

¹⁸⁹ *See id.*

¹⁹⁰ *See id.*

¹⁹¹ COLO. REV. STAT. § 10-13-101, 106.

community's quiver for providing security against financial decimation resulting from defense and enforcement of conservation easements.

2. The Land Trust Community Use of a Self-Assessment Pool

Instead of providing reciprocal insurance for member land trusts as in the interinsurance exchange, should land trusts pool resources together in a self-insurance fund to provide security against financial difficulties resulting from legal actions? Possibly, but that sort of pooling is currently prevented by law in some states.

In Colorado, for instance, only *public entities* may cooperate with one another to form a self-insurance or self-assessment pool to provide insurance coverage.¹⁹³ While such pools are not construed to be insurance companies, or regulated as insurance companies, under existing laws, such pools are only allowed to be created by public entities including counties, municipalities, school districts, and "any other type of district or authority organized pursuant to law."¹⁹⁴

Under Colorado Revised Statute § 8-44-204, public entities may cooperate with one another to provide insurance coverage for compensation, benefits, and liability coverage.¹⁹⁵ These public entity pools and the members thereof may combine and commingle all funds appropriated by the members and received by the pool for liability and property insurance, as well as for other purposes of the pool.¹⁹⁶ Such a pool may invest in securities, or in subordinated debentures in addition to liability coverage.¹⁹⁷

Every self-insurance pool must submit a plan of operation describing facilities to manage the pool, administration of claims and servicing, description of the duties and responsibility of

¹⁹² See discussion *supra* Part IV, A., 2., b.

¹⁹³ COLO. REV. STAT. § 8-44-204 *et seq.* (1998); COLO. CODE REGS. § 2-2-1 (1998).

¹⁹⁴ COLO. REV. STAT. § 8-44-204(2).

¹⁹⁵ COLO. REV. STAT. § 8-44-204(3).

¹⁹⁶ COLO. REV. STAT. § 24-10-115.5(7).

any management provider, types of coverage, a feasibility study articulating future loss experience, and a list of proposed members.¹⁹⁸ The members of the pool must elect or appoint a board of directors and officers to oversee the management of the pooled fund.¹⁹⁹ The pool must apply for and receive a certificate of authority from the insurance commissioner.²⁰⁰

Like the interinsurance exchange, this pooling mechanism might provide an opportunity for land trusts to work together, to pool resources to enable them to provide for their own, and others legal costs for liability and enforcement stemming from monitoring and defending conservation easements. The programs are distinct from one another, however, because the pooling mechanism is not necessarily an insurance program, per se, as the interinsurance program certainly is. Rather, the pooled fund can operate as a safety net of funds to provide for *whatever* needs of members of the pool arise, assuming of course, that the members of the pool are public entities.²⁰¹

Right now, this mechanism of funding for risk is not feasible for land trust organizations in Colorado and other states with similar legislation, because they do not appear to qualify under the definition of public entities, unless they can be construed to be “any other type of district or authority.”²⁰² However, if the definition of public entity is broadened by the Colorado legislature, or if the legislation is amended in some other way to provide for the inclusion of land trusts in the pooling mechanism, land trusts in Colorado and other states might be able to create their own pooled funds for the enforcement or defense of conservation easements.

Unless and until such revisions or formal interpretations are made, land trusts in Colorado are prohibited by law to engage in any type of pooling of funds. Because pooling is prevented,

¹⁹⁷ COLO. REV. STAT. § 8-44-204(9)(b); 24-10-115.5(8)(b).

¹⁹⁸ COLO. REV. STAT. § 8-44-204(5); § 24-10.115.5(4).

¹⁹⁹ COLO. REV. STAT. § 8-44-204.

²⁰⁰ COLO. REV. STAT. § 8-44-204(5).

²⁰¹ COLO. REV. STAT. § 8-44-204(2), (10).

to date, land trusts in Colorado will be wise to continue to consider other, individual and joint insurance coverage options.

3. The Land Trust Community as an Insurance Purchasing Group

There is no mystery to this option. The assumption is that market share dictates demand and response within that market. If land trusts band together as a unit and approach the insurance industry as a buying and purchasing *group*, they will have much more leverage to dictate the type of coverage they want and then shop for the best deal. Joining together to approach the insurance industry and comparing coverage plans between different carriers means that the land trust community might be able to dictate custom coverage on a national scale.

One of the drawbacks of land trusts' current D&O and/or CGL coverage is that it may not cover land trusts' enforcement and defense of conservation easement actions. By contrast, a group of organizations with great buying power could probably dictate the structure and scope of any insurance coverage that those organizations interested in receiving the coverage sought. Enforcement and defense of conservation easements should be on the top of the list for such coverage.

Already, the Chubb group is underwriting insurance coverage in the form of D&O and CGL policies for land trusts.²⁰³ This coverage is being marketed through the "Conserve-a-Nation" program.²⁰⁴ An individual involved in both the insurance industry and the land trust community has been proposing a calculated market approach to the insurance industry for over two years now. He, and others who support the market approach, urge the land trust community

²⁰² COLO. REV. STAT. § 8-44-204(1).

²⁰³ See discussion *supra* at Part IV, A., 1.

²⁰⁴ See discussion *supra* at Part IV, A., 1. Telephone Interview with John L. Dana, Vice President of O'Gorman & Young, Inc., (Oct. 1998). See also Letter from Andy Zepp, Vice President for Program, Land Trust Alliance, to the land trust list-serve in response to author's inquiry (October 9, 1998)(on file with the author).

to band together in pursuit of the insurance coverage that they need.²⁰⁵ One potential proponent of such a program would be the national Land Trust Alliance. To date, L.T.A. has researched such a role and has yet to take action citing the complexity and variation of the state insurance laws and regulations.²⁰⁶ Although many think that L.T.A. should be the proponent of any national movement to obtain insurance, it is important to remember that many different kinds of organizations aside from land trusts protect property through the use of conservation easements, and a better proponent may be a completely new entity to unite all holders of easements.

Aside from comprehending varying state coverage issues, the most challenging aspect of this proposal would be coordination and unification of the land trust community in its quest for risk management. Arriving at the proper coverage for over 1200 land trusts before making a unified demand of the insurance sector may very well be an impossible task. However, keeping in mind that other industries receive insurance coverage on the national level even though regulations may vary from state to state,²⁰⁷ the thought of the land trust community at least

²⁰⁵ *See id.*

²⁰⁶ Letter from Andy Zepp, Vice President for Program, Land Trust Alliance, to the land trust list-serve in response to author's inquiry (October 9, 1998)(on file with the author):

Regarding recent discussions on an easement insurance program; an insurance agent who was also a land trust board member did investigate the feasibility of a national easement insurance program last year, but I don't believe he got anywhere. LTA did investigate this a few years ago, and found that there are a number of challenges inherent with an easement insurance program, particularly at the national level. Dealing with 48 different easement enabling statutes, verification of adequate monitoring, and determining when litigation is appropriate are just a few of the issues that would present a challenge at the national level.

...

At this time, LTA has no plans to create a national easement insurance program.

Id.

²⁰⁷ The Nature Conservancy's insurance coverage, for instance, is covered nationally by a national insurance company, although that coverage varies from state to state according to state statutes and regulations. It would be the burden of the prospective insurance carrier to reconcile the differences from state to state, not the burden of the land trust community. Other examples of national industries receiving insurance coverage from national carriers that varies from state to state include ski companies owning several ski areas in different states, individual automobile

expressing an interest in broad-based coverage as a potential market may not be so far-fetched.

After all, the benefits yielded to the insurance industry, and ultimately to the land trust community, by just proposing and presenting the need for coverage for defense and enforcement of easements far outweighs the difficulties of attempting to coordinate all the land trusts under all the different laws in the country. Further, it is the responsibility of the insurer, not the insured, to ensure compliance with different state statutes and regulations. In fact, just opening a dialogue about the potential for national coverage would be helpful if for nothing else but to identify the pitfalls and advantages of such potential coverage.

Bringing the insurance industry to the table to discuss coverage for land trusts is one way to start examining the issues surrounding such broad-based coverage, including differences in state regulation. Trying to mobilize the land trust community behind a hypothetical insurance policy is a futile effort, but as there already at least a groundswell of interest in the provision of such coverage,²⁰⁸ and relying on the “if you build it they will come” approach, if the land trust community presents a market for this coverage, it is more than likely that the insurance industry will respond, and provide its own suggested models.

Further, if the land trust community presents an interest in exploring the possibilities of national coverage, and several insurance companies find this to be an appealing market, one can be sure that these companies would identify and resolve the discrepancies between different state regulations in order to ensure proper coverage.

The first step is for the land trust community to present an interest in knowing more about its possible coverage, and such an expression of interest should probably come from a representative of the land trust community, although it does not have to. There is a genuine

insurance, and any franchise or retail company, such as Wal-Mart, that occurs in many different states, and still receives coverage from the same carrier on a national basis.

²⁰⁸ See Land Trust List Serve Dialogue, responses to questions posed by author (September 29,

interest and curiosity by parts of the land trust community in pursuing this potential insurance,²⁰⁹ but the interest needs to be taken a step beyond affirmation within the community, and be offered to the insurance industry itself. Of course, if no one approaches the insurance industry, or if the community does approach the industry and the industry is apathetic, the land trust community still be encouraged that it has other community insurance solutions, such as captive insurance.

4. Captive Insurance for the Land Trust Community

In a group captive, all the rules of the individual captive apply,²¹⁰ except that the insureds are members of an association or are entities facing similar risks.²¹¹ Groups wanting captive insurance but that do not want to own the insurance company created, or that do not have the capital to contribute to form the insurance company, may instead rent-a-captive.²¹² A rent-a-captive leases an existing insurance company to an association or group so that group can avoid forming its own captive.²¹³

Groups can also create their own captive, as opposed to renting. Because of the tax aspects, a group captive endeavor might be of greatest benefit to nonprofit entities such as land trusts.²¹⁴ Entities in a group under a captive insurance plan exchange insurance contracts through an attorney-in-fact, who acts as the manager of the insurance.²¹⁵ Risk is therefore transferred among the group members who benefit from the income and share in the losses based on their individual contributions to the captive.²¹⁶

Captives are popular among groups needing coverage for unusual risks, for which land

1989-October 12, 1998)(on file with the author).

²⁰⁹ See Land Trust List Serve Dialogue, responses to questions posed by author (September 29, 1989-October 12, 1998)(on file with the author).

²¹⁰ See discussion *supra* at Part III, A., 2.a.

²¹¹ See Jacoby & Roth, *supra* note 138, at C9.

²¹² See *id.*

²¹³ See *id.*

²¹⁴ See *id.* See discussion *infra* Part V, B., 3 for a discussion of the tax aspects of captives.

²¹⁵ See *id.*

trusts and the defense and enforcement of conservation easements might qualify.²¹⁷ Football teams, clergy, doctors, corporations, and airlines have all formed captive insurance groups to manage their sometimes nontraditional risks²¹⁸ Therefore, as a community or group, it is probably worthwhile for the land trust community to look into.

B. Solutions for the Tax-Exempt, Nonprofit Land Trust Community

Not surprisingly, the same models that apply to the individual land trust also apply to the land trust community as a whole, most of which is made up of nonprofit, tax-exempt 501(c)(3) organizations. These options, like those in the individual land trust section, stem from the land trust community's largely, though not entirely, 501(c)(3) status.

1. The 501(c)(3) Land Trust Community Creation of a Separate Entity

As previously discussed, the tax code permits a tax-exempt organization to establish a separate entity or fund that is also tax-exempt.²¹⁹ A group of tax-exempt land trusts could therefore presumably establish a separate entity to assist the land trusts in some way, and it too, would be tax-exempt.

Although a separate entity seeking tax exemption as an integral part of another entity cannot be engaged primarily in an activity that would generate “more than insubstantial unrelated business income for the other entity,” the land trust community could still take the opportunity to create another entity for the purpose of guiding and funding defense and enforcement actions since these actions would be an integral part of, and directly related to, the

²¹⁶ *See id.*

²¹⁷ *See id.*

²¹⁸ *See id.*

²¹⁹ I.R.C. § 509(a); HOPKINS at 52: An organization that functions as an integral part of the exempt activities of a related entity or entities may itself be tax-exempt. Tax exemption of this nature is known as derivative or vicarious exemption and permits exemption on the basis that the subsidiary organization's activities are an integral part of the activities of the parent organization. Reg. § 502-1(b); HOPKINS at 552.

land trust community.²²⁰

For instance, the land trust community could create a separate entity with the capacity to oversee the potential cases arising from enforcement and defense of conservation easements for many land trusts at once. The land trust community could create a board for the separate entity comprised of land trust directors, lawyers and other conservationists involved in the land trust community. The purpose of the board would be to evaluate membership issues for those wanting to belong to the separate entity, and bringing together resources in anticipation of future legal actions. Each land trust wanting to could pay a premium to belong to, or become a member of this entity, in exchange for the promise of protection by the entity based on a favorable evaluation of the land trust's conservation easements and its management and monitoring policies and practices.

Membership dues collected from member land trusts could then be grown into a much larger resource over time, thereby ensuring the acquisition of good legal assistance. Attorneys working in the conservation field would probably be eager to be involved in defense and enforcement actions for conservation easements, especially if they could recover their fees. The autonomy, security, and guarantee of good legal assistance engendered by such a separate entity and fund distinguishes this opportunity from reliance on a traditional insurance company, which might force a land trust to use the company's attorneys in an easement case, or even more perturbing, might settle a claim without any land trust involvement at all.

Perhaps the most appealing aspect of a separate nonprofit entity created for the land trust community, aside from its obvious flexibility, is that such an entity could provide continuing feedback, guidance, and legal support to the entire community preventatively, *before* situations escalated to the stage of a lawsuit. The separate entity could assist land trusts to understand their

²²⁰ Reg. § 1.502-1(b); HOPKINS at 552.

due diligence and monitoring responsibilities when accepting conservation easements, and throughout the monitoring process. Such assistance from the separate entity could, in fact, prevent the occurrence of a portion of defense and enforcement actions through proper diligence and monitoring.

The community could nominate a board of directors, who then could determine how to govern, accept members, and raise funds. Once the board decides how to run itself and act on behalf of its membership, it can advertise for and accept members to belong to the separate entity. Then the board can start giving advice and helping land trusts in the monitoring and enforcement of their easements.

To take the separate entity model a step further, the land trust community could create a separate entity to provide itself with commercial insurance. Land trusts wanting to create a separate entity to provide insurance could first become themselves an *association* that could then create a separate entity to engage in the tax-exempt related activities of the land trust community.²²¹ Tax-exempt associations provide services to their members in exchange for dues, which are considered to be income related to the activities of the association.²²²

However, where an association actively and regularly manages an insurance program for its members, for a fee, and a substantial portion of its income and expenses are traceable to the provision of insurance, the association's management is regarded as an unrelated taxable business by the IRS.²²³ An association managing an insurance program for its members, or operating a self-insurance fund covering its members' liability will be taxed as engaging in the "unrelated activity" of providing insurance for profit,²²⁴ *unless* perhaps, the provision of

²²¹ See HOPKINS at 689.

²²² Rev. Rul. 74-81, 1974-1 C.B.135; HOPKINS at 687-88.

²²³ Rev. Rul. 66-151; Priv. Ltr. Rul. 7840014; HOPKINS at 691.

²²⁴ See HOPKINS at 689.

insurance is conducted by a separate entity on behalf of a parent association.²²⁵

Therefore, if an association on behalf of its membership created a separate entity, and one of the duties of the separate entity was to manage an insurance program on behalf of the association, this activity should still qualify as tax-exempt.²²⁶ The goal of the association would be the provision of insurance through the separate entity for the benefit of its members.

The option of creating a separate nonprofit to protect land trusts and conservation easements is very appealing, especially with the prospect of creating a separate entity to bring together the leading minds in the state or country to act as the board of directors for that entity. Either through a separate fund and lawyer-providing entity, or an association and a separate insurance providing entity, protection of land trusts and their conservation easements could be achieved.

2. The 501(c)(3) Land Trust Community and a Public Interest Law Firm

As mentioned previously, a public interest law firm is a separate entity that provides a charitable service that is of benefit to the community as a whole--legal representation for important but under-represented citizen interests.²²⁷ Creation of a separate entity to provide for legal assistance would guarantee the land trust community a way to defray legal costs and create an epicenter for legal knowledge of and experience with mediating, arbitrating, defending and enforcing conservation easements.

The land trust community certainly could not go wrong by creating a legal entity in the form of a public interest law firm to protect its interests, both in enforcement and defense of easements. Although it is unclear what such an undertaking might entail or cost, it could be very similar to the start-up costs and efforts of the creation of a separate entity, with the added twist

²²⁵ See HOPKINS at 689.

²²⁶ See HOPKINS at 689.

²²⁷ Rev. Rul. 75-74; HOPKINS at 163.

that the separate entity is a law firm.

The most important facets of creating a public interest law firm are similar to those of a separate entity: the provision of lawyers and legal assistance for every need of the land trust community, warehousing legal knowledge in one place that the community knows of and supports, and hopefully, giving advice early and consistently throughout the easement process, so that land trusts might ultimately avoid legal problems altogether. Also, the public interest firm could engage in alternative dispute resolution mechanisms, such as mediation and arbitration, as is required by some conservation easements. This model is much the same as the separate entity model, except the lawyers are involved from the genesis of the entity.

In fact, the best approach to the public interest law firm might be to create a separate entity to oversee the land trust community's legal issues, and when it becomes apparent that there is a great need and demand for it, turn that entity into a public interest law firm. That way, the separate entity could start out on a small scale, with perhaps just one lawyer to begin with, warehousing information and giving assistance. As the community's need for more assistance, or dependence on such assistance grows, so could the public interest law firm develop and more individuals could be hired, so that the law firm might grow, even just one person at a time.

As previously noted, paying one person or even just a few person's salaries might eventually save hundreds of thousands of dollars otherwise paid to insurance companies or surety agencies when there might not ever even be any claims against the land trust, or to law firms on a case-by-case basis. Having just one individual or firm available to help with legal advice might make the public interest law firm all worthwhile, and turn it into an invaluable asset of the land trust community.

The land trust community is currently struggling just to stay informed of ongoing legal actions and current legal trends and issues. Rather than relying on rumor and speculation, the

public interest law firm could provide guidance to the land trust community to avoid its potentially litigious future, and assist in mediations and arbitrations, with the help of the best legal tools available: preparation, knowledge, and experience.

3. The 501(c)(3) Land Trust Community Creation of a Charitable Risk Pool

As aforementioned, a qualified charitable risk pool is a separate entity that is organized and operated solely to pool insurable risks of its members and to provide information to its members with respect to loss control and risk management.²²⁸ No profit or other benefit may be accorded to any member of the organization creating the charitable risk pool other than through the provision of insurance to its members.²²⁹ The pool must be organized as a nonprofit organization under state law authorizing risk pooling for charitable organizations, must be exempt from state income tax, and must have at least \$1 million in start-up capital from member charitable organizations.²³⁰ Although this start-up capital is virtually unthinkable for an individual land trust to meet, it is not unreasonable to envision over 1200 land trusts working together to contribute to this amount of capital.

Creation of a charitable risk pool for land trusts could be a powerful group effort for the

²²⁸ I.R.C. § 501(n)(2)(A); HOPKINS at 238.

²²⁹ H.R. Rep. No. 737, 104th Cong. 2d Sess. 189 (1996); HOPKINS at 238.

²³⁰ I.R.C. § 501(n)(4)(A); HOPKINS at 238; Start-up capital means any capital contributed to, and any program-related investments made in the risk pool before the pool commences operations. *See id.* Also, the pool must be controlled by a board of directors elected by its members, and must provide three elements in its organizational documents indicating that members must be tax-exempt charitable organizations at all times, that if a member loses its tax-exempt status it immediately notify the organization, and that no insurance coverage apply to a member after the determination that the member no longer qualifies as a tax-exempt organization. I.R.C. §§ 501(n)(4)(B); 501(n)(2)(C); 501(n)(C)(3); HOPKINS at 238-39. The rule that a charitable organization cannot be exempt from taxation if a substantial part of its activities consists of providing commercial-type insurance is not applicable to charitable risk pools. I.R.C. § 501(n)(1)(B); HOPKINS at 239. This body of statutory law overrides otherwise applicable caselaw denying tax-exempt status to eligible charitable risk pools. *See HOPKINS* at 239. Because this category of tax exemption is based on qualification as a charitable organization, a risk pool must satisfy all of the other requirements for achievement of this tax-exempt status. *See id.* at 239.

land trust community. For instance, an individual land trust could create its own risk pool to provide for its own insurance for defense and enforcement of easements, or, all the land trusts in a state, or in the country, could create one charitable risk pool for the protection of all their collective easements.

Of course, once created, the risk pool basically becomes a form of self-insurance, and though not governed as such, comes with all the same concerns of any insurance company trying to protect a pool of funds. However, not being governed as an insurance company would presumably provide the pool members and board of directors more flexibility in crafting their coverage within the pool. Also, membership determinations would have to be made with some standards of acceptability, just as under the separate entity option.

Although the start-up costs of this pool seem extraordinary, and while it is true that if spread out among trusts, they may be achievable, even if they are, the state law governing this type pooling mechanism may still prohibit it in some states, as discussed under the self-assessment model. Since the option of a charitable risk pool was only added to the federal tax statutory law in 1996, it is possible that the comparable state law has not yet been caught up to the federal act. Amending legislation in the relevant states to permit creation of such pools would solve this inadequacy and provide another avenue for land trusts to protect their easements.

The charitable risk pool option, along with the options of a separate entity and a public interest law firm, provides some formidable opportunities for 501(c)(3) land trust community to pool funds or resources, and enforce and defend its conservation easements.

CONCLUSION AND RECOMMENDATIONS

What lies ahead for the individual land trust and the land trust community is largely

unknown, but one certainty is known, that not all future landowners are going to abide by the restrictions placed on their property as set out in their conservation easements. Perpetuity is a long time. Without bolstering the support systems and defense mechanisms of the nonprofit land trust holders of conservation easements in this country, the tie that binds the land trust to the landowner will surely be broken. The models presented in this article are intended to stimulate discussion and invite scrutiny so that the best options for the individual land trust and the land trust community might emerge and rise out of such dialogue to protect the land trusts and the conservation easements they hold.