

GLOSSARY

Ad Valorem - A direct tax calculated “according to value” of property. Ad valorem tax is based on an assigned valuation (market or assessed) of real property and, in certain cases, on a valuation of tangible or intangible personal property. In virtually all jurisdictions, ad valorem tax is a lien on the property enforceable by seizure and sale of the property. An ad valorem tax is normally the one substantial tax that may be raised or lowered by a local governing body without the sanction of superior levels of government (although statutory restrictions such as tax rate limitations may exist on the exercise of this right). Thus, ad valorem taxes often function as the element used by local governments to assure that their budgets remain in balance.¹ (see also **General Obligation Bond**).

Amortization Schedule - A table showing the periodic repayment of an amount of indebtedness, such as a mortgage or bond. This table is often set up to show interest payments in addition to principal repayments.²

Arbitrage - The simultaneous purchase and sale of an asset in order to profit from a difference in the price. It is a trade that profits by exploiting price differences of identical or similar financial instruments, on different markets or in different forms. Arbitrage exists as a result of market inefficiencies; it provides a mechanism to ensure prices do not deviate substantially from fair value for long periods of time.³ Federal income tax laws generally restrict the ability to earn arbitrage in connection with tax-exempt bonds.⁴

Basis - The original cost of an asset to be used to determine the amount of capital gain tax upon its sale. An "adjusted basis" includes improvements, expenses, and damages between the time the original basis (price) is established and transfer (sale) of the asset. "Stepped up basis" means that the original basis of an asset (especially real property) will be stepped up to current value at the time of the death of the owner, and thus reduce capital gain taxes if the beneficiary of the deceased person sells the asset. For example, a property is purchased for \$30,000, and when the owner dies, it is worth \$250,000. When an heir receives the property, he or she can sell it for \$250,000 with no capital gains tax, but if the parent had sold it before his or her death there would have been capital gains on \$220,000.⁵

Bond - A security evidencing the issuer’s obligation to repay a specified principal amount on a date certain (maturity date), together with interest either at a stated rate or according to a formula for determining that rate. Bonds are distinguishable from notes, which usually mature in a much shorter period of time. Bonds may be classified according to, among other characteristics, maturity structure (serial vs. term), source of payment (general obligation vs. revenue), issuer

¹ http://www.msrb.org/msrb1/glossary/view_def.asp?param=ADVALOREMTAX

² http://www.msrb.org/msrb1/glossary/view_def.asp?param=AMORTIZATIONSCHEDULE

³ <http://www.investopedia.com/terms/a/arbitrage.asp>

⁴ http://www.msrb.org/msrb1/glossary/view_def.asp?param=ARBITRAGE

⁵ <http://dictionary.law.com/Default.aspx?selected=42>

(state vs. municipality vs. special district), price (discount vs. premium), rating (rated vs. unrated, or among different categories of ratings) or purpose of financing (transportation vs. health care).⁶

Bond Counsel - An attorney or law firm, typically retained by the issuer, to give a legal opinion that the issuer is authorized to issue proposed municipal securities, the issuer has met all legal requirements necessary for issuance and interest on the proposed securities (if they are intended to be tax-exempt bonds) will be excluded from gross income of the holders thereof for federal income tax purposes and, where applicable, from state and local taxation. Typically, bond counsel may prepare, or review and advise the issuer regarding, authorizing resolutions, trust indentures, official statements, validation proceedings and litigation.⁷

Cash - The value of assets that can be converted into cash immediately, as reported by a company. Usually includes bank accounts and marketable securities, such as government bonds and banker's acceptances. Cash equivalents on balance sheets include securities that mature within 90 days (e.g., notes).⁸

Capital Gain - The difference between the sales price and the original cost (plus improvements) of property. For example, a property is purchased in 1950 for \$20,000 and sold today for \$400,000, which there is a potential of tax on a \$360,000 gain. There are some statutory cushions to ease this blow, such as a one-time \$125,000 deduction from the gain (profit) on sale of real property if the seller is over 55, deferred (temporarily put off) tax if investment property is "exchanged" (profits are invested in other property) under strict rules, making lifetime gifts to children or charity, or buying another home. Another escape is death, which gives the property to heirs at the value on the day of the owner's death without capital gains tax ("stepped up basis").⁹ (see also **Basis** and **Capital Gains Tax**)

Capital Gains Tax - The tax levied on profits from the sale of capital assets (land or a building not purchased or sold in the normal course of business). A long-term capital gain, which is achieved once an asset is held for at least 12 months, is taxed at a maximum rate of 20% (taxpayers in 28% tax bracket) and 10% (taxpayers in 15% tax bracket). Assets held for less than 12 months are taxed at regular income tax levels, and, since January 1, 2000, assets held for at least five years are taxed at 18% and 8%.¹⁰ (see also **Basis** and **Capital Gain**)

Conservation Easement - Easement restricting a landowner to land uses that that are compatible with long-term conservation and environmental values.¹¹ (see also **Easement**)

Coupon - A colloquial term for a bond's interest rate.¹² (see also **Interest (Rate)**, **STRIPS**, and **Zero Coupon Bonds**)

⁶ http://www.msrb.org/msrb1/glossary/view_def.asp?param=BOND

⁷ http://www.msrb.org/msrb1/glossary/view_def.asp?param=BONDCOUNSEL

⁸ <http://www.bloomberg.com/invest/glossary/bfglosc.htm>

⁹ <http://dictionary.law.com/Default.aspx?selected=129>

¹⁰ <http://www.bloomberg.com/invest/glossary/bfglosc.htm>

¹¹ <http://www.epa.gov/OCEPATERMS/CTERMS.HTML>. See http://www.farmlandinfo.org/documents/27762/ACE_1-04.pdf and <http://www.cals.ncsu.edu/wq/lpn/PDFDocuments/uniform.pdf>

¹² http://www.msrb.org/msrb1/glossary/view_def.asp?param=COUPON

Coupon Rate - The annual rate of interest payable on a security expressed as a percentage of the principal amount.¹³

Debt Service - The amount of money necessary to pay interest on outstanding bonds, the principal of maturing bonds and the required contributions to a sinking fund for term bonds. This amount is also known as the "debt service requirement." "Annual debt service" refers to the total principal and interest paid in a calendar year, fiscal year, or bond fiscal year. "Total debt service" refers to the total principal and interest paid throughout the life of a bond issue. "Average annual debt service" refers to the average debt service payable each year on an issue.¹⁴

Discount - The condition of the price of a bond that is lower than par. The discount equals the difference between the price paid for a security and the security's par value. For example, if a bond with a par value of \$1,000 is currently selling for \$990 dollars, it is selling at a discount.¹⁵

Discounted IPA - A hybrid IPA methodology that combines the leveraging power of Traditional IPAs in the use of Zero Coupon Bonds, with the fiscal conservatism of Self-Funded IPAs, where the debt service burden in future years is minimized because of the discounted purchase price. In return for discounting the purchase price, landowners are guaranteed a higher interest rate and the ability to earn significant tax-exempt interest payments, the potential of lower capital gains taxes, and the potential for a charitable contribution for the discounted purchase price.

Easement - The right to use the real property of another for a specific purpose. The easement is itself a real property interest, but legal title to the underlying land is retained by the original owner for all other purposes. Typical easements are for access to another property, for utility or sewer lines both under and above ground, use of spring water, entry to make repairs on a fence or slide area, drive cattle across and other uses. Easements can be created by a deed to be recorded just like any real property interest, by continuous and open use by the non-owner against the rights of the property owner for a statutory number of years, typically five ("prescriptive easement"), or to do equity (fairness), including giving access to a land-locked piece of property (sometimes called an "easement of necessity"). Easements may be specifically described by boundaries ("24 feet wide along the northern line for a distance of 180 feet"), somewhat indefinite ("along the trail to the northern boundary") or just for a purpose ("to provide access to the Jones property") sometimes called a "floating easement." There is also a "negative easement" such as a prohibition against building a structure which blocks a view¹⁶ and a conservation easement, which prohibits residential, commercial, or industrial development of certain properties to protect its conservation values. (see also **Conservation Easement**).

Face Amount - (see **Par Value**)

Fair Market Value - The amount for which property would sell on the open market if put up for sale. This is distinguished from "replacement value," which is the cost of duplicating the

¹³ http://www.msrb.org/msrb1/glossary/view_def.asp?param=COUPONRATE

¹⁴ http://www.msrb.org/msrb1/glossary/view_def.asp?param=DEBTSERVICE

¹⁵ <http://www.investopedia.com/terms/d/discount.asp>

¹⁶ <http://dictionary.law.com/Default.aspx?selected=603>

property. Real estate appraisers will use "comparable" sales of similar property in the area to determine market value, adding or deducting amounts based on differences in quality and size of the property.¹⁷

Fee - (see **Fee Simple**)

Fee Simple - absolute title to land, free of any other claims against the title, which one can sell or pass to another by will or inheritance. This is a redundant form of "fee," but is used to show the fee (absolute title) is not a "conditional fee," "determinable fee," or "fee tail."¹⁸

Fiscal Year - A twelve-month period at the end of which financial position and results of operations of an entity are determined. Financial reporting, budgeting and accounting periods are determined on the basis of the applicable fiscal year.¹⁹ Typically, state and local government fiscal years run from July 1 to June 30, while the federal government runs from October 1 to September 30.

Floor - (see **Interest Rate Floor**)

Full Faith and Credit - (see **General Obligation Bond**)

General Fund - In public sector accounting, the primary or catchall fund of a government, government agency, or nonprofit entity such as a university. It is similar to a firm's general ledger account, and records all assets and liabilities of the entity that are not assigned to a special purpose fund. It provides the resources necessary to sustain the day-to-day activities and thus pays for all administrative and operating expenses. When governments or administrators talk about 'balancing the budget' they typically mean balancing the budget for their general fund.²⁰

General Obligation Bond - A bond that is secured by the full faith, credit and taxing power of an issuer. General obligation bonds issued by local units of government are typically secured by a pledge of the issuer's ad valorem taxing power; general obligation bonds issued by states are generally based upon appropriations made by the state legislature for the purposes specified. Ad valorem taxes necessary to pay debt service on general obligation bonds are often not subject to the constitutional property tax millage limits (an "unlimited tax bond"), although in some cases such limit may exist (a "limited tax general obligation bond"). Such bonds constitute debts of the issuer and often require approval by election prior to issuance. In the event of default, the holders of general obligation bonds have the right to compel a tax levy or legislative appropriation.²¹

Installment Purchase Agreement (IPA) - An acquisition methodology that utilizes U.S. Treasury Securities to fund fee or easement purchases for the mutual benefit of the conservation community and landowners. In return for deferring receipt of the principal amount of the

¹⁷ <http://dictionary.law.com/Default.aspx?selected=724>

¹⁸ <http://dictionary.law.com/Default.aspx?selected=736>

¹⁹ http://www.msrb.org/msrb1/glossary/view_def.asp?param=FISCALYEAR

²⁰ http://www.investorwords.com/7323/general_fund.html

²¹ http://www.msrb.org/msrb1/glossary/view_def.asp?param=GENERALOBLIGATIONBOND

purchase price until the securities mature, landowner receive semi-annual tax-exempt interest payments and are able to defer capital gains taxes until the maturity date, at which time they receive the principal in a lump sum payment. Traditionally, state and local government entities purchase a U.S. Treasury Security known as a Zero Coupon Bond to fund the principal amount, which is discounted well below face value, which in turn allows minimal initial investment on the entities' part so that more acquisitions can be undertaken in a given fiscal year.

Installment Sale - A method of sale that allows for partial deferral of any capital gain to future taxation years. Installment sales require the buyer to make regular payments, or installments, on an annual basis, plus interest if installment payments are to be made in subsequent taxation years.²²

Interest (Rate) - The amount paid by a borrower as compensation for the use of borrowed money. This amount is generally calculated as an annual percentage of the principal amount.²³

Interest Rate Floor - an agreement whereby the issuer agrees to pay a stated rate of interest even if the actual rate on the variable rate debt is lower.²⁴

Issuer - A state, political subdivision, municipality, or governmental agency or authority that raises funds through the sale of municipal securities.²⁵

Maturity Date (Maturity) - The date the principal of a municipal security becomes due and payable to the security holder.²⁶

Municipal Securities - A general term referring to securities issued by local governmental subdivisions such as cities, towns, villages, counties or special districts, as well as securities issued by states and political subdivisions or agencies of states. A prime feature of these securities is that interest or other investment earnings on them usually are excluded from gross income of the holder for federal income tax purposes. Issuers of municipal securities are exempt from most federal securities laws.²⁷

Outstanding (Outstanding Bonds) - Bonds that have been issued but have not yet matured or been otherwise redeemed.²⁸

Par (Par Value) - The amount of principal that must be paid at maturity. The par value is also referred to as the "face amount" of a security.²⁹

²² <http://www.investopedia.com/terms/i/installment-sale.asp>

²³ http://www.msrb.org/msrb1/glossary/view_def.asp?param=INTEREST

²⁴ http://www.msrb.org/msrb1/glossary/view_def.asp?param=INTERESTRATEFLOOR

²⁵ http://www.msrb.org/msrb1/glossary/view_def.asp?param=ISSUER

²⁶ http://www.msrb.org/msrb1/glossary/view_def.asp?param=MATURITY

²⁷ http://www.msrb.org/msrb1/glossary/view_def.asp?param=MUNICIPALSECURITIES

²⁸ http://www.msrb.org/msrb1/glossary/view_def.asp?param=OUTSTANDING

²⁹ http://www.msrb.org/msrb1/glossary/view_def.asp?param=PARVALUE

Paying Agent - The entity responsible for transmitting payments of interest and principal from an issuer of municipal securities to the security holders (i.e. the landowner). The paying agent is usually a bank or trust company, but may be the treasurer or some other officer of the issuer.³⁰

Premium - The difference between the higher price paid for a fixed-income security and the security's face amount at issue. If a fixed-income security (bond) is purchased at a premium, existing interest rates are lower than the coupon rate. Investors pay a premium for an investment that will return an amount greater than existing interest rate.³¹

Principal - The face amount or par value of a security payable on the maturity date.³²

Securitization - The process of taking an illiquid asset, or group of assets, and through financial engineering, transforming them into a security.³³

Security - Generally, an instrument evidencing debt or equity in a common enterprise in which an investment is made on the expectation of financial gain. The term includes notes, stocks, bonds, debentures or other forms of negotiable and non-negotiable equities or evidences of indebtedness or ownership.³⁴ (see also **Municipal Securities** and **Treasury Securities**).

Self-Funded IPA - An IPA that typically pays landowners the appraised fair market value of the easement (or fee interest) as principal and pays semi-annual interest on the deferred principal amount at the current yield on U.S. Treasuries. Because principal and interest are paid for at closing (through the purchase of a combination of T-Bonds and Zeros or SLGS) future debt service is covered. While landowners can take advantage of all of the tax benefits associated with IPAs, the conservation community has no more leveraging ability than with a cash offer, unless the purchase price is discounted by the landowner as part of the transaction.

Settlement (Closing) - The process of completing a financial transaction. For mortgage loans, the process of signing mortgage documents, disbursing funds, and, if applicable, transferring ownership of the property. In some jurisdictions, closing is referred to as “escrow,” a process by which a buyer and seller deliver legal documents to a third party who completes the transaction in accordance with their instructions.³⁵

SLGS - An acronym (pronounced “slugs”) for “State and Local Government Series.” SLGS are special Treasury securities sold by the United States Treasury Department to states, municipalities and other local government bodies.³⁶ The SLGS program was initiated in 1972, as the result of federal legislation enacted in 1969, which restricted state and local government entities from earning arbitrage profits from investing bond proceeds in higher yielding investments. Under the SLGS program, the U.S. Treasury offers special low-yield securities to

³⁰ http://www.msrb.org/msrb1/glossary/view_def.asp?param=PAYINGAGENT

³¹ <http://www.investopedia.com/terms/p/premium.asp>

³² http://www.msrb.org/msrb1/glossary/view_def.asp?param=PRINCIPAL

³³ <http://www.investopedia.com/ask/answers/07/securitization.asp>

³⁴ http://www.msrb.org/msrb1/glossary/view_def.asp?param=security

³⁵ <http://www.ftc.gov/bc/edu/pubs/consumer/homes/zrea03.pdf>

³⁶ http://www.msrb.org/msrb1/glossary/view_def.asp?param=SLGS

state and local governments and other issuers of tax-exempt bonds for investment of proceeds subject to IRS arbitrage restrictions.³⁷

STRIPS - Acronym for “Separate Trading of Registered Interest and Principal Securities.” STRIPS consist of an ownership interest in a specified principal amount of a Treasury security that has been stripped (at issuance) of the right to receive any interest payments thereon, instead resulting in the owner of the STRIPS receiving a single payment upon “maturation” of the STRIPS. STRIPS have the economic characteristics of a zero coupon bond.³⁸ (see also **Zero Coupon Bonds**)

Traditional IPA - An IPA that typically pays the appraised fair market value of the easement as principal and pays interest on the deferred principal amount at the current yield on U.S. Treasury STRIPS. Because Zero Coupon Bonds are purchased by state and local government entities to finance the principal payment, more easement purchases can be accomplished in a given fiscal year because Zeros can be had for less than face value. However, semi-annual interest payments must be paid to landowners in returning for them deferring the payment of principal, requiring additional resources from the conservation community since Zeros only cover the principal payment. The commitment to pay future debt service, particularly where dedicated funding sources do not exist, has proved problematic for many state and local government entities, who either shy away from the concept or engage in it only to find themselves limited future purchases until some of the outstanding debt service is paid down.

Treasury Securities - Debt obligations of the United States Government sold by the Treasury Department in the form of bills, notes and bonds (as well as SLGS sold to issuers of municipal securities) backed by the full faith and credit of the United States Government:³⁹

Bills (T-Bills) - A short-term debt obligation backed by the U.S. Government with a maturity of less than one year. T-bills are sold in denominations of \$1,000 up to a maximum purchase of \$5 million and commonly have maturities of one month (four weeks), three months (13 weeks) or six months (26 weeks). T-bills are issued through a competitive bidding process at a discount from par, which means that rather than paying fixed interest payments like conventional bonds, the appreciation of the bond provides the return to the holder.⁴⁰

Notes - A marketable U.S. government debt security with a fixed interest rate and a maturity between one and 10 years. Treasury notes can be bought either directly from the U.S. Government or through a bank. When buying Treasury notes from the Government, you can either put in a competitive or non-competitive bid. With a competitive bid, you specify the yield you want; however, this does not mean that your bid will be approved. With a non-competitive bid, you accept whatever yield is determined at auction.⁴¹

Bonds (T-Bonds) - A marketable, fixed-interest U.S. government debt security with a

³⁷ http://www.treasurydirect.gov/govt/resources/faq/faq_slgs.htm

³⁸ http://www.msrb.org/msrb1/glossary/view_def.asp?vID=4195

³⁹ http://www.msrb.org/msrb1/glossary/view_def.asp?param=TREASURYSECURITIES

⁴⁰ <http://www.investopedia.com/terms/t/treasurybill.asp>

⁴¹ <http://www.investopedia.com/terms/t/treasurynote.asp>

maturity of more than 10 years. Treasury bonds make interest payments semi-annually and the income that holders receive is only taxed at the federal level.⁴²

Yield - The annual rate of return on an investment, based on the purchase price of the investment, its coupon rate and the length of time the investment is held.⁴³

Zero Coupon Bonds - An original issue discount bond on which no periodic interest payments are made (hence the term “zero coupon”) but which is issued at a deep discount from par, accreting (at the rate represented by the offering yield at issuance) to its full value at maturity.⁴⁴ (see also **STRIPS**)

⁴² <http://www.investopedia.com/terms/t/treasurybond.asp>

⁴³ http://www.msrb.org/msrb1/glossary/view_def.asp?param=YIELD

⁴⁴ http://www.msrb.org/msrb1/glossary/view_def.asp?param=ZEROCOUPONBOND