

What You Need to Know from Tax Cases (Shorn of Nuance)

We prepared this summary of the basic results of conservation tax cases to aid land trusts, but not to give tax, legal or other advice. To aid digestion, we distilled the cases to only their essential points and removed all nuance. Obtain legal counsel to apply these general observations to specific cases.

These cases are nuance-laden and fact-specific. To really understand the implications, you need to read the full cases. The case law as a whole has only limited guidance on some IRC §170 issues. Where legal precedent is lacking or confused, a case can be susceptible to multiple interpretations. When facing these many uncertainties in tax court decisions, land trusts and landowners must have competent expert legal advice *and* understand their individual tolerance and capacity for managing the risk associated with conservation transactions. IRS [rulings](#), letters and [notices](#) must also be considered in interpreting these tax court decisions.

Conservation tax law continues to evolve. Land trusts should urge donors and professionals to follow §170(h) and the accompanying Treasury Regulations and to be realistic in valuation. Not all the Circuits Courts have spoken nor have they addressed all the issues. The IRS views the applicability of these cases narrowly. The First Circuit invited the IRS to issue “forward looking” regulations that give “fair warning” to taxpayers, but we don’t know what the IRS will do.

DETAILS

Contemporaneous Written Acknowledgement or Gift Letter

1. Substantial compliance does not excuse following §170(f)(8)(B)'s substantiation requirements. It's safest to strictly comply with the contemporaneous written acknowledgement (gift letters). (*Schrimsher, Bruzewicz*) but *Irby, Simmons, Averyt* and *RP Golf* are exceptions where the transaction documentation as a whole qualified as contemporaneous written acknowledgment.
2. "Contemporaneous" for gift letters means on or before the filing date of the tax return (including extensions) for the year in which the contribution was made. (*DiDonato*)
3. The contemporaneous written acknowledgement must accurately state all value the land trust transfers to the donor in the entire transaction (quid pro quo). (*Cohan -- a complex case*)
4. Insignificant services without reciprocal value are not quid pro quo because value has not been transferred. (*Dunlap, et al.*)
5. A cash contribution for easement stewardship is not a quid pro quo payment even when the payment may be a “prerequisite” to the acceptance of an easement, provided no reciprocal benefit in the form of significant services or goods is received by the donor; therefore, the cash payment is a donation. (*Scheidelman after Second Circuit opinion, Dunlap*).

Substantial Compliance, Form 8283 and Other Technicalities

1. The substantial compliance doctrine applies for minor omissions in the Form 8283 (such as the omission of property acquisition information). (*Scheidelman after Second Circuit opinion; but see Rothman reconsideration*).
2. Substantial compliance may, however, be insufficient to correct material flaws in the Form 8283 (omission of cost basis and date of acquisition, citing *Scheidelman prior to Second Circuit opinion*). (*Herman*) This is an example of evolving interpretations by the courts.

3. Attaching the full appraisal report substantially complied with the regulations despite the manner and date of acquisition and the cost basis omissions on the Form 8283. (*Friedberg*)

Mortgage Subordination, Proceeds Priority and Lender Agreements

1. Record a mortgage subordination (lender agreement) *prior to or at the time of* (contemporaneously with) *recordation* of the easement. (*Mitchel, Satullo*) It can appear in the record just before or just after the easement.
2. In *Kaufman*, the First Circuit said that a mortgage subordination granting a priority interest in insurance and condemnation proceeds to the lender did not violate the “proceeds” requirement in the Treasury Regulations.
3. In *Irby*, repayment of bargain sale purchase funds from government lenders did not violate the proceeds or perpetuity requirements.
4. Despite *Kaufman*, a lender’s subordination to the *entire* easement, including the right of the holder to its share of any proceeds, is prudent because (i) *Kaufman* footnote 5 notes that the “mortgage subordination” requirement could require it; (ii) Circuit Court opinions are the law only in the circuits in which they apply; and (iii) “full” subordination agreements allow the holder a share of proceeds upon extinguishment to replace lost conservation values.

Perpetuity

1. The *Carpenter* court held that termination by mutual agreement is not permitted, but declined to “rule that a conservation deed must require a judicial proceeding to extinguish an easement for the easement to be perpetual.” The court also said that, “the extinguishment regulation provides taxpayers with a guide, a safe harbor, by which to create the necessary restrictions to guarantee protection of the conservation purpose in perpetuity”. Exercise caution in drafting.
2. The *Carpenter* court also found that conservation easements are restricted gifts (“charitable gifts for a specific purpose”) and that after reviewing the conservation easement purposes held that “the cy pres doctrine is inapplicable to petitioners' restricted gifts.”
3. Tax-exempt organizations fail to enforce easements “at their peril.” (*Simmons, Kaufman*)
4. *Simmons* and *Kaufman* also held that a clause in a façade easement granting the holder the right to consent to changes can be exercised only consistently with the purpose of the easement allowing the holder the “flexibility to deal with remote contingencies.” This holding may be fact-specific to historic preservation cases – or not – we do not know yet.

Conservation Purposes

1. Generally a trend of deference to legitimate conservation purposes and sound land trust practices, such as annual monitoring and adequate documentation. (*Butler, Kiva, Glass*)
2. State law determines the nature of the property rights and charitable trust rules. Federal law determines the appropriate tax treatment of those rights. (*Carpenter*). State law determines if a baseline may be incorporated by reference in a conservation easement. (*Butler*)
3. Annual monitoring is sufficient to uphold perpetuity and to ensure that exercised reserved rights are not inconsistent with the protected conservation purposes. (*Butler, Friedberg*)
4. Existing land-use and zoning regulations may cause an easement donation to not be a “qualified conservation contribution” (*Asser*) or to be of no value. (*Turner, Herman, Dunlap*)
5. Quality of the habitat and the actual effect of the reserved rights are more important in determining conservation purposes than the size of the protected property. The potential for habitat can be sufficient as a conservation purpose. (*Glass, Kiva, RP Golf*)

Appraisals, Appraisers and Valuation

1. Timing matters regarding the appraisal date. (*Asser, Schultz, Lord, Ney, but see Trout Ranch*)

2. Substantial compliance can apply to appraisal requirements but material errors in methodology cannot be overlooked. Typographical errors in the appraisal that do not relate to the substance or essence of value and whether a charitable contribution was made can be overlooked. (*Friedberg*) Appraisals methodology need not be perfect to be “qualified.” (*Simmons, Scheidelman, but see Rothman reconsideration, Irby*)
3. The appraiser’s analysis in conjunction with other factors cited by the appraiser constituted “reasoned analysis” and therefore met the regulatory threshold requirements of a “qualified appraisal.” Issues of appraisal quality and the weight given to the appraisal conclusions are still unclear. (*Scheidelman Second Circuit reversal, but see Rothman reconsideration*)
4. The *Rothman* reconsideration said that the appraisal failed to satisfy 8 of 15 regulations and deprived the IRS of “sufficient information to evaluate the deductions claimed.”
5. The Tax Court must consider all the facts and circumstances in valuations. (*Whitehouse*)
6. Appraisers must correctly consider legal issues, such as access rights. (*Hughes*)
7. Use a local experienced appraiser with extensive knowledge of the local market. Local is relative to the area in question. (*Kiva Dunes*)
8. The court reduced the deduction by 90 percent because the appraisal did not adequately analyze important facts affecting the landowner’s realization of land value from mineral extraction. (*Esgar*)
9. Restrictions in other conservation easements too dissimilar from the subject easement are not "a substantial record of sales of easements comparable to the donated easement." (*Trout Ranch*)
10. Post-contribution comparables can be allowed as some weighted evidence of value despite the Treasury Regulations. (*Trout Ranch*)
11. The IRS may not use a general comparable matrix to fix value. (*Hughes*)
12. A taxpayer is allowed access to the IRS documentation for the matrix. (*RCL Properties*)
13. An appraiser must be independent of the land trust. (*Kaufman*)

Evidence

1. The taxpayer’s appraisal and testimony were so deficient that they were not admissible. (*Boltar*)
2. The taxpayer has the burden of proving the IRS incorrect by introducing credible evidence. (*Butler and numerous others*)
3. The taxpayer failed to meet the burden of proof by not calling the original appraiser as a witness. (*Evans*) But this is not an absolute requirement. (*Hughes*).
4. Attorney-client privilege did not apply to the appraiser’s work file because it was prepared primarily for easement valuation purposes, not to provide legal advice. (*Richey, Pesky*)
5. An email to the taxpayer on market value was admissible as evidence as to whether the taxpayer acted in “good faith.” The Circuit Court returned the issue to the Tax Court for a decision. (*Kaufman*)

Tax Credits

1. The holding period for tax credits began at the time of receipt of the credits, not when the taxpayer acquired the land. The credits are capital assets. (*Tempel, McNeil*)
2. A partner without a tangible business purpose beyond tax benefits should not be recognized as a partnership for federal income tax purposes because the partner was created for the express purpose of improperly passing along tax benefits. It had no meaningful stake in the success or failure of the venture, so it should be treated as a sham transaction. (*Historic Boardwalk*)

CASE CITATIONS

1. Asser (1982 East, LLC) v. Commissioner, T.C. Memo 2011-84 April 12, 2011
2. Averyt v. Commissioner, 2012 T.C. Memo 198, July 16, 2012
3. Boltar, LLC v. Commissioner, 136 T.C. 14
4. Bruzewicz v. United States, 604 F. Supp. 2d 1197 (N.D. Ill. 2009)
5. Butler v. Commissioner, T.C. Memo 2012-72, March 19, 2012
6. Carpenter v. Commissioner, T.C. Memo. 2012-1, January 3, 2012
7. Cohan v. Commissioner, T.C. Memo. 2012-8, January 10, 2012
8. DiDonato v. Commissioner, 2011 T.C. Memo 153, June 29, 2011
9. Dunlap v. Commissioner, T.C. Memo 2012-126, May 1, 2012
10. Esgar Corp. v. Commissioner, T.C. Memo 2012-35, Feb. 6, 2012
11. Evans v. Commissioner, T.C. Memo 2010-207, September 22, 2010
12. Friedberg and Moss v. Commissioner, T.C. Memo 2011-238, October 3, 2011
13. Glass v. Commissioner, 471 F.3d 698 (6th Cir. 2006), affirming 124 T.C. No. 16 (U.S.T.C. 2005)
14. Herman v. Commissioner, T.C. Docket No. 14005-07, September 13, 2011
15. Historic Boardwalk Hall LLC v. Commissioner, No. 11-1832 (3d Cir. Aug. 27, 2012).
16. Hughes v. Commissioner, T.C. Memo 2009-94
17. Irby v. Commissioner, 139 T.C. No. 14 (October 25, 2012).
18. Kaufman v. Commissioner, US Court of Appeals 1st Circuit, Nos. 11-2017, 11-2022, July 19, 2012 reversing 134 T.C. 9 (U.S.T.C. 2010)(Kaufman I), reconsideration denied, 136 T.C. 13 (U.S.T.C. 2011) (Kaufman II)
19. Kiva Dunes Conservation, LLC v. Commissioner, T.C. Memo 2009-145, June 22, 2009
20. Lord v. Commissioner, T.C. Memo 2010-196, September 8, 2010
21. Mitchell v. Commissioner, 138 T.C. No. 16, April 3, 2012
22. McNeil v. Commissioner, T.C. Memo. 2011-109, May 2012
23. Ney, Bruce K. et ux. v. Commissioner, T.C. Summ. Op. 2006-154 (U.S.T.C. 2006)
24. Pesky v. U.S. Dist. Court, D. Idaho, CIV. 1:10-186 WBS, August 29, 2011
25. RCL Properties, Inc. et al. v. United States, 102 A.F.T.R.2d (RIA) 7302 (D. Colorado 2009)
26. US v. Richey, 632 F.3d 559, 107 A.F.T.R.2d (RIA) 573 (9th Cir. 2011), reversing 2009 U.S. Dist; 103 A.F.T.R.2d (RIA) 1228 (D. Idaho 2009)
27. Rothman v. Commissioner, T.C. Memo. 2012-218; No. 17547-10, 31 July 2012
28. RP Golf, et al v. Commissioner, T.C. Memo. 2012-282, October 3, 2012
29. Satullo v. Commissioner, 1993-614 (U.S.T.C 1993)
30. Simmons v. Commissioner, 646 F.3d 6 (D.C. Cir. 2011), affirming T.C. Memo 2009-208 (U.S.T.C. 2009)
31. Scheidelman v. Commissioner, 682 F.3d 189 (2 d Cir. 2012), reversing 100 TCM (2010)
32. Schrimsher v. Commissioner, T.C. Memo 2011-71,
33. Tempel v. Commissioner, 136 T.C. 15, April 5, 2012
34. Trout Ranch, LLC v. Commissioner, No. 11-9006, United States Court of Appeals, Tenth Circuit, August 16, 2012, affirming T.C. Memo. 2010-283 (U.S.T.C. 2010)
35. Turner v. Commissioner, 126 T.C. No. 16 (U.S.T.C. 2006)
36. Whitehouse Hotel Limited Partnership v. Commissioner, 615 F.3d 321 (5th Cir. 2010), vacating and remanding 131 T.C. No. 10 (U.S.T.C. Oct. 30, 2008); upheld on reconsideration 139 T.C. No. 13 October 23, 2012.

A note about precedents: The Tax Court has different types of opinions. Only full opinions and memo opinions set official precedent.

A. **Bench Opinion** -- the Judge orally states the opinion in court during the trial session; the opinion cannot be relied on as precedent.

B. **Summary Opinion** -- cannot be relied on as precedent, and the decision cannot be appealed.

C. **Tax Court Opinion or Memorandum Opinion** -- The Chief Judge decides whether an opinion in a regular case will be issued as a Memorandum Opinion or as a Tax Court Opinion. Generally, a Memorandum Opinion is issued in a regular case that does **not** involve a novel legal issue and that addresses cases where the law is settled or factually driven. A Memorandum Opinion can be cited as legal authority, and the decision can be appealed. Generally, a Tax Court Opinion is issued in a regular case when the Tax Court believes it involves a sufficiently important legal issue or principle. A Tax Court Opinion can be cited as legal authority, and the decision can be appealed.