

Charitable Contributions

Partnership-Owned Easements Safe With Solid Appraisals

BNA Snapshot

- Practitioners: Not all syndicated deals that IRS is targeting are bad
- Zoning can strengthen property value stated in deals



By Kat Lucero

Practitioners hoping to prove their partnership-donated conservation easement deals are legitimate should look to their local zoning board for help, advocates of those types of deals say.

The Internal Revenue Service last year warned it would start flagging certain conservation easements donated by partnerships, saying in Notice 2017-10 that such deals could be considered tax shelters or “syndicated” deals. Some promoters of these deals have exaggerated appraisals to get a higher charitable deduction than the property’s value, the IRS said.

The notice also included deals “substantially similar” to the targeted transactions and stigmatized legitimate partnership-donated conservation easements, practitioners told Bloomberg BNA.

The IRS has also challenged the appraisal value of conservation easements in a series of U.S. Tax Court cases.

A conservation easement is a voluntary legal agreement that permanently restricts development on a property. Individual owners or partners can receive a tax deduction if they donate property for this purpose under §170(h). One of the ways a landowner can attract private funding for the easement is to create a partnership or passthrough entity.

But advocates for easements donated by partnerships argue that not all syndicated deals are bad. Rezoning the property before the partnership donates a conservation easement can demonstrate the parcel’s highest and best use, which is used to assess the value of the parcel. A property’s value can fluctuate for a variety of reasons, including the popularity of surrounding real estate. This strategy would be applied whether the partnership develops or conserves the property, and often involves local municipalities that determine land use laws.

Rezoning won’t be disputed if the “IRS comes in on that property,” Randy Bampfield, co-chair of the legal committee of the Partnership for Conservation (P4C), a lobbying group that supports the private funding of conservation easements through the use of partnerships. Bampfield was a former senior counsel with the Small Business/Self-Employed Division for the IRS Office of Chief Counsel.

Tax Shelter?

The IRS notice targeted suspect syndicated schemes that offer investors a deduction that “equals or exceeds an amount that is two and one-half times the amount of the investor’s investment.” It asked participants to provide additional reporting for such arrangements dating back to January 2010.

Partnership-owned easements aren’t necessarily making a profit even though “they’re getting money out of it,” said Robert D. Keller, CEO of the Atlantic Coast Conservancy Inc. and a P4C member.

P4C touts the protection of marshland in South Carolina and Georgia and a privately owned, undeveloped parcel in the Cherokee National Forest in North Carolina as examples of projects with conservation easements set up in partnerships.

But groups such as the Land Trust Alliance continue to discourage such deals and argue they are motivated by profit. "Following our first advisory to members in 2015, we repeatedly refreshed and enhanced that counsel, warning our members to steer clear of these deals," Wendy Jackson, the organization's executive vice president, said in a statement to Bloomberg BNA.

The Land Trust Alliance updated its standards and practices earlier this year to align with the IRS notice, which is "reasonable and appropriate. Any suggestions to the contrary are irresponsible," Jackson said.

Best Practices

A Florida ranch's significant win in the U.S. Tax Court inspired the recommendation of rezoning property before obtaining a conservation easement, practitioners said.

The IRS in 2014 challenged Palmer Ranch Holdings Ltd.'s conservation easement deduction worth more than \$25 million. The Tax Court ruled Oct. 13, 2016, that Palmer Ranch can use rezoning regulations on the property to support the adjusted changes in the conservation easement's fair market value.

"Zoning is an important issue to the highest and best use" of property, said Ronald Levitt, a shareholder at Sirote & Permutt PC.

While zoning can help, it isn't applicable to all property, according to Anson H. Asbury, founder and principal of Asbury Law Firm LLC.

"I'd be reluctant to say that an appraisal is less valid because it's unzoned," he said. "A competent appraisal should take into account whatever the highest and best use of the property is."

Furthermore, some small municipalities don't have local zoning boards, Asbury said, and areas such as open space are left unzoned simply because of what they are.

Another strategy for securing deals is to hire an appraiser who is experienced in conservation easements, which can be a "different language," said Steve Small of the Law Office of Stephen J. Small. Enlisting the help of a good local appraiser who understands the area's real estate market well is also an option.

Congressional Outlook

The IRS notice is being challenged in an upcoming House fiscal year 2018 spending package, which the chamber will consider in the coming weeks.

The House Appropriations Subcommittee on Financial Services and General Government's policy rider would limit the agency's rulemaking on Notice 2017-10 and any related guidance.

The policy rider "provision was added because the notice on conservation easements was issued as the Obama Administration was exiting office in December without a process for public comment," a spokesman for Rep. Tom Graves (R-Ga.), chairman of the subcommittee, said in an email.

The subcommittee puts together the appropriations bundle that includes IRS funding. The provision "designates abroad category of conservation easement donations as 'tax avoidance transactions,' which needs clarification," the spokesman said.

Senate appropriators have yet to reveal whether their funding bill would mirror the House version. However, Finance Committee Chairman Orrin G. Hatch (R-Utah) and ranking member Ron Wyden (D-Ore.) have been concerned about syndicated deals and have asked the IRS about its analysis on the materials the agency has collected.

Preliminary analysis showed that such deals have so far yielded \$217 million in deductions, IRS Commissioner John Koskinen told the Senate tax-writers in a July 13 letter.

"We applaud the continued bipartisan investigation from the Senate Finance Committee on these suspect transactions," the Land Trust Alliance's Jackson said.

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For More Information

For a discussion of charitable contributions of conservation easements in the Tax Management Portfolios, see 521 T.M., Charitable Contributions: Income Tax Aspects (U.S. Income Series), and 863 T.M., Charitable Contributions: Income Tax Aspects (Estates, Gifts and Trusts Series), and in Tax Practice Series, see ¶12390, Charitable Contributions: Requirements for Deduction, and ¶12395, Charitable Contributions: Substantiation Requirements.