

TAX COURT CASE UPDATE

Citation:

Gordon Kaufman et ux v. Commissioner, 140 T.C. No. 1, February 28, 2013.

Overview:

The Tax Court has held that a taxpayer was not entitled to claim a charitable deduction for a conservation easement because a provision in the grant allowing a substitution of the donated property was inconsistent with Regulation Section 1.170A-14(b)(2)'s requirement that the conservation purpose be protected in perpetuity.

The Facts:

In 1996, B.V. Belk, Jr., transferred land to his company, Olde Sycamore, LLC. On that property, Olde Sycamore developed a residential community that was comprised of 402 single-family home lots and built Olde Sycamore Golf Plantation.

In 2004, the taxpayer contributed a conservation easement on 184.627 acres of a golf course to a qualified organization, the Smoky Mountain National Land Trust. The conservation easement agreement allowed the parties, by agreement and subject to certain restrictions, to change what real property was subject to the conservation easement. On his 2004 return, the taxpayer claimed a \$10.5 million charitable contribution deduction for the easement.

On audit, the IRS challenged the deduction, contending that the interest in real property that the taxpayer donated was not subject to a use restriction granted in perpetuity because the conservation easement agreement allowed substitutions. The IRS characterized the easement as a "floating easement" and argued that a conservation easement that does not relate to a specific piece of property cannot give rise to a qualified conservation contribution.

Discussion:

The Tax Court denied the deduction for the contribution of the easement, concluding it was precluded by Code Section 170(h)(2)(C). It found that the taxpayer did not donate an interest in real property subject to a use restriction granted in perpetuity because the conservation easement agreement allowed the taxpayer to remove real property from the coverage of the conservation easement.

The Court reasoned that while the taxpayer agreed to not develop the golf course, the use restriction was not granted in perpetuity because he could change what property was subject to the conservation easement under the agreement. Under the terms of the conservation easement, the taxpayer could remove portions of the golf course and replace them with property currently not subject to the conservation easement. Thus, he had not donated an interest in real property that was subject to a use restriction granted in perpetuity. To conclude otherwise, The Court determined, would allow the taxpayer a deduction for agreeing not to develop the golf course when the golf course could be developed by substituting the property subject to the

conservation easement.

The Tax Court rejected the taxpayer's argument that it did not matter that the conservation easement agreement allowed substitutions because it only allowed substitutions that would not harm the conservation purposes of the conservation easement. It found that the Code Section 170(h)(5) requirement that the conservation purpose be protected in perpetuity was separate and distinct from the Code Section 170(h)(2)(C) requirement that there be real property subject to a use restriction in perpetuity. Satisfying Code Section 170(h)(5), did not necessarily affect whether there was a qualified real property interest under Code Section 170(h)(2)(C).

The Court also found that it was immaterial that the Smoky Mountain National Land Trust had to approve the substitution and that the Smoky Mountain National Land Trust could not, under the terms of the easement agreement, agree to an amendment that would result in the conservation easement failing to qualify as a qualified conservation contribution under Code Section 170(h). While there was a conflict in the agreement terms, it was clear that the right to substitute was a specific, enumerated right allowed to the taxpayer

Conclusion:

Under Code Section 170(h)(2)(C), the taxpayer could not claim a conservation easement deduction as the terms of the agreement allowed the taxpayer to change the land that was subject to the agreement. As a result, the purpose of the easement was not perpetual, and therefore, not allowed as a charitable contribution.