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ARTICLE

EXTINGUISHING AND AMENDING TAX-DEDUCTIBLE CONSERVATION EASEMENTS: PROTECTING THE FEDERAL INVESTMENT AFTER *CARPENTER*, *SIMMONS*, AND *KAUFMAN*

Nancy A. McLaughlin

UF UNIVERSITY OF FLORIDA COLLEGE OF LAW

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EXTINGUISHING AND AMENDING TAX-DEDUCTIBLE CONSERVATION EASEMENTS: PROTECTING THE FEDERAL INVESTMENT AFTER *CARPENTER*, *SIMMONS*, AND *KAUFMAN*

by

Nancy A. McLaughlin[*]

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I. INTRODUCTION

The Internal Revenue Service's victory in *Carpenter v. Commissioner* represented an important step in the agency's ongoing efforts to both address abuses and establish precedent consistent with congressional intent in the conservation easement donation context.[1] While Congress has

1. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, T.C.M. (RIA) ¶ 2012-001 (2012). For reports of abuse, see, e.g., Abusive Transactions Involving Charitable Contributions of Easements, IRS, http://www.irs.gov/Charities-&-Non-

clearly favored providing a charitable income tax deduction under Internal Revenue Code section 170(h) to encourage the donation of conservation easements, Congress also has been willing to do so only if the easements are "granted in perpetuity" to government and nonprofit holders "exclusively for conservation purposes," and the conservation purposes of such easements are "protected in perpetuity."[2]

In *Carpenter*, the Tax Court addressed a key aspect of the protected-in-perpetuity requirement — the circumstances under which government and nonprofit holders can agree to extinguish tax-deductible conservation easements. This is a critically important issue. Federal taxpayers are investing billions of dollars in conservation easements intended to permanently protect unique or otherwise significant land areas or structures.[3]

Profits/Conservation-Easements; Margaret Jackson, *Easement Deals Lead to Inquiries*, DEN. POST, Nov. 25, 2007, at A01; Jennie Lay, *Conservation Easement Conundrums*, HIGH COUNTRY NEWS, Mar. 31, 2008, http://www.hcn.org/issues/367/17604?searchterm=Conservation+Easement+Conun; Craig R. McCoy & Linda K. Harris, *Saving Treasures that Benefit Few*, PHILA. INQUIRER, Feb. 24, 2002, at A01; Lisa Provence, *Scenic Treasure: How Conservation Lines the Pockets of the Rich,* THE HOOK, Mar. 3, 2011, at 18; Joe Stephens & David B. Ottaway, *Developers Find Payoff in Preservation*, WASH. POST, Dec. 21, 2003, at A01; Joe Stephens, *For Owners of Upscale Homes, Loophole Pays; Pledging to Retain the Facade Affords a Charitable Deduction*, WASH. POST, Dec. 12, 2004, at A01; Joe Stephens & David B. Ottaway, *How a Bid to Save a Species Came to Grief*, WASH. POST, May 5, 2003, at A01; Joe Stephens, *Local Laws Already Bar Alterations; Intervention by Trusts Is Rare for Preservation,* WASH. POST, Dec. 12, 2004, at A15; Joe Stephens & David B. Ottaway, *Nonprofit Land Bank Amasses Billions*, WASH. POST, May 4, 2003, at A01; Joe Stephens & David B. Ottaway, *Nonprofit Sells Scenic Acreage to Allies at a Loss; Buyers Gain Tax Breaks with Few Curbs on Land Use*, WASH. POST, May 6, 2003, at A01; Joe Stephens, *Tax Break Turns Into Big Business*, WASH. POST, Dec. 13, 2004, at A01. For criticisms of the incentive offered to conservation easement donors under section 170(h) and proposals for reform, see, e.g., JEFF PIDOT, REINVENTING CONSERVATION EASEMENTS: A CRITICAL EXAMINATION AND IDEAS FOR REFORM (Lincoln Institute of Land Policy 2005), http://www.lincolninst.edu/pubs/dl/1051_Cons%20Easements%20PFR013.pdf; Roger Colinvaux, *The Conservation Easement Tax Expenditure: In Search of Conservation Value*, 37 COLUM. J. ENVTL. L. 1, 9–10 (2012) [hereinafter Colinvaux, *In Search of Conservation Value*]; Daniel Halperin*, Incentives for Conservation Easements: The Charitable Deduction or a Better Way*, 74 LAW & CONTEMP. PROBS. 29 (2011) [hereinafter Halperin, *Incentives for Conservation Easements*].

2. *See* I.R.C. §§ 170(h)(1), 170(h)(2)(C), 170(h)(5)(A). *See also* S. REP. NO. 96-1007 (1980), *reprinted in* 1980 U.S.C.C.A.N. 6736 (legislative history of section 170(h)).

3. *See, e.g.*, Colinvaux, *In Search of Conservation Value*, *supra* note 1, at 9–10 (estimating a total revenue loss of $3.6 billion from the federal charitable income tax deduction provided to individual conservation easement donors from 2003 through 2008; the figure would be larger if it included corporate donations); S.

Astounding amounts of governmental and judicial resources are also being expended to ensure that the easements are not overvalued, that they satisfy the elaborate conservation purposes and other threshold requirements, and that the donations are properly substantiated. For example, as indicated in Appendix A, which lists the cases to date involving challenges to deductions claimed with respect to easement donations, thirty-two such cases (more than half), have been decided since 2005, and the IRS has indicated that there are more than 200 additional cases in the litigation pipeline.[4] This enormous up-front investment of foregone revenues and government and judicial resources will be for naught, however, if the purportedly permanent protections prove to be ephemeral because government and nonprofit holders fail to enforce the easements, or agree to improperly release, modify, or extinguish the easements.[5]

REP. NO. 96-1007, *supra* note 2, pt. 2, at 9, *reprinted in* 1980 U.S.C.C.A.N. at 6745 ("provisions allowing deductions for conservation easements should be directed at the preservation of unique or otherwise significant land areas or structures"); S. REP. NO. 96-1007, *supra* note 2, pt. 2, at 13, *reprinted in* 1980 U.S.C.C.A.N. at 6748 ("the bill explicitly provides that [the 'exclusively for conservation purposes'] requirement is not satisfied unless the conservation purpose is protected in perpetuity").

4. *See also* Notice 2004-41, 2004-1 C.B. 31 (warning that the IRS intends to disallow improper deductions and impose penalties and excise taxes on taxpayers, promoters, and appraisers involved in abusive transactions); STAFF OF JOINT COMM. ON TAXATION, 109TH CONG., 1ST SESS., OPTIONS TO IMPROVE TAX COMPLIANCE AND REFORM TAX EXPENDITURES, 281 (Jan. 2005), http://www.jct.gov/publications.html?func=showdown&id=1524 (detailing problems with the incentive and proposing reforms); 1 STAFF OF S. COMM. ON FIN., 109TH CONG., 1ST SESS., REP. OF STAFF INVESTIGATION OF THE NATURE CONSERVANCY, (Comm. Print 2005), http://finance.senate.gov/ (same); Instructions for Form 8283 (Rev. Dec. 2006), http://www.irs.gov/pub/irs-pdf/i8283.pdf (requiring a detailed supplemental statement in the case of conservation easement donations); 2011 Instructions for Schedule D (Form 990) http://www.irs.gov/pub/irs-pdf/i990sd.pdf (requiring detailed additional information in the case of organizations holding conservation easements); Complaint for Permanent Injunction and Other Relief, United States v. McClain, Civ. No. 11-1087 (D.D.C. June 14, 2011) (suit filed by the Department of Justice (DOJ) against the Trust for Architectural Easements (TAE) alleging abusive and illegal façade easement donation practices); Stipulated Order of Permanent Injunction, United States v. McClain, Civ. No. 11-1087 (D.D.C. July 15, 2011) (settlement of DOJ's suit against TAE by injunction permanently prohibiting TAE from engaging in certain practices); IRS CONSERVATION EASEMENT AUDIT TECHNIQUES GUIDE, http://www.irs.gov/pub/irs-utl/conservation_easement.pdf (detailed guidance for the examination of charitable contributions of conservation easements).

5. *See, e.g.*, Nancy A. McLaughlin, *Internal Revenue Code Section 170(h): National Perpetuity Standards for Federally Subsidized Conservation Easements, Part 2: Comparison to State Law*, 46 REAL PROP. TR. & EST. L.J. 1, 28–42 (2011)

Both Congress and the Treasury Department were aware of this danger, and they built significant safeguards into section 170(h) and the regulations to ensure that the conservation purposes of tax-deductible conservation easements would, in fact, be "protected in perpetuity." One of those safeguards is Regulation section 1.170A-14(g)(6) (the extinguishment and proceeds regulation), which addresses both the circumstances under which a tax-deductible conservation easement can be extinguished and the payment of proceeds to the holder to be used for similar conservation purposes in such event. A related safeguard is Regulation section 1.170A-14(c)(2) (the restriction on transfer regulation), which mandates that the holder be prohibited from transferring the easement, whether or not for consideration, unless the transfer is either to another qualified holder that agrees to continue to enforce the easement or pursuant to an extinguishment that complies with the extinguishment and proceeds regulation.

Carpenter provides significant guidance regarding compliance with the extinguishment component of the regulations, as well as the role of state law in ensuring that conservation easements are properly administered and enforced over the long term. The case also, however, has created confusion with respect to the state law *cy pres* doctrine and has caused some to argue that the process for extinguishment set forth in the regulations should be viewed as optional, and states, localities, and even holders should be free to adopt their own extinguishment procedures in lieu of satisfying federal tax law requirements.

This Article examines *Carpenter* against the backdrop of the legislative history of section 170(h), state law, and public policy. It clarifies the manner in which the state law *cy pres* doctrine and its general charitable intent requirement should be analyzed with regard to tax-deductible

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[hereinafter McLaughlin, *National Perpetuity Standards, Part 2*] (describing cases in which government and nonprofit holders agreed to improperly amend or terminate perpetual conservation easements); *infra* notes 242–44 and accompanying text (discussing concerns about conservation easement amendments, including concerns highlighted in the Senate Finance Committee's report following its investigation of The Nature Conservancy); STAFF OF J. COMM. TAXATION, 109TH CONG., 1ST SESS., DESCRIPTION OF REVENUE PROVISIONS CONTAINED IN THE PRESIDENT'S FISCAL YEAR 2006 BUDGET PROPOSAL, 239–41 (Comm. Print 2005), http://www.jct.gov/publications.html?func=startdown&id=1523 (proposal to impose significant penalties on charities that remove, fail to enforce, or inappropriately modify conservation easements, or transfer easements without ensuring that the conservation purposes will be protected in perpetuity); Jim Waymer, *New Conservation Rules Open Door for Developers to Build on Set-Aside Acreage,* FLORIDA TODAY (Sept. 14, 2012) ("It is land supposedly protected forever from development. But new [local] rules could allow landowners to back out of 'conservation easements,' promises they made not to build on pristine land in exchange for tax breaks or other benefits.").

conservation easements. It offers suggestions as to how best to comply with the extinguishment regulation given the Tax Court's rulings in *Carpenter* and other relevant cases. It discusses the court's holding that the tax-deductible conservation easements at issue in *Carpenter* constitute restricted charitable gifts under state law and the importance of this status in ensuring that easements are administered in accordance with their terms and purposes over the long term. It also explains that Congress enacted section 170(h) to subsidize the acquisition of *perpetual* conservation easements, or those that are extinguishable by a court only upon frustration of their purposes, and Congress specifically did not defer to states, localities, or easement holders regarding transfer, release, or other extinguishment of tax-deductible easements. Also examined are the reasons underlying the restriction on transfer, extinguishment, and proceeds regulations, as well as the policy reasons supporting the application of uniform rules in this context.

Two recent Circuit Court decisions, *Simmons v. Commissioner* and *Kaufman v. Commissioner*, are also discussed.[6] Although those decisions do not directly address the extinguishment regulation, this Article explains that they undermine the IRS's efforts to enforce the perpetuity requirements in section 170(h) and the regulations, and open the door to loss of the federal investment in conservation easements and significant abuse.

This Article concludes that the IRS's strategy of relying on litigation to establish clear rules consistent with Congressional intent in this context appears unlikely to be successful, and another approach is needed. The Article recommends that the Treasury Department and the IRS clarify the regulations and issue other forward-looking guidance regarding the manner in which taxpayers must satisfy the critically important protected-in-perpetuity requirements if they wish to continue to benefit from generous (generally six-figure) deductions.[7] Without clear uniform rules addressing

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6. Commissioner v. Simmons, 646 F.3d 6 (D.C. Cir. 2011); Kaufman v. Commissioner (*Kaufman III*), 687 F.3d 21 (1st Cir. 2012).

7. The following chart indicates the number of donations of conservation easements encumbering land in the year designated and the average amount per donation:

Year	Number of Donations	Average Amount Per Donation
2005	2,307	$787,062
2006	3,529	$422,092
2007	2,405	$812,369
2008	3,158	$372,925
2009	2,102	$463,073

See Pearson Liddell & Janette Wilson, *Individual Noncash Contributions, 2009*, STAT. OF INCOME BULL., Spring 2012, at 63; Pearson Liddell & Janette Wilson, *Individual Noncash Contributions, 2008*, STAT. OF INCOME BULL., Winter 2011, at 77; Pearson Liddell & Janette Wilson, *Individual Noncash Contributions, 2007*,

the transfer, amendment, and extinguishment of tax-deductible conservation easements, the purportedly perpetual protections provided by such easements will erode over time, and the enormous public investment in these instruments will be lost.[8]

II. *CARPENTER* ON EXTINGUISHMENT

In *Carpenter*, the IRS challenged over $2.7 million of charitable income tax deductions claimed with respect to a number of conservation easements donations.[9] The taxpayers involved had acquired parcels of land located in Teller County, Colorado, from a limited liability company and shortly thereafter donated conservation easements encumbering the land to a Colorado land trust.[10] The conservation easement deeds were virtually identical and contained the following provision addressing extinguishment:

> *Extinguishment* – If circumstances arise in the future such that render the purpose of this Conservation Easement impossible to accomplish, this Conservation Easement can be terminated or extinguished, whether in whole or in part, by judicial proceedings, *or by mutual written agreement of both parties*, provided no other parties will be impacted and no laws or regulations are violated by such termination. . . .[11]

The IRS sent a notice of deficiency to each taxpayer disallowing the claimed deductions on the ground that the conservation easement donations failed to comply with the requirements under section 170.[12] Each of the taxpayers timely filed a petition with the Tax Court and their cases were consolidated.[13]

The IRS filed a motion for partial summary judgment in the Tax Court arguing that the conservation purposes of the taxpayers' conservation easements were not protected in perpetuity as required by section 170(h)(5)(A) because the deeds permit the parties to extinguish the

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STAT. OF INCOME BULL., Spring 2010, at 53; Pearson Liddell & Janette Wilson, *Individual Noncash Contributions, 2006*, STAT. OF INCOME BULL., Summer 2009, at 68; Janette Wilson, *Individual Noncash Contributions, 2005*, STAT. OF INCOME BULL., Spring 2008, at 69.

8. *See supra* note 5.

9. *See* Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1002, T.C.M. (RIA) ¶ 2012-001 at 2 (2012).

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.*

easements by mutual agreement.[14] In particular, the IRS argued that the taxpayers failed to satisfy the requirements of Regulation section 1.170A-14(g)(6)(i) (the extinguishment regulation), which provides:

> *Extinguishment – (i) In general*. If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation . . . can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined [as provided in Regulation section 1.170A-14(g)(6)(ii) (the proceeds regulation)[15]]) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.[16]

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14. *Carpenter*, 103 T.C.M. (CCH) at 1002, T.C.M. (RIA) ¶ 2012-001 at 3.

15. The proceeds regulation provides:

> *Proceeds* – In the case of a donation made after February 13, 1986, for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time . . . . [T]hat proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give[s] rise to the extinguishment of a perpetual conservation restriction under [the extinguishment regulation] paragraph . . . , the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

Reg. § 1.170A-14(g)(6)(ii).

16. The regulations contain numerous additional requirements intended to ensure that a tax-deductible conservation easement will be enforceable in perpetuity and its conservation purpose protected in perpetuity, including:

(i) the "restriction on transfer" requirement, *see* Reg. § 1.170A-14(c)(2);
(ii) the "no inconsistent use" requirement, *see* Reg. § 1.170A-14(e)(2);
(iii) the "general enforceable in perpetuity" requirement, *see* Reg. § 1.170A-14(g)(1);
(iv) the "mortgage subordination" requirement, *see* Reg. § 1.170A-14(g)(2);

The taxpayers made two arguments in response: the "so-remote-as-to-be-negligible" argument and an argument based on the state law doctrine of *cy pres*.[17] Because the IRS moved for partial summary judgment, it bore the burden of proof, and the court was required to infer facts in the manner most favorable to the taxpayers.[18] The taxpayers nonetheless lost on both counts.

A. *So-Remote-As-to-Be-Negligible Argument*

The taxpayers' first argument was based on Regulation section 1.170A-14(g)(3) (the so-remote-as-to-be-negligible regulation), which provides:

> A deduction shall not be disallowed . . . merely because the interest which passes to, or is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible.

The taxpayers claimed that summary judgment was inappropriate because there was a material question of fact as to whether the possibility of extinguishment in accordance with the terms of the easement deeds was so remote as to be negligible.[19] In other words, the taxpayers argued that failure to comply with the extinguishment regulation could be excused if it could be shown that, despite such failure, the possibility of extinguishment was so remote as to be negligible.

(iv) the "mining restrictions" requirement, *see* Reg. § 1.170A-14(g)(4);
(v) the "baseline documentation" requirement, see Reg. § 1.170A-14(g)(5)(i); and
(v) the "donee notice," "donee access," and "donee enforcement" requirements, *see* Reg. § 1.170A-14(g)(5)(ii).

For a detailed discussion of these requirements and the legislative history of section 170(h), see Nancy A. McLaughlin, *Internal Revenue Code Section 170(h): National Perpetuity Standards for Federally Subsidized Conservation Easements, Part 1: The Standards*, 45 REAL PROP. TR. & EST. L.J. 473 (2010) [hereinafter McLaughlin, *National Perpetuity Standards, Part 1*].

17. *Carpenter*, 103 T.C.M. (CCH) at 1003, T.C.M. (RIA) ¶ 2012-001 at 3–4.

18. 103 T.C.M. (CCH) at 1002, T.C.M. (RIA) ¶ 2012-001 at 3.

19. 103 T.C.M. (CCH) at 1003, T.C.M. (RIA) ¶ 2012-001 at 4.

The Tax Court disagreed. Citing its previous holding in *Kaufman v. Commissioner* (*Kaufman II*),[20] the court stated that the so-remote-as-to-be-negligible standard does not modify the extinguishment regulation.[21] Accordingly, the IRS is not required to make a showing with respect to the possibility of extinguishment in determining whether an easement complies with the extinguishment regulation. The court explained that the issue was not whether there was a possibility that events could occur that would trigger the easement deeds' extinguishment provision, but whether, upon the happening of such events, the ability to extinguish the easements as provided in the deeds — by mutual agreement of the parties — violated the requirements of the extinguishment regulation.[22] Thus, although there was a genuine issue of material fact as to whether circumstances could arise that would trigger the easement deeds' extinguishment provision, it did not preclude the entry of summary judgment on the issue of whether the donations failed to comply with the extinguishment regulation. As the court explained: "Disputes over material facts that are not outcome determinative do not preclude the entry of summary judgment."[23]

In a subsequent case, *Mitchell v. Commissioner*, the Tax Court similarly held that the so-remote-as-to-be-negligible standard could not be applied to excuse the taxpayer's failure to comply with the regulations' mortgage subordination requirement.[24] The court also took the opportunity to review the decisions that had been rendered thus far on the so-remote-as-to-

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20. Kaufman v. Commissioner (*Kaufman II*), 136 T.C. 294 (2011), *vacated and remanded in part on other grounds*, *Kaufman III*, 687 F.3d 21 (1st Cir. 2012).

21. *Carpenter*, 103 T.C.M. (CCH) at 1002-03, T.C.M. (RIA) ¶ 2012-001 at 4–5.

22. *Id.*, 103 T.C.M. (CCH) at 1003, T.C.M. (RIA) ¶ 2012-001 at 4.

23. *Id.*, 103 T.C.M. (CCH) at 1003-04, T.C.M. (RIA) ¶ 2012-001 at 4–5 (citing Anderson v. Libberty Lobby, Inc., 477 U.S. 242, 248 (1986)).

24. Mitchell v. Commissioner, Tax Ct. Rep. (CCH) Dec. 59, 013, Tax Ct. Rep. (RIA) Dec. 138.16 (2012). Regulation section 1.170A-14(g)(2), the mortgage subordination regulation, provides that "no deduction will be permitted . . . for an interest in property which is subject to a mortgage unless the mortgagee subordinates its rights in the property to the right of the qualified organization to enforce the conservation purposes of the gift in perpetuity." In *Mitchell*, the conservation easement donor failed to obtain a subordination agreement from the holder of an outstanding mortgage on the subject property until two years following the donation. The donor argued that such failure could be excused because the probability that the donor would have defaulted on the mortgage (and the easement would be eliminated) during the two year period was so remote as to be negligible. The Tax Court rejected that argument, noting that the requirements of the mortgage subordination regulation are strict requirements that may not be avoided by invoking the so-remote-as-to-be-negligible standard.

Id., Tax Ct. Rep. (CCH) Dec. 59, 013, at 4637, Tax Ct. Rep. (RIA) Dec. 138.16, at 195.

be-negligible issue. It explained that the so-remote-as-to-be-negligible standard could not be used to avoid the mortgage subordination requirement of Regulation section 1.170A-14(g)(2),[25] the judicial proceeding requirement of Regulation section 1.170A-14(g)(6)(i),[26] or the proceeds requirement of Regulation section 1.170A-14(g)(6)(ii).[27]

The Tax Court in *Mitchell* also held that the D.C. Circuit's holding in *Commissioner v. Simmons* was distinguishable.[28] In *Simmons*, the IRS argued that two façade easements failed the perpetuity requirement in section 170(h) because each easement deed provided that the holder had the right to consent to changes or abandon some or all of its rights under the easement. The D.C. Circuit held for the taxpayers, in part because it found that the possibility the donee would abandon its rights under the easements was so remote as to be negligible.[29] In distinguishing *Simmons*, the Tax Court in *Mitchell* explained that the D.C. Circuit applied the so-remote-as-to-be-negligible standard "to defeat *a general argument* made by the Commissioner as to the conservation easement's grant in perpetuity;" the D.C. Circuit did not apply that standard to defeat a specific subparagraph of Regulation section 1.170A-14(g).[30]

Carpenter and *Mitchell* suggest that it is unlikely the so-remote-as-to-be-negligible standard can be successfully invoked to avoid any of the specific requirements set forth in section 170(h) and the regulations. That would be both appropriate and sensible. The specific requirements in section 170(h) and the regulations establish bright-line rules that promote efficient and equitable administration of the federal tax incentive program. If individual taxpayers could fail to comply with those requirements and claim that their donations are nonetheless deductible because the possibility of defeat of the gift is so remote as to be negligible, the IRS and the courts would be required to engage in an almost endless series of probability assessments with regard to each individual conservation easement donation. By including specific requirements in section 170(h) and the regulations,

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25. *See id*.

26. *See id.*, Tax Ct. Rep. (CCH) Dec. 59,013, at 4636–37, Tax Ct. Rep. (RIA) Dec. 138.16 at 194–95 (citing to *Kaufman II*, 136 T.C. 294; *Carpenter*, 103 T.C.M. (CCH) 1001, T.C.M. (RIA) ¶ 2012-001).

27. *See id.* (citing to *Kaufman II*, 136 T.C. 294; *Carpenter*, 103 T.C.M. (CCH) 1001, T.C.M. (RIA) ¶ 2012-001).

28. *Mitchell*, Tax Ct. Rep. (CCH) Dec. 59, 013, at 4637, Tax Ct. Rep. (RIA) Dec. 138.16 at 195; Commissioner v. Simmons, 646 F.3d 6 (2011).

29. *Simmons*, 646 F.3d at 11–12. *See infra* Part III for a critique of *Simmons*.

30. *Mitchell*, Tax Ct. Rep. (CCH) Dec. 59, 013, at 4637, Tax Ct. Rep. (RIA) Dec. 138.16 at 195 (emphasis added).

Congress and the Treasury Department presumably intended to avoid just such inquiries.[31]

Subsequent to *Mitchell*, however, the First Circuit vacated *Kaufman II* in part in *Kaufman v. Commissioner* (*Kaufman III*) and reintroduced some confusion and uncertainty regarding the so-remote-as-to-be-negligible standard.[32] On the one hand, the First Circuit appeared to agree with the Tax Court that the so-remote-as-to-be-negligible standard cannot be invoked to cure a failure to comply with the extinguishment or proceeds regulations. In *Kaufman II*, the Tax Court held that a mortgage subordination agreement obtained in connection with the donation of a façade easement impermissibly qualified the provision included in the easement deed to satisfy the proceeds regulation.[33] In vacating that holding in *Kaufman III*, the First Circuit specifically noted that it was *not* relying on the so-remote-as-to-be-negligible regulation "because, as the Tax Court noted [in *Kaufman II*], '[o]ne does not satisfy the extinguishment provision . . . merely by establishing that the possibility of a change in conditions triggering judicial extinguishment is unexpected.'"[34]

On the other hand, in agreeing with the D.C. Circuit's holding in *Simmons* that a grant to the holder of the right to consent to changes or abandon the easement does not render the easement nondeductible, the First Circuit in *Kaufman III* cited to *Simmons* for the proposition that "deductions 'cannot be disallowed based upon the remote possibility [that the donee organizations] will abandon the easements.'"[35] That quoted statement suggests that taxpayers might be able to invoke the so-remote-as-to-be-negligible standard to cure failures to comply with the requirements of section 170(h) and the regulations in some circumstances. That suggestion is unfortunate given that the D.C. Circuit's reasoning underlying the quoted statement was flawed,[36] as well as the earlier noted rationale for not

31. *See also id.* ("The drafters of [the mortgage subordination requirement] saw taxpayers defaulting on their mortgages as more than a remote possibility. Therefore they drafted a specific provision which would absolutely prevent a default from destroying a conservation easement's grant into perpetuity.").

32. *Kaufman III*, 687 F.3d 21 (1st Cir. 2012).

33. *Kaufman II*, 136 T.C. at 310–13, *vacated and remanded in part*, *Kaufman III*, 687 F.3d 21. The proceeds regulation is reproduced *supra* note 15.

34. *Kaufman III*, 687 F.3d at 27.

35. *Id*. at 28.

36. The D.C. Circuit inappropriately relied on Stotler v. Commissioner, 53 T.C.M. (CCH) 973, T.C.M. (P-H) ¶ 87, 275 (1987), which interprets the 1979 version of the deduction provision, rather than section 170(h) and the regulations. *See* Simmons v. Commissioner, 646 F.3d. 6, 10–11 (D.C. Cir. 2011). It was not until 1980 that Congress, in response to concerns about abuse, added the protected-in-perpetuity requirement to the deduction provision and provided significant guidance regarding the meaning of that new requirement in the legislative history, much of

permitting the so-remote-as-to-be-negligible standard to be so invoked. As discussed in Part IV, along with addressing other concerns relating to the holdings in *Simmons* and *Kaufman III*, the Treasury Department and the IRS should revise the regulations or issue other guidance clarifying that the so-remote-as-to-be-negligible standard cannot, under any circumstances, be invoked to cure a failure to comply with the specific requirements of section 170(h) and the regulations.

B. Cy Pres *Argument*

As an alternative to their so-remote-as-to-be-negligible argument, the taxpayers in *Carpenter* made an argument based on the state law doctrine of *cy pres*. They argued that (1) the easement donations created charitable trusts or constituted restricted charitable gifts, and (2) the doctrine of *cy pres* thus applied, and extinguishment of the easements would therefore require a judicial proceeding despite the fact that the deeds expressly grant the parties the right to extinguish by mutual agreement.[37] The Tax Court addressed these two assertions in turn.

1. Tax-Deductible Easements as Restricted Gifts

Because the highest court in Colorado had not yet ruled on whether the gift of a perpetual conservation easement to a charitable organization constitutes a charitable trust or a restricted charitable gift, the Tax Court applied what it found to be Colorado law "after giving proper regard to relevant rulings of other courts of the state."[38] While the court determined that the taxpayers had not created charitable trusts as a result of their gifts of the easements, it held that such gifts *did* constitute restricted gifts.[39] The

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which was incorporated into the regulations, which were not issued until 1986. *See* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 475–86 (explaining the history of the deduction provision). Accordingly, the D.C. Circuit's reliance on *Stotler,* which interprets the 1979 version of the deduction provision, as authority for the interpretation of the protected-in-perpetuity requirement, which was not enacted until 1980, and Regulation section 1.170A-14(g)(1), which was not issued until 1986, was inappropriate. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 14–15 (discussing this point in more detail). The D.C. Circuit also did not recognize that the change and abandonment proviso was an impermissible qualification of the restriction on transfer provision included in the deed to satisfy Regulation section 1.170A-14(c)(2). *See infra* note 193 and surrounding text.

37. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1004, T.C.M. (RIA) ¶ 2012-001 at 5 (2012).

38. *Id.*, 103 T.C.M. (CCH) at 1004, T.C.M. (RIA) ¶ 2012-001 at 5.

39. *Id.*, 103 T.C.M. (CCH) at 1004-05, T.C.M. (RIA) ¶ 2012-001 at 5–6.

court explained that restricted gifts are "contributions conditioned on the use of a gift in accordance with the donor's precise directions and limitations."[40] The court also noted that at least one commentator has argued that conservation easements eligible for federal charitable contribution income tax deductions are, by definition, charitable gifts made for a specific purpose, i.e., restricted gifts.[41]

The Tax Court explained that the gifts of the conservation easements were restricted gifts because the "'deeds restricted Greenlands' use of the gifts to 'preserve and protect in perpetuity the Conservation Values of the Property for the benefit of this generation and generations to come.'"[42] In other words, the easements were not donated to Greenlands to be used or disposed of as it might see fit in accomplishing its general charitable conservation mission. Rather, each easement was donated to Greenlands for a specific charitable purpose — the protection of the particular property encumbered by the easement for the conservation purposes set forth in the deed in perpetuity. Accordingly, the gifts of the easements constituted restricted gifts, and Greenlands is required to administer those gifts "in accordance with the donor's precise directions and limitations."[43]

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40. *Id*., 103 T.C.M. (CCH) 1004, T.C.M. (RIA) ¶ 2012-001 at 6 (quoting Michael M. Schmidt & Taylor T. Pollock, *Modern Tomb Raiders: Nonprofit Organizations' Impermissible Use of Restricted Funds*, 31 COLO. LAW. 57, 58 (2002)).

41. *Id*. (citing McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 23). McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5 at 23, explains:

> Conservation easements eligible for federal charitable income tax deductions are also, by definition, charitable gifts made for a specific purpose — the protection of the particular property encumbered by the easement for one or more of the conservation purposes enumerated in section 170(h) in perpetuity. Under state law, the donee of a charitable gift made for a specific purpose must administer the gift consistent with its stated terms and charitable purpose.

For a discussion of the principles applicable to restricted charitable gifts in the conservation easement context, see, e.g., Nancy A. McLaughlin, *Amending Perpetual Conservation Easements: A Case Study of the Myrtle Grove Controversy*, 40 U. RICH. L. REV. 1031 (2006); Nancy A. McLaughlin & W. William Weeks, Hicks v. Dowd, *Conservation Easements, and the Charitable Trust Doctrine: Setting the Record Straight*, 10 WYO. L. REV. 73 (2010) [hereinafter McLaughlin & Weeks, *Setting the Record Straight*]; Nancy A. McLaughlin, *Conservation Easements: Perpetuity and Beyond*, 34 ECOLOGY L. Q. 673 (2007) [hereinafter McLaughlin, *Conservation Easements: Perpetuity and Beyond*].

42. *Carpenter*, 103 T.C.M. (CCH) at 1004, T.C.M. (RIA) ¶ 2012-001 at 6.

43. Charitable gifts made to government entities and charitable organizations can be either restricted or unrestricted. An *unrestricted charitable gift*

The court's holding that the conservation easements did not constitute charitable trusts but *did* constitute restricted gifts highlights an issue that sometimes creates confusion. In some states, gifts made to charitable corporations for specific purposes are referred to as charitable trusts.[44] In other states, such gifts are referred to as absolute, conditional, or restricted gifts, rather than technical trusts.[45] Regardless of the label, however, the recipient corporation must administer the gift in accordance with the terms and purpose specified by the donor.[46] A leading case in this context explains:

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is a contribution of money or property that the donor makes without attaching any conditions on its use by the recipient entity or organization. An entity or organization in receipt of an unrestricted charitable gift is free to use that gift as it sees fit in accomplishing its general public or charitable mission. The typical unrestricted charitable gift is the fifty dollar check written to a favorite charity at the end of the calendar year or the twenty dollar bill dropped in the church collection plate on Sunday, both of which the donor intends will be used by the recipient organization as it sees fit in accomplishing its general charitable mission. Unrestricted charitable gifts of land are commonly called "tradelands," reflecting that the land can be sold and the proceeds used by the charity in accomplishing its general charitable mission. A *restricted charitable gift*, in contrast, is a contribution of money or property that the donor makes to a government entity or charitable organization to be used for a specific charitable purpose and often according to carefully negotiated terms. *See, e.g.*, John K. Eason, *The Restricted Gift Life Cycle, or What Comes Around Goes Around*, 76 FORDHAM L. REV. 693, 698, 708–09 (2007) (restricted charitable gifts give rise to trust or trust-like duties, in particular the duty to abide by the terms of the gift).

44. *See, e.g.*, Chattowah Open Land Trust v. Jones, 636 S.E.2d 523, 525–27 (Ga. 2006) (devise of testator's residence and surrounding acreage to a land trust for the purpose of maintaining the property in perpetuity exclusively for conservation purposes within the meaning of section 170(h) "unambiguously created a charitable trust" and testator's failure to use the term "trust" or "trustee" did not alter the outcome as strict use of those terms is not required to establish a trust).

45. *See, e.g.*, George W. Vallery Mem. Fund. v. Saint Luke's Cmty. Found., 883 P.2d 24, 28 (Colo. App. 1993) (referring to a bequest for a specific charitable purpose as "an outright but restricted gift rather than a trust," and an "absolute bequest to a charitable organization").

46. *See, e.g.*, Lefkowitz v. Lebensfeld, 68 App.Div.2d 488, 496 (1979) ("These cases reflect the never disturbed equitable doctrine that although gifts to a charitable organization do not create a trust in the technical sense, where a purpose is stated a trust will be implied, and the disposition enforced by the Attorney-General, pursuant to his duty to effectuate the donor's wishes."); St. Joseph's Hosp. v. Bennett, 22 N.E.2d 305, 308 (N.Y. 1939) (while "[n]o trust arises . . . in a technical sense" a charitable corporation "may not . . . receive a gift made for one purpose and use it for another . . . .").

> "[e]quity will afford protection to a donor to a charitable corporation in that the [a]ttorney [g]eneral may maintain a suit to compel the property to be held for the charitable purpose for which it was given to the corporation" . . . . "The general rule is that charitable trusts *or* gifts to charitable corporations for stated purposes are [enforceable] at the instance of the [a]ttorney [g]eneral . . . . It matters not whether the gift is absolute or in trust or whether a technical condition is attached to the gift."
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> "The theory underlying the power of the [a]ttorney [g]eneral to enforce gifts for a stated purpose is that a donor who attaches conditions to his gift has a right to have his intention enforced."[47]

The difference in terminology used to describe gifts made to charitable corporations for specific purposes can be traced to a time in U.S. history when charitable trusts were not valid in some states.[48] During this

47. Carl J. Herzog Found. v. Univ. of Bridgeport, 699 A.2d 995, 997–98 (Conn. 1997) (quoting *Lefkowitz*, 68 App.Div.2d at 494–95 (1979) (emphasis added). *See also, e.g.*, SCOTT & ASCHER ON TRUSTS § 37.1.1 (5th ed. 2009) ("many of the principles that apply to charitable trusts also apply to charitable corporations. In both cases, the Attorney General can maintain a suit to prevent diversion of the property to purposes other than those for which it was given. Likewise, in both cases, cy pres may be available"). A few of the procedural rules applicable to trusts do not apply in the case of gifts to charitable corporations. *See, e.g.*, Evelyn Brody, *From the Dead Hand to the Living Dead: The Conundrum of Charitable-Donor Standing*, 41 GA. L. REV. 1183, 1209 (2007) ("[A] restricted gift . . . does not impose on the corporate charity the trust law procedural requirements for providing information to beneficiaries (although the charity would have to respond to a request for information from the attorney general) [or] for judicial accounting.").

48. *See, e.g.*, James J. Fishman, *The Development of Nonprofit Corporation Law and an Agenda for Reform*, 34 EMORY L.J. 617, 624–30, 652 (1985) [hereinafter Fishman, *Development*] (describing "the tangled history of the charitable trust in this country"); J. W. Oler, Annotation, *Nature of Estate Created by, and Enforceability of, Provision in Devise or Bequest to Charitable, Religious, or Educational Corporation as to Particular Purpose of the Corporation for Which It Shall Be Used*, 130 A.L.R. 1101 (2012) [hereinafter Oler, *Nature of Estate*] ("[S]ome jurisdictions early adopted the view that charitable trusts were invalid as lacking beneficiaries definite enough to enforce the trust . . . . [S]uch trusts [also] were not everywhere recognized as being immune from restrictions against perpetuities."). For an interesting discussion of the evolution of the laws governing charitable conveyances in the United States, see Note, *The Enforcement of Charitable Trusts in America: A History of Evolving Social Attitudes*, 54 VA. L. REV. 436 (1968).

period, courts in these states validated gifts made to charitable corporations for specific purposes by resorting to the expediency of characterizing such gifts as absolute or conditional, rather than as technical trusts.[49] Such gifts, however, still had to be applied to the particular purpose specified by the donor, the term "absolute" in this context meaning "not in trust" (and therefore not invalid), rather than that the gift was conveyed to the donee to be used in its discretion for any of its general purposes (i.e., absolute did not mean unrestricted).[50] Old habits die hard, and courts in some states continue today to characterize gifts made to charitable corporations for specific purposes as absolute or conditional, rather than as trusts, even though charitable trusts are now valid in all fifty states.[51] For convenience and

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49. Professor Fishman explains:

> To sustain a charitable bequest in the nineteenth century in states such as New York, courts had to find an intent to make an absolute gift to the specific corporation for its proper purposes, rather than an attempt to create a trust for indefinite and uncertain beneficiaries. To avoid a forfeiture of a testator's intent, courts engaged in the most tortuous reasoning to find that an absolute gift was intended to the corporation, even when the instrument used such precise terminology as: "I give, devise and bequeath . . . to . . . in trust. . . ."

Fishman, *Development*, *supra* note 48, at 629. *See also, e.g.,* Oler, *Nature of Estate*, *supra* note 48 ("In Minnesota uses and trusts were abolished by statute, except as therein specifically authorized . . . . Circumvention of the effect of this statute, in order to validate a testator's charitable disposition to a corporation for a corporate purpose, was accomplished . . . by adoption of the convenient view that such a gift was not in trust, but was 'absolute' or on condition."). The court in *Lefkowitz v. Lebensfeld*, 68 App.Div.2d 488, 494–95 (1979), describes the history of the development of the law in this context in New York.

50. *See, e.g.*, *St. Joseph's Hosp.*, 22 N.E.2d at 307 ("even when the courts found that a gift to a charitable corporation for a corporate purpose was an 'absolute' gift and not a trust, they also indicated that directions in regard to the manner in which the gift was to be held and used would be enforced").

51. MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW REGULATION 47 (2004). In an attempt to reduce the confusion caused by the different labeling of gifts made to charitable corporations for specific purposes, the American Law Institute's Restatement (Third) of Trusts provides that all such gifts constitute "charitable trusts," while the Institute's Principles of the Law of Nonprofit Organizations (Tentative Draft) takes the opposite tack and provides that all such gifts are "restricted gifts." *See* RESTATEMENT (THIRD) OF TRUSTS § 28 cmt. a (2003); PRINCIPLES OF THE LAW OF NONPROFIT ORGANIZATIONS § 400 (Tentative Draft No. 2, Mar. 18, 2009). While such attempts to reduce the confusion are laudable, they presumably would be more effective if the Institute took a consistent position. It also seems likely that state courts will continue to use the different terminology based on precedent in any event.

descriptive purposes, gifts made to charitable corporations for specific purposes are often simply referred to as "restricted gifts,"[52] and they will be referred to as such in the remainder of this article.

The status of federally subsidized conservation easements as restricted gifts is key for a number of reasons. First, such status ensures that nonprofit and government holders will be required under state law to administer the easements "in accordance with the donor's precise directions and limitations" — that is, in accordance with the specific provisions of the easements, many of which will have been included to comply with federal tax law requirements.[53] If the provisions included in a conservation easement to satisfy federal tax law requirements are not legally binding on the parties to the easement, they would constitute mere window dressing and the conservation purposes of the contributions would not be protected in perpetuity as mandated by Congress.[54]

Second, restricted gift status ensures that the state attorney general will have standing to call holders to account for failing to administer conservation easements consistent with their stated terms and purposes. Although the IRS has a few arrows in its quiver, such as the power to revoke the tax-exempt status of a nonprofit (but not governmental) holder that confers an impermissible private benefit on a property owner through the modification or termination of a conservation easement,[55] it is not clear that

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52. *See generally, e.g.*, PRINCIPLES OF THE LAW OF NONPROFIT ORGANIZATIONS § 400 (Tentative Draft No. 2, Mar. 18, 2009), discussed *supra* note 51; Michael M. Schmidt & Taylor T. Pollock, *Modern Tomb Raiders: Nonprofit Organizations' Impermissible Use of Restricted Funds*, 31 COLO. LAW. 57 (2002).

53. *See* CONSERVATION EASEMENT HANDBOOK: MANAGING LAND CONSERVATION AND HISTORIC PRESERVATION EASEMENT PROGRAMS 160–61 (Janet Diehl & Thomas S. Barrett eds., 1988) [hereinafter Diehl, 1988 CONSERVATION EASEMENT HANDBOOK] (providing a checklist of "Provisions Relating to IRS Requirements"); Thomas S. Barrett & Stefan Nagel, MODEL CONSERVATION EASEMENT AND HISTORIC PRESERVATION EASEMENT, 1996: REVISED EASEMENTS AND COMMENTARY FROM "THE CONSERVATION EASEMENT HANDBOOK" 11 (1996) [hereinafter Barrett, 1996 CONSERVATION EASEMENT HANDBOOK] (same); ELIZABETH BYERS & KARIN MARCHETTI PONTE, THE CONSERVATION EASEMENT HANDBOOK 313–14 (2d ed. 2005) [hereinafter Byers, 2005 CONSERVATION EASEMENT HANDBOOK] (same).

54. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 20.

55. *See, e.g.*, I.R.S. Priv. Ltr. Rul. 201110020 (March 11, 2011) (revoking an organization's tax-exempt status in part because the organization agreed to amend a conservation easement to permit additional development on the subject property and thereby conferred a private benefit on the landowner). *But see* Nancy A. McLaughlin & W. William Weeks, *In Defense of Conservation Easements: A Response to The End of Perpetuity*, 9 WYO. L. REV. 1, 75–78 (2009) [hereinafter McLaughlin & Weeks, *In Defense of Conservation Easements*] (explaining that

the IRS has the ability, even if it had the resources and desire, to sue to enjoin improper modifications or terminations or to have such actions declared null and void. That task falls primarily to the state attorney general, who supervises the administration of charitable assets in the state on behalf of donors and the public.[56] Accordingly, state attorneys general play a critical role in ensuring that tax-deductible perpetual conservation easements are administered in accordance with their stated terms and purposes over the long term.[57]

Restricted gift status also means that (1) state courts are likely to interpret tax-deductible conservation easements in favor of accomplishing their charitable conservation purposes, rather than in favor of the free use of land;[58] (2) tax-deductible easements may be excluded from the bankruptcy estates of donee charitable corporations;[59] (3) actions to recover tax-

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denying a holder "eligible donee" or "tax-exempt" status are relatively toothless sanctions when it comes to ensuring that conservation easements are administered in accordance with their terms and purposes over the long term). The tax benefit rule is also of limited usefulness because it would apply only in limited circumstances (i.e., where the transaction financially benefits the original donor). *See, e.g.*, MARTIN J. MCMAHON, JR. & LAWRENCE A. ZELENAK, FEDERAL INCOME TAXATION OF INDIVIDUALS 3.07[1] (2ND ED. 2012).

56. *See* FREMONT-SMITH, *supra* note 51, at 305–07. *See also* Nancy A. McLaughlin & W. William Weeks, Salzburg v. Dowd*: Another Look*, 33 WYO. LAW. 50, 52 (2010) (explaining that the IRS is charged with enforcing federal tax laws, while state attorneys general and state courts are charged with ensuring that charitable gifts are administered in accordance with their stated terms and purposes, and it is therefore no surprise that the IRS was not involved in any of the cases to date involving the improper modification or termination of conservation easements).

57. *See, e.g.*, McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 39–42 (discussing *Salzburg v. Dowd*, in which the Wyoming Attorney General filed suit objecting to a Wyoming County's termination of a tax-deductible easement at the request of new owners of the land); *id.* at 28–30 (discussing the Myrtle Grove controversy, in which the Maryland Attorney General filed suit objecting to a land trust's amendment of a tax-deductible conservation easement to allow a seven-lot upscale development on the protected property).

58. *See, e.g.*, Jackson v. Phillips, 96 Mass. 539, 550, 556 (1867) ("[G]ifts to charitable uses are highly favored, and will be most liberally construed in order to accomplish the intent and purpose of the donor. . . . If the words of a charitable bequest are ambiguous or contradictory, they are to be so construed as to support the charity, if possible."); Board of Trs. of Univ. of N. C. v. Unknown Heirs, 319 S.E.2d 239, 242 (N.C. 1984) ("It is a well recognized principle that gifts and trusts for charities are highly favored by the courts. Thus, the donor's intentions are effectuated by the most liberal rules of construction permitted.").

59. *See, e.g.*, Evelyn Brody, *The Charity in Bankruptcy and Ghosts of Donors Past, Present, and Future*, 29 SETON HALL LEGIS. J. 471, 472 (2005) ("[T]he courts will try to identify those charitable assets that are restricted in such a manner that they survive the bankruptcy proceeding.").

deductible easements that have been improperly transferred, released, modified, or terminated may not be barred by laches or the statute of limitations;[60] (4) conservation easements should not be extinguished pursuant to the doctrine of merger if the government or nonprofit holder acquires title to the subject land because the required "unity of ownership" generally will not be present;[61] and (5) attempts by state legislatures to alter the terms of existing tax-deductible easements may be found unconstitutional on a number of grounds, including the prohibition on impairment of private contracts.[62] Accordingly, restricted charitable gift status provides significant protection of the public interest and investment in tax-deductible conservation easements and is key to the success of the tax-incentive program, which depends on the proper administration and enforcement of the easements over the long term.

2. *Applicability of* Cy Pres

Having found that the conservation easement donations in *Carpenter* constituted restricted gifts, the Tax Court next turned to whether the doctrine of *cy pres* was applicable to such gifts and, if so, whether it prevented the parties from exercising the right granted to them in the deeds to mutually agree to extinguish the easements.[63] The Tax Court correctly determined that the doctrine of *cy pres* was *available* with regard to the gifts of the easements, but it did not prevent the parties from exercising their right to mutually agree to extinguish the easements. As explained below, however, the court's analysis requires some clarification and will hopefully be revised in future decisions.

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60. *See, e.g.*, Tauber v. Virginia, 499 S.E.2d. 839, 845 (Va. 1998) (laches may not be pled successfully as a defense in an equitable proceeding to bar the state attorney general from asserting a claim on behalf of the public to insure that charitable assets are distributed in accord with the charitable purposes to which they should have been devoted); Trs. of Andover Theological Seminary v. Visitors of Theological Inst. in Phillips Acad. in Andover, 148 N.E. 900, 918 (Mass. 1925) ("Generally it is true that no length of time of diversion from the plain provisions of a charitable foundation will prevent its restoration to its true purpose.").

61. *See* Nancy A. McLaughlin, *Conservation Easements and The Doctrine of Merger*, 74 LAW & CONTEMP. PROBS 279 (2011) (explaining that the two estates would be "in the same person at the same time," but generally would *not* be held "in the same right").

62. *See, e.g.*, McLaughlin & Weeks, *In Defense of Conservation Easements*, *supra* note 55, at 88–91 (gathering the relevant authorities).

63. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1004-05, T.C.M. (RIA) ¶ 2012-001 at 6–7 (2012).

(i) Availability with Regard to Restricted Gifts

The Tax Court first determined that, under Colorado law, "'even in the absence of a formal trust, the doctrine of *cy pres* is available when there is an absolute bequest to a charitable organization.'"[64] Thus, the doctrine of *cy pres* was *available* with respect to the restricted gifts of the conservation easements. This holding is unremarkable and consistent with the laws governing restricted gifts.[65]

(ii) Cy Pres *Process*

The Tax Court next described the doctrine of *cy pres*:

> [1] If property is given . . . to be applied to a particular charitable purpose, and it is or becomes impossible or impracticable or illegal to carry out the particular purpose, and [2] . . . the settlor manifested a more general intention to devote the property to charitable purposes, [3] the [gift] will not fail but the Court will direct the application of the property to some charitable purpose which falls within the general charitable intention of the settlor.[66]

This three-step process is the traditional form of the *cy pres* doctrine. In the second step, if the court does not find that the donor manifested a general

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64. *Id.*, 103 T.C.M. (CCH) at 1004-05, T.C.M. (RIA) ¶ 2012-001 at 6 (quoting George W. Vallery Mem. Fund. v. Saint Luke's Cmty. Found., 883 P.2d 24, 28 (Colo. App. 1993)). *See also supra* note 50 and accompanying text, (explaining that the term "absolute" in this context means the gift was not technically made "in trust," but the gift is still restricted and the holder is still legally bound to administer the gift in accordance with its stated terms and purpose).

65. *See, e.g.*, UNIFORM TRUST CODE § 413 cmt. (2000) ("The doctrine of cy pres is applied not only to trusts, but also to other types of charitable dispositions, including those to charitable corporations."); RESTATEMENT (SECOND) OF TRUSTS § 348 cmt. f (1959) ("The doctrine of cy pres is applicable to gifts to charitable corporations as well as to gifts to individual trustees for charitable purposes."); SCOTT & ASCHER ON TRUSTS § 37.1.1 (5th ed. 2008) ("[M]any of the principles that apply to charitable trusts also apply to charitable corporations . . . in both cases, cy pres may be available."); BOGERT & CHESTER, THE LAW OF TRUSTS AND TRUSTEES § 431 (3rd ed. 2008) ("The cy pres power is applied to absolute gifts to charitable corporations or other organizations, as well as to gifts in trust; and it applies in the case of transfers by deed.").

66. *Carpenter*, 103 T.C.M. (CCH) at 1005 n.6, T.C.M. (RIA) ¶ 2012-001 at 7 n.6 (quoting Dunbar v Board of Trs. of Clayton College, 461 P.2d 28, 30 (Colo. 1969)).

intention to devote the property that was the subject of the gift to charitable purposes (a "general charitable intent") and, instead, determines that the donor had specific intent to devote the property to only the donor's designated charitable purpose and none other, the court may *not* apply the *cy pres* doctrine to modify the purpose of the gift. In such a circumstance, the charitable gift would "fail," and the property that was the subject of the gift would pass back to the donor or the donor's residuary beneficiaries or intestate heirs.[67]

(iii) General Charitable Intent

The IRS argued that the *cy pres* doctrine was inapplicable to the restricted gifts of the conservation easements because the taxpayers "did not manifest a more general intention to devote the property to charitable purposes."[68] The Tax Court agreed, and this is where its analysis went slightly off track. The court was misled as to the property at issue when analyzing the general charitable intent requirement. In holding that *cy pres* was inapplicable to the gifts of the conservation easements, the court stated:

> [W]e are called upon to determine whether petitioners manifested a more general intent to devote *the property* to a general charitable purpose beyond the restrictions placed in the conservation easement deeds.
>
> . . . .
>
> We do not find that petitioners intended to donate *their property* to Greenlands with a general charitable purpose. The deeds make clear that petitioners wanted to retain all rights over the donated *property* not specifically granted to Greenlands in the conservation easement deeds. Should the purpose of the deeds become impossible to fulfill, petitioners

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67. *See* SCOTT & ASCHER ON TRUSTS § 39.5.3 (5th ed. 2009). For a case in which the court found that the donor lacked a general charitable intent and the charitable gift failed and passed to the donor's heirs, see Evans v. Abney, 224 Ga. 826 (1968), aff'd 396 U.S. 435 (1970)), where Senator Augustus O. Bacon's trust under his will, which left a city park to be used only by white people, was found illegal and impossible of performance, but the doctrine of *cy pres* could not be applied because the Senator did not have a general charitable intent; he left no doubt as to his wish that park be operated only on a segregated basis.

68. *Carpenter*, 103 T.C.M. (CCH) at 1005, T.C.M. (RIA) ¶ 2012-001 at 7. The IRS need not have argued that *cy pres* is inapplicable to the restricted gifts of the conservation easements because, as explained below, even if *cy pres* were determined to be applicable, it would not have prevented the parties from exercising the right granted to them in the deeds to mutually agree to extinguish the easements (i.e., it would not have saved the parties' deductions).

> demonstrated no intention to have the donated *property* put to some other general charitable use.[69]

In its references to the "property" in the foregoing excerpts, the court is referring to the land subject to the conservation easements. However, the property at issue in the *cy pres* analysis is the property that was the subject of the gift and, in *Carpenter*, the property that was the subject of each gift was a conservation easement, not the underlying land. Accordingly, the court should have asked whether the taxpayers manifested a general intent to devote *the easements* (or the value attributable thereto) to charitable purposes should the purposes of the easements ever become impossible or impracticable to carry out.

The answer to that question should have been yes because the easement deeds, consistent with the proceeds requirement of the regulations, contain provisions entitling the holder (Greenlands) to a percentage of the proceeds from the sale, exchange, or involuntary conversion of the property following extinguishment of the easement.[70] Specifically, in the event the purpose of one of the easements becomes impossible to accomplish, the easement is extinguished, and the newly unencumbered property is sold, Greenlands would be entitled to a share of proceeds as compensation for the easement (the property right it holds on behalf of the public) and, as a charity, it would be required to use those proceeds consistent with its

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69. 103 T.C.M. (CCH) at 1005, T.C.M. (RIA) ¶ 2012-001 at 6–7 (emphasis added).

70. *See* Deed of Conservation Easement between Kalyn M. Carpenter, Grantor, and The Greenlands Reserve, Grantee, dated December 24, 2003 (on file with author) at 7, which provides:

> 13. *Extinguishment* – . . . The amount of the proceeds to which Grantee shall be entitled, after the satisfaction of the prior claims, from any sale, exchange, or involuntary conversion of all or any portion of the Property subsequent to such termination or extinguishment, shall be determined, unless otherwise provided by Colorado law at the time[,] in accordance with paragraph 14, below.
>
> 14. *Proceeds* – This Conservation Easement constitutes a real property interest immediately vested in Grantee, which the parties stipulate to have fair market value determined by multiplying the fair market value of the Property unencumbered by the Conservation Easement (minus any increase in value after the date of this grant attributable to improvements) by the ratio of the value of the Conservation Easement at the time of this grant to the value of the Property, without deduction for the value of the Conservation Easement, at the time of the grant.

All of the conservation easement deeds at issue in *Carpenter* were virtually identical. *See Carpenter*, 103 T.C.M. (CCH) at 1002, T.C.M. (RIA) ¶ 2012-001 at 2.

charitable conservation mission.[71] By including provisions in a conservation easement deed tracking the proceeds regulation,[72] an easement donor manifests an intent to devote the easement (the charitable gift), or more accurately, the proceeds attributable to that gift upon extinguishment, to similar charitable purposes, rather than to have the gift "fail" and the proceeds attributable to the gift pass back to the donor or the donor's residuary beneficiaries or intestate heirs.[73] Accordingly, the taxpayers in *Carpenter* should have been found to have manifested a general charitable intent with respect to their gifts of the easements. As explained in the following section, however, that finding would not have saved their deductions.

(iv) Cy Pres *Would Not Have Trumped Parties' Express Right to Extinguish*

Even if the court had found that the taxpayers in *Carpenter* manifested a general charitable intent with respect to their gifts of the easements, it would not have meant that the *cy pres* doctrine operated to mandate a judicial proceeding to extinguish the easements. *Cy pres* would

71. *See* Deed of Conservation Easement between Kalyn M. Carpenter, Grantor, and The Greenlands Reserve, Grantee, dated December 24, 2003 (on file with author) at 7.

72. The proceeds regulation is reproduced *supra* note 15. To fully comply with the regulations, the proceeds provisions in the easements at issue in *Carpenter* should have mandated that the grantee use its share of the proceeds following extinguishment "in a manner consistent with the conservation purposes of the original contribution." *See* Reg. § 1.170A-14(g)(6)(i).

73. *See, e.g.*, Kostarides v. Central Trust Co., 122 N.W.2d 729, 733 (1963) (language in a will providing that, in the event the donor's original charitable purpose becomes partially or wholly impossible, the trustee shall apply the funds to other similar charitable purposes, "discloses a very decided general charitable intent. It is difficult to imagine how it might have been expressed more clearly"). State courts are likely to find that a conservation easement donor had a general charitable intent even if the easement does not contain a proceeds clause. *See* Nancy A. McLaughlin, *Rethinking the Perpetual Nature of Conservation Easements*, 29 HARV. ENVTL. L. REV. 421, 479 (2005) (explaining that state courts almost invariably find that a donor had a general charitable intent if the gift fails after it has been in existence for some period of time, some states apply a presumption of general charitable intent, and some states have abolished the requirement altogether); RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES § 7.11 cmt. b (2000) ("because conservation servitudes are usually intended to be 'perpetual,' finding that the grantor's intent was broad enough to encompass a more general conservation or preservation purpose than the particular use specified in the instrument will ordinarily be justified absent a contrary provision in the document creating the servitude").

still be inapplicable because the deeds expressly dictate what should be done if it becomes impossible to accomplish the donor's charitable conservation purpose (i.e., extinguishment of the easement by judicial proceeding *or* by mutual agreement of the parties and payment of a share of proceeds to Greenlands).[74]

The *cy pres* doctrine does not trump the express terms of a restricted charitable gift. Rather, it operates as a safety valve, allowing a court to step in and modify the purpose of a restricted gift if, over time, the donor's stated purpose becomes impossible or impractical *and the gift does not dictate what should be done in such circumstances*. If the gift does state what should be done in such circumstances, the terms of the gift control.[75] Accordingly, even if the court had found that the taxpayers in *Carpenter* manifested a general charitable intent with respect to their gifts of the easements, the *cy pres* doctrine would not operate to prevent the parties from exercising their right — expressly granted to them in the deeds — to mutually agree to extinguish the easements.

This has important ramifications for tax-deductible conservation easements. In *Kaufman II*, the Tax Court noted that the extinguishment regulation "appears to be a regulatory version of the doctrine of *cy pres*."[76] By incorporating that regulatory version of the *cy pres* doctrine into a conservation easement deed, the donor eliminates the need for the court to apply the state law version of the doctrine to extinguish the easement in the event continued use of the property for conservation purposes becomes impossible or impractical. The provisions of the deed expressly dictate what should be done in such circumstances, and those provisions would control.[77]

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74. *See, e.g.*, *Kostarides*, 122 N.W. 2d at 733 (*cy pres* did not apply because the provision of the will expressly dictated what should be done with the funds if it became impossible to accomplish the donor's charitable purpose in the manner he specified).

75. *See id. See also* RESTATEMENT (THIRD) OF TRUSTS § 67 (2003) ("*Unless the terms of the trust provide otherwise* [the doctrine of cy pres will apply]") (emphasis added); *id.* § 67 cmt. b ("A trust provision expressing the settlor's own choice of an alternative charitable purpose will be carried out, without the need to apply the cy pres doctrine . . . .").

76. *Kaufman II*, 136 T.C. 294, 307 (2011), *vacated and remanded in part on other grounds, Kaufman III*, 687 F.3d 21 (1st Cir. 2012).

77. The state law *cy pres* doctrine might continue to apply to such a conservation easement in one circumstance — if (i) the stated conservation purpose of the easement is narrow (such as to protect grizzly bear habitat), (ii) continuing to protect the subject property for that narrow purpose becomes impossible or impractical due to changed conditions, but (iii) continuing to protect the property for other conservation purposes, such as open space or for public outdoor recreation, is not impossible or impractical. In such a case, a state court might apply the *cy pres*

C. *Conservation Easements Extinguishable by Mutual Agreement Are Not Deductible*

Having found that the *cy pres* doctrine did not operate to prevent the parties from extinguishing the easements by mutual agreement, the Tax Court next turned to whether the ability to extinguish a conservation easement by mutual agreement violates the requirements of the extinguishment regulation. The Tax Court concluded that it does. It held that conservation easements that may be extinguished by mutual agreement of the parties — even if subject to a standard such as "impossibility" — fail as a matter of law to comply with the enforceability in perpetuity requirements under Regulation section 1.170A-14(g) and, thus, are not protected in perpetuity as required under section 170(h)(5)(A).[78]

Although the conservation easements at issue in *Carpenter* expressly provide that they are extinguishable by mutual written agreement of the parties, the Tax Court's analysis is not confined to such circumstances. In an earlier portion of the opinion, the court explained:

> To determine whether the conservation easement deeds comply with requirements for the conservation easement deduction under Federal tax law, we must look to State law to determine the effect of the deeds. State law determines the nature of the property rights, and Federal law determines the appropriate tax treatment of those rights.[79]

The court then looked to Colorado law to determine how conservation easements may be extinguished and noted that, pursuant to the

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doctrine to modify the conservation purpose of the easement, while leaving the easement otherwise intact. Such a modification would be consistent with the extinguishment regulation and, by extension, the terms of a deed incorporating that regulation. The extinguishment regulation does not contemplate that a tax-deductible conservation easement will be extinguished if changed conditions make impossible or impractical the continued use of the property for a narrowly defined conservation purpose. Rather, it appears to impose a much higher bar for extinguishment, requiring that changed conditions have made impossible or impractical the continued use of the property for "conservation purposes" generally. *See* Reg. § 1.170A-14(g)(6)(i). The extinguishment regulation does not, however, provide a mechanism for the modification of the conservation purpose of a conservation easement while leaving the easement intact. It only addresses extinguishment. Accordingly, the state law *cy pres* doctrine could be applied to modify the purpose of the easement in such a circumstance.

78. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1005, T.C.M. (RIA) ¶ 2012-001, 7–8 (2012).

79. *Id*., 103 T.C.M. (CCH) at 1004, T.C.M. (RIA) ¶ 2012-001 at 5.

Colorado easement enabling statute, "[c]onservation easements in gross may, in whole or in part, be released, terminated, extinguished, or abandoned by merger with the underlying fee interest . . . or in any other manner in which easements may be lawfully terminated, released, extinguished or abandoned."[80] The court acknowledged that "conservation easements may be extinguished through many means under Colorado state law, including by mutual consent of the parties."[81] Given that, is there a way in states with enabling statutes similar to Colorado's to comply with the extinguishment regulation?[82] The answer is yes.

If (1) a conservation easement expressly provides that it is extinguishable only in the manner provided in the regulations (in a judicial proceeding, upon a finding that continued use of the property for conservation purposes has become impossible or impractical, and with a payment of at least the required minimum proportionate share of proceeds to the holder to be used "in a manner consistent with the conservation purposes of the original contribution"); (2) that provision is not qualified in any manner (e.g., by other provisions in the deed or an outside agreement); (3) the state enabling statute does not preclude enforcement of that provision,[83]

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80. *Id.*

81. *Id.*

82. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, apps. a, b, for a survey of over one hundred state enabling statutes.

83. In most cases, the state conservation easement enabling statute should not preclude the enforcement of provisions included in a conservation easement deed to comply with the federal tax law restriction on transfer, extinguishment, division of proceeds, and other requirements. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 22–23. One can, however, imagine a state statute that provides that all conservation easements created under its auspices may be transferred, released, or terminated pursuant to *only* the process set forth in the statute and regardless of the specific terms included in the deed. If such a statute were enacted in a state (or if an existing state statute were interpreted to operate in that fashion), conservation easements subject to the statute should not be eligible for a deduction because the easements could not satisfy the requirements of section 170(h) and the regulations regardless of their terms. Donors wishing to convey easements eligible for federal tax incentives could escape the application of such a statute by conveying nonstatutory appurtenant easements (i.e., along with a conservation easement drafted to comply with federal tax law requirements, the donor would convey to the donee a small "anchor" parcel to which the easement would be appurtenant, thus ensuring the enforceability of the easement under the common law of the state). *See* Nancy A. McLaughlin, *Condemning Conservation Easements: Protecting the Public Interest and Investment in Conservation*, 41 U.C. DAVIS L. REV. 1897, 1901–02 (2008) (noting that this technique was used to validate conservation easements before the enactment of state enabling statutes).

and (4) the easement constitutes a restricted gift under state law,[84] then the easement should comply with the extinguishment requirements of the regulations. In such a case, although the enabling statute provides that a conservation easement may be released or extinguished in the same manner as other easements, including by mutual agreement of the parties, the holder could not simply agree to release or extinguish the easement because it would be legally bound to administer the easement (a restricted gift) "in accordance with the donor's precise directions and limitations" (i.e., in accordance with the terms of the deed).[85]

Although state courts should recognize the restricted gift status of tax-deductible conservation easements, particularly after *Carpenter*, there is a risk that some may not. To ensure that holders will be legally bound to administer such easements in accordance with their stated terms and purposes over the long term, which is essential to the success of the tax incentive program, the Treasury Department should revise the regulations to mandate that a tax-deductible conservation easement include a statement that the easement was conveyed, in whole or in part as a charitable gift for a specific purpose, the grantor intends to claim federal tax benefits as a result of the gift, and the grantor intends that the grantor and grantee (and their successors and assigns) will be legally bound by the terms of the easement. If this were done, it would minimize the risk that state court judges unfamiliar with the requirements of section 170(h) and the regulations might fail to recognize the status of a tax-deductible conservation easement as a restricted charitable gift and the binding nature of the restriction on transfer, extinguishment, division of proceeds, and other provisions included in the deed to satisfy federal tax law requirements. In the meantime, cautious donors should include a provision in their easement deeds confirming that the gift constitutes a restricted gift under state law. In addition, donors should refuse to accede to the demand of some holders that they include a provision in their conservation easement deeds stating that the conveyance does not

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84. The Uniform Conservation Easement Act, which contains language similar to that found in the Colorado enabling statute regarding modification and termination, explains that the act "leaves intact the existing case and statute law of adopting states as it relates to the modification and termination of easements and the enforcement of charitable trusts" and "independently of the Act, the Attorney General could have standing [to enforce a conservation easement] in his capacity as supervisor of charitable trusts." UNIFORM CONSERVATION EASEMENT ACT § 3, cmt. (2007). For a discussion of this aspect of the Uniform Conservation Easement Act, see McLaughlin & Weeks, *Setting the Record Straight*, *supra* note 41, at 81–85.

85. If a conservation easement is silent regarding extinguishment, but is extinguishable only in a judicial proceeding and upon a finding of impossibility or impracticality because it is a restricted gift and *cy pres* applies, the easement should satisfy the extinguishment regulation.

constitute a restricted gift (or is an unrestricted gift) because such a provision should render the easement ineligible for federal tax incentives.[86]

D. Extinguishment Regulation: Optional Provisions or Necessary Restrictions?

As discussed above, the Tax Court in *Carpenter* ruled that conservation easements extinguishable by mutual agreement of the parties, even if subject to a standard such as impossibility, fail as a matter of law to comply with the extinguishment regulation requirements. In the section of the opinion containing that ruling, Judge Haines also noted, in part, 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."[87] That statement has caused some to argue that the provisions of the extinguishment and proceeds regulations should be considered optional, and states, localities, and even holders should be free to craft their own extinguishment procedures.[88] However, a more narrow interpretation of Judge Haines's statement is called for when it is read in context and in light of (1) the history of the deduction provision; (2) other Tax Court cases addressing the extinguishment regulation; (3) the regulations as a whole; and (4) the reasons underlying the provisions addressing extinguishment in the regulations.

Part II.D.1 below examines Judge Haines's statement in context and in light of the foregoing sources and reasons. It concludes that the provisions of the extinguishment and proceeds regulations should be viewed, not as optional, but as imposing "the necessary restrictions" on extinguishment. It further explains that those regulations should be viewed as providing taxpayers with safe harbor language or a blueprint by which to build a conservation easement that addresses extinguishment in a manner that satisfies section 170(h)'s protected-in-perpetuity requirement.

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86. A few holders have been insisting on this provision in an attempt both to prevent the holder from being legally bound to administer the easement in accordance with its terms and purposes over the long term and to prevent the state attorney general from having standing to call the holder to account for failing to do so.

87. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1005, T.C.M. (RIA) ¶ 2012-001, 7 (2012).

88. *See* Jessica E. Jay, *When Perpetual Is Not Forever: The Challenge of Changing Conditions, Amendment and Termination of Perpetual Conservation Easements*, 36 HARV. ENVTL. L. REV. 1 (2012) [hereinafter Jay, *Perpetual Is Not Forever*], critiqued in Ann Taylor Schwing, *Perpetuity Is Forever, Almost Always: Why it is Wrong to Promote Amendment and Termination of Perpetual Conservation Easements*, 37 HARV. ENVTL. L. REV. (2012) (forthcoming 2012) (noting, in part, that Jay relies on case law that does not support her thesis).

There also are a number of compelling policy reasons for imposing uniform restrictions on the extinguishment of tax-deductible conservation easements, and for not deferring to states, localities, or holders regarding this critical issue. Those policy reasons are discussed in Part II.D.2 below. Part II.D.3 then briefly explains the interaction of federal and state law in this context.

1. Necessary Restrictions

(i) History of Deduction Provision

The author has previously described in detail the history of the conservation easement deduction provision, Congress and the Treasury Department's concerns about abuse, and the consequent elaborate requirements of section 170(h) and the regulations, and there is no need to restate that entire analysis here.[89] Accordingly, what follows is a brief discussion of only the most relevant aspects.

Congress sought, through section 170(h), to subsidize the acquisition of conservation easements that would *permanently* protect the conservation values of unique or otherwise significant properties.[90] Congress also sought to restrict the ability of government and nonprofit holders to sell, trade, release, or otherwise transfer such easements, except for transfers made to other qualified holders that agree to continue to enforce the easements.[91] In addition, although Congress recognized that state courts might extinguish tax-deductible conservation easements if continuing to use the properties for conservation purposes should become impossible or impractical due to changed conditions, Congress anticipated that such extinguishments would be rare and opted to leave it to the Treasury Department to craft rules to protect the federal interest and investment in conservation in such an unlikely event.[92]

The extinguishment and division of proceeds regulations should thus be viewed as an acknowledgment by the Treasury Department that changed

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89. *See generally* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16; McLaughlin, *National Perpetuity Standards*, *Part 2*, *supra* note 5.

90. *See supra* note 3 (quoting the legislative history of § 170(h)). *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 476–86. The term "conservation values" used herein encompasses all of the values tax-deductible conservation easements are intended to protect in perpetuity, including habitat, open space, historic, recreational, and educational values. *See* I.R.C. § 170(h)(4)(A).

91. *See* S. REP. NO. 96-1007, *supra* note 2, *reprinted in* 1980 U.S.C.C.A.N. 6736; McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 480–83, 486.

92. *See* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 484–85.

conditions might, in rare circumstances, render the continued use of property for conservation purposes impossible or impractical, and as a direction that the conservation purpose of an easement will nonetheless be treated as protected in perpetuity if, in such circumstances: (1) the restrictions are extinguishable in a judicial proceeding; (2) the holder is entitled to at least a minimum proportionate share of the proceeds from a subsequent sale, exchange, or involuntary conversion of the property; and (3) the holder is required to use such proceeds "in a manner consistent with the conservation purposes of the original contribution."[93] There is no indication that Congress or the Treasury Department contemplated that it would be permissible for perpetual conservation easements subsidized through section 170(h) to be extinguished in other circumstances, such as when continued protection of the targeted conservation values has *not* become impossible or impractical, or when a state or local public official or board determines that termination is essential to the orderly development of the area or in the public interest.[94]

In fact, if Congress or the Treasury Department had intended for tax-deductible conservation easements to be extinguishable according to varied procedures developed by states and localities, they presumably would have included a provision to that effect in section 170(h) or the regulations. Congress specifically deferred, in part, to state and local policies in section 170(h) with regard to satisfaction of the open space conservation purposes test, which refers to the preservation of land "pursuant to a clearly delineated Federal, state, or local governmental conservation policy."[95] The Treasury Department also specifically deferred to state law in the regulations with regard to the allocation of proceeds following an involuntary conversion.[96]

93. Reg. § 1.170A-14(g)(6).

94. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at apps. a, b (surveying the modification and termination provisions of over one hundred state enabling statutes).

95. *See* I.R.C. § 170(h)(4)(A)(iii)(II). Congress explained "this provision is intended to protect the types of property identified by representatives of the general public as worthy of preservation or conservation." S. REP. NO. 96-1007, *supra* note 2, pt. 2, at 11, *reprinted in* 1980 U.S.C.C.A.N. at 6747. Congress did not, however, leave the decision regarding satisfaction of the open space conservation purposes test solely to state or local policy. Rather, section 170(h) requires the donor to separately establish that the donation "will yield a significant public benefit." I.R.C. § 170(h)(4)(A)(iii)(II).

96. *See* Reg. § 1.170A-14(g)(6)(ii) (mandating that the donee must be entitled to at least a minimum percentage share of proceeds following extinguishment, "unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction"). As to why the Treasury Department deferred to state law on this point, see McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 510 n.145 and accompanying text.

But there is no mention in section 170(h), the regulations, or the legislative history regarding deference to state and local extinguishment procedures, even though some states had statutory extinguishment procedures in place at the time of the enactment of section 170(h) and the drafting of the regulations.[97] Consistent with basic rules of construction, it should be presumed that omission was purposeful,[98] and that the Treasury Department intended to impose a uniform set of rules that would protect the federal investment in those rare cases where changed conditions frustrate the purpose of a tax-deductible perpetual easement.

The foregoing interpretation is also consistent with the explanation of the extinguishment regulation provided by one of the principal drafters of the regulations. In his treatise on section 170(h), which was published soon after the regulations were issued in 1986, Stephen J. Small posed the question of "what can be done when natural or economic conditions change and the once-important conservation interests associated with property subject to an easement no longer exist[?]"[99] He answers that question in his explanation of the extinguishment regulation as follows:

> [The extinguishment regulation] represents a recognition by the Service that perpetual may not really be perpetual . . . .

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97. *See, e.g.*, VA. CODE ANN. § 10-153 (1980, 1986) (current version at VA. CODE ANN. § 10.1-1-1704 (2012)) (open-space land protected by a conservation easement can be converted or diverted if (i) the public body holding the easement determines it to be "essential to the orderly development and growth of the urban area" and "in accordance with the official comprehensive plan;" and (ii) other real property of at least equal fair market value and of as nearly as feasible equivalent usefulness and location for use as permanent open-space is substituted within a reasonable period not exceeding one year, unless the public body determines that such open-pace land or its equivalent is no longer needed); CA. GOVT. CODE § 51093 (West 1974) (the holder of an open space easement can abandon the easement at the request of a landowner if (i) the holder determines that certain conditions have been met, including that no public purpose will be served by keeping the land as open space; (ii) public hearings are held; and (iii) the landowner pays an "abandonment fee" that is deposited in the state's general fund); MASS. GEN. LAWS ANN. CH. 184, § 32 (West 1980, 1986) (conservation restrictions "may be released, in whole or in part, by the holder for such consideration, if any, as the holder may determine, in the same manner as the holder may dispose of land or other interests in land, but only after a public hearing" and approval of a certain public official or officials).

98. *See, e.g.*, Keene Corp. v. United States, 508 U.S. 200, 208 (1993) ("'[W]here Congress includes particular language in one section of a statute but omits it in another . . . it is generally presumed that Congress acts intentionally and purposefully in the disparate inclusion or exclusion.'") (quoting Russello v. United States, 464 U.S. 16, 23 (1983) (citation omitted)).

99. STEPHEN J. SMALL, THE FEDERAL TAX LAW OF CONSERVATION EASEMENTS § 14.02, 14–3 (4th ed. 1997).

> [There may be a] subsequent change or destruction of the conservation interests that were the subject of the donation . . . .
>
> [T]his section of the Regulations makes it clear to the donee organization that in such a situation the restrictions can be extinguished by judicial proceedings and the property can be sold or exchanged, as long as the subsequent application of proceeds follows the rules of [the proceeds regulation]. To those who suggest this may be a cumbersome way to deal with the problem, I would respond that these restrictions are supposed to be perpetual in the first place, and the decision to terminate them should not be made solely by interested parties. With the decision-making process pushed into a court of law, the legal tension created by such judicial review will generally tend to create a fair result.[100]

Finally, it is notable that the deduction provision was revised, first in 1977 to eliminate the deduction's availability with regard to thirty-year (or longer) term easements and require that all tax-deductible easements be "granted in perpetuity," and then again in 1980 (when section 170(h) was enacted) to further mandate that the conservation purposes of the easements must be "protected in perpetuity."[101] In explaining the new protected-in-perpetuity requirement, Congress stated, *inter alia*, that it intended "to limit the deduction only to those cases where the conservation purposes will in practice be carried out;" that it contemplated that "contributions will be made to organizations which have the commitment and the resources to enforce the [easements] and protect the conservation purposes;" and that the new protected-in-perpetuity requirement "also is intended to limit deductible contributions to those transfers which require that the donee (or successor in interest) hold the conservation easement . . . exclusively for conservation purposes (i.e., that [the easement] not be transferable by the donee except to other qualified organizations that also will hold the [easement] exclusively for conservation purposes)."[102] It is difficult to review this history and arrive at the conclusion that Congress intended to subsidize the acquisition, not of perpetual conservation easements extinguishable by a court only upon frustration of their purposes, but of easements extinguishable pursuant to

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100. *Id.* § 16.03, 16–4.

101. *See* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 476–83.

102. S. REP. NO. 96-1007, *supra* note 2, pt. 2, at 14, *reprinted in* 1980 U.S.C.C.A.N. at 6749.

widely variable state and local procedures and before their purpose have become frustrated.

(ii) Tax Court Opinions

a. Kaufman v. Commissioner

The Tax Court's first extended discussion of the protected-in-perpetuity requirement of section 170(h)(5)(A), and the extinguishment regulation in particular, appeared in *Kaufman II*.[103] Although the First Circuit vacated and remanded *Kaufman II* in part in *Kaufman III*, the Tax Court's analysis of the extinguishment regulation in *Kaufman II* remains important for a number of reasons. To begin with, the First Circuit limited its analysis of Regulation section 1.170A-14(g)(6) in *Kaufman III* to the question of whether a lender agreement impermissibly qualified the provision included in a façade easement to satisfy the proceeds regulation; the court did not discuss the extinguishment regulation.[104] Second, the Tax Court's analysis of the extinguishment regulation in *Carpenter* is based, in part, on its discussion of that regulation in *Kaufman II*. Accordingly, the analysis and holding in *Carpenter* cannot be fully understood without an understanding of the Tax Court's analysis of the extinguishment regulation in *Kaufman II*. Third, the Tax Court's opinion in *Kaufman II* provides insight into how the extinguishment regulation should be interpreted to be consistent with congressional intent.[105]

In *Kaufman II,* the Tax Court explained that section 170(h) is an exception to the general rule that partial interests in property are not deductible and noted the various requirements that must be met to be eligible for the deduction.[106] The court noted, in particular, that Regulation section 1.170A–14(g), which consists of (g)(1) through (g)(6), "elaborates on the enforceability-in-perpetuity requirement."[107] With regard to the extinguishment regulation, the court explained:

> Paragraph (g)(6) is entitled "Extinguishment" and recognizes that, after the donee organization's receipt of an interest in property, an unexpected change in the conditions surrounding the property can make impossible or impractical

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103. *Kaufman II*, 136 T.C. 294, 307 (2011), *vacated and remanded in part on other grounds*, *Kaufman III*, 687 F.3d 21 (1st Cir. 2012).

104. *Kaufman III*, 687 F.3d at 26–28.

105. *See infra* Part III (critiquing *Kaufman III*).

106. *Kaufman II*, 136 T.C. at 313, *vacated and remanded in part*, *Kaufman III*, 687 F.3d. 21.

107. *Id.* at 305.

> the continued use of the property for conservation purposes. Subdivision (i) of paragraph (g)(6) provides that those purposes will nonetheless be treated as protected in perpetuity if the restrictions limiting use of the property for conservation purposes "are extinguished by judicial proceeding and all of the donee's proceeds * * * from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution."[108]

With regard to the extinguishment and proceeds regulations combined, the Tax Court explained:

> The drafters of section 1.170A–14, Income Tax Regs., undoubtedly understood the difficulties (if not impossibility) under State common or statutory law of making a conservation restriction perpetual . . . . They understood that forever is a long time and provided what appears to be a regulatory version of cy pres to deal with unexpected changes that make the continued use of the property for conservation purposes impossible or impractical.[109]

The Tax Court in *Kaufman II* did not refer to the extinguishment regulation as optional, or but one of many possible ways in which a tax-deductible conservation easement can be extinguished. Nor did it indicate that it would be permissible for states, localities, or holders to craft their own extinguishment procedures for tax-deductible easements. Rather, the court described the extinguishment regulation in the same manner as its principal drafter, Stephen J. Small — as a recognition that changed conditions might render the continued use of the subject property for conservation purposes impossible or impractical, and a description of the process by which the easement can be extinguished in such a circumstance.

It is not surprising that the Treasury Department incorporated what "appears to be a regulatory version of *cy pres*" into the regulations to address extinguishment.[110] Congress, the Treasury Department, and the charitable conservation organizations that testified in support of section 170(h) were aware of the status of tax-deductible conservation easements as charitable gifts and of state law governing the administration and enforcement of such gifts. At the congressional hearings on proposed section 170(h), and in response to the Treasury Department's concern that charitable conservation

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108. *Id.* at 306.
109. *Id.* at 306–07.
110. *See id.* at 307.

organizations might not properly enforce conservation easements, nineteen land trusts submitted an appendix to their testimony in which they acknowledged the status of tax-deductible conservation easements as "charitable grants" and noted the power and duty of courts of competent jurisdiction and state attorneys general to enforce such grants.[111] The Treasury Department also may have recognized that the *cy pres* standard of impossibility or impracticability provides as close to perpetual protection of the purpose of a charitable gift as one can obtain under existing U.S. law.[112] In addition, unlike the real property law doctrine of changed conditions, the doctrine of *cy pres* ensures that if a conservation easement is extinguished, proceeds attributable to the easement will remain in the charitable sector to be used for similar conservation purposes on behalf of the public.[113]

Also important in the *Kaufman II* opinion is footnote seven, to which Judge Haines specifically referred in *Carpenter*.[114] Footnote seven provides:

> Our concern in *Kaufman v. Commissioner*, 134 T.C. 182 (2010), was with the allocation of proceeds on a sale, exchange, or involuntary conversion of property following

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111. *See Minor Tax Bills: Hearings Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 96th Cong. 238, 242 (1980) (App. to Testimony of French and Pickering Creeks Conservation Trust, the Brandywine Conservancy, and other Conservation Organizations in re H.R. 7318 on June 26, 1980).

112. The American Law Institute recognized this when it promulgated the *Restatement (Third) of Property*, which applies a special set of rules based on the doctrine of *cy pres* to the modification and termination of conservation easements, explaining that, "[b]ecause of the public interests involved, these servitudes are afforded more stringent protection than privately held conservation servitudes, which are subject to modification and termination under § 7.10 [the property law doctrine of changed conditions]." *See* RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 7.11 cmt. a (2000). *See also, e.g.*, BOGERT & CHESTER THE LAW OF TRUSTS AND TRUSTEES § 439 (3rd ed. 2008) (explaining that in applying *cy pres* "the court will not substitute a new scheme merely because it or the trustee believes it would be a better plan than that which the settlor provided"); McLaughlin & Weeks, *In Defense of Conservation Easements*, *supra* note 55, at 70–73 (explaining that courts apply the "impossibility or impracticality" standard conservatively in the charitable gift context).

113. *Cy pres* is distinguishable from the real property law doctrine of changed conditions, in part, because of the requirement that the holder of the easement receive compensation upon extinguishment and use such compensation for similar conservation purposes. *See, e.g.*, RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES, § 7.11 cmt. c (2000) (in other instances where changed conditions lead to the termination of a servitude, such as in residential subdivisions, there is seldom an entitlement to damages).

114. *Carpenter*, T.C.M. (CCH) at 1005, T.C.M. (RIA) ¶ 2012-1, at 7.

> judicial extinguishment of a conservation restriction burdening the property. *We did not then, nor do we now, rule on whether the language establishing the restriction* [i.e., the conservation easement deed] *must incorporate provisions requiring judicial extinguishment (and compensation)* in all cases in which an unexpected change in surrounding conditions frustrates the conservation purposes of the restriction. Such a rule is suggested, however, by the last sentence in [Regulation section 1.170A–14(c)(2), the restriction on transfer regulation].[115]

It is not surprising that the Tax Court was unwilling to rule that a tax-deductible conservation easement deed must incorporate provisions requiring judicial extinguishment and compensation to the holder in the event the purpose of the easement is frustrated due to changed conditions. The question of whether an easement must expressly state that it is extinguishable only as provided in the extinguishment and proceeds regulations was not before the court and, unlike the restriction on transfer regulation, the extinguishment and proceeds regulations do not specifically state that certain language must be included "in the instrument of conveyance" for the easement to be deductible.[116] The court also was aware that a conservation easement that is silent regarding extinguishment may nonetheless be extinguishable only as provided in the regulations (in a judicial proceeding, upon a finding that continued use of the property for conservation purposes has become impossible or impractical, and with a payment of proceeds to the holder to be used for similar conservation purposes) if the doctrine of *cy pres* applies.[117]

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115. *Kaufman II*, 136 T.C. at 307 n.7, *vacated and remanded in part*, *Kaufman III*, 687 F.3d. 21.

116. *Compare, e.g.*, Reg. § 1.170A-14(c)(2) ("A deduction shall be allowed for a contribution under this section only if *in the instrument of conveyance* the donor prohibits . . .") (emphasis added), *with* Reg. § 1.170A-14(g)(6)(ii) ("for a deduction to be allowed under this section, at the time of the gift the donor *must agree* that . . .") (emphasis added).

117. *See Kaufman II,* 136 T.C. at 304, *vacated and remanded in part*, *Kaufman III*, 687 F.3d. 21 (referring to sources discussing the application of *cy pres* to conservation easements, including the RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES § 7.11 (2000)). *See also, e.g.*, UNIFORM CONSERVATION EASEMENT ACT § 3, cmt. (2007) ("The Act leaves intact the existing case and statute law of adopting states as it relates to the modification and termination of easements and the enforcement of charitable trusts. Thus . . . the governmental body or charitable organization holding a conservation easement, in its capacity as trustee, may be prohibited from agreeing to terminate the easement (or modify it in contravention of its purpose) without first obtaining court approval in a *cy pres* proceeding.");

The Tax Court did note, however, that a rule requiring incorporation of the provisions of the extinguishment and proceeds regulations into an easement deed is suggested by the last sentence of the restriction on transfer regulation. The restriction on transfer regulation provides that a deduction will be allowed for the donation of a conservation easement only if the instrument of conveyance prohibits the donee (and its successors or assigns) from subsequently transferring the easement, whether or not for consideration, unless (1) the transfer is to another "eligible donee;" and (2) the eligible donee agrees that "the conservation purposes which the contribution was originally intended to advance will continue to be carried out."[118] The regulation also clarifies, however, that this restriction on transfer requirement will still be met if, upon impossibility or impracticality, the easement is extinguishable (and thereby transferable) in accordance with the extinguishment and proceeds provisions of the regulations.[119] The implication, which is supported by the legislative history to section 170(h) and the fact that Congress and the Treasury Department did not defer to the state enabling statutes regarding extinguishment, is that the restriction on transfer requirement will *not* be met if the easement is extinguishable (and thereby transferable) in some other manner. Thus footnote seven neither states nor implies that the provisions of the extinguishment regulation are optional.

UNIFORM TRUST CODE § 414 cmt. (2000) ("even though not accompanied by the usual trappings of a trust, the creation and transfer of an easement for conservation or preservation will frequently create a charitable trust").

118. Reg. § 1.170A-14(c)(2).

119. *Id*. The last sentence of the restriction on transfer regulation specifically references the proceeds regulation, which in turn references the extinguishment regulation. To make sense of the cross-references, however, one must refer to Proposed Regulation section 1.170A-13, published in the *Federal Register* on May 23, 1983, because the Treasury Department apparently failed to update the cross-references in the final regulations. *See* Prop. Reg. § 1.170A-13, 48 Fed. Reg. 22941-48 (May 23, 1983). In addition, the Treasury Department's failure to specifically reference a judicial proceeding in its references to extinguishment and compensation in the restriction on transfer regulation should not be interpreted to have any special import. As explained in *Food and Drug Admin. v. Brown & Williamson Tobacco Corp*., 529 U.S. 120, 133 (2000):

> It is a "fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." A court must therefore interpret the statute "as a symmetrical and coherent regulatory scheme," and "fit, if possible, all parts into an harmonious whole."

Id. (citations omitted) (quoting Gustafson v. Alloyd Co., 513 U.S. 561, 569 (1995); Davis v. Mich. Dep't of Treasury, 489 U.S. 803, 809 (1989); FTC v. Mandel Bros., Inc., 359 U.S. 385, 389 (1959)).

b. Carpenter v. Commissioner

The next Tax Court case to discuss the extinguishment regulation was *Carpenter* itself.[120] As previously discussed, Judge Haines held in *Carpenter* that conservation easements that may be extinguished by mutual consent of the parties, even if subject to a standard such as impossibility, fail as a matter of law to comply with the enforceability in perpetuity requirements under Regulation section 1.170A-14(g). In discussing this holding, Judge Haines noted, in part:

> We have previously discussed the restrictions required by the extinguishment regulation. In [footnote seven of *Kaufman II*], we declined to rule that a conservation deed must require a judicial proceeding to extinguish an easement for the easement to be perpetual. We once again decline to create an absolute rule. Rather, we find 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.[121]

It is this paragraph that has caused some to argue that the extinguishment regulation should be viewed as optional, and that states, localities, and even holders should be free to craft their own extinguishment procedures. However, Judge Haines's reference to "the restrictions *required by* the extinguishment regulation" in the first sentence of the paragraph quoted above suggests that he does not view such restrictions as optional. In addition, in light of the language of footnote seven in *Kaufman II* to which he specifically refers, Judge Haines's unwillingness to create an "absolute rule" in the second sentence of the passage quoted above should be viewed as an unwillingness to create an absolute rule that one must expressly incorporate certain provisions regarding extinguishment into a conservation easement deed for the easement to be tax-deductible. Judge Haines may have been unwilling to create such a rule for the same reasons noted above with regard to *Kaufman II* (the question was not before the court, the extinguishment and proceeds regulations do not specifically state that certain language must be included "in the instrument of conveyance," and an easement that is silent regarding extinguishment may nonetheless be extinguishable only in the manner set forth in the regulations).

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120. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, T.C.M. (RIA) ¶ 2012-001 (2012).

121. *Id.*, 103 T.C.M. (CCH) at 1005, T.C.M. (RIA) ¶ 2012-001 at 7 (citation omitted).

Judge Haines also did not state that the extinguishment regulation is a safe harbor. Rather, he stated "the extinguishment regulation provides taxpayers with *a guide, a safe harbor, by which to create the necessary [or absolutely essential] restrictions* to *guarantee protection of the conservation purpose in perpetuity*."[122] He also quoted Stephen J. Small's treatise, in which Small explained that the "restrictions are supposed to be perpetual in the first place, [and] the decision to terminate them should not be [made] solely by interested parties" (i.e., by the landowner and the holder, both of which stand to benefit financially from the extinguishment), and "[w]ith the decision-making process pushed into a court of law, the legal tension created by such judicial review will generally tend to create a fair result."[123] Accordingly, when Judge Haines's statement is read in full and in context, it suggests that the "the necessary [or absolutely essential] restrictions" on extinguishment are those set forth in the extinguishment regulation, although there may be more than one way to comply with those restrictions.

Finally, if *Carpenter* were interpreted to allow tax-deductible conservation easements to be extinguished pursuant to widely variable procedures adopted by states, localities, or individual or coalitions of holders, then to paraphrase the Fourth Circuit in *United States v. Blair*, the safe harbor would become a "safe ocean," and the regulatory exception for extinguishment (designed to apply in very limited circumstances) would swamp the statutory rule (that the easements be "granted in perpetuity" and their conservation purposes "protected in perpetuity").[124] Accordingly, the better view is that the extinguishment and proceeds regulations set forth "the necessary restrictions" on extinguishment and provide taxpayers with a guide or set of instructions by which to build a conservation easement that addresses extinguishment in a manner that satisfies section 170(h)'s protected-in-perpetuity requirement. In other words, the extinguishment regulation provides taxpayers with safe harbor language, which, if it is incorporated into a conservation easement deed, not qualified by other provisions or by a separate agreement, and legally binding on the parties under state law, will ensure that the taxpayer satisfies the extinguishment component of the protected-in-perpetuity requirement. In fact, including such language in tax-deductible conservation easements has been a longstanding practice of well-advised donors.[125]

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122. *Id.* (emphasis added). *See* THE AMERICAN HERITAGE DICTIONARY 1207 (3rd ed. 1992) (defining "necessary" as "absolutely essential").

123. *Carpenter*, 103 T.C.M. (CCH) at 1005, T.C.M. (RIA) ¶ 2012-001 at 7.

124. *See* United States v. Blair, 661 F.3d 755, 773 (4th Cir. 2011).

125. *See* Diehl, 1988 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 155, 160–61 (providing a checklist of provisions relating to IRS requirements and model extinguishment and proceeds provisions for inclusion in conservation easement deeds); Barrett, 1996 CONSERVATION EASEMENT HANDBOOK, *supra* note

c. *Mitchell* v. *Commissioner*

Judge Haines's opinion in *Mitchell*,[126] which was issued three months after the issuance of the *Carpenter* opinion, also suggests that he does not view the provisions of the extinguishment regulation as optional. Although *Mitchell* is primarily focused on the regulation's so-remote-as-to-be-negligible standard and mortgage subordination requirement, Judge Haines makes a number of references to the extinguishment regulation in the opinion. He refers to the various subparagraphs of Regulation section 1.170A-14(g), including (g)(6), as "legally enforceable restrictions" that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation as required by Regulation section 1.170A-14(g)(1).[127] He describes the extinguishment regulation in the same (non-optional) way it was described in *Kaufman II*.[128] And he refers to both the judicial proceeding and proceeds requirements of Regulation section 1.170A-14(g)(6) as "specific requirements:"

> The drafters of [the mortgage subordination regulation] saw taxpayers defaulting on their mortgages as more than a remote possibility. Therefore they drafted a specific provision which would absolutely prevent a default from destroying a conservation easement's grant in perpetuity.
>
> Similarly, the drafters included [the extinguishment and proceeds regulations] to address similar albeit different concerns. We refused to apply the so-remote-as-to-be-negligible standard in both *Carpenter* and *Kaufman II*. Both were cases where the taxpayer attempted to use the so-remote-as-to-be-negligible standard to avoid *a specific requirement of the regulations (i.e., the judicial proceeding requirement of section 1.170A–14(g)(6)(i) . . . and the proceeds requirement of section 1.170A–14(g)(6)(ii) . . .).*[129]

Accordingly, none of the references in *Mitchell* to the extinguishment regulation suggest that Judge Haines or the Tax Court view

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53, at 11, 17–18 (same); Byers, 2005 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 313–14, 375 (same).

126. Mitchell v. Commissioner, Tax Ct. Rep. (CCH) Dec. 59,013, Tax Ct. Rep. (RIA) Dec. 138.16 (2012).

127. *Id.*, Tax Ct. Rep. (CCH) Dec. 59, 013, at 4634–35, Tax Ct. Rep. (RIA) Dec. 138.16, at 190–91.

128. *Id.*, Tax Ct. Rep. (CCH) Dec. 59,013, at 4634–35, Tax Ct. Rep. (RIA) Dec. 138.16, at 191. *See supra* note 108 and accompanying text.

129. *Id.*, Tax Ct. Rep. (CCH) Dec. 59,013, at 4636, Tax Ct. Rep. (RIA) Dec. 138.16, at 195.

the provisions of that regulation as optional or but one of many possible ways that tax-deductible perpetual conservation easements may be permissibly extinguished.

(iii) Regulations

The regulations themselves also indicate that the requirements of the extinguishment regulation should not be viewed as optional. The opening paragraph of the regulations explains that a charitable income tax deduction is generally not allowed for the donation of a partial interest in property,[130] but a special exception is made "for the value of a qualified conservation contribution *if the requirements of this section are met*."[131] As Stephen J. Small explained in his treatise on section 170(h), "[a]s far as Congress and Treasury are concerned, a taxpayer who donates an easement continues to use and enjoy the property, and the requirements for taking an income tax deduction simply must be tighter to ensure that there is also a significant long-term public benefit associated with the donation."[132]

In addition, both the restriction on transfer and proceeds regulations specifically reference the extinguishment regulation and do not suggest that the provisions of that regulation are optional. As explained in the discussion of *Kaufman II* above, the restriction on transfer regulation provides that the restriction on transfer requirement will not be violated if, upon impossibility or impracticality, the easement is extinguishable (and thereby transferable) in accordance with the provisions of the extinguishment and proceeds regulations. The implication, which is supported by the legislative history of section 170(h) and the fact that Congress and the Treasury Department did not defer to the state enabling statutes regarding extinguishment, is that the restriction on transfer requirement will be violated if the easement is extinguishable (and thereby transferable) in some other manner.

The proceeds regulation is also inextricably tied to the extinguishment regulation. Although, for ease of reference, this Article refers to those two provisions as "regulations," they are part of a single paragraph in the regulations entitled "Extinguishment" — section 1.170A-14(g)(6). The proceeds regulation, which is subparagraph (g)(6)(ii) of that paragraph, provides in part

> [W]hen a change in conditions give[s] rise to the extinguishment of a perpetual conservation restriction *under [sub]paragraph (g)(6)(i) [i.e., the extinguishment*

130. Charitable gifts of partial interests in property are generally not deductible because of the potential for abuse and lack of assured benefit to the public when a donor retains use and enjoyment rights with respect to donated property.

131. Reg. § 1.170A-14(a) (emphasis added).

132. *See* Small, *supra* note 99, at 2-2 to -3.

> *regulation]*, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to [the minimum proportionate share of proceeds specified in the proceeds regulation].[133]

The proceeds regulation is intended to ensure that the federal investment in a conservation easement will be protected in the event continued use of the property for conservation purposes becomes impossible or impractical and the easement is extinguished in a judicial proceeding. If extinguishment occurs through some other means, the proceeds regulation would appear to be inapplicable. It seems unlikely that the Treasury Department intended to impose strict rules regarding protection of the federal investment if extinguishment occurs as specified in the extinguishment regulation, but leave the door open to potential loss of that investment, as well as to premature extinguishments, by permitting holders to agree to extinguish easements in other circumstances.

A taxpayer might argue that an alternative method of extinguishment "substantially complies" with the requirements of the extinguishment regulation, but the taxpayer would face an uphill battle. The Tax Court is generally willing to apply the doctrine of substantial compliance only to requirements that are "procedural or directory" or "given with a view to the orderly conduct of business," such as some of the substantiation requirements of Regulation section 1.170A-13(c).[134] The Tax Court does not apply the substantial compliance doctrine to requirements that relate to the "substance or essence" of the legislation.[135] The extinguishment and proceeds regulations should be viewed as relating to the substance or essence of the legislation given that they, along with the other "enforceable in perpetuity" requirements of Regulation section 1.170A-14(g), are intended to ensure, not that the donor has properly substantiated his entitlement to the deduction, but that the conservation purpose of the easement will be protected in perpetuity as mandated by section 170(h)(5)(A) (i.e., that a gift of a qualifying conservation contribution has actually been made).

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133. Reg. § 1.170A-14(g)(6)(ii) (emphasis added) (reproduced *supra* note 15).

134. *See, e.g.*, Bond v. Commissioner, 100 T.C. 32, 41 (1993) (quoting Taylor v. Commissioner, 67 T.C. 1071, 1077-78 (1977)).

135. *See, e.g.*, Hewitt v. Commissioner, 109 T.C. 258 (1997); Crow v. Commissioner, 28 Empl. Benefits Cas. 2558, T.C.M. (RIA) ¶ 2002-178 (2002); Estate of Clause v. Commissioner, 122 T.C. 115 (2004); Estate of Tamulis v. Commissioner, 92 T.C.M. (CCH) 189, T.C.M. (RIA) ¶ 2006-183 (2006), *aff'd*, 509 F.3d 343 (2007); Mohamed v. Commissioner,103 T.C.M. (CCH) 1814, T.C.M. (RIA) ¶ 2012-152 (2012). In *Mohamed*, the Tax Court noted that, "[s]ince *Bond*, few taxpayers have succeeded in showing substantial compliance." *Mohamed*, 103 T.C.M. (CCH) at 1819, T.C.M. (RIA) ¶ 2012-152, at 1175.

(iv) Reasons Underlying the Federal Extinguishment Requirements

Additional support for interpreting the provisions of the extinguishment regulation as "necessary restrictions" comes from an understanding of why the regulations were drafted the way they were.[136] The regulations authorize the deductibility of a conservation easement that is extinguishable (1) in a judicial proceeding; (2) upon a finding that continued use of the subject property for conservation purposes has become impossible or impractical due to an unexpected change in conditions; (3) with a payment of at least a minimum percentage share of proceeds to the holder; and (4) provided the holder uses such proceeds "in a manner consistent with the conservation purposes of the original contribution."[137] The Treasury Department included each of these four requirements in the regulations for a reason, and examining those reasons underscores the importance of each requirement.

a. Impartial Judicial Decision Maker

The extinguishment regulation contemplates that extinguishment will occur in the context of a judicial proceeding. The requirement of a judicial proceeding, coupled with the high threshold standard of "impossibility or impracticality," should operate to prevent federally subsidized conservation easements from being extinguished to satisfy short-term and often shortsighted economic, political, and development interests. State and local government officials, governing bodies, and administrative panels are likely to be subject to economic, political, and development pressures that could cause them to agree to extinguish conservation easements even if the easements continue to protect unique or otherwise significant conservation values.[138] Judges, on the other hand, generally sit in

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136. *See supra* note 122 and accompanying text (discussing Judge Haines's statement in *Carpenter* that "the extinguishment regulation provides taxpayers with *a guide, a safe harbor, by which to create the necessary restrictions*" (emphasis added)).

137. *See* Reg. § 1.170A-14(g)(6).

138. *See, e.g.*, RALPH E. HEIMLICH & WILLIAM D. ANDERSON, 2001 ECONOMIC RESEARCH SERVICE, U.S.D.A., AGRICULTURAL ECONOMIC REPORT NO. 803, DEVELOPMENT AT THE URBAN FRINGE AND BEYOND: IMPACTS ON AGRICULTURE AND RURAL LAND, 4–5 (June 2001), http://www.ers.usda.gov/publications/aer803/aer803.pdf, (discussing the difficulties facing states and localities in developing and implementing appropriate land use plans); Sarah Schindler, *The Future of Abandoned Big Box Stores: Legal Solutions to the Legacies of Poor Planning Decisions*, 83 U. COLO. L. REV. 471 (2012).

relative remove from self-interested constituents and the immediacy of such pressures, which are likely to be particularly high when it comes to attempts to develop protected lands.[139]

In addition, in applying the impossibility or impracticality standard in the charitable gift context, judges are conservative and do not authorize a change in the donor's specified charitable purpose simply because they or the donee believe the assets could be put to a better or more efficient use.[140] Judges also have hundreds of years of precedent, including many cases involving charitable gifts of real estate to be used for specific purposes, to help inform their decisions in this context. Accordingly, judges play an indispensible role as guardians of federally subsidized conservation easements and the conservation values they are intended to preserve in perpetuity for the benefit of the public.

Moreover, the unwillingness of Congress and the Treasury Department to rely on state and local policies, officials, or agencies to protect the federal investment in conservation easements is evident from the open space conservation purposes test, which refers to the preservation of land "pursuant to a clearly delineated Federal, State, or local governmental conservation policy."[141] Congress explained, "this provision is intended to protect the types of property identified by representatives of the general public as worthy of preservation or conservation."[142] Congress did not, however, leave the decision regarding satisfaction of the open space conservation purposes test solely to state or local policy. Rather, section 170(h) requires the donor to separately establish that the donation "will yield a significant public benefit," and Congress included factors to be considered

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139. *See* Jill R. Horwitz & Marion Fremont-Smith, *The Common Law Power of the Legislature: Insurer Conversions and Charitable Funds*, 83 THE MILLBANK QUARTERLY 225 (2005), http://www.law.umich.edu/centersand programs/lawandeconomics/abstracts/2007/ Documents/07-013horwitz.pdf. State judges are not entirely free from the influence of politics given that they are appointed or elected and do not serve for life. There are a number of safeguards, however, that help to ensure that judges maintain independence, including: retention reelections; codes of judicial conduct that emphasize independence, impartiality, and integrity; judicial conduct boards that investigate and prosecute judges who violate a code of judicial conduct; and judges' ability to disqualify themselves when they believe their impartiality may be subject to question.

140. *See supra* note 112. *See also, e.g.*, Cohen v. City of Lynn, 598 N.E.2d 682 (1992) (a city's conveyance to a private developer of land previously deeded to the city to be used "forever for park purposes" was invalidated because continuing to use the land for park purposes had not become impossible or impracticable).

141. I.R.C. § 170(h)(4)(A)(iii)(II).

142. S. REP. NO. 96-1007, *supra* note 2, pt. II, at 11 (1980), *reprinted in* 1980 U.S.C.C.A.N. at 6747.

in evaluating public benefit in the committee report accompanying the legislation.[143]

The regulations further provide that acceptance of a conservation easement by an agency of a state or local government only "tends to establish the requisite clearly delineated governmental policy, . . . such acceptance, without more, is not sufficient."[144] The Treasury Department was concerned that, while some states and localities might have a rigorous process for review of conservation easement acquisitions, others may have no process at all, or political or other factors that have very little to do with the conservation purposes of the gift might influence the process.[145] Accordingly, the Treasury Department determined that permitting a conservation easement to qualify under section 170(h) based solely on an acceptance by a state or local government agency would be inappropriate because such acceptance might mean nothing at all.[146] These same concerns obviously apply in the extinguishment context and with even more force given the economic and political pressures that may be brought to bear to extinguish easements.[147]

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143. I.R.C. § 170(h)(4)(A)(iii)(II); S. REP. NO. 96-1007, *supra* note 2, pt. II, at 11–12, *reprinted in* 1980 U.S.C.C.A.N. at 6746–47.

144. Reg. § 1.170A-14(d)(4)(iii)(B).

145. *See* SMALL, *supra* note 99, at § 8, 8–5.

146. *See id*.

147. One might argue that the judicial proceeding requirement should be deemed satisfied if the decision to extinguish a conservation easement is made by a state or local official or board, but is subject to judicial review. That is not what the extinguishment regulation provides, however, and there is no guarantee that such a two-tiered process would be as efficient or effective in protecting the federal investment as the process set forth in the regulation, particularly given that the extinguishment of tax-deductible conservation easements should be a rare occurrence. Moreover, significant questions regarding any such appeals process would arise. For example, who would have standing to seek judicial review of the decision by a state or local official or board to extinguish an easement? What period of time would be granted to seek such review? What standard of review would be imposed on the court? If few persons are entitled to bring such an appeal, or the period of time within which to bring the appeal is short, then appeals would be unlikely, even if the decision to terminate the easement is without merit. And if a court could reverse the decision only if there has been an abuse of discretion or clear error of law (or pursuant to some similarly demanding standard), the court would not exercise independent review as the drafters of the regulations contemplated, and reversals would be unlikely. There also would be no assurance of consistent protection of the easements or equitable treatment of donors and subsequent landowners if the various elements of the decision-making and judicial review processes varied from state to state and program to program, as they inevitably would.

b. High Standard

The extinguishment regulation contemplates that tax-deductible conservation easements will be extinguished only if it is established that continued use of the subject property for conservation purposes has become impossible or impractical due to an unexpected change in conditions. As previously noted, this standard provides as close to perpetual protection of the purpose of a charitable gift as one can obtain under existing U.S. law. The standard, properly applied, should protect conservation easements from being extinguished to satisfy short-term state and local political, economic, and development interests.[148]

Some might be concerned that the high standard for extinguishment will mean that projects of great importance to the public (such as construction of highways or electric transmission towers and lines) could be hindered or precluded by the existence of conservation easements. That concern would be unfounded. When the best place to locate a public works project is on land that is protected because it has unique or otherwise significant conservation values, the government has recourse to its power of eminent domain and can institute condemnation proceedings with respect to both the subject land and the easement.

c. Holder's Share of Proceeds

The proceeds regulation provides that, at the time of the donation of a conservation easement, the donor must agree that the donation gives rise to a property right, immediately vested in the donee, with a fair market value that is at least equal to the proportionate value that the easement, at the time of the gift, bears to the value of the property as a whole at that time.[149] That proportionate value, which is generally expressed as a percentage, must remain constant.[150] And when a change in conditions gives rise to the extinguishment of a conservation easement as provided in the extinguishment regulation, the donee, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that minimum (or floor) percentage value.[151]

The extinguishment and proceeds regulations were carefully designed to ensure that, if a conservation easement is extinguished upon frustration of its purpose, at least a minimum percentage share of proceeds from the subsequent sale or exchange of the property will be payable to the

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148. *See supra* note 140 and accompanying text.

149. Reg. § 1.170A-14(g)(6)(ii).

150. *Id.*

151. *Id. See supra* note 96 (explaining that there is an exception to this rule in the case of conversions).

holder to be used "in a manner consistent with the conservation purposes of the original contribution."[152] In other words, the regulations ensure that the federal investment in the easement will not be lost (and will not pass as a windfall to the donor or subsequent owner of the property) and, instead, will remain in the charitable sector to be used for similar conservation purposes. By requiring that the holder receive at least the designated minimum (or floor) percentage of proceeds following extinguishment, the proceeds regulation also protects against valuation abuse.[153]

d. Holder's Use of Proceeds

As noted above, following the extinguishment of an easement, the donee must use its share of the proceeds "in a manner consistent with the conservation purposes of the original contribution." Although the IRS has not issued guidance regarding the type of uses that would be deemed "consistent with the conservation purposes of the original contribution," certain uses should clearly be unacceptable, such as, in the case of government holders, the use of such proceeds to build roads or fund other development infrastructure. Moreover, allowing the proceeds from the extinguishment of federally-subsidized conservation easements (which could be in the multiple millions of dollars for a single easement) to be added to the general operating funds of either government and nonprofit holders could create significant perverse incentives for such holders to seek extinguishments. Accordingly, the "use of proceeds" provision in the extinguishment regulation serves two important purposes. It ensures that the federal funds invested in conservation and historic preservation through section 170(h) will continue to be used for those purposes in the event some easements are extinguished due to impossibility or impracticality. It also ensures that section 170(h), which Congress enacted specifically to

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152. *See* Reg. § 1.170A-14(g)(6)(i).

153. For example, assume a landowner donates a conservation easement with respect to land valued at $1 million and claims a deduction based on an appraisal indicating that the value of the easement is $900,000 (i.e., the donor claims the easement reduces the value of the land by 90 percent at the time of its donation). Assume also that the donor receives a tax benefit from the deduction of $315,000 (the amount of income tax the donor otherwise would have paid at an assumed rate of 35 percent absent the $900,000 deduction). Then a number of years later, after the statute of limitations has run on the donor's deduction, the easement is extinguished in a judicial proceeding and a court-supervised appraisal finds that the easement is (and likely was at the time of its donation) worth only 10 percent of the value of the land. Absent the minimum percentage requirement in the regulations, the holder might receive only 10 percent of the proceeds upon a subsequent sale of the land (or $100,000, assuming no change in the value of the unencumbered land), even though the public invested $315,000 in the easement.

encourage and subsidize the permanent "preservation of unique or otherwise significant land areas or structures,"[154] does not become a mechanism by which federal taxpayers indirectly provide millions of dollars of general operating funds to nonprofits and state and local governments.

As the foregoing illustrates, each of the four federal extinguishment requirements performs a critical function. Accordingly, none should be considered optional.

2. *Need for Uniform Federal Standards*

There are also a number of compelling policy reasons for imposing uniform restrictions on the extinguishment of tax-deductible conservation easements and for not deferring to states, localities, or holders regarding this critical issue.

(i) Consistent Protection of Federal Investment

As noted in the Introduction, federal taxpayers are investing billions in ostensibly "perpetual" conservation easements through section 170(h).[155] This significant federal investment is protected by: (1) requiring that all tax-deductible easements satisfy the elaborate conservation purposes and other threshold requirements of section 170(h) and the regulations; (2) prohibiting government and nonprofit holders from selling, releasing, or otherwise transferring such easements, whether or not for consideration, except to other eligible donees who agree to continue to enforce the easements; and (3) requiring that all such easements satisfy the "enforceability in perpetuity" and other requirements of the regulations, including the requirements of the extinguishment and proceeds regulations.

If tax-deductible easements could be extinguished pursuant to varied procedures set forth in state enabling statutes, there would be little consistency in the protection of the federal investment. At present, over one hundred state statutes authorize the creation or acquisition of conservation easements, and the provisions of those statutes addressing the transfer, release, modification, and termination of easements vary widely from jurisdiction to jurisdiction and program to program.[156] Such statutes are also subject to legislative revision or repeal when development pressures increase or state and local priorities change. These points are worth emphasizing. State legislatures enact state statutes, not with the intent to protect the federal

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154. *See* S. REP. NO. 96-1007, *supra* note 2, pt. II, at 9, *reprinted in* 1980 U.S.C.C.A.N. at 6745.

155. *See* Colinvaux, *In Search of Conservation Value*, *supra* note 1.

156. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, apps. a, b.

investment in perpetual conservation easements, but with state and local interests in mind, including state and local economic and development interests. For example, the Virginia Open Space Land Act authorizes a seven-member politically-appointed board (as well as counties, municipalities, and community development authorities) to extinguish open space easements to make way for "orderly development and growth" regardless of whether such easements continue to protect unique or otherwise significant conservation values.[157]

Consistent protection across the states of the federal investment in tax-deductible conservation easements and the values they are intended to preserve in perpetuity for the benefit of the public can be assured only if such easements are subject to uniform rules regarding extinguishment. Congress presumably recognized this when it declined to defer to the states regarding extinguishment and, instead, authorized deductions only for perpetual easements, or those that are transferable only to other qualified organizations that agree to continue to enforce the easements and terminable only upon frustration of their purposes.

(ii) Efficiency

If the extinguishment regulation were interpreted as setting forth only one of possibly many ways in which tax-deductible conservation easements could be permissibly extinguished, the IRS and the courts would be forced to engage in many and repeated assessments of proposed alternative extinguishment procedures. Each of the over one hundred state enabling statutes would have to be assessed, and every revision to a statute implicating the transfer, modification, release, abandonment, or extinguishment of easements would necessitate a new assessment.

Moreover, there is no indication of the standards that should be used by the IRS or the courts in assessing the acceptability of alternative extinguishment procedures. Neither section 170(h) nor the regulations indicate that alternative procedures are acceptable, much less the standards that should be used to assess such procedures, and the Tax Court in *Carpenter* rejected the argument that an alternative procedure should be deemed acceptable if it can be shown that the possibility of extinguishment pursuant to such procedure is so remote as to be negligible.

Permitting alternative and variable methods of extinguishment would also increase the already considerable complexities and uncertainties associated with valuing tax-deductible conservation easements.[158] Instead of

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157. *See id.* at 45–48.

158. For a discussion of the complexities and uncertainties associated with valuing tax-deductible conservation easements, see, e.g., JOINT COMM. ON TAXATION, 112th Cong., 2d Sess., DESCRIPTION OF REVENUE PROVISIONS

assuming that the easements will be extinguished only in the unlikely event of impossibility or impracticality, both donor and IRS appraisers would have to assess the probability of extinguishment and its effect on value with regard to each alternative extinguishment procedure, and those probabilities would change over time if state and local officials and boards were to authorize a growing number of extinguishments.

(iii) Equity

Equitable considerations provide a third compelling policy reason for interpreting the regulations as imposing uniform restrictions on extinguishment. To be eligible for a federal charitable income tax deduction with regard to the donation of a conservation easement, easement donors must satisfy the elaborate threshold requirements set forth in section 170(h) and the regulations, which apply uniformly to all donations regardless of the location of the subject property or the state statute pursuant to which the easement is created. To ensure equitable treatment of donors and subsequent owners of the burdened properties, the standards for extinguishment of such easements should be similarly uniform. That is, easement donors and subsequent owners in Montana and Michigan should not be able to more easily obtain extinguishment of the easements burdening their properties than similarly situated property owners in Maine or Minnesota — i.e., "protected in perpetuity" should not have a different meaning from state to state or program to program. The spectacle of federally subsidized, ostensibly perpetual conservation easements being more easily terminated in some states than in others would call into question the legitimacy of and diminish public support for the federal tax incentive program.

While some differences in the application of any set of extinguishment standards are inevitable, such differences and consequent inequities will obviously be minimized if the same standards apply uniformly to all tax-deductible conservation easements. Moreover, an extensive body of case law developed over hundreds of years in the charitable gift context underlies the extinguishment regulation's "impossibility or impracticality" standard and will serve as a guide to courts when applying that standard to easements.

CONTAINED IN THE PRESIDENT'S FISCAL YEAR 2013 BUDGET PROPOSAL, at 565–73 (2012), https://www.jct.gov/publications.html?func=startdown&id=4464; Halperin, *Incentives for Conservation Easements*, *supra* note 1, at 31; Nancy A. McLaughlin, *Increasing the Tax Incentives for Conservation Easement Donations—A Responsible Approach*, 31 ECOLOGY L. Q. 1, 68–91 (2004).

(iv) Effectiveness

A final reason for imposing uniform restrictions on extinguishment is effectiveness. Tax-deductible conservation easements are supposed to *permanently* protect properties that have been identified as having unique or otherwise significant conservation values, and Congress and the Treasury Department anticipated that extinguishment of such easements upon frustration of their purposes would be the rare exception rather than the rule. Accordingly, the regulations set a very high bar for extinguishment — a judicial proceeding and a finding that continued use of the property for conservation purposes has become impossible or impractical due to unexpected changed conditions.

Alternative procedures for extinguishment adopted by states, localities, or individual or groups of holders are unlikely to be as effective in carrying out Congress's intent regarding permanence because states, localities, and government and nonprofit holders craft extinguishment standards with their own interests, rather than federal interests, in mind.[159] Moreover, given that extinguishment should be the rare exception rather than the rule, there should be no need for alternative extinguishment procedures. particularly when the difficulties associated with assessing the relative effectiveness of different procedures as well as the likelihood of substantial inequities from state to state and program to program are taken into account. Accordingly, rather than relaxing the restrictions on extinguishment (an approach virtually guaranteed to increase the donation of marginal easements as well as abuse), greater care should be taken at the time of acquisition to ensure that federally subsidized easements protect properties that have unique or otherwise significant conservation values, and those values are likely to endure over time.[160]

The effectiveness of the federal tax incentive can also be viewed from a different perspective — that of encouraging conservation easement donations. The promise made to easement donors that their particular properties will be "protected in perpetuity," or at least until circumstances change so profoundly that continued use of the property for conservation purposes has become impossible or impractical, appears to be a major factor motivating many conservation easement donations.[161] If that promise could no longer be made, and states, localities, and holders were permitted to

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159. *See, e.g.*, *supra* note 157 and accompanying text.

160. *See* McLaughlin, *Conservation Easements: Perpetuity and Beyond*, *supra* note 41, at 706 (explaining that "the type of long-term protection afforded by perpetual conservation easements is not appropriate in all circumstances" and such easements should not be used indiscriminately).

161. *See* McLaughlin & Weeks, *In Defense of Conservation Easements*, *supra* note 55, at 15.

release, swap, or otherwise extinguish tax-deductible easements subject to standards that accord more weight to the short-term interests of the holder or the public than to the goal of protecting the properties' conservation values, the number of easement donations, at least by those primarily motivated by a desire to protect their land, could be expected to decline. In contrast, those motivated primarily by the prospect of receiving tax benefits would likely view the relaxing of restrictions on extinguishment as a possible way to maximize the financial benefits they can obtain from the transaction.[162]

Rather than interpreting the extinguishment regulation in a manner contrary to the intent of Congress and the drafters of the regulations, the proper course for those who wish to obtain a federal subsidy for the donation of conservation easements that may be modified or extinguished through a variety of procedures adopted by states, localities, or holders is to present a proposal for such a subsidy to Congress to be discussed and debated in a public process. It may be that the American public does not wish to subsidize the acquisition of conservation easements that are more easily modifiable and extinguishable in Montana or Michigan than in Maine or Minnesota. Moreover, any such federal subsidy, even if it had public support, should include detailed standards by which to assess the acceptability of the proposed modification and extinguishment procedures, as well as mechanisms to address the added valuation complexities, the dangers of parochialism, and the increased opportunities for abuse.

3. Federal and State Law Interaction

States are, of course, free to craft whatever modification and extinguishment procedures they deem appropriate for state-funded conservation easements, and many have done so.[163] Government and nonprofit holders are similarly free to raise funds and purchase conservation easements that are modifiable or terminable as they may see fit or upon the satisfaction of conditions of their choice, subject to whatever requirements might be imposed by the applicable state enabling statute and assuming they negotiate with the grantor for this discretion and memorialize such discretion in the easement deed (instead of representing that the easement is

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162. For example, if an easement increases in value relative to the value of the property it encumbers over time, and the holder's entitlement to proceeds upon extinguishment is limited to the minimum (or floor) percentage value established at the time of the easement's donation, the landowner could make a tidy sum through extinguishment. *See* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 510–12.

163. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, apps. a, b (surveying the state enabling statutes, some of which establish state-funded easement purchase programs).

perpetual).[164] To the extent landowners and holders wish to benefit from the federal charitable income tax deduction, however, they should be required to satisfy the requirements set forth in section 170(h) and the Regulations.

This does not mean that federal law preempts state law. Rather, it means that, to be eligible for the federal deduction, conservation easement donors must satisfy the requirements in section 170(h) and the regulations as well as any additional requirements that may be imposed on the creation, modification, or extinguishment of conservation easements under the applicable state enabling statute.[165] This is not a new concept. Congress is free to condition the receipt of federal tax incentives upon the satisfaction of federal requirements,[166] and it has been standard operating practice for well-represented easement donors to draft their easements to satisfy both state and federal requirements.[167]

As Judge Haines explained in *Carpenter*, in determining whether a conservation easement complies with the requirements for the deduction under section 170(h), one looks to state law to determine the nature of the property rights embodied in the easement, but "[f]"ederal law determines the appropriate tax treatment of those rights."[168] Accordingly, in determining whether a conservation easement complies with the extinguishment and proceeds requirements of Regulation section 1.170A-14(g)(6), one would look to the terms of the deed and state law to determine how the easement

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164. Much of the controversy over the manner in which conservation easements can be permissibly modified or terminated could be avoided if deeds expressly addressed the issue. If this were done, all parties in interest — donors, holders, the IRS, state attorneys general, funders, and the taxpaying public — would be on notice of the terms of the transaction.

165. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 20–26 (discussing the interaction of federal and state law in the conservation easement context).

166. *See, e.g.*, Estate of Gillespie v. Commissioner, 75 T.C. 374, 378–79 (1980) (whether a particular transfer qualifies for a federal estate tax charitable deduction is a matter of federal concern, and Congress may prescribe requirements for tax-deductible gifts to charity).

167. *See supra* note 125 and accompanying text.

168. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, 1004 T.C.M. (RIA) ¶ 2012-001 (2012) at 5. In a more recent case, the Tax Court explained this concept as follows:

> "A common idiom describes property as a 'bundle of sticks' . . . . State law determines *only* which sticks are in a person's bundle. . . . Once property rights are determined under State law, as announced by the highest court of the State, the tax consequences are decided under Federal law."

Patel v. Commissioner, Tax Ct. Rep. (CCH) Dec. 59,100, at 4665, Tax Ct. Rep. (RIA) Dec. 138.23, at 235 (2012) (emphasis added) (citations omitted) (quoting United States v. Craft, 535 U.S. 274, 278–79 (2002)).

may be extinguished, and then ask whether that easement, so configured, satisfies federal tax law requirements. If the holder can agree to extinguish the easement other than in a court proceeding upon a finding of impossibility or impracticality, or the holder is not entitled to at least its minimum proportionate share of proceeds following extinguishment, or the holder is not required to use those proceeds for similar conservation purposes, the conservation easement should not be tax-deductible. Similarly, if the conservation easement deed dutifully incorporates provisions that track the restriction on transfer, extinguishment, and proceeds regulations, but those provisions are qualified in some manner or are not legally binding on the parties, the easement should not be tax-deductible.

III. HARD CASES MAKE BAD LAW – *SIMMONS* AND *KAUFMAN*

Commissioner v. Simmons[169] and *Kaufman v. Commissioner (Kaufman III)*[170] both involved deductions for façade easement donations that the IRS challenged on a variety of grounds.[171] Although neither case directly addresses the extinguishment regulation at issue in *Carpenter*, two of the Circuit Courts' holdings in these cases may have an impact on the issue addressed in this Article — the circumstances under which government and nonprofit holders can agree to extinguish tax-deductible conservation easements.

As discussed below, the Circuit Court holdings in *Simmons* and *Kaufman III* evidence a decided impatience with the IRS's attempts to use litigation to establish clear rules in the conservation easement donation context. Unfortunately, that impatience led to holdings that are inconsistent with the statutory mandate that the conservation purpose of an easement be protected in perpetuity and open the door to loss of the federal investment and significant abuse. The holdings are examples of the old adage that "hard cases make bad law," which "refers to the danger that a decision operating harshly on the defendant may lead a court to make an unwarranted exception or otherwise alter the law."[172] The holdings are also contrary to the "familiar rule" that "an income tax deduction is a matter of legislative grace and . . . the burden of clearly showing the right to the claimed deduction is on the taxpayer."[173]

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169. Commissioner v. Simmons, 646 F.3d 6 (D.C. Cir. 2011).

170. *Kaufman III*, 687 F.3d 21 (1st Cir. 2012).

171. *Simmons*, 646 F.3d 6; *Kaufman III*, 687 F.3d 21.

172. *See* BRYAN A. GARNER, DICTIONARY OF LEGAL USAGE 403 (3d ed. 2011).

173. *See* INDOPCO, Inc. v. Commissioner, 503 U.S. 79, 84 (1992) ("deductions are strictly construed and allowed only 'as there is a clear provision therefor'").

On the positive side, the holdings will hopefully spur the IRS and the Treasury Department to focus some of their energy and resources on issuing forward-looking regulations and other guidance regarding how to satisfy the critically important protected-in-perpetuity requirements. Recommendations for such revisions and guidance are discussed in Part IV, but first, the bad law.

A. *Proceeds Regulation*

In two detailed and carefully considered "regular" opinions, the Tax Court held that Lorna Kaufman was not eligible for a deduction under section 170(h) for the donation of a facade easement due to a failure to comply with the proceeds regulation.[174] Although the easement contained a clause entitling the holder to the regulations' mandated minimum proportionate share of proceeds following extinguishment, the clause was qualified by an outside agreement with the bank that held a mortgage on the subject property at the time of the easement's donation. Rather than agreeing to subordinate its rights to the rights of the holder "to enforce the conservation purposes of the gift in perpetuity," as required by Regulation section 1.170A-14(g)(2) (the mortgage subordination regulation), the bank retained priority rights to all insurance or condemnation proceeds, including those paid following extinguishment of the easement. The Tax Court held that this constituted an impermissible qualification of the clause included in the easement to satisfy the proceeds regulation.

The First Circuit reversed, but its analysis is troubling. It noted that Lorna Kaufman "had no power to make the mortgage-holding bank give up its own protection against fire or condemnation."[175] While that certainly is true, it misses the point. The point is not whether Kaufman had the power to make the bank give up certain rights, but whether the conservation easement she donated satisfied the requirements of section 170(h) and the regulations and, in particular, the requirements intended to protect the public investment in the easement in the event of its extinguishment. If a lender refuses to subordinate its rights to the rights of the holder "to enforce the conservation purposes of the gift in perpetuity," which the First Circuit acknowledged

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174. Kaufman v. Commissioner (*Kaufman I*), 134 T.C. 182 (2010) and *Kaufman II*, 136 T.C. 294 (2011), *vacated and remanded in part*, *Kaufman III*, 687 F.3d 21 (1st Cir. 2012). "Regular" Tax Court opinions are generally issued in cases that the court believes involve sufficiently important legal issues or principles. *See* http://www.ustaxcourt.gov/taxpayer_info_after.htm#AFTER8. Regular opinions can be cited as legal authority and appealed, and the Tax Court treats them as binding precedent. *Id. See also* Peter A. Lowy, *U.S. Federal Tax Research*, 100-2d Tax. Mgmt. (BNA) A-63. For a reproduction of the proceeds regulation, see *supra* note 15.

175. *Kaufman III,* 687 F.3d at 26.

could be interpreted to include the holder's right to post-extinguishment proceeds,[176] the property owner has a number of options. The property owner could consider paying down the mortgage to a point at which the lender would be willing to so subordinate, paying off the mortgage, or refinancing with a different bank willing to so subordinate before making the donation. Alternatively, the property owner could not make the donation or make the donation but not claim federal tax benefits. In sum, the fact that a particular bank might refuse to subordinate its rights to the rights of the easement holder to receive its minimum proportionate share of post-extinguishment proceeds is not a justification for relaxing the regulations' specific requirements.[177]

The First Circuit's argument regarding superiority of tax liens is similarly unpersuasive.[178] The fact that tax liens may reduce the amount of proceeds available to be allocated between the two parties following extinguishment (the owner of the encumbered property and the holder of the easement) has nothing to do with whether it is appropriate for the property owner's lender to be given first priority to whatever proceeds are available. The holder of a conservation easement is the owner of a valuable property

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176. *See id.* at 27 n.5 (noting that the mortgage subordination requirement could be read broadly to require a lender to subordinate its rights to the right of the donee to receive post-extinguishment proceeds, which pursuant to the extinguishment regulation, must be used to advance conservation purposes). *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 492–94 (arguing that this is the correct interpretation of the mortgage subordination requirement on technical grounds and because the value attributable to "the gift" that was made for the benefit public and for which a federal subsidy was provided should remain in the charitable sector and be devoted to similar conservation purposes, as opposed to being paid to the landowner's lender). Because the IRS "disclaimed" this reading of the mortgage subordination requirement, the First Circuit did not pursue the issue. *Kaufman III,* 687 F.3d at 27 n.5.

177. It also is not clear that Kaufman's bank refused to subordinate its rights to the rights of the easement holder to receive its minimum proportionate share of post-extinguishment proceeds. The bank may have been presented with only the "limited" subordination agreement at issue in the case since that appears to have been the standard form used in the historic preservation context. *See infra* note 182 and accompanying text. It may be that lenders would be willing to fully subordinate their rights to the holder's right to receive a share of post-extinguishment proceeds, if asked, if the debt to equity ratio would remain sufficiently low after the donation of the easement.

178. *Kaufman III*, 687 F.3d at 26 ("the Kaufmans had . . . no power to defeat tax liens that the city might use to reach the . . . insurance proceeds — tax liens being superior to most prior claims").

right on behalf of the public[179] and should be entitled to receive the portion of the post- extinguishment proceeds attributable to that property right in preference to the landowner's lender, whose security interest should be limited to the proceeds attributable to the property owner's property interest (i.e., the encumbered property). It also should not be acceptable to relegate the holder of a conservation easement to obtaining its portion of the available proceeds from the property owner. The regulations appropriately provide that the holder must be entitled to a portion of "the proceeds" following extinguishment, not that the holder should have a potentially expensive-to-pursue claim against the possibly judgment-proof property owner for its portion.[180]

The First Circuit's holding appears to have been driven more by its irritation with the IRS's strategy of using litigation to establish clear rules in this context than a desire to ensure that holders of conservation easements receive a share of proceeds following extinguishment to be used to replace lost conservation values on behalf of the public. The First Circuit also seems to have been particularly influenced by the arguments made by the National Trust for Historic Preservation (NTHP) in its amicus brief filed in support of the taxpayer.[181]

The NTHP argued that the type of "limited" subordination agreement obtained by Kaufman had "been widely used for decades in thousands of easements without a reported objection by the [IRS]," and that the Tax Court's rulings in *Kaufman*, if allowed to stand "could disallow tax deductions for thousands of easement donations across the country."[182] However, the historic preservation organizations should have known that limited subordination agreements might not comply with federal tax law requirements. The commentary to the model conservation easement in the Conservation Easement Handbook published in 1988 explains that a limited subordination agreement is intended to "neutralize" the provision included in a conservation easement deed to satisfy the regulation's proceeds requirement, but notes that the assumption that such an agreement satisfies the requirements under section 170(h) and the regulations is "untested."[183] The 2005 edition of the handbook similarly notes the disagreement within the land trust community over whether such agreements comply with federal

179. *See* Reg. § 1.170A-14(g)(6)(ii) ("for a deduction to be allowed . . . at the time of the gift the donor must agree that the donation of the [easement] gives rise to a property right, immediately vested in the donee organization").

180. *Id.*

181. Brief for the National Trust for Historic Preservation as Amicus Curiae Supporting Petitioners, *Kaufman III*, 687 F.3d 21 (1st Cir. 2012) (No. 15997-09) [hereinafter NTHP Brief, *Kaufman III*].

182. *Id.* at 6–7.

183. *See* Diehl, 1988 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 207.

tax law requirements.[184] Accordingly, the historic preservation organizations arguably should have worked with a taxpayer to request a private letter ruling or other guidance from the IRS before endorsing the use of an untested and potentially noncompliant subordination agreement in thousands of donation transactions.[185]

The NTHP also asserted that the Tax Court's ruling in *Kaufman II*, if affirmed, would "halt the voluntary donation of conservation easements involving mortgaged properties."[186] Whether that assertion is accurate with regard to façade easement donations is unclear.[187] That assertion is not accurate with regard to the donation of conservation easements encumbering land. Donors to organizations accepting large numbers of such conservation easements have been able to secure "full" subordination agreements from lenders, in which the lenders agree to subordinate their rights to all of the rights of the holder under a conservation easement, including, implicitly, the holder's right to receive its minimum percentage share of proceeds following extinguishment.[188] In addition, the Land Trust Alliance is advising donors to

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184. *See* Byers, 2005 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 456 (explaining that, although some practitioners think limited subordinations are permissible, "[o]thers would argue, at least with respect to extinguishment, that the division-of-proceeds requirement is what allows 'the conservation purpose' of the grant to 'nonetheless be treated as protected in perpetuity' in the eyes of the IRS, and a lender must therefore subordinate to it as well").

185. *See supra* note 173 and accompanying text (explaining that deductions are a matter of legislative grace and the burden is on the taxpayer to show he has a right to the claimed deduction). Although conservation easement donors should be and often are represented by their own legal counsel, as a practical matter many rely in large part on the donee and the donee's "template" easement and supporting documents because the donee is a repeat player.

186. NTHP Brief, *Kaufman III*, *supra* note 181, at 23.

187. *See supra* note 177.

188. For example, the Virginia Outdoors Foundation, which holds most of the easements conveyed in the state of Virginia, uses a template conservation easement that provides for the lender's subordination of its rights to all the rights of the holder under the easement, including, implicitly, the holder's right to proceeds upon extinguishment. *See* Va. Outdoors Found., *Easement Documents and Forms*, VOF EASEMENT TEMPLATE, 18 (May 10, 2011), http://www.virginiaoutdoorsfoundation.org/VOF_land-documents.php; *see also* Opening Brief for Respondent at 61–62 n.13, *Kaufman I*, 134 T.C. 182, *adhered to on denial of reconsideration by*, 136 T.C. 294 (No. 15997-09) (explaining that the Compact of Cape Cod Conservation Trusts uses a subordination agreement template in which the lender "agrees to subordinate and hold its mortgage subject to the terms and provisions of [the conservation easement] to the same extent as if said mortgage had been recorded subsequent to the recording of [the conservation easement]").

continue to obtain full subordination agreements from lenders, despite the First Circuit's holding in *Kaufman III*.[189]

Although the façade easement donors, the historic preservation organizations, and the IRS all bear some blame in this context, the First Circuit clearly sympathized with the predicament in which the donors and historic preservation organizations found themselves following the Tax Court's rulings in *Kaufman II*. The First Circuit also objected to the IRS's "impromptu reading" of the proceeds regulation,[190] which can be viewed as an objection to the IRS's attempt to enforce its interpretation of the regulation without having provided taxpayers with fair warning regarding that interpretation.

An unfortunate result of the First Circuit's holding on this issue may be a nationwide race to the bottom regarding subordination agreements. Lenders that previously were willing to sign full subordination agreements are unlikely to agree to continue to do so if it is not necessary to secure the deduction. This, in turn, will mean that the valuable property interest — the easement — that was conveyed as a charitable gift to the government or nonprofit holder to be held and enforced for the benefit of the public, and in which the public heavily invested, may incongruously serve as security for the donor's debt in the event of extinguishment. Thus, donors will be poised to obtain a double benefit or windfall from conservation easement donations: (1) a sizable charitable income tax deduction upon the donation plus (2) use of the proceeds attributable to the easement (the charitable gift) upon extinguishment to pay down the donor's debt on the subject property instead of being paid to the holder to replace lost conservation values. In fact, the ability to "neutralize" the clause included in a conservation easement deed to satisfy the proceeds requirement in this manner may encourage donors to obtain mortgages on their properties before donating easements, perhaps even through controlled entities where the sole purpose of the mortgage is to neutralize the proceeds clause.

If it truly is impossible to obtain full subordination agreements in the façade easement donation context, the proper solution is not the First Circuit's race to the bottom approach with regard to all easement donations. Rather, Congress and the Treasury Department should consider whether continued investment in façade easements on properties subject to mortgages is worth the risk of the loss of that investment in the event of extinguishment.

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189. *See* LAND TRUST ALLIANCE, *IRS and Tax Court Overturned Again*, http://www.landtrustalliance.org/conservation/conservation-defense/conservation-defense-news/irs-and-tax-court-overturned-again (last visited Sept. 23, 2012) ("Donors still must obtain a lender subordination to the *entire* conservation easement, including the payment on extinguishment clause, and record it *at the same time* as the conservation easement despite this new ruling.") (emphasis in original).

190. *Kaufman III*, 687 F.3d 21, 27 (1st Cir. 2012).

If the answer to that question is yes, appropriate rules should be developed to minimize the risk. For example, the regulations could be revised to permit limited subordination agreements, but only if the debt-to-equity (or loan to value) ratio is sufficiently low at the time of the donation and, thus, the risk that the public would lose its investment in the event of extinguishment is minimal.

B. *Rights to Change or Abandon Easements*

The First Circuit in *Kaufman III* also agreed with the D.C. Circuit's holding in *Simmons* that it is permissible for the donor of a tax-deductible perpetual conservation easement to grant the holder the right to consent to changes to or abandon some or all of its rights under the easement.[191] The First Circuit adopted the D.C. Circuit's problematic and contradictory explanations for this holding, namely that (1) "[a]ny donee might fail to enforce a conservation easement, with or without a clause stating it may consent to a change or abandon its rights," (2) a tax-exempt holder would exercise such rights "at its peril," but (3) a holder needs such rights "to accommodate such change as may become necessary to make a building livable or usable for future generations while still ensuring the change is consistent with the conservation purpose of the easement."[192] There are a number of serious problems with this holding and the contradictory explanations.

1. *Noncompliance with Regulations*

The change and abandonment language at issue in *Kaufman* and *Simmons* impermissibly qualifies the clause included in the deeds to comply with the restriction-on-transfer requirement of Regulation section 1.170A-14(c)(2):

> Grantee covenants and agrees that it will not transfer, assign or otherwise convey its rights under this conservation easement except to another "qualified organization" described in Section 170(h)(3) of the Internal Revenue Code of 1986 and controlling Treasury Regulations, and Grantee further agrees that it will not transfer this easement unless the transferee first agrees to continue to carry out the conservation purposes for which this easement was created,

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191. *Id.* at 28. For criticism of the D.C. Circuit's holding and analysis with respect to this issue in *Simmons*, see McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 11–19.

192. *Kaufman III*, 687 F.3d at 28.

> *provided, however, that nothing herein contained shall be construed to limit the Grantee's right to give its consent (e.g., to changes in a Façade) or to abandon some or all of its rights hereunder*.[193]

Neither Circuit Court explained how the italicized proviso is consistent with the restriction on transfer, extinguishment, or proceeds regulations, given that a holder could transfer or extinguish an easement by abandoning its rights thereunder, and, pursuant to the proviso, could do so without complying with the restriction on transfer, extinguishment, or proceeds requirements.[194] In addition, even absent the proviso, the clause fails to state that the transferee, at the time of the transfer, must qualify as an "eligible donee" as required by Regulation section 1.170A-14(c)(2).[195] Moreover, neither court acknowledged that a holder could exercise the right to consent to changes that are not consistent with the purpose of the easement in violation of the requirement that the conservation purpose of the easement be protected in perpetuity.[196]

2. *Tax-Exempt Rules Do Not Ensure Protection in Perpetuity*

The First Circuit in *Kaufman III* stated that the concern posited by the IRS — that the proviso gives the holder a blank check to consent to changes or abandon an easement — can be addressed by "the IRS's own regulations," which "require that tax-exempt organizations . . . be operated

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193. Conservation Easement Deed of Gift between Dorothy Simmons, Grantor, and The L'Enfant Trust, Grantee 3 (Nov. 18, 2003) (on file with author) (emphasis added); Conservation Easement Deed of Gift between Ms. Dorothy Simmons, Grantor, and The L'Enfant Trust, Grantee 3 (Jan. 26, 2004) (on file with author) (emphasis added). *See also* Preservation Restriction Agreement Between Lorna E. Kaufman, Grantor, and the National Architectural Trust, Inc., Grantee 4 (Dec. 22, 2003) (on file with author).

194. In assessing the acceptability of the proviso, both Circuit Courts focused solely on the general requirement in Regulation section 1.170A-14(g)(1), and neither mentioned Regulation section 1.170A-14(c)(2) (the restriction on transfer regulation) or Regulation section 1.170A-14(g)(6)(i) and (ii) (the extinguishment and proceeds regulations).

195. Reg. § 1.170A-14(c)(2) ("subsequent transfers must be restricted to organizations qualifying, at the time of the subsequent transfer, as an eligible donee under paragraph (c)(1) of this section"). An "eligible donee" is "a qualified organization [that has] a commitment to protect the conservation purposes of the donation, and [has] the resources to enforce the restrictions" as specified in Regulation section 1.170A-14(c)(1).

196. I.R.C. § 170(h)(5)(A).

'exclusively' for charitable purposes."[197] However, the requirement that a tax-exempt organization operate exclusively for charitable purposes does not ensure that the conservation purposes of tax-deductible conservation easements will be protected in perpetuity as required by section 170(h)(5)(A) and the regulations.

First, many state and local government entities accept tax-deductible conservation easement donations and those entities are not subject to the rules governing tax-exempt organizations — a fact the Circuit Courts did not address. Thus, counties, cities, towns, community development authorities, and other state and local government entities granted unlimited rights to consent to changes or abandon tax-deductible conservation easements would be free to exercise those rights without any fear of losing tax-exempt status.

In addition, while a nonprofit holder could lose its tax-exempt status for consenting to a change or abandoning a conservation easement and thereby conferring an impermissible private benefit on the property owner, it is not clear that such a holder would risk losing its tax-exempt status for agreeing to change or abandon (i.e., extinguish) an easement, in whole or in part, provided it received adequate compensation and used that compensation consistent with its general charitable mission. The requirement that a tax-exempt organization operate exclusively for charitable purposes means the organization must engage primarily in activities that accomplish one or more of the exempt purposes specified in section 501(c)(3) and not confer impermissible benefits on private parties.[198] That requirement is not designed to ensure that the conservation purposes of tax-deductible conservation easements are protected in perpetuity as required by section 170(h)(5)(A).

Accordingly, pursuant to the proviso at issue in *Simmons* and *Kaufman*, a nonprofit holder might be able to agree to release the restrictions in or abandon a conservation easement, in whole or in part, in exchange for cash to be added to the holder's general operating funds without risking loss of tax-exempt status. Converting what were supposed to be perpetual conservation easements to cash could obviously prove very lucrative for nonprofits. A nonprofit holder might also be able to agree to abandon (i.e., extinguish) a conservation easement in exchange for a new conservation easement encumbering a different property (i.e., the holder could agree to exercise its right to abandon to effectuate a "swap") without risking loss of

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197. *Kaufman III*, 687 F.3d at 28.

198. *See* STAFF OF JOINT COMM. ON TAXATION, HISTORICAL DEVELOPMENT AND PRESENT LAW OF THE FED. TAX EXEMPTION FOR CHARITIES AND OTHER TAX-EXEMPT ORGS. 49, 52–53 (Comm. Print 2005), https://www.jct.gov/publications.html?func=startdown&id=1586. Prohibited private benefit and private inurement can occur in many different forms, including receipt of less than fair market value on the sale or exchange of property. *See id*. at 53.

tax-exempt status.[199] Indeed, in the amicus brief filed in support of the taxpayer in *Simmons*, the NTHP and other historic preservation organizations stated that they view the abandonment proviso as granting them the right to freely engage in swaps:

> Affording a conservation easement-holding organization the right to abandon an easement also is sound policy, if the circumstances of the abandonment would result in a significantly greater public benefit. For example, the organization might decide to enter an agreement with a developer that releases a single easement (e.g., on a single, modest building next to a Metro stop) in exchange for easements on significant additional properties (e.g., an entire block of nearby buildings). The right to say yes or no in such a circumstance . . . allows a responsible easement-holding organization to fulfill its mission and to ensure that historic preservation can co-exist with changing times.[200]

However, Congress clearly did not intend, through section 170(h), to subsidize the acquisition of conservation easements that would be fungible or

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199. Swaps, which involve the removal of property from an easement's restrictions in exchange for the encumbrance of some other property, are sometimes referred to as "trades" or "reconfigurations."

200. Brief for the National Trust for Historic Preservation et al. as Amici Curiae Supporting Appellee at 16–17, Commissioner v. Simmons, 646 F.3d 6 (D.C. Cir. 2011) (No. 10-1063). This position is directly contrary to the position taken by the Land Trust Alliance in its 2007 report on conservation easement amendments, which instructs:

> If the conservation easement was the subject of a federal income tax deduction, then Internal Revenue Code Section 170(h) and the Treasury Regulations Section 1.170A-14 apply. Such an easement must be "granted in perpetuity" and "the conservation purpose [of the contribution must be] protected in perpetuity." The easement must be transferable only to another government entity or qualified charitable organization that agrees to continue to enforce the easement. The easement can only be extinguished by the holder through a judicial proceeding, upon a finding that continued use of the encumbered land for conservation purposes has become "impossible or impractical," and with the payment to the holder of a share of proceeds from a subsequent sale or development of the land to be used for similar conservation purposes.

Land Trust Alliance, *Amending Conservation Easements*: *Evolving Practices and Legal Principles*, Research Report 24 (August 2007), http://learningcenter.lta.org/attached-files/0/65/6534/Amendment_Report_Final_web.pdf [hereinafter Land Trust Alliance, *Amending Conservation Easements*].

liquid assets in the hands of their government or nonprofit holders.[201] Moreover, Congress was acutely aware of the potential for abuse in this context. During the congressional hearings leading up to the enactment of section 170(h), concern was expressed that the laws and restrictions that bind charitable organizations generally are not sufficient to ensure tax-deductible conservation easements will continue to be used for the purposes for which they were donated.[202] In his testimony before Congress, the Treasury Department's then Deputy Assistant Secretary for Tax Policy, Daniel Halperin, explained:

> [I]t is not clear to us whether procedures exist to insure that a donated partial interest in property, such as a conservation easement contributed to a private charitable organization, will continue to be used for conservation purposes and for the benefit of the general public. Without mechanisms to insure the continued use of the donated interest for such purposes, it is not clear that the public interest is being properly served.[203]

Accordingly, in enacting section 170(h) in 1980, Congress imposed substantial new limitations on the deduction.[204] In particular, Congress did *not* rely on the general requirement that tax-exempt organizations operate exclusively for charitable purposes to ensure the proper administration and enforcement of tax-deductible easements over the long term. Instead, Congress specifically added the protected-in-perpetuity requirement to section 170(h)(5)(A) and provided significant guidance regarding the meaning of that new requirement in the legislative history, including its expectation that holders would not be free to sell, trade, release, or otherwise transfer tax-deductible perpetual conservation easements, except for transfers made to other qualified holders that agree to continue to enforce the

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201. *See generally* S. REP. NO. 96-1007, *supra* note 2, *reprinted in* 1980 U.S.C.C.A.N. 6736. *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 476–87 (discussing the history of the deduction provision).

202. *See, e.g.*, *Miscellaneous Tax Bills: Hearing Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 96th Cong. 5–6, 12 (1979) [hereinafter *Miscellaneous Tax Bills: Hearing*] (statement of Daniel I. Halperin, Deputy Assistant Secretary for Tax Policy, Department of the Treasury).

203. *Id*. at 12.

204. *See generally*, S. REP. NO. 96-1007, *supra* note 2, *reprinted in* 1980 U.S.C.C.A.N. 6736. *See also*, McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 478–80.

easements.[205] The Treasury Department then incorporated much of the legislative history into the regulations in the form of the restriction on transfer and other perpetuity-related requirements.[206]

Moreover, with regard to swaps specifically, this author has previously explained:

> [T]o be eligible for the federal subsidy under section 170(h), a conservation easement must satisfy one or more of the fairly elaborate conservation purposes tests as well as the myriad other requirements in section 170(h) and the Treasury Regulations at the time of its donation. If swaps were permissible, the owner of the land and the holder of the easement could, on the day following the donation or any time thereafter, agree to remove ten, fifty, or even one hundred percent of the original land from the protection of the easement in exchange for the protection of some other land, and the new land and the provisions governing its protection would not have to meet the threshold conservation purposes tests or any of the other requirements in section 170(h) and the Treasury Regulations. Permitting swaps would thus render satisfaction of the threshold conservation purposes tests and other requirements in section 170(h) and the Treasury Regulations a meaningless exercise . . . .[207]

Permitting holders to agree to swaps would also violate the restriction on transfer, extinguishment, and proceeds regulations, as those regulations prohibit swaps except in carefully prescribed circumstances — i.e., when it can be shown to the satisfaction of a court that continuing to use the originally protected property for conservation purposes has become impossible or impractical, the holder receives something of sufficient value in exchange (worth at least its minimum proportionate share of proceeds), and the protection of the new property is "consistent with the conservation purposes of the original contribution."[208] In a March 2012 Information

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205. *See* S. REP. NO. 96-1007, *supra* note 2, pt. II, at 13–14, *reprinted in* 1980 U.S.C.C.A.N. at 6748–49. *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 475–76.

206. *See* Regs. §§ 1.170A-14(b)(2), -14(c), -14(e), -14(g)(1)-(6). *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 487–513 (describing the requirements in the regulations).

207. *See* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 520–23. The goal of a swap is to free property from an easement's restrictions so that the property can be put to previously prohibited uses.

208. *See* Regs. §§ 1.170A-14(c)(2), -14(g)(6).

Letter, the IRS confirmed that the contribution of a conservation easement that authorizes swaps other in accordance with the extinguishment and proceeds requirements of Regulation section 1.170A-14(g)(6) will not be eligible for a federal charitable income tax deduction under section 170(h).[209]

3. *Rights to Change or Abandon May Render Conservation Easement Provisions Nonbinding*

As explained above, Congress did not rely on the general requirement that tax-exempt organizations operate exclusively for charitable purposes to ensure the proper administration and enforcement of tax-deductible easements over the long term. Instead, Congress added the protected-in-perpetuity requirement to section 170(h)(5)(A) and provided significant guidance regarding the meaning of that new requirement in the legislative history. The Treasury Department then incorporated much of the legislative history into the regulations, which contain numerous requirements intended to ensure that the conservation purpose of a tax-deductible conservation easement will be protected in perpetuity.

In most cases, donors satisfy these perpetuity-related requirements by including specific clauses in the conservation easement deed that track the regulations, such as restriction on transfer, extinguishment, and proceeds clauses.[210] Absent qualification, these clauses should be legally binding on both parties to the easement (the owner of the subject property and the holder of the easement) because, as recognized by the Tax Court in *Carpenter*, a tax-deductible conservation easement should constitute a restricted gift under state law, or a contribution conditioned on the use of the gift in accordance with the donor's precise directions and limitations. In addition, the state attorney general should have standing to sue the holder for failing to administer and enforce the easement consistent with its stated terms and purpose.[211]

Where the holder is granted an unlimited right to consent to changes or abandon an easement as in *Simmons* and *Kaufman*, however, the legally binding nature of the easement terms under state law is called into question.[212] A state court faced with interpreting a conservation easement

209. IRS Information Letter No. 2012-0017 (March 5, 2012), 2012 TNT 66–25, http://www.irs.gov/pub/irs-wd/12-0017.pdf.

210. *See supra* note 125 and accompanying text.

211. *See supra* note 47 and accompanying text.

212. The right to consent to changes and abandon the easements granted to the holders in *Simmons* and *Kaufman* is expressly *not* limited by other provisions in the deeds. The proviso states that "*nothing herein contained shall be construed to limit the Grantee's right* to give its consent (e.g., to changes in the Façade) or to abandon some or all of its rights hereunder." *See supra* note 193 and accompanying text (emphasis added).

that grants the holder such a right may find that the holder can exercise that right in any manner (e.g., to modify, swap, or extinguish the easement in whole or in part), provided only that such action is consistent with the holder's general public or charitable mission.[213] Accordingly, granting the holder the unlimited right to consent to changes or abandon a conservation easement may render the restriction on transfer, extinguishment, proceeds, and other provisions included in the easement deed to satisfy federal tax law requirements nothing more than window dressing (to be abided by until the statute of limitations has run on the donor's deduction and then amended away, renegotiated, or simply ignored as the holder and owner may see fit from time to time).

The D.C. Circuit and the First Circuit did not recognize that, to ensure the conservation purposes of tax-deductible conservation easements are protected in perpetuity as required by section 170(h)(5)(A), the easements must be constructed in such a manner that both the property owner *and* the government or nonprofit holder will be legally bound by the easement terms. It makes little sense, for example, to mandate that the instrument of conveyance prohibit the holder from transferring the easement except to another eligible donee that agrees to continue to enforce the easement if the holder is free (after the statute of limitations has run on the donor's deduction) to amend away, renegotiate, or ignore that provision.

4. *Local Law Does Not Ensure Protection in Perpetuity*

The D.C. Circuit in *Simmons* also implied that the conservation purposes of the façade easements at issue were protected in perpetuity because "any change in the façade to which [the holder] might consent would have to comply with all applicable laws and regulations, including the District's historic preservation laws."[214] However, although there often is substantial overlap between historic preservation laws and the restrictions in a façade easement, historic preservation laws are subject to change, which is the reason for layering a perpetual conservation easement on the property (i.e., historic preservation laws do not ensure that the conservation purposes will be protected in perpetuity in the manner required by section 170(h) and the

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213. Any conditions imposed on the modification or extinguishment of conservation easements under state law would presumably have to be satisfied, but many state enabling statues impose no such conditions. *See generally*, McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5. In addition, the conditions that are imposed in some states generally are not consistent with federal tax law requirements. *See id.*

214. Commissioner v. Simmons, 646 F.3d 6, 11 (D.C. Cir. 2011).

regulations).[215] Moreover, this imperfect backstop is generally not present in the context of conservation easements encumbering land (*i.e.*, conservation easements encumbering land typically do not merely duplicate state or local restrictive zoning or other laws; they impose substantial new restrictions on the development and use of the property). Accordingly, government and nonprofit holders granted the unlimited right to consent to changes or abandon conservation easements encumbering land would generally be able to exercise those rights to reduce or eliminate the protection of the land's conservation values. Whether this makes the rulings on this issue in *Simmons* and *Kaufman III* inapplicable to conservation easements encumbering land is not clear, as neither of the Circuit Courts discussed this issue.

5. *Accommodating Change Does Not Require Unlimited Rights to Change or Abandon*

A word is also in order concerning the amici curiae's representations regarding the need for flexibility to respond to changing conditions. The amici argued (and the Circuit Courts assumed) that the consent and abandonment proviso is "needed to allow a charitable organization that holds a conservation easement to accommodate such change as may become necessary 'to make a building livable or usable for future generations' while still ensuring that change is consistent with the conservation purpose of the easement."[216] But the amici failed to inform the Circuit Courts that it is fairly standard practice within the land trust community and consistent with the Land Trust Alliance's recommended best practices to address the need to be able to respond to changing conditions — and at the same time comply with the protected-in-perpetuity requirement of section 170(h)(5)(A) — by including an appropriately limited "amendment clause" in the easement deed.[217] The typical amendment clause grants the holder the express right to agree to changes or amendments, *but only if the amendments are, among*

215. Whether a façade easement has any value is a separate issue. Where the restrictions in a façade easement are substantially identical to those imposed by state or local historic preservation laws, there is little likelihood that such laws will be changed, and the holder has the unlimited right to consent to changes or abandon the restrictions in the easement in any event, one would expect the easement to have little or no value.

216. *Simmons*, 646 F.3d at 10; *Kaufman III*, 687 F.3d 21, 28 (1st Cir. 2012).

217. *See, e.g.*, Byers, 2005 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 377 ("Amendment provisions are becoming more common to assure and limit the Holder's power to modify." (emphasis omitted)); Land Trust Alliance, *Amending Conservation Easements*, *supra* note 200, at 17 ("Easement holders should include an amendment clause to allow amendments consistent with the easement's overall purposes, subject to applicable laws.").

other things, consistent with the conservation purpose of the easement.[218] In fact, since its first publication in 1988, the Conservation Easement Handbook has contained model "restriction on transfer" provisions that are not qualified as in *Simmons* and *Kaufman III*, as well as model "amendment clauses" that specifically limit amendments to those that are consistent with the purpose of the easement.[219] Such provisions are all that is needed to "allow a charitable organization that holds a conservation easement to accommodate such change as may become necessary 'to make a building livable or usable for future generations' while still ensuring the change is consistent with the conservation purpose of the easement."[220]

In sum, the holdings in *Simmons* and *Kaufman III* sanctioning the deductibility of conservation easements that grant the holder the unlimited right to consent to changes or abandon its rights under the easement are contrary to the restriction on transfer, extinguishment, proceeds, and other protected-in-perpetuity requirements in section 170(h) and the regulations. The holdings also create the potential for the improper modification, swapping, and extinguishment of tax-deductible easements and, thus, significant abuse.[221] While both Circuit Courts contemplated that a holder

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218. The typical amendment clause generally provides as follows:

> *Amendment*. If circumstances arise under which an amendment to or modification of this Easement would be appropriate, Grantors and Grantee are free to jointly amend this Easement; provided that no amendment shall be allowed that will affect the qualification of this Easement or the status of Grantee under any applicable laws, including [state statute] or Section 170(h) of the Internal Revenue Code . . . and *any amendment shall be consistent with the purpose of this Easement*, and shall not affect its perpetual duration. Any such amendment shall be recorded in the official records of __________ County, [state].

Diehl, 1988 CONSERVATION EASEMENT HANDBOOK, *supra* note 53, at 164 (emphasis added).

219. *See id.* at 161, 220–21 (providing model restriction on transfer provisions); *supra* note 218 (reproducing a model amendment provision).

220. *Simmons*, 646 F. 3d at 10.

221. For cases involving holders' agreements to improperly modify or extinguish tax-deductible perpetual conservation easements, see McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at pt. III.B. One such case — the Myrtle Grove controversy — involved the NTHP's agreement to amend a tax-deductible conservation easement protecting a 160-acre historic tobacco plantation from subdivision to allow a seven-lot upscale residential subdivision on the property. *Id.* at 28–30. The Maryland Attorney General filed suit objecting to the amendment on the grounds that the easement was a charitable gift held for the benefit of the public and it could not be amended as proposed without court approval and a finding that continuing to protect the property's conservation and historic values had become impossible or impractical (which it had not). The case eventually settled with the easement remaining intact. The Myrtle Grove easement did not grant the holder the

would be able to exercise its unlimited right to consent to changes or abandon an easement only in a manner consistent with the conservation purposes of the easement,[222] neither provided a convincing rationale for that conclusion.

An argument might be made that a holder that agrees to amend or abandon a conservation easement in a manner contrary to its stated conservation purposes, or to transfer, swap, or extinguish an easement in a manner contrary to the restriction on transfer, extinguishment, and proceeds regulations, should no longer qualify as an "eligible donee."[223] An argument might also be made that donations to such a holder should not be deductible because they cannot satisfy the protected-in-perpetuity requirement. Such arguments, however, even if successful, would do nothing to ensure the protection of existing conservation easements. Moreover, Congress never intended for the federal investment in conservation easements and the conservation values they are intended to protect in perpetuity to hang by such a precarious thread. Rather, Congress intended that tax-deductible easements would specifically prohibit the holder from transferring the easement except to another qualified organization that agrees to continues to enforce the easement, and that the Treasury Department would craft rules to protect the public investment in the unlikely event that a state court extinguishes an easement due to frustration of its purpose (which the Treasury Department did). The Circuit Courts in *Simmons* and *Kaufman III* ignored this history and their holdings significantly undermine the protection of the federal investment in conservation easements over the long term. Accordingly, the holdings sanctioning use of the change and abandonment proviso should be limited to the D.C. and First Circuits and façade easement donations and, as noted below, the Treasury and the IRS should address the problem in those circuits through forward looking regulations or other guidance.

C. First Circuit's Advice

In the latter part of its opinion in *Kaufman III*, the First Circuit addressed the issue of valuation.[224] It chastised the IRS for attempting to convert the "inherently factual issue" of valuation into a set of violations of the

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right to consent to changes or abandon its rights under the easement. *See* McLaughlin, *Conservation Easements: Perpetuity and Beyond*, *supra* note 41, at 690–93. For concerns about amendments, see *infra* Part IV.B.

222. Both opinions state "[t]he clauses permitting consent and abandonment . . . have no discrete effect upon the perpetuity of the easements." *Simmons*, 646 F.3d at 10; *Kaufman III*, 687 F.3d at 28. *Simmons* also states "the donated easements will prevent in perpetuity any changes to the properties inconsistent with conservation purposes." *Simmons*, 646 F.3d at 11.

223. *See* Reg. § 1.170A-14(c)(1) (defining "eligible donee").

224. *Kaufman III*, 687 F.3d at 29.

procedural requirements relating to the appraisal of an easement "in disregard of the[] language and purpose" of those requirements.[225] The First Circuit also noted, however, that façade easements that duplicate local law restrictions may be worth little or nothing,[226] that a holder receiving large cash contributions from easement donors has a substantial economic incentive to facilitate donation transactions and ensure high valuations, and that appraisers who receive fees for a succession of appraisals for gifts of easements "assuredly" have an interest in remaining on the list of those recommended by holders to potential easement donors.[227] The First Circuit acknowledged the legitimacy of the IRS's concerns about abuse in the easement donation context[228] as well as the "difficulty of detecting and investigating suspicious cases one by one."[229] It then suggested a way for the IRS to address valuation abuse in lieu of its current tactic of "overly aggressive . . . interpretations of existing regulations:"

> Without stifling Congress' aim to encourage legitimate easements, *one can imagine IRS regulations that* require appraisers to be functionally independent of donee organizations, curtail dubious deductions in historic districts where local regulations already protect against alterations, and require more specific market-sale based information to support any deduction. *Forward looking regulations also serve to give fair warning to taxpayers* .[230]

Kaufman III is not the first case in which a court has expressly invited the Treasury Department to amend its regulations.[231] Although the First Circuit offered this advice with regard to the regulations relating to

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225. *Id.*

226. *Id. at 31. See also supra* note 215.

227. *Kaufman III*, 687 F.3d at 32.

228. *Id.* ("we do not question the IRS's concern, transcending this case, that individuals and organizations have been abusing the conservation statute 'to improperly shield income or assets from taxation'").

229. *Id.*

230. *Id.* (emphasis added).

231. *See, e.g.*, Estate of Petter v. Commissioner, 653 F.3d 1012, 1023–24 (9th Cir. 2011) ("[W]e expressly invite[ ] the Treasury Department to 'amend its regulations' if troubled by the consequences of our resolution of th[is] case.") (quoting Mayo Found. for Med. Educ. & Research v. United States, 131 S. Ct. 704, 713 (2011) (quoting United Dominion Indus., Inc. v. United States, 532 U.S. 822, 838 (2001))); Scheidelman v. Commissioner, 682 F.3d 189, 198 (2d Cir. 2012) ("[O]f course, the Treasury Department can use the broad regulatory authority granted to it by the Internal Revenue Code to set stricter requirements for a qualified appraisal.").

valuation, the same advice applies with even greater force to the regulations that implement section 170(h)(5)(A)'s protected-in-perpetuity requirement. As noted in the Introduction, the enormous up-front investment in tax-deductible conservation easements will be for naught if the purportedly perpetual protections prove to be ephemeral because government and nonprofit holders are able to release, sell, swap, or otherwise extinguish the easements in disregard of the restriction on transfer, extinguishment, proceeds, and other perpetuity-related requirements. It is not enough that conservation easement donors accurately value the easements, properly substantiate their donations, and satisfy the conservation purposes tests under section 170(h); they must also comply with the critically important protected-in-perpetuity requirements.

IV. CHARTING A COURSE

Carpenter provides significant guidance regarding the meaning of section 170(h)'s protected-in-perpetuity requirement and the operation of the extinguishment regulation in particular. It tells us that the so-remote-as-to-be-negligible standard in the regulations cannot be invoked to forgive a failure to comply with the extinguishment regulation. It tells us that conservation easements extinguishable by mutual agreement of the parties, even if subject to a standard such as impossibility, fail as a matter of law to comply with the extinguishment regulation. It tells us that the extinguishment regulation provides taxpayers with a guide by which to incorporate the necessary restrictions on extinguishment into a conservation easement deed. And it indicates that tax-deductible conservation easements, which are by definition charitable gifts made for a specific purpose, should be treated as restricted gifts under state law, or "contributions conditioned on the use of [the] gift in accordance with the donor's precise directions and limitations."[232]

The confusion *Carpenter* created with respect to the state law doctrine of *cy pres* is unfortunate, but could be easily remedied by clarifying the doctrine's operation in future Tax Court decisions or at the state court level. The speculation regarding the manner in which tax-deductible easements may be permissibly extinguished is more troubling, as are the Circuit Court decisions in *Simmons* and *Kaufman III*, which undermine the IRS's ability to enforce compliance with the protected-in-perpetuity requirements and open the door to the loss of the federal investment in conservation easements and significant abuse.

Some donors and holders will heed *Carpenter*'s advice regarding the extinguishment regulation's serving as a guide by which to create the

232. Carpenter v. Commissioner, 103 T.C.M. (CCH) 1001, at 1004 T.C.M. (RIA) ¶ 2012-001, at 6 (2012).

necessary restrictions and will incorporate (or continue to include) provisions tracking the extinguishment and proceeds regulations in their conservation easement deeds. Others, however, will draft easements with an eye toward complying with only state statutory or voluntarily adopted extinguishment procedures, or will grant the holder the right to consent to changes to or abandon its rights under the easement, in each case with the goal of retaining maximum flexibility to modify, transfer, release, swap, or otherwise extinguish the easements. Accordingly, consistent with the advice of the First Circuit, the IRS and the Treasury Department should issue forward looking regulations and other guidance that will provide taxpayers with fair warning regarding how to satisfy the critically important protected-in-perpetuity requirements.

Some recommendations regarding the development, content, and form of regulatory revisions and other guidance are set forth below. Such revisions and other guidance should be designed to ensure that (1) uniform federal rules govern the transfer, amendment, and extinguishment of tax-deductible conservation easements; (2) there is transparency, in that the easements clearly state the manner in which they can be transferred, amended, and extinguished; (3) the terms of the easements addressing transfer, amendment, and extinguishment are standardized, which will facilitate compliance and review, as well as interpretation and enforcement over the long term; and (4) there is assurance that the terms included in the easements to comply with federal tax law requirements are not qualified by other provisions in the deed or by separate agreement and will be legally binding on both parties to the easement under state law.

A. *IRS Guidance*

The IRS has already issued some guidance pertaining to the protected-in-perpetuity requirement. As earlier noted, in an IRS Information Letter dated March 5, 2012, the IRS confirmed that the contribution of a conservation easement that authorizes swaps other than in in accordance with the extinguishment and proceeds regulations will not be eligible for a federal charitable income tax deduction under section 170(h).[233] In another IRS Letter dated September 18, 2012, the IRS confirmed that, while state law may provide a means for extinguishing a conservation easement for state law purposes, the requirements of section 170(h) and the extinguishment and proceeds regulations must nevertheless be satisfied for a contribution to be deductible for federal income tax purposes.[234] While these letters are helpful, they are unlikely to stop the gamesmanship in the drafting of conservation easements, and some may continue to argue that the extinguishment and

233. *See supra* note 209.
234. IRS Information Letter (Sept. 18, 2012), UIL: 170.14-00.

proceeds regulations should be viewed as optional, and states, localities, and even holders should be free to adopt their own extinguishment procedures.

Accordingly, both to help well-intentioned taxpayers comply with the restriction on transfer, extinguishment, and proceeds regulations and to reduce gamesmanship in the drafting of easements, the IRS should issue more formal guidance confirming that the provisions of the restriction on transfer, extinguishment, and proceeds regulations are not optional and, instead, represent "the necessary restrictions" on the transfer and extinguishment of tax-deductible conservation easements. The guidance should also ideally include explicitly approved safe harbor clauses, which, if they are incorporated into a conservation easement deed, not qualified by other terms of the easement or by separate agreement, and legally binding on the parties under state law, will ensure satisfaction of the restriction on transfer, extinguishment, and proceeds requirements.[235] Such safe harbor clauses and resulting standardization of key provisions of tax-deductible easements would greatly facilitate not only taxpayer compliance but also IRS and court review of easement donation transactions.[236] Standardization would also promote consistency in the interpretation and enforcement of tax-deductible easements over the long term by state attorneys general and the courts across the fifty states.[237]

The guidance should also explain the IRS's expectation that the terms of tax-deductible easements will be legally binding on the parties under state law. In the words of *Carpenter*, the contributions should be restricted gifts or "contributions conditioned on the use of [the] gift[s] in accordance with the donor's precise directions and limitations."[238] The guidance should explain that if the terms of a conservation easement are not

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235. The IRS has issued similar guidance in other contexts. *See, e.g.*, Rev. Proc. 2007-45, 2007-2 C.B. 89 (inter vivos charitable lead annuity trusts); Rev. Proc. 2007-46, 2007-2 C.B. 102 (testamentary charitable lead annuity trusts).

236. It would, of course, be impossible to standardize conservation easement instruments completely, as each easement, like the property it protects, will be unique in certain respects. Moreover, each state has its own rules governing the formalities associated with real estate conveyances. Standardization of the provisions relating to the perpetuity requirements in section 170(h) and the regulations, however, is possible and desirable.

237. *See* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at 68–69 (explaining that the terms of tax-deductible conservation easements currently vary widely from holder to holder and even donation to donation, and this variability has led to a difficult interpretive task for the IRS and state and federal courts).

238. *Carpenter*, 103 T.C.M. (CCH) at 1004 T.C.M. (RIA) ¶ 2012-001, at 6.

binding on the parties under state law, the donation of the easement will not be eligible for a deduction under section 170(h).[239]

Guidance from the IRS regarding the expected status of tax-deductible conservation easements as restricted gifts and the legally binding nature of the terms of such gifts under state law would have the added benefit of greatly assisting state attorneys general and state judges, who (as earlier explained) are on the front lines enforcing such gifts on behalf of the public.[240] Such guidance would also put other relevant parties, including state legislatures, on notice of what is required if they want property owners in the state to be able to benefit from federal tax incentives for the donation of conservation easements. That is, the restriction on transfer, extinguishment, division of proceeds, and other terms included in easement instruments to satisfy federal tax law requirements must be complied with *in addition* to any conditions or limitations that may be imposed on the modification, transfer, release, or other extinguishment of conservation easements under the applicable state law.

B. Rules for Amendments

In providing forward looking rules addressing the protected-in-perpetuity requirement in section 170(h)(5)(A), the IRS and the Treasury Department will need to address the issue of conservation easement amendments. Because tax-deductible conservation easements are intended to endure in perpetuity, or for as long as continuing to protect the property for conservation purposes remains possible or practicable, one can reasonably assume that some of these instruments will need to be amended from time to time to respond to changing conditions. The requirements in section 170(h) that a conservation easement be granted in perpetuity and its conservation purpose be protected in perpetuity would appear to establish the basic parameters for a permissible grant of amendment discretion to the holder and property owner. The conservation purpose of an easement would not be protected in perpetuity if the parties have the discretion to amend the easement in ways that adversely impact or change such purpose. On the other

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239. *See, e.g.*, *supra* note 83 and accompanying text (explaining that a state enabling statute might preclude enforcement of terms included in a conservation easement deed to satisfy federal tax law requirements); *see supra* note 86 and accompanying text (explaining that some holders insist that donors state in the conservation easement that the conveyance is an unrestricted gift in an attempt to render the provisions of the deed not legally binding on the holder).

240. *See, e.g.*, *supra* note 57 and accompanying text. Not surprisingly, the cases to date involving challenges to improper modifications and terminations of conservation easements have taken place in state courts and have not involved the IRS. *See* McLaughlin, *National Perpetuity Standards*, *Part 2*, *supra* note 5, at pt. III.B.

hand, the conservation purpose of an easement would not be jeopardized if the parties have the discretion to agree to only those amendments that further, or are at least consistent with, such purpose. The limited "amendment clauses" typically included in conservation easement deeds reflect this approach; they authorize the holder and property owner to agree to amendments, but only if the amendments are, among other things, consistent with the purpose of the easement.[241]

However, determining when an amendment furthers or is consistent with the conservation purpose of an easement, or adversely impacts or changes that purpose, can be difficult.[242] The potential for private benefit and private inurement and loss of the federal investment is particularly high in the context of amendments.[243] Some holders use creative labeling to disguise the true nature of the changes they agree to make with regard to tax-deductible conservation easements.[244] And *Simmons* and *Kaufman III*

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241. *See supra* note 218 and accompanying text.

242. *See, e.g.*, 1 STAFF OF S. COMM. ON FINANCE, 109TH CONG., 1ST SESS., REPORT OF STAFF INVESTIGATION OF THE NATURE CONSERVANCY, Exec. Summary, at, 9 (Comm. Print 2005), http://finance.senate.gov/ [hereinafter SFC Report] ("Modifications to an easement held by a conservation organization may diminish or negate the intended conservation benefits, and violate the present law requirements that a conservation restriction remain in perpetuity."); *id*. pt II, at 5 (expressing concern about "trade-off" amendments, which both negatively impact and further the conservation purpose of an easement but on balance are arguably either neutral with respect to or enhance such purpose, because of the difficulty associated with weighing increases and decreases in conservation benefits as well as private benefit concerns). *See also* McLaughlin, *National Perpetuity Standards, Part 2*, *supra* note 5, at pt. III.B. (discussing cases involving holders' improper amendment of conservation easements).

243. *See, e.g.*, SFC Report, *supra* note 242, pt. II, at 5 ("the private benefit prohibition aspect of the [amendment] procedure can be a subjective inquiry, with no bright lines available to make the determination"). The amendment of a conservation easement may increase the fair market value of the encumbered property and thereby confer an impermissible private benefit on the property owner. For example, some organizations reportedly have been amending older conservation easements to update the language and otherwise "modernize" the easements. In some cases, conservation easements that prohibited all commercial uses (and for which tax benefits were granted based, in part, on that prohibition) have been amended to permit commercial uses that are consistent with the purpose of the easement. In such cases, the amendments may have significantly increased the fair market value of the subject properties and, absent compensation to the holder on behalf of the public, conferred an impermissible private benefit on the property owners.

244. *See, e.g.*, McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 520–23 (describing *Bjork*, 886 N.E.2d 563, *appeal denied*, 897 N.E.2d 249, in which a land trust characterized the partial extinguishment of a conservation easement in exchange for the protection of other land — a partial swap — as an "amendment"); LAND TRUST ACCREDITATION COMMISSION, ACCREDITATION

mistakenly suggest that holders can be granted unlimited rights to consent to changes, at least in the façade easement context. Accordingly, rules must be developed to govern amendments and ensure that the federal interest and investment in tax-deductible conservation easements and the conservation values they are intended to preserve in perpetuity are appropriately protected. Just what those rules should be is beyond the scope of this article, but for the same fourfold policy reasons discussed in Part II with regard to extinguishment — consistent protection of the federal investment, efficiency, equity, and effectiveness — the amendment of tax-deductible conservation easements should be subject to overarching uniform federal rules that apply in addition to any conditions or limitations that may be imposed on amendments by the applicable state enabling statute or voluntarily adopted by holders.

Because the issue of amendments is complex, Congress should consider requesting that the Treasury Department, the IRS, or one of the tax-writing committees study the issue with the goal of recommending uniform federal rules.[245] The request could, for example, be made in conjunction with extending the enhanced tax incentives available with regard to conservation easement donations. A good starting point for such a study would be the information the IRS has gathered thus far from the annual Form 990 filings of nonprofit organizations. Since 2006, nonprofit organizations holding conservation easements have been required to report the number of conservation easements they modified, transferred, released, or extinguished, in whole or in part, during the tax year and to explain the changes.[246] Other sources of information include the Senate Finance Committee's report

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REQUIREMENTS MANUAL: A LAND TRUST'S GUIDE TO UNDERSTANDING KEY ELEMENTS OF ACCREDITATION, 69 (May 2012), http://www.landtrustaccreditation.org/storage/downloads/RequirementsManual.pdf (explaining that some organizations have been characterizing partial and full swaps, which involve the extinguishment in whole or in part of the original easement, as "amendments"). Recent revisions to the Instructions for Schedule D to the Form 990 are intended to prevent holders from disguising the true nature of changes made to tax-deductible conservation easements; *see* I.R.S. 2011 Instructions for Schedule D (Form 990) 2, http://www.irs.gov/pub/irs-pdf/i990sd.pdf ("An easement is . . . *released, extinguished*, or *terminated* when all or part of the property subject to the easement is removed from the protection of the easement in exchange for the protection of some other property or cash to be used to protect some other property" and "calling an action a 'swap' or a 'boundary line adjustment' does not mean the action is not also a modification, transfer, or extinguishment").

245. Among the tax-writing committees, the Senate Finance Committee or Joint Committee on Taxation would appear to be best suited to the task given their previous consideration of section 170(h). *See supra* notes 4 and 242.

246. *See* I.R.S. 2011 Instructions for Schedule D (Form 990), *supra* note 244, at 2.

following its investigation of The Nature Conservancy, which examined amendments the Conservancy agreed to as well as the organization's amendment policies;[247] the Land Trust Alliance's 2007 research report on amendments;[248] and a former administration's proposal to impose significant penalties on any charity that removes, fails to enforce, or inappropriately modifies a conservation easement, or transfers such an easement without ensuring that the conservation purposes will be protected in perpetuity.[249]

The Treasury Department or the IRS should develop a standardized amendment clause to be included in tax-deductible conservation easement deeds that grants the holder and property owner limited discretion to agree to amendments that are consistent with the purpose of the easement. Detailed guidance regarding the type of amendments that fall within and outside of that grant of discretion and the required components of the amendment process (e.g., when an appraisal is necessary to assess private benefit) should be provided. And a system of federal oversight or federal requirements should be developed for more complex amendments (including those that are not consistent with the purpose of an easement), as they are the most vulnerable to abuse.

More specific instructions regarding the manner in which modifications, transfers, releases, and extinguishments are reported on Schedule D of the Form 990 should also be provided to assist those filing and reviewing the forms and to minimize confusion and obfuscation.[250] At present, the manner in which these activities are reported (if at all) on the Form 990 varies dramatically from organization to organization.[251] The more transparent the reporting process, the more it will discourage inappropriate amendments and terminations and assist federal and state regulators in detecting and preventing abuses.

Finally, consideration should be given to requiring state and local government entities accepting tax-deductible conservation easements to similarly report annually on their modification, transfer, release, and extinguishment activities as a condition of retaining "eligible donee" status. Many state and local government entities acquire and hold tax-deductible

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247. *See* SFC REPORT, *supra* note 242.

248. *See* Land Trust Alliance, *Amending Conservation Easements*, *supra* note 200.

249. *See* STAFF OF JOINT COMM. TAXATION, 109TH CONG., 1ST SESS., DESCRIPTION OF REVENUE PROVISIONS CONTAINED IN THE PRESIDENT'S FISCAL YEAR 2006 BUDGET PROPOSAL, 239–41 (Comm. Print 2005), https://www.jct.gov/publications.html?func=startdown&id=1523.

250. In addition to appropriately categorizing the changes made, holders should be required, for example, to explain how amendments complied with the federal requirements developed as a result of the suggested study, and how any extinguishment complied with the extinguishment and proceeds regulations.

251. The Form 990s are available at http://www.guidestar.org.

conservation easements, but such entities are not required to file Form 990s. Requiring reporting from such entities would similarly discourage inappropriate amendments and terminations and assist regulators in detecting and preventing abuses.

C. Revisions to Regulations

The Treasury should consider revising the regulations to, *inter alia,* clarify the various protected-in-perpetuity requirements and the manner in which taxpayers must comply with those requirements if they expect to benefit from "six-figure deductions."[252] For example:

1. The regulations could be revised to provide that a deduction shall be allowed for the donation of a conservation easement only if the instrument of conveyance states that the grantor conveyed the easement in whole or in part as a charitable gift for a specific purpose, the grantor intends to claim federal tax benefits as a result of the gift, and the grantor intends that the grantor and grantee (and their successors and assigns) will be legally bound by the terms of the easement.

2. Regulation section 1.170A-14(g)(6) could be revised to provide that a deduction shall be allowed for the donation of a conservation easement only if the instrument of conveyance prohibits the grantee (and its successors and assigns) from extinguishing the easement (whether through sale, release, abandonment, swap, or otherwise) except as expressly provided in that regulation.[253]

3. Regulation section 1.170A-14(c)(1) could be revised to provide that a qualified organization will not be treated as having "a commitment to protect the conservation purposes of the donation" and, thus, will lose its "eligible donee" status if it agrees to modify, amend, sell, swap, release, extinguish, or otherwise transfer tax-deductible conservation easements in contravention of the restriction on transfer, extinguishment, and proceeds requirements and the rules developed to govern amendments.

4. Regulation section 1.170A-14(g)(3) (the so-remote-as-to-be-negligible regulation) could be revised to clarify that it cannot be invoked to

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252. The First Circuit noted in *Kaufman III* that "[s]ection 170(h) does not allow taxpayers to obtain six-figure deductions for gifts of lesser or no value." *Kaufman III*, 687 F.3d 21, 30 (1st Cir. 2012). Equally true is that section 170(h) should not allow taxpayers to obtain six-figure deductions for gifts of conservation easements where the conservation purposes of the easements are not protected in perpetuity.

253. *See also* McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 511–12, suggesting that the proceeds regulation be revised to eliminate perverse incentives to extinguish conservation easements.

forgive a failure to comply with the specific requirements in section 170(h) and the regulations.

5. The practicalities of obtaining mortgage subordinations could be studied and, depending on the result of the study, the mortgage subordination regulation could be either clarified or modified to appropriately protect the public investment in the event of extinguishment of an easement encumbering property subject to a mortgage.[254]

6. Safe harbor clauses, examples, and illustrations could be provided to further clarify and facilitate compliance with the rules.

D. Recommendations of Others

Another possible response to the current conundrum the IRS faces in policing conservation easement donation transactions is to simply repeal section 170(h) and replace it with either a direct spending program or a limited budget tax credit program, in each case administered by an expert federal agency. The goal would be to maximize the public benefit obtained from the federal expenditure on conservation easements while minimizing the potential for abuse. Harvard Law Professor Daniel Halperin recently proposed these reforms.[255] Professor Halperin formerly served as the Treasury Department's Deputy Assistant Secretary for Tax Policy and testified on behalf of that department regarding the deduction for conservation easement donations during the congressional hearings preceding the enactment of section 170(h).[256]

Professor Halperin argues that the deduction under section 170(h) is wasteful, inefficient, and subject to abuse.[257] He cites as primary concerns the potential that easements will not be enforced over the long term, the inadequacy of public benefit, overvaluation, and the lack of budget control.[258] He also notes that abuses are likely given that the donor "retains the benefit of the land subject to the easement and may use it in [ways] that endanger[] the conservation value[s]."[259]

While Professor Halperin provides numerous reasons to consider repeal, and the IRS's difficulties in policing conservation easement donation

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254. *See supra* pt. III.A.

255. *See* Daniel Halperin, *A Better Way to Encourage Gifts of Conservation Easements*, 136 TAX NOTES 307 (2012) [hereinafter Halperin, *A Better Way*].

256. *See, e.g.*, *Miscellaneous Tax Bills: Hearing*, *supra* note 202, at 3–4 (statement of Hon. Daniel I. Halperin, Deputy Assistant Secretary for Tax Policy, Department of the Treasury).

257. Halperin, *A Better Way*, *supra* note 255, at 307.

258. *Id.* at 308–11.

259. *Id.* at 307.

transactions add further fuel to the fire,[260] there is a long history of support for section 170(h) in Congress. Perhaps in recognition of this, Professor Halperin also recommends that certain changes be made if the deduction is continued. Relevant to this Article and the perpetuity requirements, he explains that "[a]ccurate valuation of the easement at the time of contribution is insufficient if there is inadequate protection of the perpetual easement because of failure to monitor, ignoring violations, amendment of the easement conditions, or otherwise."[261] Accordingly, he recommends that eligible donees of tax-deductible easements be limited to organizations that meet rigorous uniform standards, that an excise tax be imposed on officers and directors for non-enforcement, and that a federal agency other than the IRS be involved in enforcement.[262]

V. CONCLUSION

The enormous up-front investment in tax-deductible conservation easements will be for naught if the purportedly perpetual protections prove to be ephemeral because government and nonprofit holders are able to release, sell, swap, or otherwise extinguish the easements in disregard of the restriction on transfer, extinguishment, proceeds, and other perpetuity-related requirements. It is not enough that conservation easement donors accurately value the easements, properly substantiate their donations, and satisfy the conservation purposes tests under section 170(h); they must also comply with the critically important protected-in-perpetuity requirements.

Carpenter was an important victory for the IRS and, by extension, the public, because it provides some key guidance regarding compliance with the protected-in-perpetuity requirements. However, *Carpenter* has also engendered some confusion and speculation, and the Circuit Court decisions

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260. *See* Appendix A, *infra* (illustrating that the IRS has spent considerable time, money, and staff resources on litigation in this context since 2005, but has lost five of the six cases appealed from the Tax Court to the Circuit Courts during this time: *Glass, Whitehouse, Simmons, Scheidelman*, and *Kaufman III*).

261. Halperin, *A Better Way*, *supra* note 255, at 313.

262. *Id.* at 307, 313. Professor Halperin recommends that "eligible donees" be limited to "large institutions with a large portfolio of easements and resources and motives to enforce the easement[s]." *Id.* at 307. However, status as an eligible donee should not depend on the size of the entity or the number of easements it holds. Some large institutions with large easement portfolios may be engaged in abusive transactions or operate in disregard of federal tax law requirements and the laws governing the administration of charitable gifts, while some smaller organizations with modest easement portfolios may operate in compliance with the law and perform extraordinary services to the public in their limited geographic area. Thus, more refined measure of assessing "eligible donee" status should be developed.

in *Simmons* and *Kaufman III* have compounded the problem by undermining the IRS's efforts to enforce the protected-in-perpetuity requirements.

Clear federal rules regarding the transfer, amendment, and extinguishment of conservation easements that are consistent with congressional intent are needed, whether in the form of revisions to the regulations, formal or informal guidance from the IRS, or additions to § 170(h). Without such rules, the purportedly perpetual protections provided by tax-deductible easements will erode over time and the enormous public investment in these instruments and the conservation values they are intended to protect for the benefit of future generations will be lost.

APPENDIX A

The Table below lists the cases to date involving challenges to charitable deductions claimed with respect to conservation easement donations.

The cases are listed in the order in which they were issued. However, the date of the donation (or purported donation) is noted in the right-hand column because the law governing the deductibility of conservation easement donations has changed over time and the date of donation may be an important factor in analyzing the relevance of an older case to a current controversy.[263]

In particular, section 170(h) was enacted in 1980 and is effective for transfers made after December 17, 1980. Among other things, section 170(h) revised the conservation purposes for which tax-deductible easements may be granted and added the protected-in-perpetuity requirement of section 170(h)(5)(A).[264]

Regulations interpreting section 170(h) were published Jan. 14, 1986, and are effective with respect to contributions made on or after December 18, 1980, with several exceptions.[265]

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263. For the history of section 170(h), see McLaughlin, *National Perpetuity Standards, Part 1*, *supra* note 16, at 476–86.

264. Thus, for example, Stotler v. Commissioner, 53 T.C.M. (CCH) 973, T.C.M. (P-H) ¶ 87,275, which involved a conservation easement donation made in 1979, should carry no persuasive weight in interpreting the protected-in-perpetuity requirement of section 170(h)(5)(A) or the regulations interpreting that section as that requirement and those regulations were not in effect at the time of the 1979 donation. The D.C. Circuit made this mistake in *Simmons*. *See supra* note 36.

265. *See* Reg. § 1.170A-14(j). The mortgage subordination, division of proceeds, baseline documentation, and donee notification, access, and enforcement rights requirements apply only to donations made after February 13, 1986. *See id*. §§ 1.170A-14(g)(2), -14(g)(6)(ii), -14(g)(5)(i), -14(g)(5)(ii). The provision requiring a reduction in amount of the donor's deduction for any increase in the value of certain property owned by the donor or a related person as a result of the donation (typically referred to as "enhancement") applies only to donations made after January 14, 1986. *See id.* § 1.170A-14(h)(3)(i).

Cases **Listed in Order of Date of Opinion**	**Date of Donation**
1977	
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1985	
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1986	
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1987	
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1988	
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1989	
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1990	
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Griffin v. Commissioner, T.C. Memo. 1989-130.	1981
1991	
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1992	
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Dennis v. United States, 70 A.F.T.R.2d 92-5946 (E. D. Va. 1992).	1980
1993	
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McLennan v. United States, 994 F.2d 839 (Fed. Cir. 1993), *aff'g*, 24 Cl. Ct. 102 (1991).	1980
1994	
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1995	
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1997	
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2000	
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2009	
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Kiva Dunes v. Commissioner, T.C. Memo. 2009-145.	2002
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2010	
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2011	
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1982 East L.L.C. v. Commissioner, T.C. Memo. 2011-84.	2004
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2012	
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