UNITED STATES TAX COURT
WASHINGTON, DC 20217

OAKHILL WOODS, LLC, EFFINGHAM MANAGERS, LLC, TAX MATTERS PARTNER,	)	
Petitioner(s),	)	**CT**
v.	)	Docket No. 26557-17.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent	)	

O R D E R

This case involves a charitable contribution deduction claimed by Oakhill Woods, LLC (Oakhill), for the donation of a conservation easement. In Oakhill Woods, LLC v. Commissioner, T.C. Memo. 2020-24, we addressed cross-motions for partial summary judgment on the question whether Oakhill had satisfied for this donation the substantiation requirements of section 1.170A-13(c), Income Tax Regs.[1] The Internal Revenue Service (IRS or respondent) contended that the deduction must be denied in its entirety because Oakhill failed to attach to its 2010 Form 1065, U.S. Return of Partnership Income, a fully completed "appraisal summary" on Form 8283, Noncash Charitable Contributions. In particular, Oakhill did not disclose on that form, as was required, the "cost or adjusted basis" of the property that was the subject of the contribution. Petitioner contended that Oakhill strictly or substantially complied with that requirement or, alternatively, that the regulation was invalid. We resolved both questions in respondent's favor. See Oakhill Woods, LLC, T.C. Memo. 2020-24, at *12-*22, *22-*27.

In his motion respondent had urged an alternative ground for disallowing the charitable contribution deduction--namely, that a defect in the deed's "judicial extinguishment" provision prevented the easement from satisfying the requirement,

[1]Unless otherwise indicated, all statutory references are to the Internal Revenue Code in effect for the year at issue, and all Rule references are to the Tax Court Rules of Practice and Procedure.

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set forth in section 170(h)(5)(A), that the conservation purpose be "protected in perpetuity." In its cross-motion petitioner contended that the regulation governing this issue, sec. 1.170A-14(g)(6), Income Tax Regs., was invalid. Because challenges to the validity of that regulation were then pending in other cases, we deferred ruling on respondent's alternative theory. See Oakhill Woods, LLC, T.C. Memo. 2020-24, at *9-*10 n.4. We recently sustained the validity of that regulation, see Oakbrook Land Holdings, LLC v. Commissioner, 154 T.C. __ (May 12, 2020), and we conclude that a ruling on respondent's alternative theory is now appropriate.

The Code generally restricts a taxpayer's charitable contribution deduction for the donation of "an interest in property which consists of less than the taxpayer's entire interest in such property." Sec. 170(f)(3)(A). But there is an exception for a "qualified conservation contribution." Sec. 170(f)(3)(B)(iii), (h)(1). For the donation of an easement to be a "qualified conservation contribution," the conservation purpose must be "protected in perpetuity." Sec. 170(h)(5)(A).

The regulations set forth detailed rules for determining whether this "protected in perpetuity" requirement is met. Of importance here are the rules governing the mandatory division of proceeds in the event the property is sold following a judicial extinguishment of the easement. See sec. 1.170A-14(g)(6), Income Tax Regs. The regulations recognize that "a subsequent unexpected change in the conditions surrounding the [donated] property * * * can make impossible or impractical the continued use of the property for conservation purposes." Id. subdiv. (i). Despite that possibility, "the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding" and the easement deed ensures that the charitable donee, following sale of the property, will receive a proportionate share of the proceeds and use those proceeds consistently with the conservation purposes underlying the original gift. Ibid. In effect, the "perpetuity" requirement is deemed satisfied because the sale proceeds replace the easement as an asset deployed by the donee "exclusively for conservation purposes." Sec. 170(h)(5)(A).

The judicial extinguishment provisions of the deed in this case are substantially similar to those that we considered in Coal Prop. Holdings, LLC v. Commissioner, 153 T.C. 126, 130-131 (2019). Following our reasoning in that case, we conclude that Oakhill's deed fails to satisfy the "protected in perpetuity" requirement for two reasons.

First, the regulatory fraction used in the deed to determine the grantee's proportionate share of post-extinguishment proceeds is applied, not to the full sale proceeds--an amount presumably equivalent to the FMV of the property at the time of sale--but to the proceeds "minus any increase in value after the date of this Conservation Easement attributable to improvements." Thus, the grantee's share is improperly reduced on account of (1) appreciation in the value of improvements existing when the easement was granted plus (2) the FMV of any improvements that the donor or its successors subsequently make to the property. By reducing the grantee's share in this way, the deed violates the regulatory requirement that the donee receive, in the event the property is sold following extinguishment of the easement, a share of proceeds 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." See sec. 1.170A-14(g)(6)(ii), Income Tax Regs.[2]

As we have noted previously, the requirements of this regulation "are strictly construed." Carroll v. Commissioner, 146 T.C. 196, 212 (2016). Because the grantee in this case "is not absolutely entitled to a proportionate share of * * * [the] proceeds" upon a post-extinguishment sale of the property, the conservation purpose underlying the contribution is not "protected in perpetuity." Coal Prop. Holdings, 153 T.C. at 127, 139 (quoting Carroll, 146 T.C. at 212); accord, Plateau Holdings, LLC v. Commissioner, T.C. Memo. 2020-93; Oakbrook Land Holdings, LLC v. Commissioner, T.C. Memo. 2020-54. The U.S. Court of Appeals for the Fifth Circuit has likewise sustained the disallowance of a charitable contribution deduction where the judicial extinguishment provision of an easement deed included a carve-out for donor improvements similar to that here. See PBBM-Rose Hill, 900 F.3d at 208.

The easement deed here has a second problem, which was also present in Coal Prop. Holdings. The grantee's tentative share of the proceeds, as determined

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[2]The pre-contribution improvements to the conserved area in this case appear to have less substantial than in Coal Prop. Holdings. Cf. 153 T.C. at 131. But the deed reserved to Oakhill the right to construct "a limited number of improvements and buildings" within the conserved area, including roads, driveways, irrigation systems, ponds, and electric utility transmission lines to serve the conserved area or residential parcels adjacent to it. These factual differences have little impact on our analysis because the regulation does not permit any reduction of the donee's share on account of such donor improvements.

under paragraph 19 of the deed, is adjusted further by paragraph 17. It provides that the grantee's share will be determined under the Proceeds paragraph, but only "after the satisfaction of any and all prior claims." Prior claims against the sale proceeds might be held by various creditors of Oakhill or its successors.

It is not necessarily unreasonable for a deed to provide that prior claims may be paid from sale proceeds. What is unreasonable is the requirement that all prior claims be paid out of the grantee's share of the proceeds, even if those claims represent liabilities of Oakhill or its successors. See Coal Prop. Holdings, 153 T.C. at 145 n.5. Because the grantee's share of the proceeds is improperly reduced by carve-outs both for donor improvements and for claims against the donor, the deed's judicial extinguishment provisions do not satisfy the regulatory requirements.

If the regulation is interpreted, as we have interpreted it, to make Oakhill ineligible for a charitable contribution deduction, Oakhill contends that the regulation is invalid. It urges that section 1.170A-14(g)(6), Income Tax Regs., is an "arbitrary and capricious" rule promulgated in violation of the Administrative Procedure Act. And it contends that the regulation is substantively invalid under the test set forth in Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837 (1984). We comprehensively addressed and rejected both of these arguments in a recent Court-reviewed Opinion. See Oakbrook Land Holdings, 154 T.C. at __ (slip op. at 15-33). We need not repeat that analysis here.

Finally, petitioner draws our attention to Priv. Ltr. Rul. 200836014 (Sept. 5, 2008) (PLR), in which the IRS found unobjectionable an easement deed with a judicial extinguishment clause resembling that here. Petitioner contends that respondent's interpretation of the regulation as set forth in that PLR is binding on respondent under Auer v. Robbins, 519 U.S. 452, 461 (1997). Petitioner's argument ignores the fact that determinations embodied in a PLR "may not be used or cited as precedent." Sec. 6110(k)(3). The taxpayer in PBBM-Rose Hill brought the same PLR to the Court of Appeals' attention, but that court paid no heed to it, finding the regulation unambiguous on its face. See PBBM-Rose Hill, Ltd. v. Commissioner, 900 F.3d 195, 207-208 (5th Cir. 2018). We have done the same. See Coal Prop. Holdings, 153 T.C. at 144. In Oakbrook Land Holdings, LLC v. Commissioner, T.C. Memo. 2020-54, we dismissed reliance on Auer deference because "the 'traditional tools of construction' le[d] us to hold that the Commissioner's construction of the regulation is correct even if we look at the question de novo." Id. at *25 (quoting Kisor v. Wilkie, 588 U.S. __, __, 139 S. Ct. 2400, 2415 (2019))

In sum, we hold that the conservation purpose underlying the easement was not "protected in perpetuity" as required by section 170(h)(5)(A). For that reason the charitable contribution deduction claimed by Oakhill must be denied in its entirety. Coal Prop. Holdings, LLC, 153 T.C. at 139. We will therefore grant respondent's motion for partial summary judgment on this alternative ground as well as on the ground enunciated in our earlier opinion.

In consideration of the foregoing, it is

ORDERED that respondent's Motion for Partial Summary Judgment, filed May 18, 2018, is granted on the alternative ground set forth in this Order. It is further

ORDERED that, on or before August 10, 2020, the parties shall file a joint status report expressing their views as to the conduct of further proceedings in this case.

(Signed) Albert G. Lauber
Judge

Dated: Washington, D.C.
July 14, 2020