Conservation Easements, Recent Mayo Clinic Case, and Expanded Defenses to IRS Attacks on “Conservation Purpose”

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This article examines the main issues in conservation easement disputes, the arguments typically raised by the IRS, various Tax Court cases focused on conservation purpose, and a new, non-easement case that might fortify taxpayer defenses.

The IRS is fixated on challenging partnerships that donate conservation easements, claim the corresponding tax deductions, and pass them along to their partners. One of the many tools utilized by the IRS is conducting widespread audits and claiming that the partnerships are entitled to deductions of $0 because, among other things, their easements lack a ‘significant’ conservation purpose. This position is interesting because it is based solely on the regulations, promulgated by the IRS, not by the related law, enacted by Congress. In other words, the IRS is essentially creating its own, expansive rules and then applying them.

This article examines the main issues in conservation easement disputes, the arguments typically raised by the IRS, various Tax Court cases focused on conservation purpose, and a new, non-easement case that might fortify taxpayer defenses.

Overview of Main Issues in Conservation Easement Disputes
One must first understand the main concepts and terminology in the conservation easement arena in order to appreciate this article. These are examined below.

What Is a Qualified Conservation Contribution?
Taxpayers generally may deduct the value of a charitable donation that they
make during a year. However, taxpayers are not entitled to deduct a donation of property, if it consists of less than their entire interest in such property. One important exception is that taxpayers can deduct a donation of a partial interest in property (instead of an entire interest), provided that it constitutes a “qualified conservation contribution.” To meet this critical definition, taxpayers must show that they are (i) donating a qualified real property interest (“QRPI”), (ii) to a qualified organization, (iii) exclusively for conservation purposes.

What Is a QRPI?
A QRPI can be one of several things, including a restriction, granted in perpetuity, on the use of a particular piece of real property. These are known by many names, among them “conservation easement,” “conservation restriction,” and “perpetual conservation restriction.” Regardless of what you call them, QRPIs must be based on legally enforceable restrictions (such as those memorialized in a Deed of Conservation Easement filed in the appropriate public record) that will prevent uses of the property, forever, which are inconsistent with the conservation purposes of the donation. Stated differently, a donation is not treated as “exclusively for conservation purposes,” unless the conservation purposes are “protected in perpetuity.”

What if Different Future Uses Might Occur?
The IRS will not disallow a tax deduction merely because the interest granted to the charitable organization might be defeated in the future as a result of some act or event, provided that on the date that the easement is granted, it appears that the possibility that such act or event will take place is “so remote as to be negligible.” For instance, the fact that state law requires use restrictions, like conversation easements, to be recorded every 30 years to remain in force does not, alone, make easements non-perpetual. Another example is where a taxpayer donates land to a city government for as long as such land is used as a park. If, as of the date of the donation, the city plans to use the land for a park, and the possibility that it could be used for another purpose is negligible, then the donation is considered perpetual, and the taxpayer is entitled to a deduction.

For What Purposes Can Land Be Conserved?
A contribution has an acceptable “conservation purpose” if it meets one or more of the following requirements:

- (i) It preserves land for outdoor recreation by, or the education of, the general public;
- (ii) It protects a relatively natural habitat of fish, wildlife, or plants, or a similar ecosystem;
- (iii) It preserves open space (including farmland and forest land) for the scenic enjoyment of the general public, and will yield a significant public benefit;
- (iv) It preserves open space (including farmland and forest land) pursuant to a federal, state, or local governmental conservation policy, and will yield a significant public benefit; or
- (v) It preserves a historically important land area or a certified historic structure.

The conservation categories most relevant to this article are explained below.

Relatively natural habitat of fish, wildlife, plants, or similar ecosystem. When analyzing natural habitats, the fact that they have been altered to some extent by human activity will not result in the disallowance of the tax deduction, if the fish, wildlife, and/or plants continue to exist there in a “relatively natural state.” Preservation of a lake formed by a manmade dam or a salt pond formed by a manmade dike would still have an acceptable conservation purpose, provided that such lake or pond were a nature feeding area for a wildlife community that entailed “rare, endangered, or threatened native species.”

According to the regulations, “significant” habitats and ecosystems include, but are not limited to: (i) habitats for rare, endangered, or threatened species of animal, fish, or plants, (ii) natural areas that represent high quality examples of a terrestrial or aquatic community, such as islands that are undeveloped or not intensely developed where the coastal ecosystem is relatively intact, and (iii) natural areas which are included in, or which contribute to, the ecological viability of a local, state, or national park, nature preserve, wildlife refuge, wilderness area, or other similar conservation area.

The fact that public access to the preserved property is limited does not trigger a disallowance of the charitable deduction related to the easement. Indeed, taking it a step further, the regulations state that “a restriction on all public access” to the habitat of a threatened native species would not cause an easement donation to be non-deductible.

Open space for scenic enjoyment, plus significant public benefit. The donation of a QRPI to preserve open space (including farmland and forest land) will meet the conservation purposes test, if such preser-
viation is for the scenic enjoyment of the
general public and will yield a significant
public benefit.\textsuperscript{18} Generally speaking,
preservation belongs here if development
of the property would either (i) impair the
"scenic character" of the local rural or ur-
ban landscape, or (ii) interfere with a
"scenic panorama" that can be enjoyed
from a park, nature preserve, road, body
of water, trail, or historic structure or land,
and such area or transportation way is
open to, or utilized by, the public.\textsuperscript{19}

The regulations indicate that this no-
tion of "scenic enjoyment" will be based
on all the facts and circumstances rel-
vant to a particular easement dona-
tion.\textsuperscript{20} They also recognize that regional
variations (in terms of topography, ge-
ology, biology, and cultural and eco-
nomic conditions) call for flexibility in
analyzing "scenic enjoyment."\textsuperscript{21} The fol-
lowing factors, among others, might be
considered: (i) The compatibility of the
land use with other land in the vicinity;
(ii) The degree of contrast and variety
provided by the visual scene; (iii) The
openness of the land; (iv) Relief from
urban closeness; (v) The harmonious
variety of shapes and textures; (vi) The
degree to which the land use maintains
the scale and character of the urban
landscape to preserve open space, visual
enjoyment, and sunlight for the sur-
rounding area; (vii) The consistency of
the proposed scenic view with a me-
thodical state scenic identification pro-
gram, such as a state landscape inventory;
and (viii) The consistency of the pro-
posed scenic view with a regional or
local landscape inventory made pursuant
to a sufficiently rigorous review process,
especially if the donation is endorsed
by an appropriate state or local govern-
mental agency.\textsuperscript{22}

To satisfy this conservation purpose,
it suffices that there is visual (instead of
physical) access to the property or across
the property by the general public.\textsuperscript{23}
Moreover, the regulations indicate that
"the entire property need not be visible
to the public . . . although the public
benefit from the donation may be in-
sufficient to qualify for a deduction if
only a small portion of the property is
visible to the public."\textsuperscript{24}

A tax deduction for preservation of
open space for scenic enjoyment of the
general public will be disallowed if the
 easement permits a "degree of intrusion
or future development that would in-
terfere with the essential scenic quality
of the land . . . ."\textsuperscript{25}

All contributions made to preserve
open space must yield a "public benefit,
and such benefit must be "significant."\textsuperscript{26}
One must examine all the relevant facts
and circumstances to determine whether
safeguarding open space will trigger a
"public benefit."\textsuperscript{27} The IRS considers
the following 11 items in making a deter-
mination:

(i) the uniqueness of the property to
the area; (ii) the intensity of land
development in the vicinity of the
property (both existing development
and foreseeable trends of develop-
ment); (iii) the consistency of the pro-
posed open space use with public
programs (whether federal, state or
local) for conservation in the region,
including programs for outdoor
recreation, irrigation or water supply
protection, water quality mainte-
nance or enhancement, flood preven-
tion and control, erosion control,
shoreline protection, and protection
of land areas included in, or related
to, a government approved master
plan or land management area; (iv)
the consistency of the proposed open
space use with existing private con-
servation programs in the area, as evi-
denced by other land, protected by
easement or fee ownership, in close
proximity, (v) the likelihood that
development of the property would
lead or contribute to degradation of
the scenic, natural, or historic char-
acter of the area; (vi) the opportunity
for the general public to use the prop-
erty or to appreciate its scenic values,
(vii) the importance of the property
in preserving a local or regional land-
scape or resource that attracts
tourism or commerce to the area,
(viii) the likelihood that the donee
will acquire equally desirable and
valuable substitute property or prop-
erty rights, (ix) the cost to the donee
of enforcing the terms of the conserv-
ation restriction, (x) the population
density in the area of the property,
and (xi) the consistency of the pro-
posed open space use with a legisla-
tively mandated program identifying
particular parcels of land for future
protection.\textsuperscript{28}

The preservation of an ordinary tract
of land would not, alone, yield a "sig-
nificant public benefit."\textsuperscript{29} However,
preservation, in conjunction with other
factors, or preservation of a unique land
area for public use, would create a sig-
nificant public benefit.\textsuperscript{30}

The regulations explain that, because
the degrees of "scenic enjoyment" offered
by a variety of open space easements are
subjective, and are not as easily deline-
ated as are increasingly specific levels
of governmental policy, the "significant
public benefit" of preserving a "scenic
view" must be independently established
in all cases.\textsuperscript{31}

Open space pursuant to a government
conservation policy, plus significant public
benefit. Donating a QRPI to preserve

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\bibitem{18} Reg. 1.170A-14(d)(4)(iv)(B) (emphasis added).
\bibitem{19} Id.
\bibitem{20} Id.
\bibitem{21} Id.
\bibitem{22} Id.
\bibitem{23} Reg. 1.170A-14(d)(4)(ii)(B).
\bibitem{24} Id.
\bibitem{25} Reg. 1.170A-14(d)(4)(v).
\bibitem{26} Reg. 1.170A-14(d)(4)(vi)(A).
\bibitem{27} Id.
\bibitem{28} Id.
\bibitem{29} Reg. 1.170A-14(d)(4)(ii)(B).
\bibitem{30} Id.
\bibitem{31} Id.
\bibitem{32} Reg. 1.170A-14(d)(4)(i).
\bibitem{33} Reg. 1.170A-14(d)(4)(iii)(A).
\bibitem{34} Id.
\bibitem{35} Id.
\bibitem{36} Id.
\bibitem{37} Id.
\bibitem{38} Reg. 1.170A-14(d)(4)(iii)(B).
\bibitem{39} Id.
\bibitem{40} Id.
\bibitem{41} Reg. 1.170A-14(d)(4)(iii)(C).
\bibitem{42} Id.
\bibitem{43} Id.
\bibitem{44} Reg. 1.170A-14(d)(4)(v).
\bibitem{45} Reg. 1.170A-14(d)(4)(vi)(A).
\bibitem{46} Reg. 1.170A-14(d)(4)(vi)(A).
\bibitem{47} Id.
\bibitem{48} Reg. 1.170A-14(d)(4)(vi)(C).
\bibitem{49} Id.
\bibitem{50} Internal Revenue Service, Conservation Easement Audit Techniques Guide (ATG) (rev.
1/24/2018), page 23.
\bibitem{51} Section 170(a)(1). Reg. 1.170A-1(c)(1).
\bibitem{52} Section 170(a)(1), Reg. 1.170A-1(c)(1).
\end{thebibliography}
open space (including farmland and forest land) will have an acceptable conservation purpose if such preservation is done pursuant to a clearly delineated federal, state, or local governmental conservation policy and will yield a significant public benefit. The purpose of this standard is to protect the types of property identified by representatives of the general public (i.e., government officials) as worthy of preservation or conservation. In terms of degree, the regulations state that a “general” declaration of conservation goals by a “single” government official or legislative body is not enough, but it is not necessary that a governmental conservation policy be a “certification program” that identifies particular properties. A taxpayer will meet this standard if it makes a donation that furthers a specific, identified conservation project, including, but not limited to, (i) preservation of land within a state or local landmark district that is locally recognized as being significant to that district, (ii) preservation of a wild or scenic river, (iii) preservation of farmland pursuant to a state program for flood prevention and control, or (iv) protection of the scenic, ecological, or historic character of land that is contiguous to, or an integral part of, the surroundings of existing recreation or conservation sites.

A conservation program does not need to be funded in order to satisfy this standard; however, it must involve a significant commitment by the government regarding the program. An example would be a program granting preferential taxes or zoning for property considered protection-worthy.

The fact that a federal, state, or local government agency (or a related commission, authority, or body) has accepted an easement tends to demonstrate a clearly delineated governmental policy, but it, alone, is insufficient. The regulations acknowledge that a federal, state, or local government agency (or a related commission, authority, or body) has formed an environmental trust to accept property that meets certain conservation purposes, and such trust employs a review process requiring approval from the highest officials in the state, acceptance of a property by the trust fortifies the necessary governmental policy. Limited public access to the property would not cause the tax deduction to be disallowed, unless the conservation purpose of the donation would be “undermined or frustrated” as a result of such access restrictions. For example, a donation in conformity with a governmental policy to protect the “scenic character” of land near a river necessitates public access to the same extent as a donation aimed at preserving open space (including farmland and forest land) for the scenic enjoyment of the general public.

According to the regulations, no tax deduction for preservation of open space pursuant to a clearly delineated governmental conservation policy will be permitted if the easement allows a “degree of intrusion or future development that would interfere with the . . . governmental conservation policy that is being furthered by the donation.” As explained above, all donations of QRPI made to preserve open space, including those done pursuant to a governmental conservation policy, must yield a “significant public benefit.” The regulations acknowledge that making a donation in accordance with a “clearly delineated governmental policy,” and ensuring that such donation generates a “significant public benefit,” are two separate requirements, which must be independently met. The more specific the governmental policy, the more likely the governmental decision to accept an easement, alone, will tend to show that a “significant public benefit” exists.

Finally, the regulations recognize that, in certain situations, an open space easement might be for “scenic enjoyment” and done pursuant to a “clearly delineated governmental policy.” An example would be the preservation of a scenic view that has been identified as part of a scenic landscape inventory by a rigorous governmental review process.

Can Taxpayers Still Use the Property Under Easement?

A taxpayer can retain certain “reserved rights,” still make a qualified conservation contribution, and thus qualify for the tax deduction. However, in keeping something for themselves, taxpayers must ensure that the reserved rights do not unduly conflict with the conservation purposes.

The fact that a federal, state, or local government agency (or a related commission, authority, or body) has accepted an easement tends to demonstrate a clearly delineated governmental policy, but it, alone, is insufficient.
and willing seller would agree, with neither party being obligated to participate in the transaction, and with both parties having reasonable knowledge of the relevant facts.53 In deciding the FMV of property, appraisers and courts must take into account not only the current use of the property, but also its highest and best use (“HBU”).54 A property’s HBU is the most profitable use for which it is adaptable and needed, or likely to be needed in the reasonably near future.55 The term HBU has also been defined as the reasonably probable use of property that is physically possible, legally permissible, financially feasible, and maximally productive.56 Importantly, valuation does not depend on whether the owner has actually put the property to its HBU.57 The HBU can be any realistic, objective potential use of the property.58

**How Do Taxpayers Prove the Condition of the Property at Donation Time?**

In situations involving the donation of a QRPI where the donor reserves certain rights whose exercise might impair the conservation purposes, the tax deduction will not be allowed unless the donor “makes available” to the easement-recip- 2ient, before the donation is made, "documentation sufficient to establish the condition of the property at the time of the gift.”59 This is generally called the Baseline Report.

The Baseline Report “may” (but not “must”) include: (i) the appropriate survey maps from the U.S. Geological Survey, showing the property line and other contiguous or nearby protected areas, (ii) a map of the area drawn to scale showing all existing man-made improvements or incursions (e.g., roads, buildings, fences, or gravel pits), vegetation and identification of flora and fauna (e.g., locations of rare species, animal breeding and roosting areas, and migration routes), land use history, and distinct natural features, (iii) an aerial photograph of the property at an appropriate scale taken as close as possible to the date of the donation, and (iv) on-site photographs taken at appropriate locations on the property.60 If the easement contains restrictions regarding a particular natural resource, such as water or air quality, then the condition of the resource at or near the time of the donation must be established.61 The Baseline Report “must be accompanied by a statement signed by the donor and a representative of the [easement-recip- 2ient] clearly referencing the [Baseline Report] and in substance confirming that the property description and the natural resources inventory are accurate.62

**How Do Taxpayers Claim an Easement-Related Tax Deduction?**

Properly claiming the tax deduction triggered by an easement donation is, well, complicated. It involves a significant amount of actions and documents. The main ones are as follows: The taxpayer must (i) obtain a “qualified appraisal” from a “qualified appraiser,” (ii) demonstrate that the easement-recip- 2ient is a “qualified organization,” (iii) obtain a timely Baseline Report, generally from the easement-recipient, describing the condition of the property at the time of the donation and the reasons for which it is worthy of protection, (iv) complete a Form 8283 (Noncash Charitable Contributions) and have it executed by all relevant parties, including the taxpayer, appraiser, and easement-recipient, (v) assuming that the taxpayer is a partnership, file a timely Form 1065 (U.S. Return of Partnership Income), enclosing Form 8283 and the qualified appraisal, (vi) receive from the easement-recipient a contemporaneous written acknowledgement, both for the easement itself and for any endowment/stewardship fee donated to finance the perpetual protection of the property, (vii) ensure that all mortgages on the relevant property have been subordinated before granting the easement, and (viii) send to all partners their Schedule K-1 (Partner’s Share of In-
come, Deductions, Credits, etc.) and a copy of the Form 8283.⁶³

Technical Arguments Raised by the IRS

The first line of attack by the IRS is to raise a number of technical arguments, i.e., those not related to valuation. The ATG contains a “Conservation Easement Issue Identification Worksheet” that identifies a long list of technical challenges to which the IRS might point as a reason for completely disallowing an easement-related tax deduction.⁶⁴ Among the common challenges by the IRS are that the relevant property lacks acceptable “conservation purposes” for any number of reasons, including, but not limited to: (i) the habitat is not protected in a relatively natural state, (ii) there are insufficient threatened or endangered species on the property, (iii) the habitats or ecosystems to be protected are not “significant,” (iv) the public lacks physical or visual access to the property, (v) the conservation will not yield a significant public benefit, (vi) the property lacks historical significance, (vii) the conservation purpose does not comport with a clearly-delineated government policy, (viii) the easement allows uses that are inconsistent with the conservation purposes, and (ix) the donor has certain “reserved rights” that interfere with or destroy the conservation purposes.⁶⁵

Eligibility Requirements Expanded by the IRS

As indicated above, the IRS ordinarily starts its attack by raising various technical arguments, including that the relevant property lacks adequate conservation purposes. An important, yet largely unaddressed, issue in this area is that the IRS might have exceeded its authority in promulgating the applicable rules. This matter is clarified below.

Section 170(h)(4)(A), enacted by Congress, states that the “term conservation purpose means [among other things] the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem.”⁶⁶ By contrast, the applicable regulations, issued by the IRS, provide the following:

The donation of a qualified real property interest to protect a significant relatively natural habitat in which a fish, wildlife, or plant community; or similar ecosystem normally lives will meet the conservation purposes test …⁶⁷

Significant habitats and ecosystems include, but are not limited to, habitats for rare, endangered, or threatened species of animal, fish, or plants; natural areas that represent high quality examples of a terrestrial community or aquatic community, such as islands that are undeveloped or not intensely developed where the coastal ecosystem is relatively intact; and natural areas which are included in, or which contribute to, the ecological viability of a local, state, or national park, nature preserve, wildlife refuge, wilderness area, or other similar conservation area.⁶⁶

The legislative history provides additional insight. It states the following: [C]onservation purposes includes the protection of a [not a “significant”] relatively natural fish, wildlife or plant habitat, or similar ecosystem. Under this provision, a contribution would be considered to be made for conservation purposes if it will operate to protect or enhance the viability of an [not a “significant”] area or environment in which a fish, wildlife, or plant community normally lives or occurs. It would include the preservation of a [not a “significant”] habitat or environment which to some extent had been altered by human activity if the fish, wildlife, or plants exist there in a [not a “significant”] relatively natural state … The committee intends that contributions for this purpose will protect and preserve significant natural habitats and ecosystems, in the United States … ⁶⁷

In summary, the law expressly states that the easement must protect “a” relatively natural habitat of fish, wildlife, or plants, or similar ecosystem, whereas the regulations demand that the easement safeguard a “significant” relatively natural habitat of fish, wildlife, or plants, or similar ecosystem. The only support for the IRS to add this critical word to the regulations is one vague reference, in one congressional report. It is unclear whether Congress meant to say that taxpayers must protect “significant” natural habitats or ecosystems, whether it wanted to express that the result of this provision would be the protection of “significant” amounts of natural habitats and ecosystems, or whether this was simply an oversight given that such term is not used elsewhere when referring to safeguarding habitats and ecosystems.

In all events, the caselaw is clear that legislative reports cannot be used to supplant legislation. For instance, the court explained in one case that “[l]egislative committee reports, of course, may not be used as an excuse for ignoring statutory text.”⁶⁸ Moreover, courts have held that legislative reports should not be viewed narrowly:

In sum, we think it plainly wrong as a general matter, and in this case in particular, to regard committee reports as drafted more meticulously and as reflecting the congressional will more accurately than the statutory text itself. Committee reports, we remind, do not embody the law. Congress, as Judge Scalia recently noted, votes on the statutory words, not on different expressions packaged in committee reports.⁶⁹

Finally, courts have determined that legislative reports are particularly unreliable where the statements for which they are being used conflict with the statutes to which they refer:

When there is conflict between an unambiguous statute and its legislative history, the legislative history, particularly when equivocal, is to be accorded little or no weight … To
credit a committee report over the statute would elevate the narrow views of a legislative subgroup or of unelected congressional staff over the constitutional enactments of Congress and the President. Committee reports provide scant evidence of even a probable or constructive legislative intent, because they are crafted by staff, not necessarily read by legislators, and are subject to packing via influence of interest groups and other legislative insiders. In sum, even unequivocal evidence of Congress’ contrary purpose would not justify this court’s ignoring the plain meaning of a statute in favor of its legislative history of supplying a new statutory provision.25

The questionable insertion of this one word, “significant,” by the IRS in the conservation easement donation regulations has impacted how Tax Court cases are decided, as shown below.

Easement Cases Focused on Conservation Purpose

Conservation purpose has been an important issue in several Tax Court cases.26 The most recent one was Champions Retreat Golf Founders, LLC v. Commissioner.27 The relevant facts, contentions, and decisions in that case are discussed below.28

Background and Main Events

Champions Retreat Golf Founders, LLC ("Partnership") acquired about 463 acres in 2002 for purposes of building a golf course. The property is located near Augusta, Georgia, along the Savannah River and an offshoot, the Little River. Sumter National Forest is located on the other side of the Savannah River, about 700 feet away.

The Partnership initially raised $13.2 million to build the golf course by selling 66 residential lots in a development called Founders Village. It borrowed heavily, too. Each lot in Founders Village came with a lifetime membership at the golf club. Construction of the golf club was completed in June 2005. It is located in a development called the Reserve, which is private and accessible only through a security gate manned around the clock. The golf club occupies about 366 of the 463 acres, and features three nine-hole courses, a pro shop, restaurant, locker room, cart storage facility, driving range, and paved parking lot.

The Partnership was not profitable initially. Therefore, after learning of the decision in Kiva Dunes Conservation, LLC v. Commissioner where the Tax Court upheld a charitable tax deduction stemming from the placement of a conservation easement on an operating golf course, the accountant for the Partnership proposed doing the same thing on the entire property, including the golf course.29 The idea was to attract additional investment, such that the Partnership could reduce the balance of its construction-related debt from years earlier.

Apparently, in exploring this idea, a conservation biologist with the land conservancy to which the easement was eventually granted ("Land Trust") did an initial survey of the property in late 2009, finding that it was worthy of conservation.

The financing was done through Kiokee Creek Preservation Partners, LLC ("Kiokee Creek"), a partnership formed in September 2010. Most of the partners in Kiokee Creek, who contributed total capital of $2.7 million, were clients of the accountant. These funds were then contributed to the Partnership in exchange for a 15 percent ownership interest in the Partnership and a special allocation of the charitable deduction.

The conservation biologist with the Land Trust analyzed the property again in November 2010, shortly after the money had been raised. He concluded, as he had earlier, that the property, including the golf club, had characteristics making it conservation-worthy.

On December 16, 2010, the Partnership donated an easement to the Land Trust that covered about 349 acres, the Deed of Conservation Easement was properly recorded soon thereafter, on December 29, 2010, and the Land Trust provided the contemporaneous written acknowledgement of the easement donation on February 7, 2011. The 349 acres donated covered 25 of the 27 total holes on the three golf courses, most of the remaining two holes, and the driving range. It did not cover the pro shop, restaurant, locker room, cart storage facility, paved parking lot, or various residential developments nearby.

The conservation biologist from the Land Trust returned to the property a third time, on May 12, 2011, which was more than four months after the Partnership had granted the easement. The idea, apparently, was for the biologist to have an opportunity to observe the natural features of the property at different times/seasons throughout the year. All three visits by the biologist were cited in his Baseline Report, even though the last one occurred after the placement of the easement.

The Deed of Conservation Easement identified three conservation purposes, namely, (i) protection of a relatively natural habitat of fish, wildlife, or plants, or a similar ecosystem, (ii) preservation of open space for the scenic enjoyment of the general public, while yielding a significant public benefit, and (iii) preservation of open space pursuant to a federal, state, or local governmental conservation policy, while yielding a significant public benefit.

The Deed of Conservation Easement imposed several restrictions on the Partnership with respect to the golf course.

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27. Champions Retreat Golf Founders, LLC, TCM 2008-146.
28. The author reviewed the following documents in preparing this portion of the article: Petition filed February 23, 2015; Answer filed April 29, 2015; Pre-Trial Memo for Respondent filed October 7, 2016; Pre-Trial Memo for Petitioner filed October 7, 2016; Respondent’s Opening Brief filed January 25, 2017; Petitioner’s Opening Brief filed January 25, 2017; Respondent’s Answering Brief filed March 13, 2017, Petitioner’s Answering Brief filed March 13, 2017; First Stipulation of Facts filed October 25, 2016; Joint Stipulation of Settled Issues filed January 13, 2017.
30. Champions Retreat Golf Founders, LLC, supra note 74.
31. Id. (emphasis added).
32. Id.
33. Id.
34. Id.
These consisted of the following. First, it restricted the ways in which the Partnership could use the easement area, including the types of structures that it could build. Second, it required the Partnership to use “the best environmental practices then prevailing in the golfing industry” in maintaining the golf club, to keep records relating to such maintenance, and to submit an annual maintenance report to the Land Trust. Third, it prevented the Partnership from removing surface or ground water, live or dead trees, or any other raw materials. Fourth, it stopped the Partnership from placing signs, outdoor advertising, or any new roads. Fifth, it forced the Partnership not to manipulate a creek or pond, allow chemical discharge to flow into a creek or pond, clear vegetation within 100 feet of a creek or pond, or cause soil erosion or sedimentation into a creek or pond. Sixth, it prohibited the Partnership from dividing the easement area into lots. Finally, it obligated the Partnership to notify the Land Trust in writing before it exercises any reserved right in a way that might impair the conservation purposes.

As is true with most cases of easements, there were several exceptions to the restrictions, described above, in the Deed of Conservation Easement. For example, the Partnership can build structures covering up to 10,000 square feet on the easement area, and it can remove trees and vegetation, and it can shift features of the golf courses (including fairways and greens), as part of the building process. Moreover, the Partnership has the right to widen by 10 feet and then pave an existing road. The Partnership can also remove any tree, whether it be standing or fallen, that is within 30 feet of a playable area on the golf course. Lastly, and importantly to the case, the Partnership can maintain in manicured condition all golf course play areas, including the lakes, creeks, ponds, and other water areas that are an integral part of the golf course. The list of reserved rights entails the ability to use chemicals.

**The Tax Dispute Begins**

The Partnership claimed a charitable deduction of $10,427,435 on its 2010 Form 1065, 98.8 percent of which was allocated to Kiokee Creek, even though it held only a 15 percent ownership interest. An audit ensued, at the end of which the IRS issued an FPAA fully disallowing the charitable deduction on two main grounds. The IRS first claimed that the Partnership had one or more technical violations of the requirements under Section 170. Even if the Partnership complied with Section 170, the IRS claimed that the deduction was worthless because the Partnership had failed to establish that the value exceeds $0.

**Decision by the Tax Court**

The Partnership filed a timely Petition disputing the FPAA, the case was litigated, and the Tax Court rendered its decision. Its analysis was solely focused on one issue; that is, whether the conservation easement meets at least one of the acceptable conservation purposes. First the IRS, then the Tax Court, disagreed with the assertions by the Partnership.

Relatively natural habitat. The regulations indicate that significant habitats and ecosystems encompass, among other things, (i) habitats for rare, endangered, or threatened species of animal, fish, or plants, (ii) natural areas that represent high quality examples of a terrestrial or aquatic community; and (iii) natural areas that are included in, or contribute to, the ecological viability of a park, nature preserve, wildlife refuge, wilderness area, or other similar conservation area.

The Partnership argued that the easement area provides a habitat for several species, including birds, the southern fox squirrel, and the denseflower knotweed. The Tax Court agreed with the Partnership that the concept of “rare, endangered, or threatened,” which is not specifically defined in the regulations under Section 170, is not limited to those species listed under the Endangered Species Act of 1973. After the Tax Court applied that notion to the first species, birds, the Tax Court explained that the experts observed several types of birds that were listed on the watchlist of one conservation group or another, but they were generally found within a lower threat level or listed as not a concern in the relevant region. The Tax Court underscored that none of the birds observed had been assigned the highest threat level by any of the conservation organizations.

With respect to the southern fox squirrels, the Tax Court indicated that, while all the trial experts agreed that these creatures might be in decline, it could not conclude they fell into the category of rare, endangered, or threatened. Indeed, one conservation group indicated that the squirrels are secure on a global level, and they are still hunted legally in Georgia.

The Tax Court next turned to the denseflower knotweed. The Tax Court acknowledged that the evidence presented at trial created uncertainty about the threat status of this plant in Georgia. Nevertheless, the Tax Court focused on the fact that the plant was found almost exclusively in a 26-acre area, which constitutes just 7.5 percent of the total easement area of 349 acres. Assuming that the denseflower knotweed could grow in another similar area (i.e., undisturbed bottomland forest) in the easement area, these two parts together would comprise less than 17 percent of the total easement area. Moreover, underscored the Tax Court, one hole on the golf course is designed to drain into the only area where the plant was found, thereby introducing chemicals (e.g., fertilizers, pesticides, herbicides, and fungicides) into its habi-
tat. Interpreting the expert testimony in a manner favorable to the Partnership, the Tax Court still held that the existence of the plant on less than 17 percent of the total easement area is insufficient to fully satisfy the conservation purpose of protecting a significant relatively natural habitat.83

The Tax Court summarized its decision that the golf course easement did not protect a relatively natural habitat in the following manner:

[The Partnership] has presented evidence of only one rare, endangered, or threatened species with a habitat on the easement area—denseflower knotweed—and it inhabits just a small fraction of the easement area. To get around these facts, [the Partnership] would have us ignore the specific wording of the regulation and adopt a standard that includes any species of current or future conservation concern. This we cannot do... We, therefore, conclude that [the Partnership] has not met the conservation purpose requirement by providing a "habitat for rare, endangered, or threatened species of animals, fish, or plants."84

In terms of the water aspects of the easement area (including lakes, ponds, and creeks), one expert said that the ponds were high-quality aquatic environments. The Tax Court emphasized, however, that the chemicals used by the Partnership to maintain the golf course would damage such environments, regardless of whether the chemicals were applied directly or through runoff.85 The Partnership countered that use of chemicals should not invalidate the conservation qualities because it complied with all applicable state rules in selecting and applying chemicals, and the Deed of Conservation Easement demands that the Partnership follow the best environmental practices in the golf industry.86 The Tax Court held that it had no doubt that the Partnership aimed to use chem-
icals responsibly, but it did not prove that the best practices in the golf industry are equal to or better than “the best environmental practices then prevailing for conservation, as might be expected if conservation was the purpose of the easement.”

The Partnership also argued that the easement area is a relatively natural habitat because it constitutes a “natural area” that contributes to the ecological viability of Sumter National Forest, which is located across the Savannah River, about 700 feet away from the golf course. In short, the Partnership contended that the golf course was worthy of conservation because birds, insects, and pollen will travel back and forth to Sumter National Forest.

The Tax Court agreed that Sumter National Forest is a “national park,” but emphasized that the easement area does not constitute a “natural area,” as required by the regulation. The Tax Court then indicated that, contrary to the claims by the Partnership, just having trees, vegetation, and species that inhabit them does not suffice to be a “natural area” when such trees and vegetation are heavily managed and manicured, as they are on and around the golf course. The Tax Court went on to explain that, even if it were to hold that the areas between the fairways on the golf course resembling open pine woodlands were “natural areas” for these purposes, there is no guarantee that such areas will be adequately protected, because the Deed of Conservation Easement specifically permits the Partnership to remove any tree, standing or fallen, that is located within 30 feet of a playable area.91

Preservation of open space for the general public. As explained above, to fall into the category of preservation of open space for the scenic enjoyment of the general public, it suffices that there is visual (instead of physical) access to the property or across the property by the general public.92 Also, it is not necessary that the whole property be visible to the public.93

The Tax Court, even applying this flexible standard, determined that the conservation easement was insufficient because the public had no physical access to a private golf course protected by a gate and personnel, the only visual access would be from the two rivers running alongside the golf course, the river banks ranging from three to 10 feet high obstruct the views from the water, and there is ongoing legal uncertainty regarding whether the public can even utilize one of the two rivers, the Little River.94

In summary, the law expressly states that the easement must protect “a” relatively natural habitat of fish, wildlife, or plants, or similar ecosystem, whereas the regulations demand that the easement safeguard a “significant” relatively natural habitat of fish, wildlife, or plants, or similar ecosystem.

Conservation of open space pursuant to governmental policy. The Partnership argued that it donated the easement to the Land Trust to preserve open space pursuant to a Georgia law directing the Georgia Department of Natural Resources and local governments to create minimum standards for protecting natural resources, the environment, and vital areas, including river corridors, and the local county’s implementation of the Georgia Greenspace Program.95 The Tax Court rejected this argument, explaining that the Georgia law cited by the Partnership pointed out that such law was focused on land development, not land conservation.96

For these reasons, the Tax Court concluded that “the preservation of open space was not pursuant to a clearly delineated governmental conservation policy.”97

Ultimate Determination by Tax Court
The Tax Court resolved the entire case by deciding just one issue; that is, that the donation of the easement by the Partnership lacked sufficient “conservation purpose” to meet the requirements of Section 170(h).98

New Case Questioning Regulatory Actions by IRS
A recent case, focused on Section 170 and certain regulations promulgated by the IRS to implement it, calls into question actions by the IRS in the conservation easement field. The case, decided in August 2019, is Mayo Clinic v. United States.99 It is examined below.
Mayo is a nonprofit corporation and tax-exempt organization under Section 501(c)(3). After conducting an audit, the IRS issued a Notice of Proposed Adjustment asserting that Mayo owed tax on certain income that it received from various partnerships because Mayo was not an “educational organization.” Mayo paid the disputed taxes of approximately $12 million, filed a claim for refund, and, eventually, lodged a suit for refund with the District Court.100

According to the District Court, Mayo would be entitled to a refund if it fell into the following category described in Section 170(b)(1)(A)(ii):

An educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.102

The government’s position was that, while Mayo maintains a regular faculty, curriculum, and student body, it is not an “educational organization” and, thus, not deserving of the refund. In taking this position, the government relied on its own regulation interpreting Section 170(b)(1)(A)(ii), which states that an entity cannot be an “educational organization” unless education is its “primary function” and its noneducational functions are “merely incidental” to its educational activities.103 The relevant regulation states the following:

An educational organization is described in Section 170(b)(1)(A)(ii) if its primary function is the presentation of formal instruction and it normally maintains a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. It does not include organizations engaged in both educational and noneducational activities unless the latter are merely incidental to the educational activities.104

The District Court examined the issue applying the so-called Chevron test or standard.105 The District Court held in favor of Mayo for a number of reasons, the primary ones being that (i) the relevant statute, Section 170(b)(1)(A)(ii), did not include the primary-function test or the merely-incidental test, and (ii) Congress knew how to insert such requirements if that was its intent, as demonstrated by the fact that the following tax provision, Section 170(b)(1)(A)(iii), specifically mandates that the relevant organization have a “principal purpose or function” of providing certain services or engaging in certain activities. Some of the key quotes by the District Court are set forth below.

Congress unambiguously chose not to include a primary-function requirement in [Section] 170(b)(1)(A)(ii), and the Treasury Department exceeded the bounds of its statutory authority when it promulgated the primary-function requirement in [Reg.] 1.170A-9(c)(1). Section 170(b)(1)(A)(ii) contains no explicit primary-function requirement, but the equivalent of that very requirement appears in the very next subsection of the statute, [Section] 170(b)(1)(A)(iii). In this situation—that is, when Congress imposes a particular requirement in one subsection of a statute but not in another—settled rules of statutory construction say that the absence of the requirement is generally to be considered a deliberate omission [by Congress] that must be respected [by the IRS].106

The conclusion that a primary-function or merely-incidental requirement is inconsistent with [Section] 170(b)(1)(A)(ii) is based primarily on the implicit presence of a primary-purpose test in the next subsection of the same statute, [Section] 170(b)(1)(A)(iii). That adjoining subsection was enacted at the same time as [Section] 170(b)(1)(A)(ii) and for the same purpose.107

The corollary of determining that Congress unambiguously did not include a primary-function requirement in [Section] 170(b)(1)(A)(ii) is that Congress also must be understood to have decided not to include a merely-incidental test in this statute, at least as that test is described in the corresponding regulations.108

The government’s position that Mayo is not entitled to the refunds it seeks is premised entirely on Mayo’s alleged inability to satisfy the primary-function and merely-incidental requirements in [Reg.] 1.170A-9(c)(1). Because these requirements exceed the bounds of authority given by [Section] 170(b)(1)(A)(ii), they are unlawful.109

[T]he regulation does more than the law allows because it adds requirements—the primary-function and merely-incidental tests—Congress intended not to include in the statute. Because the government’s position is based entirely on these impermissible requirements, Mayo is entitled to the sued-for refunds.110

Application of Mayo Clinic to Conservation Easement Cases

In the context of conservation easements, Section 170(h)(4)(A), enacted by Congress, states that the term “conservation purpose” means the following:

1. the preservation of land areas for outdoor recreation by, or the education of, the general public;
2. the protection of a [not a “significant”] relatively natural habitat of fish, wildlife, or plants, or similar ecosystem;
3. the preservation of open space (including farmland and forest land) where such preservation is (I) for scenic enjoyment of the general public, or (II) pursuant to a clearly delineated federal, state, or local governmental conservation policy.

NOTES

100 Id.
101 Id.
102 Id., Reg. 1.170A-9(c)(1).
103 Id., Reg. 1.170A-9(c)(1) (emphasis added).
105 Mayo Clinic, supra note 100.
106 Id.
107 Id.
108 Id.
109 Id.
110 Id.
111 Section 170(h)(4)(A) (emphasis added).
114 See, e.g., Champions Retreat Golf Founders, LLC, supra note 74; Glass, supra note 73; Atkinson, supra note 73.
115 Champions Retreat Golf Founders, LLC, supra note 74 (emphasis added).
116 Id. (emphasis added).
117 Atkinson, supra note 73.
118 Id. (emphasis added).
and will yield a significant public benefit, or
4. the preservation of an historically important land area or a certified historic structure.111

However, the corresponding regulations, promulgated by the IRS, state that the "conservation purpose" test is met only if a taxpayer donates a QRPI "to protect a significant relatively natural habitat in which fish, wildlife, or plant community, or similar ecosystem normally lives."112 The regulations go on to provide a definition of a "significant habitat or ecosystem."113 Several Tax Court cases have focused on the adequacy of conservation purposes.114 Notably, Champions Retreat, analyzed above, was decided against the taxpayers for a few reasons, including the Tax Court did not find "a sufficient presence of rare, endangered, or threat- ened species in the easement area to satisfy the conservation purpose requirement,"115 particularly since the only pertinent species identified, the denseflower knotweed, only existed on a portion of the eased land. According to the Tax Court in Champions Retreat, "[l]ess than 17% of the easement area is not enough to fulfill the conservation purpose of providing a significant relatively natural habitat."116

The Tax Court came to a similar conclusion in an earlier case, Atkinson v. Commissioner.117 There, the Tax Court indicated that the existence of two types of rare plants on "only 24%" of the easement property "represents too insignificant a portion of the 2003 easement to lead us to conclude that the whole 2003 easement property is a significant natural habitat."118

The similarities between Mayo Clinic and the conservation easement cases is striking. First, in both instances, the relevant portion of Section 170, enacted by Congress, is devoid of certain key terms. In Mayo Clinic, the statute lacked the primary-function and merely-incidental requirements, while in the conservation easement cases, the statute does not contain the word "significant." Second, in promulgating the applicable regulations, the IRS exceeded the standards established by Congress by inserting new requirements. Third, in both instances, Congress included stricter requirements in the very next part of the law. In Mayo Clinic, 170(b)(1)(A)(iii), which follows the key provision, 170(b)(1)(A)(ii), specifically demands that the relevant organizations have a "principal purpose or function" of providing certain services or engaging in certain activities, which is akin to "primary function." With respect to easement cases, Section 170(h)(4)(A)(ii) expressly states that the donation must preserve open space and yield a "significant" public benefit, which is the term conspicuously absent from the relevant provision, Section 170(h)(4)(A)(ii).

The difference between Mayo Clinic and the conservation easement cases is that the District Court in Mayo Clinic rejected the notion that the IRS can unilaterally add requirements via a regulation, whereas the Tax Court has seemed to accept, or perhaps the partnerships neglected to adequately argue, the notion that the IRS is permitted to insert the critical term "significant" when discussing habitats and ecosystems.

Conclusion
The future holds more audits of conservation easement partnerships, which will include challenges to whether the conservation purposes were "significant" enough, at least from the IRS’s perspective. This article demonstrates that taxpayers now have more ammunition in defending against such attacks, thanks to the recent decision, Mayo Clinic, and its potential applicability to the conservation easement arena.