Conservation Easement Enforcement: IRS Quietly Eliminates Procedural Protections for Appraisers

HALE E. SHEPPARD

This article examines the main concepts around conservation easement donations, categories of IRS attacks against partnerships, evolution of the appraiser penalty rules, and impacts of new IRS guidance.

Unless somebody has been living under the proverbial rock the past few years, he is aware that the IRS is aggressively attacking "syndicated" partnerships that donate conservation easements to charity and claim the related tax deductions. This is common knowledge. What many people do not realize, though, is that the IRS is pursuing others involved with easement donations, and methodically changing the rules to achieve its goals. For instance, with absolutely no fanfare, the IRS released in late January 2020 what appeared to be a routine, innocuous, procedural memorandum called "Interim Guidance on IRC 6695A Penalty Case Reviews" ("Interim Guidance").[1] The reality is that this Interim Guidance triggers a critical change, eliminating the multi-level review procedure formerly used by the IRS to protect appraisers against improper penalties and disciplinary referrals. This article explains the main concepts around easement donations, categories of IRS attacks against partnerships, evolution of the appraiser penalty rules, and impacts of the new Interim Guidance.

Overview of Conservation Easement Concepts

One must first have a basic understanding of the applicable terms and concepts to appreciate the significance of this article

HALE E. SHEPPARD (B.S., M.A., J.D., LL.M., LL.M.T.) is a Shareholder in the Tax Controversy Section of Chamberlain Hrdlicka. Hale specializes in tax audits, tax appeals, and tax litigation. You can reach Hale by phone at (404) 658-5441 or by e-mail at hale.sheppard@chamberlainlaw.com. *Copyright ©2020, Hale E. Sheppard.*

What Is a Qualified Conservation Contribution?

Taxpayers generally may deduct the value of any charitable contribution that they make during a year.[2] However, taxpayers are not entitled to deduct donations of property if they consist of less than their entire interest in such property.[3] 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."[4] To meet this critical definition, taxpayers must show that they are donating a qualified real property interest ("QRPI"), to a qualified organization, exclusively for conservation purposes.[5]

A QRPI can be one of several things, including a restriction, granted in perpetuity, on the use of a particular piece of real property.[6] This is known by many names, among them "conservation easement."[7] Regardless of what you call them, QRPIs must be based on legally enforceable restrictions, memorialized in a Deed of Conservation Easement filed with the proper court or other location, preventing uses of the property, forever, which are inconsistent with the conservation purposes.[8]

For What Purposes Can Land Be Conserved?

A donation has a "conservation purpose" if it meets one of the following requirements: (1) It preserves land for outdoor recreation by, or the education of, the general public; (2) It preserves a relatively natural habitat of fish, wildlife, or plants, or a similar ecosystem; (3) It preserves open space (including farmland and forest land) for the scenic enjoyment of the general public and will yield a significant public benefit; (4) 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 (5) It preserves a historically important land area or a certified historic structure.[9] Such conservation purposes must be protected forever in order to trigger the tax deduction. Indeed, a donation is not treated as "exclusively for conservation purposes," unless the conservation purposes are "protected in perpetuity."[10]

Can Taxpayers Reserve Rights in the Donated Property?

Taxpayers can retain "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.[11] The IRS openly recognizes, in its Conservation Easement Audit Techniques Guide ("ATG"), that reserved rights are ubiquitous. The ATG states the following about taxpayer holdbacks:

> *All conservation easement donors reserve some rights to the property.* Depending on the nature and extent of these reserved rights, the claimed conservation purpose may be eroded or impaired to such a degree that the contribution may not be allowable. A determination of whether the reserved rights defeat the conservation purpose must be determined based on all the facts and circumstances.[12]

How Do Taxpayers Prove the Condition of the Property?

In situations involving the donation of a QRPI where the donor reserves certain rights, the tax deduction will not be allowed unless the donor "makes available" to the easement-recipient, before the donation is made, "documentation sufficient to establish the condition of the property at the time of the gift."[13] This is generally called the Baseline Report.

The Baseline Report "may" (but not "must") include (1) the appropriate survey maps from the U.S. Geological Survey, showing the property line and other contiguous or nearby protected areas, (2) a map of the area drawn to scale showing all existing man-made improvements or incursions, vegetation, flora, and fauna (*e.g.*, locations of rare species, animal breeding and roosting areas, and migration routes), land use history, and distinct natural features, (3) an aerial photograph of the property at an appropriate scale taken as close as possible to the date of the donation, and (4) on-site photographs taken at appropriate locations on the property.[14]

What Is an Easement Worth?

Generally, a deduction for a charitable donation is allowed in the year in which it occurs.[15] If the donation consists of something other than money, the amount normally is the fair market value ("FMV") of the property at the time the taxpayer makes the donation.[16] For these purposes, the term "FMV" ordinarily means the price on which a willing buyer 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.[17]

The regulations provide special rules for calculating a deduction stemming from the donation of a conservation ease-

NOTES

1 Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.
2 Section 170(a)(1); Reg. 1.170A-1(a).
3 Section 170(f)(3)(A); Reg. 1.170A-7(a)(1).
4 Section 170(f)(3)(B)(iii); Reg. 1.170A-7(a)(5).
5 Section 170(h)(1).
6 Section 170(h)(2); Reg. 1.170A-14(a); Reg. 1.170A-14(b)(2).
7 Reg. 1.170A-14(b)(2).
8 Reg. 1.170A-14(g)(1); *Turner*, 126 TC 299, 311 (2006).
9 Section 170(h)(4)(A); Reg. 170A-14(d)(1); S. Rept. 96–1007, at 10 (1980).
10 Section 170(h)(5)(A); Reg. 1.170A-14(e)(1).
11 Reg. 1.170A-14(b)(2).
12 IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), p. 23; *see also* Reg. 1.170A-14(e)(2) and (3).
13 Reg. 1.170A-14(g)(5)(i).
14 Reg. 1.170A-14(g)(5)(i).
15 Section 170(a)(1).
16 Section 170(a)(1); Reg. 1.170A-1(c)(1).
17 Reg. 1.170A-1(c)(2).
18 Reg. 1.170A-14(h)(3)(i).
19 IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), p. 41.
20 IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), p. 41.
21 *Stanley Works & Subs.*, 87 TC 389, 400 (1986); Reg. 1.170A-14(h)(3)(i) and (ii).
22 *Olson*, 292 U.S. 246, 255 (1934).
23 *Esgar Corp.*, 744 F.3d 648, 659 n. 10 (CA-10, 2014).
24 *Esgar Corp.*, 744 F.3d 648, 657 (CA-10, 2014).
25 *Symington*, 87 TC 892, 896 (1986).
26 *See* IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), pp. 24-30; IRS Publication 1771, Charitable Contributions—Substantiation and Disclosure Requirements; IRS Publication 526, Charitable Contributions; Section 170(f)(8); Section 170(f)(11); Reg. 1.170A-13; Notice 2006-96; TD 9836.
27 IRS, Conservation Easement Audit Techniques Guide. (Rev. 11/4/2016).

ment.[18] The IRS provides the following summary and hints about valuation to its personnel in the ATG. It explains that the best evidence of FMV of an easement is the sale price of easements comparable to the easement in question, but, "in most instances, there are no comparable easement sales."[19] Appraisers, therefore, often must use the before-and-after method. The ATG acknowledges that this effectively means that an appraiser must determine the highest and best use ("HBU"), *and* the corresponding FMV of the relevant property twice. First, the appraiser calculates the FMV if the property were put to its HBU, which generates the "before" value. Second, the appraiser identifies the FMV, taking into account the restrictions on the property imposed by the easement, which creates the "after" value.[20] The difference between the "before" and "after" value, with certain other adjustments, produces the value of the easement donation.

As indicated in the preceding paragraph, in deciding the FMV of property, appraisers and courts must take into account not only the current use of the property, but also its HBU.[21] A property's HBU is the highest and most profitable use for which it is adaptable and needed, or likely to be needed, in the reasonably near future.[22] 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.[23] Importantly, valuation does not depend on whether the owner has actually put the property to its HBU.[24] The HBU can be *any* realistic potential use of the property.[25] Common HBUs are construction of a residential community, creation of a mixed-use development, and mining the property.

How Do Taxpayers Claim the Tax Deduction?

Properly claiming the tax deduction triggered by an easement donation is surprisingly complicated. It involves a significant amount of actions and documents. The main ones are as follows: The taxpayer must (1) obtain a "qualified appraisal" from a "qualified appraiser," (2) demonstrate that the easement-recipient is a "qualified organization," (3) obtain a Baseline Report describing the condition of the property at the time of the donation and the reasons why it is worthy of protection, (4) complete a Form 8283 (Noncash Charitable Contributions) and have it executed by all relevant parties, including the taxpayer, appraiser, and easement-recipient, (5) assuming that the taxpayer is a partnership, file a timely Form 1065, enclosing the Form 8283 and qualified appraisal, (6) receive from the easement-recipient a proper "contemporaneous written acknowledgement," both for the easement itself and for any endowment/stewardship fee donated to finance perpetual protection of the property, and (7) send all the partners their Schedule K-1 (Partner's Share of Income, Deductions, Credits, etc.) and a copy of the Form 8283.[26]

The new IRS Interim Guidance triggers a critical change, eliminating the multi-level review procedure formerly used by the IRS to protect appraisers against improper penalties and disciplinary referrals.

Categories of IRS Attacks Against Partnerships

The IRS has been advancing numerous arguments against partnerships that donate conservation easements, and the list continues to expand. The arguments can be divided into the following five categories.

Category #1—Common Technical Arguments

The ATG provides guidance to Revenue Agents and other IRS personnel who are conducting examinations of partnerships making easement donations.[27] It contains a "Conservation Easement Issue Identification Worksheet," which identifies a large number of technical challenges that the IRS might raise to challenge an easement-related tax deduction, including the following:

- The easement-recipient failed to give a proper "contemporaneous written acknowledgement" letter.
- The appraisal was not attached to the partnership's Form 1065.
- The appraisal was not prepared in accordance with the Uniform Standards of Professional Appraisal Practice ("USPAP").
- The appraisal fee was based on a percentage of the easement value.
- The appraisal was not timely, in that it was not sufficiently proximate to the making of the donation or the filing of the Form 1065.
- The appraisal was not a "qualified appraisal."
- The appraiser was not a "qualified appraiser."
- The Form 8283 was missing, incomplete, or inaccurate.
- The donor's cost or adjusted basis in the donated property, as listed on Form 8283, was improperly calculated.
- Not all appraisers who participated in the analysis signed Form 8283.
- The Baseline Report was insufficient in describing the condition of the property.
- The Baseline Report was not completed during the designated timeframe.
- Any mortgages or other encumbrances on the property were not satisfied or subordinated to the easement before the donation.
- The Deed of Conservation Easement contains an improper clause regarding how the proceeds from sale of the protected property upon extinguishment of the easement would be allocated among the donor and easement-recipient.
- The Deed of Conservation Easement contains an amendment clause, which, in theory, might allow the parties to modify the donation, after taking the tax deduction, in such a way as to

undermine the conservation purposes.

- The Deed of Conservation Easement contains a merger clause, as a result of which the fee simple title and the easement could end up in the hands of the same party, thereby undermining the ability to protect the property forever.
- The Deed of Conservation Easement was not timely filed with the proper court or other location.
- The easement-recipient was not a "qualified organization."
- The easement-recipient was not an "eligible donee."[28]

The list of attacks enumerated above is not comprehensive. Indeed, the ATG clarifies that the list is partial and encourages Revenue Agents to review additional sources for more inspiration, including Section 170, legislative history, tax regulations, Notice 2006-96, and evolving caselaw.[29]

Category #2—Besmirching the Conservation Purposes

Along with alleging that the partnership should get an easement-related deduction of $0 based on various "technical" arguments, the IRS often questions whether a particular property is worthy of being protected in the first place. For instance, the IRS frequently argues that the relevant property lacks acceptable "conservation purposes" for any number of reasons, including the habitat is not protected in a relatively natural state, there are insufficient threatened or endangered species on the property, the habitat or ecosystem to be protected is not "significant," the public lacks physical or visual access to the property, the conservation will not yield a significant public benefit, the property lacks historical significance, the conservation purposes do not comport with a clearly delineated government policy, the easement permits uses of the property that are inconsistent with the conservation purposes, the donor has certain "reserved rights" that interfere with or destroy the conservation purposes, etc.[30]

Category #3—Legal/Tax Doctrines

Cautious people generally have backup plans, and the IRS is no different when it comes to easement disputes. It tends to raise additional legal/tax arguments, in case the Tax Court is not buying its technical challenges or attacks on conservation purpose.

The IRS has been threatening to raise these types of arguments for a long time. The ATG, for example, has suggested for years that Revenue Agents assert that the easement donation lacked charitable intent because there was some form of quid pro quo between the partnership and the easement-recipient and/or that the partnership improperly conditioned the donation on getting the full tax deduction claimed on its Form 1065.[31]

When the IRS issued Notice 2017-10 labeling certain easement donations "listed transactions," it warned of its plan to attack easements based on the partnership anti-abuse rules, the economic substance doctrine, and other unspecified rules and doctrines.[32]

More recently, when the U.S. Department of Justice ("DOJ") filed a Complaint in District Court in December 2018 seeking an injunction against various parties in the easement arena, it alleged that the entities involved in easement donations are not true partnerships for federal tax purposes, they exist solely as conduits to "sell" tax deductions, they are "shams," and they "lack economic substance."[33]

The IRS has also showed its willingness to raise novel legal/tax positions in Tax Court litigation. Case in point, the IRS argued in a recent dispute that the partnership engaged in "disguised sales" of tax deductions, the allocation of the charitable donation deductions to the partners related to the easement did not have substantial economic effect, and each partner's deduction should be limited to the amount of his capital contribution to the partnership.[34]

Category #4—Calling Valuations Inflated

As explained above, valuing a conservation easement, which is a voluntary agreement by the partnership to permanently give up its right to develop and financially maximize certain property, is unique because of the need to consider the HBU. The ATG specifically recognizes the need to determine the HBU as part of the valuation process, as does the Tax Court.[35] One relatively obscure case, *Terrene Investments, Ltd.*, illustrates the power and effect of the buyer (but not the seller) understanding the true HBU when acquiring property.[36] The main facts from that case were as follows: Individual taxpayers bought 74 acres for $50,000. They immediately cut and sold the timber on the property for $45,000. They then contributed the property to a partnership, which, in turn, subdivided the property into three parcels. The partnership obtained a qualified appraisal indicating that the HBU of the property was mining. The partnership donated one parcel to a foundation

NOTES

[28] IRS, Conservation Easement Audit Techniques Guide. (Rev. 11/4/2016), pp. 78-81.

[29] IRS, Conservation Easement Audit Techniques Guide. (Rev. 11/4/2016), pp. 78-81.

[30] IRS, Conservation Easement Audit Techniques Guide. (Rev. 11/4/2016), pp. 78-81; *Champions Retreat Golf Founders, LLC*, TCM 2018-146 (holding that the existence of the rare plant on less than 17% of the total easement area is insufficient to fully satisfy the conservation purpose of protecting a significant relatively natural habitat); *Atkinson*, TCM 2015-236 (holding 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").

[31] IRS, Conservation Easement Audit Techniques Guide. (Rev. 11/4/2016), pp. 78-81.

[32] Notice 2017-10, section 1.

[33] *Nancy Zak, Claud Clark, EcoVest Capital Inc., Alan N. Solon, Robert M. McCullough, and Ralph R. Teal*, Case No. 1:18-cv-05774, D.C.N.D. Ga,, Complaint filed 12/18/2018, p. 47.

[34] *Champions Retreat Golf Founders, LLC*, TCM 2018-146.

[35] IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), p. 41; *Stanley Works & Subs.*, 87 TC 389, 400 (1986); *Esgar Corp.*, 744 F.3d 648, 659 n. 10 (CA-10, 2014); *Symington*, 87 TC 892, 896 (1986).

[36] TCM 2007-218.

[37] *Id.*

[38] REG-140029-07, Fed. Reg. Vol. 73, No. 153, 8/7/2008, Preamble, p. 45911 (emphasis added).

[39] *See, e.g., TOT Property Holdings, LLC*, Tax Court Bench Opinion, 12/13/2019 (focusing on the fact that the original landowner purchased the land for about $486,000, he later contributed the land for partnership interests that he quickly sold for about $1,050,000, and the relevant partnership donated an easement on the land

and claimed a deduction of $2.5 million based on the mining HBU, which the IRS did not challenge. The partnership later donated another parcel to a foundation and claimed a deduction of $2.7 million using the same mining HBU, which the Tax Court ultimately valued at $1.31 million. The Partnership retained the third parcel.[37] In summary, the taxpayers essentially paid $5,000 (*i.e.*, $50,000 minus the $45,000 made from timber sales) for property historically used for agriculture, recognized its hidden financial potential, and successfully claimed $3.81 million in charitable donation deductions thanks to the mining HBU.

The IRS, for its part, has told the public for years that appraisers working for taxpayers must contemplate the HBU in order to meet the applicable substantiation rules. The Preamble to the regulations about "qualified appraisals" states the following in this regard:

> [S]ome commentators requested a specific reference to [HBU] in the proposed regulations. This suggestion was not incorporated in the proposed regulations because USPAP Standards Rule 1-3(b) requires an appraiser to "develop an opinion of the [HBU] of the real estate" when it is "necessary for credible assignment results in developing a market value opinion." *An appraisal that does not include a development of [HBU] when required by USPAP is not consistent with the substances and principles of USPAP.*[38]

Despite express and repeated acknowledgment by the IRS and the Tax Court of the fundamental role of the HBU in calculating the value of an easement donation, the IRS has shifted course in recent years. Now, instead of focusing on the value of the property at the moment of the donation, assuming that it would be exploited to its fullest economic potential by the partnership were it not for the easement, the IRS centers on other figures of questionable relevance in the easement-valuation context. These often consist of (1) the value of the property for local property tax purposes, (2) the asking price of the property for an attempted, yet unsuccessful, sale close in time to the easement donation, (3) the amount that the partnership paid for the land, directly or indirectly, and/or (4) the total capital contributions made to the partnership by the individual investors, who ultimately received the tax benefits.[39]

This is consistent with the ATG, which explains that a final notice issued to taxpayers in the easement arena "will generally include a tiering of proposed penalties with multiple alternative positions."[41]

Some penalties can be avoided if the taxpayer can demonstrate that there was "reasonable cause" for the violation.[42] Others will not be asserted if the value was based on a qualified appraisal by a qualified appraiser and the taxpayer made a good faith investigation of the value of the property.[43] Still other penalties, like the one for making a gross valuation misstatement, cannot be overcome by evidence of "reasonable cause" or by any other justification or excuse. It is mathematical in nature; that is, if the value of the easement originally claimed by the partnership on Form 1065 and Form 8283 exceeds the value ultimately determined (by the IRS, Tax Court, or Court of Appeals) by a certain percentage, the gross valuation misstatement penalty applies, period.[44]

Properly claiming the tax deduction triggered by a conservation easement donation is surprisingly complicated.

Category #5—Penalties

Penalties in the easement arena are numerous, and they feature unique terminology, exceptions, and applications, as examined below.

Variety of common penalties. In addition to disallowing all or most of an easement-related deduction based on some combination of technical, conservation, legal/tax, and valuation issues, the IRS ordinarily proposes several penalties, ranging in severity. These include (1) negligence, (2) substantial understatement of income tax, (3) substantial valuation misstatement, (4) gross valuation misstatement, or (5) reportable transaction understatement.[40]

Focus on gross valuation misstatements. This article centers on gross valuation misstatements in the easement context, thereby necessitating additional background.

The IRS generally may impose a penalty equal to 40% of the tax underpayment in situations where such underpayment is attributable to a "gross valuation misstatement."[45] This exists if the value or adjusted basis of any property claimed on a tax return is 200% or more of the correct amount.[46]

As explained above, taxpayers cannot raise defenses when it comes to gross valuation misstatements.[47] The legislative history confirms that reasonableness is not a factor to consider: "[T]he reasonable cause exception . . . does not apply in the case of gross valuation misstatements."[48] The regulations, piling on, clarify that "[t]here is no disclosure exception" to the gross valuation mis-

NOTES

claiming a value of $6.9 million); *see also Oakhill Woods, LLC*, TCM 2020-24 (explaining that the original landowner bought the land for $2,491 per acre, the partnership valued land at $20,975 per acre when donated a few years later, and the partnership "took the position that the [land] had appreciated by more than 800% during the 3-1/2 years amid the worst real estate crisis since the Great Depression.")

[40] Section 6662; Section 6662A.

[41] IRS, Conservation Easement Audit Techniques Guide (Rev. 11/4/2016), p. 77.

[42] Section 6664(c)(1); Section 6664(d)(1); Reg. 1.6664-4.

[43] Section 6664(c)(3); Reg. 1.6664-4.

[44] Section 6664(c)(3); Reg. 1.6664-4.

[45] Section 6662(h)(1).

[46] Section 6662(h)(2)(A)(i); *see also Todd*, 862 F.2d 540 (CA-5, 1988) (citing U.S. Committee on Joint Taxation, General Explanation of the Economic Recovery Act of 1981, JCS-71-81, at p. 333) (explaining the meaning of "attributable to" in this context).

[47] Section 6664(c)(3).

[48] U.S. Joint Committee on Taxation, Technical Explanation of H.R. 4, The Pension Protection Act of 2006, as Passed by the House on July 28, 2006, and as Considered by the Senate on August 3, 2006. JCX-38-06 (8/3/2006), p. 311.

statement either.[49] In other words, the partnership cannot avoid the penalty, despite the fact that it repeatedly and openly disclosed all relevant information to the IRS on the Form 1065, Form 8283, Form 8886, qualified appraisal, Schedule K-1, and, likely, Form 8918. The Preamble to the regulations puts it most bluntly in response to requests by practitioners to allow a limited exception to valuation penalties:

> Congress did not, by statute or legislative history, provide a disclosure exception from the valuation misstatement penalty and, accordingly, there is no basis for applying such an exception under the regulations. Moreover, the courts have consistently applied the penalty without regard to whether the valuation misstatements were based on legal or factual errors. Accordingly, the final regulations continue to provide that there is no disclosure exception to the valuation misstatement penalty.[50]

One more point is critical because, as highlighted earlier in this article, the primary position by the IRS in easement disputes is that the deduction should be $0. Thus, a gross valuation penalty will always be triggered, at least initially. The regulations make this clear: "The value or adjusted basis claimed on a return for any property with a correct value or adjusted basis of zero is considered to be 400 percent or more of the correct amount. There is a gross valuation misstatement with respect to such property, therefore, and the applicable penalty rate is 40 percent."[51] Certain commentators complained that this rule was "too harsh," but the IRS ignored this criticism on grounds that "this approach is consistent with the principle inherent in the statute that relatively greater misstatements are subject to penalty at a higher rate, as well as with the statutory language."[52]

New IRS Attacks on Appraisers

Congress and the IRS have gradually been taking steps that make it easier for the IRS to attack appraisers. This causes general concern, but what is most worrisome is that virtually nobody seemed to notice, or appreciate the consequences of, the actions taken by the IRS in January 2020. The evolution of the most pertinent events is chronicled below.

Section 170

Section 170(a)(1) provides that a deduction for making a charitable donation will be allowed "only if verified under the regulations" issued by the IRS. The core problem was that the IRS did not issue any regulations for many years. This absence of guidance, predictably, led to supposed abuses by taxpayers. The IRS expressed concern to Congress that donated property was being overvalued, taxpayers were content playing the "audit lottery," and widespread publicity about non-compliance by donors and lax enforcement by the IRS was causing other taxpayers to disrespect the law.[53]

Congressional Mandate in 1984

Congress took action to strengthen substantiation requirements and curtail overvaluations. Instead of adhering to the traditional legislative course of adding new tax provisions or modifying existing ones, Congress used a novel approach in the Deficit Reduction Act of 1984 ("DRA").[54] It simply referenced Section 170(a)(1), pointed out that the existing statutory language contemplated the IRS issuing regulations, and instructed the IRS to do so by 12/31/1984, focusing on the concepts of qualified appraisers, qualified appraisals, and appraisal summaries.[55]

Congress, as part of the DRA, also expanded the rules that govern the behavior of tax professionals, commonly known as Circular 230, such that the Office of Professional Responsibility ("OPR") or its predecessor could punish not only misbehaving accountants and attorneys, but also appraisers who violated Section 6701 by aiding and abetting taxpayers in filing returns showing tax understatements.[56] Below is the legislative history making it clear that, while Congress generally wanted OPR to have authority to regulate appraisers, it insisted that punishment was inappropriate, unless (1) the appraiser knew that his appraisal would be used in connection with an income tax return, (2) the appraiser knew the valuation was overstated, and (3) the appraiser thus knew that the appraisal would result in a tax understatement.

> Congress believes that professional appraisers who seek to present evidence to the [IRS] should be subject to the same type of professional regulation that applies to attorneys and accountants practicing before the [IRS] and to attorneys appearing in court proceedings.[57]
>
> The Secretary of the Treasury is authorized to bar from appearing before the [IRS] or Treasury Department, for the purpose of offering opinion evidence on the value of property or other assets, any individual against whom a civil penalty for aiding and abetting the understatement of tax (Section 6701) has been assessed. Thus, an appraiser

NOTES

49 Reg. 1.6662-5(a).

50 TD 8381, 12/30/1991, Preamble.

51 Reg. 1.6662-5(g).

52 TD 8381, 12/30/1991, Preamble.

53 U.S. Joint Committee on Taxation, General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984. JCS-41-84 (12/31/1984), pp. 503-504.

54 P. L. 98-369, 7/18/1984.

55 P.L. 98-369, 7/18/1984, section 155(a); House Conference Report 98-861, 98th Cong., 2d Session (6/23/1984).

56 P. L. 98-369, 7/18/1984, section 155(c).

57 U.S. Joint Committee on Taxation, General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984. JCS-41-84 (12/31/1984), pp. 511-512.

58 U.S. Joint Committee on Taxation, General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984. JCS-41-84 (12/31/1984), p. 507.

59 TD 8003 (12/31/1984). The regulations were later finalized in TD 8199 (5/5/1988).

60 TD 8003 (12/31/1984); Temp. Reg. 1.170A-13T(c)(5)(i)(D).

61 P.L. 108-357, 10/22/2004; section 883; House Conference Report 108-755, 108th Cong., 2d. Sess., (10/7/2004), pp. 745-747.

62 P.L. 108-357, 10/22/2004; section 883; House Conference Report 108-755, 108th Cong., 2d. Sess., (10/7/2004), pp. 745-747.

63 Section 6695A(a).

64 Section 6695A(b).

65 Section 6695A(c).

66 Section 6696(a).

67 Section 6696(d)(1).

68 Section 6696(b).

69 Section 6696(c).

> who aids or abets in the preparation or presentation of an appraisal in connection with the tax laws will be subject to disciplinary action if the appraiser knows that the appraisal will be used in connection with the tax laws and will result in an understatement of the tax liability of another person. The Secretary is also given authority to provide that the appraisals of an appraiser who has been disciplined have no probative effect in any administrative proceeding before the Department of the Treasury or the [IRS].
>
> Also, to be qualified, the appraisal must state that it is being prepared for income tax purposes, and must be signed by the appraiser, whose tax identification number must be listed. Accordingly, if the appraiser prepared such an appraisal (or appraisal summary) knowing that the appraisal overvalued the property (and hence, if used, would result in an understatement of the donor's tax liability), such appraiser would be subject to the civil tax penalty for aiding and abetting an understatement of tax liability (Sec. 6701).[58]

The IRS issued temporary regulations on 12/31/1984, as required by Congress in the DRA.[59] Among other things, the regulations stated that, in order to meet the definition of qualified appraiser, the person had to execute a declaration on the appraisal summary that he understood that "a false or fraudulent overstatement of the value of the property described in the qualified appraisal or appraisal summary may be subject to a civil penalty under Section 6701 for aiding and abetting an understatement of tax liability, and consequently the appraiser may have appraisals disregarded [pursuant to Circular 230]."[60]

Legislation in 2004

In 2004, Congress enacted the American Jobs Creation Act, which created new Section 170(f)(11). This provision essentially codified the earlier regulations issued by the IRS pursuant to the DRA regarding qualified appraisers, qualified appraisals, appraisal summaries, etc.[61] Congress also empowered the IRS to issue new or additional regulations, as necessary, to carry out the purposes of Section 170(f)(11).[62]

Legislation in 2006

Congress then passed the Pension Protection Act ("PPA") in 2006. This legislation did two important things when it comes to appraisers; namely, it created a new appraiser penalty under Section 6695A, and it eliminated the need for the IRS to first assess an aiding and abetting penalty against an appraiser under Section 6701 before referring him to OPR for potential disciplinary action. These two major changes are examined below.

Introduction of new Section 6695A penalty. The PPA generated a new appraiser penalty under Section 6695A. Section 6695A provides that the IRS can assess a penalty if a person prepares a property appraisal, he knows or should have known that the appraisal would be used in connection with a return or claim for refund, and the appraisal value results in one of several things, including a "gross valuation misstatement" by a partnership making an easement donation.[63]

The penalty under Section 6695A generally is the smaller of the following two items: (1) 10% of the amount of the tax underpayment, or $1,000, whichever amount is larger, or (2) 125% of the gross income received by the person who prepared the appraisal.[64] The IRS will not assess the penalty, though, in situations where the appraiser can establish, to the satisfaction of the IRS, that the value in the original appraisal (*i.e.*, before the appraisal was challenged by the IRS and before the value was ultimately determined by the courts) was "more likely than not" the correct value.[65]

Section 6695A entails some unique procedural aspects. For instance, the penalty does not supersede any other applicable penalties against an appraiser; rather, the IRS assesses it "in addition to any other penalties provided by law."[66] Moreover, the IRS generally has three years from the time that the taxpayer filed the relevant tax return or Claim for Refund based on appraisal to assess the penalty.[67] Finally, the normal deficiency procedures related to income and other taxes do *not* apply to these appraiser penalties, meaning that once the IRS assesses them, it immediately starts taking collection actions.[68]

This means that the main options available to penalized appraisers are limited to two. They could pay the entire penalty up front, file a Claim for Refund, and then lodge a Suit for Refund in federal court, if the IRS either issues a Notice of Disallowance or ignores the Claim for Refund for more than six months. The alternative would be to wait for the IRS to send a "final" lien or levy notice, request and participate in a collection due process ("CDP") hearing with a Settlement Officer, and, if the IRS issues an unfavorable Notice of Determination, file a Petition with the Tax Court claiming that the Settlement Officer abused his administrative discretion.[69] Both options tend to be slow, uncertain, and expensive.

The IRS has been advancing numerous arguments against partnerships that donate conservation easements, and the list continues to expand.

Elimination of precursor to OPR referrals. The legislative history to the PPA indicates that Congress authorized the IRS to go straight to OPR; that is, it no longer needed to first conduct an examination of the appraiser, prove intent of wrongdoing, and assess an aiding and abetting penalty under Section 6701. In explaining the law in effect *before* the PPA, the legislative history confirms the existence of the prior multi-level review system:

> The [Treasury Department] also is authorized to bar from appearing before the [Treasury] Department, for the purpose of offering opinion evidence on the value of property or other assets, any individual against whom a civil penalty [under Section

6701] for aiding and abetting the understatement of tax has been assessed.[70]

This is consistent with the language of Circular 230 *before* the PPA, which contained the following limitation:

> Whenever the Director of Practice is advised or becomes aware that a penalty has been assessed against an appraiser under Section 6701(a) of the Internal Revenue Code, the Director of Practice may reprimand the appraiser or . . . institute a proceeding for disqualification of the appraiser.[71]

Contrast the preceding language to the portion of the legislative history, quoted below, which describes the new state of the law *after* enactment of the PPA:

> *The provision eliminates the requirement that the [IRS] assess against an appraiser the civil penalty [under Section 6701] for aiding and abetting the understatement of tax before such appraiser may be subject to disciplinary action.* Thus, the [IRS] is authorized to discipline appraisers after notice and hearing. Disciplinary action may include, but is not limited to, suspending or barring an appraiser from: preparing or presenting appraisals on the value of property or other assets before the [Treasury] Department or the IRS; appearing before the [Treasury] Department or the IRS for the purpose of offering opinion evidence on the value of property or other assets; and providing that the appraisals of an appraiser who has been disciplined have no probative effect in any administrative proceeding [e.g., audit or conference with the Appeals Office] before the [Treasury] Department or the IRS.[72]

Initial concerns about effects of PPA. Practitioners quickly identified several concerns with the rules created by, and appraiser protections abolished by, the PPA.[73] First, the IRS promised to issue regulations clarifying Section 6695A issues more than a decade ago, but has yet to do so, leaving taxpayers in the dark about certain key issues.[74]

Second, practitioners were skeptical whether the more-likely-than-not exception to the Section 6695A penalty has any true functionality, pondering how the IRS or a court would accept the notion that the original appraisal was more-likely-than-not correct, when the ultimate value was so far off as to trigger a gross valuation misstatement.

Third, questions arose regarding the standard that the IRS would use for making disciplinary referrals to OPR, emphasizing that Congress might have gone too far:

> The PPA may have tipped the balance between preventing abuse and discouraging [charitable] giving by eliminating the requirement that the [IRS] assess the civil penalty [under Section 6701] for aiding and abetting an understatement of tax before an appraiser may be suspended or barred from preparing or presenting appraisals for tax purposes. [Section 6695A] is somewhat worrisome, for without the prerequisite finding of willful misevaluation, it is unclear what standard will be used to make disciplinary decisions. Although enforcement of penalties against appraisers who knowingly exaggerate the value of donated assets is widely supported (even by appraisers), appraisers now risk losing the ability to practice their trade for making honest mistakes when appraising unique or otherwise hard-to-value assets.[75]

Fourth, commentators suggested that the threat of potential Section 6695A penalties, coupled with the IRS's broad authority to place appraisers in the crosshairs of OPR, could lead appraisers to understate (as opposed to overstate) property values: "An unfortunate aspect of the new provision is that appraisers may feel coerced to 'back off' during an audit in order to avoid the penalty—even if they sincerely believe that their appraisal accurately reflects value."[76]

Finally, and perhaps most importantly, anxieties increased because of the power, held jointly by the IRS and OPR, to ruin an appraiser's career with diminished procedural protections. The following comments capture the general sentiment:

> There is another hammer given in the [PPA] to the Treasury with which to bludgeon appraisers: the threat of blacklisting. Section 10.50(b) of the Circular permits the Treasury, in essence, to blacklist appraisers – that is, to rule that the appraiser is barred from presenting evidence or testimony in any administrative proceeding before the Treasury or the IRS and that any appraisal made by that appraiser after the effective date of disqualification will not have any probative effect in any administrative proceeding before the Treasury or the IRS. However, before the [PPA], the Treasury could blacklist only if the

NOTES

[70] U.S. Committee on Joint Taxation, "Technical Explanation of H.R. 4, the Pension Protection Act of 2006, as Passed by the House on July 28, 2006, and as Considered by the Senate on August 3, 2006." JCX-38-06 (8/3/2006), p. 310.

[71] Treasury Department, Circular No. 230 (Rev. 6-2005), 31 CFR 10.60(b).

[72] U.S. Committee on Joint Taxation, "Technical Explanation of H.R. 4, the Pension Protection Act of 2006, as Passed by the House on July 28, 2006, and as Considered by the Senate on August 3, 2006." JCX-38-06 (8/3/2006), p. 311 (emphasis added).

[73] *See, e.g.*, Meade and Chiang, "Recent Judicial Guidance on Valuing Conservation Easements," 21(5) Taxation of Exempts, March/April 2010; McDowell, "Charitable Contributions of Real Estate Interests," 35(1) Journal of Real Estate Taxation (2007); Dahlin and Pederson, "The Pension Protection Act Encourages Charitable Giving with Some Caveats," 34(2) Journal of Real Estate Taxation (2007); Hall, "Grim Tale of Aggressive IRS Enforcement," 16(5) Valuation Strategies, May/June 2013.

[74] IRSIG SBSE-04-0809-105 (8/18/2009).

[75] Madrigal, "Charitable Giving Incentives and Reforms in the Pension Protection Act," 18(4) Taxation of Exempt (Jan/Feb. 2007).

[76] Zeydel et al., "What Estate Planners Need to Know about the New Pension Protection Act," 105 JTAX 199 (Oct. 2006).

[77] Blattmachr et al., Circular 230 Deskbook, Practising Law Institute, 2006, pp. 2-28 and 2-29.

[78] Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001. The Interim Guidance is scheduled to become part of the Internal Revenue Manual within the next two years.

[79] Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.

[80] IRM 20.1.12.7 (12/18/2017).

[81] IRM 20.1.12.7 (12/18/2017); IRM 20.1.12.7.2 (12/18/2017).

[82] IRM 20.1.12.7 (12/18/2017); IRM 20.1.12.7.2 (12/18/2017).

[83] IRM 20.1.12.7 (12/18/2017); IRM 20.1.12.7.2 (12/18/2017).

[84] IRM 20.1.12.7.4 (12/18/2017).

[85] IRM 20.1.12.7.4 (12/18/2017).

[86] IRM 20.1.12.7.4 (12/18/2017).

[87] IRM 20.1.12.7.4 (12/18/2017).

[88] Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001 (emphasis added).

[89] Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.

> penalty under Section 6701 of the Code had been imposed on the appraiser. [Section 6701] permits the penalty to be imposed only if, among other conditions, the appraiser knew the appraisal would result in an underpayment of tax. The [PPA] eliminates the requirement of a Section 6701 penalty. It seems that being subjected to the new appraiser penalty under Section 6695A might serve as a basis for blacklisting.[77]

New Internal IRS Procedures Issued in January 2020

Perhaps one of the most important changes in recent years with respect to appraisers occurred in late January 2020, and almost nobody took notice. This might have been the intention of the IRS, when it quietly released the Interim Guidance, which, at first glance, seems to be just another tedious procedural memo.[78] However, this Interim Guidance, directed to "all employees" in the Large Business & Internal Division and in the Small Business/Self-Employed Division, deprives appraisers of crucial procedural safeguards.[79] Because appraisals are pivotal in conservation easement cases, the Interim Guidance acquires major importance in this context.

Appreciating the changes triggered by the Interim Guidance requires an understanding of the prior rules. A comparison between old and new is set forth below.

Procedures before the Interim Guidance. The portion of the IRM called "Referrals and Penalty Case Review Procedures" has historically contained a multi-level review process designed to ensure that a particular degree of wrongdoing by the appraiser had occurred before assessing penalties, making referrals to OPR, etc.[80] The IRM featured the unique procedures and terminology described in the following paragraphs.

An Examining Appraiser (*i.e.*, an IRS Appraiser, Engineer, or Valuation Specialist) generally would recommend a Section 6695A penalty to the Revenue Agent, if the valuation reached the level of a gross valuation misstatement.[81] To support this recommendation, the Examining Appraiser prepared a memorandum, for internal use only, including an explanation as to why the appraiser was incorrect and why he knew or should have known better.[82] Next, a so-called Penalty Review Team would review the recommendation and opine *before* the IRS could assess a Section 6695A penalty. The Penalty Review Team was comprised of "experienced" IRS Appraisers and Valuation Specialists, along with one or more Review Managers.[83]

The process historically used by the Penalty Review Team was as follows. The Review Manager assigned the case to a Primary Review Appraiser, who studied the original appraisal, reviewed the memorandum prepared by the Examining Appraiser in support of a Section 6695A penalty, determined if the penalty case should proceed, and reported this decision to the Review Manager.[84]

If the Primary Review Appraiser recommended continuing the penalty case, he assisted the Revenue Agent in preparing an Information Document Request ("IDR") for the taxpayer's appraiser, requesting his grounds for meeting the more-likely-than-not exception to penalties. Next, the Revenue Agent and Primary Review Appraiser met with the taxpayer's appraiser, in person or by phone, to allow him the chance to discuss his responses to the IDR. If the Primary Review Appraiser concluded the penalties were appropriate after the interview, he prepared a memorandum for the Revenue Agent explaining why the exception was inapplicable. The Primary Review Appraiser would then forward the entire case file to the Review Manager.[85]

Continuing the belt-and-multiple-suspenders approach, if the Primary Review Appraiser wanted to assess the Section 6695A penalty, the Revenue Manager assigned a Secondary Review Appraiser. His role consisted of reviewing the entire file, including the memorandum drafted by the Primary Review Appraiser, preparing his own written analysis and opinion about the applicability of the penalty, and returning the case file, as augmented, to the Review Manager.[86]

Finally (after obtaining and reviewing opinions about the Section 6695A penalty by the Revenue Agent, Examining Appraiser, Primary Review Appraiser, and Secondary Review Appraiser), the Review Manager prepared the "final concurrence" and forwarded the materials for inclusion in the appraiser's workfile.

In addition to disallowing all or most of an easement-related deduction based on some combination of issues, the IRS ordinarily proposes several penalties, ranging in severity.

Following the former process from start to finish, the IRS would not assess Section 6695A penalties against an appraiser until the matter had been considered by at least five separate, experienced IRS employees.[87]

Procedures after the Interim Guidance. The Interim Guidance might have gone unnoticed initially, but its purpose is evident:

> This memorandum issues guidance *eliminating the multi-tiered review process for IRC 6695A appraiser penalty cases* and establishing a process for Examining Appraisers to notify the [Revenue Agent] of a potential IRC 6695A penalty case.[88]

Under the new Interim Guidance, if an Examining Appraiser determines a gross valuation misstatement while, say, auditing a conservation easement donation, he simply needs to get written approval from his immediate supervisor (with an e-mail sufficing) and then notify the Revenue Agent that the Section 6695A penalty might apply.[89] Moreover, the Interim Guidance says that, while the decision to open a Section 6695A penalty case normally is based on the recommendation of an Examining Appraiser, Revenue Agents "should open" a penalty case "whenever they determine penalty

consideration is warranted."[90] The Interim Guidance goes on to explain that a Revenue Agent is only required to seek assistance, through the so-called Specialist Referral System, in situations where the Revenue Agent believes that he needs help from an Examining Appraiser.[91] Finally, the Interim Guidance expressly states that the Revenue Agent is solely responsible for assessing the Section 6695A penalty based on information obtained during the examination, preparing the related Form 886-A (Explanation of Items), and closing the penalty case.[92]

Exploring Impacts of the Interim Guidance

The prior procedures required analysis and agreement by at least five experienced IRS employees (*i.e.*, the Revenue Agent, Examining Appraiser, Primary Review Appraiser, Secondary Review Appraiser, and Review Manager) before Section 6695A penalties would be assessed. By comparison, the Interim Guidance contemplates the Revenue Agent, who likely has no training or education whatsoever in the field of valuation, making this decision alone, or at most with input from just one Examining Appraiser.

This expanded level of autonomy granted to Revenue Agents by the Interim Guidance becomes more disturbing after consulting related portions of the IRM. For instance, the IRM instructs Revenue Agents to assess Section 6695A penalties quickly, *before* conducting a detailed review, in situations where an appraiser refuses to voluntarily sign a Form 872-AP (Consent to Extend the Time on Assessment of IRC Section 6695A Penalty).[93] In this regard, the IRM states that the IRS ordinarily should not assess a Section 6695A penalty against an appraiser until the related audit of the taxpayer has been completed, but tells Revenue Agents to make a "protective assessment" if the assessment period is within 180 days of expiring.[94]

The IRM also explains that "[i]f the claimed value of the property on the return or claim for refund, which is based on an appraisal, results in a . . . gross valuation misstatement, with respect to such property, the [Revenue Agent] should open an IRC 6695A penalty case."[95]

The IRM further instructs Revenue Agents to "exercise discretion" when referring an appraiser to OPR based on assessment of a Section 6695A penalty, but encourages referrals when there is a "pattern of conduct."[96] The IRM adds to this point, explaining that an OPR referral is "mandatory" when violations by an appraiser are "willful."[97]

The Treasury Department, through OPR, generally regulates the practice of taxpayer representatives before the IRS.[98] As part of this power, after notice and opportunity for a proceeding, OPR may suspend, disbar, or censure any representative who is incompetent or disreputable, or who violates the pertinent regulations.[99] Moreover, when it comes to appraisers, OPR may provide that their appraisals shall have no probative effect in any administrative proceeding, and may also bar appraisers from presenting evidence or testimony in any such proceeding.[100] The ban applies, "regardless of whether the evidence or testimony would pertain to an appraisal made prior to or after the effective date of disqualification."[101]

Appraisers of easements have been sanctioned under these rules in the past. For instance, a group of appraisers who valued facade easements entered into a settlement agreement with OPR after admitting, presumably under considerable pressure and threat of larger sanctions, that they had violated Circular 230 when they failed to exercise due diligence "in preparing or assisting in the preparation of, approving, and filing tax returns, documents, affidavits, and other papers related to [IRS] matters" and "in determining the correctness of oral or written representations made by the practitioner" to the IRS.[102]

More recently, in the DOJ action started in December 2018 seeking a permanent injunction against various players in the easement arena, one of the principal allegations is that the behavior of the appraiser warranted penalties under Section 6695A.[103] In addition, a federal court upheld an injunction against an individual who prepared thousands of valuations of timeshares donated to a particular charity, nearly half of which contained gross valuation misstatements under Section 6695A.[104]

Moreover, when the IRS announced in Notice 2017-10 that certain easement donations would be treated as "listed transactions," it stated that, along with penalizing "participants" and "material advisors," the IRS planned to sanction appraisers for valuation misstatements under Section 6695A.[105] Consistent with Notice 2017-10, the IRS Commissioner sent updated information and statistics about conservation easements to Congress in February 2020. He explained, among other things, that the IRS is currently auditing or investigating promoters, return preparers, land trusts, appraisers, and others, as well as "evaluating numerous referrals of practitioners to [OPR]."[106]

Conclusion

Congress made it clear in 1984 that referring appraisers to OPR for potential

NOTES

90 Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.

91 Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.

92 Tax Notes Doc. 2020-3440 (1/22/2020), consisting of LB&I-20-0120-001.

93 IRM 20.1.12.3 (12/18/2017).

94 IRM 20.1.12.3 (12/18/2017).

95 IRM 20.1.12.3 (12/18/2017).

96 IRM 20.1.12.7(1) (12/18/2017).

97 IRM 20.1.12.7(1) (12/18/2017).

98 31 U.S.C. section 330(a)(1).

99 31 U.S.C. section 330(c).

100 31 U.S.C. section 330(d)

101 31 CFR 10.50(b)(1).

102 31 CFR 10.22(a); IRS News Release, IR-2014-31, "IRS Bars Appraisers from Valuing Facade Easements for Federal Tax Purposes for Five Years," 3/19/2014.

103 *Zak et al*, Civil Action No. 1:18-cv-05774-AT, D.C.N.D. Ga., Complaint, 12/18/2018, Count II, paragraphs 189 through 200.

104 *Tarpey*, 119 AFTR2d 2017-1320 (D. Montana, 2017).

105 Notice 2017-10, 2017-4 IRB 544 (12/23/2016), section 3.

106 "Land Trust Alliance Calls for Action on Conservation Easements," 2020 Tax Notes Today Federal 38-9, Doc. 2020-7149 (2/25/2020); Parillo, "No Notable Decrease in Syndicated Easement Deals," 2020 Tax Notes Today Federal 39-1, Doc. 2020-7321 (2/27/2020).

disciplinary actions could not occur, unless the IRS first managed to prove that an appraiser intentionally overvalued property and thus was subject to penalties under Section 6701 for aiding and abetting tax understatements. Approximately 20 years later, upon enacting the PPA in 2006, Congress removed this precondition. Most recently, in January 2020, the IRS quietly issued the Interim Guidance, which eliminates the multi-level administrative review process that prevented assessment of improper Section 6695A penalties.

Revocation of procedural protections is always troublesome, but it acquires additional significance in the easement context, where the IRS (1) operates a "compliance campaign" to audit every "syndicated" easement, (2) concludes in virtually every case (regardless of the amount of due diligence conducted, the strength of appraisals offered by taxpayers, the quality and economic potential of the property donated, etc.) that the easement-related deduction should be $0, (3) argues that the donations are based on gross valuation misstatements, and (4) instructs Revenue Agents to evaluate appraisal issues while conducting the income tax audit. Taxpayers need to be aware of the Interim Guidance and its potential effects on partnerships and appraisers when engaging in disputes with the IRS. ●