NATIONAL TAXPAYERS UNION

Issue Brief

JULY 30, 2019
BY BRYAN HICKMAN

Environmental Tax Deduction At Risk Due to Overzealous IRS

Introduction

For more than a half century, the U.S. Tax Code has provided incentives to encourage private conservation, the most prominent being the deduction for conservation easements under Section 170(h).[1] This provision furnishes a charitable tax deduction for taxpayers who place easements on their property for conservation purposes and then donate the easements to qualified conservation organizations.

Officially codified in 1980 and renewed and updated on several occasions, the deduction for conservation easements has enjoyed broad bipartisan support, even as the divide between Republicans and Democrats on broader tax policy has widened considerably. From the outset, it was intended to promote private stewardship of conservation lands to spare taxpayers the costs of government-run land preservation efforts. And, by any objective measure, the deduction has been a success.

Key Facts:

The conservation easement deduction has been a huge success for the cause of environmental conservation.

The IRS has waged a war on those who claim conservation easement deductions in direct conflict with how Congress has passed and promoted the deduction.

Congress has an obligation to direct the IRS to administer the conservation easement deduction fairly and as intended.

[1] 26 U.S.C. §170(h)

Recently, concern has arisen about conservation easements claimed by partnerships (and LLCs, S-corporations) with the benefits of the deduction spread out among the multiple partners. These arrangements are typically referred to as conservation partnerships, but disparagingly referred to as "syndicated easements." In December 2016, in the waning days of the Obama Administration, the IRS issued Notice 2017-10 in response to concerns about conservation partnerships that "purport to give investors the opportunity to obtain charitable contributions deductions in amounts that significantly exceed the amount invested."[2] Specifically, the Notice designated some of these partnerships – those nefariously referred to as "syndicated" conservation partnerships – as "listed transactions," triggering a host of additional filing requirements and subjecting landowners and claimants to stiffer fines and penalties for noncompliance.

As written and enforced, Notice 2017-10 threatens the ongoing effort to promote private conservation and poses a real danger to taxpayer rights. By focusing on a specific class of taxpayer, i.e. conservation partnerships, the notice fails to address the underlying concern of valuation or qualification of conservation easement donations. It also imposes significant burdens on taxpayers without a tangible benefit to the IRS enforcement efforts while undermining the Congress's intent behind the conservation easement deduction. This paper will address these concerns, propose more reasonable alternatives, and provide additional evidence of the benefits of private conservation.

Ideology Over Sound Public Policy

The problems surrounding Notice 2017-10 start at the most basic level: it doesn't address the issues its authors, at least ostensibly, intended to solve. Once again, the notice marks deductions claimed by "syndicated" conservation partnerships as "listed transactions," subjecting them to more burdensome disclosure and filing requirements, which are discussed below in more detail. The added obligations apply to any participant in an easement partnership since 2010 that resulted in a deduction greater than 2.5 times the amount originally invested in the partnership.[3] In other words, the IRS has determined that deductions of certain amounts claimed by certain classes of taxpayers – participants in conservation partnerships – are inherently suspect and in need of greater restriction.

Efforts by some lawmakers have mirrored the IRS approach. In the past two Congresses, senators and representatives have introduced legislation that would, for a time, cap the easement deduction for a participant in a conservation partnership at 2.5 times their initial investment.[4] As with Notice 2017-10, the authors' stated purpose behind these bills is to prevent abuses that occur when partnerships claim overvalued deductions and reap undue tax benefits. And, just like the IRS's efforts, this approach focuses on the class of taxpayers making the claim and the size of their benefit and ignores the real problems that result in improper deductions.

These distinctions are based less on sound policy and more on the ideologically driven perception that the deduction has been claimed by the wrong people who, in the eyes of the IRS, have "profited" too much. It is true that conservation partnerships allow people who would not otherwise have the means or opportunity to benefit from the conservation easement deduction. However, this is a feature, not a bug, of this type of arrangement. Ultimately, one of the key benefits of Section 170 (h) is that it diversifies and expands opportunities for conservation beyond the most affluent taxpayers. If they are properly arranged and executed, conservation partnerships align quite closely with Congress's obvious intent behind the statute.

[2] Internal Revenue Service. (2016.) "Listing Notice--Syndicated Conservation Easement Transactions" (2017-10).
[3] *Ibid*.
[4] Charitable Conservation Easement Program Integrity Act of 2019, S.170, 116th Cong. (2019).

Those, like the IRS, seeking to restrict the use of conservation easement deductions – and those who openly or implicitly oppose such deductions outright – usually focus their arguments on issues surrounding valuation and qualification. Both are legitimate concerns, and neither of them are addressed by Notice 2017-10.

Valuations are a key issue because the amount of any conservation easement deduction is determined by the appraised value of what was donated. Section 170(h) allows taxpayers to deduct the difference between the "highest and best use" valuation of the conserved land – e.g., the value of the land if they chose to develop it – and the land's value once it's encumbered by the easement. Essentially, it's a deduction for the land value the taxpayer forfeits as a result of the easement. If a taxpayer receives an appraisal that over-values the property, this can improperly inflate the size of their deduction.

Easement qualifications are also a vital concern. Congress has stipulated that, in order to qualify for the deduction, an easement must be donated "exclusively for conservation purposes," which include the preservation of land for things like outdoor recreation, habitat protection, open space, and historically important locations or structures.[5] The IRS has scrutinized and litigated most of these requirements at one point or another, sometimes with unwarranted zeal. Proper enforcement of easement qualifications is surely necessary to preserve congressional intent and ensure the tax benefits apply to appropriate conservation endeavors. But in tax enforcement, there is a fine line between proper and excessive.

With respect to these key factors, "syndicated" conservation partnerships are no different from typical conservation easement arrangements. The appraisal standards and requirements are the same, as are the rules determining which donations qualify for the deduction. Notice 2017-10 doesn't change any of these rules or impose any new standards, it simply makes it more onerous for a designated class of taxpayers to claim the deduction.

Additionally, while the IRS may be suspicious of these types of charitable contributions that appear to be motivated by and result in substantial returns on taxpayer investments, conservation easements aren't wholly unique in that regard. Indeed, at the right time and place, any type of appreciable property, if donated to charity, can render a considerable tax benefit for the donors. For example, if a taxpayer bought shares of Apple in 2008 and then donated them in 2018, the value of the potential deduction would be 14 times larger than the taxpayer's initial investment. Last year, a painting displayed in the Chicago Convention Center fetched a price at auction that was 900 times higher than the purchase price in 1997.[6] Hypothetically, if a small handful of millionaires jointly purchased the painting in 1997, donating the painting to charity in 2018 would offset all their tax liabilities for several years.

These types of exponential returns aren't commonplace with property donations, and certainly not with conservation easements. The point is donations of property subject to appreciation – whether it's a conservation easement, stock in a corporation, or a piece of art – can increase and decrease in value over time. The policy goal behind deductions for charitable contributions is to encourage taxpayers to make donations. With Section 170(h) the goal is more specific: to encourage taxpayers to choose conservation over other land uses and to do so by donating appreciated property. Once again, if the IRS's intent is to prevent abuse – and not to undermine Congress's intent – focusing enforcement efforts on the type of donor or the size of the return, is, at best, inefficient. Alternatively, if observers and critics – including those at the IRS – believe for some reason the incentives provided by Section 170(h) are just too strong and the subsequent returns are just too big, Congress is the proper venue for making those kinds of recalibrations, with a legislative process that allows taxpayers' voices to be heard.

[5] 26 U.S. Code § 170(h).

[6] Deb, Sopan. "Painting That Hung in a Chicago Convention Center Brings Unexpected Windfall." *The New York Times*, May 17, 2018.

Put simply, the Notice is the wrong tool for preventing improper conservation easement deductions. If the IRS is serious about addressing over-valued easement deductions or easements created for improper conservation purposes under Section 170(h), there are several more effective alternatives, including many that have worked in the past. For example, the IRS could release more "Job Aids" to facilitate a better dialogue between government administrators and practitioners in the private sector. This wouldn't be official guidance, but an ongoing interaction between the IRS, its own employees, and outside stakeholders to discuss key technical matters in a structured forum. In Gift and Estate Tax Valuation Insights, Weston Kirk wrote that for other complicated areas of the tax code, Job Aids can "provide clarity and understanding of the Service's stance without creating significant disputes between taxpayers, their advisers, and the Service's agents, saving the Service time and taxpayer money in attempting to pass and then properly enforce its regulations."[7] The same recommendation could easily apply to the processing of conservation easements and would more effectively address overvaluation and bad appraisals without the antagonism we see under the current approach.

Furthermore, the IRS could convene – or with congressional direction establish – an easement advisory panel, whose experts from the public and private sectors could mediate and clarify disputes regarding easement donation valuations for tax purposes. A similar advisory panel was established and had some success in addressing issues surrounding art donations. Senators Christopher Murphy and Richard Blumenthal, who first raised the concept of an easement advisory body with then-IRS Commissioner John Koskinen, noted that the Art Advisory Panel resolved more than 95 percent of disputed cases brought before it, "without an audit process that is lengthy and expensive for the Service, taxpayer, and donor."[8]

The IRS could also update and clarify its regulations on appraisals. Or, it could develop new rules specific to appraising conservation easements to ensure a more professional and transparent appraisal process that requires both taxpayers and the IRS to adhere more closely to the Uniform Standards of Professional Appraisal Practice.

On the qualification side, the IRS could update its regulations for "qualifying organizations" that accept conservation easements to ensure they meet minimum standards for accepting and administering easements. The definition of a proper "conservation purpose" could also be clarified. As with appraisals and valuations, strengthening qualifications standards through an ongoing dialogue on best practices would go much further.

By embracing these types of alternatives – and others discussed below – the IRS could shift away from its current litigation mentality to an issue resolution mentality, bringing a much welcome reduction in friction between the agency and practitioners. In June 2019, IRS Chief Counsel Michael Desmond seemed to acknowledge this tension, saying: "I think we would like to think more generally about keeping cases out of litigation by giving good guidance on the front end so that things don't end up in litigation, but if that happens, how do we figure out a way to get cases like that resolved over the longer term under terms that are acceptable to both taxpayers and the IRS."[9] From both the taxpayers' and government's perspective, a more measured and incremental approach would be far more productive than the one currently underway.

[7] Kirk, Weston C. "Proposed Regulations Related to Section 2704 and the Case for Applying FLP Valuation Discounts." *Gift and Estate Tax Valuation Insights*, Winter 2016.

[8] Murphy, Christopher (United States Senate) and Blumenthal, Richard (United States Senate). Letter to: Hon. John Koskinen (Acting Commissioner, Internal Revenue Service). United States Senate, February, 23, 2016. Retrieved from: https://www.murphy.senate.gov/download/22316-irs-letter.

[9] Desmond, Michael. (June 27, 2019). Podcast interview with "Talking Tax".

Compliance Costs

When the IRS stamps a "listed transaction" label on a particular arrangement, the affected taxpayers – in this case, the participants in qualified conservation partnerships – are required to complete and submit IRS Form 8886, a Reportable Transaction Disclosure Statement, with their tax returns. Those who qualify as "Material Advisors" on these transactions must file separate disclosures on IRS Form 8918.[10] According to the IRS's published instructions, the estimated time for completing Form 8886 is 21.5 hours for every individual filing.[11] Each filing of Form 8918, according to the same IRS estimates, takes roughly 14.5 hours to complete.[12] Experience tells us these time estimates are likely understated.

There are a number of feasible alternatives for calculating the added compliance costs associated with these additional time and paperwork burdens. And, depending on the methodology used, the results range from considerable to catastrophic. For example, according to the Bureau of Labor Statistics' (BLS) most recent figures, the average compensation for full-time private sector employees is around $34.05 an hour.[13] Using that number, the estimated labor cost for completing and filing Form 8886 would be roughly $732 per filing – 21.5 hours at $34.05 an hour. For Form 8918, the average wage multiplied by the IRS's estimated hours gives us a projection of about $500 per filing. Given the level of expertise and the likely above-average wages of taxpayers claiming this deduction, another – and likely more accurate – approach would be to use the BLS compensation figures for professional and related workers, who, according to the most recent figures, were paid $55.92 an hour on average.[14] Using that figure, the labor costs go up to over $1,200 and $800 for every filing of Form 8886 and Form 8918 respectively.

But, there's a good chance that even that estimate is too low. According to the most recent fees survey from the National Society of Accountants, the average hourly rate charged for preparation of federal and state tax returns is $158.[15] Assuming that the filings are prepared by someone with at least the skill level of an average tax practitioner, the estimated per-filing cost could be $3,400 or higher for Form 8886 and $2,300 for Form 8918. Though, since the minimum fee threshold for material advisors is $50,000, the average accountant or tax preparer's fee is likely far too low a baseline with regard to Form 8918.

In 2017, the IRS reportedly received 39,619 disclosures on Form 8886 for conservation easements covered by the Notice.[16] Using the government figures cited above, the estimated time required to file all these disclosures would reach more than 850,000 hours. The associated labor costs would range from about $29 million to $134 million, depending on the average wage or fee figures used in the calculations. In addition, the IRS reportedly received 6,501 Form 8918 Material Advisor disclosures in that same year[17], which would require more than 94,000 total hours of labor according to the government's own estimates. The approximate systemwide costs for that disclosure would between $3.2 million and $14.8 million, depending on the hourly figure used.

Once again, these estimates are very likely lower than the actual figures since fees associated with these types of specialized filings almost certainly exceed those charged for preparing a typical return. In

[10] Internal Revenue Service. (2016.) "Listing Notice--Syndicated Conservation Easement Transactions" (2017-10).
[11] "Instructions for Form 8886: Reportable Transaction Disclosure Statement," Internal Revenue Service. Revised August 2017.
[12] "Instructions for Form 8918: Material Advisor Disclosure Statement," Internal Revenue Service. Revised June 2017.
[13] Bureau of Labor Statistics. (2019). "Employer Costs for Employee Compensation News Release" (USDL-19-0449).
[14] *Ibid*.
[15] "Income and Fee Survey." National Society of Accountants, December 2018. Retrieved from: https://mainstreetpractitioner.org/wp-content/uploads/2018/11/MSP-December-2018.pdf.
[16] Enclosure, page 1
[17] *Ibid*.

addition, these numbers don't even touch on the opportunity costs that come with all this compliance, such as disincentives to engage in productive behavior, lost time, and even societal stress, all of which have been cited by economists as adding to the price tag associated with tax compliance generally.[18]

Making all this worse is the fact that the IRS doesn't get much in the way of new or substantive information from these forms. Under the law, taxpayers claiming a charitable deduction for any noncash donation – including conservation easements – already have to file a completed IRS Form 8283 – signed by the donee – with their tax return.[19] All Form 8283 donations valued over $500,000 must be accompanied by a signed appraisal, and anyone who fails to submit or properly complete Form 8283 risks losing their deduction. Other material disclosures made with this form include the donor's basis in the property, the fair market valuation, as well as details related to the qualified conservation purpose. In addition, appraisals that significantly misstate the value of the easement property can result in significant tax penalties. Ultimately, if the goal is more transparency, the IRS could have more easily revised Form 8283, which would have provided them any additional information they deemed necessary without the increased time and financial burden. However, if the real aim is to make it harder to claim a deduction for conservation easements, the listed transaction requirements certainly do the job.

The IRS: Judge, Jury, and Executioner

The costs of the IRS's approach toward conservation easements goes beyond the added paperwork requirements. The agency has had an inordinate focus on conservation easements for years, and, while the Notice is just one in a serious of aberrant enforcement efforts, it is a major escalation in hostilities.

Of all the "reportable transactions" overseen by the IRS's Office of Tax Shelter Analysis, those getting the "listed transaction" label face the most severe potential consequences. Donors failing to complete and file IRS Form 8886 face penalties of up to $100,000 for individuals, or as much as $200,000 for different filing entities. Material advisors who fail to file or properly complete IRS Form 8918 can be fined $200,000 or 50 percent of the gross income they received for their advice or assistance – 75 percent if the failure is deemed intentional.[20] And, in both cases, there is no reasonable cause exception to mitigate the consequences of noncompliance.

In the nearly 30-year history of the "listed transaction" designation, the IRS has applied the label to 36 types of arrangements, and only two have been announced in the last decade - and for good reason. The "listed transaction" designation serves a narrow purpose: to gather advance information on a type of suspicious taxpayer behavior that is not otherwise reported on a return or is difficult to detect through other investigative means. Once again, prior to the Notice, easement donors claiming a charitable deduction already had to disclose any relevant information with IRS Form 8283. The disclosures required for listed transactions do not provide any material information about the value or qualifications of the easement.

In addition, if you examine other listed transactions, you'll notice that tax deductions for conservation easements by partnerships of unrelated individuals bear little or no resemblance to the claims or transactions that normally justify the designation. For example, Notice 99-59, issued in 1999, warned of a tax scheme referred to as a Bond and Option Sales Strategy ("BOSS") "in which taxpayers would claim tax losses for capital outlays that they have in fact recovered." In these arrangements, promoters

---

[18] Estimates of these opportunity costs vary according to methodology and assumptions. For one example, see, Payne, James L. *Costly Returns: The Burdens of the U.S. Tax System* (ICS Press, 1993). Payne estimates that opportunity costs add 65 cents to every dollar of federal income tax extracted from the economy.
[19] "Instructions for Form 8283," Internal Revenue Service. (Revised December 2014.)
[20] 26 U.S. Code § 6707

created foreign corporations for the sole purpose of selling stock to partnerships set up by taxpayers. The corporation would then distribute encumbered securities to its stockholders, reducing, or even zeroing out, its common stock value. This complex set of arrangements could not be easily discerned from tax returns, which led to the listed transaction notice.[21]

Shortly thereafter, another tax scheme – often referred to as "Son of BOSS" – emerged wherein taxpayers would claim an artificial capital loss to offset real capital gains. Under the most common version of this arrangement, a taxpayer would take on debts with unusually high interest rates and then set up a partnership to assume the indebtedness, exaggerating the basis of partnership distributions and creating loses that only existed on paper. In 2000, the IRS issued Notice 2000-44 to sound an alarm about these types of tax sheltering arrangements.[22]

Donations of conservation easements by partnerships are different from these and other types of listed transactions. For one thing, they involve real property. For another, when a partnership claims a deduction for a conservation easement, the basis of the deduction will be the valuation and qualification determinations. And, with both those factors, partnerships and individuals are subject to the same rules – forming a partnership does not make it any easier for taxpayers to conceal problematic transactions.

Procedurally speaking, Notice 2017-10 was hastily put into effect with no public input, which resulted not only in unfair impositions on taxpayers, but also several instances of bureaucratic mismanagement.[23] In addition, the requirements under the Notice were retroactive to 2010, imposing even greater recordkeeping, substantiation, and compliance costs on taxpayers, which is to be expected whenever policymakers create new tax rules and apply them to the past.

Proposed Legislation Misses the Point

Interestingly, the Joint Committee on Taxation (JCT) recently determined that the current Senate legislation (S. 170) aimed at restricting partnership easement deductions would have no revenue impact apart from the retroactive adjustments donors would have to make with regard to deductions claimed in previous years. JCT also determined that, because the bill has the effect of simply delaying relevant deduction claims, it would have a negligible impact on the number of deductions claimed by the disfavored partnerships. This further demonstrates the point that focusing on the type of taxpayers claiming easement deductions – and not the practices that directly cause improper deductions – is the wrong approach.[24] Notably, this less-than-overwhelming assessment from JCT didn't stop the bill's proponents from publicly touting the score.[25]

---

[21] Internal Revenue Service. (1999). "Notice 99-59: Tax avoidance using distributions of encumbered property" (1999-52 I.R.B.).

[22] Internal Revenue Service. (2000). "Notice 2000-44: Tax avoidance using artificially high basis" (2000-36 I.R.B.).

[23] Tucker, Thoni J. and Levitt, Ronald. "Conservation Easement Listed Transactions; New Notice 2017-29 (Or: The Good, the bad and the Ugly—Sorry Clint Eastwood!)" Lexology: Conservation Easement Blog, April 28,2017.

First, in its haste to issue reportable "transaction numbers" for participants in conservation partnerships to use when filling out the additional paperwork, the IRS provided 10-digit numbers, only to discover after the fact that its computer systems could only accommodate nine-digit numbers.

Later, in response to concerns from practitioners, the IRS issued Notice 2017-29 to clarify that donee organizations would not be considered Material Advisors under 2017-10. It also gave taxpayers an additional four months to comply with the new requirements and file disclosures for back tax years, but Material Advisors did not get a similar reprieve. The updated notice included deadlines that did not take into account taxpayers filing extension requests, confusing many additional taxpayers.

[24] "JCT Says Conservation Easement Bill Would Raise $6.6 Billion," *Tax Notes*, July 9, 2019.

[25] Daines, Steve. "Daines Bill Set to Generate $6.6 Billion in Federal Revenue," United States Senate, July 11, 2019.

IRS Stacks the Deck Against Taxpayers

The substantive and procedural harms resulting from Notice 2017-10 exacerbate the already untenable nature of IRS enforcement, particularly as it has been applied to donations of conservation easements. For example, when the IRS sets its form and paperwork requirements, it also sets its own standards for substantial compliance to filing rules and deadlines. This may seem intuitive, but, with conservation easements, the agency has a history of challenging even the most minute procedural or paperwork shortfalls and oversights in order to invalidate deductions. In the Cave Buttes, LLC v. Commissioner case, the IRS needled the taxpayer because the appraisal listed the qualifications of only one of two appraisers that worked on the easement, even though a fair reading of the IRS's rules only require the information from one appraiser. In addition, only one of the appraisers signed the Form 8283 disclosure, and the IRS challenged the deduction even though the form had only one signature line.[26] Fortunately, the taxpayers won that case, but far more often than not, taxpayers will end up losing their deductions when the IRS raises an issue with procedures or paperwork, even when the mistakes have no impact on the validity of the deduction or the agency's ability to process it.

When auditing easement deductions, the IRS makes its own valuation and qualification determinations, sets the penalties, and oversees collection actions. To be clear, both valuation and qualification are vital considerations and there should be plain and enforceable standards for both. But the IRS has a distinguished track record of hamstringing taxpayers along these lines as well. For instance, when challenging easement appraisals, the IRS has taken a "zero valuation" stance on numerous occasions, often providing ridiculous justifications for doing so. In such cases, the IRS will usually insist on its own valuation assessments, often demanding and enforcing a massive haircut on the deduction. There are legitimate reasons for appraisers acting in good faith to have different opinions on factors that affect property values. Yet, the agency tends to insist on litigating disputes over their valuations in Tax Court.

An examination of the most relevant Tax Court cases – most of them addressing issues of valuation or procedural foot-faults on easement deduction claims – is illustrative here. On average, the Tax Court issues a decision on these cases nine years after a donation is made.[27] Assuming the IRS challenge to a deduction arises the year after it is claimed, taxpayers can reasonably expect to go through eight years of dispute and litigation before getting a resolution to their case. All of that comes at significant expense to taxpayers without any guarantee that they will ever be made whole. In fact, if a taxpayer wins in Tax Court, their ability to recoup any attorney's fees is severely limited – capped by statute at around $200 an hour and only if the IRS cannot establish that its position was "substantially justified,"[28] which most tax practitioners acknowledge is a high bar for taxpayers seeking even partial recovery.[29] Other federal laws – such as Section 7421 of the Tax Code – put almost insurmountable restrictions on taxpayers seeking injunctions against the IRS, even if the IRS's position or conduct is manifestly improper or unreasonable. Therefore, it's more than logical to conclude that, for the average taxpayer claiming an average easement deduction, the cost of engaging in years-long litigation over appraisals can be overwhelming and ultimately not worth the expense.

As stated previously, none of these practices originated with the issuance of Notice 2017-10. Nevertheless, they are indicative of the mindset at the IRS that led to this point. And, once again, the Notice gives the

[26] Ecuyer, Joseph J. "Like a Dog with a Bone, IRS Continues to Insist on Strict Compliance with Appraisal Substantiation Requirements," *Bloomberg BNA*, September 30, 2016.
[27] Author's calculations of opinions of the U.S. Tax Court on conservation easements. See conservation easement opinions at ustaxcourt.gov.
[28] 26 USC Section 7430
[29] Camp, Bryan. "Lesson from the Tax Court: It Takes More Than Winning To Get Attorneys Fees Under Section 7430." Tax-Prof Blog, May 6, 2019.

IRS a new set of tools it can use against taxpayers claiming conservation easement deductions, even if the deductions are legitimate.

Private Conservation: A Win for U.S. Taxpayers

One of the more bewildering aspects of the IRS's posture toward donations of conservation easements is that these types of easements, and private conservation more generally, provide a number of tangible benefits. These include both fiscal and economic benefits as well as positive societal outcomes. By any objective measure, the positive impact of private conservation and donated conservation easements far outweighs any foregone federal tax revenues associated with the deduction.

According to the most recent available IRS numbers, taxpayers deducted a total of $2.3 billion for noncash donations of conservation easements in 2015. That was down a little from $3.2 billion in 2014.[30] In recent communications to Congress, the IRS indicated that, in 2016, deductions just for easements impacted by the Notice in 2016 exceeded $6 billion[31], an admittedly significant increase in claims over a year, though the IRS has not yet made the full numbers available. To be clear, the true revenue cost of the conservation easement deduction is significantly lower than these yearly figures. Taxpayers using the deduction can reduce their tax liability by, at most, 40 percent of the deducted amount. Therefore, in 2014, all conservation easement deductions – whether by individuals, typical partnerships, or "syndicated" partnerships – lowered tax revenue by no more than $1.3 billion, or roughly 40 percent of $3.2 billion. This amounted to a tiny fraction of the $1.395 trillion in total federal income tax revenue from that fiscal year.

While this may seem like nitpicking, it is important to nail down the specifics of these dollar figures because opponents and skeptics of the conservation easement deduction often use them – intentionally or possibly in error – in ways that inflate the apparent cost of the deduction or the size of the easement issue. For example, some have cited surges in overall conservation easement deductions alone as prima facie evidence of widespread impropriety[32] , even though the aggregate number provides zero information about validity of any particular deduction. Others have claimed that the IRS's tally of deductions associated with disclosures required after Notice 2017-10 – which almost certainly includes a number of valid claims – represents the total cost of syndicated easement deductions by partnerships.[33] And, some have even cited the dollar figure for ALL conservation easement deductions – both individuals and partnerships counting the amount deducted, not the actual reduced liability – as the revenue loss resulting just from syndicated easements.[34] In all these instances, the misuse of IRS figures misstate the amount of lost revenue and overstate the size of the potential issue. Ultimately, even if taxpayers claim a total $6-7 billion in easement deductions in a single year, the maximum revenue loss – the only amount that can reasonably be called a "cost" to taxpayers – is less than $3 billion.

Still, instead of focusing on the cost, the more important question is: What are taxpayers getting in return?

---

[30] Sherlock, Molly F. "Charitable Conservations Contributions: Potential for Abuse?" Congressional Research Service, July 19, 2019.

[31] Kauttner, David J. (Acting Commissioner, Internal Revenue Service, Department of the Treasury). Letter to: Sen. Orrin Hatch (Chairman, Committee on Finance, United States Senate). Supplement to IRS Notice 2017-10, Department of the Treasury, July 12, 2018. Retrieved from: https://www.ntu.org/library/doclib/2018/07/IRS-syndicated-easements-letter.pdf.

[32] See, e.g., Looney, Adam. "Estimating the rising cost of a surprising tax shelter: the syndicated conservation easement," Brookings Institution, December 20, 2017.

[33] See, e.g., Lysen, Joshua. "Charitable Conservation Easement Program Integrity Act Expected to Generate $6.6 Billion in Federal Revenue." Land Trust Alliance, July 11, 2019.

[34] See, e.g., "Grassley, Wyden Launch Probe of Conservation Tax Benefit Abuse," United States Senate Committee on Finance, March 27, 2019.

One way to look at this question is to compare private conservation with government-run lands programs. At the federal level, best estimates are that the U.S. government controls around 640 million acres of domestic land. It is unclear exactly how much federal taxpayer money goes into land management, but the total budgets of the federal agencies most responsible for managing federal land – the Bureau of Land Management, Fish and Wildlife Services, National Park Service, and the U.S. Forest Service – suggest that the federal government spends at least $15 billion a year to manage its lands.[35] That is $15 billion a year that is subject to all the pressures and restrictions that accompany federal government spending, with the added drawbacks of federal lands policy and regulations. These include complex rules on resource extraction, often arbitrary – and politically motivated – land designations, and prohibitions on leasing land for resource purposes. The result is a costly land-management system that continually operates at a loss.

Looking at the comparison just in terms of labor efficiency, private conservation lands are far better managed. To illustrate, consider National Park Service, which administers 85 million acres (more than two-thirds of it in Alaska alone), employs roughly 20,000 paid workers and utilizes the services of roughly 315,000 volunteers.[36] In contrast, the Land Trust Alliance's National Land Trust Census estimates that private land trusts manage just over 56 million acres in the U.S., with barely more than 8,000 employees and about 208,000 volunteers.[37] In other words, land trusts manage about 40 percent more land area per employee than the National Park Service.

Taking state efforts into account is also illustrative. According to the Property and Environment Research Center (PERC), states spend a combined $16.5 billion a year to manage the lands within their care. Yet, because states are often required by law to use their trust lands to raise revenues in perpetuity, they have incentives to maximize the economic viability of the land and shrink their overhead. As a result, PERC has estimated that, for every dollar spent per acre on trust lands, states earn a return of $14.51. The feds lose 27 cents for every dollar they spend managing their lands.[38]

Private conservation easements – in both a practical and substantive sense – are quite similar to state trust lands. Both require managers to balance competing priorities, with an eye toward maximizing value and collaboration between easement donors and their donee organizations. Private conservation easements are not as limited by regulatory and bureaucratic requirements that governments must deal with, allowing for more entrepreneurial and innovative approaches to land stewardship and more responsive decision making.

These advantages aren't just theoretical. Numerous studies have demonstrated the benefits of private land conservation and donations of privately-owned easements. For example, a recent study by Colorado State University (CSU) analyzed the impact of the state's conservation easement investments, which included conservation easement tax credits – with value calculations much like the federal tax deduction – and direct grants issued to purchase easements. According to the study, the two programs supported conservation of nearly 2.1 million acres of land across the state, all while addressing the state's major conservation priorities. All told, researchers determined that for every dollar invested under the program, the people of Colorado received between $4 and $12 in public benefits.[39]

[35] Vincent, Carol Hardy et al. "Federal Land Ownership: Overview and Data," Congressional Research Service, March 3, 2017.
[36] "Frequently Asked Questions," National Park Service, U.S. Department of the Interior, October 29, 2018.
[37] "2015 National Land Trust Census," Land Trust Alliance, December 1, 2016. Retrieved from: http://www.landtrustalliance.org/census-map.
[38] Fretwell, Holly and Regan, Shawn. "Divided Lands: State vs. Federal Management in the West," PERC Public Lands Report, March 2015.
[39] Seidl, A., et al. "Colorado's return on investments in conservation easements: Conservation Easement Tax Credit program and Great Outdoors Colorado." Colorado State University, Fort Collins, Colorado, 2017.

Likewise, a recent study by the Texas Land Council found that lands put into conservation by private land trusts produce more than $1 billion in benefits and savings to Texas taxpayers every year. Moreover, the study found that every dollar the state puts in conservation easements leverages $7.50 in additional funds from other sources.[40] Many other studies of state investments in conservation – most of which include significant investments in conservation easements – suggest much of the same.

Put simply, the conservation easement deduction can accurately be considered a federal investment in conservation lands, not a deadweight loss from a tax expenditure. Therefore, ensuring the deduction is used only for worthy projects and preventing taxpayers from gaming the system with improper or inaccurate valuations are both worthy goals that preserve the integrity of that investment. Notice 2017-10, however, is not focused on ensuring wise investments or maximizing return for the taxpayers. On the contrary, it is built around the notion that too many people are claiming the benefit and that certain taxpayer arrangements are undesirable, even if the deduction is for a sound conservation investment. This approach is both harmful to taxpayers and to broader conservation efforts.

Conclusion

While the issues surrounding the conservation easement deduction are important, this is admittedly an arcane area of the tax code. And, if the problems noted here were unique and limited to the enforcement and administration of the conservation easement deduction, this discussion might not warrant so much attention from taxpayer advocates. However, the harms caused by the IRS's approach to conservation easements are indicative of problems throughout the IRS.

Perhaps some of these problems could be addressed through changes at the agency. The IRS could certainly act on its own to rein in the over-zealous and heavy-handed tactics we're seeing with conservation easements and elsewhere. The agency could unilaterally implement virtually all of the changes recommended above, which would be significant improvements and go a long way toward respecting taxpayer rights.

But, as with almost any Executive Branch practice, change is unlikely to come without outside pressure. Therefore, Congress has an obligation to ensure the IRS is administering and enforcing the law as intended. To date, efforts in Congress have seemingly assumed the IRS is acting appropriately. This is certainly unfortunate, but, as the tax-writing committees continue to investigate and examine these issues and members of Congress reflect on the incentives that provisions like the conservation easement deduction were intended to provide, there will be multiple opportunities to change course and provide much-needed safeguards for taxpayers. Hopefully, in the end, Congress will find itself on the side of taxpayer rights.

About the Author

Bryan Hickman is a Policy Fellow with National Taxpayers Union. He is a writer and communications professional with an extensive policy background developed over nearly 14 years working on Capitol Hill, including multi-year stints on the Senate Finance and Judiciary Committees. His credentials include a J.D. from The George Washington University Law School and B.S. and M.S. degrees in political science from Utah State University.

[40] "Valuing Economic Benefits of Texas Conservation Lands," Texas Land Trust Council, January 2019.

2019 National Taxpayers Union
122 C Street NW, Suite 650, Washington, DC 20001
ntu@ntu.org