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Taxpayer Defeats IRS Penalty in Tax Court for Conservation Easement Transaction

December 21, 2021

On November 20, 2021, the Tax Court ruled in favor of our client facing penalties related to disallowed charitable contribution deductions for conservation easements. In *Plateau Holdings, LLC v. Commissioner*, T.C. Memo. 2021-133, the Tax Court found that the client had reasonable cause for the understatement of the tax liability at issue because (1) the taxpayer could reasonably believe that the attorney who drafted the deed of easement for the recipient did so in a manner that complied with the regulations, and (2) there was "substantial authority" that the contested clause in the deed would not prevent a charitable contribution deduction.

In an earlier ruling issued prior to Caplin & Drysdale's representation, the Tax Court determined that the taxpayer was not entitled to its charitable contribution deduction because the easement was overvalued and also because a defect in the deed of easement caused the deduction to fail the perpetuity requirement of the Treasury regulations. The prior opinion left open the issue of whether the taxpayer should be penalized for the portion of its tax liability that was understated as a result of the easement's failure to satisfy the perpetuity requirement.

After retaining Caplin & Drysdale, the taxpayer argued that it should not be subject to the penalty because it relied on the beneficiary land trust's attorney to draft the deed of easement in compliance with the Treasury regulations. The Taxpayer also argued that the authority existing at the time the deed was drafted, including an IRS letter ruling on charitable contribution deductions, indicated that the position it had taken was objectively reasonable. After briefing, the Tax Court agreed with the taxpayer and concluded that penalties were not appropriate in these circumstances.

The taxpayer's win is significant because the clause at issue in the deed of easement is repeated verbatim in numerous deeds of conservation easement throughout the industry, and it has been seized upon by the IRS and the Tax Court as a reason to disallow charitable contribution deductions in other cases. Although similarly situated taxpayers may face an uphill battle on the deductibility of the contribution, they now have judicial support to defend against the IRS's assertion of penalties. As every case is different, we urge similarly situated taxpayers to consult with counsel to determine whether the arguments employed in this case are appropriate in their matters before the IRS and the Tax Court.

For more information regarding this Alert, please contact members of Caplin & Drysdale's Tax Controversy Group:

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The firm's reputation over the years has earned us the trust and respect of clients, industry peers, and government agencies. Moreover, clients rely on our broad knowledge of the law and our keen insights into their business concerns and personal interests. Our lawyers' strong tactical and problem-solving skills - combined with substantial experience handling a variety of complex, high stakes, matters in a boutique environment - make us one the nation's most distinctive law firms.

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