Wachter v. Commissioner, 142 T. C. No. 7 (U. S. Tax Court 2014)

In Wachter v. Commissioner, the U. S. Tax Court ruled that a North Dakota statute limiting easements to 99 years prevented conservation easements from being considered perpetual, thus disallowing charitable contribution deductions under federal tax law. The court's decision underscores the importance of state law in determining the validity of conservation easements for tax purposes, impacting how taxpayers can claim deductions for such contributions.

Parties

Patrick J. Wachter and Louise M. Wachter, and Michael E. Wachter and Kelly A. Wachter (Petitioners) v. Commissioner of Internal Revenue (Respondent).

Facts

The Wachters, through entities WW Ranch and Wind River Properties LLC (treated as partnerships for tax purposes), claimed charitable contribution deductions for 2004 through 2006. WW Ranch reported deductions based on bargain sales of conservation easements, while Wind River reported cash contributions. The easements were sold to the American Foundation for Wildlife (AFW), partially funded by North Dakota Natural Resource Trust (NRT), which also provided appraisals and cash contributions. The deductions were disallowed by the Commissioner, leading to notices of deficiency and subsequent litigation.

Procedural History

The Commissioner issued notices of deficiency disallowing the charitable contribution deductions and asserting accuracy-related penalties. The Wachters filed petitions with the U. S. Tax Court, which consolidated the cases. The Commissioner moved for partial summary judgment on the issues of the perpetuity of the easements under North Dakota law and the sufficiency of contemporaneous written acknowledgments for the cash contributions.

Issue(s)

Whether a North Dakota statute limiting easements to 99 years precludes the Wachters' conservation easements from qualifying as granted "in perpetuity" under I. R. C. sec. 170(h)(2)(C) and (5)(A)?

Whether the documents provided by the Wachters satisfy the "contemporaneous written acknowledgment" requirement of I. R. C. sec. 170(f)(8) and sec. 1. 170A-13(f)(15), Income Tax Regs. ?

Rule(s) of Law

Under I. R. C. sec. 170(h)(2)(C), a qualified real property interest includes "a

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restriction (granted in perpetuity) on the use which may be made of the real property. ” I. R. C. sec. 170(h)(5)(A) requires that the contribution be “exclusively for conservation purposes. ” For cash contributions of $250 or more, I. R. C. sec. 170(f)(8) mandates a contemporaneous written acknowledgment from the donee.

Holding

The court held that North Dakota law limiting easements to 99 years precludes the Wachters’ conservation easements from qualifying as granted “in perpetuity” under I. R. C. sec. 170(h)(2)(C) and (5)(A), thus disallowing the charitable contribution deductions. On the issue of the cash contributions, the court found that material facts remained in dispute regarding the contemporaneous written acknowledgment requirement, and thus summary judgment was not appropriate.

Reasoning

The court’s reasoning focused on the perpetuity requirement under I. R. C. sec. 170(h)(2)(C) and (5)(A). The court determined that North Dakota law, which limits easements to a maximum of 99 years, prevents the easements from being considered perpetual. The court rejected the Wachters’ argument that the possibility of the land reverting back after 99 years was a remote future event, as the event was not only possible but inevitable under state law. The court distinguished this from situations where long-term leases might be treated as equivalent to fee simple interests, noting that such situations do not involve the express statutory requirement of perpetuity as in section 170(h)(2)(C). Regarding the cash contributions, the court found that the Commissioner failed to prove that the Wachters expected or received benefits not disclosed in the acknowledgment letters, and that the Wachters might be able to provide additional documentation to meet the requirements of a contemporaneous written acknowledgment.

Disposition

The court granted the Commissioner’s motion for partial summary judgment on the issue of the noncash contributions, disallowing the charitable contribution deductions for the conservation easements. The court denied the motion for partial summary judgment on the issue of the cash contributions, leaving that issue to be resolved at trial.

Significance/Impact

The Wachter decision has significant implications for the interplay between state and federal law regarding conservation easements. It underscores that state laws limiting the duration of easements can affect their qualification for federal tax deductions, potentially impacting conservation efforts and tax planning strategies. The decision also highlights the importance of strict adherence to the contemporaneous written acknowledgment requirements for cash contributions,

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emphasizing the need for clear documentation to support charitable deductions.

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