Nathaniel A. Carter and Stella C. Carter v. Commissioner of Internal Revenue, T. C. Memo. 2020-21 (U. S. Tax Court 2020)

In Carter v. Commissioner, the U. S. Tax Court ruled that a conservation easement did not qualify for a charitable deduction under IRC §170(h) due to the donors' retained right to build homes in undefined areas, which failed the perpetual restriction requirement. The court also invalidated proposed gross valuation misstatement penalties due to untimely supervisory approval, impacting how such penalties are enforced in future tax cases.

Parties

Nathaniel A. Carter and Stella C. Carter, petitioners, and Ralph G. Evans, petitioner, versus Commissioner of Internal Revenue, respondent. The cases were consolidated for trial, briefing, and opinion in the U. S. Tax Court.

Facts

In 2005, Dover Hall Plantation, LLC (DHP), owned by Nathaniel Carter, purchased a 5,245-acre tract in Glynn County, Georgia. In 2009, Ralph Evans purchased a 50% interest in DHP. In 2011, DHP conveyed a conservation easement over 500 acres of Dover Hall to the North American Land Trust (NALT), a qualified organization under IRC §170(h)(3). The easement generally prohibited dwellings but allowed DHP to build single-family homes in 11 unspecified two-acre building areas, subject to NALT's approval. DHP claimed a charitable contribution deduction for the easement on its 2011 tax return, and Carter and Evans claimed their respective shares on their individual returns. The Commissioner disallowed these deductions and proposed gross valuation misstatement penalties under IRC §6662.

Procedural History

The Commissioner issued notices of deficiency on August 18, 2015, disallowing the charitable contribution deductions claimed by Carter and Evans for 2011, 2012, and 2013, and proposing gross valuation misstatement penalties. On May 8, 2015, Revenue Agent Christopher Dickerson sent examination reports (RARs) and Letters 5153 to the Carters and Evans, proposing adjustments and penalties. These letters did not include "30-day letters" offering appeal rights because the taxpayers did not agree to extend the period of limitations on assessment. The Tax Court consolidated the cases and held a trial to determine the validity of the claimed deductions and penalties.

Issue(s)

Whether the conservation easement granted by DHP to NALT constitutes a "qualified real property interest" under IRC §170(h)(2)(C) when it allows for the construction of single-family homes in unspecified building areas? Whether the gross valuation misstatement penalties under IRC §6662 were timely approved by the Revenue Agent's immediate supervisor?

Rule(s) of Law

IRC §170(h)(1) defines a "qualified conservation contribution" as a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. IRC §170(h)(2)(C) includes a "restriction (granted in perpetuity) on the use which may be made of real property. " IRC §6751(b)(1) requires that no penalty shall be assessed unless the initial determination of such assessment is personally approved in writing by the immediate supervisor of the individual making such determination.

Holding

The Tax Court held that the conservation easement did not meet the perpetual restriction requirement of IRC §170(h)(2) because the building areas allowed for uses antithetical to the easement's conservation purposes. Consequently, the easement was not a "qualified real property interest," and no charitable contribution deductions were allowed under IRC §170. The court also held that the gross valuation misstatement penalties were not sustained due to untimely supervisory approval under IRC §6751(b)(1).

Reasoning

The court relied on Pine Mountain Pres. , LLLP v. Commissioner, 151 T. C. 247 (2018), to determine that the building areas, though subject to some restrictions, were exempt from the easement because they permitted uses antithetical to its conservation purposes, such as the construction of single-family homes. The court found that the residual restrictions within the building areas were not meaningful under IRC §170(h)(2) because they did not prevent the development of homes, which is contrary to the preservation of open space and natural habitats. Regarding the penalties, the court concluded that the initial determination of the penalties was communicated to the taxpayers via the RARs and Letters 5153 on May 8, 2015, before the written approval by the Revenue Agent's supervisor on May 19, 2015. Thus, the approval was untimely under IRC §6751(b)(1).

Disposition

The Tax Court disallowed the charitable contribution deductions claimed by Carter and Evans and did not sustain the gross valuation misstatement penalties. Decisions were entered under Rule 155.

Significance/Impact

Carter v. Commissioner reinforces the strict interpretation of the perpetual restriction requirement for conservation easements under IRC §170(h)(2), emphasizing that any retained development rights must not undermine the conservation purposes. The decision also clarifies the timing requirement for supervisory approval of penalties under IRC §6751(b)(1), affecting the IRS's enforcement of penalties and potentially impacting future tax litigation involving similar issues.

