Land Trusts in the Twenty-First Century: How the Tax Abuse and Corporate Governance Threaten the Integrity of Charitable Land Preservation

Erin B. Gisler

Follow this and additional works at: http://digitalcommons.law.scu.edu/lawreview

Part of the Law Commons

Recommended Citation

Available at: http://digitalcommons.law.scu.edu/lawreview/vol49/iss4/8
LAND TRUSTS IN THE TWENTY-FIRST CENTURY: HOW TAX ABUSE AND CORPORATE GOVERNANCE THREATEN THE INTEGRITY OF CHARITABLE LAND PRESERVATION

Erin B. Gisler*

I. INTRODUCTION

Massachusetts’s The Trustees of Reservations became the nation’s first land trust1 in 1891 by acquiring the twenty-acre Virginia Woods as its first property to preserve.2 Now, more than one hundred years later, land trusts operate in all fifty states.3 Paralleling dramatic population growth and sprawl,4 land trust growth gained momentum in the 1980s with the passage of the Uniform Conservation Easement Act,5 as well as...
as a new tax provision that allowed for an income tax deduction for a charitable contribution of land.\textsuperscript{6} The conservation movement also encouraged the passage of additional tax incentives in the twenty-first century.\textsuperscript{7} However, as with any kind of financially motivating laws, abuse is inevitable. Particularly with the fair market valuations that must occur when a donor contributes land, appraisals hinder the conservation process by enabling self-interested landowners to attain an inaccurately high land value estimate so as to deduct more income taxes.\textsuperscript{8} Today, land trusts' goodwill suffer from transacting with landowners who attain dishonest appraisals.\textsuperscript{9} The reputations of land trusts have also been tarnished by the unethical practices of The Nature Conservancy, one specific land trust that has drawn the negative attention of journalists and Congress.\textsuperscript{10}

This comment explores the pivotal role of land trusts in the conservation boom and in upholding the integrity of land conservation. Part II provides a background of land trusts and their functions; it also reviews how land conservation and land trusts became popular as a result of statutory changes in federal tax law, and how such popularity has encouraged even more pro-conservation legislation.\textsuperscript{11} Part III presents one of the major threats to the conservation movement: tax abuse.\textsuperscript{12} Part IV analyzes this problem from the viewpoint of individual landowners seeking hefty income tax deductions

\begin{itemize}
\item \textsuperscript{6} Easement Act defines a conservation easement as:
\begin{quote}
\begin{itemize}
\item a nonpossessory interest of a holder in real property imposing limitations or affirmative obligations the purposes of which include retaining or protecting natural, scenic, or open-space values of real property, assuring its availability for agricultural, forest, recreational, or open-space use, protecting natural resources, maintaining or enhancing air or water quality, or preserving the historical, architectural, archaeological, or cultural aspects of real property.
\end{itemize}
\end{quote}
\end{itemize}

\textit{UCEA} § 1(1).

\begin{itemize}
\item \textsuperscript{7} I.R.C. § 170(h) (2006).
\item \textsuperscript{9} \textit{See} discussion \textit{infra} Part IV.A.
\item \textsuperscript{10} \textit{See} discussion \textit{infra} Part IV.B.
\item \textsuperscript{11} \textit{See} David B. Ottaway \& Joe Stephens, \textit{Nonprofit Land Bank Amasses Billions; Charity Builds Assets on Corporate Partnerships}, WASH. POST, May 4, 2003, at A01.
\item \textsuperscript{12} \textit{See} \textit{infra} Part III.
\end{itemize}
and discusses how land trusts, and The Nature Conservancy in particular, can lose sight of their missions to conserve by engaging in unethical, profit-motivated behavior. Part V's proposal suggests a number of methods all parties involved in land conservation can implement to adhere to ethical and responsible standards.

II. BACKGROUND: LAND TRUSTS

A. Land Trusts in the United States

As awareness of environmental issues and the importance of land conservation continues to grow, the United States has seen a boom in legislation and programs aimed at protecting various land resources. Land trusts have blossomed and developed into the main facilitators of land preservation. By helping landowners conserve their land, land trusts "act to acquire land, conservation easements, management agreements, or other interests in real property for the purpose of enabling public benefit from the land." Land trusts protect a variety of types of land, including wildlife habitats, forests, open space, watersheds, wetlands, scenic views and roads, and ecosystems.

Midway through the twentieth century, about fifty land trusts existed, mostly in the Northeast region of the United States. Spurred by rapid population growth and land development, the number of land trusts began to steadily increase in the 1960s. As of 2005 there were more than 1600 land trusts across the country, a thirty-two percent increase since 2000. California is home to the highest number of land trusts—198 as of 2005, conserving 1,732,471 acres.

13. See infra Part IV.
14. See infra Part V.
15. Gustanski, supra note 4, at 12.
16. Id.
17. Id.
18. Id. at 21.
19. Id. at 17.
21. Id. at 5.
acres of land. However, the largest concentration of land trusts is still in the Northeast. As a whole, the United States conserves nearly twelve million acres of land.

Americans have demonstrated an interest in land trusts and preservation by increasing state and local bond initiatives for conservation. The year 2006 witnessed the passage of 133 measures in California, Georgia, New Jersey, South Carolina, and Texas, collectively approving $6.7 billion for conservation. A boost in philanthropic endeavors also reflects the public’s awareness of conservation efforts. The end of 2005 saw land trust membership reach 1.5 million, with monetary donations doubling land trusts’ operating budgets between 2000 and 2005. The number of land trust volunteers also grew a remarkable sixty-three percent within the same time period.

Not only are the hundreds of land trusts across the United States diverse, but the type of land protected varies as well. Nine land trusts operate nationwide and at least two of those, The Nature Conservancy and The Humane Society of the United States Wildlife Land Trust, also operate in

22. Id. at 20 chart 5.
23. Id. at 21. More than 3.5 million acres, or thirty percent of the total number of acres conserved in the United States, are protected in the Northeast. See id. at 21–22 chart 5. “The preponderance of land trusts in the Northeast reflects the birth of land trusts there more than 100 years ago.” Id. at 5.
24. ALDRICH ET AL., supra note 20, at 21 chart 5.
25. See id. at 7.
26. Id.
27. Id. at 12. While memberships with different land trusts vary, individual members of the Land Trust Alliance, for example, pay thirty-five dollars and receive “a year's subscription of Saving Land, the national journal for land trusts and conservation” and the recognition that they subscribe to the conservation efforts of the Alliance. Land Trust Alliance, Get Involved, Membership, Individual Membership, http://www.landtrustalliance.org/get-involved/membership/individual/individual (last visited Mar. 15, 2009).
28. ALDRICH ET AL., supra note 20, at 12.
29. Id. There were 55,597 volunteers in 2000 and 90,871 in 2005. Id. While large land trusts have plentiful budgets, many organizations are very small with minimal budgets, operated solely by volunteers. Federico Cheever, Public Good and Private Magic in the Law of Land Trusts and Conservation Easements: A Happy Present and a Troubled Future, 73 DENV. U. L. REV. 1077, 1085 (1996).
foreign countries.\textsuperscript{31} Local land trusts, on the other hand, operate on a smaller scale and employ unique approaches to conserving local resources.\textsuperscript{32} The diversity of local land trusts stems from differences in vegetation, state and local laws, and the individual cultures of the people living in each locality.\textsuperscript{33}

Nearly all of the country’s land trusts belong to the Land Trust Alliance, a non-profit organization whose mission is to “save the places people love by strengthening land conservation across America.”\textsuperscript{34} The Land Trust Alliance encourages the successful operation of land trusts by organizing a national rally, issuing a variety of publications,\textsuperscript{35} promulgating ethical standards and practices for adoption by land trusts,\textsuperscript{36} and representing land conservation values at the nation’s capital.\textsuperscript{37} The emphasis that the Land Trust Alliance places upon land trust education and effective operation demonstrates that the popularity of land donation and conservation is not immune to vulnerability. This comment will expose some weaknesses of land trusts as nonprofit organizations.

B. Land Trust Functions

1. The Popularity of Conservation Easements

Although land trusts can conserve land in any number of

\begin{itemize}
\item \textsuperscript{32} See BREWER, supra note 3, at 269.
\item \textsuperscript{33} See id.
\item \textsuperscript{34} Land Trust Alliance, About Us, Who We Are, http://www.landtrustalliance.org/about-us/who-we-are (last visited Mar. 15, 2009).
\item \textsuperscript{35} Publications include books, videos, brochures, and software covering a range of topics, including fundraising, land transactions, landowner resources, and organizational management. See Land Trust Alliance, Resources, Publications, http://www.landtrustalliance.org/resources/publications (last visited Mar. 15, 2009).
\item \textsuperscript{37} BREWER, supra note 3, at 178–79.
\end{itemize}
ways, acquisition typically arises either through fee simple\textsuperscript{38} ownership or a conservation easement.\textsuperscript{39} Land trusts often acquire title in fee, which means title passes completely from the original landowner to the land trust.\textsuperscript{40} With a conservation easement, however, land trusts merely hold a right to protect the land and prevent development.\textsuperscript{41} Protection by a conservation easement has surpassed all other methods of acquisition and is the most common means for private land conservation in the country.\textsuperscript{42} By the end of 2005, conservation easements protected more than six million acres of land.\textsuperscript{43}

Conservation easements appeal to landowners for a number of reasons. Essential to the concept of a conservation easement is that the landowner retains private ownership of the preserved land while giving up specific rights that ensure its conservation.\textsuperscript{44} Because conservation easements aim to protect land, a landowner normally relinquishes the right to develop, subdivide, and/or log trees.\textsuperscript{45} Land trusts work with landowners to tailor each conservation easement to the particular needs and interests of the individual owner and property.\textsuperscript{46} Conservation easements also normally enable a landowner to retain possessory rights, allowing the landowner to continue residing on the land while ensuring its lasting protection.\textsuperscript{47}

2. Methods of Acquisition

While contract flexibility makes conservation easements extremely popular, donating or selling title to a land trust

\begin{itemize}
\item \textsuperscript{38} Fee simple is "[a]n interest in land that, being the broadest property interest allowed by law, endures until the current holder dies without heirs." BLACK'S LAW DICTIONARY 648 (8th ed. 2004).
\item \textsuperscript{39} Duncan M. Greene, Comment, Dynamic Conservation Easements: Facing the Problem of Perpetuity in Land Conservation, 28 SEATTLE U. L. REV. 883, 887 (2005).
\item \textsuperscript{40} See supra note 38 and accompanying text.
\item \textsuperscript{41} UCEA, supra note 5, § 1(1).
\item \textsuperscript{42} Gustanski, supra note 4, at 9.
\item \textsuperscript{43} ALDRICH ET AL., supra note 5, § 1(1).
\item \textsuperscript{44} See JANET DIEHL & THOMAS S. BARRETT, THE CONSERVATION EASEMENT HANDBOOK: MANAGING LAND CONSERVATION AND HISTORIC PRESERVATION EASEMENT PROGRAMS 5 (1988).
\item \textsuperscript{45} See id.
\item \textsuperscript{46} See id.
\item \textsuperscript{47} See Greene, supra note 39, at 889.
\end{itemize}
serves as the easiest way to ensure conservation. Landowners have several options with respect to land donations: donating land outright, donating a remainder interest with a life estate, or donating by will. Financial incentives to donate land include both relief from property taxes and other taxes imposed on the sale of land (i.e., capital gains, conveyance, and transfer taxes). Moreover, landowners who donate their land can take an income tax deduction for the fair market value of the land as a charitable donation. Landowners can also donate land and continue to receive income through a charitable gift annuity or a charitable remainder unitrust.

For landowners who wish to receive some cash in exchange for their land, land trusts can arrange bargain sales. Through a bargain sale, the land trust buys the landowner's land for less than fair market value. The landowner receives the reduced purchase price and the ability to deduct the difference between the fair market value and

---

48. See BREWER, supra note 3, at 140.

49. The landowner owns the land for the remainder of her lifetime (she has a life estate) and upon her death the land passes to a land trust (the trust has the remainder interest). See BLACK'S LAW DICTIONARY 588, 1319 (8th ed. 2004).


51. Id. at 136.

52. See discussion of tax legislation infra Part II.C. See also BREWER, supra note 3, at 141.

53. A charitable gift annuity is "a contract under which a charity, in return for a transfer of cash or other property, agrees to pay a fixed sum of money for a period measured by one or two lives." American Council on Gift Annuities, Donors' Corner, http://www.acga-web.org/donorscorner.html (last visited Mar. 15, 2009); see also I.R.C. § 664(d)(1) (2006).

54. Like a charitable gift annuity, charitable remainder unitrusts (or CRUTs) allow the land donor (the income beneficiary) to receive annual income payments from the land trust, except a CRUT pays the landowner a fixed percentage (between five and fifty percent) of the net fair market value of the land. See I.R.C. § 664(d)(2). Charitable gift annuities and CRUTs are often utilized by landowners with a lot of equity who would experience high capital gains tax consequences if they sold their land. Land Trust Alliance, Have Land to Save?, How to Conserve Your Land, Additional Conservation Methods, http://www.landtrustalliance.org/conserve/have-land-to-save/how-to-conserve-your-land-1/conservation-methods (last visited Mar. 15, 2009).

55. Land Trust Alliance, supra note 54.

56. Id.
the purchase price as a charitable contribution. 57

When a land trust acquires a conservation easement, the landowner receives a tax benefit because the development restriction has decreased the value of the property. 58 To determine the amount of a deduction for donating a conservation easement to a land trust, an appraiser determines the fair market value of the property both before and after the conservation restrictions are imposed. 59 The difference between the two values represents the deductible amount. 60

3. Land Trusts Compared to Government Agencies

While landowners may donate a property interest to a governmental municipality and receive a tax deduction, 61 the proliferation of private land trusts in the past twenty-five years demonstrates the desirability of working with a private organization. 62 There is no doubt that landowners prefer the ease of working with the private sector with respect to land conservation transactions. 63

Nonprofit land trusts offer a level of service to landowners and potential donors that their governmental counterparts cannot provide. 64 Land trusts attract land donors because they, as private organizations, can handle deals quickly, flexibly, and privately. 65 Land trusts also proffer effective negotiations with varying contract provisions and knowledgeable staff members who can help a deal progress. 66

Although conserved lands often go to land trusts originally, many land trusts sell or donate the land to a state

57. Id.
59. Id.
60. Id.
63. See id. at 4.
64. See id. at 4–5.
65. See id.
66. See id.
or federal agency. Known as a “pass-through,” this type of land transfer enables land trusts and landowners to have efficient and flexible transactions while transferring the responsibility of managing and monitoring the land to a public agency. Pass-through land transfers exemplify how land trusts aim to accommodate landowners’ personal desires while ensuring that the land is regulated by an agency with plentiful resources.

C. Legislative Promulgation of Conservation Boom

The legal developments surrounding land conservation that have ensued since 1980 help explain how the practice of land preservation grew so quickly. The Internal Revenue Code (“I.R.C.”) section 170(h) and the Uniform Conservation Easement Act are the two laws that have the greatest effect on land conservation.

1. Tax Code Changes

In 1980, under President Jimmy Carter, Congress passed new tax legislation to codify permanently “the deductibility of conservation and historic preservation easement donations.” Although the contribution need not be an easement, I.R.C. section 170(h) defines a “qualified conservation contribution” as a contribution to a qualified organization exclusively for conservation purposes, granted in perpetuity. The passage of I.R.C. section 170(h) permitted a landowner to take a charitable tax deduction of up to thirty percent of her adjusted gross income for the donation of a qualified conservation contribution for the year of the transaction plus the five following years. The passage of this tax provision

67. BREWER, supra note 3, at 91.
68. See id. Private conservation deals involving large or expensive areas of land particularly benefit from government partnerships because sizeable areas of land often cover several political jurisdictions and need the resources of the taxpayer. See Endicott, supra note 62, at 6.
69. See BREWER, supra note 3, at 91.
72. J. Breting Engel, The Development, Status, and Viability of the Conservation Easement as a Private Land Conservation Tool in the Western
coincided with rising land values and an ever-growing demand for land; it was an optimal time for the government to pass tax incentives that would encourage conservation.73

2. Model Conservation Easement Statute

Although a clear factor, the revised tax code was not the sole contributor to the land trust boom.74 The early 1980s also saw the approval of the Uniform Conservation Easement Act (the "UCEA") by the National Conference of Commissioners on Uniform State Laws.75 Adopted in all but one state,76 the UCEA "established the model for state statutes to codify the conservation easement as a unique property interest"77 and immunized conservation easements from adverse common law principles.78 Although not all land trusts hold conservation easements, those that do "must conform to the requirements for easement holders imposed by the conservation easement statutes in the states in which they operate."79 Essentially, the UCEA enables a governmental or charitable organization, trust, or association whose purpose is to protect natural, scenic, or cultural resources to hold conservation easements.80

The tax code revisions and the passage of the UCEA laid the foundation for the donation of land and conservation easements. These important preliminary steps paved the way for charitable contributions of open space to take place in the private sector. Land trusts have become the convenient choice as preservers of donated land.81 As nonprofit organizations, they serve a purpose the government would otherwise have to serve and they gain the trust of the public.

---

73. Small, supra note 70, at 55.
74. Id.
75. Gustanski, supra note 4, at 11.
76. See BREWER, supra note 3, at 150. Wyoming is the only state that has not either adopted the UCEA or written a statute mirroring the provisions of the UCEA's authorization of conservation easements. Id.
77. Engel, supra note 72, at 38.
78. Id.
79. Cheever, supra note 29, at 1083–84.
81. See Endicott, supra note 62, at 4–5.
by not providing a benefit to any private shareholders.

D. Results of the Boom

1. Recent Legislation

The success of initial conservation legislation encouraged the passage of additional tax incentives. The Taxpayer Protection Act, enacted in 1997, added section 2031(c) to the tax code.\(^{82}\) This section enables a decedent’s estate to deduct up to forty percent of the conserved land’s value, capped at $500,000, from the decedent’s federal estate tax liability.\(^{83}\) Estate tax breaks invaluably benefit heirs of land who wish to keep it undeveloped but would be unable to afford the estate tax liability were the land not conserved by the decedent.\(^{84}\)

There is no doubt that much of the popularity of land conservation can be credited to the financial incentives available to landowners, in addition to pure altruism.\(^{85}\) Although the original I.R.C. section 170(h) offered appealing tax deductions to landowners who donated at least a partial property interest to a land trust, the tax incentive to donate land increased in 2006.\(^{86}\) President George W. Bush signed the Pension Protection Act of 2006, which increased the deduction to up to fifty percent of the landowner’s adjusted gross income along with an extension of the carry-forward period from five to fifteen years after the year of the transaction.\(^{87}\) In other words, a land donor can deduct up to fifty percent of his taxable income in the year he donates the land and for the following fifteen years.\(^{88}\) The new tax benefits expired at the end of 2007; however, they were renewed for an additional two years in May 2008.\(^{89}\) These tax

\(^{82}\) Small, supra note 70, at 60; I.R.C. § 2031(c) (2006).

\(^{83}\) Small, supra note 70, at 61.

\(^{84}\) See Engel, supra note 72, at 49.


\(^{87}\) See id.

\(^{88}\) See id.

incentives are set to expire at the end of 2009.\textsuperscript{90} Tax incentives, such as those offered in the Pension Protection Act, play a major role in a landowner's decision to donate conservation easements or all or part of her land in fee to land trusts.\textsuperscript{91} The tax savings realized by donating land or a conservation easement is not always the most financially wise decision, however.\textsuperscript{92} Landowners who have a relatively low income or an extremely valuable piece of land cannot maximize the financial advantage of their donation in tax deductions.\textsuperscript{93} Increasing the allowable deduction and carry-forward period demonstrates how increased incentives work to make donative land conservation appealing to a wider array of landowners. Thus, legislation that heightens permanently the amount deductible for donating such property interests is vital to the continued success of land trusts.

2. Negative Consequences

Unfortunately, income tax breaks in any form attract dishonest taxpayers who abuse the system by claiming more deductions than legally permissible. In the realm of land conservation, tax abuse results when taxpayers claim charitable contribution deductions for "amounts that exceed the fair market value of the donated easement [or land]."\textsuperscript{94} Landowners often find ways of inflating the fair market value of their land in an attempt to increase their deductions.\textsuperscript{95} Landowners have also donated conservation easements on lands not intended to be developed, for example, by restricting the development of golf courses and unusable areas of completed subdivisions.\textsuperscript{96} In other words, they have received tax deductions for restricting development that they

\textsuperscript{90} Id.
\textsuperscript{91} See Engel, supra note 72, at 40.
\textsuperscript{92} See BREWER, supra note 3, at 141.
\textsuperscript{93} See id.
\textsuperscript{95} Garrison, supra note 85, at 51.
know would never occur in the first place.

In 2003, the Washington Post published an exposé on conservation easement abuse.97 The series of articles caught the attention of Congress and the Internal Revenue Service (the "IRS"),98 and also paralleled litigation in federal court.99 One of the world's largest land trusts, The Nature Conservancy (the "Conservancy"),100 was the center of attention in Congress's investigation101 and threatened to ruin the reputation of land trusts' conservation efforts.102

III. PROBLEM: EASEMENT AND TAX ABUSE

As illustrated above, the conservation boom elevated land preservation to one of the hottest topics in environmental protection. As a result, land trusts stand out as nonprofit organizations that specialize in acquiring land and conservation easements to permanently restrict future development. In addition to a desire to protect land, grantor landowners and grantee land trusts have something else in common: income tax benefits. Abuses of the conservation system threaten both individual landowners who donate property interests and land trusts that successfully operate because of their tax-exempt status.

The following section analyzes how landowners abuse conservation easements by either obtaining an appraisal that overestimates the fair market value of the property or by placing a restrictive easement upon property that does not qualify for a tax deduction.103 The analysis will also consider

---

102. See Engel, supra note 72, at 52.
103. To receive a charitable contribution tax deduction for donating a real property interest, the I.R.C. defines a qualified real property interest as any of
the trouble the Conservancy encountered after the Washington Post exposed its unscrupulous business practices. Land trusts across the county must learn from the Conservancy's mistakes and work to maintain the legitimacy of land trusts and private land conservation. This analysis aims to reconcile how increased tax incentives can promote genuine conservation measures while also undermining it by encouraging easement abusers to wrongfully obtain tax deductions. With congressional legislation working to make the substantial income tax deductions for donors of conservation easements a permanent part of the tax code, scrutinizing the effects of such legislation is imperative.

IV. ANALYSIS: SHEDDING LIGHT ON EASEMENT AND TAX ABUSE

Investigative reporters for the Washington Post, David B. Ottaway and Joe Stephens, wrote a series of articles exposing the general abuses of land conservation and improper conduct by the Conservancy. As a result of their depiction, the Senate Joint Committee on Taxation proposed to change, or possibly do away with, the tax incentives encouraging private land preservation. The Senate Finance Committee also investigated the Conservancy with the hope of understanding the issues raised by the Washington Post with regard to federal tax benefits available to exempt organizations and donors of charitable gifts.

A. Landowners Claiming Inappropriate Deductions

Although the Washington Post articles brought considerable attention to the Conservancy, the exposé also

the following: "(A) the entire interest of the donor other than a qualified mineral interest, (B) a remainder interest, and (C) a restriction (granted in perpetuity) on the use which may be made of the real property." I.R.C. § 170(h)(1)-(2) (2006).


105. See Ottoway & Stephens, supra note 10.

106. Engel, supra note 72, at 51.

107. Id. at 52.
touched upon a number of deceptive practices employed by landowners who wanted to deduct a substantial amount from their income taxes.\textsuperscript{108} Because appraisals are inexact, it comes as no surprise that the main form of abuse stems from appraisal valuations.\textsuperscript{109} The fair market value of potentially donated land represents a main consideration for a grantor;\textsuperscript{110} the higher the appraised value of the land a grantor obtains, the larger the income tax deduction she will receive. Treasury Regulations define fair market value as "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts."\textsuperscript{111} Although this concept can be easily stated, the most prevalent factual disputes in federal taxation come from disagreements over fair market valuation\textsuperscript{112} because of the inherent subjectivity of the appraisal process.\textsuperscript{113} Each parcel of land is unique and as a result the Treasury Regulations have not set forth a specific rule for determining fair market value.\textsuperscript{114}

Although no definite rule exists for determining fair market value, there are three professionally accepted methods of estimating the value: the "Comparable Sales" (market data) approach, the "Cost" approach, and the "Income" approach.\textsuperscript{115} However, each of these methods

\begin{itemize}
\item \textsuperscript{108} See Stephens \& Ottaway, supra note 96; Stephens, Easement Abuses, supra note 104.
\item \textsuperscript{109} Thomas A. Coughlin III, Increased Tax Penalties for Valuation Overstatements, in LAND-SAVING ACTION, supra note 50, at 210, 210.
\item \textsuperscript{110} Id.
\item \textsuperscript{111} Treas. Reg. § 1.170-1(c)(1) (1960).
\item \textsuperscript{112} Coughlin, supra note 109, at 210.
\item \textsuperscript{113} Alex E. Sadler, The Inherent Ambiguity of Commercial Real Estate Values, 13 VA. TAX REV. 787, 800 (1994).
\item \textsuperscript{114} Id. at 801.
\item \textsuperscript{115} THE LAND TRUST ALLIANCE, APPRAISING EASEMENTS: GUIDELINES FOR VALUATION OF HISTORIC PRESERVATION AND LAND CONSERVATION EASEMENTS 24 (2d ed. 1990). The "Comparable Sales" approach compares the sales of similar properties recently sold in the same or similar market. Id. This approach is not reliable when there are few comparable sales from which a fair market value can be derived, which is common for properties with conservation easements. Id. The "Cost" approach, which is based on the premise "that an improved property will sell at a price reasonably related to the depreciated cost of a newly constructed version of itself," is typically inappropriate for vacant land. Id. at 26. The "Income" approach capitalizes the net operating income that a property generates at an acceptable rate. Id. at 27. When estimating the
requires making certain assumptions about the real estate market, which causes the process to be inherently ambiguous.\textsuperscript{116} If an appraisal does become the focus of tax litigation, the appraiser will testify about his or her professional qualifications and familiarity with the market of the land on which the valuation was made.\textsuperscript{117} When an appraiser lacks credibility in these areas or fails to introduce reliable evidence to substantiate the valuation, courts have shown a tendency to reject the fair market valuation.\textsuperscript{118}

The following subsections will explore the issue of inaccurate valuations specific to open space and conservation easements.

1. Examples of Early Tax Abuse

Even before donating land to a land trust became a popular method of land conservation, the IRS challenged charitable contribution deductions resulting from land donation and laid the legal groundwork for disallowing deductions based on improper appraisals.\textsuperscript{119}

In 1983, the United States Court of Appeals for the First Circuit ruled in favor of the IRS in \textit{Great Northern Nekoosa Corp. v. United States}.\textsuperscript{120} Great Northern Nekoosa Corporation ("Great Northern"), the taxpayer, donated the Allagash Falls to the State of Maine for charitable purposes in 1969.\textsuperscript{121} Great Northern had purchased the 640 acres in 1943 for $25,000.\textsuperscript{122} When Great Northern decided to donate the land, it used an expert appraiser to determine the fair market value for income tax deduction purposes.\textsuperscript{123} The appraiser determined the fair market value to be at least $1,000,000, basing his valuation on the property's possible use as a hydroelectric power plant site, even though the

value of an easement, all of the approaches should be used when possible for determining both the before and after valuations. \textit{Id.} at 24.

\textsuperscript{116} See Sadler, \textit{supra} note 113, at 803–04.
\textsuperscript{117} See \textit{id.} at 808.
\textsuperscript{118} See \textit{id.}
\textsuperscript{119} See Akers v. Comm'n, 799 F.2d 243 (6th Cir. 1986); Great Northern Nekoosa Corp. v. United States, 711 F.2d 473 (1st Cir. 1983).
\textsuperscript{120} \textit{Great Northern Nekoosa Corp.}, 711 F.2d at 475–76.
\textsuperscript{121} \textit{Id.} at 473–74.
\textsuperscript{122} \textit{Id.} at 473.
\textsuperscript{123} \textit{Id.} at 474.
United States enacted the National Wild and Scenic Rivers Act that prohibited the construction of a power plant at Allagash Falls. Conversely, the IRS's expert appraised the value of the land to be $26,240, a value that did not take into consideration a potential power site.

After the IRS assessed Great Northern with an income tax deficiency of nearly $700,000, including interest, Great Northern paid the deficiency and brought suit in federal district court for a refund. At the appellate court, Great Northern lost its appeal after failing to meet its burden of proof that "any rational prospective purchase[r]" would not take the encumbrance of the National Wild and Scenic Rivers Act into consideration when purchasing the land.

Three years later, the United States Court of Appeals for the Sixth Circuit addressed whether the fair market value of a donated parcel of land could be determined by its value if subdivided. In this case, the taxpayer landowners, the Akers, bought the Treanor Tract for $125,000 in 1965. The Akers granted a scenic easement to the Tennessee Conservation League in 1977 and an appraiser valued the land at $971,000—its value had it been divided into twenty-four lots. The IRS's expert appraised the land at a fair market value of $505,000—almost half of what the Akerses' appraiser estimated. Again, the court found for the IRS, rejecting the fair market value that considered the land's subdivided value. The court reasoned that the land conveyed prior to the easement was one parcel and that "the regulatory definition does suggest that the appropriate question is what a hypothetical Malcolm Forbes [publisher of Forbes magazine] would have paid for it as one tract, rather

124. Id.
125. Id.
126. Great Northern Nekoosa Corp. v. United States, 711 F.2d 473, 474 (1st Cir. 1983).
127. Id. at 475–76.
128. Id. at 475.
129. Id.
131. Id.
132. Id. at 244–45.
133. Id. at 245.
134. Id.
135. Id.
than what two dozen hypothetical yuppies would have paid for it as 24 ‘Ranchettes.’”

The pre-boom conservation transactions that ended with the landowners in court demonstrate the inherent blurriness of land appraisals. Gray areas in the legal system result in litigation, especially when taxpayers pursue large income tax deductions. The following sections will reveal how, as land conservation became more commonplace and well known, landowners became more creative in taking advantage of the tax system and appraisals.

2. Deceptive Practices

Some of the most lucrative and suspect tax deductions have gone to developers and golf course owners. For example, some developers who subdivide land reduce their income taxes by donating an easement restricting development on the unusable sections of a subdivision. Golf course owners have found a questionable practice that results in huge tax deductions—placing conservation easements on their fairways.

While wealthy developers and golf course owners have found ways to milk the system for substantial tax deductions, small, private landowners have also abused the system. It is not unusual “for an appraiser to assume the highest possible level of development that could be approved under local zoning and value the land under that intense level of build-out, totally without regard for whether there is sufficient and realistic market demand for the product.”

An inflated appraisal of a land’s fair market value increases the difference between it and the purchase price (if the land is sold to a land trust at a reduced price) or the value of the land

137. See Stephens & Ottaway, supra note 96; Stephens, Easement Abuses, supra note 104.
138. See Stephens & Ottaway, supra note 96. (“Luxury-home builders in North Carolina paid $10 million for a tract in the mountains, developed a third of the land, then claimed a $20 million deduction.”).
139. Stephens, Easement Abuses, supra note 104. In South Carolina, “[s]even of the most lucrative tax deductions went to the owners of golf courses, who . . . claimed deductions totaling $125 million.” Id.
140. See generally Stephens, Fairfax Case, supra note 104.
141. Garrison, supra note 85, at 51 (interviewing Stephen Small).
with development restrictions (in the case of a conservation easement), thereby enlarging the amount that can be deducted.\(^{142}\)

3. Crackdown

Since the investigative spotlight focused on conservation easement abuse, the IRS responded by placing easement donation abuses on its “Dirty Dozen” list of tax scams\(^ {143}\) and by issuing notices to warn taxpayers about the consequences regarding improper deductions for conservation easements.\(^ {144}\) In its June 30, 2004 Notice, the IRS stated that it was aware of people claiming deductions for donations of easements that do not qualify as conservation contributions, as well as taxpayers “claiming deductions for amounts that exceed the fair market value of the donated easement.”\(^ {145}\) The IRS warned that it could disallow improper deductions, impose penalties, and excise tax for such deductions,\(^ {146}\) and could also penalize appraisers for dishonest or fraudulent appraisals.\(^ {147}\)

Moreover, the IRS mandated that taxpayers claiming deductions for donating a property interest must include the appraisal with their return\(^ {148}\)—a requirement that also puts appraisers under the microscope of the IRS.\(^ {149}\) The I.R.C. has two sections relevant to the imposition of penalties for an appraiser who participates in a gross valuation overstatement for any deduction\(^ {150}\) or aids or abets in the understatement of a person’s tax liability.\(^ {151}\) Despite these specific consequences, both sections impose a penalty of a mere $1000

\(^{142}\) See, e.g., id. (explaining how one can inflate fair market value by considering the maximum level of development that zoning would allow even in a remote location where demand for such a development does not exist).


\(^{145}\) I.R.S. Notice IR-2004-86, supra note 94.

\(^{146}\) I.R.S. Notice 2004-41, supra note 98.

\(^{147}\) See I.R.S. Notice IR-2004-86, supra note 94.

\(^{148}\) Garrison, supra note 85, at 51.

\(^{149}\) Id.


\(^{151}\) See I.R.C. § 6701.
for an inaccurate appraisal.\textsuperscript{152}

4. \textit{The IRS Takes a Stand}

In 2006, the tax court ruled, for the first time, to completely throw out a conservation easement and the subsequent income tax deduction.\textsuperscript{153} \textit{Turner v. Commissioner} stands as the first major success for the IRS since it vowed to crack down on easement abuse.\textsuperscript{154}

James D. Turner, a real estate lawyer, and his wife acquired the 29.3-acre Grist Mill property through several transactions in 1997 and 1998 for $2,550,000.\textsuperscript{155} President George Washington owned and operated Grist Mill beginning in 1771.\textsuperscript{156} Accordingly, the property is within the Woodlawn Heights historical overlay district near Mount Vernon, Virginia.\textsuperscript{157} Over half of the Grist Mill property is part of a floodplain and therefore unable to be developed residentially, although all of the property is zoned for residential use.\textsuperscript{158}

Despite floodplain restrictions that limited residential development to thirty homes, Turner and his colleagues characterized the land as being able to contain up to sixty-two residences (as if the entire property, floodplain included, could be developed).\textsuperscript{159} Turner began talks with the Mount Vernon Ladies' Association ("MVLRA"), a private nonprofit organization and a concerned neighbor, about the imposition of a conservation easement should the land be developed.\textsuperscript{160} As negotiations developed, MVLA believed that the land had the potential to contain more than sixty homes (based on Turner's earlier mischaracterization), which it did not want to see happen.\textsuperscript{161} Turner agreed to donate a conservation easement.

\textsuperscript{152} See id.; I.R.C. § 6700. Under § 6700, the appraiser may only be penalized the amount of income derived for the appraisal if that amount is less than $1000. I.R.C. § 6700(a)(2)(B)(1).
\textsuperscript{154} Stephens, \textit{Fairfax Case}, supra note 104.
\textsuperscript{155} Turner, 126 T.C. at 301.
\textsuperscript{156} Id. at 302.
\textsuperscript{157} Id.
\textsuperscript{158} Id.
\textsuperscript{159} Id. at 303, 306.
\textsuperscript{160} See id. at 302, 305–06.
easement to Fairfax County\textsuperscript{162} that would limit the number of homes to only thirty (the actual number of homes that could be built) for the benefit of the historic and scenic character of Grist Mill.\textsuperscript{163} On the same day in 1999 that Turner executed the conservation easement to Fairfax County, he sold the same 29.3 acres to a developer for $2,800,000 (slightly more than what Turner had paid the previous year).\textsuperscript{164}

For the 1999 income tax year, Turner claimed an income tax deduction based on the appraised value of the land at $3,120,000—a value wrongly based on the assumption that all of the property could have been developed, including the area hindered by the floodplain.\textsuperscript{165} The United States Tax Court held that Turner was not entitled to the deduction because the attempted grant did not meet the requirements of section 170(h)(4)(A) in serving a conservation purpose.\textsuperscript{166} Therefore, it did not qualify as a conservation easement.\textsuperscript{167} The court found that the attempted conservation easement did not preserve open space or any historically important land because Turner essentially developed the land as was allowable by the floodplain classification.\textsuperscript{168} Nothing prohibited the new landowners from re-zoning the land, building homes twice the size of those planned for development, or obstructing scenic views.\textsuperscript{169} In addition to disallowing Turner's income tax deduction of $342,781, the judge also ruled for a penalty of $56,000.\textsuperscript{170}

Turner's improper transaction epitomizes how landowners can exploit the benefits of conservation easements. In this case, Turner's dishonesty not only cost him the disqualification of the easement, but also a stiff

\textsuperscript{162} Although not a private land trust, Fairfax County is a qualified organization under I.R.C. § 170(h)(3). \textit{Id.} at 312.
\textsuperscript{163} \textit{Id.} at 306, 309.
\textsuperscript{164} \textit{Id.} at 307–09.
\textsuperscript{165} \textit{Id.} at 309.
\textsuperscript{166} \textit{Id.} at 317.
\textsuperscript{168} \textit{Id.}
\textsuperscript{169} \textit{Id.} at 314.
\textsuperscript{170} Internal Revenue Code section 6662(a) provides that "if any portion of an underpayment is due to negligence, then a taxpayer will be liable for a penalty equal to [twenty] percent of the underpayment that is attributable to negligence." \textit{Turner}, 126 T.C. at 318 (citing I.R.C. § 6662(a) (2006)); Stephens, \textit{Fairfax Case, supra} note 104.
penalty. Unfortunately, a developer built twenty-nine homes on the historic land and no conservation took place because the homes built corresponded to the number allowed under the floodplain restriction. Since the legality of the tax deduction represented the issue before the court, the court could do no more than uphold the IRS's tax deficiency and penalize Turner. This serves as both a major hindrance to conservation efforts and a strong motivator to promote proper appraisals. The next section exposes the potential wrongdoings of a specific land trust, and discusses how land trusts, as nonprofit organizations, should focus on the preservation of the land trust movement itself.

B. Land Trusts in Trouble—Learning from The Nature Conservancy

While private landowners who benefit from inflated land valuations face consequences from the IRS, land trusts also face repercussions for their misdeeds. Land trusts play an instrumental role in the conservation process and aside from facilitating inappropriate transactions, land trusts are not insulated from their own internal issues. The exposé published in the Washington Post highlighted the unethical and at times illegal practices of the Conservancy uncovered by the Senate Finance Committee's investigation. The most egregious practices involved deals with the organization's own board members or corporate partners.

1. Conflicts of Interest

Prior to the Washington Post series, the Conservancy routinely benefited its trustees and supporters by buying scenic properties, restricting development through a conservation easement (although such easements often did not restrict residential building) and then selling the land at a discounted rate to the trustees and supporters. These buyers would then donate cash to the Conservancy for a
handsome income tax deduction.\textsuperscript{176} These transactions resulted in little, if any, costs to the Conservancy, but provided acreage to add to its list of protected lands and made for happy supporters and trustees.\textsuperscript{177}

The board members of the Conservancy, who work for a variety of corporations such as General Motors, Georgia-Pacific,\textsuperscript{178} Orvis Services Co.,\textsuperscript{179} and S.C. Johnson & Sons Inc.,\textsuperscript{180} also have used their ties to the Conservancy to benefit themselves and their companies while improving the Conservancy's apparent success.\textsuperscript{181} The Conservancy used the relationships with certain board members and their corporations to obtain discounts on the purchases of land, products, legal assistance, and development rights.\textsuperscript{182} Although the Conservancy disclosed all such business deals to the IRS and had the board members recuse themselves from voting on related transactions, the Conservancy reported that eleven board members or their corporations had dealt with the Conservancy in one or more financial transactions since 1998.\textsuperscript{183} While these practices may not have been entirely unethical, because the Conservancy is a nonprofit corporation, it must protect itself from self-dealing that could lead to the revocation of its tax-exempt status.\textsuperscript{184}

2. \textit{Corporate Partnerships}

In addition to using corporate board members to secure low-cost transactions, the Conservancy also profited from its corporate ties by selling its logo to give corporations a kinder
image. The Conservancy enabled its board members’ companies to use the Conservancy logo on its products for a six-figure fee. The addition of the Conservancy logo on product packaging, such as on the boxes for General Mills Nature Valley granola bars, leads consumers to believe that they are buying environmentally friendly products, when, in reality, all General Mills did was write a check to the Conservancy. As an offended consumer activist opined, displaying the rented Conservancy logo “does not guarantee the product inside is more environmentally friendly than the next brand on the supermarket shelf” and optimizes the conflicts of interests between the Conservancy and its board members.

Having originally worked to increase the Conservancy’s corporate ties, David Morine, a former head of land acquisition, regrets having allowed corporate executives to serve on the board. Morine blames the Conservancy’s focus on the corporate dollar on the “carnivorous” tendencies of the executives and their propensity to take charge.

3. Effect on Land Trusts

The corporate ties that the Conservancy established reveal its evolution from a private land conservation organization into a corporate one. With its sights set on profiting while buying and conserving land, the Conservancy became more of a “free market conservation juggernaut” with unethical practices rather than an exemplary representation of nonprofit land trusts. The size and structure of the Conservancy put it on a level of its own compared to other land trusts. Despite the Conservancy having a much broader scope and breadth of assets than most land trusts, the Conservancy’s tarnished reputation formed a

185. See id.
186. Id.
187. See id.
188. Id.
189. See id.
190. See Ottoway & Stephens, supra note 10.
191. Engel, supra note 72, at 52.
192. Id.
193. Id. at 52–53.
dark cloud over land conservation.\textsuperscript{194} The *Washington Post* and the Senate Joint Committee on Taxation did an injustice to most local and regional land trusts by equating them with the Conservancy.\textsuperscript{195} The Senate committee even went so far as to propose an elimination of charitable contribution deductions relating to personal residence properties.\textsuperscript{196} Although the fallout from the Conservancy debacle threatened the continued success of land conservation, the legislature did expand tax incentives in 2006 with the Pension Protection Act and "put an end to the scare caused by the [Conservancy] scandal and the ensuing [Joint Committee on Taxation] proposal."\textsuperscript{197}

V. PROPOSAL: STEPS NEEDED TO PREVENT ABUSE

In light of the tax abuse and dishonest appraisal practices described above, this comment proposes a number of ways to avert further mishandlings. The following proposal recommends legislation, internal practices for land trusts, and government enforcement.

A. Legislation

1. Confidence in the Appraisal Process

Although they may be encouraged mostly by altruism, landowners often decide to donate land or a conservation easement to gain tax benefits. Similarly, land trusts operate as nonprofit organizations and are therefore exempt from income taxation. Even though donations of real property are between a grantor landowner and a grantee land trust, the philosophy behind land conservation is that it should benefit the public at large. Land trusts must adhere to their missions of conservation for the greater good while contracting with landowners in a way that encourages charitable giving.

Fair market valuation issues lie central to the problem of maximizing both tax deductions and charitable donations. A

\begin{itemize}
  \item \textsuperscript{194} See \textit{id.}\
  \item \textsuperscript{195} \textit{Id.}\
  \item \textsuperscript{196} \textit{Id.} at 51.\
  \item \textsuperscript{197} Engel, \textit{supra} note 72, at 54.
\end{itemize}
high appraisal will enable the landowner to take more of a deduction and cause the land trust to pay more in a bargain sale. With the interested parties having different hopes for the appraised fair market value, the transaction's outcome is largely dependent upon the appraiser. The importance of having an objective appraiser cannot be stressed enough. The land acquisition process will progress smoothly if both parties (landowner and land trust) believe that the appraisal is objective and accurate.

Very few universal guidelines currently exist in the appraisal process. While individual states may have standards of their own, nationwide rules that are clear and realistic to implement are necessary. The United States Department of the Interior has proposed the Cooperative Conservation Enhancement Act (the "CCEA"), which if passed, would lessen the red tape in federal partnerships with landowners who wish to conserve their land. This promotion of government partnerships aims to encourage conservation while also implementing more government oversight.

Although oversight may help lessen some abusive practices such as inaccurate appraisals, government intervention may lack appeal to potential donors and land trustees. Transactions with land trusts are so popular because they provide privacy and efficiency. The CCEA aims to reduce barriers to partnering with the government. However, working with the government is inherently bureaucratic and arduous. The federal government thus should propose legislation that sets standards, while keeping the federal government's hands out of the transactions. For example, Congress must create specific rules regarding the appraisal process, and more specifically, the hiring and qualifications of appraisers and requirements for the number and review of appraisals.

Congress can help prevent appraisal abuse by modifying

---

200. See id.
the I.R.C. to require more objectivity in the appraisal process. The I.R.C. currently only requires that a taxpayer complete and submit one appraisal with his tax return.\textsuperscript{201} Therefore, legislation should require that in every transaction, two separate appraisers conduct two individual appraisals. The appraisers should then agree to the most accurate amount. Legislation should also require that the acquiring party, whether a private land trust or a governmental agency, hire the appraisers for a flat fee. Because the landowner may collude with an appraiser to determine a high fair market value in order to secure a larger tax break, appraisers hired by the land trust are more likely to be unbiased. Requiring land trusts to hire the appraisers would also increase the likelihood that the appraisers would be familiar with open space fair market values and other conservation easements in the area.

Additionally, the current penalty for appraisers ($1000 at most)\textsuperscript{202} is not substantial enough to deter gross overstatements. Not only should legislation require new and specific guidelines for obtaining appraisals, but the penalties for the appraisers themselves should also be increased for fraudulent valuations.

\textbf{2. Land Trusts Responsible for Reviewing and Posting Appraisals}

Legislation should require that private land trusts and state agencies report any information about the appraisers used in land transactions along with all appraisal amounts to the IRS or the Department of the Interior. Legislators may also consider requiring that appraisals be made available to the public to encourage accuracy and accountability. Although landowners appreciate the privacy inherent in transacting with private land trusts, they may need to sacrifice this advantage in an attempt to uphold the integrity of land conservation.

\textsuperscript{201} See IRS, \textit{Publication 561: Determining the Value of Donated Property} 11 (Apr. 2007).

B. Land Trusts: Stick to the Mission

The Conservancy's poor governance taught an important lesson to all land trusts. Land trusts are nonprofit organizations that aim to protect land for the sake of the environment and the public. Corporate board membership should be discouraged or at least deemphasized. Corporate connections are likely to lead to incentives and benefits that draw attention away from the mission of open space conservation and could ultimately lead to possible disqualification of tax-exempt status.

Self-dealing and insider transactions taint the integrity of nonprofit organizations and must be avoided. Serving as the heart of land conservation efforts, land trusts must make their mission statements known and publicize the ways in which they carry out such missions. The proliferation of land trusts since the 1980s demonstrates their instrumental role in land preservation. The Conservancy's problems illustrate how land trusts' reputations can be hindered when they draw the negative attention of the IRS. Land trusts' missions must remain central to all transactions and should not be discounted or manipulated in favor of appeasing corporate executives serving as board members.

C. Governmental Enforcement

Lastly, the government should better arm itself with enforcement capabilities. The IRS's crackdown on inaccurate tax deductions should continue, especially in the wake of new legislation. Since the deductible amounts increased in 2006 and may be renewed permanently, the IRS is going to see more charitable contributions to land trusts in the future. With increased incentives, a responsible government must have the resources to enforce the laws and uphold the integrity of the tax system. While the IRS can revoke the tax-exempt status of land trusts after improprieties have occurred, the preceding legislative proposals aim to prevent abuse of the system.

VI. CONCLUSION

Land conservation in the United States would not be what it is today without the existence of private land trusts. Land trusts play an integral role in the land preservation
process, so much so that any threats to their integrity could impact conservation efforts substantially in this country. The vulnerabilities of conservation transactions, specifically land appraisal inaccuracies and tax abuse, taint the process and hinder the work of land trusts. Land conservation can continue to be a success in the United States, especially with governmental support of increased benefits to charitable donors of land. Land trusts must combat deficiencies in the system by keeping passionate board members who do not hold controversial ties to corporations, limiting self-dealing transactions, and espousing mission statements aimed at environmental protection and public accessibility to scenic open space. In conjunction with land trust veracity, proper legislation addressing the appraisal process and government enforcement of the tax laws will support an upstanding image of land conservation and charitable contributions. If the reputations of land trusts remain strong and tax laws promote land donation, land conservation will continue to flourish.