No. 22-___

In the Supreme Court of the United States

OAKBROOK LAND HOLDINGS, LLC,
WILLIAM DUANE HORTON, Tax Matters Partner,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITION FOR WRIT OF CERTIORARI

David W. Foster
Counsel of Record
Armando Gomez
SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, D.C. 20005
(202) 371-7000
david.foster@skadden.com

Michelle Abroms Levin
Gregory P. Rhodes
Logan C. Abernathy
DENTONS US LLP
305 Church Street SW
Suite 800
Huntsville, AL 35801

Isabelle K. Farrar
SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP
500 Boylston Street
Boston, MA 02116

Counsel for Petitioner

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

Question Presented

This petition presents a direct conflict regarding whether the Treasury Department violated the Administrative Procedure Act (the "APA") by failing to respond to comments from the public when promulgating a regulation governing charitable donations.

Petitioner donated a conservation easement on land that it owned to a qualified charity, and it claimed the corresponding income tax deduction. The IRS—invoking 26 C.F.R. § 1.170A-14(g)(6)(ii) (the "Proceeds Regulation")—denied the entire deduction. The Proceeds Regulation requires easement deeds to guarantee that the charity will receive a specified portion of the proceeds in the unlikely event that the easement is judicially extinguished. The IRS determined that Petitioner's easement did not guarantee a sufficient portion of the proceeds to the charity.

When Treasury proposed the Proceeds Regulation, multiple commenters identified problems with the regulation (including the very issue on which the Tax Court disallowed Petitioner's deduction) and explained why those problems mattered. Treasury did not respond to—or even acknowledge—the comments.

A divided Sixth Circuit panel held that Treasury's failure to respond to the comments did not violate the APA. The Sixth Circuit acknowledged that its holding conflicts with a unanimous published Eleventh Circuit decision that the same regulation violated the APA.

The question presented is: Whether Treasury's failure to respond to comments raising concerns about the Proceeds Regulation, 26 C.F.R. § 1.170A-14(g)(6)(ii), violated the Administrative Procedure Act?

Parties to the Proceedings

Petitioner Oakbrook Land Holdings, LLC, William Duane Horton, Tax Matters Partner, was the petitioner in the Tax Court and the appellant in the Sixth Circuit.

Respondent Commissioner of Internal Revenue was the respondent in the Tax Court and the appellee in the Sixth Circuit.

Rule 29.6 Disclosure Statement

Petitioner Oakbrook Land Holdings, LLC does not have a parent corporation. There is no publicly held company that owns 10% or more of Petitioner's stock.

Related Proceedings

The proceedings directly related to this proceeding are:

- *Oakbrook Land Holdings, LLC, William Duane Horton, Tax Matters Partner v. Commissioner of Internal Revenue*, No. 20-2117 (6th Cir. March 14, 2022)
- *Oakbrook Land Holdings, LLC, William Duane Horton, Tax Matters Partner v. Commissioner of Internal Revenue*, No. 5444-13 (United States Tax Court May 12, 2020)

TABLE OF CONTENTS

Page

TABLE OF APPENDICES

TABLE OF AUTHORITIES

Page(s)

CASES:

OTHER AUTHORITIES:

PETITION FOR WRIT OF CERTIORARI

This case presents a clear and intractable conflict over an important question of administrative law. The Sixth Circuit and the Tax Court divided internally on the question, and the Sixth Circuit acknowledged that its decision created a conflict with the Eleventh Circuit's unanimous decision on the same question. *Compare* App. 2a-6a and 61a-170a *with Hewitt v. Commissioner*, 21 F.4th 1336 (11th Cir. 2021). This Court should grant certiorari to correct the Sixth Circuit's and the Tax Court's flawed application of the Administrative Procedure Act, 5 U.S.C. § 551 et seq., and to restore uniformity to administrative agency obligations to respond to public comments.

Congress amended the Internal Revenue Code in 1980 to encourage land conservation by providing an income tax deduction for the value of conservation easements donated to a qualifying charitable organization. 26 U.S.C. § 170(h). Congress placed a number of restrictions on this deduction, including that the easement's conservation purpose must be "protected in perpetuity." *Id.* § 170(h)(5)(A).

However, after the donation, an unexpected change in the conditions surrounding the land could occur that would make continued conservation impossible or impractical, leading to judicial extinguishment of the easement. (For example, the government could condemn some or all of the land to build a school or road.) If that happens, how is the charitable organization compensated after extinguishment? Congress did not answer this question in the statute.

In 1983, Treasury proposed a large package of regulations to address the conservation easement income tax deduction. Qualified Conservation Contribution; Proposed Rulemaking, 48 Fed. Reg. 22,940 (May 23, 1983); App. 217a. Throughout the regulations, and in the subparagraph addressing the possibility of judicial extinguishment, Treasury balanced at least three policy objectives: (1) encouraging donations of conservation easements given "that conservation easements now play an important role in preservation efforts," (2) satisfying "the need of potential donors to be secure in their knowledge that a contemplated contribution will qualify for a deduction," and (3) ensuring that "the conservation purpose is protected in perpetuity." S. Rep. No. 96-1007, at 9, 13 (1980).

There were many ways that Treasury could have struck this balance with respect to the possibility of extinguishment, such as (1) deeming the possibility sufficiently remote so as not to implicate the perpetuity requirement, (2) clawing back the tax deduction to the extent of any proceeds received by the donor, (3) allowing landowners and charities to negotiate over this point, (4) allowing state law to dictate the relative property rights of the landowner and the charity, or (5) requiring that the donor agree to include a formula in the easement deed that would specify how to share some or all of the post-extinguishment proceeds with the charity. If it chose option (5), Treasury confronted numerous policy choices in selecting the terms of the formula, such as whether and how to account for any landowner improvements made to the property after the donation.

The regulation that Treasury proposed deferred to state law if the state provided that the landowner would be entitled to the full proceeds. App. 223a ("unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction"). Otherwise, the regulation required that the donor agree at the time of the donation to provide a specified portion of the proceeds to the charity. App. 222a-223a.

Treasury received more than 700 pages of comments from 90 commenters on the proposed package of regulations, thirteen of whom specifically expressed concern with what is now the Proceeds Regulation, 26 C.F.R. § 1.170A-14(g)(6)(ii). *See* App. 8a; *see also* App. 137a-138a (Holmes, J., dissenting). Many of the commenters were conservation organizations that raised a variety of issues with Treasury's policy choices reflected in the proposed rule, including two that are relevant here: "Why did Treasury choose to require that a donee receive a proportionate share rather than a fixed sum if the easement is extinguished or condemned? And why did Treasury choose to require that a donee share in the value added to the property by later improvements to it?" App. 138a (Holmes, J., dissenting).

The New York Landmarks Conservancy identified specific "inequities" with the proposed Proceeds Regulation and argued that it "contain[s] problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of these provisions." App. 226a; 228a. It argued that "the proposed provisions would thwart the purpose of the statute by deterring prospective donors." App. 226a. It included a mathematical example highlighting the proposed formula's "fail[ure] to take into account that improvements may be made thereafter by the owner which should properly alter the ratio." App. 227a. Other commenters identified different potential problems with the proposed regulation and requested that Treasury remove it altogether. *See* App. 230a-242a.

When it issued the final regulations, Treasury provided no response to, or acknowledgement of, these comments. *See* Income Taxes, Qualified Conservation Contributions, 51 Fed. Reg. 1496 (Jan. 14, 1986); App. 243a-252a. The statement of basis and purpose—a mere two pages (six columns) of the Federal Register—accompanying the final regulations did not even mention the Proceeds Regulation. And it specifically asserted that the notice-and-comment requirements of the APA "did not apply." App. 251a-252a.

In the absence of any response from Treasury, or justification for its policy choices, a leading conservation organization developed a model easement deed, used by thousands of donors to conserve tens of millions of acres of land, that contained a provision that allows landowners to retain any post-extinguishment proceeds attributable to post-donation improvements made to the land. In 2016, the IRS began denying the entire charitable deduction for any easement donation by taxpayers who used the model deed. As one Tax Court opinion in this case put it, the IRS is denying deductions based on "future hypothetical proceeds from a future hypothetical extinguishment." App. 172a; *see also* Nancy Ortmeyer Kuhn, *A Split in the Circuits: Will Supreme Court Take Up Easement Challenge?*, Bloomberg Law (Apr. 5, 2022), https://news.bloomberglaw.com/environment-and-energy/a-split-in-the-circuits-will-supreme-court-take-up-easement-challenge (describing the "'gotcha' quality of the IRS' current position" given that "[t]here is no evidence that any proceeds have actually been distributed utilizing the proceeds regulation's formula or the taxpayers' easement deeds' formulas").[1]

In 2008, Oakbrook agreed to conserve approximately 106 acres of ridgeline property on White Oak Mountain outside Chattanooga, Tennessee. *See* App. 9a. The Southeast Regional Land Conservancy used a model deed to impose the necessary restrictions on Oakbrook's land. App. 176a. The IRS denied Oakbrook's tax deduction, and just before trial the IRS asserted that Oakbrook's donation violated the Proceeds Regulation. Oakbrook argued that Treasury's failure to consider the comments that it received regarding the proposed Proceeds Regulation violated the APA.

The Tax Court considered whether Treasury's failure to address the comments on the proposed Proceeds Regulation violated the APA. Following a vote by seventeen of the court's active judges, a majority of the Tax Court upheld the regulation in an opinion by Judge Lauber. App. 61a. Judges Toro and Holmes authored separate opinions explaining why the regulation violated the APA's procedural requirements. App. 89a (Toro, J., concurring in the result); App. 131a (Holmes, J., dissenting).

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[1] The land use restrictions in a donated easement remain binding forever under state law whether or not the IRS allows the federal income tax deduction that Congress promised.

The Tax Court denied Oakbrook's deduction and also applied its holding to other cases presenting the same issue, including *Hewitt v. Commissioner*, which involved land conservation in Alabama. Oakbrook and the Hewitts filed separate appeals in the Sixth and Eleventh Circuits, respectively, arguing that the Proceeds Regulation was invalid.

The Eleventh Circuit, in a unanimous opinion by Judge Lagoa, held that the Proceeds Regulation "is arbitrary and capricious under the APA for failing to comply with the APA's procedural requirements and is thus invalid." *Hewitt v. Commissioner*, 21 F.4th 1336, 1350 (11th Cir. 2021).

But the Sixth Circuit, in an opinion by Judge Moore, found *Hewitt* "unpersuasive" and concluded that Treasury was not required to respond to the comments on the Proceeds Regulation. App. 27a. The Sixth Circuit held that Treasury was not required to respond to the comments that it received because the comments "did not engage with [the] perpetuity requirement and whether the rule served this end." App. 23a. As Judge Guy explained in his concurring opinion, this rationale conflicts with *Hewitt* and with decisions from other Courts of Appeals, including *United States v. Nova Scotia Food Products Corp.*, 568 F.2d 240 (2d Cir. 1977) and *Carlson v. Postal Regulatory Commission*, 938 F.3d 337 (D.C. Cir. 2019). *See* App. 43a-50a (Guy, J., concurring in the judgment).

This Court has held that the APA requires administrative agencies to "consider and respond to significant comments received during the period for public comment." *Perez v. Mortg. Bankers Ass'n*, 575 U.S. 92, 95 (2015). Where agencies do not comply with this requirement, a "reviewing court shall * * * hold unlawful and set aside" the resulting regulation. 5 U.S.C. § 706(2)(A).

The question of when a comment is sufficiently significant to require an agency response affects not only Treasury and the IRS but also all other administrative agencies that promulgate legislative rules—and the members of the public that they regulate. This case thus has implications far beyond the tax context.

Absent this Court's intervention, other administrative agencies will invoke the Sixth Circuit's decision to support post-hoc justifications for their failure to respond to comments and thereby unduly narrow their obligation to interact with the regulated public. There is no justification for reducing the accountability of administrative agencies to the public in this manner.

As matters now stand, hundreds if not thousands of taxpayers who made charitable donations to conserve millions of acres of land, as encouraged by Congress, find themselves in financial limbo. The Tax Court is deferring decision in many of their cases, including those appealable to other Courts of Appeals, pending resolution of the split in authority. Because the various opinions from the Tax Court, Eleventh Circuit, and Sixth Circuit have fully debated the relevant issues of administrative law, the question presented is ripe for review by this Court. The Court should grant certiorari to determine whether Treasury's failure to respond to comments invalidates the Proceeds Regulation.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Sixth Circuit is reported at 28 F.4th 700 and reproduced at App. 2a-60a. One opinion of the Tax Court is reported at 154 T.C. 180 and reproduced at App. 61a-170a. Another opinion of the Tax Court, T.C. Memo. 2020-54, is not reported, but is reproduced at App. 171a-207a.

JURISDICTION

The United States Court of Appeals for the Sixth Circuit rejected Oakbrook's challenge to 26 C.F.R. § 1.170A-14(g)(6)(ii) in a decision rendered on March 14, 2022. The court denied a petition for rehearing en banc on July 6, 2022. App. 1a. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATION INVOLVED

The statutes involved are 5 U.S.C. §§ 553 and 706 and 26 U.S.C. § 170(h).

The regulation involved is 26 C.F.R. § 1.170A-14(g)(6)(ii), which provides in relevant part:

> **(ii) *Proceeds.*** * * * [F]or a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time. * * * For purposes of this paragraph (g)(6)(ii), that proportionate value of the donee's property rights shall

> remain constant. Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

STATEMENT OF THE CASE

A. Treasury's Proposed Rulemaking

Congress revised the Internal Revenue Code in 1980 to encourage private land conservation by allowing a charitable contribution deduction for gifts of qualified conservation contributions, *i.e.*, donations of conservation easements to charity. Congress imposed a number of requirements on tax deductions for these gifts, one of which was that the conservation purpose of the gift be "protected in perpetuity." 26 U.S.C. § 170(h)(5)(A).

In 1983, Treasury published a notice of proposed rulemaking on the income tax deduction for conservation easements. The notice cited House and Senate Committee reports on the 1980 legislation as having "provided, for the first time, an in-depth statement of congressional intent concerning the donation of partial interests for conservation purposes (H.R. Rep. No. 96-1278, S. Rep. No. 96-1007)." App. 219a. Treasury stated that "[t]he regulations reflect the major policy decisions made by the Congress and expressed in these committee reports." *Id.*

The Report of the Senate Committee on Finance that Treasury cited recognized that "conservation easements now play an important role in preservation efforts." S. Rep. No. 96-1007, at 9 (1980). Given "the need of potential donors to be secure in their knowledge that a contemplated contribution will qualify for a deduction" the report instructed that "the committee expects that regulations under this section will be classified among those regulation projects having the highest priority." *Id.* at 13.

The proposed regulations consisted of "10 paragraphs, 23 subparagraphs, 30 subdivisions, and 21 examples" regarding this charitable contribution deduction. App. 69a. "One of these 23 subparagraphs became" the Proceeds Regulation, 26 C.F.R. § 1.170A-14(g)(6)(ii). App. 69a-70a. It mandated that landowners agree in advance to grant a portion of the proceeds from any sale or exchange following a future judicial extinguishment to the charity.

Treasury received more than 700 pages of public comments from 90 commenters and held a five-hour hearing at which thirty members of the public spoke. App. 70a, 117a (Toro, J., concurring in the result).

B. The Comments Treasury Received

Thirteen of the 90 submitted comments addressed the proposed Proceeds Regulation, including two key questions that are relevant here. "Why did Treasury choose to require that [the donee charity] receive a proportionate share rather than a fixed sum if the easement is extinguished or condemned? And why did Treasury choose to require that a donee charity share in the value added to the property by later donor landowner improvements?" App. 138a (Holmes, J., dissenting).

The New York Landmarks Conservancy ("NYLC") raised these questions in a five-page comment letter. *See* App. 224a-229a. NYLC stated that the proposed judicial extinguishment provisions "contain problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of these provisions." App. 226a. It said that "the proposed provisions would thwart the purpose of the statute by deterring prospective donors." *Id.* NYLC identified four specific "inequities" caused by the provisions. App. 228a. One of those inequities was that the "formula fails to take into account that improvements may be made thereafter by the owner which should properly alter the ratio." App. 227a. It demonstrated this problem by applying values to an example Treasury had proposed regarding a different issue elsewhere in the proposed regulations. *See* App. 227a-228a. NYLC posited that, in Treasury's example, the owner of Greenacre, land whose fair market value was $100,000, donated an easement to charity to protect the scenic view of a nearby national park, resulting in a 10% reduction in the value of Greenacre. Thereafter, the owner spends $2 million on the construction of homes as contemplated by Treasury's example. If the easement were subsequently extinguished, the proposed Proceeds Regulation would require the charity to receive 10% of all of the proceeds, including any proceeds attributable to the homes. If the landowner had borrowed money to construct the improvements, its share of the proceeds might be insufficient to repay the loan. NYLC said "[t]his would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization." App. 228a.

The Landmarks Preservation Council of Illinois ("LPCI") explained that the Proceeds Regulation "create[s] a potential disincentive to the donation of easements" because the Proceeds Regulation could leave a building owner in a situation where the proceeds he receives from a subsequent sale are insufficient to pay the donee and third parties, such as lenders. App. 240a. As an alternative, the LPCI suggested that the issue of post-extinguishment proceeds "should not be treated in the regulations, but should be negotiated, defined, and incorporated by the donor and donee into the conservation right document on a property by property basis." App. 241a.

The Land Trust Exchange's comments identified similar problems and observed that "[t]his section may result in donors and donees having to pay real estate transfer taxes." App. 232a. As an alternative, the Land Trust Exchange suggested "the tax benefit rule and the remote future event rule should make this section unnecessary."[2] *Id.*

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[2] The remote future event rule in the proposed and final regulations provides that "[a] deduction shall not be disallowed * * * merely because the interest which passes to, or is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible. * * * For example, a state's statutory requirement that use restrictions must be rerecorded every 30 years to remain enforceable shall not, by itself, render an easement nonperpetual." App. 222a, 253a.

The Trust for Public Land stated, "[w]e have serious doubts whether the provision for the allocation of the [sale proceeds] following extinguishment of an easement could be enforced against anyone other than the original donor of the easement, if that is what is intended." App. 242a. This commenter also suggested: "[W]e think this provision goes further than the regulations need to go. The remote future event rule of §1.170A-13(g)(2) should suffice." *Id.*

Other commenters, including the Maine Coast Heritage Trust and the Nature Conservancy, suggested that the rule needed more clarity and that donee charities should be entitled to both the original proportionate value and any subsequent increase in value attributable to market forces. *See* App. 233a-237a.

C. The Statement of Basis and Purpose

Treasury published the final regulations in the Federal Register on January 14, 1986. Income Taxes, Qualified Conservation Contributions, 51 Fed. Reg. 1496 (Jan. 14, 1986); *see* App. 243a-252a. It began its two-page (six column) statement of basis and purpose with a boilerplate statement that it was issuing the regulations "[a]fter consideration of all comments." App. 244a. And then it gave no response whatsoever to any of the comments on the Proceeds Regulation. Indeed, it did not even mention the Proceeds Regulation.

Instead, the preamble stated that "the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public comment procedure requirement of 5 U.S.C. 553 did not apply."[3] App. 251a-252a.

D. The Land Trust Alliance Model Deed

If Treasury had agreed with the comments, it could have deleted the Proceeds Regulation or modified it to address the identified inequities. If Treasury had disagreed with the comments, it could have said so and explained why. Either way, taxpayers considering whether to conserve their land would have adjusted their behavior accordingly.

But Treasury remained silent.

In 2005, the Land Trust Alliance, a national land conservation organization that represents more than 1,000 member land trusts, published the second edition of The Conservation Easement Handbook (the "Handbook"). Elizabeth Byers & Karin Marchetti Ponte, The Conservation Easement Handbook (2d ed. 2005). When allocating proceeds, the Handbook's model excludes "any increase in value after the date of

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[3] This reflects Treasury's longstanding practice of claiming nearly all of its regulations are interpretative. *See* Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727, 1729 (2007) ("Treasury acknowledges that APA section 553 governs its various regulatory efforts. Treasury also contends, however, that most Treasury regulations are interpretive in character and thus exempt from the public notice and comment requirements by the APA's own terms." (footnote omitted)).

this grant attributable to improvements not paid for by Holder" from the value of the property. *Id.* at 463. The Handbook explains that the regulations do not address "appreciation in value due to improvements," and that "allocation [consistent with the model deed] * * * is certainly called for as a matter of basic fairness." *Id.* at 464.

As a result, this is a "clause commonly found in easements, particularly in the southeastern part of the country." App. 172a.

Treasury's silence even infected the IRS. Just three months before Oakbrook donated its easement as described below, the IRS released to the public a private letter ruling interpreting the Proceeds Regulation to permit proceeds attributable to post-donation improvements to be excluded from the pool of proceeds that must be divided between the landowner and the charity. *See* I.R.S. P.L.R. 200836014 (dated June 3, 2008, and released to the public on September 5, 2008).[4]

E. Oakbrook's Easement Donation

Oakbrook's founder Duane Horton grew up in the Chattanooga, Tennessee area. After founding a successful construction business, he expanded into real estate development. App. 173a. In 2007, he formed Oakbrook Land Holdings, LLC to purchase and develop an overgrown 143-acre property outside Chattanooga, Tennessee on White Oak Mountain, a

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[4] Private letter rulings are evidence of the IRS's administrative practice on a particular issue but are not binding authority. *Rowan Cos. v. United States*, 452 U.S. 247, 261 n.17 (1981); 26 U.S.C. § 6110(k)(3).

half-mile from the Tennessee/Georgia border. App. 173a-174a.

Mr. Horton intended to develop the property with residences and a commercial service area, but he had to overcome a number of obstacles. Mr. Horton successfully sought to have a portion of the property rezoned, obtained permits to build (and did build) a bridge across a creek that had rendered much of the property inaccessible, and installed a high-pressure sewer pump station. App. 174a.

In 2008, Mr. Horton learned about a conservation easement placed on nearby property and started researching conservation easements. App. 174a. Conserving a portion of the Oakbrook property appealed to him because it would protect the ridgeline for his nine children to enjoy. His interest piqued, he learned more about conservation easements from the Executive Director of the Southeast Regional Land Conservancy (the "Conservancy"), which agreed to draft the paperwork should Oakbrook decide to donate an easement to the Conservancy. *Id.*

When Mr. Horton told his investors about his plan to conserve a portion of the Oakbrook property, they initially balked because they wanted to develop the property. App. 174a. But Mr. Horton eventually persuaded them to agree to give up their right to develop 106 acres and to conserve it forever by donating a conservation easement. *Id.*

Mr. Horton was not an expert in the tax rules governing deductions for easement donations, so Oakbrook relied heavily on the Conservancy to draft the easement deed. App. 175a. The Conservancy used its standard deed language, which likely was drawn from other model agreements, including those produced by the Land Trust Alliance. App. 176a.

The Executive Director of the Conservancy testified that he "did not think it right for the Conservancy to share in any condemnation award or extinguishment proceeds attributable to any improvements" Oakbrook makes after the donation because the Conservancy "did not pay for those improvements." Moreover, he believed that the Conservancy's deed, which guaranteed it "an absolute" amount, "is [al]ways going to exceed * * * the minimum required by the IRS." App. 177a (alteration and omission in original).

Therefore, the Oakbrook deed's extinguishment clause provides that the Conservancy would receive a fixed amount of the proceeds equal to the difference between the fair market value of the property with and without the easement, as measured on the date of the donation, *i.e.*, the amount of the tax deduction claimed by Oakbrook. App. 175a-176a. The clause also provides that the Conservancy would not be entitled to any portion of the proceeds attributable to improvements to the property made by Oakbrook after the donation. *Id.*

Oakbrook donated the easement to the Conservancy in 2008. App. 174a. Oakbrook is classified as a partnership for federal tax purposes, and on its 2008 tax return, it claimed a deduction of $9.545 million, which Oakbrook's appraiser determined to be the difference between the price at which it could sell the Oakbrook property for development and the residual value of the property under easement. App. 177a-178a.

F. The Tax Court Opinions

The IRS opened an examination of Oakbrook's 2008 tax return. In 2012, the IRS issued a Notice of Final Partnership Administrative Adjustment disallowing the deduction (on grounds other than the Proceeds Regulation). App. 178a. In 2013, Oakbrook petitioned the Tax Court for readjustment under 26 U.S.C. § 6226 (as in effect for the 2008 tax year). App. 10a-11a.

The IRS first made the argument that Oakbrook's deed did not comply with the Proceeds Regulation in a motion for partial summary judgment filed in August 2016. By that time, Oakbrook's conservation easement had been in place for almost eight years (where it remains today, without any suggestion of potential judicial extinguishment).

Judge Holmes presided over the Tax Court trial of the Oakbrook case in October 2016. App. 11a. In May 2020, the Tax Court issued two opinions in the case, a reviewed opinion by the full Tax Court regarding the validity of the Proceeds Regulation (with Judge Holmes in dissent) and a memorandum opinion by Judge Holmes containing the Court's factual findings and applying the reviewed opinion's legal conclusions.

The reviewed opinion, authored by Judge Lauber, concluded that the Proceeds Regulation is a legislative rule and that Treasury complied with the APA in issuing it. *See* App. 73a-81a. The Tax Court majority was of the view that "[t]he purpose of the 'judicial extinguishment' rule is plain on its face." App. 80a. Moreover, Treasury was not required to explain the basis and purpose for each individual component of such a large regulation project. *Id.* Treasury made "numerous changes" to the proposed regulations and stated that it was adopting the regulations "[a]fter consideration of all comments." App. 77a (quoting T.D. 8069, 1986-1 C.B. at 90).

Judge Toro authored a concurring opinion. *See* App. 89a-130a. In his view, section 170(h) itself (without resort to the Proceeds Regulation) required that the charity's share of the proceeds be calculated based on the fair market value as of the date of extinguishment, not the value as of the date of the gift as provided for in Oakbrook's deed.[5] *See* App. 90a-97a.

Judge Toro proceeded to explain why the Proceeds Regulation "fails to meet the procedural requirements of the Administrative Procedure Act." App. 90a; *see* App. 109a-130a. He observed that "Treasury was simply following its historical position that the APA's procedural requirements did not apply to these types of regulations." App. 118a. Thus, "it is not difficult to see why that agency might think that a rather brief explanation, offered as it were out of its own generosity, should be good enough." App. 119a.

Judge Toro explained that "[t]he record leaves no doubt that NYLC made comments 'that can be thought to challenge a fundamental premise' underlying the proposed agency decision.'" App. 123a (quoting *Carlson v. Postal Regul. Comm'n*, 938 F.3d 337, 344 (D.C. Cir. 2019) (quoting *MCI WorldCom Inc. v. FCC*, 209 F.3d 760, 765 (D.C. Cir. 2000))). "But Treasury gave

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[5] The Sixth Circuit held that the IRS waived this argument (which Judge Toro raised *sua sponte*) by not making it before the Tax Court. App. 12a-14a. Neither the Tax Court majority nor the dissent addressed the argument. App. 13a.

no explanation" for how it "addressed the concerns expressed in the NYLC Comment Letter." App. 124a. Thus, "Treasury's actions did not provide 'an explanation [that] is clear enough that its "path may reasonably be discerned."'" *Id.* (quoting *Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 221 (2016) (quoting *Bowman Transp., Inc. v. Ark.-Best Freight Sys., Inc.*, 419 U.S. 281, 286 (1974))).[6]

Judge Holmes penned a lengthy dissent, which opened with the observation that "[o]ur holding today will likely deny any charitable deduction to hundreds or thousands of taxpayers who donated the conservation easements that protect perhaps millions of acres." App. 131a. He explained that thirteen of the 90 comments on the regulations project had "specifically expressed concern with" the Proceeds Regulation. App. 137a. After reviewing the comments, he concluded that "[t]hese are multiple serious comments that identified problems with the regulation when it was proposed and explained why those problems mattered. Comments with this level of detail and dispute among the commenters would seem enough to conclude that Treasury had before it 'significant' comments. Such comments deserve responses." App. 142a.

Judge Holmes made the practical point that "[h]ad Treasury responded in any meaningful way to the comments that it received, such as those from NYLC,

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[6] Judge Toro also concluded that the Proceeds Regulation is an unreasonable interpretation of the statute and therefore invalid under *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). *See* App. 105a-109a.

neither donors and donees, nor courts" would have to grapple with the issues raised in the case. App. 143a (citing the IRS's 2008 private letter ruling). "Such widespread industry confusion is precisely what APA section 553 is intended to avoid." *Id.*

Judge Holmes addressed each of the majority's arguments for letting the regulation stand. He explained that the commenters raised significant issues with the proposed regulation that merited a response. Contrary to the majority's claim that commenters did not propose alternatives, commenters "wrote in to propose other alternatives to achieve the Code's requirement that the conservation purpose of a donated easement be preserved 'in perpetuity.'" App. 149a. He explained that Treasury's unsupported statement that it had considered "all comments" was insufficient under *Motor Vehicle Manufacturers Ass'n of the United States, Inc. v. State Farm Mutual Automobile Insurance Co.*, 463 U.S. 29 (1983) (decided three years before the Treasury finalized the Proceeds Regulation), and *Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 223 (2016). App. 150a-159a. Finally, he explained that the majority's determination that "minor changes to the proposed regulation" were a sufficient basis on which to uphold the regulation was incorrect because the changes to this proposed regulation did not allow a reviewing court to "infer an agency's reasoned response to a significant comment." App. 160a. Accordingly, Judge Holmes said that the court should "hold that Treasury's failure to respond to significant comments in the Final Rule's statement of basis and purpose violated APA section 553(c)."[7] App. 161a.

Nevertheless, bound by the Tax Court's reviewed opinion, Judge Holmes denied Oakbrook's deduction in his memorandum opinion. App. 171a-207a.

G. The Sixth Circuit's Decision

The Sixth Circuit, in an opinion by Judge Moore and joined by Judge Gibbons, affirmed. The Sixth Circuit first held that the IRS had waived any argument that Oakbrook's deed did not comply with the statute by not raising the argument before the Tax Court. App. 12a-14a. The Sixth Circuit majority observed that Judge Toro's concurring opinion in the Tax Court had "raised this issue *sua sponte* with neither the majority nor the dissent addressing it." App. 13a. Moreover, the Sixth Circuit observed that the argument depended on economic projections "not in the record" and that instead the IRS had relied on data pulled from the websites Zillow.com and Neighborhoodsout.com while it was preparing its appellate brief. The Sixth Circuit stated, "we are hesitant to rely on economic projections that have not been vetted by the adversarial process." App. 13a & n.4.

Turning to the Proceeds Regulation, the majority first addressed the adequacy of Treasury's concise statement of basis and purpose. The majority concluded that "the statutory text and legislative history that Treasury contemplated in promulgating [the Proceeds Regulation] illuminate the regulation's basis

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[7] Judge Holmes also questioned whether the Proceeds Regulation survived scrutiny under *State Farm* and *SEC v. Chenery Corp.*, 318 U.S. 80 (1943).

and purpose: to provide an administrable mechanism that would ensure that an easement's conservation purpose as per I.R.C. § 170(h)(5)(A) continued to be protected should the interest be extinguished."[8] App. 19a. Therefore, "its concise statement suffices." *Id.*

The majority then held that none of the comments regarding the Proceeds Regulation required Treasury's response. NYLC's comment did not require any response because it "did not engage with I.R.C. § 170(h)(5)(A)'s perpetuity requirement and whether the rule served this end." App. 23a. A comment from the Landmarks Preservation Council of Illinois did not require a response because it was "wrong" and therefore "did not raise a significant issue." App. 23a-24a. The Land Trust Exchange and the Trust for Public Land suggested that a different part of the regulation package (26 C.F.R. § 1.170A-14(g)(3)) was sufficient to protect Treasury's concerns about perpetuity. App. 24a. That comment required no response because "[n]either organization provided any indication of how expanding [paragraph (g)(3)] would fulfill Congress's express aim in I.R.C. § 170(h)(5)(A) of limiting deductions to those instances where an easement's conservation purpose can be safeguarded forever." *Id.*

The majority opinion acknowledged "a recent decision by the Eleventh Circuit that held the proceeds regulation to be procedurally invalid under the APA. *See Hewitt v. Commissioner*, 21 F.4th 1336, 1339 (11th Cir. 2021)." App. 27a. It stated that "we find that decision's reasoning to be unpersuasive." *Id.* It observed that the Eleventh Circuit had found NYLC's comment

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[8] The Internal Revenue Code (or "I.R.C.") is codified in Title 26 of the United States Code.

significant because it "raised significant concerns about possible deterrent effects that the proceeds regulation could have on donations." *Id.* In the majority's view, "highlighting this point overlooks a crucial condition that Congress demanded be met by donors seeking deductions: an easement's conservation purpose must be 'protected in perpetuity.'" *Id.*

Judge Guy concurred in the judgment. He would have found that the "the regulation is procedurally invalid under the Administrative Procedure Act (APA) for substantially the same reasons stated by the Eleventh Circuit in [*Hewitt*] and by the concurring and dissenting opinions in [the Tax Court's *Oakbrook* opinion]." App. 39a. (He concurred, rather than dissented, because he credited the argument that the Sixth Circuit held the IRS had waived. App. 53a-59a.)

Judge Guy explained that NYLC's comment was significant for two reasons. App. 43a-44a. First, it showed that the regulation would thwart one of the purposes of the statute by deterring prospective donors. App. 43a. Second, the comment cast doubt on the reasonableness of the regulation's formula and further showed that the proposed regulation would "obviously" deter donors. *Id.* "The bottom line is there is no doubt that NYLC's comment '"can be thought to challenge [two] fundamental premise[s]" underlying the proposed agency decision' and Treasury failed to respond." App. 45a (quoting *Carlson v. Postal Regul. Comm'n*, 938 F.3d 337, 344 (D.C. Cir. 2019) (quoting *MCI WorldCom Inc. v. FCC*, 209 F.3d 760, 765 (D.C. Cir. 2000))).

Judge Guy reasoned that the majority had erred by "treat[ing] one other statutory goal—perpetuity—as a trump card, such that Treasury was free to ignore any comment unless the comment showed that the regulation failed to satisfy the perpetuity requirement." App. 48a. (cleaned up). He rejected the majority's efforts to discern what Treasury was thinking: "Treasury was required to *explain to the public*, why post-donation improvements are not taken into account and why it balanced the competing statutory interests in favor of adopting a fixed-ratio formula."[9] App. 49a.

Notwithstanding his view that the Proceeds Regulation was invalid under the APA, Judge Guy would have excused the IRS's failure to raise its statutory argument in the Tax Court and hold that Oakbrook's deed did not comply with the statute's perpetuity requirement because it fixed the amount to which the charity was entitled at the time of grant rather than at the time of extinguishment. App. 53a-59a.

The Sixth Circuit denied rehearing en banc on July 6, 2022. App. 1a.

REASONS FOR GRANTING THE PETITION

I. The Sixth Circuit's Decision Conflicts with the Eleventh Circuit's *Hewitt* Decision.

The Sixth Circuit's decision created a square—and widely acknowledged—conflict with the Eleventh Circuit regarding the validity of the Proceeds Regulation. *See* Sup. Ct. R. 10(a).

In *Hewitt v. Commissioner*, 21 F.4th 1336 (11th Cir. 2021), the Eleventh Circuit held that "the Commissioner's interpretation of § 1.170A-14(g)(6)(ii) is arbitrary and capricious and violates the APA's

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[9] Judge Guy also concluded that the Proceeds Regulation does not survive under *Chevron*. App. 53a.

procedural requirements." *Id.* at 1339. The court began by listing the APA's procedural requirements for legislative rules as set forth in *Perez v. Mortgage Bankers Ass'n*, 575 U.S. 92 (2015). The most important of these for present purposes is that "the agency 'must consider and respond to significant comments received during the period for public comment.'" *Hewitt*, 21 F.4th at 1342 (quoting *Perez*, 575 U.S. at 96).

The court reviewed the "most extensive" comments submitted by the New York Landmarks Conservancy, along with comments and concerns from six other conservation organizations about the Proceeds Regulation. *Id.* at 1345-1346. But "Treasury did not discuss or respond to the comments made by NYLC or the other six commenters concerning the extinguishment proceeds regulation." *Id.* at 1346 (citing 51 Fed. Reg. at 1497-1498).

The Eleventh Circuit concluded that the comments from NYLC "challenged a fundamental premise underlying Treasury's proposed regulations by 'in effect counter[ing] that the proposed rule on future donor improvements was contrary to those policy decisions [mentioned in the proposed regulations], would lead to inequitable results that were inconsistent with the statute, and would deter future contributions.'" *Id.* at 1351 (quoting App. 123a (Toro, J., concurring in the result)). Thus, "[s]imply put, NYLC's comment was significant and required a response by Treasury to satisfy the APA's procedural requirements." *Id.*

In rejecting the IRS's arguments that NYLC's comment was not significant, the Eleventh Circuit quoted Treasury's preamble to the proposed regulations, which stated that the "regulations reflect the major policy decisions made by the Congress and expressed in the[ ] committee reports." *Id.* at 1351 (alteration in original) (quoting 48 Fed. Reg. at 22,940). The IRS argued that NYLC's comment was not significant because "Treasury's 'primary (if not exclusive) consideration in crafting the proceeds regulation was the meaning of the statutory perpetuity requirement' and that, as such, NYLC was required 'to explain why the rule would not further the goal of ensuring that the conservation purpose embodied in the perpetual use restriction would be protected in perpetuity as required by the statute.'" *Id.* at 1352 (quoting IRS Br. at 29-30). The Eleventh Circuit rejected the IRS argument as "inconsistent with the committee reports Treasury purportedly relied on." Specifically, "one of the purported purposes set forth in the committee reports was to allow deductions for the donation of conservation easements to encourage donation for such easements. *See* S. Rep. No. 96-1007, at 9." *Id.* Thus, "NYLC's comment was specific to, and casted doubt on, the reasonableness of the proceeds regulation in light of one of Congress's committee reports." *Id.*

The Eleventh Circuit rejected additional IRS arguments that Treasury's revisions to the proposed Proceeds Regulation in the final regulation support its representation that it considered "all comments" in the final regulations' preamble. The Eleventh Circuit held the IRS to its concession that the revisions were "simply 'clarifications' in response to other comments," and the court therefore held that the revisions did not "provide any indication that Treasury was responding to NYLC's significant comment about the post-donation improvements issue." *Id.* at 1353.

In creating the circuit split, the Sixth Circuit found *Hewitt*'s "reasoning to be unpersuasive." App. 27a. It found that Treasury was not required to respond to the New York Landmarks Conservancy's comment because "the comment did not engage with I.R.C. § 170(h)(5)(A)'s perpetuity requirement and whether the rule served this end." App. 23a. The Sixth Circuit stated that "[a]lthough encouraging the donation of conservation easements is undeniably a goal of the statute, highlighting this point overlooks a crucial condition that Congress demanded be met by donors seeking deductions: an easement's conservation purpose must be 'protected in perpetuity'." App. 27a (quoting 26 U.S.C. § 170(h)(5)(A)).

Hewitt and *Oakbrook* thus are in direct conflict regarding the validity of the Proceeds Regulation, the significance of the comments submitted to Treasury, and the obligations of agencies to explain their rules. Those acknowledging the existence of the split include the Tax Court judges tasked with deciding whether to reaffirm their *Oakbrook* decision or instead to follow *Hewitt*. The Tax Court is a court of nationwide jurisdiction, and it has a "rule of applying the law of the court of appeals to which an appeal would be taken." *Commissioner v. Portland Cement Co. of Utah*, 450 U.S. 156, 164 & n.14 (1981) (citing *Golsen v. Commissioner*, 54 T.C. 742 (1970), *aff'd on other grounds*, 445 F.2d 985 (10th Cir. 1971)). Therefore, in cases appealable to the Eleventh Circuit, the Tax Court is following *Hewitt*. *See, e.g.*, *Sparta Pink Prop., LLC v. Commissioner*, T.C. Memo. 2022-88 (acknowledging the split and denying IRS motion for partial summary judgment under the Proceeds Clause); *Thompson v. Commissioner*, T.C. Memo. 2022-80 (same). But in cases appealable to other courts of appeals, the Tax

Court has been deferring the choice whether to follow *Hewitt* or *Oakbrook*. For example, in *Gray Mare Farms, LLC v. Commissioner*, a case that may be appealable to the Fourth Circuit, Tax Court Judge Cohen cited *Hewitt* and *Oakbrook* in observing that the "the validity of [the Proceeds R]egulation is the subject of a conflict between the Circuit Courts of Appeal" and that "summary judgment on the disputed issue of law is premature and unproductive." *Gray Mare Farms LLC v. Commissioner*, No. 6682-20 (T.C. July 25, 2022) (order denying IRS motion for partial summary judgment).

In the end, "[t]he split in the circuits is undeniable, and millions, if not billions, of tax dollars are at stake. Also at stake are millions of acres of land and species of birds and animals that may or may not be protected pending the outcome of this issue." Nancy Ortmeyer Kuhn, *A Split in the Circuits: Will Supreme Court Take Up Easement Challenge?*, Bloomberg Law (Apr. 5, 2022), https://news.bloomberglaw.com/environment-and-energy/a-split-in-the-circuits-will-supreme-court-take-up-easement-challenge. The Court should grant certiorari to determine whether the comments that Treasury received were significant enough to merit a response from Treasury.

II. The Sixth Circuit's Decision Conflicts with Decisions of Other Courts of Appeals Regarding the Significance of Comments Outside the Tax Context

The square split between *Oakbrook* and *Hewitt* regarding the validity of the Proceeds Regulation is a sufficient reason for this Court to grant the petition. But the effects of the Sixth Circuit's decision in this case stretch far beyond tax law. This Court held in

Mayo Foundation for Medical Education & Research v. United States, 562 U.S. 44 (2011), that the administrative law principles that govern the tax system are the same as those that apply to other agencies. Therefore, the Sixth Circuit's decision in this case may be invoked by other administrative agencies to disregard comments they receive from the public. Professor Kristin E. Hickman, who currently serves as Chair of the Committee on Judicial Review of the Administrative Conference of the United States, has explained, "[t]his split has tremendous implications not only for Treasury but for agencies across the administrative state that dedicate substantial effort to responding to comments submitted in the course of notice-and-comment rulemaking." Kristin E. Hickman, *The Federal Tax System's Administrative Law Woes Grow*, ABA Tax Times (May 2022). This is because "the key split between the Sixth and Eleventh Circuits over the requirement that an agency respond to significant regulations comes down to a fundamental disagreement over what makes a comment significant." *Id.*

In his dissenting opinion in the Tax Court, Judge Holmes observed that, with respect to when a comment is significant, "there is not a precise definition in the caselaw—rather there are themes." App. 147a. The themes that Judge Holmes identified included:

- An agency should address why it rejected proffered alternatives. *See Indep. U.S. Tanker Owners Comm. v. Dole*, 809 F.2d 847, 852 (D.C. Cir. 1987) (faulting the agency for "fail[ing] to give an adequate account" of "why alternative measures were rejected").

- A reviewing court (and the public) "should be able to 'see what major issues of policy were ventilated by the informal proceedings and why the agency reacted to them as it did.'" *Auto. Parts & Accessories Ass'n v. Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968).

- Comments that are significant are those, "which, if true, raise points relevant to the agency's decision and which, if adopted, would require a change in an agency's proposed rule." *Home Box Off., Inc. v. FCC*, 567 F.2d 9, 35 n.58 (D.C. Cir. 1977).

See App. 147a-148a. The Sixth Circuit's treatment of the comments Treasury received regarding the Proceeds Regulation conflicts with the D.C. Circuit's articulation of these themes. Contrary to the Sixth Circuit's opinion, the comments indeed "identified inequities with the regulation, suggested alternatives, identified potential negative effects on the willingness of donors to make donations, uncovered potential conflicts with state law, and simply asked for more clarity." App. 150a (Holmes, J. dissenting).

In his Sixth Circuit concurring opinion, Judge Guy highlighted two specific cases in which the Courts of Appeals invalidated regulations based on failure to respond to comments that would have been deemed not significant under the Sixth Circuit's decision. App. 47a-49a (Guy, J., concurring in the judgment).

First, in *United States v. Nova Scotia Food Products Corp.*, 568 F.2d 240 (2d Cir. 1977), the Second Circuit confronted a regulation promulgated under a statute that deemed food to be "adulterated" "if it has been prepared, packed, or held under insanitary conditions whereby it may have become contaminated with filth, or whereby it may have been rendered injurious to health." *Id.* at 244 (quoting 21 U.S.C. § 342(a)(4)). To prevent botulism, the Food and Drug Administration proposed regulations that required the fish to be cooked to a certain internal temperature and in a certain salinity. Nova Scotia Food Products Corp. ("Nova Scotia") commented that the proposed temperature and salinity specifications "will completely destroy the product." *Id.* at 245. The Second Circuit, after reviewing Judge Friendly's opinion in *Associated Industries of New York State, Inc. v. U.S. Department of Labor*, 487 F.2d 342, 352 (2d Cir. 1973), held that "to sanction silence in the face of such vital questions would be to make the statutory requirement of a 'concise general statement' less than an adequate safeguard against arbitrary decision-making." *Nova Scotia*, 568 F.2d at 253. Nova Scotia's comment was significant because it highlighted an unintended consequence of a proposed rule—unrelated to the specific statutory purpose (preventing botulism) that the regulation was promulgated to accomplish. Under the Sixth Circuit's definition of "significant comments" in this case, Nova Scotia's comment could not have been significant because it did not address the botulism-prevention statutory purpose.[10]

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[10] The Sixth Circuit majority sought to distinguish *Nova Scotia* on the ground that the proposed regulations were trying to accomplish two policy goals—"to address a spate of botulism cases" and "ensure that fish could be safely consumed." App. 22a. The same is true here. The committee reports that Treasury cited as providing "an in-depth statement of congressional intent," App. 219a, described multiple goals, including both encouraging conservation easement donations and protecting the easement's conservation purposes in perpetuity.

Second, in *Carlson v. Postal Regulatory Commission*, 938 F.3d 337 (D.C. Cir. 2019), the agency decided to increase the price of stamps by five cents in order to achieve one statutory goal of "simplicity of structure." *Id.* at 342 (quoting 39 U.S.C. § 3622(c)(6)). Mr. Carlson commented that a five-cent increase was "inconsistent with the statutory objective of 'establish[ing] and maintain[ing] a just and reasonable schedule for rates.'" *Id.* (alteration in original) (quoting 39 U.S.C. § 3622(b)(8)). The D.C. Circuit held that this comment was significant "because [it] challenged the Commission's primary rationale by raising substantial countervailing statutory considerations." *Id.* at 347 (citing *MCI WorldCom, Inc. v. FCC*, 209 F.3d 760, 765 (D.C. Cir. 2000)). That is precisely what the New York Landmarks Conservancy's comment did in this case.

This Court recently emphasized the important role that the APA plays in encouraging active dialog between administrative agencies and the regulated public. "Notice and comment gives affected parties fair warning of potential changes in the law and an opportunity to be heard on those changes—and it affords the agency a chance to avoid errors and make a more informed decision." *Azar v. Allina Health Servs.*, 139 S. Ct. 1804, 1816 (2019) (citing 1 Kristen E. Hickman & Richard J. Pierce, Jr., Administrative Law § 4.8 (6th ed. 2019)). Treasury's decision not to respond to the comments that it received regarding the Proceeds Regulation denied the regulated public fair warning of the IRS's eventual litigating position and led to the confusion reflected in the 2008 IRS private letter ruling that the IRS now claims are incorrect. As a result, the IRS has denied hundreds if not thousands of deductions with a resulting flood of litigation.

Allowing the Sixth Circuit's cramped definition of "significant comments" to stand would serve only to ensure that similar scenarios will play out in other administrative law contexts.

III. The Split Is Unlikely to Resolve on Its Own and This Case Is an Appropriate Vehicle for Resolution of the Split

This Court has long held that "[t]he revenue laws are to be construed in the light of their general purpose to establish a nationwide scheme of taxation uniform in its application," *United States v. Irvine*, 511 U.S. 224, 238 (1994) (quoting *United States v. Pelzer*, 312 U.S. 399, 402-403 (1941)); *see also Wash. Energy Co. v. United States*, 94 F.3d 1557, 1561 (Fed. Cir. 1996) ("[T]he need for uniformity of decision applies with special force in tax matters."). Absent this Court's intervention, the outcome in this case will turn not on uniform nationwide application of tax law, but on geography: If the Oakbrook property were located just a half-mile to the south on the other side of the Tennessee/Georgia border (and therefore in the Eleventh Circuit), *Hewitt* would dictate the opposite result.

It is unlikely that the circuit split will resolve on its own. The Sixth Circuit denied rehearing en banc in this case, and a recent Eleventh Circuit opinion concluded that "*Hewitt* invalidated the regulation on which the tax court relied in disallowing Glade Creek's charitable contribution deduction. We must follow *Hewitt*." *Glade Creek Partner, LLC v. Commissioner*, No. 21-11251, 2022 WL 3582113, at *3 (11th Cir. Aug. 22, 2022) (citation omitted). The Tax Court is deferring additional rulings regarding the validity of the Proceeds Regulation in cases appealable to other Courts of Appeals. In the meantime, donors who wish to conserve their property but contemplate future improvements after the easement is granted are likely to be chilled from conservation by the ongoing uncertainty.

This case presents an appropriate vehicle for resolution of the split. The view expressed in Judge Toro's concurring opinion in the Tax Court and Judge Guy's concurring opinion in the Sixth Circuit that Oakbrook's easement deed is inconsistent with the statute's "protected in perpetuity" requirement does not pose any obstacle to this Court's review. The IRS waived that argument by not raising it in the Tax Court, and the Sixth Circuit correctly held that it would be inappropriate to excuse that waiver given that the argument depended on economic projections from commercial real estate websites that the IRS had not introduced into the record and thus that had not been subjected to the adversarial process. It would likewise be inappropriate to deny certiorari based on this unpreserved argument.

Oakbrook properly challenged the validity of the Proceeds Regulation under the APA, and the IRS did not raise any defenses to assertion of the APA challenge. Seventeen Tax Court judges fully aired the competing arguments in three separate opinions. The Eleventh Circuit and the Sixth Circuit considered the arguments and came to conflicting conclusions. The issues are fully developed and squarely presented to this Court. This Court should grant review to restore nationwide uniformity to the application of the tax law governing land conservation and charitable contribution deductions.

CONCLUSION

For the foregoing reasons, the Court should grant the petition for a writ of certiorari.

Respectfully submitted,

David W. Foster
Counsel of Record
Armando Gomez
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
1440 New York Ave., NW
Washington, D.C. 20005
(202) 371-7000
david.foster@skadden.com

Michelle Abroms Levin
Gregory P. Rhodes
Logan C. Abernathy
DENTONS US LLP
305 Church Street SW
Suite 800
Huntsville, AL 35801

Isabelle K. Farrar
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM LLP
500 Boylston Street
Boston, MA 02116

October 4, 2022

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

[Filed: July 06, 2022]

No. 20-2117

OAKBROOK LAND HOLDINGS, LLC;
WILLIAM DUANE HORTON, TAX MATTERS PARTNER,

Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee.

ORDER

BEFORE: GUY, MOORE, and GIBBONS, *Circuit Judges.*

The court received a petition for rehearing en banc. The original panel has reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case. The petition then was circulated to the full court. No judge has requested a vote on the suggestion for rehearing en banc.

Therefore, the petition is denied.

ENTERED BY ORDER OF THE COURT

/s/ Deborah S. Hunt
Deborah S. Hunt, Clerk

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No. 20-2117

OAKBROOK LAND HOLDINGS, LLC;
WILLIAM DUANE HORTON, TAX MATTERS PARTNER,
Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

On Appeal from the United States Tax Court.
No. 005444-13—Mark V. Holmes, *Judge*.

Argued: October 27, 2021
Decided and Filed: March 14, 2022

Before:
GUY, MOORE, and GIBBONS,
Circuit Judges.

COUNSEL

ARGUED: David William Foster, SKADDEN, ARPS, SLATE, MEAGHER & FLOM, LLP, Washington, D.C., for Appellants. Nathaniel S. Pollock, UNITED STATES DEPARTMENT OF JUSTICE, Washington, DC, for Appellee. ON BRIEF: Michelle Abroms Levin, SIROTE & PERMUTT, P.C., Huntsville, Alabama, Gregory P. Rhodes, SIROTE & PERMUTT, P.C., Birmingham, Alabama, for Appellants. Nathaniel S. Pollock, Francesca Ugolini, Arthur T. Catterall, UNITED STATES DEPARTMENT OF JUSTICE, Washington, DC, for Appellee. Joseph D. Henchman, NATIONAL TAXPAYERS UNION FOUNDATION, Washington, D.C., Kip D. Nelson, FOX ROTHSCHILD LLP, Greensboro, North Carolina, for Amici Curiae.

MOORE, J., delivered the opinion of the court in which GIBBONS, J., joined. GUY, J. (pg. 28-41), delivered a separate opinion concurring in the judgment only.

OPINION

KAREN NELSON MOORE, Circuit Judge. Under § 170(h) of the Internal Revenue Code, taxpayers who donate an easement in land to a conservation organization may be eligible to claim a charitable deduction on their Federal income tax returns. Crucially, the easement's conservation purpose must be guaranteed to extend in perpetuity to qualify for the deduction. *See* 26 U.S.C. (I.R.C.) § 170(h)(5)(A). Unexpected developments, however, may make this impossible long after the donor has deeded the easement away. How, then, can an easement satisfy the perpetuity requirement?

Contemplating such scenarios, the Department of Treasury has promulgated a rule, 26 C.F.R. (Treas. Reg.) § 1.170A-14(g)(6). This regulation addresses situations in which unforeseen changes to the surrounding land make it "impossible or impractical" for an easement to fulfill its conservation purpose. Treas. Reg. § 1.170A-14(g)(6)(i). In these events, the conservation purpose may still be protected in perpetuity "if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds . . . from a subsequent sale or exchange of the property are used by the donee" to further the original conservation purpose. *Id.* Proceeds are calculated by a formula in § 1.170A-14(g)(6)(ii), a provision to which we refer as the "proceeds regulation."

On this appeal from the United States Tax Court, the petitioners, Oakbrook Land Holdings, LLC (Oakbrook) and William Duane Horton, challenge the validity of the proceeds regulation. The petitioners contend that, in promulgating this rule, Treasury violated the notice-and-comment requirements of the Administrative Procedure Act (APA). The petitioners also argue that Treasury's interpretation of § 170(h)—the statute that the rule implements—is unreasonable. Finally, the petitioners argue that the proceeds regulation is arbitrary or capricious. The full Tax Court considered these arguments and found them to be unpersuasive. *See Oakbrook Land Holdings v. Comm'r*, 154 T.C. 180, 181 (T.C. 2020). We agree with the Tax Court and AFFIRM.

I. BACKGROUND

Due to the nature of the issues, we outline the statutory and regulatory framework that governs charitable deductions for conservation easements before describing the rulemaking process of the proceeds regulation. Once that is established, we turn to the facts of this case.

A. Statutory and Regulatory Framework

Section 170(a)(1) of the Internal Revenue Code allows taxpayers to deduct charitable donations made during the tax year. The Code generally disallows gifts that consist of less than the taxpayer's entire interest in the property—such as an easement—from qualifying for a deduction. *See* I.R.C. § 170(f)(3)(A); *Glass v. Comm'r*, 471 F.3d 698, 706 (6th Cir. 2006). There is an exception if the interest is a "qualified conservation contribution." I.R.C. § 170(f)(3)(B)(iii). This type of gift may qualify for a deduction if it is "of a qualified real property interest," "to a qualified organization," and is "exclusively for conservation purposes." I.R.C. § 170(h)(1)(A)–(C). Easements can qualify as such contributions. *See Glass*, 471 F.3d at 699-700.

Perpetuity is vital to the statutory scheme. An easement is a qualified real property interest only if its deed creates "a restriction (granted *in perpetuity*) on the use which may be made of the real property." I.R.C. § 170(h)(2)(C) (emphasis added). Driving home how important the parenthetical phrase in § 170(h)(2)(C) is, a nearby provision explains that a contribution will not be treated as having been made exclusively for conservation purposes "unless the conservation purpose is protected *in perpetuity*." I.R.C. § 170(h)(5)(A) (emphasis added). In other words, the donation of an easement will not qualify for a charitable deduction unless the taxpayer can guarantee that both the grant of the interest and the conservation goals which it serves will endure for quite a long time—forever, to be exact. *See Hoffman Props. II*, *LP v. Comm'r*, 956 F.3d 832, 835 (6th Cir. 2020).

Although I.R.C. § 170(h)(5)(A) expressly mandates that a donated easement's conservation purpose must be protected in perpetuity, the section does not detail what should happen if some external event frustrates this purpose, such as when unforeseen changes in the surrounding land undermine the easement's conservation goals or when a government entity condemns the property. *See generally* Nancy A. McLaughlin, *Con-*

servation Easements and the Proceeds Regulation, 56 REAL PROP. TR. & EST. L. J. 111, 122, 150-52 (2021) (discussing ways in which easements' conservation purposes can be thwarted). For guidance in these scenarios, taxpayers must turn from the text of I.R.C. § 170(h)(5)(A) to the administrative regulation implementing it.

Treasury Regulation § 1.170A-14(g)(6) governs in the event of an "extinguishment." When a "subsequent unexpected change in the conditions surrounding the property . . . . make[s] impossible or impractical the continued use of the property for conservation purposes," the perpetuity requirement of I.R.C. § 170(h)(5)(A) can still be satisfied if two conditions are met. First, the restriction is "extinguished by judicial proceeding." Treas. Reg. § 1.170A-14(g)(6)(i). Second, "all of the donee's proceeds (determined under paragraph (g)(6)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution." *Id.*

Upon extinguishment, a donee organization must receive as proceeds "a fair market value that is at least equal to the *proportionate value* that the perpetual conservation restriction at the time of the gift[] bears to the value of the property as a whole at that time." Treas. Reg. § 1.170A-14(g)(6)(ii) (emphasis added). To determine the "proportionate value" of an easement, the fair market "value of the conservation easement at the time of the gift [must be] divided by the value of the property as a whole at that time." *PBBM-Rose Hill, Ltd. v. Comm'r*, 900 F.3d 193, 207 (5th Cir. 2018). For example, if, at the time of the donation, the fair market value of an easement was $25,000 and the value of the land was $100,000, then the easement would be assessed at twenty-five percent of the value of the property. Next, if a judicial extinguishment occurs, the donee must receive proceeds equal to the proportionate value from any "subsequent sale, exchange, or involuntary conversion." Treas. Reg. § 1.170A-14(g)(6)(ii). The donee in the previous example would therefore receive twenty-five percent of any proceeds of a sale, exchange, or involuntary conversion that followed judicial extinguishment of the easement. Finally, no "amount, including that attributable to improvements, may be subtracted out" of this percentage.[1] *PBBM-Rose Hill*, *Ltd.*, 900 F.3d at 208.

Although the possibility of an easement being judicially extinguished is a contingency, taxpayers still need to address this issue in the easement's deed. The deed must entitle the donee "to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction" should a judicial extinguishment occur.[2] Treas. Reg. § 1.170A-14(g)(6)(ii). Failure to draft a deed that achieves this goal will leave the taxpayer unable to claim a charitable deduction for their donation. Treas. Reg. § 1.170A-14(g)(1).

B. Promulgation of Treas. Reg. § 1.170A-14(g)(6)(ii)

On May 23, 1983, Treasury issued a notice of proposed rulemaking with "proposed regulations relating to contributions of partial interests in property for conservation purposes." 48 Fed. Reg. 22940, 22940

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[1] The parties do not appear to dispute how proceeds are calculated under the regulation.

[2] Treasury Regulation § 1.170A-14(g)(6)(ii) also contains an exception for when "state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction," but the current case does not implicate this provision.

(May 23, 1983). In that notice, Treasury detailed the legislative history of § 170(h), describing how Congress had shifted from limiting the deductibility of conservation easements to allowing them when the easement was "perpetual." *Id.* The preamble noted that the proposed regulations "reflect the major policy decisions made by the Congress and expressed in [its] committee reports." *Id.* Among the proposed rules was the proceeds regulation.

A period of public input followed Treasury's publication of the notice of proposed rulemaking in which the agency received comments regarding the regulations. Ninety organizations submitted over 700 pages of commentary that addressed various aspects of the regulations. *Oakbrook Land Holdings*, 154 T.C. at 186. Of these commentators, approximately a dozen mentioned the proceeds regulation, though mostly in passing. *Id.* We detail several of these comments further below. Treasury also held a public hearing on the proposed regulations on September 15, 1983. *Id.* at 188.

When Treasury issued the final regulations, the accompanying preamble stated that the agency had promulgated the regulations "[a]fter consideration of all comments regarding the proposed amendments." 51 Fed. Reg. 1496, 1496 (Jan. 14, 1986). Some comments that Treasury received during the rulemaking process did cause the agency to alter parts of the regulations, leading the agency to summarize these comments and the changes that they prompted. *Id.* at 1497-98. Treasury also revised the proceeds regulation, but these changes were editorial in nature and aimed at clarifying the rule, not altering its meaning.[3]

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[3] Instead of providing that the donor agree at the time of the gift that the donee receive on a subsequent sale, exchange, or involuntary conversion of the property "a minimum ascertainable

Treasury did not specifically address any comments that it received about the proceeds regulation.

C. Oakbrook's Easement

Oakbrook is a Tennessee Limited Liability Company with its principal place of business in Chattanooga. Joint Appendix (J.A.) at 98-99 (Stipulation of Facts at ¶ 1). William Duane Horton and a group of investors formed the company to purchase and develop a 143-acre parcel of land on White Oak Mountain, an outcropping of the Appalachians near Chattanooga. *Id.* at 1179-80 (Tax Ct. Mem. Op. at 3-4). In 2007, Oakbrook bought the land for $1,700,000. *Id.* at 1180 (Tax Ct. Mem. Op. at 4).

Originally Horton and his wife found the property in their search for a place to build a home. *Id.* at 1179 (Tax Ct. Mem. Op. at 3). The property's proximity to Chattanooga led Horton to believe that residential units could be developed there, and this is what Oakbrook set about to achieve after purchasing the land. *Id.* at 1180 (Tax Ct. Mem. Op. at 4). After learning about conservation easements, Horton convinced his fellow investors in 2008 to have Oakbrook donate a conservation easement on 106 acres of the land to the Southeast Regional Land Conservancy (SRLC), reserving the remaining acreage for development. *Id.* at 1181 (Tax Ct. Mem. Op. at 5).

The deed that conveyed the easement provided for allocation of proceeds upon extinguishment or con-

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proportion of the fair market value to the entire property," 48 Fed. Reg. at 22946, the final rule ensured that the donee receive "a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift[] bears to the value of the property as a whole at that time." 51 Fed. Reg. at 1505.

demnation, and the parties do not dispute how this calculation works. *Id.* at 121-22 (Deed at Article VI, § B(2)–(3)). Under the deed, the fair market value of the easement is determined by calculating the fair market value of the land *without* the encumbrance of the easement, and then subtracting from this number the fair market value of the land *with* the easement. *Id.* at 121 (Deed at Art. VI, § B(2)). The fair market value of each is determined at the time of the gift, creating a fixed value. *Id.* The deed then requires one more subtraction: the fixed value of the easement must be reduced by the value of any post-donation improvements made by Oakbrook to the land as specified by any subsequent condemnation award. *Id.* at 121-22 (Deed at Art. VI, § B(2)).

While negotiating these terms, Oakbrook arranged for an appraisal of the conservation easement to determine the amount to claim as a charitable deduction. *Id.* at 1184 (Tax Ct. Mem. Op. at 8). Initially, the appraiser valued the easement at $19,500,000, but Horton expressed unease about setting the value so high, likely because Oakbrook had bought all 143 acres the year before for $1,700,000. *Id.* The appraiser then reassessed the easement at $9,545,000. *Id.* Oakbrook claimed this amount as a charitable deduction for the 2008 tax year. *Id.* at 1184-85 (Tax Ct. Mem. Op. at 8-9).

D. Procedural History

After Oakbrook filed its 2008 tax return, the Internal Revenue Service (IRS) examined the claimed charitable contribution deduction. *Id.* at 1185 (Tax Ct. Mem. Op. at 9). Because the easement's deed did not comply with Treas. Reg. § 1.170A-14(g)(6)(ii), the IRS disallowed Oakbrook's deduction in full. *Id.* at 17-29, 213-22 (Disallowances). Oakbrook timely petitioned the Tax Court for a readjustment. *Id.* at 8-16 (Pet. for Readjustment). Tax Court Judge Holmes held a bench trial in October 2016 to resolve the matter. *Id.* at 4 (Tax Ct. Dkt. at 4).

In the Tax Court, the petitioners argued both that the easement deed satisfied Treas. Reg. § 1.170A-14(g)(6)(ii) and, alternatively, that the regulation was invalid. *Id.* at 1179 (Tax Ct. Mem. Op. at 3). The full Tax Court heard argument concerning the validity of Treas. Reg. § 1.170A-14(g)(6)(ii), *see Oakbrook Land Holdings*, 154 T.C. at 180-81, while Judge Holmes heard arguments about whether Oakbrook's deed violated the regulation, J.A. at 1179 (Tax Ct. Mem. Op. at 3). The full Tax Court upheld the regulation. *See Oakbrook Land Holdings*, 154 T.C. at 180-81, 198-200, 230. At the same time, Judge Holmes held that Oakbrook's deed violated the proceeds regulation in two ways: first by ascribing a fixed rather than proportionate value that would go to SRLC upon judicial extinguishment, and second by subtracting from this amount any post-donation improvements that Oakbrook made to the land. J.A. at 1212-17 (Tax Ct. Mem. Op. at 36-41).

The petitioners timely appealed. *Id.* at 1226-27 (Notice of Appeal). *See* 26 U.S.C. § 7483. We have jurisdiction over the case under 26 U.S.C. § 7482(a).

II. ANALYSIS

On appeal, the petitioners take aim directly at the proceeds regulation, arguing that the Tax Court erred in upholding the regulation. We review the Tax Court's findings of fact for clear error and its application of law de novo. *Glass*, 471 F.3d at 706. Our "function in reviewing final agency action following informal rulemaking [such as Treasury's promulgation of the proceeds regulation] is prescribed by the APA." *Simms v. Nat'l Highway Traffic Safety Admin.*, 45 F.3d 999, 1003 (6th Cir. 1995). Under § 706(2)(A) of the APA, we must set aside agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."

A. Enforceability of Oakbrook's Deed Under I.R.C. § 170(h)

Before addressing the proceeds regulation's validity, we must address a preliminary matter. To count as a qualified real property interest under I.R.C. § 170(h)(1)(A), the Commissioner argues that a conservation easement's deed must guarantee that the donee will receive the fair market value of the interest upon judicial extinguishment. Pointing to the provisions in the deed that fix the easement's value at the time of the gift and then subtract the worth of post-donation improvements, the Commissioner concludes that Oakbrook's deed would fail to compensate SRLC at fair market value should the easement be extinguished. Under this reading of I.R.C. § 170(h)(1)(A), the Commissioner argues, we need not determine whether Treas. Reg. § 1.170A-14(g)(6)(ii) is a valid regulation because Oakbrook's deed violates the statute.

Regardless of whether this interpretation of I.R.C. § 170(h)(1)(A) is correct, the Commissioner introduces it for the first time on appeal. The only issue that the Commissioner raised below about Oakbrook's deed satisfying § 170(h) was the argument in his pretrial memorandum that the deed inadequately defined the physical area intended for conservation purposes, leaving it impossible to determine what was being conserved and what was not. J.A. at 40, 47-49 (Resp't Pretrial Mem. at 3, 10-12). Nowhere did the Commissioner argue that the deed would fail to compensate

SRLC at fair market value should the easement be extinguished. Instead, Judge Toro's concurrence in the Tax Court's opinion raised this issue *sua sponte* with neither the majority nor the dissent addressing it. *Oakbrook Land Holdings*, 154 T.C. at 203-07.

"[A]ppellate courts ordinarily abstain from entertaining issues that have not been raised and preserved in the court of first instance." *Wood v. Milyard*, 566 U.S. 463, 473 (2012). This case demonstrates the wisdom of this approach. For Oakbrook's deed to violate the Commissioner's interpretation of the statute, it must fail to provide whatever the fair market value of the easement will be upon extinguishment. But this conclusion relies on an assessment of the projected economic worth of the property interest, which is not in the record.[4] Should the fair market value of the interest have increased by the time of extinguishment, then the Commissioner will be proven right. Should the value decline, then the Commissioner will be proven wrong. Either way, future events, not statutory text, hold the answer. *Cf. United States v. Ellison*, 462

[4] Instead of citing to the record, the Commissioner cites to data pulled from Zillow.com and Neighborhoodscout.com to support the proposition that under the terms of the deed, judicial extinguishment "20, 50, or 100 years from now" would lead to SRLC receiving less than the easement's fair market value. Resp't Br. at 36. Likewise, the Commissioner asserts, without any citations, that the value of fixed structures that Oakbrook may add to the property will likely increase over time, which, because of the mechanism in the deed that allows Oakbrook to recoup this value, would further cut into the amount SRLC would receive in the event of judicial extinguishment. *Id.* at 38. Although the concurrence appears confident in these assessments, we are hesitant to rely on economic projections that have not been vetted by the adversarial process, provide no supporting evidence, and are based on commercial real estate websites.

F.3d 557, 560-61 (6th Cir. 2006) (addressing argument not raised below where issue turned on pure question of law). For this reason, we decline to address the Commissioner's newly raised argument.

B. Procedural Issues with Treas. Reg. § 1.170A-14(g)(6)(ii)

This leaves us to examine the validity of Treas. Reg. § 1.170A-14(g)(6)(ii). Under the APA, whenever agencies promulgate "a rule that 'intends to create new law, rights or duties' such as this regulation does, they must engage in a process known as notice-and-comment rulemaking. *Tennessee Hosp. Ass'n v. Azar*, 908 F.3d 1029, 1042 (6th Cir. 2018) (quoting *Michigan v. Thomas*, 805 F.2d 176, 182-83 (6th Cir. 1986)). *See also* 5 U.S.C. § 553(b). There are three steps involved in this process. First, the agency must publish a "notice of proposed rule making" in the Federal Register. 5 U.S.C. § 553(b). Next, the agency must afford "interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments." § 553(c). Finally, "[a]fter consideration of the relevant matter presented, the agency shall incorporate in the rules adopted a concise general statement of their basis and purpose." *Id.*

The petitioners contend that the agency deviated from the APA's notice and comment requirements in two ways. First, the petitioners argue that Treasury inadequately explained the rationale for the proceeds regulation in its concise general statement of basis and purpose. Second, the petitioners argue that the agency failed to respond to certain comments about the regulation, which, according to the petitioners, raised significant issues. We consider each argument in turn.

1. Adequacy of Treasury's Concise Statement of Basis and Purpose

After the comment period closed, Treasury issued a concise statement of basis and purpose for Treas. Reg. § 1.170A-14 that explained the regulations' goals and addressed various comments made about the rules. *See* 51 Fed. Reg. at 1497-98. This statement lacked an explanation for the policy rationale behind Treas. Reg. § 1.170A-14(g)(6)(ii) specifically. Instead, Treasury explained that the regulations contained in Treas. Reg. § 1.170A-14 "provide necessary guidance to the public for compliance with the law and affect donors and donees of qualified conservation contributions." 51 Fed. Reg. at 1496. To the petitioners, this explanation is far too succinct to provide adequate insight into the proceeds regulation's rationale. Placing this explanation within the context of the rulemaking leads us to the opposite conclusion.

What an agency must include in a concise general statement of basis and purpose is dictated by competing considerations. Courts, on the one hand, must be able "to see what major issues of policy were ventilated by the informal proceedings and why the agency reacted to them as it did." *Simms*, 45 F.3d at 1005 (quoting *Auto. Parts & Accessories Ass'n*, *Inc. v Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968)). Judicial scrutiny does not "contemplate that the court itself will, by a laborious examination of the record, formulate in the first instance the significant issues faced by the agency and articulate the rationale of their resolution." *Auto. Parts & Accessories Ass'n*, *Inc.*, 407 F.2d at 338. Agencies, on the other hand, operate with scarce time and limited resources. *See Vermont Yankee Nuclear Power Corp. v. Nat. Res. Defense Council*, *Inc.*, 435 U.S. 519, 551 (1978). These limitations mean that an agency cannot "discuss every item of fact or opinion included in the submissions made to it in informal rule making." *Simms*, 45 F.3d at 1005 (quoting *Auto. Parts & Accessories Ass'n*, *Inc.*, 407 F.2d at 338).

Balancing these considerations, the APA's concise-general-statement requirement "is not meant to be particularly onerous." *Nat'l Mining Ass'n v. Mine Safety & Health Admin.*, 512 F.3d 696, 700 (D.C. Cir. 2008). Absent an ideal statement, courts may still conduct judicial review and uphold a regulation "where the basis and purpose [are] considered obvious." *Cal-Almond*, *Inc. v. U.S. Dep't of Agric.*, 14 F.3d 429, 443 (9th Cir. 1993); *see also Schiller v. Tower Semiconductor Ltd.*, 449 F.3d 286, 303 (2d Cir. 2006); *Citizens to Save Spencer Cnty. v. U.S. EPA*, 600 F.2d 844, 884 (D.C. Cir. 1979). If a statement is truly concise, then "[a] careful reading of the agency's published notices, from its original grant of the petition for rulemaking to its final rule, [may still] disclose[] a 'reasoned path'" that the agency followed to reach its ultimate rule. *Simms*, 45 F.3d at 1006 (quoting *Neighborhood TV Co. v. FCC*, 742 F.2d 629, 639 (D.C. Cir. 1984)).

Juxtaposing the final version of Treas. Reg. § 1.170A-14(g)(6)(ii) with the notice of proposed rulemaking reveals that the basis and purpose of the rule are apparent. In the background section of the proposed version of the proceeds regulation, Treasury provided a brief history of how the Code had treated the charitable deductions of conservation easements. 48 Fed. Reg. at 22940. This history traced how contributions of partial interests went from being disfavored under the Tax Reform Act of 1969, to being allowed under the Tax Reduction and Simplification Act of 1977. *Id.* This allowance came with a caveat: conservation easements had to "be perpetual in order to qualify for a deduction under section 170." *Id.* After Congress again amended the Code with the Tax Treatment Extension Act of 1980, Treasury proposed the proceeds regulation to implement I.R.C. § 170(h). 48 Fed. Reg. at 22940. Notably, although I.R.C. § 170(h)(5)(A) required that easements' conservation purposes be protected in perpetuity, the provision was silent about how to guarantee this requirement in the event of extinguishment. Facing this lacuna, it was obvious that Treasury would need to craft a regulation that spoke to the issue of protecting an easement's conservation purpose should unforeseen circumstances stymie this end.[5]

As it contemplated promulgating the regulations of which Treas. Reg. § 1.170A-14(g)(6)(ii) was a part, Treasury noted its animating concerns. Foremost among these was the "problem" of "how to provide a workable framework for donors, donees, and the Internal Revenue Service to judge the deductibility of open space easements." 48 Fed. Reg. at 22940. Treasury's explicit reliance on the committee reports that accompanied the 1980 reforms to the Code make clear the contours of this problem. *See id.* (detailing how the proposed regulations "reflect the major policy decisions . . . expressed" in H.R. REP. No. 96-1278 (1980) and S. REP. No. 96-1007 (1980)).

Both the House Ways and Means Committee and the Senate Finance Committee noted that conservation easements threatened to incentivize "tax-avoidance transactions in which the taxpayer could obtain

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[5] Although Congress was aware that extinguishment could pose difficulties for ensuring that a conservation easement's purpose was protected in perpetuity, a coalition of land trusts convinced it to leave the creation of rules to govern these circumstances to Treasury. *See* McLaughlin, *supra*, at 122-23 (detailing legislative history).

a deduction for a gift to a charity of the use of part of his property." H.R. REP. No. 96-1278, at 14; S. REP. No. 96-1007, at 8. To avoid such abuse, the committees emphasized that the "bill would restrict the qualifying contributions where there is no assurance that the public benefit, if any, furthered by the contribution would be substantial enough to justify the allowance of a deduction." H.R. REP. No. 96-1278, at 15; S. REP. No. 96-1007, at 10. Key among these restrictions was the addition of a requirement not previously in the Code: that an easement's conservation purpose be protected in perpetuity to qualify for a charitable deduction. *See* H.R. REP. No. 96-1278, at 18 ("Moreover, the bill explicitly provides that [the] requirement [that a contribution is made exclusively for conservation purposes] is not satisfied unless the conservation purpose is protected in perpetuity."); S. REP. No. 96-1007, at 13 (same). An easement's deed needed to "prevent uses of the retained interest inconsistent with the conservation purposes" for an eternity. H.R. REP. No. 96-1278, at 18; S. REP. No. 96-1007, at 13.

Along with stressing the need for restrictions in the deed to ensure that an easement served its conservation purpose in perpetuity, the congressional committees were concerned about how the burdens and benefits associated with fulfilling this requirement might be allotted. For instance, when the Senate Committee on Finance reported the bill out of committee, it noted that the perpetuity requirement of I.R.C. § 170(h)(5)(A) aimed "to limit the deduction only to those cases where the conservation purposes will in practice be carried out." S. REP. No. 961007, at 14. With this goal in mind, the Committee noted that contributions must "be made to organizations which have the commitment and the resources to enforce the perpetual restrictions and to protect the conservation purposes." *Id.* Yet whereas the Committee was concerned about the welfare of the donee, it sought to bar the donor from receiving any benefit from the donation above and beyond the deduction. *See id*. at 15 ("[T]here may be instances in which the grant of an easement may serve to enhance, rather than reduce, the value of property, and in such instances no deduction would be allowable . . . ."). Solely in circumstances where these high bars could be cleared would an easement qualify for a charitable deduction under § 170(h). *See id.* at 14, 15; *see also* H.R. REP. No. 96-1278, at 19, 20 (same discussion).

Taken together, then, the statutory text and the legislative history that Treasury contemplated in promulgating Treas. Reg. § 1.170A-14(g)(6)(ii) illuminate the regulation's basis and purpose: to provide an administrable mechanism that would ensure that an easement's conservation purpose as per I.R.C. § 170(h)(5)(A) continued to be protected should the interest be extinguished. That the regulation allots proceeds in a manner more favorable to donees than to donors merely demonstrates Treasury's acute awareness of Congress's decision to concern itself with the welfare of one entity over the other once the donation was made. Because we can discern this from the information that Treasury provided during the rulemaking, its concise statement suffices.[6]

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[6] Unlike *Dominion Resources*, *Inc. v. United States*, on which the concurrence relies to reach the opposite conclusion, the proceeds regulation does not "directly contradict[]" Congress's intent, as is clear from the legislative history that Treasury provided in its notice of proposed rulemaking. 681 F.3d 1313, 1317 (Fed. Cir. 2012). The fact that Treasury provided citations to the congressional reports that informed its thinking provides another contrast to the agency's actions in *Dominion*, where

2. Failure to Respond to Comments

In the concise general statement of basis and purpose that accompanied the final rule, Treasury also did not address any comments that touched on Treas. Reg. § 1.170A-14(g)(6)(ii). For the petitioners, this oversight is the main procedural deficiency with the rule. To this end, they list a series of comments that mentioned the proceeds regulation, argue that at least some of these required Treasury's attention, and conclude that the agency's failure to do so is fatal to the regulations. Having thoroughly examined these comments, we disagree.

The APA's requirement of soliciting comments serves several ends. "In addition to increasing the quality of rules, the required public participation helps 'ensure fair treatment for persons to be affected by' regulation." *United States v. Cain*, 583 F.3d 408, 420 (6th Cir. 2009) (quoting *Dismas Charities*, *Inc. v. US. Dep't of Justice*, 401 F.3d 666, 678 (6th Cir. 2005)). From these principles follows an agency's duty to respond to "significant points raised by the public." *Sherley v. Sebelius*, 689 F.3d 776, 784 (D.C. Cir. 2012) (quoting *Home Box Office*, *Inc. v. FCC*, 567 F.2d 9, 35-36 (D.C. Cir. 1977)). After all, if an agency could ignore every comment regardless of its content, then the process of soliciting public input would be pointless. *See id.*

Yet the inverse is true, too. Requiring an agency to respond to every comment regardless of its content would transform rulemaking into

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Treasury provided no indication of its rationale for the proposed rule. *Id.* at 1319. These citations allow us to discern what the Federal Circuit could not: the "reasoned path" that Treasury followed in arriving at the regulation. *Simms*, 45 F.3d at 1006 (quoting *Neighborhood TV*, 742 F.2d at 639).

> a game or a forum to engage in unjustified obstructionism by making cryptic and obscure reference to matters that "ought to be" considered and then, after failing to do more to bring the matter to the agency's attention, seeking to have that agency determination vacated on the ground that the agency failed to consider matters "forcefully presented."

Vermont Yankee, 435 U.S. at 553-54. Recognizing that notice-and-comment rulemaking is not an administrative sport, we have repeatedly concluded that an agency must "give reasoned responses to all *significant* comments in a rulemaking proceeding," not that an agency must respond to *all* comments. *United States v. Utesch*, 596 F.3d 302, 310 (6th Cir. 2010) (quoting *PPG Indus., Inc. v. Costle*, 630 F.2d 462, 466 (6th Cir. 1980)) (emphasis added); *see also Navistar Intl Transp. Corp. v. US. EPA*, 941 F.2d 1339, 1359 (6th Cir. 1991).

Significance is difficult to measure in the abstract. The petitioners catalog cases that they argue use different "tests" for determining whether a comment requires an agency's response. *See*, *e.g.*, *Indep. U.S. Tanker Owners Comm. v. Dole*, 809 F.2d 847, 852 (D.C. Cir. 1987); *Home Box Office*, *Inc.*, 567 F.2d at 35 n.58; *United States v. Nova Scotia Food Prods. Corp.*, 568 F.2d 240, 253 (2d Cir. 1977). Rather than provide discrete tests, however, these cases demonstrate that assessing significance is context dependent and requires reading the comment in light of both the rulemaking of which it was part and the statutory ends that the proposed rule is meant to serve.

"Accordingly, an agency must respond to comments 'that can be thought to challenge a fundamental premise' underlying the proposed agency decision."

Carlson v. Postal Regul. Comm'n, 938 F.3d 337, 344 (D.C. Cir. 2019) (quoting *MCI WorldCom, Inc. v. FCC*, 209 F.3d 760, 765 (D.C. Cir. 2000)). A comment must provide enough facts and reasoning to show the agency what the issue is and how it is relevant to the agency's aims. *See Vermont Yankee*, 435 U.S. at 553; *Home Box Office, Inc.*, 567 F.2d at 35 n.58. Comments that do so are "significant enough to step over a threshold requirement of materiality" needed for an agency to address them. *Vermont Yankee*, 435 U.S. at 553 (quoting *Portland Cement Ass 'n v. Ruckelshaus*, 486 F.2d 375, 394 (D.C. Cir. 1973)).

To make this concrete, consider one of the cases upon which petitioners rely. In *United States v. Nova Scotia Food Products Corp.*, the Second Circuit considered a rule issued by the Food and Drug Administration (FDA) to address a spate of botulism cases within the inland fish market and ensure that fish could be safely consumed. 568 F.2d at 243. While promulgating the rule, which required all fish to be cooked or brined according to its specifications, the FDA ignored a comment by Nova Scotia Food Products Corp., a company that sold smoked whitefish. *Id.* at 245. Nova Scotia had recommended that the agency adopt a rule tailored to the heat tolerance of each species so that their product would not be "completely destroy[ed]," due to whitefish being unable to withstand the rigors of the proposed rule. *Id.* The Second Circuit held that the FDA's failure to respond to Nova Scotia's and similar comments rendered the rule arbitrary or capricious. *Id.* at 253. It was unclear how making a fish product inedible would further the FDA's goal of rendering fish safe for human consumption. *Id.*

After examining the comments that petitioners have identified, we hold that none required Treasury's response as Nova Scotia's did the FDA's. Of the comments to which Treasury did not respond, the petitioners focus their attention on four: those made by the New York Landmarks Conservancy, the Landmarks Preservation Council of Illinois, the Land Trust Exchange, and the Trust for Public Land. Situating these comments in the context of the problem that Treasury sought to solve—providing a method for I.R.C. § 170(h)(5)(A)'s perpetuity requirement to be met upon judicial extinguishment—shows why they do not qualify as significant.

The New York Landmarks Conservancy's comment noted three issues with the proceeds regulation: that, based on undisclosed anecdotal evidence, the rule would deter donors from donating easements; that providing the donee with the value of post-donation improvements made by the donor was inequitable; and that it was "possible" that the regulation's allocation of proceeds would conflict with some states' condemnation laws, though the organization did not identify the laws or states. J.A. at 671-72 (N.Y. Landmarks Conservancy Cmt. at 3-4). Although these remarks registered the New York Landmarks Conservancy's dissatisfactions with the proceeds regulation, the comment did not engage with I.R.C. § 170(h)(5)(A)'s perpetuity requirement and whether the rule served this end. Instead, it left Treasury to guess at the connection, if any, between the organization's problems and the proceeds regulation's basis and purpose. Treasury was not required to respond to the comment.

Next, the Landmarks Preservation Council of Illinois commented that how Treas. Reg. § 1.170A-14(g)(6)(ii) calculated proceeds would put a donor at risk of having to pay the donee additional funds if a condemnation award did not cover the amount of money calculated by the rule. J.A. at 778 (Landmarks Pres. Council of Ill. Cmt. at 5). The organization's concern, however, was not only "purely speculative." *Home Box Office, Inc.*, 567 F.2d at 35 n.58. It was also wrong. Because Treas. Reg. § 1.170A-14(g)(6)(ii) calculates proceeds by using a formula based on the proportionate value, not the fixed value, of the easement, the donor could never owe to the donee more than what the extinguishment proceeds are. So, if an easement was worth fifty percent of the value of the donor's entire property at the time of the grant, then the donee would be entitled to fifty percent of any extinguishment proceeds, whatever the amount of those proceeds is. Given that the comment did not raise a significant issue, Treasury was not obliged to respond it.

Both the Land Trust Exchange and the Trust for Public Land suggested that Treasury adopt the remote future event rule in lieu of the proceeds regulation. J.A. at 685 (Land Tr. Exchange Cmt. at 7); *id.* at 795 (Tr. for Pub. Land Cmt. at 7). The organizations' proposals refer to the provision of the regulations that bears the same name, Treas. Reg. § 1.170A-14(g)(3). The remote future event rule provides a "narrow exception to the perpetuity requirement" of I.R.C. § 170(h)(5)(A), *Hoffman Props.*, 956 F.3d at 837, allowing deductions when the conservation purpose of an easement may be defeated by an "act or event" whose occurrence is "so remote as to be negligible." Treas. Reg. § 1.170A-14(g)(3). Neither organization provided any indication of how expanding this rule—which permits deductions in the face of uncertainty—would fulfill Congress's express aim in I.R.C. § 170(h)(5)(A) of limiting deductions to those instances where an easement's conservation purpose can be safeguarded forever. Because Treasury could not ignore this goal, the agency was not required to respond to comments that would have led it to do so.

The Land Trust Exchange asserted that the tax benefit rule rendered the proceeds regulation unnecessary as well. J.A. at 685 (Land Tr. Exchange Cmt. at 7). Again, how so is unclear from the comment. The tax benefit rule allows a taxpayer to exclude "income attributable to the recovery during the taxable year of any amount deducted in any prior taxable year to the extent such amount did not reduce the amount of tax imposed by this chapter." I.R.C. § 111(a). This rule—which benefits the donor—bears no relation to the requirement under I.R.C. § 170(h)(5)(A) that an easement's conservation purpose be protected in perpetuity. Nor did the Land Trust Exchange Treasury provide an explanation that would have made it necessary for Treasury to consider the tax benefit rule in this context.

Finally, the other comments that the petitioners reference in passing did not raise significant concerns. Pet'r Br. at 33. Most comments provided only cursory commentary on Treas. Reg. § 1.170A-14(g)(6)(ii), often with either no discussion of the facts on which they were basing their criticisms, or only vague indications of the sources of these facts. *See Home Box Office*, *Inc.*, 567 F.2d at 35 n.58. Comments that provided alternatives to the proceeds regulation failed to discuss how these alternatives would satisfy I.R.C. § 170(h)(5)(A). *See* J.A. at 721 (Brandywine Conservancy Cmt. at 3); *id.* at 723 (Wash. Tr. for Hist. Pres. Cmt. at 1); *id.* at 801 (Ginsberg Cmt. at 5). Indeed, no comment that addressed the regulation raised a concern about it failing to satisfy that provision's perpetuity requirement. The APA thus did not require that Treasury provide a response to these comments either.

The petitioners' attempt to reach a different conclusion based on the facts of two of our cases—*Simms v. National Highway Traffic Safety Administration* and *PPG Industries*, *Inc. v. Costle*—falls short. *Simms* provides little guidance here. In that case, the National Highway Traffic Safety Administration (NHTSA) of the Department of Transportation promulgated a rule regarding how wheelchairs were to be secured on school buses based on "static" rather than "dynamic" testing of securements. 45 F.3d at 1005. Addressing challenges on the adequacy of NHTSA's response to comments that advocated for dynamic testing, we upheld the rule, pointing to the fact that, although NHTSA acknowledged in its concise general statement that "dynamic testing was the preferred approach among commentators," the agency had also "explained the benefits of using static testing and discussed its rationale for rejecting dynamic testing." *Id.* Besides the fact that in the present case there was no well-developed, "preferred approach" among the commentators that Treasury ignored, *Simms* illustrates only what an adequate response to significant comments looks like. But such comments were not before Treasury here.

PPG Industries is unhelpful as well. In that case, the Environmental Protection Agency (EPA) designated Summit County, Ohio as needing to take special air pollution abatement measures. *PPG Industries*, 630 F.2d at 464. The EPA had previously relied on faulty computer modelling in making its designation. *Id.* at 465. When the plaintiffs challenged the new designation, the EPA responded that it had "reanalyzed" the previously faulty data that it computed. *Id.* at 466. The EPA, however, was unable to point to anywhere in the administrative record to support this reanalysis. *Id.* We remanded to the agency so that an administrative record could be developed. *Id.* at 468. Although the petitioners in the present case rely on the fact that we criticized "EPA's perfunctory treatment" of comments that made it "impossible to determine whether the agency's Summit County designation was arbitrary [or] capricious," this misses the forest for the trees. *Id.* at 466. Unlike in *PPG Industries*, *Inc.*, there is no indication here that Treasury relied on faulty or impermissible premises in promulgating the proceeds regulation.

The petitioners also direct us to a recent decision by the Eleventh Circuit that held the proceeds regulation to be procedurally invalid under the APA. *See Hewitt v. Comm'r*, 21 F.4th 1336, 1339 (11th Cir. 2021). Unlike the concurrence, we find that decision's reasoning to be unpersuasive. In concluding that the New York Landmarks Conservancy's comment raised significant concerns about possible deterrent effects that the proceeds regulation could have on donations, the Eleventh Circuit stressed that one of I.R.C. § 170's aims is "to allow deductions for the donation of conservation easements to encourage donation for such easements." *Id.* at 1352. Although encouraging the donation of conservation easements is undeniably a goal of the statute, highlighting this point overlooks a crucial condition that Congress demanded be met by donors seeking deductions: an easement's conservation purpose must be "protected in perpetuity."[7] I.R.C. § 170(h)(5)(A).

That the proceeds regulation interprets I.R.C. § 170(h)(5)(A) and is meant to enforce Congress's goal

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[7] As noted *supra*, the committee reports emphasized this restriction, too. *See* H.R. REP. No. 96-1278, at 18; S. REP. No. 96-1007, at 13.

of limiting deductions to those instances in which the perpetuity requirement can be satisfied is evident from the regulations. Not only does the plain language of the proceeds regulation address this end, *see* Treas. Reg. § 1.170A-14(g)(6)(i) ("the conservation purpose can nonetheless be treated as protected in perpetuity" if the proceeds regulation is followed upon judicial extinguishment), but the rule is also part of a section in the regulations titled

"Enforceable in perpetuity," Treas. Reg. § 1.170A-14(g), that contemplates various scenarios in which the perpetuity requirement of I.R.C. § 170(h)(5)(A) would not be met, *see*, *e.g.*, Treas. Reg. § 1.170A-14(g)(2), *id.* § 1.170A-14(g)(4). Other than missing § 1.170A-14(g)(2), which regulates how mortgages impact the perpetuity requirement and was added in response to other comments, the proposed rule contained the same relevant language. *See* 48 Fed. Reg. at 22945–47. Put differently, I.R.C. § 170(h)(5)(A) embodies a particular policy that restricts deductions to where an easement's conservation purpose can be protected forever, and Treas. Reg. § 1.170A-14(g)(6)(ii) interprets how to implement that policy. The Eleventh Circuit's decision thus does not alter our conclusion that Oakbrook has failed to cite comments that raised valid concerns about how the regulation served this policy.

At this point, the concurrence interjects to accuse us of treating the perpetuity requirement of I.R.C. § 170(h)(5)(A) as a trump card. But we did not decide that perpetuity should play a vital role in the statutory scheme. Congress did. Even aside from the legislative history on which Treasury expressly relied in crafting the proceeds regulation, the statute's text makes it apparent that what Congress sought to encourage is not simply the donation of conservation easements as the concurrence believes. Rather, Congress intended to incentivize the donations of only those easements that met a highly circumscribed set of prerequisites. These easements must be "of a qualified real property interest," which includes the requirement that the interest contain a perpetual restriction on its use. I.R.C. § 170(h)(1)(A), (2)(C). Donations must be "to a qualified organization." I.R.C. § 170(h)(1)(B). And, of course, they must be "exclusively for conservation purposes"—purposes that must be ensured to endure forever. I.R.C. § 170(h)(1)(C), (5)(A). *Cf. Carlson*, 938 F.3d at 342, 345-46 (noting that "simplicity of structure" was one of the "fourteen [statutory] factors" that Congress explicitly deemed it necessary for the Postal Service to contemplate in rulemaking).

Congress has long understood that any deductions it crafts are to be "strictly construed." *Indopco*, *Inc. v. Comm'r*, 503 U.S. 79, 84 (1992) (citing *New Colonial Ice Co. v. Helvering*, 292 U.S. 435, 440 (1934); *Deputy v. Du Pont*, 308 U.S. 488, 493 (1940)). If there ever was an instance in which this canon of statutory interpretation lined up with congressional intent, it is one in which Congress created a deduction predicated on eternal, unending, ceaseless vigilance.

Such a requirement is strict indeed. We thus cannot do as the comments identified by petitioners did and overlook Congress's decision to emphasize that a conservation easement's purpose be protected in perpetuity. Instead, we agree with the Tax Court. Treasury's lack of a response to these comments does not jeopardize the validity of Treas. Reg. § 1.170A-14(g)(6)(ii).

C. *Chevron* Deference

The petitioners also challenge Treas. Reg. § 1.170A-14(g)(6)(ii) as violating *Chevron USA Inc. v. Natural Resources Defense Council*, *Inc.*, 467 U.S. 837 (1984). As background, the proceeds regulation implements I.R.C. § 170(h)(5)(A), which provides: "A contribution shall not be treated as exclusively for conservation purposes unless the conservation purpose is protected in perpetuity." Because the regulation does not allow donors to be compensated for post-donation improvements, the petitioners maintain that the proceeds regulation is not a permissible construction of I.R.C. § 170(h). We are unpersuaded.

"In *Chevron*, the Supreme Court observed that, pursuant to the principle of deference to administrative interpretations, 'considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer.'" *Alliance for Cmty. Media v. FCC*, 529 F.3d 763, 776 (6th Cir. 2008) (quoting *Chevron*, 467 U.S. at 844). To determine whether deference to Treasury's statutory interpretation is warranted, we employ the familiar, two-step *Chevron* analysis. *See Mayo Found. for Med. Educ. & Rsch. v. United States*, 562 U.S. 44, 53-58 (2011). "The initial question under step one of the *Chevron* framework is `whether Congress has directly spoken to the precise question at issue' by employing precise, unambiguous statutory language." *Alliance for Cmty. Media*, 529 F.3d at 776-77 (quoting *Chevron*, 467 U.S. at 842). It is undisputed that I.R.C. § 170(h)(5)(A), the provision requiring that the conservation purpose of a donation be "protected in perpetuity," does not speak to the precise question at issue: how judicial extinguishment affects the perpetuity requirement.

Our analysis thus proceeds to the second step of *Chevron*, which asks whether Treasury's interpretation was "based on a permissible construction of the statute." *Tennessee Hosp. Ass'n*, 908 F.3d at 1037-38 (quoting *Chevron*, 467 U.S. at 843). "If a statute is ambiguous, and if the implementing agency's construction is reasonable, *Chevron* requires a federal court to accept the agency's construction of the statute, even if the agency's reading differs from what the court believes is the best statutory interpretation." *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 980 (2005). "Whether an agency's construction is reasonable depends, in part, 'on the construction's "fit" with the statutory language, as well as its conformity to statutory purposes.'" *Good Fortune Shipping SA v. Comm'r*, 897 F.3d 256, 262 (D.C. Cir. 2018) (quoting *Goldstein v. SEC*, 451 F.3d 873, 881 (D.C. Cir. 2006)).

At its core, the petitioners' position centers on the fact that "[n]othing in § 170(h) suggests that a qualified organization must be compensated above the value of its qualified real property interest in the event the easement is extinguished." Pet'r Br. at 55. This statement is true, but incomplete: nothing in that section suggests that donors must be compensated for their post-donation improvements upon extinguishment either. Instead, the section is silent on what should happen if an easement is extinguished by judicial proceedings, including about what should happen with the value added by any post-donation improvements made by a donor.

Although it does not answer this exact question, the text of I.R.C. § 170(h)(5)(A) still provides direction. Section 170(h)(5)(A) requires that easements' conservation purposes be protected in perpetuity after the donation. This leaves donees responsible for stewarding the interest through eternity, a task that consumes not only time but resources, too.[8] A rule that, in the event of extinguishment, allowed donors to retain the value of post-donation improvements such as the petitioners propose would "likely enrich property owners at the public's expense, and leave donees with fewer proceeds with which to advance similar conservation purposes elsewhere." McLaughlin, *supra* at 139. Erring on the side of providing the donee with higher rather than lower proceeds, moreover, buoys the donee's ability to ensure that the conservation purpose of the easement continues upon extinguishment. With additional funds at its disposal, the conservation organization will likely have more options available to further the original conservation purpose in line with § 170(h)(5)(A). *See id.* at 136. Treasury Regulation § 1.170A-14(g)(6)(ii) does just that and is thus a reasonable interpretation of the section.

Bolstering the reasonableness of the proceeds regulation is the fact that Congress has amended I.R.C. § 170 over thirty times during the past thirty-four years but has not voided Treas. Reg. § 1.170A-14(g)(6)(ii). *See Oakbrook Land Holdings*, 154 T.C. at 199-200, 199 n.5 (cataloguing amendments to § 170). "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." *Cottage Sav. Ass'n v. Comm'r*, 499 U.S.

[8] As also noted *supra*, the legislative history that Treasury cited in its notice of proposed rulemaking confirms that Congress was concerned about donees having sufficient resources to ensure that an easement's conservation purpose be protected in perpetuity. *See* H.R. REP. No. 96-1278, at 19; S. REP. No. 96-1007, at 14.

554, 561 (1991) (quoting *United States v. Correll*, 389 U.S. 299, 305-06 (1967)). Over three decades of congressional acquiescence to the proceeds regulation leaves us confident that the regulation is owed our deference under *Chevron.*

Against this conclusion, the petitioners point to the other provision of I.R.C. § 170(h) that contains a perpetuity requirement, § 170(h)(2)(C). This subsection provides the definition of "qualified real property interest," which is "a restriction (granted in perpetuity) on the use which may be made of the real property." I.R.C. § 170(h)(2)(C). According to the petitioners, a donee has no interest in donor improvements under this subsection, and therefore it is unreasonable to give a donee the proceeds after judicial extinguishment that result from a donor's post-donation improvements.

Whatever else I.R.C. § 170(h)(2)(C) requires, the petitioners have not established that it requires donors to receive the value of their post-donation improvements. The subsection's text does not dictate this outcome, for all that it provides is that a qualified real property interest both be a restriction on the use of real property, and that the restriction be "granted in perpetuity." *Id.* Subsection 170(h)(2)(C) simply does not encompass post-donation improvements or suggest to whom their value should accrue upon judicial extinguishment. That gap was left for Treasury to fill, as it reasonably did with the proceeds regulation.

D. Arbitrary or Capricious Review

Coupled with their *Chevron* argument, the petitioners argue that Treasury acted arbitrarily or capriciously in promulgating Treas. Reg. § 1.170A-14(g)(6)(ii) for two distinct reasons: because Treasury provided no explanation for why it adopted the rule, and because Treasury failed to consider a variety of alternatives.[9] Neither argument is convincing.

When determining whether a final agency action is arbitrary or capricious, the scope of our review is "an extremely narrow one." *Navistar Int'l Transp. Corp.*, 941 F.2d at 1352. A court may not "substitute its judgment for that of the agency." *Greenbaum v. U.S. EPA*, 370 F.3d 527, 542 (6th Cir. 2004) (quoting *Bowman Transp., Inc. v. Arkansas-Best Freight Sys., Inc.*, 419 U.S. 281, 285 (1974)). Instead, we consider whether "the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Ne. Ohio Reg'l Sewer Dist. v. U.S. EPA*, 411 F.3d 726, 731 (6th Cir. 2005) (quoting *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co. (State Farm)*, 463 U.S. 29, 43 (1983)). "Even when an agency explains its decision with less than ideal clarity, a reviewing court will not upset the decision on that account if the agency's path may reasonably be discerned." *Id.* (quoting *Alaska Dep't of Env't Conservation v. U.S. EPA*, 540 U.S. 461, 497 (2004)).

The petitioners' first argument for why Treas. Reg. § 1.170A-14(g)(6)(ii) is arbitrary or capricious duplicates their argument for why the rule's concise general

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[9] The petitioners insist that their arbitrary-or-capricious arguments are part of the *Chevron* analysis. Because we have previously analyzed these issues separately, *see Atrium Med. Cir. v. U.S. Dep't of HHS*, 766 F.3d 560, 567 (6th Cir. 2014), we do so here.

statement of basis and purpose is deficient. In essence, the petitioners argue that the proceeds regulation could not be the product of reasoned decision-making because Treasury provided no explanation for why the agency settled on that formula for calculating proceeds. Yet given the context of the rulemaking and the statutory issue that the agency confronted, we reiterate that the concise statement of basis and purpose that accompanied the proceeds regulation adequately explained Treasury's rationale: to create an administrable mechanism for enforcing I.R.C. § 170(h)(5)(A)'s perpetuity requirement.

Insofar as the petitioners try to bolster their arbitrary-or-capricious argument by relying on *SEC v. Chenery Corp.*, 318 U.S. 80, 88 (1943), this, too, fails. In *Chenery*, the Supreme Court limited the grounds on which an agency's action could be upheld to those on which the agency relied at the time. 318 U.S. at 88. Under this rule, an agency must defend its actions based on the reasons that animated the act at issue, not for reasons that it formulated during litigation. *State Farm*, 463 U.S. at 50. *Chenery* does not, however, narrow our inquiry into an agency's contemporaneous rationale solely to the concise general statement. *See State Farm*, 463 U.S. at 43. As the Supreme Court has held in the context of determining whether a particular statutory interpretation guided an agency's actions, courts may accept the explanation provided by an agency during litigation for its conduct when this is "the only plausible explanation" of the course taken in the rulemaking. *Nat'l R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407, 420 (1992); *see also Nat'l Elec. Mfrs. Ass'n v. U.S. Dept. of Energy*, 654 F.3d 496, 513 (4th Cir. 2011).

Such is the case here. Contrary to what the petitioners maintain, the Commissioner's rationale for the proceeds regulation—namely, that it was promulgated to create an administrable rule which ensured that a donee would receive sufficient funds upon extinguishment to continue the conservation purpose—aligns with the obvious concern evinced by Treasury during the rulemaking process that I.R.C. § 170(h)(5)(A)'s perpetuity requirement be satisfied in the event of judicial extinguishment. This rationale both tethered the regulation to its statutory source and left us a clear thread to trace how Treasury navigated between these two points. Treasury's citations to the committee reports provided further guidance into its decision to craft a rule that stood to benefit donees over donors upon extinguishment, an aim which coincided with Congress's "major policy decisions" concerning which entity should be favored post-donation.[10] 48 Fed. Reg. at 22940.

Moving to the petitioners' second rationale, none of the alternatives to which they point required Treasury's consideration. Two sources of possible alternatives—the RESTATEMENT (THIRD) OF PROPERTY § 7.11 (Am. Law. Inst. 2000) and the testimony of SLRC's Executive Director, James Wright, at the trial before Judge Holmes in 2016, *see* J.A. 405-08 (Wright Test. Tr. at 205-08); Pet'r Br. at 51—did not exist when Treasury was promulgating the proceeds regulation in the 1980s. "[A] rulemaking 'cannot be found wanting

[10] The concurrence would have us ignore the Supreme Court because of its reading of *National Railroad. Passenger Corp.* as a "dead letter in legal history." Concur. op. at 37. We must, however, decline to conclude that "more recent cases have, by implication, overruled an earlier precedent" of the Court. *Agostini v. Felton*, 521 U.S. 203, 237 (1997).

simply because the agency failed to include every alternative device and thought conceivable by the mind of man . . . regardless of how uncommon or unknown that alternative may have been"—or, in this case, regardless of how distant in the future that alternative was from existing. *State Farm*, 463 U.S. at 51 (quoting *Vermont Yankee*, 435 U.S. at 551); *see also Simms*, 45 F.3d at 1006.

The petitioners also flag a Maryland statute that governed condemnation awards and which the Maryland Agricultural Land Preservation Foundation attached to its comment. *See* J.A. at 742 (Md. Agric. Land Pres. Found. Cmt. attach.). According to the petitioners, this statute provided an alternative approach to how Treas. Reg. § 1.170A-14(g)(6)(ii) allocates proceeds. If it did, however, the Maryland Agricultural Land Preservation Foundation apparently did not think so. The organization's comment neither drew attention to this statute, nor put it forward as an alternative to the proceeds regulation. Instead, the Maryland Agricultural Land Preservation Foundation lumped this statute in with a series of laws from which the organization derived its legislative mandate. *Id.* at 725 (Md. Agric. Land Pres. Found. Cmt. at 1). Because even the organization that cited the statute did not consider it to be an alternative to the proceeds regulation, Treasury did not have to assess whether it was one.

Finally, the petitioners' heavy reliance on *State Farm* and *Judulang v. Holder*, 565 U.S. 42 (2011), to support their arbitrary-or-capricious arguments is misplaced. In *State Farm*, the alternative that the agency failed to consider—airbags—was well-known at the time, including to the agency itself. *See* 463 U.S. at 48. In *Judulang*, the agency had applied diverse statutory factors in an arbitrary manner. *See* 565 U.S. at 58-59. The petitioners have not pointed to an alternative to the proceeds regulation that was both well established and that Treasury ignored. Additionally, the regulation is a reasonable way to ensure that the perpetuity requirement of I.R.C. § 170(h)(5)(A) is protected in the event of a judicial extinguishment of a conservation easement. Therefore, Treasury acted neither arbitrarily nor capriciously in promulgating Treas. Reg. § 1.170A-14(g)(6)(ii).

III. CONCLUSION

For the foregoing reasons, we AFFIRM the judgment of the Tax Court upholding the procedural and substantive validity of Treas. Reg. § 1.170A-14(g)(6)(ii).

CONCURRING IN THE JUDGMENT

RALPH B. GUY, JR., Circuit Judge, concurring in the judgment only. The Department of the Treasury must play by the same rules as other federal agencies. The Supreme Court made that clear when it refused to "carve out an approach to administrative review good for tax law only" and "expressly 'recognized the importance of maintaining a uniform approach to judicial review of administrative action.'" *Mayo Found. for Med. Educ. & Rsch. v. United States*, 562 U.S. 44, 55 (2011) (cleaned up) (quoting *Dickinson v. Zurko*, 527 U.S. 150, 154 (1999)). But it seems the majority opinion has done the opposite for Treasury's proceeds regulation (Treas. Reg. § 1.170A-14(g)(6)(ii)). In my view, the regulation is procedurally invalid under the Administrative Procedure Act (APA) for substantially the same reasons stated by the Eleventh Circuit in *Hewitt v. Commissioner of IRS*, 21 F.4th 1336 (11th Cir. 2021), and by the concurring and dissenting opinions in *Oakbrook Land Holdings*, *LLC v. Commissioner of IRS*, 154 T.C. 180, 200-30 (2020) (Toro, J., concurring in the judgment, joined in full by Urda, J., and joined in part by Gustafson and Jones, JJ.); *id*. at 230-259 (Holmes, J., dissenting). But I would conclude that the Commissioner's statutory argument is not forfeited and affirm on that basis.

I.

The proceeds regulation at issue is procedurally invalid under 5 U.S.C. §§ 553(c), and 706(2)(A), of the APA. *Hewitt*, 21 F.4th at 1350-53; *Oakbrook*, 154 T.C. at 216-30 (Toro, J., concurring in the judgment); *id.* at 230-53 (Holmes, J., dissenting).[1]

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[1] Insofar as it concerns the validity of the proceeds regulation, this case is materially identical to *Hewitt* because, there, the tax

"One of the basic procedural requirements of administrative rulemaking is that an agency must give adequate reasons for its decisions." *Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 221 (2016). Further, lain agency must consider and respond to *significant comments* received during the period for public comment." *Perez v. Mortg. Bankers Ass'n*, 575 U.S. 92, 96 (2015) (emphasis added) (collecting cases). Treasury cannot get by without any explanation for the regulation and without responding to the *significant* comment submitted by the New York Land Conservancy (NYLC). *See* 51 Fed. Reg. 1496, 1496 (Jan. 14, 1986). (*Contra* Maj. Op. 6, 10, 16).

As the Eleventh Circuit held, NYLC's comment "was significant and required a response by Treasury to satisfy the APA's procedural requirements." *Hewitt*, 21 F.4th at 1351. Because Treasury "failed to respond to NYLC's significant comment concerning the post-donation improvements issue as to proceeds, it violated the APA's procedural requirements." *Id.* at 1353.

The majority opinion makes NYLC's four-page comment seem insignificant by condensing it to one sentence and omitting the most important part. *Compare* (Maj. Op. 16), *with Hewitt*, 21 F.4th at 1345 (quoting extensively from NYLC's comment). In part, NYLC's comment made the following points:

1. Most importantly, NYLC stated that the proceeds regulation "contemplates that a ratio of value of the conservation restriction to value of the fee will be fixed at the time of the donation and will remain in effect

court decided the case based upon its *Oakbrook* decision. *Hewitt*, 21 F.4th at 1339. But the Eleventh Circuit reversed—and rightly so. *Id.* at 1353.

forever thereafter. *This formula fails to take into account that improvements may be made thereafter by the owner which should properly alter the ratio."* J.A. 671 (emphasis added). NYLC drove the point home with a specific example. Suppose the owner of property worth $100,000 grants a "scenic easement" worth 10% of the value of the entire parcel, guaranteeing that the owner of Parkacre and his successors will never build high-rise buildings in order to ensure Parkacre is a place to enjoy nature and sunlight. *See* J.A. 670-71; *see also* 48 Fed. Reg. 22940, 22944-55 (May 23, 1983). The parcel owner then spends $2 million to build rental housing units on the parcel. *Id.* If the easement is later extinguished in eminent domain proceedings for the parcel, "the donee organization would be entitled . . . to 10% of the sale price of the entire parcel including the improvements," i.e., 10% of $2.1 million. J.A. 671. *"This would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization." Id.* (emphasis added).

2. NYLC thus contended that the proceeds regulation "contain[s] *problems of policy and practical application* so pervasive as to cause [NYLC] to recommend strongly the deletion of these provisions. *The statute was enacted by Congress to encourage the protection of our significant natural and built environment through the donation of conservation restrictions and yet*, *the proposed provisions would thwart the purpose*

of the statute by deterring prospective donors." J.A. 670 (emphasis added).

3. NYLC spoke from first-hand experience, recounting that "it is our experience that prospective donors frequently raise the question that 'perpetuity' is a long time and may impose unforeseeably heavy burdens on themselves or future owners under unforeseeable future circumstances. We find ordinarily that these concerns are mollified upon the donor's recognition that common law permits extinguishment of restrictions . . . . Obviously, the prospect of extinguishment would no longer mollify these fears if a split of proceeds under unknown circumstances would be required." J.A. 670-71.

4. NYLC—a donee organization—emphasized that "[t]he value of a conservation restriction to the donee organization is not a monetary value but a philanthropic value as a device for achieving the charitable objectives of the organization," such that "the extinguishment of a conservation restriction cannot be compensated by the payment of money." J.A. 671. To that end, NYLC stated that it "would prefer to eliminate" the proceeds regulation rather than "trade on the prospect of future windfalls when restrictions are extinguished." *Id.*

5. "In light of the potential inequities described," NYLC concluded by *"recommend[ing] that the proposed proceeds formula be revised to prevent such inequities,"* but *"strongly recommend[ed] deletion of the*

> *entire extinguishment provision."* J.A. 672 (emphasis added).

NYLC's comment was "significant": It "show[ed] why [a] mistake was of possible significance in the results." *Vt. Yankee Nuclear Power Corp. v. Nat. Res. Def. Council*, *Inc.*, 435 U.S. 519, 553 (1978) (quoting *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375, 394 (D.C. Cir. 1973)). The comment is significant for two principal reasons.

First, NYLC's comment is significant because it showed that the regulation "would thwart" one of "the purpose[s] of the statute by deterring prospective donors." J.A. 670; *accord Hewitt*, 21 F.4th at 1351. That is, "[o]ne of the policy decisions reflected in th[e] 'committee reports,' expressly referenced by Treasury," *Hewitt*, 21 F.4th at 1351 (quoting 48 Fed. Reg. at 22940), "provided that 'the preservation of our country's natural resources and cultural heritage is important,' that 'conservation easements now play an important role in preservation efforts,' and that 'provisions allowing deductions for conservation easements should be directed at the preservation of unique or otherwise significant land areas or structures.'" *Id.* (quoting S. REP. No. 96-1007, at 9 (1980)); *see also BC Ranch II*, *L.P. v. Comm 'r of IRS*, 867 F.3d 547, 553-54 (5th Cir. 2017).

Second, NYLC cast doubt on the reasonableness of the regulation's formula and further showed that it would "obviously" deter donors because "the regulation's proceeds formula: (1) 'contemplates that a ratio of value of the conservation restriction to value of the fee will be fixed at the time of the donation and will remain in effect forever thereafter'; and (2) 'fail[ed] to take into account that improvements may be made thereafter by the owner which should properly alter the ratio.' *Hewitt*, 21 F.4th at 1351 (quoting NYLC's comment); *see* J.A. 670-71. The majority opinion does not grapple with this second aspect of the reasoning in *Hewitt.* If it was a significant comment to suggest that an agency's uniform cook temperature for all fish should be altered to each species of fish so that the product is not destroyed, *United States v. Nova Scotia Food Prods. Corp.*, 568 F.2d 240, 243, 252-53 (2d Cir. 1977); (Maj. Op. 15-16), then NYLC's comment was likewise significant because it argued that a donor's post-donation improvements "should properly alter the ratio" so that Congress's tax incentive for prospective donors is not destroyed. J.A. 671.

Treasury might have explained that post-donation improvements might cause a slight *indirect* increase in the value of an easement and that the donee should reap the total value *of the easement.* But Treasury did not. More importantly, Treasury left everyone to wonder: Why would the easement holder be entitled to receive a proportional percentage of the *actual value of* the donor's post-donation improvements, i.e., rental housing units or a country club and golf course? Why would the statutory tax deduction incentivize any donor to grant a conservation easement if it means the donor (and any successors) must agree to give the donee the easement proceeds *and* a proportional ratio of *any* future improvements in the event of judicial extinguishment? Or why would Treasury require that the value of separate property rights (the easement and the property burdened) *always* maintain a proportional value relationship when "there is commonly little, if any, relation." RESTATEMENT (FIRST) OF PROPERTY § 508 cmt. b (Am. Law. Inst. 1944). This court should not "sanction silence in the face of such vital questions." *Nova Scotia Food Prods.*, 568 F.2d at 253.[2]

The bottom line is there is no doubt that NYLC's comment "'can be thought to challenge [two] fundamental premise[s]' underlying the proposed agency decision" and Treasury failed to respond. *Carlson v. Postal Regul. Comm'n*, 938 F.3d 337, 344 (D.C. Cir. 2019) (quoting *MCI WorldCom, Inc. v. FCC*, 209 F.3d 760, 765 (D.C. Cir. 2000)); *see Hewitt*, 21 F.4th at 1351-52. (*Contra* Maj. Op. 15-16 (stating the same test but a contrary conclusion). In other words, Treasury's decision is arbitrary and capricious because it "entirely failed to consider [these] important aspect[s] of the problem." *Nat'l Ass'n of Home Builders v. Defs. of Wildlife*, 551 U.S. 644, 658 (2007) (quoting *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983)).

Two of the cases Oakbrook relies upon underscore the errors in this case. Both cases invalidated agency action because the agency's explanation was insufficient.

At issue in *Dominion Resources, Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012), was a Treasury

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[2] The Restatement (Second) of Property did not address easements because the Restatement (First) of Property remained the prevailing rules for easements at the time Congress added the perpetuity requirements in I.R.C. § 170(h)(2)(C), and (h)(5)(A). *See* RESTATEMENT (SECOND) OF PROPERTY: LANDLORD AND TENANT intro. (Am. L. Inst. 1983), and intro RESTATEMENT (SECOND) OF PROPERTY: DONATIVE TRANSFERS. (Am. L. Inst. 1977). The law of easements was not revisited until 2000, but even then the changes were intended to "simplif[y] and clarif[y] this area of the law and were largely a matter of "form rather than of substance." *See* RESTATEMENT (THIRD) OF PROPERTY: SERVITUDES intro. (Am. L. Inst. 2000).

regulation interpreting "the avoided-cost rule set out in the statute at I.R.C. § 263A(f)(2)(A)(ii)," "as applied to property temporarily withdrawn from service." 681 F.3d at 1317. *Dominion* explained that the notice of proposed rulemaking "provided no rationale other than the general statement that the regulations are intended to implement the avoided-cost method." *Id.* at 1319. Here, Treasury did not even do that much. And, as in this case, the agency in *Dominion* "provided no rationale in the final regulations." *Id.* The Federal Circuit reversed the trial court because it "erroneously stretched to conclude that 'the path that Treasury was taking in the rulemaking proceedings can be discerned, albeit somewhat murkily.'" *Id.*

Treasury gave us even less to work with than in *Dominion.* Here, the notice of proposed rulemaking simply stated that the regulations relate to "contributions not in trust of partial interests in property" under "section 6 of the Tax Treatment Extension Act of 1980" and that "[t]he regulations reflect the major policy decisions made by the Congress and expressed in these committee reports." 48 Fed. Reg. at 22940. The final regulations merely stated that the "regulations provide necessary guidance to the public for compliance with the law and affect donors and donees of qualified conservation contributions." 51 Fed. Reg. at 1496. From these statements and the use of "protected in perpetuity" in Treas. Reg. § 1.17A-14(g)(6)(i), the majority opinion stretches to conclude that Treasury "tethered the regulation to its statutory source and left us a clear thread to trace how Treasury navigated between these two points." (Maj. Op. 25).

We may be able to discern that Treasury was interpreting Congress's perpetuity requirement, but the thread stops there. As in *Dominion*, the proceeds regulation is invalid because Treasury provided "no explanation for the way that use of [a fixed ratio at the time of the grant] implements the [protected-in-perpetuity] rule." 681 F.3d at 1319. Treasury compounded its error by failing to address NYLC's significant comment that post-donation improvements should "properly alter the ratio," rather than be divvied up according to a ratio fixed at the time of the grant.[3]

The reasoning in *Carlson v. Postal Regulatory Commission*, 938 F.3d 337 (D.C. Cir. 2019), explains why NYLC's comment required a response. *Carlson* considered an agency's decision to increase the cost of letter stamps by five cents. 938 F.3d at 341. The Postal Service's proposal noted that "keeping the price of stamps 'at round numbers divisible by five" would help achieve one of the statutory goals, "simplicity of structure." *Id.* at 342. Carlson, a "postal customer and watchdog," chimed in during notice-and-comment, arguing: (1) that "keeping the price of a stamp divisible by five did not promote the value of 'simplicity of structure"; (2); that "raising the price of stamps by five

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[3] The majority opinion cites three rare cases from other circuits for the proposition that a statement of basis and purpose is not necessary "where the basis and purpose [are] considered obvious." (Maj. Op. 11 (quoting *Cal-Almond*, *Inc. v. U.S. Dep't of Agric.*, 14 F.3d 429, 443 (9th Cir. 1993)). But the basis for Treasury's fixed-ratio formula is far from obvious. This is not a case where the agency used a "mechanical application of the statutory formula" to merely set a rate per pound of almonds to fund its operations, as required. *See Cal-Almond*, 14 F.3d at 433, 439, 443. Here, Treasury *created a formula* for the division of proceeds from the sale of discrete property interests based upon the word "perpetuity," I.R.C. § 170(h)(2)(C), and (h)(5)(A), or at least that is what we can gather from the proceeds regulation itself because Treasury did not provide an explanation.

cents was inconsistent with the statutory objective of 'establish[ing] and maintain[ing] a just and reasonable schedule for rates' (similar to NYLC's argument that the fixed-ratio formula is flawed and would "thwart" the statutory goal of encouraging conservation easements); and (3) that "the detrimental 'effect of rate increases upon the general public' weighed against the Postal Service's proposal" (analogous to NYLC's statement that "problems of policy and practical application" and "inequities" weighed in favor of revising the regulation or deleting it altogether). *Id.* at 342, 345-47 (alterations in original). The agency did not respond to Carlson's comments, but it did more than Treasury here; it at least "referenced, but did not resolve, Carlson's" first point. *Id.* at 342. The court held that all of Carlson's comments were significant and "warranted [a] response" because they concerned "several relevant statutory objectives and factors." *Id.* at 345. "By failing to consider relevant statutory objectives and factors and declining to respond to significant public comments, the Commission violated the APA when it approved the stamp price hike." *Id.* at 351. The same is true here.

The majority opinion acknowledges that "encouraging the donation of conservation easements is undeniably a goal of the statute." (Maj. Op. 19). Yet it treats one other statutory goal—perpetuity—as a trump card, such that Treasury was free to ignore any comment unless the comment showed that the regulation "fail[ed] to satisfy" the "perpetuity requirement." (Maj. Op. 18; *see id.* 16-21, 23-24).

On the contrary, "[e]ven when an agency has significant discretion in deciding how much weight to accord each statutory factor, that does not mean it is free to ignore any individual factor entirely." *Carlson*, 938 F.3d at 344 (cleaned up) (quoting *Tex. Oil & Gas Ass'n v. EPA*, 161 F.3d 923, 934 (5th Cir. 1998)); *see also Intl Ladies' Garment Workers' Union v. Donovan*, 722 F.2d 795, 818 (D.C. Cir. 1983) (holding that the agency "must explain why a particular proposal is inconsistent with the balance between regulation and competition" (citation omitted)); *Nova Scotia Food Prods.*, 568 F.2d at 253 ("[T]he administrative process should disclose, at least, whether the proposed regulation is considered to be commercially feasible, or whether other considerations prevail even if commercial infeasibility is acknowledged."). As in *Carlson*, Treasury "also failed to evaluate how other statutory objectives and factors," such as encouraging the donation of conservation easements, "might bear on the proposed [proceeds regulation] or outweigh [Treasury's *purported*] reliance on" the perpetuity requirement. *Id.* at 347.

Treasury was required to *explain to the public*, why post-donation improvements are not taken into account and why it balanced the competing statutory interests in favor of adopting a fixed-ratio formula. "[A]n agency may justify its policy choice by explaining why [its] policy 'is more consistent with statutory language' than alternative policies," but Treasury is not permitted to remain silent and leave it for a court to "supply a reasoned basis for the agency's decision." *Encino Motorcars*, 579 U.S. at 223 (citation omitted). (*Contra* Maj. Op. 13, 19-20, 22, 25).

Against this backdrop, NYLC's comment required a response because it was based on first-hand experience, and common sense for that matter; it challenged the logic of the fixed-ratio formula that Treasury created; and it raised relevant statutory objectives. After all, if individuals "must turn square corners when they deal with the Government," it is only fair that "the Government should turn square corners in dealing with the people." *Dep't of Homeland Sec. v. Regents of the Univ. of Cal.*, 140 S. Ct. 1891, 1909 (2020) (citations omitted). Because Treasury failed to respond to NYLC's comment, the proceeds regulation is procedurally invalid.

The majority opinion concedes that "if an agency could ignore every comment regardless of its content, then the process of soliciting public input would be pointless." (Maj. Op. 14 (citing *Sherley v. Sebelius*, 689 F.3d 776, 784 (D.C. Cir. 2012)). But in the end, the majority has rendered that process meaningless because Treasury provided no explanation for its decision and Treasury ignored NYLC's *significant* comment and every other comment about the proceeds regulation.

II.

Treasury's decision to remain silent has consequences: We cannot rely on *post hoc* explanations; nor can a court offer the reasons that might have supported Treasury's decision. The majority explains why the proceeds regulation is needed to implement the statute's protected-in-perpetuity requirement and why, as a matter of policy, the division of extinguishment proceeds should be "more favorable to donees than to donors," such that the easement holder should receive a fixed ratio of the actual value of the *donor's* post-donation improvements. (Maj. Op. 13, 19-20, 22, 25). The problem is that Treasury did not provide these reasons at the time it promulgated the proceeds regulation.

"It is a 'foundational principle of administrative law' that judicial review of agency action is limited to 'the grounds that the agency invoked when it took the action.'" *Dep't of Homeland Sec.*, 140 S. Ct. at 1907 (quoting *Michigan v. EPA*, 576 U.S. 743, 758 (2015)). "It is not the role of the courts to speculate on reasons that might have supported an agency's decision. [W]e may not supply a reasoned basis for the agency's action that the agency itself has not given.'" *Encino Motorcars*, 579 U.S. at 224 (quoting *State Farm*, 463 U.S. at 43). That also means "courts may not accept . . . counsel's *post hoc* rationalizations for agency action." *State Farm*, 463 U.S. at 50. This "rule serves important values": It promotes "agency accountability"; instills "confidence that the reasons given are not simply 'convenient litigating position[s]'"; and preserves "the orderly functioning of the process of review." *Dep't of Homeland Sec.*, 140 S. Ct. at 1909 (citations omitted).

The Commissioner's brief and the majority opinion offer a similar rationale and cite the same law review article published in 2021. (Appellee Br. 61-63; Maj. Op. 13, 22). But "[t]he functional reasons for requiring contemporaneous explanations apply with equal force regardless whether *post hoc* justifications are raised in court by those appearing on behalf of the agency or by agency officials themselves." *Dep't of Homeland Sec.*, 140 S. Ct. at 1909.

Yet the claim is made that: "[T]he Supreme Court has held in the context of determining whether a particular statutory interpretation guided an agency's actions, courts may accept the explanation provided by an agency during litigation for its conduct when this is 'the only plausible explanation' of the course taken in the rulemaking." (Maj. Op. 25 (quoting *Nat'l R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407, 420 (1992)).

But *Boston & Maine Corp.* is not relevant. There, the Court addressed an agency's "interpretation of the word 'required,'" which the agency "did not in so many words articulate" in the context of an *adjudication—not* notice-and-comment rulemaking. *See id.* at 409-10; *United States v. Mead Corp.*, 533 U.S. 218, 230 n.12 (2001). Moreover, the Court deferred to the agency's "position before the Court" because "the only plausible explanation" of the agency's opinion was that the agency's adjudicative "decision was based on the [same] proffered interpretation." 503 U.S. at 418, 420. That is a world apart from the situation here: a proceeds regulation interpreting the statutory requirements that a deed must grant an easement "in perpetuity" for a "conservation purpose [that] is protected in perpetuity." I.R.C. § 170(h)(2)(C), (h)(5)(A). It is one thing to say that it is obvious Treasury's regulation is interpreting the protected-in-perpetuity requirement. But it is a stretch to say that there *is only one* plausible rationale (if any) for a regulation that divides proceeds according to a fixed ratio set at the time of the easement grant. Otherwise, *Boston & Maine* would swallow the rule that we may consider "only contemporaneous explanations for agency action." *Dep't of Homeland Sec.*, 140 S. Ct. at 1908.

The Supreme Court has never again so much as mentioned the statement the majority relies on from *Boston & Maine*. Instead, the Court has since repeatedly said the opposite, and that shows *Boston & Maine* is a dead letter in legal history. *See* 503 U.S. at 425-28 (White, J., joined by Blackmun and Thomas, JJ., dissenting) (arguing *State Farm* controls and "the majority is simply wrong" to defer to "the *post hoc* rationalization of Government lawyers"); *cf. Trump v. Hawaii*, 138 S. Ct. 2392, 2423 (2018). There is no reason to resurrect the statement in *Boston & Maine*.

III.

The proceeds regulation also does not survive *Chevron*. Where, as here, the rulemaking process was "procedurally defective," a regulation does not receive *Chevron* deference. *Household Credit Servs. v. Pfennig*, 541 U.S. 232, 242 (2004) (quoting *Mead*, 533 U.S. at 227); *accord Mayo Found.*, 562 U.S. at 53; *see*, *e.g.*, *Encino Motorcars*, 579 U.S. at 220-21, 224.[4]

IV.

But this does not mean Oakbrook should prevail outright. Because Oakbrook's deed calls for the donee to receive a *fixed amount* in the event of a judicial extinguishment, the deed violates the plain language of Congress's requirement that the conservation easement must be granted in perpetuity under I.R.C. § 170(h)(2)(C). (Appellee Br. 32-35, 37); *see Oakbrook*, 154 T.C. at 204-07 (Toro, J., concurring in the judgment, joined by Gustafson, Urda, and Jones, JJ.).

Congress did not require much as it relates to "perpetuity." The easement deed need only impose "a restriction (granted in perpetuity) on the use which may be made of the real property," I.R.C. § 170(h)(2)(C), and ensure that "the conservation purpose" (the restriction) is "protected in perpetuity," § 170(h)(5)(A); *see also* Pub. L. No. 96-541, § 6, 94 Stat. 3204, 3206-07 (1980). At the time of enactment in 1980, dictionaries defined "perpetuity" as "forever." *Hoffman Props. II*, *LP v. Comm'r of IRS*, 956 F.3d 832, 834 (6th Cir. 2020) (citations omitted).

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[4] The Eleventh Circuit decided not to reach the claimants' *Chevron* arguments because it concluded that Treas. Reg. § 1.170A-14(g)(6)(ii) is procedurally invalid under the APA. *Hewitt*, 21 F.4th at 1339 n.1.

"Property is often described as a bundle of rights or sticks," meaning "that ownership of property involves certain 'sticks' (or 'strands') of legal rights"—e.g., the right to possess, the right to use and develop, the right to exclude, the right to convey, and the right to profit from property—and thus "the aggregate of all of the sticks constitutes the full 'bundle' of rights." *See* 2A JULIUS L. SACKMAN ET AL., NICHOLS ON EMINENT DOMAIN § 6.01(8) (Matthew Bender 3d ed. 2021), and accompanying footnotes; *see also Andrus v. Allard*, 444 U.S. 51, 65-67 (1979); *Kaiser Aetna v. United States*, 444 U.S. 164, 176 (1979). An easement is "[a]n interest in land owned by another person" that "may last forever, but it does not give the holder the right to possess, take from, improve, or sell the land." *Easement*, BLACK'S LAW DICTIONARY (11th ed. 2019); *see also* RESTATEMENT (FIRST) OF PROPERTY §§ 450, 452 (Am. L. Inst. 1944). By 1965, it was well understood that a "conservation easement" "permanently restricts or imposes affirmative obligations on the property's owner or lessee to retain or protect natural, scenic, or open-space values of real property, . . . while allowing the landowner to continue to own and use the land, sell it, or transfer it to heirs." *Easement (conservation easement)*, BLACK'S LAW DICTIONARY, *supra*.

With that understanding, the statute only requires a donor to give a qualified organization one right from the bundle—the right to forever prevent uses of the property in a way inconsistent with the qualified conservation purpose. *See*, *e.g.*, *Hoffman Props.*, 956 F.3d at 835; *Pine Mt. Pres. v. Comm'r of IRS*, 978 F.3d 1200, 1206 (11th Cir. 2020); *BC Ranch II*, 867 F.3d at 551-54. Oakbrook's deed does that. *See* J.A. 112-19. Oakbrook holds all the remaining rights.

From there, the statute requires that the easement be "granted in perpetuity," I.R.C. § 170(h)(2)(C), meaning the donee must "*hold* [that] property interest in perpetuity[.]" *Glass v. Comm'r of IRS*, 471 F.3d 698, 713 (6th Cir. 2006) (cleaned up; emphasis added). When that provision was enacted, the blackletter law of property dictated that "[u]pon the extinguishment of an easement by eminent domain, the owner of the easement is entitled to compensation *measured by the value of the easement*." RESTATEMENT (FIRST) OF PROPERTY § 508 (emphasis added); *see also id.* § 508 cmt. b ("Fair value for purposes of the award is the loss to the owner of the easement[.]"); *id*. § 566 cmt. b. Indeed, the Supreme Court "repeatedly held that just compensation normally is to be measured by 'the market value of the property *at the time of the taking* contemporaneously paid in money.'" *United States v. 50 Acres of Land*, 469 U.S. 24, 29 (1984) (emphasis added) (quoting *Olson v. United States*, 292 U.S. 246, 255 (1934)); *accord Horne v. Dep't of Agric.*, 576 U.S. 351, 368-69 (2015).[5] Today, Tennessee follows the same rules.[6]

[5] The Restatement (First) of Property articulates the prevailing rules for easements at the time Congress added the perpetuity requirements in I.R.C. § 170(h)(2)(C), and (h)(5)(A). *See supra* n.2.

[6] "The appraisal shall value the property considering its highest and best use, its use *at the time of the taking*, and any other uses to which the property is legally adaptable *at the time of the taking."* Tenn. Code Ann. § 29-17-1004 (emphasis added); *see also id.* § 29-17-902 (providing that the condemning governmental authority "shall proceed to determine what it deems to be the amount of damages to which the owner is entitled because of the taking of such property or property rights"); *id.* § 29-17-910 ("*In all instances the amount to which an owner is entitled* shall

Oakbrook's deed, however, limits the donee's proceeds to a fixed amount determined *at the time of the grant.* J.A. 121-22. Oakbrook admits that "'perpetuity'—as used in connection with conservation easements—draws on the term's common-law meaning and denotes only that the granted property won't automatically revert to the grantor, his heirs, or assigns." *Pine Mt. Pres.*, 978 F.3d at 1209; (Reply Br. 6). But Oakbrook's deed does not treat the donee as the holder of the easement right at the time of judicial extinguishment because the donee's easement rights are not appraised at the time of judicial extinguishment. Rather, the announcement of a judicial extinguishment effectively means the easement right reverts to Oakbrook because the donee receives a fixed amount set at the time of the grant. Accordingly, Oakbrook did not gift an easement interest "granted in perpetuity." *See* I.R.C. § 170(h)(2)(C).

In that regard, Oakbrook's deed makes this case different from *Hewitt.* There, the deed provided that, upon judicial extinguishment, the donee will receive "a fair market value determined by": (1) finding the current "fair market value of the Property unencumbered by the Easement *(minus any increase in value after the date of th[e] grant attributable to improvements)*"; and (2) multiplying that amount "by the ratio of the value of the Easement at the time of this grant to the value of the Property." *Hewitt*, 21 F.4th at 1340 (emphasis in original). While Oakbrook's deed similarly subtracts post-donation improvements, it differs because it fixes the fair market value "as of the date of th[e] Conservation Easement" grant. J.A. 121.

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be determined by ascertaining the fair cash market *value of the property or property rights taken*.") (emphasis added).

The only problem is that, although the Commissioner presses this statutory argument now, the Commissioner did not raise the argument before the tax court. It appears four of the tax court judges decided to raise the argument *sua sponte*. *See Oakbrook*, 154 T.C. at 204-07 (Toro, J., concurring in the judgment, joined by Gustafson, Urda, and Jones, JJ.). The only statutory argument the Commissioner raised was that Oakbrook's easement deed "violates I.R.C. § 170(h)(2)(C) and (h)(5)(A) because the area covered by the conservation easement is not clearly defined." J.A. 34, 39-40, 47-49. The same provisions are the basis of the Commissioner's current statutory argument.

"[W]e customarily require the party to raise the issue in the [trial] court" before we will consider the issue on appeal. *Sheet Metal Workers' Health & Welfare Fund of N Carolina v. L. Off. of Michael A. DeMayo, LLP*, 21 F.4th 350, 355 (6th Cir. 2021) (explaining the reasons for the rule). "An exception can be made, however, for 'exceptional cases' or if failing to consider the argument would result in a 'plain miscarriage of justice.'" *United States v. Ellison*, 462 F.3d 557, 560 (6th Cir. 2006) (Gibbons, J.) (quoting *Pinney Dock & Transp. Co. v. Penn Cent. Corp.*, 838 F.2d 1445, 1461 (6th Cir. 1988)); *see also Sheet Metal*, 21 F.4th at 357.

As in *Ellison*, this is "an exceptional case." 462 F.3d at 560. The question here is "purely a legal one"—whether a deed provides that extinguishment proceeds are measured by the value of property rights at the time of extinguishment in order to satisfy the statutory requirement that a conservation easement must be "granted in perpetuity." *Id.* The parties also have fully briefed the issue, so it is "'presented with sufficient clarity and completeness' to ensure a proper resolution." *Id.* at 560-61 (quoting *Pinney Dock*, 838 F.2d at 1461). "It requires no further development of the record at the [trial] court level, and thus, [Oakbrook] will not be prejudiced by the inability to present evidence to that court." *Id.* at 561 (reversing district court based on new argument).

In terms of fairness to the tax court, *see Sheet Metal*, 21 F.4th at 356, there is a significant difference between considering an argument to reverse a trial court and considering an argument to affirm. After all, we "may affirm a decision of the district court for any reason supported by the record, including on grounds different from those on which the district court relied." *Thomas v. City of Columbus*, 854 F.3d 361, 364-65 (6th Cir. 2017) (citation omitted); *accord US. Postal Serv. v. Nat'l Ass 'n of Letter Carriers*, *AFL-CIO*, 330 F.3d 747, 750 (6th Cir. 2003).

Setting aside any exception to the forfeiture rule, our court and the Supreme Court "recognize a distinction between failing to properly raise a claim before the district court and failing to make an argument in support of that claim." *United States v. Reed*, 993 F.3d 441, 453 (6th Cir. 2021) (citation omitted); *see also Citizens United v. FEC*, 558 U.S. 310, 330-31 (2010) (concluding that the argument that a case "should be overruled is 'not a new claim,' but instead, "it is—at most—'a new argument to support what has been a consistent claim: that the FEC did not accord Citizens United the rights it was obliged to provide by the First Amendment" (cleaned up)). The Commissioners' "arguments" that Oakbrook's deed violates § 170(h)(2)(C) and (h)(5)(A) "in two different ways, by [failing to sufficiently define the conservation area] and by [failing to satisfy the perpetuity requirements], are not separate *claims*. They are, rather, separate *arguments* in support of a single claim—that the [deed] effects [a violation of the statute]." *Yee v. City of Escondido*, 503 U.S. 519, 534-35 (1992). "Having raised a [statutory violation] claim in the [tax] courts, therefore, [Oakbrook] could have formulated any argument [it] liked in support of that claim here." *Id.* at 535.

Accordingly, I would address the Commissioner's statutory argument.

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I would conclude that the proceeds regulation is invalid. But I would still affirm on the basis that Oakbrook's deed violates the perpetuity requirement under I.R.C. § 170(h)(2)(C).

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

[Filed March 14, 2022]

No. 20-2117

OAKBROOK LAND HOLDINGS, LLC;
WILLIAM DUANE HORTON, Tax Matters Partner,

Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee.

Before: GUY, MOORE, and GIBBONS,
Circuit Judges.

JUDGMENT

On Appeal from the United States Tax Court.

THIS CAUSE was heard on the record from the Tax Court and was argued by counsel.

IN CONSIDERATION THEREOF, it is ORDERED that the judgment of the Tax Court is AFFIRMED.

ENTERED BY ORDER OF THE COURT

/s/ Deborah S. Hunt
Deborah S. Hunt, Clerk

APPENDIX C

154 T.C. 180

UNITED STATES TAX COURT

[Filed May 12, 2020]

Docket No. 5444-13.

OAKBROOK LAND HOLDINGS, LLC,
WILLIAM DUANE HORTON, TAX MATTERS PARTNER,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

In 2008 P donated a conservation easement to a qualified organization and claimed a charitable contribution deduction under I.R.C. sec. 170(a). The easement deed provided that, if the conservation restriction were extinguished at some future date, the donee would receive a share of the proceeds equal to the fair market value of the easement on the date the contribution was made. The deed further provided that the donee's share as thus determined would be reduced by the value of any improvements made by the donor after granting the easement. R disallowed the deduction, contending (among other things) that the extinguishment clause violated the requirements of sec. 1.170A-14(g)(6), Income Tax Regs.

In *Oakbrook Land Holdings, LLC v. Commissioner*, T.C. Memo. 2020-54, issued concurrently with this

Opinion, the Court holds that the easement deed violates the "protected in perpetuity" requirement of I.R.C. sec. 170(h)(5), as interpreted in sec. 1.170A-14(g)(6), Income Tax Regs., because the donee's share of the extinguishment proceeds (1) is based on a fixed historical value rather than a proportionate share, and (2) is reduced by the value of any improvements made by the donor. This Opinion addresses petitioner's challenge to the validity of the regulation.

Held: Sec. 1.170A-14(g)(6), Income Tax Regs., was properly promulgated and is valid under the Administrative Procedure Act, 5 U.S.C. sec. 553 (2018).

Held, *further*, the construction of I.R.C. sec. 170(h)(5) as set forth in sec. 1.170A-14(g)(6), Income Tax Regs., is valid under *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984).

David M. Wooldridge, Michelle A. Levin, Ronald A. Levitt, and *Gregory P. Rhodes*, for petitioner.

W. Benjamin McClendon, Bruce K. Meneely, Robert W. Dillard, and *William W. Kiessling*, for respondent.

LAUBER, *Judge:* Oakbrook Land Holdings, LLC (Oakbrook), purchased 143 acres of land near Chattanooga, Tennessee, in December 2007 for $1,700,000. In December 2008, slightly more than one year later, Oakbrook donated a conservation easement over a portion of the tract to the Southeast Regional Land Conservancy (SRLC). On its Federal income tax return for 2008, Oakbrook claimed for this donation a charitable contribution deduction of $9,545,000. Oakbrook thus took the position that the land covered by the easement had appreciated in value by about 700% in a single year during the worst real estate crisis to hit the United States since the Great Depression.

The case was tried before Judge Holmes in 2016, and the facts are stated more fully in a separate Memorandum Opinion authored by him and filed concurrently herewith. *Oakbrook Land Holdings, LLC v. Commissioner,* T.C. Memo. 2020-54. That opinion holds that the easement Oakbrook granted did not satisfy the "protected in perpetuity" requirement of section 170(h)(5)(A) and section 1.170A-14(g)(6), Income Tax Regs.[1] That is because the donee's share of the proceeds, in the event the property were sold following a judicial extinguishment of the easement, would be (1) determined according to a fixed historical value rather than a proportionate share of the proceeds and (2) reduced by the value of any improvements made by the donor. See *Oakbrook Land Holdings, LLC,* T.C. Memo. 2020-54, at *36-*37. In this Opinion we address and reject petitioner's challenge to the validity of this regulation.

FINDINGS OF FACT

In December 2008 Oakbrook executed a Conservation Easement and Declaration of Restrictions and Covenants (Deed) with SRLC, a "qualified organization" under section 170(h)(3). This easement covered 106 acres (or 75%) of the tract Oakbrook had purchased the previous December. The parties understood that changed circumstances might make it impossible, at some point in the future, to continue protecting the conservation area. Should that happen, article VI, section B(2), of the Deed governed how Oakbrook and SRLC would divide the proceeds of sale following a judicial extinguishment of the easement. It provided:

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[1] Unless otherwise indicated, all statutory references are to the Internal Revenue Code (Code) in effect for the year at issue. We round most monetary amounts to the nearest dollar.

> This Conservation Easement gives rise to a real property right and interest immediately vested in SRLC. For purposes of this Conservation Easement, the fair market value of SRLC's right and interest shall be equal to the difference between (a) the fair market value of the Conservation Area as if not burdened by this Conservation Easement and (b) the fair market value of the Conservation Area burdened by this Conservation Easement, as such values are determined as of the date of this Conservation Easement, (c) less amounts for improvements made by * * * [Oakbrook] in the Conservation Area subsequent to the date of this Conservation Easement, the amount of which will be determined by the value specified for these improvements in a condemnation award in the event all or part of the Conservation Area is taken in exercise of eminent domain * * * . If a change in conditions makes impossible or impractical any continued protection of the Conservation Area for conservation purposes, the restrictions contained herein may only be extinguished by judicial proceeding. Upon such proceeding, SRLC, upon a subsequent sale, exchange or involuntary conversion of the Conservation Area, shall be entitled to a portion of the proceeds equal to the fair market value of the Conservation Easement as provided above.

In the event all or part of the conservation area were taken by eminent domain "so as to abrogate the restrictions imposed by this Conservation Easement, * * * [the] proceeds shall be divided in accordance with the proportionate value of SRLC's and * * * [Oakbrook's] interests as specified above." Deed art. VI, sec. B(3).

Oakbrook timely filed a Form 1065, U.S. Return of Partnership Income, for its 2008 taxable year. On that return it claimed a charitable contribution deduction of $9,545,000 for its donation of the easement. The Internal Revenue Service (IRS) selected Oakbrook's return for examination. On December 6, 2012, the IRS issued Oakbrook's tax matters partner (TMP or petitioner) a notice of final partnership administrative adjustment that disallowed the charitable contribution deduction in full. The TMP timely petitioned for readjustment of the partnership items.

Trial was held before Judge Holmes in Birmingham, Alabama, in 2016. At trial the Court heard testimony from the SRLC representative who had drafted the Deed. In post-trial briefs petitioner contended that (1) the extinguishment provision of the Deed complies with the requirements of section 1.170A-14(g)(6), Income Tax Regs., and (2) in the alternative, the regulation is invalid.

Judge Holmes interpreted the Deed to mean that, in the event of a sale following judicial extinguishment of the easement, SRLC's share of the proceeds would be limited to the "initial fixed value" of the easement, i.e., its fair market value (FMV) on the date it was granted. *Oakbrook Land Holdings, LLC*, T.C. Memo. 2020-54, at *35. The donee's proceeds as thus determined would then be reduced by the value (as specified in any future condemnation award) of any improvements that Oakbrook had made to the conservation area after donating the easement. *Ibid.* Thus, if property values rose after that date, SRLC's share would not "be protected from inflation either in local land prices or the economy more generally." *Id.* at *35-*36. Conversely, if property values fell, SRLC might not receive even the initial fixed value of the easement because of the reduction for improvements. *Id.* at *36.

The Court concluded that the Deed, as thus construed, failed to satisfy the requirements of section 1.170A-14(g)(6), Income Tax Regs., for two reasons. First, the regulation requires that the donee be entitled to a proportionate share of the proceeds, not to a fixed dollar amount keyed to the easement's initial value. *Oakbrook Land Holdings, LLC*, T.C. Memo. 2020-54, at *37. Second, the regulation does not permit a reduction of the donee's proceeds on account of improvements made by the donor. *Id.* at *37-*38 (citing *PBBM-Rose Hill, Ltd. v. Commissioner*, 900 F.3d 193, 208 (5th Cir. 2018)). In this Opinion we address petitioner's challenge to the validity of this regulation.

OPINION

A. *Statutory and Regulatory Framework*

Section 170(a)(1) allows a deduction for any charitable contribution made within the taxable year. If the taxpayer makes a charitable contribution of property other than money, the amount of the contribution is generally equal to the FMV of the property at the time the gift is made. See sec. 1.170A-1(c)(1), Income Tax Regs.

The Code generally restricts a taxpayer's charitable contribution deduction for the donation of "an interest in property which consists of less than the taxpayer's entire interest in such property." Sec. 170(0(3)(A). But there is an exception to this rule for a "qualified conservation contribution." Sec. 170(f)(3)(B)(iii). This exception applies where: (1) the taxpayer makes a contribution of a "qualified real property interest," (2) the donee is a "qualified organization," and (3) the contribution is "exclusively for conservation purposes." Sec. 170(h)(1).

Section 170(h)(5)(A) provides that a contribution will not be treated as being made exclusively for conservation purposes "unless the conservation purpose is protected in perpetuity." The regulation interpreting this provision recognizes that "a subsequent unexpected change in the conditions surrounding the [donated] property * * * can make impossible or impractical the continued use of the property for conservation purposes." Sec. 1.170A-14(g)(6)(i), Income Tax Regs. Despite that possibility "the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding" and the easement deed ensures that the charitable donee, following sale of the property, will receive a proportionate share of the proceeds and use those proceeds consistently with the conservation purposes underlying the original gift. *Ibid.* In effect, the "perpetuity" requirement is deemed satisfied because the sale proceeds replace the easement as an asset deployed by the donee "exclusively for conservation purposes." Sec. 170(h)(5)(A).

Section 1.170A-14(g)(6)(i), Income Tax Regs., provides that the donee must be entitled to proceeds "determined under paragraph (g)(6)(ii)." That paragraph, captioned "Proceeds," provides in part as follows:

> [F]or a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the

> time of the gift, bears to the value of the property as a whole at that time. * * * For purposes of this paragraph * * * , that proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give[s] rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds * * * .

This regulation requires that the easement deed guarantee the donee "a proportionate share of extinguishment proceeds." *Carroll v. Commissioner*, 146 T.C. 196, 219 (2016); *see PBBM-Rose Hill*, 900 F.3d at 207 ("[T]he 'proportionate value' is a fraction equal to the value of the conservation easement at the time of the gift, divided by the value of the property as a whole at that time."). Further, the regulation does not permit that "any amount, including that attributable to improvements, may be subtracted out" of the proceeds against which the proportionate value is applied. *PBBM-Rose Hill*, 900 F.3d at 208; *accord*, *Coal Prop. Holdings, LLC v. Commissioner*, 153 T.C. 126, 136-137 (2019).

B. *Regulatory Background*

The Tax Reform Act of 1969, Pub. L. No. 91-172, sec. 201, 83 Stat. at 556, generally disallowed charitable contribution deductions for gifts of partial interests in property. In 1980 Congress revised the Code to allow deductions for such gifts when they constitute "qualified conservation contributions." *See* Tax Treatment Extension Act of 1980 (1980 Act), Pub. L. No. 96-541, sec. 6, 94 Stat. at 3206 (adding section 170(h)). Congress specified numerous requirements for a "qualified conservation contribution," including the requirements that the contribution be made "exclusively for conservation purposes" and that the "conservation purpose [be] protected in perpetuity." *Ibid.* (codified at section 170(h)(1)(C), (5)(A)).

On May 23, 1983, the Department of the Treasury (Treasury) issued a notice of proposed rulemaking with "proposed regulations relating to contributions of partial interests in property for conservation purposes." 48 Fed. Reg. 22940 (May 23, 1983). The preamble explained the history of congressional enactments in this area, highlighting the requirement that a donated easement "be perpetual in order to qualify for a deduction." *Ibid.* Treasury noted that the House and Senate committee reports accompanying the 1980 Act had "provided, for the first time, an in-depth statement of congressional intent concerning the donation of partial interests for conservation purposes." *Ibid.* The preamble stated that the proposed regulations "reflect the major policy decisions made by the Congress and expressed in these committee reports." *Ibid.*

The proposed regulations spanned nine pages of the Federal Register and included provisions--many quite technical--addressing concepts such as "qualified real property interest," "perpetual conservation restriction," "historically important land area," "certified historic structure," "conservation purpose," and "significant public benefit." *Id.* at 22941-22949. Overall, the proposed regulations covering "qualified conservation contributions" consisted of 10 paragraphs, 23 subparagraphs, 30 subdivisions, and 21 examples. One of these

23 subparagraphs became what is now section 1.170A-14(g)(6), Income Tax Regs., covering judicial extinguishment of easements and allocation of the resulting proceeds. 48 Fed. Reg. at 22946.

In response to its request for public comments, Treasury received more than 700 pages of commentary. Ninety organizations or individuals submitted comments addressing various aspects of the proposed rules. Of the 90 commenters only 13 mentioned the judicial extinguishment provision. Of those 13 most devoted only a few sentences to this subject, generally at the end of a submission that emphasized other matters.

Most of the commenters who mentioned the judicial extinguishment provision supported it. The Maine Coast Heritage Trust "strongly endorse[d] the proposed provisions for extinguishing easements." Other commenters echoed this point, emphasizing that the proportionate value assigned to the easement should be "the *minimum* that a grantee organization should receive." Several commenters recommended that the proceeds formula be revised to make it more favorable to the donee, such that the donee's share would be "equal to the *greater* of its original proportionate value or its proportionate value at the time of the extinguishment."

Some commenters who supported the judicial extinguishment rule suggested minor tweaks to it. The National Trust for Historic Preservation recommended "including 'refinancing' in the list of events that would trigger the property owner's obligation to pay the easement holder for the value of its extinguished easement rights." The Washington Trust for Historic Preservation recommended that the list of triggering events, rather than being expanded, should be restricted to "'acts of God' which substantially destroy the property." The Natural Lands Trust recommended that the fraction determining the donee's share be computed on the basis of values existing "at the time of the extinguishment."

Several commenters suggested that the judicial extinguishment rule might be unnecessary or difficult to enforce against future owners. Two commenters noted concern that donors or donees mfight be subject to State transfer taxes upon distribution of extinguishment proceeds. Three commenters questioned the "proportionate value" approach as applied to facade easements on certified historic structures, while agreeing that this approach was appropriate "as applied to open space easements" on land.

Two commenters were definitely opposed to the judicial extinguishment rule, fearing that it would "create a potential disincentive to the donation of easements." According to the Landmarks Preservation Council of Illinois, the "proportionate value" approach to distribution of proceeds was problematic as applied to facade easements on "endangered historic properties * * * in downtown commercial areas." The New York Landmarks Conservancy (NYLC), which was "dedicated to the preservation of architecturally, historically and culturally significant buildings," devoted two pages of comments to the judicial extinguishment rule, focusing its concern on the supposed "deterrent effect" of this provision. Noting that judicial extinguishment was a "relatively remote" possibility, it questioned whether the regulations needed to address this point.

NYLC was the only commenter to mention donor improvements to the conservation area. It urged that the proportionate value formula "fails to take into account that improvements may be made * * * by the owner which should properly alter the ratio." It contended that failure to offset improvements against the donee's share of the proceeds "would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization." But NYLC suggested no alternative text to address this concern, other than to "recommend deletion of the entire extinguishment provision." Nor did any other commenter suggest alternative text to address the concerns (if any) that it expressed.

A public hearing on the proposed amendments to the regulations was held on September 15, 1983. On January 14, 1986, Treasury adopted the proposed amendments with numerous revisions. *See* T.D. 8069, 1986-1 C.B. 89. The preamble to the final regulations provides a summary of the law and states that, "[a]fter consideration of all comments regarding the proposed amendments * * * , those amendments are adopted as revised by this Treasury decision." *Id.* at 90.

In a section captioned "Summary of Comments," the preamble explained that Treasury had made substantial revisions in response to the comments it received. The preamble discussed seven aspects of the proposed regulations in detail; in each case Treasury revised or clarified text, filled in gaps, or provided additional explanatory examples. *Id.* at 90-91. Several of these provisions had generated "many comments." *Ibid.*

The "judicial extinguishment" provision is not among the amendments specifically addressed in the "Summary of Comments." However, Treasury did make changes to that provision in response to the comments it received. As originally proposed, the "judicial extinguishment" rule vested the donee with a property right having an FMV "that is a minimum ascertainable proportion of the fair market value to the entire property." 48 Fed. Reg. at 22946. The final regulation revised subparagraph (6)(ii) to refer to a property right with an FMV "that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time." Sec. 1.170A-14(g)(6)(ii), Income Tax Regs.; *see* T.D. 8069, 1986-1 C.B. at 99. Treasury concurrently made three other technical and conforming changes to the text of this provision.

These changes to the "judicial extinguishment" rule responded to comments that Treasury had received from the Nature Conservancy, the Maine Coast Heritage Trust, the Brandywine Conservancy, and the Land Trust Exchange. (The Land Trust Exchange had synthesized comments from land trusts across the country.) These commenters urged that "the proportionate value, not the absolute value, * * * is the important figure," and that "the proportionate value assigned to an easement at the time of gift is the *minimum* that a grantee organization should receive in the event of an extinguishment and sale."

C. *Procedural Validity of the Regulation*

Petitioner first contends that the judicial extinguishment regulation is procedurally defective on the theory that it was not properly promulgated as required by the Administrative Procedure Act (APA), 5 U.S.C. sec. 553 (2018).

1. *Legislative vs. Interpretive Rules*

Administrative law distinguishes between interpretive and legislative agency rules. "An interpretive rule merely clarifies or explains preexisting substantive law or regulations." *SIH Partners LLLP v. Commissioner*, 150 T.C. 28, 40 (2018) (citing *Elizabeth Blackwell Health Ctr. for Women v. Knoll*, 61 F.3d 170, 181 (3d

Cir. 1995)), aff'd, 923 F.3d 296 (3d Cir. 2019); see *Tenn. Hosp. Ass'n v. Azar*, 908 F.3d 1029, 1042 (6th Cir. 2018). A legislative rule, on the other hand, "creates rights, assigns duties, or imposes obligations, the basic tenor of which is not already outlined in the law itself." *SIH Partners*, 150 T.C. at 40 (quoting Dia *Navigation Co. v. Pomeroy*, 34 F.3d 1255, 1264 (3d Cir. 1994)); see *Tenn. Hosp. Ass'n*, 908 F.3d at 1042. Legislative rules have "the force and effect of law." *Chrysler Corp. v. Brown*, 441 U.S. 281, 303 (1979) (quoting *Batterton v. Francis*, 432 U.S. 419, 425 n.9 (1977)).

Section 170(h)(5)(A) requires that the conservation purpose underlying the easement be "protected in perpetuity." But the statute does not indicate how (or whether) this requirement could be deemed satisfied given the possibility that the easement might later be extinguished. The regulation specifies the circumstances in which "the conservation purpose can nonetheless be treated as protected in perpetuity." Sec. 1.170A-14(g)(6)(i), Income Tax Regs.

To secure this treatment the regulation requires that the donor agree, at the time of the gift, to a specified division of proceeds in the event the property is sold following judicial extinguishment of the easement. *Ibid.* The required division of proceeds is set forth in subparagraph (6)(ii). Because the regulation imposes a requirement not explicitly set forth in the statute, it is appropriately treated as a legislative rule. Cf. *SIH Partners*, 150 T.C. at 40-41.

2. *Procedural Requirements for Legislative Rules*

Legislative rules are subject to APA notice-and-comment rulemaking procedures. *See* 5 U.S.C. sec. 553(b); *Tenn. Hosp. Ass'n*, 908 F.3d at 1042. To issue a legislative regulation consistently with the APA an agency must: (1) publish a notice of proposed rulemaking in the Federal Register; (2) provide "interested persons an opportunity to participate * * * through submission of written data, views, or arguments"; and (3) "[a]fter consideration of the relevant matter presented, * * * incorporate in the rules adopted a concise general statement of their basis and purpose." *See* 5 U.S.C. sec. 553(b) and (c).

The administrative record for T.D. 8069 shows (and petitioner does not dispute) that Treasury satisfied the first two requirements. Petitioner contends that Treasury failed to consider a "relevant matter presented" to it and failed to include in the final regulations a "concise general statement of their basis and purpose."

The APA provides that a reviewing court shall set aside agency action that is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. sec. 706(2)(a). The scope of our review "is a narrow one" because "[t]he court is not empowered to substitute its judgment for that of the agency." *Bowman Transp., Inc. v. Ark.-Best Freight Sys., Inc.*, 419 U.S. 281, 285 (1974) (quoting *Citizens to Pres. Overton Park, Inc. v. Volpe*, 401 U.S. 402, 416 (1971)). We consider only whether the agency "articulate[d] a satisfactory explanation for its action." *Motor Vehicle Mfrs. Ass'n, Inc. v. State Farm Mut. Auto. Ins. Co. (State Farm)*, 463 U.S. 29, 43 (1983).

While we cannot provide a reasoned basis for agency action that the agency itself did not supply, we will "uphold a decision of less than ideal clarity if the agency's path may reasonably be discerned." *Bowman Transp., Inc.*, 419 U.S. at 285-286. "So long as an agency's rationale can reasonably be discerned and that rationale coincides with the agency's authority and obligations under the relevant statute, a reviewing court may not 'broadly require an agency to consider all policy alternatives in reaching decision.'" *SIH Partners*, 150 T.C. at 47 (quoting *State Farm*, 463 U.S. at 51). Indeed, "regulations with no statement of basis and purpose have been upheld where the basis and purpose w[ere] considered obvious." *Cal-Almond, Inc. v. U.S. Dep't of Agric.*, 14 F.3d 429, 443 (9th Cir. 1993) (citing *Citizens to Save Spencer Cty. v. EPA*, 600 F.2d 844, 884 (D.C. Cir. 1979)).[2]

The preamble to the final regulations explains that they were being promulgated to "provide necessary guidance to the public for compliance with the law," as recently amended by Congress, "relating to contributions * * * of partial interests in property for conservation purposes." T.D. 8069, 1986-1 C.B. at 89. The preamble to the proposed regulations supplied extensive background about the legislative history, explaining that "[t]he regulations reflect the major policy decisions made by the Congress and expressed in the[] committee reports." 48 Fed. Reg. at 22940. Treasury noted that "[t]he most difficult problem posed in this regulation was how to provide a workable

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[2] In *State Farm* the Supreme Court found agency action arbitrary and capricious because it "failed to present an adequate basis and explanation" of its decision to reverse a longstanding rule. *State Farm*, 463 U.S. at 34. On the basis of the record in that case, the agency's explanation was "not sufficient to enable * * * [the Court] to conclude that the rescission was a product of reasoned decisionmaking." *Id.* at 52. Here, Treasury was promulgating new rules in response to Congress' amendments to section 170. Treasury was not reversing an earlier policy supported by a body of fact that would require substantial evidence to justify a reversal of course. *See SIH Partners*, 150 T.C. at 43-44 (distinguishing *State Farm* on the same ground).

framework for donors, donees, and the * * * [IRS] to judge the deductibility of open space easements," inviting public comments on this and other points. *Ibid.*

In response to this request Treasury received comments from 90 organizations and individuals who supplied voluminous commentary on many aspects of the proposed regulations. Treasury considered these comments and made numerous changes throughout, highlighting the most important revisions in a two-page "Summary of Comments." T.D. 8069, 1986-1 C.B. at 90-91. The preamble to the final regulations states that, "[a]fter consideration of all comments regarding the proposed amendments * * * , those amendments are adopted as revised by this Treasury decision." *Id.* at 90. This Court has found a similar statement, coupled with the administrative record, sufficient to find that Treasury had considered the relevant matter presented to it. *See Wing v. Commissioner*, 81 T.C. 17, 31-32 (1983) (upholding a regulation whose preamble stated that, "[a]fter consideration of all comments regarding the proposed amendments, this Treasury Decision is adopted" (quoting T.D. 7523, 42 Fed. Reg. 63640 (Dec. 19, 1977))).

The preamble to the final regulations discusses seven major groups of comments and the changes Treasury made in response to them. But an agency cannot reasonably be expected to address every comment it received. The APA "has never been interpreted to require the agency to respond to every comment, or to analyse every issue or alternative raised by the comments, no matter how insubstantial." *Thompson v. Clark*, 741 F.2d 401, 408 (D.C. Cir. 1984). "We do not expect the agency to discuss every item of fact or opinion included in the submissions made to it." *Simms v. Nat'l Highway Traffic Safety Admin.*, 45

F.3d 999, 1005 (6th Cir. 1995) (quoting *Auto. Parts & Accessories Ass'n, Inc. v. Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968)); *see Action on Smoking & Health v. Civil Aeronautics Bd.*, 699 F.2d 1209, 1216 (D.C. Cir. 1983) ("An agency need not respond to every comment.").

The two aspects of the "judicial extinguishment" rule to which petitioner objects are the requirement that the donee receive a proportional share of the proceeds and the fact that the "proportionate share" formula does not account for the possibility of donor improvements. Treasury clearly considered the comments it received on the first point because it substantially revised the text of section 1.170A-14(g)(6)(ii), Income Tax Regs., in response to those comments. *See supra* pp. 14-15.

Only one of the 90 commenters mentioned donor improvements, and it devoted exactly one paragraph to this subject. That commenter, NYLC, was concerned about facade easements on historic structures, as opposed to "perpetual open space easements," with which Treasury was chiefly concerned. *See* 48 Fed. Reg. at 22940. And NYLC mentioned this point to support its belief that donors of facade easements "are likely to be discouraged from making a donation," a supposition that Treasury may reasonably have discounted.

In any event, "[t]he administrative record reflects that no substantive alternatives to the final rules were presented for Treasury's consideration." *SIH Part*ners, 150 T.C. at 44; *see* dissenting op. p. 102 ("A comment is * * * more likely to be significant if the commenter suggests a remedy for the purported problem it identifies."). NYLC offered no suggestion about how the subject of donor improvements might be handled; it simply recommended "deletion of the entire extinguishment provision." Only one other commenter of the

13 mentioning judicial extinguishment voiced that recommendation.[3]

The APA requires "consideration of the relevant matter presented" during the rulemaking process. 5 U.S.C. sec. 553(c). Our review of the administrative record leaves us with no doubt that Treasury considered the relevant matter presented to it. *See Wing*, 81 T.C. at 33. And we find equally little merit in petitioner's assertion that Treasury failed to "incorporate

[3] Our dissenting colleague errs in relying on *United States v. Nova Scotia Food Prods. Corp.*, 568 F.2d 240 (2d Cir. 1977), to support his position. *See* dissenting op. pp. 110-113. That case involved a Food and Drug Administration (FDA) regulation establishing minimum "time, temperature, and salinity" requirements for processing fish. The Second Circuit invalidated the regulation as applied to one category of fish product, "non-vacuum-packed hot-smoked whitefish." *Nova Scotia Food Prods. Corp.*, 568 F.2d at 253. The court first held that the FDA had "failed to disclose to interested parties the scientific data and the methodology upon which it relied." *Id.* at 250. "When the basis for a proposed rule is a scientific decision, the scientific material which is believed to support the rule should be exposed to the view of interested parties for their comment." *Id.* at 252. The court also held that the agency had failed to consider: (1) evidence that heating "certain types of fish to high temperatures will completely destroy the product," (2) the suggestion that using "nitrite and salt as additives could safely lower the high temperature otherwise required," and (3) the suggestion that different processing requirements should be established for different species of fish. *Id.* at 245. Here, the basis for the proposed regulation was not "a scientific decision"; Treasury relied on no undisclosed data when proposing its regulation; the two commenters who opposed the judicial extinguishment rule offered no concrete alternative suggestions; and the concerns they expressed lacked the significance of concerns about destroying the commercial viability of a product, which the Second Circuit aptly described as "vital questions" in *Nova Scotia Food Prods. Corp.*, 568 F.2d at 252.

in the rules adopted a concise general statement of their basis and purpose." *See* 5 U.S.C. sec. 553(c).

The preamble to the final regulations explains that they were being promulgated to "provide necessary guidance to the public for compliance with the law," as recently amended by Congress, "relating to contributions * * * of partial interests in property for conservation purposes." T.D. 8069, 1986-1 C.B. at 89. The preamble to the proposed regulations emphasized the requirement that conservation easements "be perpetual in order to qualify for a deduction." 48 Fed. Reg. 22940. The purpose of the "judicial extinguishment" rule is plain on its face--to provide a mechanism to ensure that the conservation purpose can be deemed "protected in perpetuity" notwithstanding the possibility that the easement might later be extinguished. Sec. 1.170A-14(g)(6)(i), Income Tax Regs. Even where a regulation contains no statement of basis and purpose whatsoever, it may be upheld "where the basis and purpose * * * [are] considered obvious." *Cal-Almond,* Inc 14 F.3d at 443.

Petitioner insists that Treasury failed to comply with the APA because the preamble to the final regulations did not discuss the "basis and purpose" of the judicial extinguishment provision specifically. But this provision represented one subparagraph of a regulation project consisting of 10 paragraphs, 23 subparagraphs, 30 subdivisions, and 21 examples. No court has ever construed the APA to mandate that an agency explain the basis and purpose of each individual component of a regulation separately. "[T]he detail required in a statement of basis and purpose depends on the subject of the regulation and the nature of the comments received." *Reytblatt v. U.S. Nuclear Regulatory Comm'n*, 105 F.3d 715, 722 (D.C. Cir. 1997) (quoting *Action on Smoking & Health*, 699 F.2d at 1216). This statement need only "contain sufficient information to allow a court to exercise judicial review." *United States v. Garner*, 767 F.2d 104, 117 (5th Cir. 1985); *see Simms*, 45 F.3d at 1005 (quoting *Auto. Parts & Accessories Ass'n, Inc.*, 407 F.2d at 338).

The broad statements of purpose contained in the preambles to the final and proposed regulations, coupled with obvious inferences drawn from the regulations themselves, are more than adequate to enable us to perform judicial review. We find that Treasury's rationale for the judicial extinguishment rule "can reasonably be discerned and * * * coincides with the agency's authority and obligations under the relevant statute." *SIH Partners*, 150 T.C. at 47. We accordingly hold that Treasury satisfied all applicable APA requirements when promulgating this rule.[4]

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[4] Petitioner cites only one case in which a Federal court has invalidated a Treasury regulation on the theory that the regulation was not properly promulgated under the APA. *See Dominion Res., Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012). That case involved a regulation governing capitalization of interest under section 263A. The Federal Circuit first held the regulation substantively invalid under *Chevron* step two, concluding that it "directly contradict[ed] the avoided-cost rule that Congress intended the statute to implement." *Dominion Res., Inc*., 681 F.3d at 1317. The court also held that Treasury did not "provide a reasoned explanation for adopting * * * [the] regulation," thus violating "the *State Farm* requirement that the regulation must articulate a satisfactory or cogent explanation." *Id.* at 1319. Since the court found the regulation inconsistent with the statute, it unsurprisingly found that Treasury was obligated to explain why it nevertheless adopted the rule. No such problem exists here: The judicial extinguishment rule is clearly consistent with, and was designed to ensure satisfaction of, the statutory requirement that the conservation purpose be "protected in perpetuity." Sec. 170(h)(5)(C). Petitioner does not allege any inconsistency

D. *Substantive Validity of the Regulation*

1. *The "Judicial Extinguishment" Provision Generally*

Having concluded that the regulation was properly promulgated, we turn to petitioner's contention that the regulation is substantively invalid. When considering a challenge to the substantive validity of a regulation, we generally employ the two-part test established by *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984). The first prong of that test asks "whether Congress has directly spoken to the precise question at issue." *Id.* at 842. "If the intent of Congress is clear, that is the end of the matter." *Ibid.*

Section 170(h)(5)(A) sets forth a general requirement that the conservation purpose be "protected in perpetuity." Congress does not appear to have considered the possibility that an easement might be judicially extinguished, and the statute does not address how that possibility would affect a taxpayer's ability to satisfy the "perpetuity" requirement. Congress therefore did not speak directly to the question at issue.

We accordingly proceed to *Chevron* step two, which requires us to consider whether the regulation "is based on a permissible construction of the statute." *Chevron*, 467 U.S. at 843. If the statute is silent, we must give deference to the interpretation embodied in the agency's regulation unless it is "arbitrary, capri-

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between the statute and the regulation; rather, it faults Treasury for failing to refine the proceeds formula to make it slightly more favorable to donors in the unlikely event of judicial extinguishment. As explained in the text, only 1 of 90 commenters (NYLC) even mentioned this issue, and its proposed solution was to eliminate the judicial extinguishment rule in its entirety. Treasury did not abuse its discretion in rejecting that option.

cious, or manifestly contrary to the statute." *Id.* at 844; *see United States v. Mead Corp.*, 533 U.S. 218, 227 (2001). In other words we must sustain the regulation so long as it represents a "reasonable interpretation" of the law Congress enacted. *Chevron*, 467 U.S. at 844; *see SIH Partners*, 150 T.C. at 50.

Petitioner does not challenge the validity of the "judicial extinguishment" regulation as a whole, and it would be difficult to do so. Treasury faced a conundrum: How could the IRS determine that a conservation purpose was protected in perpetuity, thus enabling the donor to qualify for a deduction in the year he made the gift, when the easement might be extinguished at some future date? The regulation solves this problem by requiring the donor to agree, up front, to divide with the donee any proceeds from a post-extinguishment sale. The "perpetuity" requirement is deemed satisfied because "the donee organization can use its proportionate share of the proceeds to advance the cause of historic preservation elsewhere." *Carroll*, 146 T.C. at 214 (quoting *Kaufman v. Shulman*, 687 F.3d 21, 26 (1st Cir. 2012)).

2. *Proportionate Value*

While not disputing the validity of Treasury's overall objective, petitioner urges that the regulation is unreasonable in two respects. First, petitioner challenges the "proportionate value" approach to division of sale proceeds. Under section 1.170A-14(g)(6)(ii), Income Tax Regs., the donee's share is determined by multiplying the sale proceeds by a fraction, the numerator of which is the FMV of the easement at the time it was granted, and the denominator of which is the FMV of the entire property at that time. Petitioner contends that Treasury should have capped the donee's share at the FMV of the easement at the time it was granted.

We cannot say that the regulation's "proportionate value" approach is "arbitrary, capricious, or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844. Under the regulation the donee acquires "a property right, immediately vested in the donee organization," in a share of any future proceeds. Sec. 1.170A-14(g)(6)(ii), Income Tax Regs. Needless to say, the easement might be extinguished many years after it was granted, and considerable inflation in property values might occur in the interim. If the donee's share were limited to the easement's historical FMV, its property right could be eviscerated in real dollar terms. This would allow the donor or its successors to "reap[] a windfall if the property is destroyed or condemned." *Carroll*, 146 T.C. at 214 (quoting *Kaufman*, 687 F.3d at 26). That outcome would be at odds with the regulation's central purpose: to ensure satisfaction of the statute's "protected in perpetuity" requirement by supplying the donee with an asset that replaces, in real terms, the easement that has been lost.

3. *Donor Improvements*

Second, petitioner contends that the regulation is invalid because it does not permit the donee's share of the proceeds to be reduced by the value of improvements (if any) made by the donor. The regulation as proposed did not address donor improvements, and only one of 90 commenters mentioned the point. See *supra* pp. 21-22. Once again, we cannot say that the absence of a provision addressing donor improvements renders the regulation "arbitrary, capricious, or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844.

Treasury's goal in prescribing this regulation was to ensure satisfaction of the statute's "protected in perpetuity" requirement. In effect this requirement is deemed satisfied because the sale proceeds replace the easement as an asset deployed by the donee "exclusively for conservation purposes." Sec. 170(h)(5)(A). In certain factual scenarios, reducing the donee's proceeds on account of donor improvements could frustrate this goal, especially if local land values should decline.

For example, assume that a taxpayer donates an easement valued at $1 million on property valued at $2 million without the easement. The taxpayer thereafter spends $1 million improving the property. Many years later, there is an economic downturn, the easement is extinguished, and the property is sold for $2 million. Under the regulation the donee would be entitled to $1 million (half of the proceeds) and the conservation purpose would be deemed "protected in perpetuity." Sec. 170(h)(5)(A). But if improvements were carved out, the donee's share would be reduced to $500,000 or zero, depending on whether the carve-out was applied to the entire proceeds or to the donee's 50% share.

NYLC, the only commenter to mention donor improvements, notably did not suggest any text to address this problem. And addressing it would have raised a host of questions: Would the donee's proceeds be reduced by improvements the donor had made before granting the easement, after granting it, or both? Would the donor get credit for improvements to the land itself (such as grading) or only for erecting structures? Would the donee's proceeds be reduced by the donor's cost for the improvements or by their FMV at the time the easement was extinguished? And how would the problem mentioned in the previous paragraph be solved, to prevent the donee's share from being severely reduced or even eliminated? It is conceivable that Treasury could have drafted a regulation that addressed the possibility of donor improvements, dealing with these ancillary questions in some rational way. But that was a policy decision for Treasury, not this Court, to make.

Treasury's overarching goal was to guarantee that the donee, upon judicial extinguishment of the easement, would receive the full share of proceeds to which it was entitled. The few commenters who addressed this point offered differing views on precisely how the donee's "proportionate share" should be determined. NYLC regarded the formula as too favorable to the donee because it did not account for possible donor improvements. Other commenters urged that the formula should be made *more favorable* to the donee, with the donee's share being "equal to the *greater* of its original proportionate value or its proportionate value at the time of the extinguishment."

We find that Treasury exercised reasoned judgment by adhering to a simple rule that splits sale proceeds in a direct proportional manner on the basis of a fraction determined as of the date the gift was made. Because the regulation as drafted ensures satisfaction of the statutory mandate that the conservation purpose be "protected in perpetuity," sec. 170(h)(5)(A), we cannot find the regulation to be "arbitrary, capricious, or manifestly contrary to the statute," *Chevron*, 467 U.S. at 844.

Finally, the age of this regulation gives weight to the presumption of reasonableness. "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." *Cottage Sav. Ass'n v. Commissioner*, 499 U.S. 554, 561 (1991) (quoting *United States v. Correll*, 389 U.S. 299, 305-306 (1967)). "[A]gency interpretations that are of long standing come before us with a certain credential of reasonableness, since it is rare that error would long persist." *Smiley v. Citibank (S.D.), N.A.*, 517 U.S. 735, 740 (1996); *see Carlebach v. Commissioner*, 139 T.C. 1, 12 (2012) (sustaining under *Chevron* step two a regulation that had "gain[ed] legitimacy" because it had persisted substantially unchanged since 1944).

The regulation petitioner challenges was promulgated in January 1986. It has never been amended. In the past 34 years Congress has amended section 170 more than 30 times,[5] but these amendments have

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[5] [5]*See* Pub. L. No. 99-514, secs. 142(d), 231(f), 301(b)(2), 1831, 100 Stat. at 2120, 2180, 2217, 2851 (1986); Pub. L. No. 100-203, sec. 10711(a)(1), 101 Stat. at 1330-464 (1987); Pub. L. No. 100-647, sec. 6001(a), 102 Stat. at 3683 (1988); Pub. L. No. 101-508, secs. 11801(a)(11), (c)(5), 11813(b)(10), 104 Stat. at 1388-520, 1388-523, 1388-554 (1990); Pub. L. No. 103-66, secs. 13172(a), 13222(b), 107 Stat. at 455, 479 (1993); Pub. L. No. 104-188, secs. 1206(a), 1316(b), 110 Stat. at 1776, 1786 (1996); Pub. L. No. 105-34, secs. 224(a), 508(d), 602(a), 973(a), 111 Stat. at 818, 860, 862, 898 (1997); Pub. L. No. 105-206, sec. 6004(e), 112 Stat. at 795 (1998); Pub. L. No. 105-277, sec. 1004(a)(1), 112 Stat. at 2681-888 (1998); Pub. L. No. 106-170, secs. 532(c)(1)(A) and (B), 537(a), 113 Stat. at 1930, 1936 (1999); Pub. L. No. 106-554, secs. 1(a)(7), 165(a)-(e), 114 Stat. at 2763, 2763A-626 (2000); Pub. L. No. 107-16, sec. 542(e)(2)(B), 115 Stat. at 84 (2001); Pub. L. No. 107-147, sec. 417(7), (22), 116 Stat. at 56, 57 (2002); Pub. L. No. 108-81, sec. 503, 117 Stat. at 1003 (2003); Pub. L. No. 108-311, secs. 207(15), (16), 306(a), 118 Stat. at 1177, 1179 (2004); Pub. L. No. 108-357, secs. 335(a), 413(c)(30), 882(a), (b), (d), 883(a), 884(a), 118 Stat. at 1478, 1509, 1627, 1631, 1632 (2004); Pub. L. No. 109-73, secs. 305(a), 306(a), 119 Stat. at 2025 (2005); Pub. L. No. 109-135, sec. 403(a)(16), (gg), 119 Stat. at 2619, 2631 (2005); Pub. L. No. 109-222, sec. 204(b), 120 Stat. at 350 (2006); Pub. L. No. 109-280, secs. 1202(a), 1204(a), 1206(a), (b)(1), 1213(a)(1), (b)-(d), 1214(a) and (b), 1215(a), 1216(a), 1217(a), 1218(a), 1219(c)(1), 1234(a), 120 Stat. at 1066, 1068, 1075, 1077, 1079, 1080, 1085, 1100 (2006); Pub. L. No. 109-432, sec. 116(a)(1), (b)(1) and (2), 120 Stat. at 2941 (2006); Pub. L. No. 110-172, secs. 3(c), 11(a)(14)(A) and (B), (15) and (16), 121 Stat. at 2474, 2485 (2007); Pub. L. No. 110-234, sec. 15302(a),

never suggested any disagreement with the construction of the statute that Treasury adopted in section 1.170A-14(g)(6), Income Tax Regs. This "strongly suggests that * * * [Congress] did not view Treasury's construction * * * as unreasonable or contrary to the law's purpose." *SIH Partners*, 150 T.C. at 53-54 (sustaining under *Chevron* step two a regulation that had persisted substantially unchanged for nearly 50 years).

To implement the foregoing,

An appropriate decision will be entered.

Reviewed by the Court.

FOLEY, GALE, THORNTON, PARIS, MORRISON, KERRIGAN, BUCH, NEGA, PUGH, ASHFORD, and COPELAND, *JJ.*, agree with this opinion of the Court.

GUSTAFSON, *J.*, agrees with parts A, B, C, D.1, and D.2 of this opinion.

HOLMES, *J.*, dissents.

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122 Stat. at 1501 (2008); Pub. L. No. 110-246, secs. 4(a), 15302(a), 122 Stat. at 1664, 2263 (2008); Pub. L. No. 110-343, secs. 321(b), 323(a)(1), (b)(1), 324(a), (b), 122 Stat. at 3873, 3874, 3875 (2008); Pub. L. No. 111-312, secs. 301(a), 723(a) and (b), 740(a), 741(a), 742(a), 124 Stat. at 3300, 3316, 3319 (2010); Pub. L. No. 112-240, secs. 206(a) and (b), 314(a), 126 Stat. at 2324, 2330 (2013); Pub. L. No. 113-295, secs. 106(a) and (b), 126(a), 221(a)(28), 128 Stat. at 4013, 4017, 4041 (2014); Pub. L. No. 114-41, sec. 2006(a)(2)(A), 129 Stat. at 457 (2015); Pub. L. No. 114-113, secs. 111(a)-(b)(2), 113(a) and (b), 331(a), 129 Stat. at 3046, 3047, 3104 (2015); Pub. L. No. 115-97, secs. 11011(d)(5), 11023(a), 13305(b)(2), 13704(a), 13705(a), 131 Stat. at 2071, 2074, 2126, 2169 (2017); Pub. L. No. 115-141, sec. 401(a)(52), (b)(14), 132 Stat. at 1186, 1202 (2018); Pub. L. No. 115-232, sec. 809(h)(1), 132 Stat. at 1842 (2018).

TORO, *J.*, concurring in the result: The question before the Court is whether an easement granted by Oakbrook Land Holdings, LLC ("Oakbrook") to the Southeast Regional Land Conservancy ("SRLC") in December 2008 constitutes a "qualified conservation contribution" under section 170(h)(1), entitling Oakbrook to the charitable contribution deduction claimed for that year. Applying the text of the statute to the terms of the easement before us leads me to conclude that the easement is not a "qualified conservation contribution" because it fails to grant to the charity all of the rights inherent in the interest in real property contemplated by the statute. Thus, in my view, the Commissioner was right to disallow Oakbrook's charitable contribution deduction, and the deficiency that the Commissioner determined must be upheld. *See infra* Part I. Because the opinion of the Court announces the same disposition, I concur in that result.

Since applying the text of the statute to the terms of the easement before us suffices to resolve the dispute before the Court, there is no need to address the much more difficult question of the validity of section 1.170A-14(g)(6), Income Tax Regs. *Accord Stromme v. Commissioner*, 138 T.C. 213, 218 n.8 (2012) ("For now, the better course is 'to observe the wise limitations on our function and to confine ourselves to deciding only what is necessary to the disposition of the immediate case.'" (quoting *Whitehouse v. Ill. Cent. R.R.*, 349 U.S. 366, 372-373 (1955))); *see McLaine v. Commissioner*, 138 T.C. 228, 242 (2012) (expressing the same view); *see also*, *e.g.*, *PDK Labs. Inc. v. DEA*, 362 F.3d 786, 799 (D.C. Cir. 2004) (Roberts, J., concurring in part and concurring in the judgment) (explaining that where "a sufficient ground [exists] for deciding * * * [a] case, * * * the cardinal principle of judicial restraint--if it is not necessary to decide more, it is necessary not to decide more--counsels us to go no further"). Unlike the opinion of the Court, I would leave that question for another day when its answer would make a difference to the resolution of a case before us.

Because the opinion of the Court decides to do otherwise, however, I explain below why a portion of the regulation upheld by the opinion of the Court, if interpreted as the Commissioner urges, reflects an unreasonable interpretation of the statute under step two of the framework established by *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984), *see infra* Part II, and also fails to meet the procedural requirements of the Administrative Procedure Act ("APA"), 5 U.S.C. sec. 553 (2018), *see infra* Part III.

I. *The Easement Fails To Meet the Statutory Requirements.*

I begin by considering first things first: whether the Conservation Easement and Declaration of Restrictions and Covenants (the "Deed") through which Oakbrook granted an easement covering about three-quarters of its tract to SRLC passes muster under section 170(h). As the opinion of the Court observes, the parties understood that changes in circumstances might make it impossible to continue protecting the conservation area in the future. *See* op. Ct. p. 4.

The dispute before us focuses on the provisions of the Deed addressing the possibility of unanticipated changes in circumstances. If that possibility were to materialize, the Deed provides that the donee will be entitled to an amount

> equal to the difference between (a) the fair market value of the Conservation Area as if not burdened by this Conservation Easement and (b) the fair market value of the Conserva-

> tion Area burdened by this Conservation Easement, as such values are determined as of the date of this Conservation Easement, (c) less amounts for improvements made by [Oakbrook] in the Conservation Area subsequent to the date of this Conservation Easement * * *

Deed art. VI, sec. B(2). As explained further below, this provision fails to convey to the donee the requisite rights under section 170(h)(2)(C) and (5)(A).

A. *Statutory Framework*

Section 170 generally allows a deduction for contributions to certain charitable organizations. *See* sec. 170(a), (c). *See generally Glass v. Commissioner*, 471 F.3d 698, 706-708 (6th Cir. 2006) (providing a summary of the rules governing deductions for qualified conservation easements), *aff'g* 124 T.C. 258 (2005). But section 170 also imposes restrictions on the types of contributions for which a deduction is allowed. As relevant here, subparagraph A of section 170(0(3) generally disallows a deduction for contributions of partial interests in property. Yet what subparagraph A takes away, subparagraph B gives back in certain circumstances. In the words of that provision, "[s]ubparagraph (A) shall not apply to * * * [among others] a qualified conservation contribution." Sec. 170(0(3)(B)(iii).

Section 170(h)(1) tells us what a "qualified conservation contribution" is:

> For purposes of subsection (f)(3)(B)(iii), the term "qualified conservation contribution" means a contribution--
>
> (A) of a qualified real property interest,
>
> (B) to a qualified organization,

(C) exclusively for conservation purposes.

That definition includes its own defined terms. Thus, section 170(h)(2) explains:

> For purposes of * * * [section 170(h)], the term "qualified real property interest" means any of the following *interests in real property:*
>
> (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. [Emphasis added.]

Section 170(h)(3) goes on to explain what a "qualified organization" is for these purposes,[1] and section 170(h)(4) defines what constitutes a "conservation purpose." The statute also provides that "[a] contribution shall not be treated as exclusively for conservation purposes *unless the conservation purpose is protected in perpetuity."* Sec. 170(h)(5)(A) (emphasis added).[2]

The upshot of these provisions is that a donor who contributes to an appropriate organization a partial "interest[] in real property" may be entitled to a charitable contribution deduction if (1) that interest is a restriction on how the real property may be used, (2) the restriction is granted in perpetuity, (3) the restriction advances (that is, is "for") a conservation

[1] The parties agree that the easement at issue was granted to a "qualified organization," making it unnecessary to linger over this requirement.

[2] The parties also agree that the easement was for a "conservation purpose." As explained in more detail below, the dispute is whether it was "exclusively" so.

purpose, and (4) the conservation purpose is protected in perpetuity.

B. *Application of Statutory Framework to the Easement*

Oakbrook cannot prevail because the easement at issue here fails to meet the requirements of the statute. Specifically, Deed article VI, section B(2), which sets forth the formula to determine the amount to which SRLC would be entitled where an unexpected change in conditions makes impossible or impractical the continued use of the easement for conservation purposes, runs counter to the Code.

The Code does not address explicitly what should happen if unexpected changes that occur after the granting of the easement make it impossible or impractical to continue using the property for the conservation purposes set out in the Deed. But that does not mean that it is silent on this score, and the parties appear to agree that, if the donor and the donee's real property interests are converted into money as a result of such unexpected changes, the statutory requirement of section 170(h)(5)(A) can be satisfied so long as the donee receives an appropriate amount of money and uses that money in a manner consistent with the purposes of the original contribution. The only question is what the appropriate amount of money should be.

Oakbrook maintains that the requirement of section 170(h)(5)(A) is met so long as the donee, upon a sale or other disposition after extinguishment by judicial proceeding, would obtain an amount equal to the fair market value of the easement at the time the easement was established, subject to reduction for subsequent improvements funded exclusively by the donor.[3] But Oakbrook's position ignores the fact that, to be eligible for a deduction under section 170(h) in the first place, a donor must grant to a donee an "interest[] in real property." Sec. 170(h)(2). One of the rights inherent in a real property interest (and presumably required to be transferred to the donee in order to satisfy section 170(h)(2)(C)) is the property holder's right to be compensated at fair market value upon a subsequent transfer or taking. *See* Tenn. Code Ann. sec. 29-17-910 (2020) ("In all instances the amount to which an owner is entitled shall be determined by ascertaining the fair cash market value of the property or property rights taken[.]"); *McKinney v. Smith Cty.,* No. M1998-00074-COAR3CV, 1999 WL 1000887, at *6-*7 (Tenn. Ct. App. Nov. 5, 1999) (addressing the compensation due to the owner of an "easement of access [that] has been taken or impaired by the State" and collecting authorities).[4]

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[3] By contrast, the Commissioner maintains that, under the terms of the easement, the donee must both get the benefit of any appreciation in the value of the easement from the time the easement was granted up to the time it is converted into money and share in any appreciation attributable to improvements to the property funded exclusively by the donor.

[4] For additional analysis on this point, consider also *Olson v. United States,* 292 U.S. 246, 254-255 (1934) (noting, in a case involving an easement permitting private land to be flooded from time to time, that "'no private property shall be appropriated to public uses unless a full and exact equivalent for it be returned to the owner'" and observing that "[t]hat equivalent is the market value of the property at the time of the taking contemporaneously paid in money" (quoting *Monongahela Navigation Co. v. United States,* 148 U.S. 312, 326 (1893))), and *United States v. Miller,* 317 U.S. 369, 373-374 (1943) (observing that "the courts early adopted, and have retained, the concept of market value" for determining the value of property taken by Government action). *See also United States ex rel. Tenn. Valley Auth. v. Easement and Right of Way Over a Tract of Land in Madison Cty.*, 405 F.2d 305,

The fair market value of a real property interest would be expected to change--i.e., increase or decrease--based on changes in circumstances.[5] But, under the approach

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307 (6th Cir. 1968) (calculating "just compensation" after State condemnation of easement); *Turner v. United States*, 23 Cl. Ct. 447 (1991) (applying *Miller* in awarding damages with respect to a flooding easement); *United States v. An Easement and Right-of-Way Over 3.74 Acres of Land, More or Less, in Montgomery Cty.*, 415 F. Supp. 3d 812, 818-819 (M.D. Tenn. 2019) (calculating "just compensation" after State condemnation of easement); 2 Thompson on Real Property, Thomas Editions, sec. 14.04(c)(1) (2019) ("Ownership has been likened to a bundle of sticks. Each stick represents one of the total number of possible interests in sum of rights, powers, privileges, immunities and liabilities. * * * If one conceives of property as likened thus to a bundle of rights, privileges, immunities and liabilities adaptable to any physical thing, the fee simple absolute is the largest segment thereof that the political philosophy of the time and place permits any private individual to obtain."); 9 Thompson on Real Property, *supra*, sec. 80.08(b)(2)(ii) ("Where the taking is not total, the 'before and after' rule is commonly used. Just compensation for a partial taking is calculated either at (a) the value of the remainder before taking minus the value of the remainder after taking, or (b) the value of the entire tract before the taking minus the value of the remainder after the taking." (Fn. ref. omitted.)).

[5] "For those who consider legislative history relevant," *Warger v. Shauers*, 574 U.S. 40, 48 (2014), I note for context that, in their reports on the bills proposing what became section 170(h), both the House Ways and Means Committee and the Senate Finance Committee took as a given the right of an easement holder to be compensated at fair market value for transferring that right, *see* H.R. Rept. No. 96-1278, at 19 (1980); S. Rept. No. 96-1007, at 14 (1980), 1980-2 C.B. 599, 606. As the House committee report observed:

> In general, a deduction is allowed for a charitable contribution in the amount of the fair market value of the contributed property, defined as the price at which the property would change hands between a willing buyer and a willing seller. Thus, the amount of the deduction for the contribution of a conservation

Oakbrook proposes (and the Deed reflects), the only amount guaranteed to the owner of the easement (i.e., the donee) in the event the real property rights are converted into cash is a fixed dollar amount equal to the fair market value of the easement as of the grant date. That fixed dollar amount fails to account for any market-based appreciation that may have occurred after the grant of the easement. The formula set out in the Deed exposes the fundamental problem for Oakbrook--under the terms of the Deed, the donee never received the type of "interest[] in real property" contemplated by section 170(h)(2)(C) and further protected by section 170(h)(5)(A). Put another way, by failing to convey to the donee the unrestricted right to be compensated at fair market value upon a future transfer or taking, the Deed so restricted the donee's interest as to cause it to fall outside the purview of section 170(h)(2)(C).

The shortcoming inherent in the Deed also affects Oakbrook's compliance with section 170(h)(5)(A). The payment of a predetermined fixed amount would be insufficient as compensation for a right "protected in perpetuity" if the fair market value of the property had appreciated since the date the easement was granted. When a transfer of money to the donee is intended to

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> easement or other restriction is the fair market value of the interest conveyed to the recipient. However, because markets generally are not well established for easements or similar restrictions, the willing buyer/ willing seller test may be difficult to apply *(although it may become increasingly possible to determine the value of conservation easements by reference to amounts paid for such interests in easement acquisition programs as such programs increase).* * * *

H.R. Rept. No. 96-1278, at 19 (emphasis added); S. Rept. No. 96-1007, at 14, 1980-2 C.B. at 606.

satisfy the "perpetuity of purpose" requirement of section 170(h)(5)(A), no reasonable reading of the statute would bless the donee receiving an amount that is less than the fair market value of its "interest[] in real property" as of the time of the conversion of its interest into cash.[6]

In short, because the Deed fails to satisfy the provisions of the statute, Oakbrook would not be entitled to a charitable contribution deduction. The Commissioner's disallowance of that deduction must therefore be sustained.

II. *The Commissioner's Reading of the Donor Improvements Portion of the Regulation Does Not Survive Substantive Review Under Step Two of Chevron.*

As explained above, the statute provides a sufficient basis for denying the deduction at issue here. In light of that conclusion, I need not address the validity of the regulation. Indeed, we should not. As Justice Frankfurter once cautioned, when faced with "perplexing

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[6] As the Supreme Court has observed, "[b]ecause the Constitution protects rather than creates property interests, the existence of a property interest is determined by reference to 'existing rules or understandings that stem from an independent source such as state law.'" *Phillips v. Wash. Legal Found.*, 524 U.S. 156, 164 (1998) (quoting *Bd. of Regents of State Colls. v. Roth*, 408 U.S. 564, 577 (1972)). Tennessee accordingly could mandate that the donor receive all amounts from any judicial extinguishment. As Oakbrook has not made that point (which would clinch the case on its behalf), I assume that, under Tennessee law, Oakbrook is not entitled to such proceeds and that such proceeds would be allocated to the donor and the donee on the basis of the relevant values of the real property interests at issue at the time of extinguishment. *Cf.* Tenn. Code Ann. sec. 29-16-203(c)(1) (2020) (providing rules for the allocation of proceeds between a landlord and a tenant in an eminent domain proceeding).

questions," "[t]heir difficulty admonishes us to observe the wise limitations on our function and to confine ourselves to deciding only what is necessary to the disposition of the immediate case." *Whitehouse*, 349 U.S. at 372-373. This Court has heeded that admonition in the past. *Stromme v. Commissioner*, 138 T.C. at 218 n.8 (citing *Whitehouse*, 349 U.S. at 372-373, *Ashwander v. Tenn. Valley Auth.*, 297 U.S. 288, 345-346 (1936) (Brandeis, J., concurring), and *Liverpool, N.Y. & Phila. S.S. Co. v. Comm'rs of Emigration*, 113 U.S. 33, 39 (1885)); *accord McLaine v. Commissioner*, 138 T.C. at 242. It should do so here as well.

The opinion of the Court nonetheless has chosen to consider and uphold the validity of the regulation. In so doing, it endorses the gloss that the Commissioner has applied to the regulation with respect to donor improvements--a topic wholly absent from the text of the regulation. Because the opinion of the Court upholds the regulation in its entirety, it becomes necessary to set out my reasons for disagreeing with the Court's conclusion on this score. As explained in further detail below, I believe that, if interpreted as the Commissioner requests, the portion of the regulation addressing donor improvements does not survive substantive review under step two of the *Chevron* framework.

Before turning to this point, however, I consider first whether the regulation at issue needs to be interpreted as the Commissioner urges.

A. *Section 1.170A-14(g)(6) Is Susceptible to Two Potential Readings.*

As discussed above section 170(h)(1)(C) allows a deduction only when the contribution of a qualified real property interest is "exclusively for conservation purposes," and section 170(h)(5)(A) provides that "[a] contribution shall not be treated as exclusively for conservation purposes *unless the conservation purpose is protected in perpetuity."* (Emphasis added.) Moreover, when it comes to easements, the grant must be "in perpetuity." Sec. 170(h)(2)(C). Implementing these provisions, section 1.170A-14(g)(6)(ii), Income Tax Regs., provides that

> for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time. * * *

The regulation provides, in my view, a fuller description of what the statute requires--that is, the conveyance of an "interest[] in real property" "granted in perpetuity" that does not limit in any way the charity's inherent right to monetize the fair market value of the conveyed interest at some point in the future. *See supra* Part I.A. and B. So far, the regulation is consistent with the statute and is unobjectionable.

The regulation goes on to explain that "[f]or purposes of this paragraph (g)(6)(ii), that proportionate value of the donee's property rights shall remain constant." Sec. 1.170A-14(g)(6)(ii), Income Tax Regs. This sentence is susceptible to two different readings.

1. *Alternative 1*

On the one hand, the sentence could be read to provide that, all else being equal, the proportionate values of the partial interests owned by the donor and the donee, respectively, do not change even as the fair market value of the property as a whole may vary with market conditions. To illustrate, if the value of the easement at the time the gift is made is $500,000, and the value of the property as a whole at the same time is $1,000,000, the proportionate value of the donee's property right would be 50% and the proportionate value of the donor's property right would also be 50%. Thus, if the property remains unchanged by the donor and is sold after a judicial extinguishment proceeding, as provided in section 1.170A-14(g)(6)(i), Income Tax Regs., the donee and the donor would each be entitled to 50% of the proceeds. This would be true whether the property as a whole had increased in value to, say, $1,500,000 or had decreased in value to, say, $500,000. In the first instance, the donee would be entitled to $750,000 of the proceeds (i.e., 50% of $1,500,000), and, in the second, the donee would be entitled to $250,000 (i.e., 50% of $500,000). In either situation, the donee would receive a portion of the proceeds attributable to its own interest, taking into account market developments. Consistent with this reading, the last sentence of section 1.170A-14(g)(6)(ii), Income Tax Regs., provides:

> Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(I) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the *perpetual conservation restriction* * * * [Emphasis added.]

This reading of the regulation leaves open the possibility that improvements by the donor to its own partial real property interest may need to be taken into account if they occur. When such improvements are made, the parties would be expected to determine the fair market value of their respective interests as of the time of the improvements and provide for future allocations of proceeds in light of the improvements. Continuing with the example set out above, assume that three years after the easement is granted, when the value of the property as a whole has increased to \$2,000,000, the donor decides to build a house worth \$2,000,000 on the property as permitted by the express terms of the easement. *Cf.* sec. 1.170A-14(f), *Examples* (3) and (4), Income Tax Regs.; Letter from Michael S. Gruen, Easements Comm. Chairman, New York Landmarks Conservancy, to Commissioner of Internal Revenue (Aug. 31, 1983), Respondent's Response to Order Dated 02/27/2019, at 372 (filed Mar. 27, 2019) (the "NYLC Comment Letter") (setting out a similar example in comments provided to Treasury in response to the proposed regulations on conservation easements). Before the house is built, the value of the easement would be \$1,000,000 (\$2,000,000 times the preimprovement share of 50%). After the house is built, one would expect the value of the easement not to have changed, since the house improved the donor's retained real property interest. With respect to the donor, the interest in the unimproved land would be expected to be worth \$1,000,000 (\$2,000,000 times the preimprovement share of 50%), and the interest in the improvements would be expected to be worth \$2,000,000. If, shortly after completion of the house, the property were required to be sold to a governmental entity for \$4,000,000 to permit the construction of a highway, the proceeds could be allocated as follows:

Recipient and interest	*Amount*	*Share of total proceeds*
Proceeds attributable to donee's interest	$1,000,000	25%
Proceeds attributable to donor's interest in unimproved land	1,000,000	25%
Proceeds attributable to donor's improvements	2,000,000	50%
Total	4,000,000	100%

As the example illustrates, the "proportionate value of the donee's property rights" remains constant when compared to the donor's property rights as they existed at the time of the grant. Although each of those rights is now worth only 25% of the total value of the property as a whole (and they were worth 50% of the total value of the property as a whole before the house was constructed), they still have a one-to-one relationship to each other.[7] Thus, under this reading of the regulation,

[7] The analysis set out in this Part II.A.1. is consistent with the analysis of the U.S. Court of Appeals for the Fifth Circuit in *PBBM-Rose Hill, Ltd. v. Commissioner*, 900 F.3d 193, 207-208 (5th Cir. 2018). There the Fifth Circuit made clear that all of the proceeds from a future sale must be taken into account before the ratio is applied and that those proceeds may not be reduced first to account for donor improvements. *Id.* at 208 (explaining that, because the deed at issue "permits the deduction of the value of improvements from the proceeds, prior to the donee taking its share, the provision fails to meet the requirement set forth in § 1.170A-14(g)(6)(ii)"); *see also Carroll v. Commissioner*, 146 T.C. 196, 203 (2016) (addressing a deed that had a similar provision). The Fifth Circuit did not consider the central analytical issue in this case--how to determine the proper ratio between the inter-

permitting the donor to be compensated with respect to future expenditures incurred in improving the donor's own property interest would not be inconsistent with the text of the regulation.[8]

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ests of donee and donor when the donor has made subsequent improvements to its retained interest, thereby increasing the fair market value of the property as a whole. The analysis set out in the text starts at the same point as the Fifth Circuit did--"the total amount brought in from the sale," *PBBM-Rose Hill, Ltd. v. Commissioner*, 900 F.3d at 208--and then focuses on how the donee's and donor's shares are computed before those shares are applied to the undiminished proceeds from the sale, *see also infra* note 8.

[8] Note that, under this reading of the regulation, donor improvements would not receive priority of compensation as compared to the donee's interest. For example, if, after the house was built, real property values in the area declined significantly and the overall fair market value of the property was reduced to $1,000,000, proceeds from a sale at that time would be distributed as follows:

Recipient and interest	*Amount*	*Share of total proceeds*
Proceeds attributable to donee's interest	$250,000	25%
Proceeds attributable to donor's interest in unimproved land	250,000	25%
Proceeds attributable to donor's improvements	500,000	50%
Total	1,000,000	100%

As before, the "proportionate value of the donee's property rights" remains constant when compared to the donor's property rights as they existed at the time of the grant. They still have a one-to-one relationship to each other. And, although the donee would receive only $250,000 of the overall proceeds, the reduction from the initial value of $500,000 is attributable to market forces. As the initial example in the text shows, *see supra* pp. 47-48, the donee would have received a similar (reduced) compensation if

2. *Alternative 2*

The Commissioner maintains that the regulation does considerably more work than suggested by the reading under Alternative 1. In his view, the Deed must provide that the proportionate value of the donee's property rights will remain constant no matter what the donor does with respect to its own partial real property interest after the easement is granted. Under this categorical reading, if the donor makes significant improvements to its own partial interest, the donor may not be entitled to be compensated for the value of those improvements if the value of the property is converted into cash in the future.

To illustrate using the example from above, if, shortly after the house is completed, the property were required to be sold to a governmental entity for $4,000,000 to permit the construction of a highway, according to the Commissioner, the proceeds should be allocated as follows:

Recipient and interest	*Amount*	*Share of total proceeds*
Proceeds allocated to donee	$2,000,000	50%
Proceeds allocated to donor (for unimproved land and the house)	2,000,000	50%
Total	4,000,000	100%

no improvements had been made and the overall value of the property at some point had declined to $500,000 from the initial overall value of $1,000,000.

It is not clear to me how a rule that is focused on the "proportionate value of the *perpetual conservation restriction*," sec. 1.170A-14(g)(6)(ii), Income Tax Regs. (emphasis added), may be read to force the donor to promise in the deed that the donor will turn over to the donee proceeds properly attributable to the donor's own retained real property interest. But that is how the Commissioner reads the regulation and what the opinion of the Court accepts today. To my eye, however, that reading cannot survive step two of the *Chevron* analysis.[9]

B. *The Commissioner's Reading of the Donor Improvements Portion of the Regulation Does Not Survive Substantive Review Under Step Two of Chevron.*

Two preliminary comments before getting to the substantive issue. First, although in reviewing the validity of a regulation a court generally begins by considering whether the regulation complies with the APA's procedural requirements, in this case, it is useful to turn first to the substantive validity of the regulation, as an understanding of the substantive merits of the issue also sheds light on the validity of the procedures employed by Treasury in promulgating the regulation.

Second, for purposes of this analysis, I assume without deciding that the statute is ambiguous regarding the allocation of proceeds in the event of a judicial extinguishment of an easement. *See Good*

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[9] *Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.,* 467 U.S. 837 (1984), provides the framework for analysis here unless and until that case is overruled. *See Baldwin v. United States,* 589 U.S. ___, 140 S. Ct. 690 (2020) (Thomas, J., dissenting from denial of certiorari).

Fortune Shipping SA v. Commissioner, 897 F.3d 256, 261 (D.C. Cir. 2018) ("[W]e may * * * assume arguendo that the statute is ambiguous and proceed to *Chevron's* second step."), *rev'g* 148 T.C. 262 (2017).

Now to the merits. The question under *Chevron* step two is whether the interpretation of the regulation offered by the Commissioner reflects a permissible reading of the statute. As the Supreme Court has said:

> *Chevron* directs courts to accept an agency's reasonable resolution of an ambiguity in a statute that the agency administers. * * * *[Chevron],* at 842-843. Even under this deferential standard, however, "agencies must operate within the bounds of reasonable interpretation." *Utility Air Regulatory Group v. EPA,* 573 U.S. ___, ___ (2014) (slip op., at 16) (internal quotation marks omitted). * * *

Michigan v. EPA, 576 U.S. ___, ___, 135 S. Ct. 2699, 2707 (2015); *see also Tenn. Hosp. Assoc. v. Azar,* 908 F.3d 1029, 1037-1038 (6th Cir. 2018) (summarizing standard of review); *Atrium Med. Ctr. v. U.S. Dep't of Health & Human Servs.,* 766 F.3d 560, 566-568 (6th Cir. 2014) (same). Here, the Commissioner "strayed far beyond those bounds" when he read section 170(h)(5)(A) to require a donor to turn over to the donee a portion of the proceeds attributable to its own permissible retained real property interest. *Michigan,* 576 U.S. at ___, 135 S. Ct. at 2707.

It is well settled that

> [w]hether an agency's construction is reasonable depends, in part, "on the construction's 'fit' with the statutory language, as well as its conformity to statutory purposes." *Goldstein v. SEC,* 451 F.3d 873, 881 (D.C. Cir.

> 2006) (quoting *Abbott Labs. v. Young,* 920 F.2d 984, 988 (D.C. Cir. 1990)). Indeed, "[t]he starting place for any *Chevron* Step Two inquiry is the text of the statute." *Van Hollen v.* FEC, 811 F.3d 486, 492 (D.C. Cir. 2016).

Good Fortune Shipping SA v. Commissioner, 897 F.3d at 262.

I begin at the same starting place--the statutory text. The statute provides a deduction for a contribution to a qualified organization of a "qualified real property interest" made "exclusively for conservation purposes." Although the statute makes clear that there can be no deduction unless the conservation purposes are "protected in perpetuity," one cannot lose track of the fact that the deduction is predicated on a "qualified real property interest" being contributed to a qualified organization. Thus, the most that a qualified organization can be entitled to receive if its "qualified real property interest" is extinguished in the future is the full value of that interest. Whatever the purpose of a contribution, that purpose may not be invoked to require the donor to give the donee, as a precondition to receiving a deduction for his contribution, a right to receive compensation properly attributed to the real property interest that the Code permits the donor to retain. A regulation interpreted to require otherwise cannot be a permissible interpretation of the statutory text before us. Under that text, the interest the donee organization must obtain in connection with a contribution is the "qualified real property interest" transferred to it. Requiring the donor to promise to turn over to the donee proceeds in excess of the fair market value of that interest is inconsistent with the statutory framework, and nothing in the "statutory purposes" compels a different conclusion. *Goldstein,* 451 F.3d at 881 (quoting *Abbott Labs.,* 920 F.2d at 988).

The opinion of the Court admits that "[i]t is conceivable that Treasury could have drafted a regulation that addressed the possibility of donor improvements, dealing with [the types of questions noted above] in some rational way." *See* op. Ct. p. 30. But the opinion of the Court overlooks the lack of a "rational" solution to those problems, by noting that "that was a policy decision for Treasury, not this Court, to make." *See id.* In the Court's view, "Treasury's overarching goal [in prescribing the regulation] was to guarantee that the donee, upon judicial extinguishment of the easement, would receive the full share of proceeds to which it was entitled. * * * Treasury exercised reasoned judgment by adhering to a simple rule that splits sale proceeds in a direct proportional manner." *See id.* p. 31.

I agree with the opinion of the Court that the donee should "receive the full share of proceeds to which *it was entitled." See id.* (emphasis added). But a rule interpreted to require the deed to allocate to the donee not only the proceeds attributable to *its own* real property interest but also a share of the proceeds attributable to the interest the Code permits *the donor* to retain does not ""'fit'" with the statutory language" and is unreasonable. *Good Fortune Shipping SA v. Commissioner,* 897 F.3d at 262 (quoting *Goldstein,* 451 F.3d at 881). Calling it a "policy decision" does not change the fact that the rule, as interpreted by the Commissioner, yields in certain circumstances a result that is entirely unreasonable and without any basis in the statute. Under *Chevron,* Treasury is entitled to draw lines on the page provided by Congress; *Chevron* does not give Treasury legislative authority to substitute a different page for the one Congress enacted into law. *See id.* (citing *Goldstein,* 451 F.3d at 881). In short, in my judgment, if section 1.170A-14(g)(6)(ii), Income Tax Regs., is interpreted as the Commissioner maintains with respect to all future donor improvements, it is an unreasonable interpretation of the statute and therefore invalid.[10]

III. *If Read as the Commissioner Proposes, the Donor Improvements Portion of the Regulation Does Not Comply With the Procedural Requirements of the APA.*

Treasury might not have found itself in this predicament under *Chevron* if it had followed more carefully the APA's procedural requirements, which are designed to help agencies consider exactly this type of issue before a rule becomes final. It is to those requirements that I now turn.

In evaluating whether the categorical reading of the donor improvements rule advanced by the Commissioner meets the procedural requirements of the APA, I consider first the framework that governs judicial

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[10] I note that my conclusion here does not help Oakbrook. The Deed provides that proceeds from a future sale must first be paid to Oakbrook in respect of "improvements made by * * * [Oakbrook] in the Conservation Area subsequent to the date of this Conservation Easement." Deed art. VI, sec. B(2). As explained above, *see supra* notes 7 and 8, I do not think that an "improvements are compensated first" approach is consistent with the real property interests contemplated by the Code. Accordingly, this aspect of Oakbrook's Deed provides an additional, and independent, ground for denying the deduction at issue. This aspect of the Deed also provides one more reason to reserve for another day a decision on whether the regulation, as interpreted by the Commissioner, is valid insofar as it addresses improvements made by a donor after the granting of the easement.

review in this area. I then apply that framework to Treasury's rulemaking process in the case before us.

A. *Applicable Framework for Judicial Review*

The APA sets out procedural requirements for the promulgation of legislative rules. As relevant here, an agency wishing to adopt such a rule must provide notice in the Federal Register. 5 U.S.C. sec. 553(b). In addition,

> [a]fter notice required by this section, the agency shall give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments with or without opportunity for oral presentation. After consideration of the relevant matter presented, the agency shall incorporate in the rules adopted a concise general statement of their basis and purpose. * * *

5 U.S.C. sec. 553(c). Section 706 of the APA, which sets the boundaries for judicial review of agency actions, provides that a "reviewing court shall * * * hold unlawful and set aside agency action, findings, and conclusions found to be * * * arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 5 U.S.C. sec. 706(2)(A) (2018).

The framework for reviewing whether an agency has complied with the procedural requirements of the APA is well established. As the Supreme Court has explained with respect to legislative rules such as the ones before us:

> One of the basic procedural requirements of administrative rulemaking is that an agency must give adequate reasons for its decisions.

> The agency "must examine the relevant data and articulate a satisfactory explanation for its action including a rational connection between the facts found and the choice made." *Motor Vehicle Mfrs. Assn. of United States, Inc. v. State Farm Mut. Automobile Ins. Co.,* 463 U.S. 29, 43 (1983) (internal quotation marks omitted). That requirement is satisfied when the agency's explanation is clear enough that its "path may reasonably be discerned." *Bowman Transp., Inc. v. Arkansas-Best Freight System, Inc.*, 419 U.S. 281, 286 (1974). But where the agency has failed to provide even that minimal level of analysis, its action is arbitrary and capricious and so cannot carry the force of law. *See* 5 U.S.C. § 706(2)(A); *State Farm, supra,* at 42-43.

Encino Motorcars, LLC v. Navarro, 579 U.S. ___, ___, 136 S. Ct. 2117, 2125 (2016).

When the record does not contain "that minimal level of analysis," "[i]t is not the role of the courts to speculate on reasons that might have supported an agency's decision. '[W]e may not supply a reasoned basis for the agency's action that the agency itself has not given.'" *Id.* at ___, ___, 136 S. Ct. at 2125, 2127 (quoting *State Farm,* 463 U.S. at 43); *see also Atrium Med. Ctr.,* 766 F.3d at 568 ("[A]n agency cannot bolster its case with rationales offered post hoc." (citing *Columbus & S. Ohio Elec. Co. v. Costle,* 638 F.2d 910, 912 (6th Cir. 1980))).

As the Supreme Court further explained in *Judulang v. Holder,* 565 U.S. 42, 52-53 (2011),

> [t]he scope of * * * [judicial] review under * * * [section 706(2)(A) of the APA] is "narrow";

> as we have often recognized, "a court is not to substitute its judgment for that of the agency." *Motor Vehicle Mfrs Ass'n of United States, Inc. v. State Farm Mut. Automobile Ins.* Co., 436 U.S. 29, 43 (1983); see *Citizens to Preserve Overton Park, Inc. v. Volpe,* 401 U.S. 402, 416 (1971). Agencies * * * have expertise and experience in administering their statutes that no court can properly ignore. But courts retain a role, and an important one, in ensuring that agencies have engaged in reasoned decisionmaking. When reviewing an agency action, we must assess, among other matters, "'whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment.'" *State Farm,* 463 U.S. at 43 (quoting *Bowman Transp. Inc. v. Arkansas-Best Freight System, Inc.,* 419 U.S. 281, 285). That task involves examining the reasons for agency decisions--or, as the case may be, the absence of such reasons. See *FCC v. Fox Television Stations, Inc.,* 556 U.S. 502, 515 (2009) (noting "the requirement that an agency provide reasoned explanation for its action").

Accord Atrium Med. Ctr., 766 F.3d at 567 ("At base, arbitrary and capricious review functions to 'ensur[e] that agencies have engaged in reasoned decisionmaking.'" (quoting *Judulang,* 565 U.S. at 53)).

A recent decision by the U.S. Court of Appeals for the District of Columbia Circuit aptly summarizes the APA's procedural requirements, particularly as they address the need for an agency to consider comments:

> "The APA's arbitrary-and-capricious standard requires that agency rules be reasonable and

reasonably explained." *Nat'l Tel. Coop. Ass'n v. FCC,* 563 F.3d 536, 540 (D.C. Cir. 2009). An agency violates this standard if it "entirely fail[s] to consider an important aspect of the problem." *State Farm,* 463 U.S. at 43. An agency also violates this standard if it fails to respond to "significant points" and consider "all relevant factors" raised by the public comments. *Home Box Office, Inc. v. FCC,* 567 F.2d 9, 35-36 (D.C. Cir. 1977).

Accordingly, an agency must respond to comments "that can be thought to challenge a fundamental premise" underlying the proposed agency decision. *MCI WorldCom, Inc. v. FCC,* 209 F.3d 760, 765 (D.C. Cir. 2000). An agency need not "discuss every item of fact or opinion included in the submissions made to it." *Del. Dep't of Nat. Res. & Envtl. Control v. EPA,* 785 F.3d 1, 17 (D.C. Cir. 2015) (citation omitted). An agency's response to public comments, however, must be sufficient to enable the courts "to see what major issues of policy were ventilated . . . and why the agency reacted to them as it did." *Id.* (citation omitted). Even when an agency "has significant discretion in deciding how much weight to accord each statutory factor," that does not mean it is "free to ignore any individual factor entirely." *Tex. Oil & Gas Ass'n v. EPA,* 161 F.3d 923, 934 (5th Cir. 1998) (citing *Weyerhaeuser Co. v. Costle,* 590 F.2d 1011, 1045 (D.C. Cir. 1978)) (evaluating agency's consideration of statutory factors under arbitrary-and-capricious review).

Carlson v. Postal Regulatory Comm'n, 938 F.3d 337, 343-344 (D.C. Cir. 2019). Put another way, "[a]n agency is required to provide a meaningful opportunity for comments, which means that the agency's mind must be open to considering them." *Grand Canyon Air Tour Coal. v. FAA,* 154 F.3d 455, 468 (D.C. Cir. 1998) (citing *McLouth Steel Prods. Corp. v. Thomas,* 838 F.2d 1317, 1323 (D.C. Cir. 1988)). "An agency must also demonstrate the rationality of its decision-making process by responding to those comments that are relevant and significant." *Id.* (citing *Prof l Pilots Fed'n v. FAA,* 118 F.3d 758, 763 (D.C. Cir. 1997), and *Home Box Office,* 567 F.2d at 35);[11] *see also PPG Indus., Inc. v. Costle,* 630 F.2d 462, 466 (6th Cir. 1980) (explaining that the APA requires agencies "to give reasoned responses to all significant comments in a rulemaking proceeding").

The reasons for the procedural requirements of the APA are not difficult to understand.

> [They] are intended to assist judicial review as well as to provide fair treatment for persons affected by a rule. To this end there must be an exchange of views, information, and criticism between interested persons and the agency. Consequently, the notice required by the APA, or information subsequently supplied to the public, must disclose in detail

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[11] As the Court of Appeals in *Home Box Office, Inc. v. FCC,* 567 F.2d 9, 35 n.58 (D.C. Cir. 1977), noted:

> In determining what points are significant, the "arbitrary and capricious" standard of review must be kept in mind. Thus only comments which, if true, raise points relevant to the agency's decision and which, if adopted, would require a change in an agency's proposed rule cast doubt on the reasonableness of a position taken by the agency. * * *

> the thinking that has animated the form of a proposed rule and the data upon which that rule is based. Moreover, a dialogue is a two-way street: the opportunity to comment is meaningless unless the agency responds to significant points raised by the public. A response is also mandated by *Overton Park,* which requires a reviewing court to assure itself that all relevant factors have been considered by the agency.

Home Box Office, 567 F.2d at 35-36 (fn. ref. omitted) (citations omitted); *see also Dismas Charities, Inc. v. U.S. Dep't of Justice,* 401 F.3d 666, 678 (6th Cir. 2005) ("[O]ne of the central purposes of the * * * [notice-and-comment requirement] is to give those with interests affected by rules the chance to participate in the promulgation of the rules * * * [and] ensure fair treatment for persons to be affected by regulations.").

Notwithstanding the very good reasons for requiring an agency to respond to comments,

> an agency's failure to address a particular comment or category of comments is not an APA violation *per se. See, e.g., Thompson v. Clark,* 741 F.2d 401, 408 (D.C. Cir. 1984) ("[APA § 553] has never been interpreted to require the agency to respond to every comment, or to analyze every issue or alternative raised by the comments, no matter how insubstantial."). We review an agency's response to comments under the same arbitrary-and-capricious standard to which we hold the rest of its actions. *See Home Box Office,* 567 F.2d at 35 n.58. Put simply, "The failure to respond to comments is significant only insofar as it demonstrates that the agency's decision was

> not based on a consideration of the relevant factors." *Covad Commc'ns v. FCC,* 450 F.3d 528, 550 (D.C. Cir. 2006) (quoting *Thompson,* 741 F.2d at 409).

Sherley v. Sebelius, 689 F.3d 776, 784 (D.C. Cir. 2012); *see also PPG Indus.,* 630 F.2d at 466.

B. *Application of Framework for Judicial Review*

Having outlined above the framework that governs our review of the regulation at issue here, I turn next to applying that framework.

1. *Treasury's Rulemaking Process*

I begin by summarizing what we know about Treasury's rulemaking process in this case. On May 23, 1983, Treasury and the Internal Revenue Service (the "IRS")[12] issued a notice proposing "regulations relating to contributions of partial interests in property for conservation purposes." 48 Fed. Reg. 22940 (May 23, 1983). The stated purpose of the notice was "to clearify [sic] the statutory rules in effect under * * * [the Tax Treatment Extension Act of 1980]." *Id.* The notice also observed that "[t]he regulations reflect the major policy decisions made by the Congress and expressed in * * * [the] committee reports" that accompanied the legislation. *Id.* The notice spanned roughly eight pages of the Federal Register, including a one-page preamble. The notice also invited public comments and explained that "[a] public hearing * * * [would] be held upon written request to the Commissioner by any person who has submitted written comments." *Id.* at 22941. The initial deadline for submitting comments was July 22, 1983. *Id.* at 22940. That

[12] For simplicity, I refer to both Treasury and the IRS as "Treasury."

deadline was subsequently extended to September 1, 1983. See 48 Fed. Reg. 33006 (July 20, 1983).

In response to the notice, Treasury received more than 700 pages of comments during the extended comment period[13] and at least another 130 pages after the comment period had closed.[14] A hearing on the proposed regulation was requested and was held on September 15, 1983. Thirty-seven members of the public were originally scheduled to speak at the hearing, and 30 actually spoke. The hearing lasted more than five hours, and the transcript exceeds 200 pages.

A Treasury Decision adopting final regulations was published in the Federal Register on January 14, 1986. *See* T.D. 8069, 1986-1 C.B. 89, 51 Fed. Reg. 1496 (Jan. 14, 1986). The Treasury Decision spanned roughly 12 pages, of which approximately 10 contained the actual text of the regulations. That left just over two pages for Treasury's responses to comments and other administrative matters (for example, the Paperwork Reduction Act notice and drafting information). Put another way, Treasury used six columns of the Federal Register to address more than 700 pages of timely

[13] Some public comments in the administrative record were transmitted after the close of the extended comment period on September 1, 1983, but before the public hearing took place on September 15, 1983.

[14] Although some comments cover overlapping issues, they do not appear to be mass generated by nonexistent commenters. Cf. James V. Grimaldi, "U.S. News: FCC Chief Proposes Revamp of Online Comments," Wall St. J., July 12, 2018, at A3; James V. Grimaldi and Paul Overberg, "Fiduciary Rule Draws A Lot of Fake Critics," Wall St. J., Dec. 28, 2017, at Bl; James V. Grimaldi and Paul Overberg, "Fake Comments Hit Rule Making--Phony Submissions Target Net Neutrality," Wall St. J., Dec. 13, 2017, at A1.

comments and more than 200 pages of public testimony. Those six columns were intended to cover comments on a "regulation project consisting of 10 paragraphs, 23 subparagraphs, 30 subdivisions, and 21 examples." *See* op. Ct. p. 24.

One might wonder how an agency familiar with the D.C. Circuit's decision in *Home Box Office,* which by 1986 had been on the books for more than eight years, could have thought that six columns in the Federal Register sufficed to "respond[] to significant points raised by the public" in more than 700 pages, or how that response constituted a "dialogue" between the agency and the public contemplated by the APA as interpreted by *Home Box Office* and the authorities on which it relied. *Home Box Office,* 567 F.2d at 35-36 (fn. ref. omitted); *see also PPG Indus.,* 630 F.2d at 466 (reiterating that the APA requires agencies "to give reasoned responses to all significant comments in a rulemaking proceeding"). Even for an agency determined to be exceedingly "concise," six columns in the Federal Register would be a tight amount of space to show "what major issues of policy were ventilated . . . and why the agency reacted to them as it did." *Carlson,* 938 F.3d at 344 (alteration in original) (quoting *Del. Dep't of Nat. Res. & Envtl. Control v. EPA,* 785 F.3d 1, 17 (D.C. Cir. 2015)).

But, in my view, Treasury did not think it confronted such a Herculean task. It is more likely that Treasury was simply following its historical position that the APA's procedural requirements did not apply to these types of regulations.[15] As the Treasury Decision

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[15] *See* Kristin E. Hickman, "Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements," 82 Notre Dame L. Rev. 1727, 1729 (2007) ("Treasury acknowledges that APA section

explains, Treasury took the view that "[a]lthough a notice of proposed rulemaking which solicited public comments was issued, the * * * [IRS] concluded when the notice was issued that the regulations are interpretative and that the notice and public comment procedure requirement of 5 U.S.C. 553 did not apply."[16] T.D. 8069, 1986-1 C.B. at 92. When an agency engaged in a particular rulemaking exercise believes the APA does not require it to provide notice and receive comments at all, it is not difficult to see why that agency might think that a rather brief explanation, offered as it were out of its own generosity, should be good enough.[17]

The problem with this position, however, is that Treasury's conclusion that the regulation at issue here did not require notice and comment was mistaken, as the opinion of the Court correctly makes clear. *See* op.

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553 governs its various regulatory efforts. Treasury also contends, however, that most Treasury regulations are interpretive in character and thus exempt from the public notice and comment requirements by the APA's own terms." (Fn. ref. omitted.)).

[16] On this basis, the Treasury Decision concluded that "the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6)." T.D. 8069, 1986-1 C.B. 89, 92, 51 Fed. Reg. 1498.

[17] There is no doubt that Treasury knows how to provide meaningful responses to comments when it considers itself bound by the notice and comment requirements of the APA. *See, e.g.,* T.D. 9846, 2019-9 I.R.B. 583, 84 Fed. Reg. 1838 (Feb. 5, 2019) (Treasury Decision concerning regulations under section 965 spanned 78 pages of the Federal Register, including a preamble of more than 36 pages, of which more than 30 pages responded to comments); T.D. 9790, 2016-45 I.R.B. 540, 81 Fed. Reg. 72858 (Oct. 21, 2016) (Treasury Decision concerning regulations under section 385 spanned 127 pages of the Federal Register, including a preamble of more than 90 pages, of which more than 80 pages responded to comments).

Ct. pp. 17-18. In light of that conclusion, at least with respect to the donor improvements interpretation that the Commissioner advances before us, the six Federal Register columns that Treasury offered fail to provide "that minimal level of analysis" required by the APA. *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2125.

As explained further below, Treasury failed to "respond to 'significant points' and consider 'all relevant factors' raised by the public comments." *See Carlson,* 938 F.3d at 344 (quoting *Home Box Office,* 567 F.2d at 35-36); *PPG Indus.,* 630 F.2d at 466.

2. *Application of Framework to Treasury's Rulemaking Process*

The question of how to treat donor improvements undertaken after the grant of the easement in the event the property was subsequently sold was put squarely before Treasury during the comment period. On August 31, 1983, the New York Landmarks Conservancy ("NYLC") submitted a comment letter of just over four pages. *See* NYLC Comment Letter, *supra.* Two of those pages were dedicated to the extinguishment provisions at issue here, and nearly half of that discussion focused on the treatment of future improvements made by the donor. On future improvements, the NYLC Comment Letter explained as follows:

> The structure of § 1.170A-13(g)(5)(ii) [the proposed rule for what is now section 1.170A-14(g)(6)(ii), Income Tax Regs.,] contemplates that a ratio of value of the conservation restriction to value of the fee will be fixed at the time of the donation and will remain in effect forever thereafter. *This formula fails to take into account that improvements may be made thereafter by the owner which should*

> *properly alter the ratio.* For example, (using the facts of example 4 in § 1.170A-13(f) [the proposed rule for what is now section 1.170A-14(f), Income Tax Regs.,] at page 22945), suppose the donation of a scenic easement upon Greenacre providing limited cluster development in areas generally not visible from a nearby national park. At the time of the donation, Greenacre was worth $100,000 and the easement accounts for 10% of the value. Thereafter, the owner spends $2 million on the construction of housing units to be rented. If the easement were subsequently extinguished, the donee organization would be entitled under § 1.170A-13(g)(5)(ii) to 10% of the sale price of the entire parcel including the improvements. *This would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization.*
>
> * * * * * * *
>
> In light of the potential inequities described above, the * * * [NYLC] recommends that the proposed proceeds formula be revised to prevent such inequities should the Department of the Treasury decide to retain the provision. However, the * * * [NYLC] strongly recommends deletion of the entire extinguishment provision.

Respondent's Response to Order Dated 02/27/2019, at 374-375 (emphasis added).

The NYLC Comment Letter supported its recommendation as follows:

> The provisions for apportionment of proceeds in the case of extinguishment of a conserva-

> tion restriction * * * contain problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of these provisions. The statute was enacted by Congress to encourage the protection of our significant natural and built environment through the donation of conservation restrictions and yet, the proposed provisions would thwart the purpose of the statute by deterring prospective donors.

Id. at 373.

As shown above, the NYLC Comment Letter made clear that, in its view, it would be inappropriate to condition the availability of the deduction for a conservation easement on the donor's agreement to turn over to the donee proceeds attributable to improvements on the real property interest that the Code permitted the donor to retain. The NYLC Comment Letter expressly tied its comments both to a specific rule included in the proposed regulations--proposed section 1.170A-13(g)(5)(ii) (which ultimately became current section 1.170A-14(g)(6)(ii), Income Tax Regs.)--and to a specific fact pattern contemplated by the proposed regulations--Example (4) in proposed section 1.170A-13(0 (which ultimately became Example (4) in section 1.170A-14(f), Income Tax Regs.). The NYLC Comment Letter also explained that the proposed rule would "thwart the purpose of the statute," which, according to NYLC, was to "encourage the protection of our significant natural and built environment through the donation of conservation restrictions." *Id.* at 373. A proposed rule that required a donor to turn over to the donee proceeds that were properly attributable to the retained interest of the donor "would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization." *Id.* at 374. In light of these concerns, NYLC recommended that this provision be deleted or, at the very least, "be revised to prevent * * * [the] inequities" it had identified. *Id.*

The record leaves no doubt that NYLC made comments "'that can be thought to challenge a fundamental premise' underlying the proposed agency decision." *Carlson,* 938 F.3d at 344 (quoting *MCI WorldCom, Inc.,* 209 F.3d at 765). The preamble to the proposed regulations had explained that the proposed rules "reflect the major policy decisions made by the Congress." 48 Fed. Reg. 22940. The NYLC Comment Letter in effect countered that the proposed rule on future donor improvements was contrary to those policy decisions, would lead to inequitable results that were inconsistent with the statute, and would deter future contributions. In short, the NYLC Comment Letter offered comments that, "if adopted, would require a change in an agency's proposed rule." *Home Box Office,* 567 F.2d at 35 n.58. Those comments were both "relevant and significant," requiring a response. *Grand Canyon,* 154 F.3d at 468; *accord Carlson,* 938 F.3d at 343-344.

Unfortunately, however, the Treasury Decision finalizing the regulations contains no such response. The Treasury Decision changed the sentence on which the Commissioner relies with respect to donor improvements as follows (with the relevant change underscored):

> (1) Proposed Regulation: "For purposes of this paragraph (g)(5)(ii), *that original minimum proportionate value* of the donee's property rights shall remain constant." 48 Fed. Reg. 22946.

> (2) Final Regulation: "For purposes of this paragraph (g)(6)(ii), *that proportionate value* of the donee's property rights shall remain constant." T.D. 8069, 1986-1 C.B. at 99.

But Treasury gave no explanation as to how the change addressed the concerns expressed in the NYLC Comment Letter. In short, Treasury's actions did not provide "an explanation [that] is clear enough that its 'path may reasonably be discerned.'" *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2125 (quoting *Bowman Transp.,* 419 U.S. at 286).[18] Nor does Treasury's action provide any insight on "what major issues of policy were ventilated . . . and why the agency reacted to them as it did" on this point. *Carlson,* 938 F.3d at 344 (quoting *Del. Dep't of Nat. Res. & Envtl. Control,* 785 F.3d at 17). Absent any explanation from Treasury on why the considerations raised by NYLC should not have been heeded, "[i]t is not the role of the courts to speculate on reasons that might have supported an agency's decision. '[W]e may not supply a reasoned basis for the agency's action that the agency itself has

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[18] In *Bowman Transportation,* the case that gave rise to the "path may reasonably be discerned" formulation, the Supreme Court observed that the Interstate Commerce Commission had in fact provided an explanation of how it had viewed the relevant evidence and proceeded to discuss that explanation. *Bowman Transp., Inc. v. Ark.-Best Freight Sys., Inc.,* 419 U.S. 281, 290 (1974) ("The question before the Commission was whether service on the routes at issue would be enhanced by permitting new entry, and as to this the performance by prospective entrants on new routes was of limited relevance. The Commission noted with respect to transit times that different highway conditions might make experience there a poor indication of the times applicants could provide on the routes they sought to enter."). The record here fails to provide even "that minimal level of analysis," *Encino Motorcars, LLC v. Navarro,* 579 U.S. ___, ___, 136 S. Ct. 2117, 2125 (2016), required by *Bowman Transportation.*

not given.'" *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2127 (quoting *State Farm,* 463 U.S. at 43).[19]

The opinion of the Court's defense of the future donor improvements portion of the regulation is unpersuasive. The Court observes that "[t]he preamble to the final regulations states that, '[a]fter consideration of all comments regarding the proposed amendments * * * , those amendments are adopted as revised by this Treasury decision,'" *see* op. Ct. p. 20 (quoting T.D. 8069, 1986-1 C.B. at 90), and also notes that "[t]his Court has found a similar statement, coupled with the administrative record, sufficient to find that Treasury had considered the relevant matter presented to it," *see id.* (citing *Wing v. Commissioner,* 81 T.C. 17, 31-32 (1983)). But as the U.S. Court of Appeals for the Sixth Circuit has observed "[w]e are not required to 'take the agency's word that it considered all relevant matters.'" *PPG Indus.,* 630 F.2d at 466 (quoting *Asarco, Inc. v. EPA,* 616 F.2d 1153, 1160 (9th Cir. 1980)). Moreover, the opinion of the Court's reliance on *Wing* is misplaced, as that case was decided before the Supreme Court and the Courts of Appeals had articulated fully the framework for judicial review

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[19] The opinion of the Court notes that NYLC "offered no suggestion about how the subject of donor improvements might be handled; it simply recommended 'deletion of the entire extinguishment provision.'" *See* op. Ct. p. 22. If the Court means to suggest that a comment may be disregarded unless it proposes specific text for how the regulation should be changed, that is not required by the APA. Once a commenter brings a relevant and significant issue to the agency's attention, it is the agency's responsibility to determine how that comment should be implemented. The agency cannot rely on the public to do its homework. *See Home Box Office,* 567 F.2d at 35-36 ("[T]he opportunity to comment is meaningless unless *the agency* responds to significant points raised by the public." (Emphasis added; fn. ref. omitted.)).

of legislative rules under the procedural requirements of the APA. *See supra* Part III.A.

The opinion of the Court also appears to suggest that because "[o]nly one of the 90 commenters mentioned donor improvements, and it devoted exactly one paragraph to this subject," *see* op. Ct. p. 21, Treasury was not required to respond to it. This is not so. A "relevant and significant comment" requires a response, regardless of whether the point is made by many, a few, or even a single commenter. *See, e.g., Carlson,* 938 F.3d at 342, 345-349 (invalidating an increase in the price of stamps, in part, on the basis of comments from Douglas Carlson, "a postal customer and watchdog"). Moreover, a comment does not lose its significance because it is presented succinctly. After all, the Commissioner can hardly complain about NYLC's brevity in this case. The Commissioner's own position with respect to future donor improvements is based on a single sentence, and NYLC's comments on this issue were certainly longer than a sentence. In addition, the Commissioner's actions belie any claim that the comment did not raise a significant issue. As Oakbrook observes in its "Reply to Memorandum Regarding the Validity of Treas. Reg. Section 1.170A-14(g)(6)(ii)," "[i]t is disingenuous for Respondent to now argue that comments regarding the * * * [regulation at issue] are not 'significant,' when Respondent has repeatedly denied taxpayers' deductions for failure to comply with" that regulation.

The opinion of the Court also seems to suggest that the scope of the project--the fact that it included "10 paragraphs, 23 subparagraphs, 30 subdivisions, and 21 examples," *see* op. Ct. p. 24--somehow excuses Treasury's failure to respond to comments on the provision at issue here. But Treasury chose the scope of the project. If the project was too large to permit an appropriate response to all “relevant and significant comments,” then Treasury could have broken the project down into smaller parts. What it could not do is avoid the “dialogue” required by the APA and say nothing about “significant points raised by the public.” *Home Box Office,* 567 F.2d at 35-36 (fn. ref. omitted). As the opinion of the Court acknowledges, the “detail required in a statement of basis and purpose depends on the subject of the regulation and the nature of the comments received.” *See* op. Ct. p. 24 (quoting *Reytblatt v. U.S. Nuclear Regulatory Comm’n,* 105 F.3d 715, 722 (D.C. Cir. 1997)). Although “[t]his statement need only ‘contain sufficient information to allow a court to exercise judicial review,’” see id. (quoting *United States v. Garner,* 767 F.2d 104, 117 (5th Cir. 1985)), it does require *some* information. And here Treasury offered no response at all.

Finally, I note that this would not be the first case in which a court invalidated a Treasury regulation on procedural grounds, as the opinion of the Court acknowledges. *See id.* note 4. Oakbrook’s “Reply to Memorandum Regarding the Validity of Treas. Reg. Section 1.170A-14(g)(6)(ii)” cites, at 5 and 6, the U.S. Court of Appeals for the Federal Circuit’s decision in *Dominion Res., Inc. v. United States,* 681 F.3d 1313, 1319 (Fed. Cir. 2012). That decision held (in Part V) that “[t]he associated-property rule in Treasury Regulation § 1.263A-11(e)(1)(ii)(B) as applied to property temporarily withdrawn from service also violates the *State Farm* requirement that Treasury provide a reasoned explanation for adopting a regulation.”[20] *Id.*; *see also*

[20] In addition to holding that the regulation at issue failed to satisfy *Motor Vehicle Mfrs Ass’n of United States, Inc. v. State Farm Mut. Automobile Ins. Co.,* 436 U.S. 29 (1983), the majority

id. at 1320 (Clevenger, J., concurring in part and concurring in the result) ("There appears to be no dispute among the panel that the government has not articulated any rational explanation for many details of the regulation before us, from the regulation's first proposal in the mid-'90s up to the current date. Such a failure makes the regulation procedurally unlawful. I would reverse on the grounds set forth in part V of the majority opinion[.]"). The opinion of the Court attempts to distinguish *Dominion Resources* from this case on the ground that the majority in *Dominion Resources* also held that the regulation there failed under step two of *Chevron*. *See* op. Ct. note 4. But that distinction does not carry the day. The procedural holding in the case was an independent ground for the decision, as the concurring judge made clear.[21] *See Woods v. Interstate Realty Co.,* 337 U.S. 535, 537 (1949) ("[W]here a decision rests on two or more grounds, none can be

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in *Dominion Res., Inc. v. United States,* 681 F.3d 1313 (Fed. Cir. 2012), held that the regulation failed under step two of the *Chevron* analysis, hence the "also" in the quotation above.

[21] Judge Clevenger disagreed with the majority's decision to reach the *Chevron* step two analysis, observing:

> The outcome of this case can and should extend from *State Farm.* The government's failure to justify its regulation *ab initio* left open the question of whether the avoided cost principle necessarily undermines any rationale that could justify treating an adjusted basis of property withdrawn from service for improvement as a production expenditure, for purposes of calculating interest to be capitalized. Such reaffirms my conclusion that this appeal does not present an appropriate vehicle for deciding the *Chevron* question. It is therefore a more discreet approach to leave that question aside. * * *

Dominion Res., 681 F.3d at 1322 (Clevenger, J., concurring in part and concurring in the result).

relegated to the category of obiter dictum." (citing *United States v. Title Ins. & Tr. Co.,* 265 U.S. 472, 486 (1924), and *Massachusetts v. United States,* 333 U.S. 611, 623 (1948))). Treasury's procedural missteps here are similar to, and perhaps more significant than, those in *Dominion Resources.*[22]

Returning to the facts of this case, if Treasury had paid closer attention to the NYLC Comment Letter, it might have course-corrected and adopted a formula that properly accounted for future donor improvements and foreclosed the categorical interpretation advanced by the Commissioner in this case. That is after all why the APA requires agencies "to provide a meaningful opportunity for comments, which means that the agency's mind must be open to considering them." *Grand Canyon,* 154 F.3d at 468 (citing *McLouth,* 838 F.2d at 1323). By failing to do so here, Treasury did itself a disservice.

For the reasons set out above, I believe the donor improvements rule, as read by the Commissioner, is inconsistent with the procedural requirements of the APA. "When an administrative agency sets policy, it must provide a reasoned explanation for its action. That is not a high bar, but it is an unwavering one. Here, * * * [Treasury] has failed to meet it." *Judulang,* 565 U.S. at 45. With respect, I cannot agree with the Court's contrary conclusion.

* * *

[22] Treasury's failure to comply with the procedural requirements of the APA also resulted in the invalidation of a temporary regulation issued under section 7874. *See Chamber of Commerce v. IRS,* No. 1:16-CV-944-LY, 2017 WL 4682050 (W.D. Tex. Oct. 6, 2017).

I end where I began. The ultimate question before the opinion of the Court is whether Oakbrook is entitled to the charitable contribution deduction it claimed on the basis of the easement it granted to SRLC. As I have explained, applying the text of the statute to the terms of that easement leads to the conclusion that the easement is not a "qualified conservation contribution." Accordingly, Oakbrook is not entitled to a charitable contribution deduction. That conclusion fully resolves the dispute before us. The remaining issues raised by the parties present "perplexing questions," on which the members of this Court do not agree. As Justice Frankfurter once cautioned, "[t]heir difficulty admonishes us to observe the wise limitations on our function and to confine ourselves to deciding only what is necessary to the disposition of the immediate case." *Whitehouse,* 349 U.S. at 372373. That is what I would have done. Because the Court does otherwise, I respectfully concur only in the result.

GUSTAFSON, J., agrees with parts I, II.A, and II.B of this concurring opinion, URDA, J., agrees with this concurring opinion, and JONES, J., agrees with part I of this concurring opinion.

HOLMES, J., dissenting: Our holding today will likely deny any charitable deduction to hundreds or thousands of taxpayers who donated the conservation easements that protect perhaps millions of acres. *See Oakbrook Land Holdings, LLC v. Commissioner,* T.C. Memo. 2020-54, at *7 n.2. This is the second time we've taken an ax to entire forests of these deductions. In *Pine Mountain Pres., LLLP v. Commissioner,* 151 T.C. 247 (2018), *appeal filed* (11th Cir. May 7, 2019), we went ahead and held that reserving a limited right to build on conserved property--unless the site is described with exceptional precision--destroys any deduction for the donation, knowing that we were setting up a conflict with the only circuit court to rule on the issue. *See id.* at 272-73 (stating that we will not follow *BC Ranch II, L.P. v. Commissioner,* 867 F.3d 547 (5th Cir. 2017), *vacating and remanding Bosque Canyon Ranch, L.P. v. Commissioner,* T.C. Memo. 2015-130).

In today's case, we hold that the Treasury Department gets to ignore basic principles of administrative law that require an agency "to give reasoned responses to all significant comments in a rulemaking proceeding." *PPG Indus., Inc. v. Costle,* 630 F.2d 462, 466 (6th Cir. 1980). A court is supposed to ensure that an agency has taken "a 'hard look' at all relevant issues and considered reasonable alternatives." *Simms v. Nat'l Highway Traffic Safety Admin.,* 45 F.3d 999, 1004 (6th Cir. 1995) (quoting *Neighborhood TV Co., Inc. v. FCC,* 742 F.2d 629, 639 (D.C. Cir. 1984)). But if the majority is right, the Treasury Department can get by with the administrative-state equivalent of a quiet shrug, a knowing wink, and a silent fleeting glance from across a crowded room.

This is not the way rulemaking is supposed to be. And it is not the way that the Article III courts, including the court to which an appeal of this case lies, review the validity of regulations. To explain what we should have done,

- briefly review some general principles of administrative law that are relevant here,
- explain why this regulation is procedurally invalid,
- suggest that even if procedurally valid its thin administrative record might make it substantively invalid, and
- summarize where this leaves conservation-easement-deduction law after today.

I.

A.

We begin by blazing through this thicket to where the trails of administrative and procedural law meet. The majority mentions the age of this regulation as a reason to uphold it. *See* op. Ct. pp. 31-33. But when could it have been challenged?[1] Title 28 U.S.C. section 2401(a) provides that, with limited exceptions not relevant here, "every civil action commenced against the United States shall be barred unless the complaint is filed within six years after the right of action first accrues."

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[1] The Ninth Circuit asked this question even when the parties didn't raise it. *See* Order, Sept. 28, 2018, at 1, *Altera Corp. v. Commissioner,* 926 F.3d 1061 (9th Cir. 2019) (Nos. 16-70496, 16-70497) (ordering the parties to be prepared to discuss whether the six-year statute of limitations should be applicable to a tax regulation, as well as offering the opportunity to file supplemental briefs on the question).

Treasury issued the regulation at issue in 1986. *See* 51 Fed. Reg. 1496 (Jan. 14, 1986). Oakbrook was formed in August 2007 and filed its petition in March 2013, within six years of the regulation's first invading its interest.[2] And the Sixth Circuit has held that 28 U.S.C. "[s]ection 2401(a) does not limit a federal court's subject-matter jurisdiction." *Herr v. U.S. Forest Serv.,* 803 F.3d 809, 818 (6th Cir. 2015). The age of this regulation is no obstacle to challenging its validity here.

This is a shallow root that Oakbrook can just stroll over.

B.

With this pop quiz in civil procedure over, we can graduate to Ad Law 101. As a general matter, for a regulation--including tax regulations--to be valid its promulgation must comply with the notice-and-comment procedures of the Administrative Procedure Act (APA).[3]

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[2] The Anti-Injunction Act (AIA) prohibits taxpayers from bringing suit "for the purpose of restraining the assessment or collection of any tax." Sec. 7421(a). Courts interpret this language to mean that the AIA "generally bars pre-enforcement challenges to certain tax statutes and regulations." *Fla. Bankers Ass'n v. U.S. Dep't of Treasury,* 799 F.3d 1065, 1066 (D.C. Cir. 2015). This does make tax law exceptional, but even on this topic there has been one powerful dissental, *see CIC Servs., LLC v. IRS,* 925 F.3d 247, 259-61 (6th Cir. 2019) (Nalbandian, J., dissenting), *cert. granted,* ___ U.S. ___, ___ S. Ct. ___, 2020 WL 2105208 (May 4, 2020), and academic analysis, *see* Kristin E. Hickman & Gerald Kerska, "Restoring the Lost Anti-Injunction Act", 103 Va. L. Rev. 1683 (2017), that suggest a change may be coming. We, of course, look to the law as it currently is.

[3] Notice-and-comment procedures apply only to "legislative rules"--i.e. rules with the force of law. *See Perez v. Mortg. Bankers Ass'n,* 575 U.S. 92, 96 (2015). I agree with the majority that this rule, even though the Treasury Department called it "interpre-

See 5 U.S.C. sec. 553(a)-(c) (2006); *Perez v. Mortg. Bankers Ass'n,* 575 U.S. 92, 96 (2015); *Mayo Found. for Med. Educ. & Research v. United States,* 562 U.S. 44, 55 (2011) ("[W]e are not inclined to carve out an approach to administrative review good for tax law only. To the contrary, we have expressly '[r]ecogniz[ed] the importance of maintaining a uniform approach to judicial review of administrative action.'" (quoting *Dickinson v. Zurko,* 527 U.S. 150, 154 (1999))); *Children's Hosp. of the King's Daughters, Inc. v. Azar,* 896 F.3d 615, 619-20 (4th Cir. 2018). If a regulation is promulgated properly under notice-and-comment procedures, we must next look to review the substance of the agency action--i.e., does the agency action run counter to the statutory language, *see Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.,* 467 U.S. 837, 842-43 (1984), or was the agency's decision making arbitrary and capricious, see APA sec. 706(2)(A); *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.,* 463 U.S. 29, 46 (1983). Only if we find that the agency's action complied with APA section 553 do we then apply the arbitrary-and-capricious standard of APA section 706(2)(A), *see HLI Lordship Indus., Inc. v. Comm. for Purchase from the Blind & Other Severely Handicapped,* 791 F.2d 1136, 1140 (4th Cir. 1986) ("The 'concise general statement' mandated by [APA section] 553(c), and other procedural requirements, are preconditions to the highly deferential 'arbitrary and capricious' standard of review."), or *Chevron's* related standard.[4]

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tive", is actually "legislative" and, therefore, notice-and-comment procedures apply. *See* op. Ct. pp. 16-17.

[4] But, as Justice Thomas has argued, the *Chevron* two-step may even be contrary to the APA itself. *See Baldwin v. United States,* 589 U.S. ___, ___, 140 S. Ct. 690, 692 (2020) (Thomas, J., dissenting from denial of certiorari).

And, as a general point, the agency's articulation for a regulation's validity must be contemporaneous with its issuance of the final rule and within the administrative record, because a reviewing court "may not supply a reasoned basis for the agency's action that the agency itself has not given." *State Farm,* 463 U.S. at 43; *see also Atrium Med. Ctr. v. HHS,* 766 F.3d 560, 568 (6th Cir. 2014) ("[A]n agency cannot bolster its case with rationales offered post hoc"). This is not to say that an agency must perfectly articulate its reasons for choices made, as a court will "uphold a decision of less than ideal clarity if the agency's path may reasonably be discerned." *Bowman Transp., Inc. v. Ark.-Best Freight Sys., Inc.,* 419 U.S. 281, 286 (1974). "But where the agency has failed to provide *even that minimal level of analysis,* its action is arbitrary and capricious." *Encino Motorcars, LLC v. Navarro,* 579 U.S. ___, ___, 136 S. Ct. 2117, 2125 (2016) (emphasis added).

Oakbrook's main argument is directed towards Treasury's alleged procedural shortcomings in promulgating section 1.170A-14(g)(6)(ii), Income Tax Regs. The foundation of this argument is that Treasury failed to provide a reasoned basis in the administrative record for its action. Oakbrook argues that this not only makes it "difficult to discern the meaning of the Regulation, [or] how to apply it in practice," but frustrates any meaningful analysis of "whether the [Treasury]'s action in promulgating the Regulation is arbitrary and capricious." This argument goes to the heart of Treasury's rulemaking procedure under the APA and may be of decisive importance because only regulations issued in a valid manner are eligible for deference. *See Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2125. There are no special procedural rules for tax regulations--we have to look to the APA, which itself "sets forth the full extent of judicial authority to review executive agency action for procedural correctness." *FCC v. Fox Television Stations, Inc.,* 556 U.S. 502, 513 (2009).

On this point, I do agree with the majority, which correctly points out, *see* op. Ct. p. 17, that APA section 553 has three requirements for an agency that wants to issue regulations through informal rulemaking. It must (1) publish a notice of proposed rulemaking in the Federal Register; (2) provide the public with an opportunity to participate in the rulemaking--commonly through the submission of written comments; and (3) after consideration of relevant public submissions, publish the final rule and a concise statement of its basis and purpose. APA sec. 553(b)-(c). But the majority, I fear, has missed the main root of Oakbrook's argument--that at the time of the regulation's promulgation, commenters made significant comments, and Treasury failed to address them in its statement of the regulation's basis and purpose. *See, e.g., Reytblatt v. U.S. Nuclear Regulatory Comm'n,* 105 F.3d 715, 722 (D.C. Cir. 1997) (basis and purpose statement inextricably intertwined with receipt of comments); *United States v. Nova Scotia Food Prods. Corp.,* 568 F.2d 240, 252 (2d Cir. 1977) ("concise general statement" required by APA section 553(c) is inadequate when material comments are left completely unanswered).

II.

With these general principles in place, one can turn to the merits of Oakbrook's procedural challenge to the regulation--that Treasury failed to respond to significant comments relating to section 1.170A-14(g)(6)(ii), Income Tax Regs.

A.

Let's turn first to the comments sent to Treasury while it contemplated the regulation before us.[5] Treasury received approximately 90 comments regarding the substance of the proposed section 170A regulations.[6] Among those, the following commenters specifically expressed concern with what is now section 1.170A-14(g)(6)(ii), Income Tax Regs.:

- New York Landmarks Conservancy;
- Philadelphia Historic Preservation Corporation;
- The Trust for Public Land;
- Landmarks Preservation Council of Illinois;
- Maine Coast Heritage Trust;
- The Nature Conservancy;
- Western Pennsylvania Conservancy;
- Brandywine Conservancy, Inc.;
- Hofstra University;
- Natural Lands Trust, Inc.;
- National Trust for Historic Preservation;
- The Washington Trust for Historic Preservation; and

[5] We directed the Commissioner to provide the comments that the public submitted during the rulemaking proceeding. He filed the entire administrative record for T.D. 8069, 1986-1 C.B. 89, in which the Final Rule was published. That record amounted to over 2,500 pages, and included over 550 pages of submissions from the public.

[6] This number excludes timely comments that asked only to participate in the public hearing.

- Land Trust Exchange.

These commenters raised a variety of potentially significant issues with the proposed rule, but I focus only on those relevant to Oakbrook's challenge here: Why did Treasury choose to require that a donee receive a proportionate share rather than a fixed sum if the easement is extinguished or condemned? And why did Treasury choose to require that a donee share in the value added to the property by later improvements to it? (We'll follow the majority's shorthand and call these the problems of proportionate share and donor improvements.) The comments submitted by the New York Landmarks Conservancy (NYLC) addressed these questions most extensively. According to the NYLC, "[t]he provisions for apportionment of proceeds in the case of extinguishment of a conservation restriction * * * contain problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of these provisions." Respondent's Response to Order Dated 02/27/2019, Administrative Record (Response to Order) at 373, *Oakbrook Land Holdings, LLC v. Commissioner,* T.C. Memo. 2020-54.

The NYLC identified four specific "inequities" with the provisions. First, it believed that the provisions would deter prospective donors from donating conservation easements if they were required to share extinguishment proceeds at some indeterminate time under unforeseen circumstances. *Id.* From its experience, the common-law doctrine of changed conditions allayed such concerns among easement donors but, as proposed, the extinguishment provisions "would no longer mollify these fears if a split of proceeds under unknown circumstances would be required." *Id.* at 374; *see also Oakbrook,* T.C. Memo. 2020-54, at *14-

*16 (also discussing "changed conditions" as it applies to conservation easements under common law).

Second, it felt that provisions in the proposed regulations that recognized a property right vested in the donee improperly assumed that a conservation easement represented a positive economic value to donees because of the possibility that donees might one day receive proceeds from extinguishment.[7] *See* Response to Order at 374. It argued that any such assumption was "unrealistic" since "[t]he value of a conservation restriction to the donee organization is not a monetary value but a philanthropic value as a device for achieving the charitable objectives of the organization." *Id.* So while the NYLC acknowledged it would welcome the receipt of extinguishment proceeds, it preferred the elimination of the provision because it believed that its deterrent effect on potential donors would harm conservancies more than "the prospect of

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[7] The Western Pennsylvania Conservancy (WPC) and the Maine Coast Heritage Trust (MCHT) also identified this assumption as a problem with the proposed rule and suggested that it could have untoward accounting and tax consequences. Both argued that conservation easements have a negative economic value because donees have to pay the cost of monitoring and enforcing compliance with their restrictions, while being unable to sell them except in the narrowest of circumstances. To suggest otherwise, the MCHT claimed, is not only "misleading" but could actually "jeopardize its status as a publicly-supported charity" if it were required to report conservation easements as massive assets or contributions on its Form 990, Return of Organization Exempt From Income Tax. Response to Order at 511. The WPC raised the somewhat related concern that the implication of the regulation might "require donors or conservancies to pay transfer taxes--yet another significant cumulative burden which * * * will weigh heavily against the utility of this conservation tool." *Id.* at 783.

future windfalls when restrictions are extinguished" might benefit them. *Id.*

The NYLC identified as a third problem the potential conflict between the proposed rule and state condemnation law. *Id.* at 375. To illustrate its concern, it gave an example where an easement is extinguished upon condemnation. It claimed that in such a situation "state law would operate to determine whether the conservation organization's restriction had a compensable value." *Id.* The problem, it argued, is that "[i]t is possible that some states would not provide compensation for such a property interest, yet under the proposed regulation, the owner of the condemned property would be required to share the condemnation proceeds with the conservation organization." *Id.*

The NYLC had one final concern--that "[t]he structure of [section 1.170A-14(g)(6)(ii), Income Tax Regs.,] contemplates that a ratio * * * will be fixed at the time of the donation" but that the "formula fails to take into account that improvements may be made thereafter by the owner which should properly alter the ratio." *Id.* at 374. The NYLC then provided an example where a donor improves the donated property after the gift and the donee shares in the value of those improvements upon extinguishment, which it argued "would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization." *Id.* This is precisely the argument that Oakbrook makes regarding the allocation of extinguishment proceeds attributable to improvements.

Not all commenters, however, agreed with the NYLC on this point--but even they requested more clarity. Both the Nature Conservancy and the MCHT felt that the proposed rule needed to clarify that donees would be entitled upon extinguishment to both the original proportionate value and any subsequent increase in value attributable to market forces. *See id.* at 511, 579. The Brandywine Conservancy, Inc., made a similar argument and stated that the proposed rule would "unnecessarily restrict the amount payable to the holder of an easement, if changes in surrounding territory have made the easement proportionately more valuable than the retained interest." *Id.* at 593. That conservancy argued that the rule should be changed so that a donee is "entitled to proceeds equal to the *greater* of its original proportionate value or its proportionate value at the time of the extinguishment." *Id.*

The Trust for Public Land (TPL) questioned whether the provision for the allocation of extinguishment proceeds could be enforced against anyone other than the original donor, but also felt that the regulations imposed an undue burden on donors in light of the tax-benefit rule and the remote-future-event rule.[8] TPL thought those rules would adequately address Treasury's concerns. *Id.* at 844. It suggested that the "tax benefit rule is a satisfactory means of meeting any concern the IRS may have that a donor might receive the double benefit of an easement deduction followed by later recovery of the value donated." *Id.* TPL also suggested that the remote-future-event rule should sufficiently assuage any concern that conservation easements

[8] "[T]he tax benefit rule ordinarily applies to require the inclusion of income when events occur that are fundamentally inconsistent with an earlier deduction." *Hillsboro Nat'l Bank v. Commissioner,* 460 U.S. 370, 372 (1983). The remote-future-event rule permits a charitable-contribution deduction only if, on the date of donation, the possibility that the donee's vested interest "may be defeated by the performance of some act or happening of some event * * * is so remote as to be negligible." Sec. 1.170A-14(g)(3), Income Tax Regs.

might not be protected in perpetuity, because it would bar a deduction if a donor knows at the date of donation that a change in circumstances will occur in the foreseeable future that will extinguish the easement. *Id.*

These are multiple serious comments that identified problems with the regulation when it was proposed and explained why those problems mattered. Comments with this level of detail and dispute among the commenters would seem enough to conclude that Treasury had before it "significant" comments. Such comments deserve responses.

We turn our attention to Treasury's response.

B.

What we hear is the chirping of crickets.

The Final Rule's statement of basis and purpose shows absolutely no mention of the extinguishment-proceeds clause at all, much less any mention of the proportionate-share or improvements problems--and no reasoned response to any of the public's comments on those provisions.[9] The majority doesn't deny this, see op. Ct. pp. 23-25, and we aren't even the first court to notice: In *Kaufman v. Shulman,* 687 F.3d 21, 26 (1st Cir. 2012), the First Circuit was forced to guess at the apparent purpose of the section 1.170A-14(g)(6)(ii),

[9] At least one commenter had also noticed that the proposed regulation might cause special problems for conservation easements aimed at preserving building facades. The Philadelphia Historic Preservation Corporation argued that "[t]he provisions relating to extinguishment of easements * * * are a bit perplexing and * * * unreasonable as applied to facade easements." Response to Order at 770. Treasury didn't respond to this comment either.

Income Tax Regs., after noting that it "was unexplained when first promulgated."

This makes the defining characteristic of section 1.170A-14(g)(6)(ii), Income Tax Regs., its utter lack of any contemporaneous explanation of its key choices--to require that donees get a fraction, rather than an absolute amount, of extinguishment proceeds and to require that they get a share of any proceeds from a donor's improvements to the property. There is no prefiguring of these choices in the legislative history or the notice of proposed rulemaking, and no explanation of them in the Final Rule. Had Treasury responded in any meaningful way to the comments that it received, such as those from the NYLC, neither donors and donees, nor courts, *see, e.g., Oakbrook,* T.C. Memo. 2020-54, at *20-*28 (highlighting the confusing nature of section 1.170A-14(g)(6), Income Tax Regs., and attempting to discern its meaning), nor the IRS, *compare* Priv. Ltr. Rul. 200836014 (Sept. 5, 2008) (stating that the regulation isn't violated by a conservation easement in which a donee receives only proceeds less any amount attributable to an improvement), *with Oakbrook,* T.C. Memo. 2020-54, at *36 (addressing the IRS's argument that a conservation easement in which a donee receives only proceeds less any amount attributable to an improvement is a violation of the regulation), would have to grapple with whether "proportionate value" establishes a fraction or a fixed value, or whether a donee is entitled to any extinguishment proceeds attributable to the value of improvements or rising land values. Such widespread industry confusion is precisely what APA section 553 is intended to avoid. So while we don't demand a perfect explanation for Treasury's decisionmaking, *see Bowman Transp.,* 419 U.S. at 286, we should demand some, *see Encino*

Motorcars, 579 U.S. at ___, 136 S. Ct. at 2125. And here, there wasn't any.

C.

But the majority would let the regulation stand despite this silence. It argues in turn that:

- Treasury didn't need to respond to these comments because the statement of basis and purpose made obvious what it was doing, *see* op. Ct. pp. 23-24;
- even if Treasury wasn't obvious in what it was doing, it did say it considered "all comments" and that's good enough, *see id.* p. 20; and
- even if it didn't say that it considered "all comments" it did make some changes to the proposed regulation from which we can infer its response to them, *see id.* p. 21.

Let's look at each point.

1.

The majority argues that Treasury didn't need to respond to comments regarding section 1.170A-14(g)(6)(ii). In fact, it had "no doubt" that Treasury considered the relevant matter--the agency had responded to most of the comments that it received on other parts of the rulemaking, and no agency has to address all the comments it receives. *See* op. Ct. pp. 23-24. I address this argument somewhat in reverse. There are cases that say that not every comment has to be addressed--how could it be otherwise when there are some rules that receive more than one million comments?[10] *See* Clean Water Rule: Definition of "Waters of the United States," 80 Fed. Reg. 37057 (June 29, 2015).[11] In the modern era, agencies can receive comments over the internet and run deduplicating software to make their jobs easier. *See* Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, "Abuses of the Federal Notice-and-Comment Rulemaking Process" 13-16 (Oct. 4, 2019). They can group comments that are similar or identical, and they can distill comments to fairly paraphrase the key points that they make. I therefore agree with the majority that no court has ever construed the APA to require a response to every comment separately, and that courts have construed the APA to require an agency's response to be based on the nature of the comments it has received. *See* op. Ct. p. 24; *see also Reytblatt,* 105 F.3d at 722 (quoting *Action on Smoking and Health v. CAB,* 699 F.2d 1209, 1216 (D.C. Cir. 1983)).

But the analysis shouldn't stop there--what is the *nature* of a comment that triggers an agency's obliga-

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[10] Compared to what the EPA and FCC receive, 700 pages of even "voluminous" commentary from only 90 commenting organizations, *see* op. Ct. p. 11, is rather small. Agencies frequently have to deal with more commenters and more pages of comments. *See, e.g.,* 84 Fed. Reg. 68834 (Dec. 17, 2019) (receiving over 7,700 comments on a proposed Treasury regulation dealing with section 162, 164, and 170A); 84 Fed. Reg. 2952, 2952-53 (receiving 335 comments related to 199A regulations).

[11] So many comments can crash an agency's website. *See* Soraya Nadia McDonald, "John Oliver's Net Neutrality Rant May Have Caused FCC Site Crash", Washington Post, June 4, 2014 (describing how John Oliver encouraged his viewers to comment on the FCC's proposed net-neutrality rule and the system subsequently stopped working because of more than 45,000 new comments that came in).

tion to respond? The caselaw tells us to look at a comment's *significance*. Agencies must "give reasoned responses to *all significant comments* in a rulemaking proceeding." *PPG Indus.,* 630 F.2d at 466 (emphasis added); *see also Perez,* 575 U.S. at 96 ("An agency must consider and respond to *significant comments* received during the period for public comment." (emphasis added)); *Interstate Nat. Gas Ass'n of Am. v. FERC,* 494 F.3d 1092, 1096 (D.C. Cir. 2007) (agencies must "give reasoned responses to *all significant comments"* (emphasis added)). This is because "the opportunity to comment is meaningless unless the agency responds to *significant* points raised by the public." *Home Box Office, Inc. v. FCC,* 567 F.2d 9, 35-36 (D.C. Cir. 1977) (emphasis added) (citing *Portland Cement Ass'n v. Ruckelshaus,* 486 F.2d 375, 393-94 (D.C. Cir. 1973)); *see also Nova Scotia,* 568 F.2d at 252 ("It is not in keeping with the rational process [of APA section 553(c)] to leave vital questions, raised by comments which are of cogent materiality, completely unanswered"). So, though an agency doesn't have to respond to all comments, it must respond to all *significant* comments.

This makes it important to figure out which comments are "significant" and which are not. The majority doesn't even address whether the comments here are significant.[12] But it implies that the only comments

[12] The majority focuses instead on whether Treasury considered relevant matter (which the majority has "no doubt" that it did) and whether the basis and purpose is obvious. *See* op. Ct. pp. 23-24. To support this proposition the majority cites *Cal-Almond, Inc v. U.S. Dept. Of Agric.,* 14 F.3d 429, 443 (9th Cir. 1993). *See* op. Ct. p. 24. In *Cal-Almond,* however, the agency had altogether ignored notice-and-comment procedures; the question was whether this failure was harmless error. *Cal-Almond,* 14 F.3d at 441. There wasn't even a proposed rule to comment on--interested parties had the opportunity to submit input only orally at an open

that are significant are those that "suggest alternative text." *See* op. Ct. pp. 13-14, 22 n.3. It gives no cite for this, nor could it do so, because there is not a precise definition in the caselaw--rather there are themes.

One is that an agency should address why it rejected proffered alternatives. *See Indep. U.S. Tanker Owners Comm. v. Dole,* 809 F.2d 847, 852 (D.C. Cir. 1987) (stating that the Secretary failed to address why alternative measures were rejected); *Nova Scotia,* 568 F.2d at 253 ("Though this alternative was suggested by an agency of the federal government, its suggestion, *though acknowledged,* was never answered" (emphasis added)).

Another theme is that it is not rational to "leave vital questions, raised by comments which are of cogent materiality, completely unanswered." *Nova Scotia,* 568 F.2d at 252. I agree that "[w]e do not expect the agency to discuss every item of fact or opinion included in the submissions made to it in informal rulemaking." *Id.* (quoting *Auto. Parts & Accessories Ass'n, Inc. v. Boyd,* 407 F.2d 330, 338 (D.C. Cir. 1968)). But we should be able to "see what major issues of policy were ventilated by the informal proceedings and why the agency reacted to them as it did." *Id.* (quoting *Auto. Parts,* 407 F.2d at 338). We should be able to see why Treasury "[chose] to follow one course rather than another." *See Indus. Union Dep't, AFL-CIO v. Hodgson,* 499 F.2d 467, 475 (D.C. Cir. 1974).

Significant comments are also those "which, if true, raise points relevant to the agency's decision and

board meeting. *See* 45 Fed. Reg. 56795 (Aug. 26, 1980). There is nothing in that opinion about how to gauge whether a comment was significant and whether the agency's response when it issued its final rule was adequate.

which, if adopted, would require a change in an agency's proposed rule." *Home Box Office,* 567 F.2d at 35 n.58. Significant comments are not just those that include drafts of alternative regulatory language, but those that identify a specific and objective issue created by the language of the proposed rule and give some explanation for why that language is troublesome. Think of this as the what and why test: (1) *what* is the problem; and (2) *why* is it a problem? A comment is thus more likely to be significant if the commenter suggests a remedy for the purported problem it identifies. Insignificant comments, on the other hand, are those which are "purely speculative and do not disclose the factual or policy basis on which they rest." *Id.* In the absence of significant comments or an explicit congressional directive, there is no requirement that "an agency engage in and document an exhaustive review of hypothetical 'aspect[s] of the problem.'" *SIH Partners LLLP v. Commissioner,* 150 T.C. 28, 47 (2018), *aff'd*, 923 F.3d 296 (3d Cir. 2019); *see also Thompson v. Clark,* 741 F.2d 401, 408 (D.C. Cir. 1984) NAPA section 553(c)] has never been interpreted to require the agency to respond to every comment, or to analy[z]e every issue or alternative raised by the comments, no matter how insubstantial").

When it came to the proportionate-share and donor-improvements issues, the Treasury received several comments. The NYLC believed that the regulation "contain[ed] problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of [the] provisions." Response to Order at 373. The NYLC didn't stop there, but rather identified four specific inequities with the provision:

- it would deter prospective donors from donating conservation easements, *id.*;

- the provision improperly assumed that a conservation easement represented a positive economic value to donees based on the possibility that the donees might one day receive proceeds from extinguishment, *id.* at 374;
- there was a potential conflict with the provision and state condemnation law, *id.* at 375; and
- the ratio fails to take into account improvements made by the owner after donation which should alter the ratio, *id.* at 374.

TPL agreed with the NYLC--believing that the provision was an undue burden on donors in light of the tax-benefit rule and the remote-future-event rule. *Id.* at 844. But there were those that disagreed with NYLC's points, including the Nature Conservancy, the MCHT, and Brandywine Conservancy, Inc.--feeling that the donees should be entitled to any subsequent increase in value attributable to market forces.[13] *See id.* at 511, 579, 593. But even these commenters thought the provision needed to be clearer. *Id.*

As Oakbrook points out, there were a number of comments on the extinguishment-proceeds regulation that were "significant" under these guidelines. Commenters didn't just say, "Delete the regulation, we don't like it." They wrote in to propose other alternatives to achieve the Code's requirement that the conservation purpose of a donated easement be preserved "in perpetuity."

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[13] The majority incorrectly asserts that only NYLC mentioned donor improvements. *See* op. Ct. p. 13. But TPL, Nature Conservancy, MCHT, and Brandywine Conservancy also mention them. *See* Response to Order at 511, 579, 593, 844.

These alternatives included reliance on the common-law doctrines of changed conditions to deal with the remote contingency of condemnation or judicial extinguishment. Another comment proposed reliance on the tax-benefit rule or the remote-future-event rule instead of the challenged regulation. Some pointed out that the proportionate-value rule might overcompensate donees and discourage donations, which might be thought of as contrary to the evident policy of section 170A to encourage donations of genuine conservation easements. The NYLC thought that requiring the cost of improvements to be ignored in splitting up proceeds would lead to a windfall to donees.

The majority seems to conclude that these comments were *not* significant in the specific sense in which the caselaw defines the concept: A comment "which, if true, raise points relevant to the agency's decision and which, if adopted, would require a change in an agency's proposed rule * * * ." *Home Box Office,* 567 F.2d at 35 n.58. Looking at the comments offered here--which identified inequities with the regulation, suggested alternatives, identified potential negative effects on the willingness of donors to make donations, uncovered potential conflicts with state law, and simply asked for more clarity--this is a bewildering conclusion. Under the caselaw, the comments made were significant and are entitled to an agency response.

The majority though says no sweat--even if these comments are significant, Treasury did respond to them by stating in the preamble that it considered "all comments" and by making changes to the proposed regulation.

2.

Before determining whether the agency's response here was adequate, one must first look to caselaw to determine what an adequate response even looks like. Generally, the point of the APA's procedural rules for notice-and-comment rule-making is to ensure that "there [] be an exchange of views, information, and criticism between interested persons and the agency." *Home Box Office,* 567 F.2d at 35. The notice-and-comment procedure promotes the quality of agency rules and "ensure[s] fair treatment for persons to be affected by" them. *Dismas Charities, Inc. v. U.S. Dep't of Justice,* 401 F.3d 666, 678 (6th Cir. 2005); *see also United States v. Cain,* 583 F.3d 408, 420 (6th Cir. 2009). It also provides courts with a meaningful opportunity to "see what major issues of policy were ventilated by the informal proceedings and why the agency reacted to them as it did." *Simms,* 45 F.3d at 1005 (quoting *Auto. Parts,* 407 F.2d at 338).

This is why in *Dominion Resources, Inc. v. United States,* 681 F.3d 1313, 1319 (Fed. Cir. 2012), *rev'g* 97 Fed. Cl. 239 (2011), Treasury's explicit statement that it rejected the commentators' recommendation and brief explanation in general terms of how one of the provisions worked wasn't enough. *Dominion Resources* reviewed the promulgation of Treasury regulation section 1.263A-11(e)(1)(ii)(B).[14] This regulation governed

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[14] Finding other procedural challenges to Treasury regulations may prove difficult--it wasn't until 2011 that the Supreme Court definitively pronounced that "we are not inclined to carve out an approach to administrative review good for tax law only. To the contrary, we have expressly '[r]ecogniz[ed] the importance of maintaining a uniform approach to judicial review of administrative action.'" *Mayo Found.,* 562 U.S. at 55 (quoting *Dickinson,* 527 U.S. at 154). The majority though confines its discussion of the

how much interest expense a corporation had to capitalize--instead of deduct--when it borrowed money to improve real property. What made it controversial was that it required the capitalization of interest incurred to pay not only the cost of an improvement to real property, but of the interest incurred on the entire basis of the property being improved while it was offline to add the improvement. *See* T.D. 8584, 1995-1 C.B. 20, 26. A utility company challenged its validity in *Dominion Resources,* 97 Fed. Cl. 239.

Like the regulation here, the challenged regulation in *Dominion Resources* was part of a very large project to implement a new part of the 1986 Code. As here, there had been comments on the entire regulation, as well as the specific part of it that was under attack. *See Dominion Res.,* 97 Fed. Cl. at 255-56. Unlike its silence here, Treasury's response to the comments that it'd received on the associated-property rule at issue in *Dominion Resources* were less laconic.[15] It summarized those comments in the preamble to the final regulation, and it even explained how the challenged part of the regulation would work, although the

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most relevant circuit-court case that analyzes how a Treasury regulation can be procedurally defective to a footnote. *See* op. Ct. p. 25 n.4.

[15] This rule had the shorthand name of the "associated-property rule" because it governed interest capitalization on the property associated with an improvement that needed to be taken out of service while the improvement was made. *See Dominion Res.,* 97 Fed. Cl. at 240 (stating the issue of the case required analysis of "the Treasury Department's associated-property rule for capitalizing interest on a taxpayer's installation or construction of improvements or additions to property used to generate income. The associated-property rule relates to property temporarily removed from service in connection with installation or addition of an improvement * * * .")

preamble did "not explain why the commentators' suggestion was rejected." *Id.* at 256.

The company pointed this out--"Dominion contends that Treasury 'failed to provide any explanation of the reasoning that led it to adopt the associated-property rule.'" *Id.* at 258. The trial court nevertheless upheld the rule, because Treasury seemed to have made some changes to its text in response to the comments, id. at 259; and Treasury, after summarizing some of the comments, did state "[t]he final regulations do not adopt the suggestion," *id.* at 256. As that court reasoned, "lack of exactitude and the ensuing confusion do not signify that Treasury acted to establish the final rule in an arbitrary and capricious manner. The 'path' that Treasury was taking in the rulemaking proceedings can be 'discerned,' albeit somewhat murkily." *Id.* at 259.

And then the case was appealed.

The Federal Circuit reversed. It was not enough for Treasury to mention or paraphrase the comments that it received, *see* T.D. 8584, 1995-1 C.B. 20, 26 (summarizing potential issues and alternatives raised by the comments); and it was not enough to provide general statements that a regulation was intended to implement a particular Code section or use a particular method, see id. at 21 (stating regulation designed to reduce complexity without undermining the Code provision). *See Dominion Res.,* 681 F.3d at 1319. The problem with the regulation was that a statement that Treasury had rejected a comment, or provided an explanation of how the regulation would work, is not the same as giving *reasons* for rejecting a comment or choosing why to make the regulation work one way instead of another. It's not "reasoned decision making" without reasons. *See id.* (finding that the agency failed to explain the rational connection between the facts and choices made despite statements that it had rejected comments, *see* T.D. 8584, 1995-1 C.B. at 27, and failed to explain how the regulation worked, *see id.* at 26). "An agency must cogently explain why it has exercised its discretion in a given manner." *Dominion Res.,* 681 F.3d at 1319 (quoting *State Farm,* 463 U.S. at 48). Judge Clevenger summarized the problem more pithily in his concurrence, where he wrote that "the government has not articulated any rational explanation for many details of the regulation before us, from the regulation's first proposal in the mid-'90s up to the current date. Such a failure makes the regulation procedurally unlawful." *Id.* at 1320 (Clevenger, J., concurring).[16]

Oakbrook's argument in this case is stronger--Treasury didn't even acknowledge the relevant comments or expressly state its disagreement with them. Instead it just ignored them. There is not even "a minimal level of analysis," as the Supreme Court, just a couple years ago, insisted an agency must show if it hopes to avoid its regulation's being held procedurally invalid. *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2120.

Nova Scotia also shows what should happen when an agency doesn't consider significant comments.[17]

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[16] The majority misreads *Dominion Resources* to apply only to regulations that are inconsistent with statutory text. *See* op. Ct. p. 25 n.4. Not so--a regulation that is contrary to the text of a statute is invalid as "not in accordance with law." APA sec. 706(2)(A). Treasury's failure to follow the APA's procedural requirements was an independent, alternative reason for invalidating the regulation. *See Dominion Res.,* 681 F.3d at 1319.

[17] In *Nova Scotia,* the agency was responding to several cases of botulism in fish. The challenged regulations required the fish to be cooked at a certain temperature, for a certain time, and in

There, the court found no concise general statement of why it was necessary that the regulation apply to all species of fish and why the regulation was necessary even though it was commercially infeasible for some fisheries. *Nova Scotia,* 568 F.2d at 253. The court pointed out that the Treasury failed to address suggested alternatives and was silent about the comments that asserted the proposed regulations were economically infeasible. *Id.*

But what is more illuminating is what the agency in *Nova Scotia* did do. The agency did make minor changes from the proposed regulation to the final regulation to address some comments received. *Id.* at 244. The agency did assure the reader of the preamble that it had considered the comments that it received. 35 Fed. Reg. 17401 (Nov. 13, 1970). The agency did summarize those comments. It even gave a general reason--that the regulation required for all fish the safest known procedure to prevent botulism.[18] *Id.*

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brine of a certain percentage of salinity. *Nova Scotia,* 568 F.2d at 243-44.

[18] The preamble actually had a fair amount of detail:

> Current good manufacturing practice (sanitation) in manufacture, processing, packing, or holding of smoked and smoke-flavored fish for human food.
>
> In the FEDERAL REGISTER of October 23, 1969 (34 F.R. 17176), the Commissioner of Food and Drugs proposed regulations (Subpart A, Part 128a) covering current good manufacturing practice (sanitation) in the manufacture, processing, packing, or holding of smoked fish. In response, comments were received from two trade associations, eight manufacturers, and the Bureau of Commercial Fisheries, Department of Interior. The comments include opposition to certain requirements and suggestions for clarifying and technical changes.

But those changes and several short paragraphs of explanation were not enough in *Nova Scotia.*[19] And in

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> The principal objection is that the process requirements in the proposed regulations cannot be applied to all species of fish presently being smoked by the industry and that the regulations should therefore specify time-temperature requirements, as developed by research and study, on a species-by-species basis.
>
> The Commissioner finds: (1) That although adequate times, temperatures, and salt concentrations have not been demonstrated for each individual species of fish presently smoked, the processing requirements of the proposed regulations are the safest now known to prevent the outgrowth and toxin formation of C. botulinum Type E; and (2) that since the public health hazard of C. botulinum Type E in smoked fish is not restricted to a single species of fish, the conditions of current good manufacturing practice for this industry should be established without further delay.
>
> Therefore, having considered the comments received and other relevant material, the Commissioner concludes that the proposed regulations, with most of the suggested clarifying and technical changes incorporated, should be adopted as set forth below.
>
> Accordingly, pursuant to provisions of the Federal Food, Drug, and Cosmetic Act * * * the following new Subpart A is added * * * .

35 Fed. Reg. 17401, 17401 (Nov. 13, 1970).

[19] The majority reads into *Nova Scotia* a phantom limitation of its holding to what it calls "scientific decision" regulations. *See* op. Ct. p. 22 n.3. But the Second Circuit invalidated the regulation at issue on two separate grounds. Only the first was that "[w]hen the basis for a proposed rule is a *scientific decision,* the scientific material which is believed to support the rule should be exposed to the view of interested parties for their comment." *Nova Scotia,* 568 F.2d at 252 (emphasis added). But there was a second reason for the court's holding--the agency had failed to respond to significant comments. *Id.* This part of the opinion doesn't even invoke the words "scientific decision." *Id.* at 252-53. *Nova Scotia*

Oakbrook we don't get several short paragraphs, we don't get even one short paragraph--we get *bupkis*. The IRS ignored comments that questioned the practical application of the regulation, its clarity, and special problems it would cause some donors. I agree that section 553(c) doesn't require an encyclopedia, but it has to require more than nothing; and ignoring comments in the preamble is not responding to them. As Judge Gurfein wrote in *Nova Scotia,* 586 F.2d at 252, "[t]he agencies certainly have a good deal of discretion in expressing the basis of a rule, but the agencies do not have quite the prerogative of obscurantism reserved to legislatures."

3.

The majority nevertheless says there's enough there to uphold the regulation. It first points us to the preamble to the final regulations, see op. Ct. pp. 19, 25, and insists that "all comments" were considered by Treasury here. But if we look at the notice of the final regulation, we see no meaningful consideration of comments at all.

It is true that Treasury said there that it was adopting the rule "after consideration of *all* comments." 51 Fed. Reg. at 1496 (emphasis added). And before *Encino Motorcars,* before *Chevron,* and even before

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cannot so easily be cabined. *See, e.g., Nutritional Health All. v. FDA,* 318 F.3d 92, 94, 98 (2d Cir. 2003) (applying *Nova Scotia* to a regulation regarding packaging rules); *Nat'l Black Media Coal. v. Fed. Commc'ns Comm'n,* 791 F.2d 1016, 1018, 1023 (2d Cir. 1986) (holding that an agency violated *Nova Scotia* when it failed to disclose studies and maps it relied on when crafting a regulation regarding frequency allocations for AM broadcast channels); *United States v. Garner,* 767 F.2d 104, 117-18, 121 (5th Cir. 1985) (analyzing a regulation requiring individuals to refinance their loans under *Nova Scotia*).

State Farm we *did* reason our way to upholding tax regulations by noting the ritual invocation of this magic phrase. *See Wing v. Commissioner,* 81 T.C. 17, 31-32 (1983).

But what we never seem to have noticed is how common this statement is. It certainly pops up with startling frequency in the IRS Cumulative Bulletin. *See*, *e.g.,* T.D. 8584, 1995-1 C.B. at 21 ("After careful consideration of all the comments"); T.D. 8540, 1994-2 C.B. 297, 297 ("After consideration of all of the comments received"); T.D. 8476, 1993-2 C.B. 13, 14 ("After consideration of the comments"); T.D. 8069, 1986-1 C.B. at 90 ("After consideration of all comments regarding the proposed amendments"); T.D. 8067, 1986-1 C.B. 218, 219 ("After consideration of all comments and testimony received on the proposed amendments"); T.D. 8075, 1986-1 C.B. 245, 246 ("After consideration of all written comments received"); T.D. 8065, 1986-1 C.B. 254, 254 ("After consideration of all comments regarding the proposed regulations"); T.D. 8081, 1986-1 C.B. 343, 344 ("After consideration of all comments received").

It is as if this phrase is from a form in Treasury's regulation-drafting guide--which it is. *See* Internal Revenue Manual pt. 32.1.5.4.7.1(1) (Example 4) (Aug. 21, 2018) ("After consideration of all the comments, the proposed regulations are adopted as amended"). The APA, however, has no provision for agencies to use ritual incantations to ward off judicial review. *See Dominion Res.,* 681 F.3d at 1319 (determining that the agency's statement of "[a]fter careful consideration of all the comments," T.D. 8584, 1995-1 C.B. at 21, was not a satisfactory explanation of its action). The same phrase was used by the Department of Labor when it issued the regulation that the Supreme Court invalidated in *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2126 ("The Department said that, in reaching its decision, it had 'carefully considered all of the comments, analyses, and arguments made for and against the proposed changes"). But this makes sense--because if the APA did allow comments to be disregarded with this simple magical phrase as part of a standard form, it would make commenting meaningless. *See Sherley v. Sebelius,* 689 F.3d 776, 784 (D.C. Cir. 2012) (indicating that agency action which makes commenting meaningless violates the APA) (citing *Home Box Office,* 567 F.2d at 35-36).

This was not enough in *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2127, where the Court observed that "when it came to explaining the 'good reasons for the new policy' * * * the Department said almost nothing."

It should not be good enough for us today.

4.

The majority's final argument on this topic is that Treasury actually did respond to them--not with anything in a statement that accompanied the final rule, but by changing the proposed rule before it went final. *See* op. Ct. p. 21 ("Treasury *clearly* considered the comments * * * because it *substantially* revised the text [of the regulation] in response to [the] comments" (emphasis added)). This argument, however, was rejected by Federal Circuit in *Dominion Resources,* 681 F.3d at 1319, and the Second Circuit in *Nova Scotia,* 568 F.2d at 244, 252-53.

Even if the IRS had been making a pure policy decision with no factfinding needed at all, it would still have had to identify the considerations it found persuasive. *Indus. Union Dep't,* 499 F.2d at 476. In

Ishtyaq v. Nelson, 627 F. Supp. 13 (E.D.N.Y. 1983), for example, the plaintiffs argued that a regulation lacked an adequate "concise general statement." The court disagreed because the agency had acknowledged the comments, stated its position on the principal objection raised by commenters, and showed why it chose to follow one course of action rather than another. *Id.* at 21-23.

So this idea that the agency here could respond to significant comments by making only minor changes to the proposed regulation, absent any supplemental explanation, is insufficient as a response to significant comments. But maybe the majority is right and I and the appellate courts are wrong, and a court may infer an agency's reasoned response to a significant comment.

The problem is that even if Treasury could respond in this way to significant comments, it didn't in fact do that here. There *were* changes made to the proposed regulation before it became final--but these changes were far from what the majority describes as "substantially revised" language. A change from a donee's entitlement to extinguishment proceeds that have an FMV that is "a minimum ascertainable proportion of the fair market value to the entire property," 48 Fed. Reg. 22946 (May 23, 1983), to "at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time," 51 Fed. Reg. 1496, 1505 (Jan. 14, 1986), has no obvious explanation other than to increase editorial clarity. And the second change that the Commissioner and majority point to--going from "original proportionate value" to "that proportionate value"--seems entirely editorial. The majority implies that these changes are substantial, yet one would be hard pressed to think of any set of facts in which the changed language would change the outcome in any particular case.

The Supreme Court in *Encino Motorcars,* 579 U.S. at ___, 136 S. Ct. at 2126, invalidated a regulation from an agency that offered "barely any explanation." Here we have none. We should, therefore, hold that Treasury's failure to respond to significant comments in the Final Rule's statement of basis and purpose violated APA section 553(c). That is reason enough to hold section 1.170A-14(g)(6)(ii), Income Tax Regs., invalid under APA section 706(2)(D). To do otherwise would be to hold that "the opportunity to comment is meaningless." *Home Box Office,* 567 F.2d at 35.

III.

There's another problem with our opinion. Even if this regulation were to be procedurally valid, it might well be substantively invalid. Oakbrook argued in its original posttrial briefs that we should use the *Chevron* two-step.[20] The Commissioner agreed, and the majority tags along. *See* op. Ct. p. 26.

Under this familiar standard, courts defer to an agency's reasonable construction of an ambiguous statute that Congress has tasked the agency with administering. *Chevron,* 467 U.S. at 843-44. At the first step, courts employ "traditional tools of statutory construction" to determine whether "Congress has directly spoken to the precise question at issue." *Id.* at 842, 843

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[20] After the Fifth Circuit's decision in *PBBM-Rose Hill,* 900 F.3d 193, and the realization that this case was the first to challenge the regulation's validity, we ordered production of the administrative record of the regulation's origin and gave the parties the opportunity to file another round of briefs to make any arguments on the regulation's validity that they wanted to preserve.

n.9. If it has, the statute is unambiguous, and we apply it as written; for "that is the end of the matter." *Id.* at 842. But "if the statute is silent or ambiguous with respect to the specific issue," we move to the second step, which asks "whether the agency's answer is based on a permissible construction of the statute." *Id.* at 843. Where "Congress has explicitly left a gap for the agency to fill" by regulation, we defer to the agency's construction unless it is "arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 843-44. As a trial court, it's not up to us to challenge the *Chevron* standard, but the majority should have at least acknowledged that there are contrary positions about whether *Chevron* supplies the only standard of review.

This is especially true because Oakbrook now also relies on *State Farm.* In that case, the Supreme Court was asked to determine whether an agency's decision to rescind a regulation was arbitrary and capricious. *State Farm,* 463 U.S. at 34. In holding that it was, the Court established four factors that courts might consider in determining whether an agency action is deficient, and stated:

> Normally, an agency rule would be arbitrary and capricious if the agency has [(1)] relied on factors which Congress has not intended it to consider, [(2)] entirely failed to consider an important aspect of the problem, [(3)] offered an explanation for its decision that runs counter to the evidence before the agency, or [(4)] is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.

Id. at 43.

So how do we review the substantive agency action? Well, the relationship between *State Farm* and *Chevron* is less than clear right now.[21] *State Farm* is still the go-to standard for challenges to a regulation's validity on the ground that it is arbitrary and capricious under the APA, while *Chevron* (particularly step two) is principally used for challenges to a regulation's validity on the ground that it is unreasonable. In recent years the line between *State Farm* and *Chevron* step two has blurred. *See Judulang v. Holder,* 565 U.S. 42, 52 n.7 (2011) ("[The] analysis would be the same, because under *Chevron* step two, we ask whether an agency interpretation is 'arbitrary or capricious in substance"). In a case appealed to the Ninth Circuit, we ourselves held that "regardless of the ultimate standard of review--the final rule must satisfy *State Farm's* reasoned decisionmaking standard." *Altera Corp. v. Commissioner,* 145 T.C. 91, 117 (2015), *rev'd,* 926 F.3d 1061 (9th Cir. 2018), *petition for hearing en banc denied,* 941 F.3d 1200 (9th Cir. 2019), *petition for cert. filed* No. 19-1009 (Feb. 13, 2020).

But not all courts agree. The Second Circuit, for example, held that the district court's application of the *State Farm* standard at *Chevron* step two was reversible error: "While we have great respect for the district court's careful and searching analysis * * *, we

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[21] One thing we do know is that courts analyze the validity of regulations under *State Farm* even where the regulation does not "reverse[] an earlier policy supported by a body of fact." *Compare* op. Ct. p. 19 n.2, *with Fed. Energy Regulatory Comm'n v. Elec. Power Supply Assoc.,* 577 U.S. ___, ___, 136 S. Ct. 760, 771-72, 782-84 (2016) (*State Farm* review of a regulation that didn't reverse policy); *Bowen v. Am. Hosp. Ass'n,* 476 U.S. 610, 613-17, 626-42 (1986) (same); *Atrium Med. Ctr. v. HHS,* 766 F.3d 560, 567 (6th Cir. 2014) (same); *and All. for Comty. Media v. FCC,* 529 F.3d 763, 769, 786-87 (6th Cir. 2008) (same).

conclude that it erred by incorporating the *State Farm* standard into its *Chevron* Step Two analysis and thereby applying too strict a standard of review." *Catskill Mountains Chapter of Trout Unitd., Inc. v. EPA,* 846 F.3d 492, 521 (2d Cir. 2017). A brief survey of the other circuits since *Judulang* shows just how unsettled this question remains:

- *Craker v. DEA,* 714 F.3d 17, 26 (1st Cir. 2013) (even if agency's statutory interpretation satisfies *Chevron,* it may still be set aside as arbitrary and capricious under *State Farm*);
- *Almy v. Sebelius,* 679 F.3d 297, 302 (4th Cir. 2012) (*Chevron* operates "[i]n addition to" *State Farm*);
- *Sw. Elec. Power Co. v. EPA,* 920 F.3d 999, 1028 (5th Cir. 2019) *(Chevron* step two and the APA share the arbitrary and capricious standard and the analysis under the two standards proceeds similarly) (citing Richard J. Pierce, Jr., Administrative Law Treatise, sec. 3.6 (5th ed. 2010) (suggesting that *Chevron* step two has "complete overlap" with the APA and *State Farm* if rule challenged as "unreasonable"));
- *Abraham Lincoln Mem'l Hosp. v. Sebelius,* 698 F.3d 536, 547 (7th Cir. 2012) (suggesting a distinction between arbitrary-and-capricious review under *State Farm* and *Chevron* step two);
- *Altera,* 926 F.3d at 1075-76 (adopting Second Circuit analysis of *Catskill Mountain); but see Turtle Island Restoration Network v. United States Dep't of Commerce,* 878 F.3d 725, 732-33 (9th Cir. 2017) *(Chevron* step two equivalent to the *State Farm* arbitrary-and-capricious review);

- *Nutraceutical Corp. v. Von Eschenbach,* 459 F.3d 1033, 1037-38 (10th Cir. 2006) (suggesting overlap between *State Farm's* arbitrary and capricious standard and *Chevron* step two); *see also Gutierrez-Brizuela v. Lynch,* 834 F.3d 1142, 1149-58 (10th Cir. 2016) (Gorsuch, J., concurring) (questioning the constitutionality of *Chevron*);
- *Nat'l Mining Ass'n v. Sec'y, U.S. Dep't of Labor,* 812 F.3d 843, 865 n.23 (11th Cir. 2016) (*Chevron* step two functionally equivalent to arbitrary and capricious review under the *State Farm*);
- *Sorenson Commc'ns, LLC v. FCC,* 897 F.3d 214, 230 (D.C. Cir. 2018) (identifying significant overlap between *Chevron* step two and *State Farm*); and
- *Balestra v. United States,* 803 F.3d 1363, 1368 n.2 (Fed. Cir. 2015) *(State Farm* often overlaps with analysis under *Chevron* step two, but the two standards should be applied separately).[22]

Because this case is appealable, absent stipulation to the contrary, to the Sixth Circuit, I would follow its approach. *See Golsen v. Commissioner,* 54 T.C. 742, 756 (1970), *aff'd*, 445 F.2d 985 (10th Cir. 1971). That approach is to analyze challenges to a regulation under *Chevron* step two and *State Farm* independently. *See Atrium Med. Ctr.,* 766 F.3d at 567 ("Even if an agency's statutory interpretation is permissible under *Chevron* * * *, the agency's action may still be 'arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.' (quoting APA sec. 706(2)(A))); *see also Nat'l Truck Equip. Ass'n*

[22] The Third and Eighth Circuits seem not to have considered this question.

v. Nat'l Highway Traffic Safety Admin., 711 F.3d 662, 668-69 (6th Cir. 2013).

The goal of review under either APA section 706(2)(A) or (D), and under *Chevron* or *State Farm* is to ensure that an agency engages in reasoned decisionmaking. According to the Sixth Circuit, "[a]t base, arbitrary and capricious review functions to 'ensur[e] that agencies have engaged in *reasoned decisionmaking.*'" *Atrium Med. Ctr.,* 766 F.3d at 567 (emphasis added) (quoting *Judulang,* 565 U.S. at 53). Reasoned decisionmaking means that the agency "examine[s] the relevant data and articulate[s] a satisfactory explanation for its action including a rational connection between the facts found and the choice made." *State Farm,* 463 U.S. at 43 (internal quotation marks omitted); *see also* APA sec. 553(c).

Oakbrook argues that the regulation is arbitrary and capricious under the APA and the *State Farm* standard, and the Commissioner just as plainly defends the regulation as reasoned decisionmaking. The majority today doesn't even address this argument; it should have. And following the Sixth Circuit's lead, we should run this regulation not only through *Chevron* but through *State Farm* too.

As to how this regulation fares under *Chevron,* I agree with the majority that "perpetuity" allows for a wide range of possible interpretations; it certainly doesn't by itself show Congress spoke on the issue of preserving the conservation purposes of a donated easement that has been extinguished or condemned. That's enough to skip past step one.

The problem is with step two, and it affects both the "proportionate value" and "donee improvements" parts of the challenged regulation. The majority finds the regulation reasonable in requiring a proportionate split of the proceeds from an easement's extinguishment because "considerable inflation in property values might occur in the interim." *See* op. Ct. p. 28. It similarly finds the regulation's ban on reducing the donee's share of proceeds to account for improvements reasonable because "[i]n certain factual scenarios, reducing the donee's proceeds on account of donor improvements could frustrate this goal, especially if local land values should decline." *See id.* p. 29.

These seem like perfectly plausible reasons. But they are not the ones that Treasury itself offered at the time it issued the regulation. This raises another problem for the Commissioner in his defense--the *Chenery* rule. The *Chenery* rule prevents an agency from relying on *post hoc* rationalizations to defend its decisionmaking. *SEC v. Chenery Corp.,* 318 U.S. 80, 87 (1943) ("The grounds upon which an administrative order must be judged are those upon which the record discloses that its action was based."); *see also State Farm,* 463 U.S. at 50 (courts may not accept post hoc rationalizations). And *Chevron* step 2 is limited by *Chenery*. *Bank of Am., N.A. v. FDIC,* 244 F.3d 1309, 1319 (11th Cir. 2001) (stating that *Chenery* must be considered at step 2 of *Chevron*); *see also Council for Urological Interests v. Burwell,* 790 F.3d 212, 222 (D.C. Cir. 2015); *America's Cmty. Bankers v. FDIC,* 200 F.3d 822, 835 (D.C. Cir. 2000). We shouldn't be coming up with our own *post hoc* justifications for the reasonableness of the rule if the Commissioner's lawyers wouldn't be able to.

The same problem affects our analysis of the substantive validity of this regulation under *State Farm.* The Sixth Circuit has warned agencies that its arguments in favor of a regulation not being "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" is likewise limited by the *Chenery* rule. *See Atrium,* 766 F.3d at 567-68 ("[T]he ground upon which an administrative order must be judged are those upon which the record discloses that its action was based." (quoting *Chenery,* 318 U.S. at 87)).

The majority today comes up with as good a set of arguments as possible to justify the reasonableness of the regulatory choices that Treasury made when it was drafting this regulation. But Treasury didn't make them. Or at least it didn't make them in the administrative record of this regulation.

IV.

I will end with where I began in today's Memorandum Opinion on the less controversial parts of this case: Conservation-easement cases might have been more reasonably resolved case-by-case in contests of valuation. The syndicated conservation-easement deals with wildly inflated deductions on land bought at much lower prices would seem perfectly fine fodder for feeding into a valuation grinder. Valuation law is reasonably well known, and valuation cases are exceptionally capable of settlement.

Congress, however, enacted these sections of the Code and presumably wanted reasonably valued conservation easements to be allowed. Yet we've come to a point where we are disallowing a great many conservation-easement deductions altogether, not for exaggeration of their value or lack of conservation purpose, but because of very contestable readings of what it means for an easement to be perpetual. We did defuse the Commissioner's thermonuclear-bomb of an argument that the retained power of parties to any contract to modify its terms meant that no easement anywhere at any time could ever preserve its conservation purpose "in perpetuity." *Pine Mountain,* 151 T.C. at 280-82. But our agreement with the Commissioner in *Pine Mountain* last year that a reserved right to build a home on property subject to an easement is defeated if its location is not precisely defined will lead, at best, to a circuit conflict that the Supreme Court will have to resolve.[23]

Today we uphold a regulation that will invalidate who knows how many other conservation-easement deductions, and will almost certainly lead to appeals in multiple circuits. If the Commissioner continues to seek gross-misvaluation penalties, we will also have to figure out in a great many cases how to determine which portion of an underpayment is attributable to a valuation misstatement and which is due to a failure of the conservation easement altogether, when it

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[23] One can even foresee a conflict between the acceptable power to amend and the unacceptable "floating homesite" provision: Imagine the case where a general provision in an easement deed allows for amendments so long as the donee finds that the conservation purpose is preserved, but has no express provision that allows the donor to add improvements except to build a single home in a location fixed with extreme precision by the deed. Years pass, it comes time to build, but in building the donor discovers a sinkhole on the edge of the building area, making it unbuildable. He determines he could avoid the sinkhole by shifting the location of the building area one foot from its original location. With the donee's permission, he amends the deed, as is his right under the general amendment provision, to shift the boundary of the building area. Why this deduction would be allowable, while another in which a deed of easement expressly permits a donor to shift the location of the building area with the same required permission and preservation of conservation purpose, is not obvious.

might justly be said to be attributable to both. *See PBBM-Rose Hill,* 900 F.3d at 214.

I fear that our efforts to clear cut and brush hog our way out of the volume of conservation-easement cases we have to deal with has left us a field far stumpier than when we began.

I respectfully dissent.

APPENDIX D

T.C. Memo. 2020-54

UNITED STATES TAX COURT

[Filed May 12, 2020]

Docket No. 5444-13.

OAKBROOK LAND HOLDINGS, LLC, WILLIAM DUANE HORTON, TAX MATTERS PARTNER,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

David M. Wooldridge, Michelle A. Levin, Ronald A. Levitt, and *Gregory P. Rhodes,* for petitioner.

W. Benjamin McClendon, Bruce K. Meneely, Robert W. Dillard, and *William W. Kiessling,* for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

HOLMES, *Judge:* In recent years the Commissioner has attacked a popular form of charitable contribution--the donation of conservation easements.[1] Many of these attacks are surgical strikes on what he believes are gross exaggerations of the value of particular easements. But he has also launched three sorties--all predicated on the requirement that such easements be

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[1] *See, e.g.,* I.R.S. News Release IR-2005-129 (Oct. 27, 2005) (referring to certain conservation easements as abusive).

"perpetual"--that he hopes will cause more widespread casualties:

- an attack on the power of donor and donee to change the terms of the easement after its contribution;
- an attack on the retained right of the donor to add improvements to the property described in the easement; and
- an attack on a clause commonly found in easements, particularly in the southeastern part of the country, that divides between donor and donee future hypothetical proceeds from a future hypothetical extinguishment of the easement in a way that he claims violates one of his regulations.

In *Pine Mountain Pres., LLLP v. Commissioner,* 151 T.C. 247, 280-82 (2018), we held that the retained power of all parties to all contracts to change contractual terms does not by itself deprive a deed of easement of its required perpetuity. We also held there that a donor's retained right to add improvements "appurtenant to residential development" does violate the perpetuity requirement as a matter of law when the precise location of those improvements is not set forth in the deed of easement. *Id.* at 275-79.

In this case, the Commissioner seeks to destroy any charitable-contribution deduction for an easement whose deed contains an extinguishment clause that he argues does not meet the requirements of one of his regulations, section 1.170A-14(g)(6)(ii), Income Tax Regs. This case appears to be the first one in which the donor fights back by challenging the validity of that regulation.

What the regulation means and whether it's valid are questions whose answers will affect a great many such donations. There's a difference of opinion in the Court on the question of the regulation's validity; there is not on the factfinding and application of the regulation to those facts.

FINDINGS OF FACT

In 2007 a couple was driving on a country road about fifteen minutes outside Chattanooga in search of the perfect place for a new home. They stopped at a briar-covered for-sale sign on a 143-acre piece of land on White Oak Mountain. The property was significantly larger and considerably more overgrown than what they wanted, but they thought it could be the diamond in the rough for which they had been prospecting.

To understand why requires understanding who the husband in this couple is. Duane Horton grew up in Chattanooga, earned a degree in construction from Georgia Tech, and moved back to his home town. He started his career there in 1998, and in 2002 he formed a construction company. Horton proved to be a talented entrepreneur, and his company grew and became quite successful. In 2007 Horton and a number of his subcontractors, suppliers, and past clients formed a real-estate development company and a real-estate investment fund. The development company excels in "working with larger pieces of property that are * * * usually in high-growth sectors of the area that may have challenges, * * * [such as] lack of infrastructure, access issues, rezoning issues, or topography issues, * * * and solv[ing] those problems and unlock[ing] the potential value of the property." So when Horton drove past the property in 2007, he was uniquely able to see its potential, and he quickly contacted various investors to plan how to buy and develop it.

Horton and these investors formed Oakbrook Land Holdings, LLC in August 2007 and four months later it bought the property for $1,700,000. Oakbrook planned at first to develop the subject property with "higher-end, single-family residences with a commercial service area." But before that vision could be realized, Oakbrook had to overcome a number of thorny obstacles, briars the least among them. It started by building a bridge across the "Hurricane Creek;" this alone created access to more than 80% of the previously inaccessible property. It then installed a high-pressure sewer-pump station and won rezoning of a portion of the property from A-1 Agricultural District to C-2 Local Business and Commercial District.

As 2007 turned into 2008, Horton learned about a conservation easement on an entirely unrelated property in North Georgia. He was intrigued and began to do some research. At some point in 2008 he started to think about placing a conservation easement on the Oakbrook property. He met with James Wright, executive director of the Southeast Regional Land Conservancy, who gave him a short course on the easement process and told him that the Conservancy's lawyers would draft the legal paperwork should Oakbrook want to give it an easement. Horton took what he learned to the other Oakbrook investors who, despite some early opposition, agreed to the idea. Oakbrook's next move was to transfer some of the acreage to related entities in mid-December 2008, which enabled it to be developed without restriction. This left Oakbrook with approximately 106 acres.

Later that month Oakbrook donated a conservation easement on all 106 acres to the Conservancy through a document called "Conservation Easement and Declaration of Restrictions and Covenants" (Deed).

Because of its unfamiliarity with conservation easements, Oakbrook and its members relied heavily on the Conservancy to draft this Deed. We specifically find that Horton, acting on behalf of Oakbrook, was reasonable in inferring that the Conservancy's experience meant that the deeds it had drafted conformed to the Code and regulations.

The Deed's key section for this opinion is Article VI, Section B(2). It governs how Oakbrook and the Conservancy will divide between themselves any proceeds if the easement is extinguished by changed circumstances or condemnation:

> This Conservation Easement gives rise to a real property right and interest immediately vested in [the Conservancy]. For purposes of this Conservation Easement, the fair market value of [the Conservancy]'s right and interest shall be equal to the difference between (a) the fair market value of the Conservation Area as if not burdened by this Conservation Easement and (b) the fair market value of the Conservation Area burdened by this Conservation Easement, as such values are determined as of the date of this Conservation Easement, (c) less amounts for improvements made by O[akbrook] in the Conservation Area subsequent to the date of this Conservation Easement, the amount of which will be determined by the value specified for these improvements in a condemnation award in the event all or part of the Conservation Area is taken in exercise of eminent domain as further described in this Article VI, Section B(3) below. If a change in conditions makes impossible or impractical any continued

> protection of the Conservation Area for conservation purposes, the restrictions contained herein may only be extinguished by judicial proceeding. Upon such proceeding, [the Conservancy], upon a subsequent sale, exchange or involuntary conversion of the Conservation Area, shall be entitled to a portion of the proceeds equal to the fair market value of the Conservation Easement as provided above. [The Conservancy] shall use its share of the proceeds in a manner consistent with the conservation purposes set forth in the Recitals herein.

Article VI, Section B(3) goes on to state:

> Whenever all or part of the Conservation Area is taken in exercise of eminent domain * * * so as to abrogate the restrictions imposed by this Conservation Easement, * * * [the] proceeds shall be divided in accordance with the proportionate value of [the Conservancy]'s and O[akbrook]'s interests as specified above; all expenses including attorneys fees incurred by O[akbrook] and [the Conservancy] in this action shall be paid out of the recovered proceeds to the extent not paid by the condemning authority.

According to Wright, the above language is standard among the Conservancy's conservation easements. And although he couldn't say with absolute certainty, Wright was "pretty sure" the language was adopted from numerous other model agreements, including those produced by the Land Trust Alliance.[2]

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[2] Wright suggested that the Conservancy has 85 easements with similar language. According to *amici* in another case,

Wright explained that, as with the regulation, this extinguishment clause starts by defining the fair market value (FMV) of the easement as the difference between the property's value without the easement and the property's value with the easement. Wright stressed that he viewed this language as securing a fixed amount for the Conservancy. He explained that the Conservancy expected that Oakbrook would exercise its right to improve the property within the limits set by the Deed, but did not think it right for the Conservancy to share in any condemnation award or extinguishment proceeds attributable to any improvements: The Conservancy, Wright credibly testified, "did not pay for those improvements" and shouldn't have a "property interest in those improvements." He also had a view on what the regulation required: "[R]ather than having a proportion * * * -- the Treasury regulation requires at a minimum that a proportion -- * * * our language establishes fair value a[s] an absolute -- it's not a proportion; therefore, it is [al]ways going to exceed * * * the minimum required by the IRS."

While Oakbrook worked toward closing on the easement, it also started to look for an appraiser to value the conservation easement for purposes of claiming a charitable deduction. Oakbrook picked Dave Roberts, who valued the easement at $9,545,000. This is the amount Oakbrook claimed on its Form

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however, there is reason to believe thousands of conservation easements have similar language. Brief for Land Trust Alliance, Inc. et al. as Amici Curiae Supporting Petitioners at 6, *PBBM-Rose Hill, Ltd. v. Commissioner,* 900 F.3d 193 (5th Cir. 2018) (No. 17-60276).

1065, U.S. Return of Partnership Income, as a charitable contribution.[3]

To prepare its 2008 return Oakbrook hired Henderson Hutcherson & McCullough, PLLC (HHM), an accounting firm familiar with Oakbrook and the requirements for conservation-easement deductions. Horton was unfamiliar with conservation easements and under intense scrutiny by Oakbrook's investors, so he discussed Oakbrook's 2008 tax return with HHM multiple times. This assured him that the easement deduction was proper.

HHM's assurance did not extend to the Commissioner, who timely issued an FPAA[4] to Oakbrook for its 2008 tax year. In it, the Commissioner completely disallowed Oakbrook's charitable contribution and asserted an accuracy-related penalty under section 6662 for negligence, disregard of regulations, or substantial

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[3] Roberts initially valued the easement at approximately $19,500,000. Horton asked for a second appraisal because "a number of consultants and investors * * * didn't feel comfortable with that high of a value."

[4] FPAAs are notices of final partnership administrative adjustment. Before its repeal, *see* Bipartisan Budget Act of 2015, Pub. L. No. 114-74, sec. 1101(a), 129 Stat. at 625, part of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. No. 97-248, secs. 401-407, 96 Stat. at 648-71, governed the tax treatment and audit procedures for certain partnerships. TEFRA partnerships are subject to special tax and audit rules. *See* secs. 6221-6234. When the IRS audits a TEFRA partnership return and determines an adjustment is necessary, it sends the partnership an FPAA. The FPAA describes all the proposed changes at the partnership level. TEFRA partnerships designate a partner to act as the tax matters partner to deal with the IRS. Sec. 6231(a)(7). (Unless otherwise indicated, all section references are to the Internal Revenue Code in effect at all relevant times.)

understatement. Oakbrook timely petitioned this Court, and we tried the case in Birmingham, Alabama.[5]

The Code requires a conservation easement to be "perpetual". Sec. 170(h)(2)(C), (5)(A). The Commissioner disallowed Oakbrook's deduction in part because he concluded that the Deed's extinguishment clause would split the proceeds from the property's condemnation or the easement's termination in a way that failed to protect the contribution's conservation purpose in perpetuity. *See* sec. 170(h)(1)(C), (5)(A). He points to section 1.170A-14(g)(6)(ii), Income Tax Regs.--part of a bigger set of regulations that more comprehensively fences in the Code's perpetuity requirement. The problem these regulations try to solve stems from the fact that perpetuity can be a very long time: What happens if a local government condemns part of the property for a road, or a local power authority floods the property as part of a hydropower project, or anything else happens to the property that would destroy its conservation purpose? Under common law such events can "extinguish" the easement; the Commissioner's regulation is meant to regulate the division of any compensation for this extinguishment between the donor and donee so that the donee can continue to pursue the easement's conservation purpose elsewhere and into the future.

The Commissioner attacks the Deed's extinguishment clause with two related arguments. The first is that the clause's formula to distribute extinguishment proceeds doesn't correctly track the regulation, because it would distribute to the Conservancy a fixed amount,

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[5] Oakbrook's principal place of business was in Chattanooga, Tennessee, at the time the petition was filed. This case is therefore appealable to the Sixth Circuit. *See* sec. 7482(b)(1)(E).

and not a proportion, of any such proceeds. The second is that the clause would subtract from those proceeds the value of improvements that Oakbrook could make after the donation. Oakbrook responds that the extinguishment clause complies with the regulation but, if it does not, the regulation is invalid.[6]

OPINION

I. *Qualified Conservation Contributions*

Conservation easements are supposed to preserve properties with natural, historical, or cultural significance through perpetual restrictions on their use. They also allow donors to take charitable deductions, some of which can be quite sizable.

The popularity of conservation easements has risen dramatically in recent years. The National Conservation Easement Database (NCED) has cataloged 167,721 conservation easements in effect throughout the United States, which affect more than 27,700,000 acres of land. Nat'l Conservation Easement Database, https://www.conservationeasement.us (last visited February 5, 2020).[7] The number of acres conserved under easement is up from the nearly 16,800,000 in 2015,

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[6] 6 In his brief the Commissioner also claimed that Oakbrook is liable for a gross-valuation misstatement penalty under section 6662(h), a substantial-valuation misstatement penalty under section 6662(e), or in the alternative, a substantial-understatement-of-tax penalty under section 6662(d). He has since conceded that these penalties do not apply.

[7] Even the NCED, which provides the most complete up-to-date census data, admits that its numbers are significantly understated. The NCED estimates that it lists only 49% of publicly held easements and 90% of non-profit-held easements across the United States. *Completeness,* Nat'l Conservation Easement Database, https://www.conservationeasement.us/completeness (last visited May 11, 2020).

13,200,000 in 2010, and 6,100,000 in 2005. Land Trust Alliance, 2015 *National Land Trust Census Report,* http://s3.amazonaws.com/landtrustalliance.org/2015 NationalLandTrustCensusReport.pdf.

As the popularity of conservation easements has increased, so too have the Commissioner's suspicions about them. *See, e.g., PBBM-Rose Hill, Ltd. v. Commissioner,* 900 F.3d 193 (5th Cir. 2018); *BC Ranch II, L.P. v. Commissioner, 8*67 F.3d 547 (5th Cir. 2017), *vacating and remanding* T.C. Memo. 2015-130; *Belk v. Commissioner,* 774 F.3d 221 (4th Cir. 2014), *aff'g* 140 T.C. 1 (2013); *Glass v. Commissioner,* 471 F.3d 698 (6th Cir. 2006), *aff'g* 124 T.C. 258 (2005); *Pine Mountain,* 151 T.C. 247. In December 2016 the Commissioner released a notice in which he characterized syndicated conservation-easement transactions[8] as potential "tax avoidance transactions," and then proceeded to include syndicated conservation easements as his newest addition to the list of 35 other "Recognized Abusive and Listed Transactions." *See* I.R.S. Notice 2017-10, 2017-4 I.R.B. 544; *Recognized Abusive and Listed Transactions,* Internal Revenue Serv., https://www.irs.gov/businesses/corporations/listed-transactions (last updated Jan. 31, 2020).

The Code, however, makes at least some conservation easements legitimate, even though section 170(f)(3)(A) generally disallows a charitable-contribution deduction for any gift of real property that "consists of less than

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[8] Syndicated conservation easements are transactions in which "a promoter offers prospective investors in a partnership or other pass-through entity ('pass-through entity') the possibility of a charitable contribution deduction for donation of a conservation easement." I.R.S. Notice 2017-10, 2017-4 I.R.B. 544, 545. The easement at issue in this case is not a syndicated conservation easement.

the * * * entire interest in such property." The key is for a donor to meet the unusually complicated rules for a donation of a "qualified conservation contribution." Sec. 170(f)(3)(B)(iii). A "qualified conservation contribution" is "a contribution--(A) of a qualified real property interest, (B) to a qualified organization, (C) exclusively for conservation purposes." Sec. 170(h)(1). Although a contribution must satisfy each of these requirements, our focus in this opinion is on the third requirement--that the contribution be "exclusively for conservation purposes," sec. 170(h)(1)(C), which the Code defines in the negative: "A contribution shall not be treated as exclusively for conservation purposes unless the conservation purpose is *protected in perpetuity,"* sec. 170(h)(5)(A) (emphasis added).

We begin with a bit of a refresher on the common law of servitudes. A servitude is "a legal device that creates a right or an obligation that runs with land or an interest in land." 1 Restatement, Property 3d (Servitudes), sec. 1.1(1) (2000). It can be granted either appurtenant--meaning "the rights or obligations of a servitude are tied to ownership or occupancy of a particular unit or parcel of land," *id.* sec. 1.5(1), or in gross--meaning "the benefit or burden of a servitude is not tied to ownership or occupancy of a particular unit or parcel of land," *id*. sec. 1.5(2). Easements, a form of servitude, may also be appurtenant or in gross, but because "most conservation and preservation servitudes are granted to governmental bodies, land trusts, or other charitable entities * * * , the benefit will usually be in gross." *Id.* sec. 1.6 cmt. a.

States were wary of simply applying traditional servitude law to conservation easements. Servitudes, like other contracts, are usually between private parties, and situations may arise where the parties no longer want to enforce the restriction or the restriction's continued enforcement becomes unjust. Imagine, for example, a homeowners association (HOA) whose members agree to build ranch-style homes to preserve their views of a nearby mountain, only to have an office building that blocks those views appear on a lot between the HOA homes and the mountain. A disgruntled homeowner might sue his HOA and urge that this change in condition should terminate the restriction. *See* 2 Restatement, *supra,* sec. 7.10. Termination of a servitude for changed conditions benefits all the property owners that used to be bound by it, so the common law seldom requires any money damages when one is extinguished. *Id.* sec. 7.11 cmt. c.

That general rule of implicit compensation for the loss of a servitude wouldn't work with conservation easements. And neither would the general power of parties to servitudes, like parties to every other contract, to change their terms. *See id.* sec. 7.1. Conservation easements are usually clothed with assertions of a significant public interest, not only because their enforcement preserves valuable land for public benefit, but also because "their creation is subsidized indirectly by tax deductions and directly through purchases by public agencies and nonprofit corporations." *Id.* sec. 7.11 cmt. a. Permitting an unrestricted right to modify a conservation easement, or terminate one altogether, could result in a loss of the public's investment.

Applying the common-law rule--extinguishment without cash compensation--could also lead to unusual results. A landowner with a black heart could place a conservation easement on his property, take the associated deduction, and then pave paradise and put up a parking lot on adjoining property. He might prove that the easement's conservation purpose was destroyed and should no longer restrict development of the subject property, and then sell the now-unburdened land. *See id.* cmt. d. The common-law rule of only implicit compensation for termination of an easement could embolden landowners (imagine well-financed developers) to use the threat of protracted changed-conditions litigation to coerce donees (imagine thinly staffed nonprofit organizations) into modifying or terminating their easements. *Id.* The cynic, or even just the realist, can also foresee some probability of collusion between donors and donees of conservation easements if conservation easements could create benefits with both their formation and their destruction.

As conservation easements became popular, states enacted statutes to change this feature of common law. Tennessee is among them. *See* Tenn. Code Ann. sec. 66-9-306 (West 2020) (conservation easement valid even if no privity of estate or contract or no benefit to any other land, and "[n]o conservation easement shall be held automatically extinguished because of violation of its terms or frustration of its purposes"). These state-law changes help make conservation easements perpetual, but the mix of statute, regulation, and caselaw that defines what "perpetual" means can be confusing and might undermine a great many conservation deeds of easement for reasons their drafters never expected.

One part of the solution is to limit the ability of donors and donees to declare "changed circumstances" all by themselves. Conservation easements typically have clauses, like the one here between Oakbrook and the Conservancy, that provide "[i]f a change in conditions makes impossible or impractical any continued protection of the Conservation Area for conservation purposes, the restrictions contained herein may only be extinguished by judicial proceeding." Deed, Article VI, Section B(2). Getting a judge involved means there will be a third party to monitor whether conditions really have changed.

But there's a special problem with what happens to an easement that simply cannot be preserved forever. If a conserved building is obliterated in a disaster, or a conserved open space is condemned for public use, then insurance money or a condemnation award may be substituted for the property. The original easement is no more, but how can money preserve the easement's conservation purpose "in perpetuity?" In this situation the law causes the conservation purpose to jump into the money into which the easement has been converted. If part of that money goes to the easement holder, the conservation purpose is considered to have survived. That's in the Deed here, too, in the section that says the Conservancy "shall be entitled to a portion of the proceeds equal to the fair market value of the Conservation Easement as provided above." *Id.*

Then there's the particular problem that arises when the donor reserves the right to build various structures on the conservation area. For example, if the donor reserves and subsequently exercises his right to build a home on the land, and the entire property is later condemned, the condemnation award will necessarily include that added value. But is it the donor or the donee who is entitled to the proceeds attributable to the value of the home?

The Code doesn't answer these questions--it just says that the conservation purpose of a conservation easement must be preserved "in perpetuity." Sec. 170(h)(5)(A). But the Treasury Department issued a regulation that more precisely defines the term. There we find that a conservation purpose is not perpetual if the donee organization that holds the easement is unable to carry on the conservation purpose following judicial extinguishment. *See* sec. 1.170A-14(g)(6)(i), Income Tax Regs. To avoid this, the regulation provides that if

> a subsequent unexpected change in the conditions surrounding the property * * * make[s] impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's *proceeds* (determined under paragraph (g)(6)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

Id. (emphasis added).

But just how much of the "proceeds" must the donee receive upon extinguishment, either by judicial decree of changed circumstances or by condemnation? For that answer, we look to paragraph (g)(6)(ii), which reads:

> at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a *property right,* immediately vested in the donee organization, with a *fair market value that is at least equal to the proportionate value* that the perpetual conservation restriction at the time of the gift, bears to the value of the property

> as a whole at that time. *See* § 1.170A-14(h)(3)(iii) relating to the allocation of basis. * * * [T]hat *proportionate value* of the donee's property rights *shall remain constant.* Accordingly, when a change in conditions gives rise to the extinguishment of a perpetual conservation restriction * * * the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, *must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction,* unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

Id. subdiv. (ii) (emphases added).

It is the meaning and application of this regulation that the parties dispute.

II. *Application of the Regulation*

Both the regulation and the relevant section of the Deed are densely written, and the parties disagree about what they mean. We therefore need to

- interpret the regulation,
- construe the Deed's extinguishment clause, and
- analyze whether the extinguishment clause meets the requirements of the regulation.

A. *Interpreting the Regulation*

Our first chore is to analyze what this regulation means. We have already done this in *Coal Property Holdings, LLC v. Commissioner,* 153 T.C. 126 (2019). We held there that the regulation requires the grantee's proportionate share upon extinguishment of a conservation easement to be a percentage determined by a fraction, the numerator of which is "the fair market value of the conservation easement on the date of the gift," and the denominator of which is "the fair market value of the property as a whole on the date of the gift." *Id.* at 137 (quoting *Carroll v. Commissioner,* 146 T.C. 196, 216 (2016)).

We issued *Coal Properties* while deliberating on this case, and Oakbrook makes arguments here that Coal Properties didn't, so we'll briefly review them. Oakbrook points out that the regulation doesn't say proportionate share but proportionate "value"--which it contends means a "fixed value," i.e., a *whole number,* and not a fraction at all. And a whole number that as of the donation date is equal to the difference between the FMV of the property before and after the easement goes into effect. This reading, Oakbrook contends, means that upon extinguishment the Conservancy must be entitled to at least that fixed value. And because the regulation requires that the value be fixed *as of the donation date,* the donee is not entitled to any proceeds attributable to the value of postdonation improvements. The Commissioner tells us that it is the donee's *property right* that must at least equal the "proportionate value" of the restriction to the FMV of the property as a whole. That would be similar to a fractional interest in the property and would mean that the donee would be entitled to any extinguishment proceeds multiplied by that fraction.

Oakbrook tells us that the donee's property right must have *afair market value* that must at least equal the "proportionate value" of the restriction to the FMV of the property as a whole. If Oakbrook is right, then the only reason to figure out the proportion of the FMV of the easement to the value of the property as a whole is to make a one-time calculation as of the date of the easement to fix the amount that the Conservancy would be entitled to upon any future condemnation or extinguishment.

We noted in *Coal Properties* that there has also been one circuit court that's looked at the problem. *See PBBM-Rose Hill,* 900 F.3d at 205-07. That court found the regulation ambiguous, and observed that if "proportionate value" modifies "property right," it equals a fraction, but if it modifies "fair market value," it equals "the dollar amount of the value of the conservation easement at the time of the gift." *Id.* at 206.

Notice that both these conflicting readings require tinkering with the actual language of the regulation. The Commissioner would be happier with a regulation that said "proportionate share" instead of "proportionate value," and Oakbrook would be happier with a regulation that deleted the word "proportionate" from the phrase "proportionate value." It argues that we should hold that an easement's conservation purpose would be protected in perpetuity so long as the FMV of a donee's property interest equals the value of the perpetual conservation restriction at the time of the gift. But "proportionate" isn't the only part of the regulation that Oakbrook's reading would have us cut out--it would also force us to excise the rest of the key sentence--"bears to the value of the property as a whole at that time." Sec. 1.170A-14(g)(6)(ii), Income Tax Regs. This reading would have us allocate proceeds through the use of subtraction, not multiplication. Treasury's regulation writers, however, know how to command subtraction. *See*, *e.g.,* sec. 1.422-1(a)(2)(ii), Income Tax Regs. ("[C]apital gain or loss must be recognized * * * to the extent of the *difference* between the amount realized from such transfer and the adjusted basis of such share" (emphasis added)). And reading "proportionate" out of "proportionate value"--much less effectively excising an entire chunk of a sentence of the regulation--runs afoul of the traditional rule that courts should attempt to give meaning to every word of a regulation. *See Rosenberg v. XM Ventures,* 274 F.3d 137, 141-42 (3d Cir. 2001).

The Commissioner's edit--rewrite "proportionate value" to mean "proportionate share"--is much lighter than Oakbrook's. But it is still a gloss and not a plain reading. The Fifth Circuit took a lengthy look at these conflicting interpretations, and concluded that the regulation was ambiguous. *PBBM-Rose H*ill, 900 F.3d at 205-07. Ambiguity then meant that the court felt free to range outside the regulation to construe it. *Id.* at 206. It was particularly careful to observe that when a regulation is ambiguous, courts should defer to the agency that issued it. *Id.* at 206-07 (deferring to the Commissioner's interpretation "[b]ecause the extinguishment regulation is ambiguous" and citing Tex. *Clinical Labs, Inc. v. Sebelius,* 612 F.3d 771, 777 (5th Cir. 2010)).

It relied, in other words, on Auer deference. *See Auer v. Robbins,* 519 U.S. 452, 461 (1997). Where a regulation is ambiguous, Auer tells us to give the agency's "interpretation 'controlling' weight unless it is 'plainly erroneous or inconsistent with the regulation.'" *Ohio Dep't of Medicaid v. Price,* 864 F.3d 469, 477 (6th Cir. 2017) (quoting Auer, 519 U.S. at 461). We didn't have occasion to mention the possible problems of the Fifth Circuit's reliance on Auer deference when we looked at the problem in *Coal Properties.* But, like the Fifth Circuit, we found some comfort in the consistency of the Commissioner's interpretation over many years, as one can see in numerous private letter rulings (PLRs) issued as far back as 1999. *See* Priv. Ltr. Ruls. 200836014 (Sept. 5, 2008), 200403044 (Jan. 16, 2004), 200208019 (Feb. 22, 2002), 199933029 (Aug. 20, 1999).[9]

The Supreme Court recently reaffirmed Auer. *Kisor v. Wilkie,* 588 U.S. ___, 139 S. Ct. 2400 (2019). But in doing so it restated the principles of that deference:

- *Auer* deference doesn't apply unless a regulation is genuinely ambiguous after exhausting "all the 'traditional tools' of construction." *Kisor,* 588 U.S. at ___, 139 S. Ct. at 2415 (quoting *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 4*67 U.S. 837, 843 n.9 (1984));
- the agency's reading of an ambiguous regulation must still itself be reasonable, *id.;*
- the reading of an ambiguous regulation must also "be one actually made by the agency," its authoritative or official position and not one that is *ad hoc, id.* at ___, 139 S. Ct. at 2416;
- the agency's reading must in some way "implicate its substantive expertise," *id.* at ___, 139 S. Ct. at 2417; and
- the reading "must reflect 'fair and considered judgment', *id.* (quoting *Christopher v. SmithKline Beecham Corp.,* 567 U.S. 142, 155 (2012)).

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[9] Of course PLRs aren't binding on parties, save for the party to whom one is issued, see sec. 6110(k)(3), but "they may be cited as evidence of administrative interpretation," *Comerica Bank, N.A. v. United States,* 93 F.3d 225, 230 (6th Cir. 1996) (citing *Phi Delta Theta Fraternity v. Commissioner,* 887 F.2d 1302 (6th Cir. 1989), *affg* 90 T.C. 1033 (1988)).

In construing this regulation, we see no need to rely on *Auer* deference because the "traditional tools of construction" lead us to hold that the Commissioner's construction of the regulation is correct even if we look at the question *de novo*. We can add to our plain-language analysis in *Coal Properties* a couple additional points. Notice the command in the middle of the regulation to "[s]ee [sec.] 1.170A-14(h)(3)(iii)[, Income Tax Regs.,] relating to the allocation of basis." Sec. 1.170A-14(g)(6)(ii), Income Tax Regs. That regulation tells us that "[t]he amount of the basis that is allocable to the qualified real property interest shall bear the same *ratio* to the total basis of the property as the [FMV] of the qualified real property interest *bears to* the [FMV] of the property before the granting of the qualified real property interest." *Id.* para. (h)(3)(iii) (emphasis added). This language is clear. It establishes a "ratio", which is "the quotient of one quantity divided by another of the same kind, usually expressed as a fraction." Webster's New World College Dictionary 1206 (5th ed. 2016). And it tells us that the fraction's numerator is the FMV of the easement, and its denominator is the FMV of the property unburdened by the easement--effectively the same fraction that the Commissioner contends is meant by "proportionate value." What's more, to set up the numerator and the denominator for this fraction, it uses the words "bears to," which are the same words used in section 1.170A-14(g)(6)(ii), Income Tax Regs., when defining "proportionate value." This buttresses our holding that "proportionate value" means a fraction and not a whole number.

We also observe that this is what "proportionate value" seems to mean elsewhere in the U.S. Code and in other regulations. For example, the U.S. Code section that apportions federal funds among the states for animal health and disease research programs, provides:

> 48 percent [of federal funds] shall be distributed among the several States in the *proportion* that the value of and income to producers * * * in each State *bears to* the total value of and income to producers * * * in all the States. The Secretary shall determine the total value of and income * * * in all the States and the *proportionate value* of and income * * * for each State * * * .

7 U.S.C. sec. 3195(c)(4)(B) (emphasis added). This directs the Secretary of Agriculture to establish a "proportion" for each state equal to the value produced by each state divided by, or which "bears to," the value produced in all states. *See id.* The next sentence then refers to this "proportion" as "the proportionate value * * * for each State." *Id.* That's a fraction.

The phrase "proportionate value" also pops up in two other Treasury regulations. Section 20.2107-1, Estate Tax Regs., provides that if a nonresident expatriate decedent owns or is considered to own a certain amount of the voting shares in a foreign corporation at the time of his death, his gross estate must include an *amount* based upon the FMV of his percentage ownership interest in the foreign corporation and the portion of the foreign corporation's total assets situated in the U.S. *See id.* para. (b)(1). It then refers to the includible amount as the "proportionate value" and directs us to "example (2) in subparagraph (2)." *Id.* subdiv. (iii)(c). That example tells us that the "proportionate value" includible in the gross estate is an amount which results from multiplying fractions and FMVs. *See id.* subpara. (2), Example (2).

The only other Treasury regulation that uses "proportionate value" is section 25.2515-1(d)(2)(ii), Gift Tax Regs., which deals with the effect of an exchange of real property held by tenants in common. It provides that such an exchange will not terminate a tenancy so long as the tenant-spouses hold title in the exchanged property "in an identical tenancy." *Id.* The next sentence states that "a tenancy is considered identical if the *proportionate values* of the spouses' respective rights (other than any change in the *proportionate values* resulting solely from the passing of time) are identical to those held in the property which was sold." *Id.* (emphasis added). The regulation doesn't provide any examples, but the reference to "proportionate value" seems to mean a fraction of an amount equal to each spouse's property right multiplied by the FMV of the property held by the tenancy. We do not think it could reasonably refer to an amount equal to the *difference* between the values of the spouses' respective rights.

All this also supports our precedent that "proportionate value" means a fraction, and not a value. This makes us sufficiently confident of our reading to hold that even without Auer deference, the Commissioner has the better argument on the meaning of "proportionate value" in the regulation.

B. *Construing the Deed*

Before we can apply the regulation to the Deed, we also need to construe the Deed. This is no easy task, because the drafters of the Deed's contested section were trying to solve a cluster of related, but distinct, problems. So we need to dissect the chunk of language reprinted *supra* pp. 6-7 to see how it addresses each of these problems.

The first, as we've seen, is to limit the ability of the Conservancy and Oakbrook to undo the easement by deciding between themselves that changed circumstances sufficient to undermine the easement's conservation purpose exist. They had to do this under Tennessee law as well as the Code, and did so in the middle of the paragraph: "If a change in conditions makes impossible or impractical any continued protection of the Conservation Area for conservation purposes, the restrictions contained herein may only be extinguished by judicial proceeding." Deed, Article VI, Section B(2). The Commissioner doesn't dispute that this language succeeds in its job of meeting the requirement in section 1.170A-14(g)(6)(i), Income Tax Regs., that the restrictions be ended only in judicial proceedings if they are to meet the Code's requirement of perpetuity.

The second problem is what to do with proceeds from extinguishment. The Deed language gets tangled with itself because it tries to address not just the allocation of such proceeds, but the foreseeable contingency that Oakbrook will exercise its retained right to add improvements to the conserved area. Thus we see this sentence:

> For purposes of this Conservation Easement, the fair market value of [the Conservancy]'s right and interest shall be equal to the difference between (a) the fair market value of the Conservation Area as if not burdened by this Conservation Easement and (b) the fair market value of the Conservation Area burdened by this Conservation Easement, as such values are determined as of the date of this Conservation Easement, (c) less amounts for improvements made by O[akbrook] in the Conservation Area subsequent to the date of

> this Conservation Easement, the amount of which will be determined by the value specified for these improvements in a condemnation award in the event all or part of the Conservation Area is taken in exercise of eminent domain.

Deed, Article VI, Section B(2).

The Commissioner interprets this sentence to mean that the value of the Conservancy's property interest equals the value of the easement as of the date of donation less the value of any subsequent improvements. He argues this clause actually reduces the Conservancy's interest in extinguishment proceeds by the value of such improvements, and the value may fluctuate over time. In the event those improvements are "quite extensive," he argues, a situation could arise in which the Conservancy would receive nothing upon extinguishment.

Oakbrook responds that the Commissioner isn't reading the sentence correctly. It directs our attention to the last few lines of the sentence: "(c) less amounts for improvements made by Oakbrook] in the Conservation Area subsequent to the date of this Conservation Easement, *the amount of which will be determined by the value specified for these improvements in a condemnation award in the event all or part of the Conservation Area is taken in exercise of eminent domain* as further described in this Article VI, Section B(3) below." (Emphasis added.)

Oakbrook argues that the Commissioner's concern about subtracting the value of any future improvement from what the Conservancy would otherwise get is overblown. Any such subtraction would occur only if it is "determined by the value specified * * * in a condemnation award." In the case of a partial condemnation of only a little bit of the conservation area not occupied by any improvement, there would be no subtraction and the Conservancy would get the entire condemnation award up to the FMV of the easement as of the date of donation--a better deal, it points out, than the merely fractional part of that hypothetical award that the Commissioner says is required.

And this leads to the third problem that this language addresses--what to do when there is a judicial extinguishment of the easement followed by a later (possibly much later) sale of the property. Oakbrook says that the Conservancy would do just fine. The proceeds from such a sale would go to the Conservancy in an amount equal to the FMV of its easement because "upon such proceeding [, i.e., a judicial extinguishment proceeding], [the Conservancy], upon a subsequent sale, exchange or involuntary conversion of the Conservation Area, shall be entitled to a portion of the proceeds equal to the fair market value of the Conservation Easement as provided above." Because in this contingency there would be no specification "for these improvements in a condemnation award," the Conservancy would get its money off the top and not have to worry about the value of any improvements.

Oakbrook also argues more generally that the Commissioner's readings of the regulation and Deed would harm the Conservancy if the value of the conserved land decreases, or if it is partially condemned. Let's begin with an example where the value of land decreases following donation of the conservation easement. Imagine that the donated land at the time of the easement has an unencumbered FMV of $100,000 and an encumbered FMV of $50,000. Oakbrook adds improvements of $100,000. Property values then collapse and the easement is judicially extinguished (or condemned without specification of the value of the improvements) with proceeds recovered of $60,000. Under the Commissioner's interpretation of the Deed, the Conservancy would receive nothing because the S100,000 in improvements is greater than the proceeds. And even if the land went unimproved, the Conservancy would get only 50% of the recovered proceeds, or $30,000. If Oakbrook is right, however, the Conservancy would in both situations get its fixed value determined at the date of donation, or $50,000.

And if the land was improved and then partially condemned? Assume again that the easement was worth $50,000 at the date of donation and Oakbrook added $100,000 in improvements. Some time later the local highway authority condemns a sliver of the land that did not include the improvements to widen an adjoining road. The condemnation award would be small--let's say $5,000. Again, under the Commissioner's interpretation of the Deed, the Conservancy would get nothing because the condemnation award was less than the value of the improvements; and under his interpretation of the regulation, Oakbrook should receive just $2,500, which is the Conservancy's proportionate share of the unimproved property's value. But under Oakbrook's interpretation, because there would be no condemnation of any improvements, and because $5,000 is less than $50,000, the Conservancy would get the entire condemnation award whether or not there had been improvements.

State law defines property interests. *Case v. United States,* 633 F.2d 1240, 1246 (6th Cir. 1980); *Howard v. United States,* 566 S.W.2d 521, 525 (Tenn. 1978). And Tennessee law, following the usual common-law rule, allows for the admission of parol evidence to inform the meaning of a contract's ambiguous language if not introduced to contradict it. *Burlison v. United States,* 533 F.3d 419, 429 (6th Cir. 2008). So we asked the Conservancy's representative, Wright, how the Deed's proceeds clause would operate when the easement was extinguished after improvements were made. We found his answer entirely credible:

> [A]s long as there's a condemnation award and *if the award were to specifically identify those improvements* being the value of them, those would be deducted from the proceeds, because they aren't relevant to the valuation of the easement. [Emphasis added.]

And again:

> [A]s long as the condemnation award specifically identifies those as subsequent additions, because if they were not, then the land trust would [in]ure [to] a benefit for which it is not entitled. They did not pay for those improvements. They have no property interest in those improvements. Therefore, if we were to keep the award that took those improvements into consideration, the land trust would be getting unjust compensation because we didn't pay for those. We have to strip those away, get back to the matter at hand, and that is the value of the donation at the time of the donation.

And finally, in the case of a partial condemnation:

> [A certain conservation easement is] a small part of a big property but nevertheless a utility came in and obtained a judgment to put a pipeline in the [easement] property. Of

> course, the owner didn't want it. He supported it but it's a utility, and we're going to lose and so, therefore, we've already gotten the judgment and was in the process of settling it. The award coming out of that -- no questions asked, there's no argument over it, the land trust is a hundred percent of the condemnation reports.

We also asked Wright about scenarios where this construction would not favor the Conservancy. Consider an increase in land values. If there were '70s-era inflation, the easement was extinguished, and the property then sold for $200,000, what would the Conservancy get? When we asked Wright at trial about this very scenario, he confirmed that the Conservancy would be entitled only to its initial fixed value.

We conclude from this that Oakbrook's reading of this section of the Deed is correct. The value of any improvements would be subtracted from any condemnation award only if it was specified in that award. The Conservancy would get the FMV of the easement as of the date of donation, and it would get the entire amount of any award for a partial condemnation not affecting any improvements or a future sale after judicial extinguishment, up to that FMV. It would not, however, be protected from inflation either in local land prices or the economy more generally; and it would not get the entire FMV if prices collapsed before a later condemnation or extinguishment.

C. *Applying the Regulation to the Deed*

The Commissioner argues that Oakbrook's Deed, even if we interpret it the way Oakbrook wants us to, violates the regulation twice. First, he reiterates that it fails to define a fraction to be multiplied by the amount of any future proceeds. The Commissioner has to win on this argument--once we interpret the regulation to require a fraction multiplied by future proceeds, Oakbrook can't argue that the Deed conforms to the regulation. But the Commissioner argues that the Deed also fails because the regulation prohibits any scenario in which a donor gets to recover, either through condemnation or sale after extinguishment, any compensation for its improvements in excess of a share of the proceeds defined by the before-and-after-easement value of the unimproved land at the time of donation. We are left with the distinct sense that there are some plausible scenarios where Oakbrook's construction of "proportionate value" would protect an easement's conservation purposes in perpetuity better than the Commissioner's would. The Commissioner's construction might not compensate a donee as well as Oakbrook's, should property values decrease or if the property were only partially condemned. But our task here is to see how the Deed squares with the regulation, not whether there are plausible scenarios where the Deed would compensate the Conservancy better than the regulation.

This is where Oakbrook's argument fails. The regulation prohibits any scenario in which Oakbrook gets to recover compensation other than a proportionate share of the proceeds, with the proportion defined by the easement's FMV over the FMV of the unencumbered and unimproved property.

It also doesn't matter that the value fixed by the Deed "will *almost* universally be more than the percentage of proceeds the IRS claims the land trust is entitled to under the language" of section 1.170A-14(g)(6)(ii), Income Tax Regs., as Oakbrook argues. In other words, Oakbrook argues the Deed "substantial[ly] compli[es]" with the regulation. On this point, we need only cite *Kaufman I,* where we held that a donor must show strict, and not substantial, compliance with the perpetuity requirements of the regulation. *See Kaufman I, 1*34 T.C. at 186 (petitioners "cannot avoid the strict requirement in section 1.170A-14(g)(6)(ii), Income Tax Regs., simply by showing that they would most likely be able to satisfy" their obligation to the land trust).

We agree again with the Fifth Circuit in *PBBM-Rose Hill,* 900 F.3d at 207. It held that "[t]he ordinary meaning of 'proceeds' is 'the *total* amount brought in,' such as 'the proceeds of sale.' *Id.* (alterations in original) (citations omitted). It also noted that the fact that the regulation explicitly contemplates that a donor may reserve the right to make improvements, *see* sec. 1.170A-14(g)(5)(i), Income Tax Regs., "but chose not to carve out an exception for the allocation of proceeds in the event of extinguishment when such improvements have been made," suggests no such carve-out was intended, *PBBM-Rose Hill,* 900 F.3d at 208. Substantial compliance does not work here.

Oakbrook also argues that it's unfair for a donee to receive extinguishment proceeds attributable to the value of improvements made solely by the donor--it would amount, says Oakbrook, to an unintended charitable donation for which it receives no deduction. While we might otherwise be sympathetic to this argument, we have identified as a purported purpose of the regulation the avoidance of windfalls to donors, not donees, if an easement is extinguished. *See Kaufman III,* 687 F.3d at 26.

It's also easy enough to imagine scenarios where a fixed value might be unfair to donees. The other purpose of section 1.170A-14(g)(6)(ii), Income Tax Regs., that we've identified is "to assure that the donee organization can use its proportionate share of the proceeds to advance the cause of historic preservation [or other conservation cause] elsewhere." *Kaufman III,* 687 F.3d at 26. If this is true, it would seem that providing a donee with a share of proceeds attributable to inflation or rising property values better achieves this purpose. If, for example, an easement is extinguished years after its donation, during which time land values have skyrocketed, a donee organization's entitlement to a portion of the resulting increased proceeds may likely be the only way that it could afford to further its conservation purpose elsewhere.

We do note that the Commissioner's interpretation of improvements in this case contradicts his position in Priv. Ltr. Rul. 200836014 (Sept. 5, 2008), which Oakbrook claims has since been adopted by numerous land trusts, and which it argues would undermine the vast majority of easements. The relevant sentence states, "the portion of the proceeds of any subsequent sale or exchange (or condemnation) of the Protected Property payable to the Donee represents a *percentage interest* in the [FMV] of the Protected Property *(less an amount attributable to the value of a permissible improvement made by Grantors, if any, after the date of the contribution of the Easement). Id.* (emphasis added). We don't need to parse a nonprecedential PLR too closely. But this sentence is noteworthy for its seeming to construe "proportionate value" to mean "percentage interest." This is entirely consistent with the Commissioner's position in this case and tends to show continuity in the Treasury's construction of its own regulation.

Oakbrook is correct, however, that the parenthetical clause in the PLR that calls for the amount attributable to the value of improvements made after the easement to be taken off the top contradicts the Commissioner's current position. The Fifth Circuit addressed this exact issue by finding the regulation's meaning unambiguous as to improvements--they cannot be subtracted. *PBBM-Rose Hill, 9*00 F.3d at 208. It also noted that "even if the regulation were ambiguous, [the Court] would not follow the [Commissioner]'s interpretation in the ruling because it contravene[d] a plain reading of the regulation without an explanation." *Id.* at 208-09 (citing *Tex. Clinical Labs, Inc.,* 612 F.3d at 777); *see also Salamalekis v. Comm'r of Soc. Sec.,* 221 F.3d 828, 832 (6th Cir. 2000) (stating that a court may defer to an agency's position when that position "presents a reasonable construction of an ambiguous provision of * * * the agency's regulations"). And PLRs simply aren't precedential--we therefore agree with the Fifth Circuit that the language of the regulation is unambiguous on this issue.[10]

Oakbrook's Deed violates the regulation because the Conservancy must be entitled to any proceeds from extinguishment or condemnation that are at least equal to the total proceeds (unadjusted by the value of any of Oakbrook's improvements), multiplied by a fraction defined by the ratio of the FMV of the easement to the FMV of the unencumbered property determined as of the date of the Deed.

Our holding as to the meaning of section 1.170A-14(g)(6)(ii), Income Tax Regs., doesn't necessarily doom Oakbrook's deduction. Oakbrook argues in the

[10] We are also wary of accepting the contention that numerous land trusts adopted their current deed language that subtracts the value of improvements from the proportionate value calculation, based upon a sentence of a PLR released in 2008--it seems to us that such language existed in deeds well before 2008.

alternative that this regulation is invalid.[11] About this there is disagreement within the Court, and we air that disagreement in a separate opinion that we also release today. *See Oakbrook Land Holdings, LLC v. Commissioner,* 154 T.C. ___ (May 12, 2020).

III. *Penalty*

That leaves only the Commissioner's determination that a penalty under section 6662 was applicable to Oakbrook. This penalty is applicable when a partnership takes a return position that might create a substantial understatement of tax due at the partner level, sec. 6662(b)(2), or that is negligent or shows disregard of the rules and regulations, sec. 6662(b)(1). The Code tells us that negligence is the "failure to make a reasonable attempt to comply with the [Code]" and that disregard includes "careless, reckless, or intentional disregard." Sec. 6662(c). And the Code also tells us that an understatement is substantial if it exceeds the greater of $5,000 or "10 percent of the tax required to be shown on the return." Sec. 6662(a), (b)(2), (d)(1)(A). (The determination of an underpayment cannot be made at the partnership level because partnerships don't pay taxes, partners do. We can still, however, determine the *applicability* of the understatement (or negligence, or intentional-disregard) penalty at the partnership level. *See VisionMonitor Software, LLC v. Commissioner,* T.C. Memo. 2014-82, 108 T.C.M. (CCH) 256, 260 (2014).)

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[11] Despite the Commissioner's suggestion to the contrary, no court has directly addressed whether section 1.170A-14(g)(6)(ii), Income Tax Regs., is invalid. In *PBBM-Rose Hill* the Fifth Circuit refused to address the issue because the taxpayer had not first raised it in this Court. *See PBBM-Rose Hill,* 900 F.3d at 209 n.8.

These penalties don't apply to a taxpayer who had reasonable cause for an underpayment and acted in good faith. Sec. 6664(c)(1); sec. 1.6664-4(a), Income Tax Regs. The determination of whether a taxpayer acted with reasonable cause and in good faith is one we make on a case-by-case basis. Sec. 1.6664-4(b)(1), Income Tax Regs. One circumstance that indicates reasonable cause and good faith is an honest misunderstanding of fact or law that is reasonable in light of all of the facts and circumstances. *Id.* Reliance on certain facts can constitute good faith if, "under all the circumstances, such reliance was reasonable and the taxpayer acted in good faith." *Id.*

Here, we deny any deduction for Oakbrook's donation of the conservation easement because the provisions in the Deed violated the extinguishment-proceeds clause in the regulation. But we think Oakbrook's position was reasonable: There is the PLR that the IRS itself issued that suggested a clause like the one in the deed would work. Section 1.6662-3(b)(3), Income Tax Regs., tells us that a return position generally satisfies the reasonable-basis standard if it is based on, among other types of authorities, private letter rulings. *See* secs. 1.6662-3(b)(3), 1.6662- 4(d)(3)(iii), Income Tax Regs.; *see also Bunney v. Commissioner,* 114 T.C. 259, 267 n.10 (2000) (PLRs may be authorities showing reasonableness of return position). There is disagreement among us on whether the contested regulation is valid, and that might also be some indication of the objective reasonableness of Oakbrook's position. Trial proved that Horton knew he was unfamiliar with the mechanics of setting up a conservation easement and relied on what he saw as the safety of form language that echoed the PLR. We find this was reasonable under these circumstances, and based on the credibility of his trial testimony, taken entirely in good faith.

Oakbrook's error--if it turns out to be an error--was reasonable.

We therefore also conclude that the penalty that the Commissioner determined was applicable cannot be sustained.

An appropriate decision will be entered.

APPENDIX E

United States Code Annotated
Title 5. Government Organization and Employees (Refs & Annos)
Part I. The Agencies Generally
Chapter 5. Administrative Procedure (Refs & Annos)
Subchapter II. Administrative Procedure (Refs & Annos)

5 U.S.C.A. § 553

§ 553. Rule making.

* * *

(c) After notice required by this section, the agency shall give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments with or without opportunity for oral presentation. After consideration of the relevant matter presented, the agency shall incorporate in the rules adopted a concise general statement of their basis and purpose. When rules are required by statute to be made on the record after opportunity for an agency hearing, sections 556 and 557 of this title apply instead of this subsection.

* * *

United States Code Annotated
Title 26. Internal Revenue Code (Refs & Annos)
Subtitle A. Income Taxes (Refs & Annos)
Chapter 1. Normal Taxes and Surtaxes (Refs & Annos)
Subchapter B. Computation of Taxable Income
Part VI. Itemized Deductions for Individuals and Corporations (Refs & Annos)

§ 170. Charitable, etc., contributions and gifts.

* * *

(h) Qualified conservation contribution.—

(1) In general.—For purposes of subsection (f)(3)(B)(iii), the term "qualified conservation contribution" means a contribution—

(A) of a qualified real property interest,

(B) to a qualified organization,

(C) exclusively for conservation purposes.

(2) Qualified real property interest.—For purposes of this subsection, the term "qualified real property interest" means any of the following interests in real property:

(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.

(3) Qualified organization.—For purposes of paragraph (1), the term "qualified organization" means an organization which—

(A) is described in clause (v) or (vi) of subsection (b)(1)(A), or

(B) is described in section 501(c)(3) and—

(i) meets the requirements of section 509(a)(2), or

(ii) meets the requirements of section 509(a)(3) and is controlled by an organization described in subparagraph (A) or in clause (i) of this subparagraph.

(4) Conservation purpose defined.—

(A) In general.—For purposes of this subsection, the term "conservation purpose" means—

(i) the preservation of land areas for outdoor recreation by, or the education of, the general public,

(ii) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem

(iii) the preservation of open space (including farmland and forest land) where such preservation is—

(I) for the scenic enjoyment of the general public, or

(II) pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or

(iv) the preservation of an historically important land area or a certified historic structure.

(B) Special rules with respect to buildings in registered historic districts.—In the case of any contribution of a qualified real property interest which is a restriction with respect to the exterior of a building described in subparagraph (C)(ii), such contribution shall not be considered to be exclusively for conservation purposes unless—

(i) such interest—

(I) includes a restriction which preserves the entire exterior of the building (including the front, sides, rear, and height of the building), and

(II) prohibits any change in the exterior of the building which is inconsistent with the historical character of such exterior,

(ii) the donor and donee enter into a written agreement certifying, under penalty of perjury, that the donee—

(I) is a qualified organization (as defined in paragraph (3)) with a purpose of environmental protection, land conservation, open space preservation, or historic preservation, and

(II) has the resources to manage and enforce the restriction and a commitment to do so, and

(iii) in the case of any contribution made in a taxable year beginning after the date of the enactment of this subparagraph, the taxpayer includes with the taxpayer's return for the taxable year of the contribution—

(I) a qualified appraisal (within the meaning of subsection (f)(11)(E)) of the qualified property interest,

(II) photographs of the entire exterior of the building, and

(III) a description of all restrictions on the development of the building.

(C) Certified historic structure.—For purposes of subparagraph (A)(iv), the term "certified historic structure" means—

(i) any building, structure, or land area which is listed in the National Register, or

(ii) any building which is located in a registered historic district (as defined in section 47(c)(3)(B)) and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

A building, structure, or land area satisfies the preceding sentence if it satisfies such sentence either at the time of the transfer or on the due date (including extensions) for filing the transferor's return under this chapter for the taxable year in which the transfer is made.

(5) Exclusively for conservation purposes.—For purposes of this subsection—

(A) Conservation purpose must be protected.— A contribution shall not be treated as exclusively for conservation purposes unless the conservation purpose is protected in perpetuity.

(B) No surface mining permitted.—

(i) In general.—Except as provided in clause (ii), in the case of a contribution of any interest where there is a retention of a qualified mineral interest, subparagraph (A) shall not be treated as met if at any time there may be extraction or removal of minerals by any surface mining method.

(ii) Special rule.—With respect to any contribution of property in which the ownership of the surface estate and mineral interests has been and remains separated, subparagraph (A) shall be treated as met if the probability of surface mining occurring on such property is so remote as to be negligible.

(6) Qualified mineral interest.—For purposes of this subsection, the term "qualified mineral interest" means—

(A) subsurface oil, gas, or other minerals, and

(B) the right to access to such minerals.

* * *

APPENDIX F

Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service,
Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Computation of Taxable Income
Itemized Deductions for Individuals
and Corporations

26 C.F.R. § 1.170A–14, Treas. Reg. § 1.170A–14

Effective: July 30, 2018

§ 1.170A–14 Qualified conservation contributions.

* * *

(g) Enforceable in perpetuity—(1) In general. In the case of any donation under this section, any interest in the property retained by the donor (and the donor's successors in interest) must be subject to legally enforceable restrictions (for example, by recordation in the land records of the jurisdiction in which the property is located) that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation. In the case of a contribution of a remainder interest, the contribution will not qualify if the tenants, whether they are tenants for life or a term of years, can use the property in a manner that diminishes the conservation values which are intended to be protected by the contribution.

* * *

(3) Remote future event. A deduction shall not be disallowed under section 170(f)(3)(B)(iii) and this section merely because the interest which passes to, or

is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible. See paragraph (e) of § 1.170A–1. For example, a state's statutory requirement that use restrictions must be rerecorded every 30 years to remain enforceable shall not, by itself, render an easement nonperpetual.

* * *

(6) Extinguishment. (i) In general. If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined under paragraph (g)(6)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

(ii) Proceeds. In case of a donation made after February 13, 1986, for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time. See § 1.170A–14(h)(3)(iii) relating to the allocation of basis. For purposes of this paragraph (g)(6)(ii), that proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

* * *

APPENDIX G

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1, 20, and 25

[LR-200-76]

Qualified Conservation Contribution; Proposed Rulemaking

AGENCY: Internal Revenue Service, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to contributions of partial interests in property for conservation purposes. Changes to the applicable tax law were made by section 6 of the Tax Treatment Extension Act of 1980. This document is intended to clearify the statutory rules in effect under that Act.

DATE: Written comments and requests for a public hearing must be delivered or mailed by July 22, 1983. The amendments are proposed to be applicable for contributions made on or after December 18, 1980, and are proposed to be effective the date final regulations are published in the Federal Register.

ADDRESS: Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, D.C. 20224, Attention: CC:LR:T (LR-200-76).

FOR FURTHER INFORMATION CONTACT: John R. Harman of the Legislation & Regulations Division, Office of the Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224, Attention: CC:LR:T, 202-566-3287, not a toll-free call.

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments proposed to conform the Income Tax Regulations (28 CFR Part 1) under section 170 of the Internal Revenue Code of 1954 (Code) relating to contributions not in trust of partial interests in property to section 6 of the Tax Treatment Extension Act of 1980.

The Tax Reform Act of 1969 and the regulations promulgated thereunder limited the deductibility of the donation of easements generally to charitable contributions of perpetual open space easements in gross, (section 170(f)(3)(B)(ii) of the Code and § 1.170A-7(b)(1)(ii) of the Income Tax Regulations). Although subsequent revenue rulings held that a variety of easements were deductible under the limitation of the 1969 Act (See, *e.g.*, Rev. Rul. 75-358, 1975-2 C.B. 76), Congress in 1976 added further legislative authority for the deductibility of easement donations.

Section 2124(e) of the Tax Reform Act of 1976 (Pub. L. 94–455, 90 Stat. 1919) provided, for the first time, specific statutory authority under section 170 of the Code for the deductibility of the donation to a qualified organization of easements, remainder interests, and certain other partial interests in property. The 1976 Act allowed the deduction for partial interests donated for a term of 30 years or more, but required that the donation be made "for conservation purposes." Conservation purposes was defined in section 170(f)(3)(C).

Section 309 of the Tax Reduction and Simplification Act of 1977 (Pub. L. 95-30, 91 Stat. 154) made two changes in the statutory language codified by the 1976 Act. The first change eliminated the deductibility of term easements for conservation purposes and required that such easements be perpetual in order to qualify for a deduction under section 170. The second change set the expiration date of these provisions at June 14, 1981.

Section 6 of the Tax Treatment Extension Act of 1980 made extensive changes in the existing statute, eliminated the expiration date, and incorporated the relevant language into a new section 170(h). The House and Senate Committee reports accompanying the legislation also provided, for the first time, an in-depth statement of congressional intent concerning the donation of partial interests for conservation purposes (H.R. Rep. No. 98-1278, S. Rep. No. 96-1007). The regulations reflect the major policy decisions made by the Congress and expressed in these committee reports.

Additional Information

Generally, the donation of an easement to preserve open space is deductible under section 170(h)(4)(A)(iii) if such preservation will yield a significant public benefit and is either for the scenic enjoyment of the general public or its pursuant to a clearly delineated governmental policy. The most difficult problem posed in this regulation was how to provide a workable framework for donors, donees, and the Internal Revenue Service to judge the deductibility of open space easements.

Defining "Significant public benefit" with any degree of precision is impossible. Any attempt to reduce the test to a mathematical formula would be arbitrary. The factors included at § 1.170A-13(d)(4)(iv) are not intended to be exclusive; however, a longer list of factors would always fall short of being all-inclusive. The same statements can be made concerning the list of factors proposed under § 1.170A-13(d)(4)(ii) with respect to "scenic enjoyment."

It is believed, however, that the "sliding scale" approach proposed in §1.170A-13(d)(4)(vi) that establishes a relationship between the requirements of "significant public benefit" and "clearly delineated governmental policy" will eliminate much of the uncertainty that surrounds this part of the statute. Additionally, by including prior state and local governmental determinations of specific resources to be protected as a criteria for meeting the "significant public benefit" and "scenic enjoyment" tests, a degree of certainty will be available to taxpayers in jurisdictions that have carefully articulated preservation policies. In the end, of course, some exercise of judgment and of responsibility is ultimately required by both donors and donees.

Comments and Requests for a Public Hearing

Before adopting these proposed regulations, consideration will be given to any written comments that are submitted (preferably seven copies) to the Commissioner of Internal Revenue. All comments will be available for public inspection and copying. A public hearing will be held upon written request to the Commissioner by any person who has submitted written comments. If a public hearing is held, notice of the time and place will be published in the Federal Register.

Executive Order 12291 and Regulatory Flexibility Act

The Commissioner of Internal Revenue has determined that this proposed rule is not a major rule as defined in Executive Order 12291. Accordingly, a Regulatory Impact Analysis is not required. The Internal Revenue Service has concluded that although this document is a notice of proposed rulemaking that solicits public comments, the regulations proposed herein are interpretative and the notice and public procedure requirements of 5 U.S.C. 553 do not apply. Accordingly, no Regulatory Flexibility Analysis is required for this rule.

Drafting Information

The principal authors of this regulation are John R. Harman and Stephen J. Small of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulation, both on matters of substance and style.

List of Subjects

26 CFR 1.61-1–1.281-4

Income taxes, Taxable income, Deductions, Exemptions.

26 CFR Part 20

Estate taxes.

26 CFR Part 25

Gift taxes.

Proposed Amendments to the Regulations

The proposed amendments to 26 CFR Parts 1, 20, and 25 are as follows:

PART 1—[AMENDED]

* * *

§ 1.170A-13 Qualified conservation contributions.

* * *

(g) *Enforceable in perpetuity—*

* * *

(2) *Remote future event.* A deduction shall not be disallowed under section 170(f)(3)(B)(iii) and this section merely because the interest which passes to, or is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible. See paragraph (e) of § 1.170A-1. For example, a state's statutory requirement that use restrictions must be rerecorded every 30 years to remain enforceable shall not, by itself, render an easement nonperpetual.

* * *

(5) *Extinguishment.* (i) *In general.* If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined under paragraph (g)(5)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

(ii) *Proceeds.* In case of a donation made after (the date final regulations are published in the Federal Register), for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is a minimum ascertainable proportion of the fair market value to the entire property, See

§ 1.170A-13(h)(3)(iii). For purposes of this paragraph (g)(5)(ii), that original minimum proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(5)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to the original proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

APPENDIX H

NEW YORK LANDMARKS CONSERVANCY

August 31, 1983

Commissioner of Internal Revenue
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Attention: CC:LR:T (LR-200-76)

Dear Commissioner:

On behalf of the New York Landmarks Conservancy and as Chairman of the Conservancy's Easements Committee, I submit the following comments to you with respect to the Department of the Treasury's proposed regulations published in the Federal Register on Monday, May 23, 1983, Vol. 48, No. 100, pp. 22940 et seq., entitled "Qualified Conservation Contribution; Proposed Rulemaking." The New York Landmarks Conservancy is a private, not-for-profit corporation dedicated to the preservation of architecturally, historically and culturally significant buildings throughout the State of New York. Since 1976, the Conservancy has operated a successful program for the acceptance of easements on worthy sites and structures.

Our comments are as follows:

1. On May 13, 1981, William H. Whyte, a member of the Conservancy's Easements Committee and Laurie Beckelman, Executive Director of the Conservancy, met with Stephen small, then a staff member of the Internal Revenue Service and Thomas Coughlin, Assistant General Counsel at the National Trust for Historic Preservation to discuss the prospective content of the proposed regulations. The Conservancy would like to express its deep appreciation that its

concerns as expressed at that meeting regarding preservation of open space in urban areas are so extensively and ably reflected in the proposed regulations which concern the donation of scenic easements within urban landscapes, in particular, Section 1.170A-13 (d) (4) (ii) at page 22943.

To further clarify the applicability of the proposed regulations with respect to the preservation of open space in urban areas we propose two additional illustrations to be included in Section 1.170A-13 (d)(4)(iv)(B) at page 22944:

Illustration #1 Parkacre is a small urban park open to the public, containing plantings and a waterfall, located in a densely populated business district of a city. Parkacre provides the public with relief from urban closeness and enjoyment of the landscaping and sunlight. The owner of a low-rise property across the street and to the south of Parkacre donates a conservation easement to Parkacre or another qualified conservation organization whereby the donor guarantees that he and his successors in interest will restrict the development of his property in perpetuity in order to provide Parkacre with continued access to the sunlight which passes over his property to Parkacre.

Illustration #2 A,B,C,D,E and F are each owners of adjacent low-rise harmonious residential buildings on an urban street in the midst of a densely populated section of a city. These buildings are not architecturally distinguished; however the buildings allow the sunlight to penetrate to the street utilized by the public and they maintain the scale and character of the urban streetscape. In relation to the developed surrounding area, these buildings provide diversity in height, building density and architectural style. A,B,C,D,E and F each contribute a conservation easement on his respective building to a qualified conservation organization to ensure that the scale, character and sunlight provided by these buildings will be preserved for the benefit of the public.

2. The provisions for apportionment of proceeds in the case of extinguishment of a conservation restriction (contained principally in § 1.170A-13(g)(5)(ii) at page 22946) contain problems of policy and practical application so pervasive as to cause us to recommend strongly the deletion of these provisions. The statute was enacted by Congress to encourage the protection of our significant natural and built environment through the donation of conservation restrictions and yet, the proposed provisions would thwart the purpose of the statute by deterring prospective donors.

We believe prospective donors of conservation restrictions are likely to be discouraged from making a donation which may tie themselves or future owners to share proceeds of a sale or exchange with the charitable organization to which the restriction was granted under circumstances which cannot possibly be foreseen. Indeed, it is our experience that prospective donors frequently raise the question that "perpetuity" is a long time and may impose unforeseeably heavy burdens on themselves or future owners under unforeseeable future circumstances. We find ordinarily that these concerns are mollified upon the donor's recognition that common law permits extinguishment of restrictions when they no longer serve the original intended purposes. Obviously, the prospect of extinguishment would no longer mollify these fears if a split of proceeds under unknown circumstances would be required. In light of the deterrent effect of the extinguishment provision and the fact that the possibility of extinguishment is relatively remote, it seems unnecessary for the Department of the Treasury to provide for allocation of proceeds after extinguishment.

It is the assumption of the extinguishment provision that a conservation restriction as held by a conservation organization has a market value in the sense of a price at which it can be traded on the free market; however, this assumption seems unrealistic. The value of a conservation restriction to the donee organization is not a monetary value but a philanthropic value as a device for achieving the charitable objectives of the organization. While it is true, of course, that any charitable organization welcomes the receipt of hard cash for its charitable activities, in a very real sense the extinguishment of a conservation restriction cannot be compensated by the payment of money. The Conservancy, therefore, would prefer to eliminate from the proposed regulations a provision likely to deter gifts of conservation restrictions than to trade on the prospect of future windfalls when restrictions are extinguished.

The structure of § 1.170A-13(g)(5)(ii) contemplates that a ratio of value of the conservation restriction to value of the fee will be fixed at the time of the donation and will remain in effect forever thereafter. This formula fails to take into account that improvements may be made thereafter by the owner which should properly alter the ratio. For example,(using the facts of example 4 in § 1.170A-13(f) at page 22945), suppose the donation of a scenic easement upon Greenacre providing limited cluster development in areas generally not visible from a nearby national park. At the time of the donation, Greenacre was worth $100,000 and the easement accounts for 10% of the value. Thereafter, the owner spends $2 million on the construction of housing units to be rented. If the easement were subsequently extinguished, the donee organization would be entitled under § 1.170A-13(g)(5)(ii) to 10% of the sale price of the entire parcel including the improvements. This would obviously be undesirable to the prospective donor and would constitute a windfall to the donee organization.

In another example, if an encumbered property were condemned and the conservation restriction was subsequently extinguished, state law would operate to determine whether the conservation organization's restriction had a compensable value. It is possible that some states would not provide compensation for such a property interest, yet under the proposed regulation, the owner of the condemned property would be required to share the condemnation proceeds with the conservation organization.

In light of the potential inequities described above, the Conservancy recommends that the proposed proceeds formula be revised to prevent such inequities should the Department of the Treasury decide to retain the provision. However, the Conservancy strongly recommends deletion of the entire extinguishment provision.

3. Section 1.170-13 (d)(5) at page 22944 states, in part:

> When restrictions to preserve a building or land area within a registered historic district permit future development on the site, a deduction will be allowed under this section only if the terms of of the restrictions require that such development conform with appropriate local, state, or Federal standards for construction or rehabilitation within the district.

We believe that the meaning of "appropriate" must be defined in order to avoid any confusion that may arise as to when local, state or Federal standards should apply in certain situations. Perhaps the word "applicable" substituted for the word "appropriate" would clear up the ambiguity.

4. Section 1.170A-13 (d) (5) (ii) (C) at page 22944 defines as an historially important land area "Any land area adjacent to a property listed individually in the National Register of Historic Places (but not within a registered historic district) in a case where the physical or environmental features of the land area contribute to the historic or cultural integrity of the structure." The Conservancy interprets the word "adjacent" to include land areas which may be nearby but are not necessarily contiguous to properties listed individually in the National Register of Historic Places. We note that this interpretation is consistent with the policy expressed by § 1.170A-13(d)(4)(B) at page 22943 favoring preservation of views from historic structures. Clarification that "adjacent" carries the meaning we understand would, of course, be desirable.

5. With respect to Section 1.170A-13 (e)(2) at page 22944 the Conservancy requests clarification that physical "access" may be limited in the interests of privacy or other personal interests so long as one or more public purposes (such as visual access) are sufficiently provided for.

The Conservancy requests the privilege of testifying at the hearing scheduled for September 15, 1983.

Sincerely,

/s/ Michael S. Gruen
Michael. S. Gruen

APPENDIX I

LAND TRUST EXCHANGE

August 29, 1983

Commissioner of Internal Revenue
Internal Revenue Service
1111 Constitution Avenue
Washington, D.C. 20224

RE: CC:LR:T (LR-200-76)
Proposed Regulations - §170(h)

Dear Sir:

I am writing on behalf of the Land Trust Exchange, a non-profit communications, technical assistance, and policy network. It services more than 500 private land conservation organizations in 43 states. These local and regionally-based groups are making significant cost-effective contributions to the nation's land conservation needs, individually and collectively.

The Land Trust Exchange is concerned by the likely impact of the proposed regulations on the continued viability of easements for conservation purposes. We believe the proposed regulations may seriously interfere with the continued willingness of landowners to donate easements.

The many comments submitted by local land conservation groups to the Service express the depth and range of concerns. During the past three months, the Exchange has compiled these comments under the direction of its Vice-Chairman, Benjamin R. Emory. A synthesis was prepared and disseminated as part of the Exchange's *Conservation Tax Program* edited by its General Counsel, Kingsbury Browne. I am enclosing copies of Mr. Emory's synthesis to assist in the review and evaluation process.

* * *

Conservation
Tax Program
A Service of the Land Trust Exchange

August 25, 1983

Synthesis of Comments
from Land Trusts Regarding
Proposed IRS Regulations on
Conservation Easements

Prepared By Benjamin R. Emory

Following is a review of the various comments received by the Land Trust Exchange. This synthesis was prepared by Ben Emory who serves as vice-chairman and staff consultant to the Exchange, and brings 12 years of experience with conservation easements and working for a land trust. It flags the major issues which have been raised and hopefully will assist in further review of the proposed regulations.

* * *

The Land Trust Exchange has been reviewing the numerous comments received from land trusts and from people who work closely with land trusts. No matter how politely the letter of comment to the IRS are phrased, there is obvious, deep dissatisfaction with the proposed Regulations. On the other hand, the statute itself is seriously deficient from the point of view of many land trusts, and the IRS cannot rectify all the problems.

The volume of paper that has been generated is substantial, and land trusts and their attorneys have only limited time to prepare comments as well as study the comments of others. This synthesis tries to flag the major issues that have been raised and hopefully will assist in further review of the proposed Regulations.

* * *

HISTORICAL LAND AND BUIILDINGS:

* * *

p. 22946; (g)(5)(ii): A reviewer criticizes the straight proportional approach to the distribution of proceeds in the event of an extinguishment is unfair as applied to easements on structures. A second concern is that a casualty loss may result in a partial extinguishment of an easement.

(Vermont Law School - Edmund Kellogg, Robert Shustermann--Philadelphia Preservation Corporation, Maryland Environmental Trust.)

* * *

PROCEEDS FROM A SALE FOLLOWING EXTINGUISHMENT:

p. 22946; (g)(5)(ii): From a donee's point of view an easement is not a financial asset and has no market value. This section may result in donors or donees having to pay real estate transfer taxes. Also, the tax benefit rule and the remote future event rule should make this section unnecessary. Another reviewer makes a very different suggestion- that the donee should be entitled to the greater of the easement's original proportionate value or its proportionate value at the time of the extinguishment. (See also comments under "HISTORIC LAND AND BUILDINGS.")

(Western Pennsylvania Conservancy, Trust for Public Land, Hofstra University-Ginsberg-Catskill Center for Conservation and Development. Ivins. Phillips & Barker – Brandywine Conservancy.)

* * *

APPENDIX J

Maine Coast Heritage Trust
Davis Hartwell, *Executive Director*
P.O. Box 426, Northeast Harbor, Maine 04662
(207) 276-5156

Earl Ireland, *Associate Director*
Box 120, U.S. Route 1, Falmouth, Maine 04105
(207) 781-3157

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23 August 1983

Mr. John R. Harman
Legislation & Regulations Division
Office of the Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D. C. 20224

Attn: CC:LR:T

Dear Mr. Harman:

* * *

7. Paragraph (g)(5) – Enforceable in perpetuity; Extinguishment.

We strongly endorse the proposed provisions for extinguishing easements. They help to resolve a major issue in the use of conservation easements and we commend the IRS for its innovation in this regard.

We have three major concerns, however. First, we feel that the grantee should not play a role in valuing the gift for tax purposes. While we occasionally advise prospective grantors as to the possible value of an easement through our use of experienced appraisers and attorneys, we carefully instruct grantors that they may not rely on our opinions. Our business is conserving land, not giving tax advice. The regulations should make it clear that determining the value of the conservation easement is the responsibility of the grantor.

Second, we agree with The Nature Conservancy that the regulations should be clear that the proportionate value assigned to an easement at the time of gift is the *minimum* that a grantee organization should receive in the event of an extinguishment and sale of the easement, thus allowing the grantee to capture any increase in the proportionate value of the easement.

Third, we are concerned about the effect of this provision on accounting practices of private conservation organizations and on the IRS reporting requirements. Currently, we do not book conservation easements at a dollar value because they have no economic value to us. In fact, they represent a great potential cost in monitoring and enforcement, and it is primarily for their negative value that we note them in our financial statements.

The extinguishment provisions in the regulations suggest that conservation easements may have a positive economic value for the grantee and that the grantee should record the proportionate value of a conservation easement in relation to the entire subject property. To express this as an absolute dollar amount would be misleading, however, because it is the proportionate value, not the absolute value, that is the important figure. Also, the grantee is not at liberty to dispose of its conservation easements; it holds them essentially in trust and, under the proposed regulations, it can convert them to cash only upon a sale following a court order based on a change in the conditions surrounding the easement property. Thus, the value of an easment to the grantee must be discounted by the remote probability of this event.

The problem of valuing easements from the grantee's standpoint is particularly difficult in connection with reporting its contributions on Form 990 and maintaining its status as a publicly-supported charity. The deducted value of a single conservation easement could exceed the entire annual operating budget of a small or even medium-sized land trust. A land trust operating a successful program might receive at least one such substantial easement each year for several years. This may jeopardize its status as a publicly-supported charity.

To avoid this problem, we urge that the IRS not require land trusts to report conservation easements at their deducted value[*] or, alternatively, that the IRS not treat conservation easements as contributions for the purposes of the public support tests. The regulations should recognize that a conservation easement, once granted, sacrifices economic value for environmental benefits. Thus, its economic value to the grantee is far less than the value contributed by the grantor.

* * *

APPENDIX K

The Nature Conservancy
1800 North Kent Street
Arlington, Virginia 22209
(703) 841-5300

August 17, 1983

Mr. Roscoe L. Egger, Jr.
Commissioner
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224
Attention: CC:LR:T (LR-200-76)

Dear Commissioner Egger:

* * *

Proposed Regulations
Qualified Conservation Contribution
CC:LR:T (LR-200-76)
The Nature Conservancy -
Written Comments

* * *

Section 1.170A-13(g)(5)(ii)

Comment: 1. The donee organization should not play a role at the time of the gift in determining the proportionate value of the donee's property rights. Otherwise, the donee will indirectly be playing a role in the valuation of the gift, a role that should be avoided at all times by the donee organization. Therefore, the regulations should be clarified to state that the determination of the value and of the proportionate value of the donee's property rights shall be the responsibility of the donor.

Comment: 2. The proportionate share of the proceeds to which the donee may be entitled must be "at least equal to the original proportionate value of the perpetual conservation restriction.” We think the regulations should be clear that the original proportionate value is the minimum that donee organization will receive, but that the donee organization will also receive the benefit of any increase in value when the donee interests increase based on changes in the market for such interests.

* * *

APPENDIX L

Ivins, Phillips & Barker
1700 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
(202) 393-7600

August 8, 1983

Commissioner of Internal Revenue
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Attention: CC:LR:T (LR-200-76)

Re: Proposed Regulation § 1.170A-13
Qualified Conservation Contributions

* * *

Paragraph (g)(5)(ii) may unnecessarily restrict the amount payable to the holder of an easement, if changes in surrounding territory have made the easement proportionately more valuable than the retained interest. The donee should be entitled to proceeds equal to the greater of its original proportionate value or its proportionate value at the time of the extinguishment.

* * *

APPENDIX M

Landmarks Preservation Council of Illinois
407 South Dearborn Street
Chicago, IL 60605 • 312-922-1742

July 20, 1983

Mr. Roscoe Edger, Commissioner
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Attn: CC:LR:T [LR-200-76]

* * *

(Page 22946-7 Federal Register:
Subsection (5) Extinguishment

(i) In general. If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined under paragraph (g)(5)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

(ii) Proceeds. In case of a donation made after (the date final regulations are published in the Federal Register), for a deduction to be allowed under this section, at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization, with a fair market value that is a minimum ascertainable proportion of the fair market value to the entire property. See §1.170A-13(h)(3)(iii). For purposes of this paragraph (g)(5)(ii), that original minimum proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions gives rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(5)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to the original proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.

LPCI opposes the inclusion of these two subsections of the proposed regulations on both general and specific grounds.

First, LPCI urges caution in the treatment of the concept of "extinguishment" in the regulations. A conservation right is an agreement between a donor and a donee organization to protect specified features of an historic property in perpetuity. The discussion in the regulations of the conditions under which that binding agreement may be abrogated lends an undesirable air of legitimacy to the concept of "extinguishment."

Second, these sctions of the regulations create a potential disincentive to the donation of easements. Because of their high land value, some of the most endangered historic properties are those located in the downtown commercial areas of many cities. At the same time, and because of the potential future value of the land without the restriction of an easement, owners of these properties are often reluctant to donate a preservation easement. LPCI suggests that Subsection (5)(ii) of these regulations creates an additional unneeded and undesirable disincentive to the donation of preservation easements.

Specifically, there are two immediately apparent problems related to the method stated in Subsection (5)(ii) for disposition of the proceeds after the sale or exchange of a property upon which an easement has been extinguished.

1. The obligation imposed on the donor or subsequent owner to pay to the donee organization an amount at least equal to the original proportionate value of the easement potentially places the donor at risk for an amount of money for which he may not be compensated by the disposition proceeds of sale. In other words, the donor's obligation to the donee organization under those circumstances is a constant proportion of value, which must be satisfied notwithstanding the claims of others, such as lenders, on the property.

2. The introduction of this formula based on the original fair market value of the easement adds a complicating factor to the problem of appraising easement value.

In view of these objections, LPCI suggests that the issue of the disposition of proceeds of sale or exchange of an easement property should not be treated in the regulations, but should be negotiated, defined, and incorporated by the donor and donee into the conservation right document on a property by property basis.

* * *

APPENDIX N

Trust for Public Land
82 Second Street
San Francisco, CA 94101

July 18, 1983

Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Attention: CC:LR:T (LR-200-76)

Re: Proposed Regulations – Qualified Conservation Contribution; Comments and Request for Public Hearing

* * *

5. §1.170A-13(g)(5)(ii) Proceeds. We have serious doubts whether the provision for the allocation of the proceeds of a sale following extinguishment of an easement could be enforced against anyone other than the original donor of the easement, if that is what is intended. If not, we suggest that the tax benefit rule is a satisfactory means of meeting any concern the IRS may have that a donor might receive the double benefit of an easement deduction followed by later recovery of the value donated. If the concern is to assure the perpetuity of the gift for conservation purposes, we think this provision goes further than the regulations need to go. The remote future event rule of §1.170A-13(g)(2) should suffice. The possibility that a conservation gift will become obsolete, although certain to be realized in some cases, must be negligible at the time a particular gift is made in order for it to qualify under the rule. The perpetuity requirement need demand no more than this.

* * *

APPENDIX O

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1, 20, 25, and 602

[T.D. 8069]

Income Taxes; Qualified Conservation Contributions

AGENCY: Internal Revenue Service, Treasury.

ACTION: Final regulations.

SUMMARY: This document contains find regulations relating to contributions not in trust of partial interests in property for conservation purposes. Changes to the applicable law made by the Temporary Tax Provisions, Extension and the Tax Reform Act of 1984 are reflected in this document. These regulations provide necessary guidance to the public for compliance with the law and affect donors and donees of qualified conservation contributions.

DATES: Except as otherwise provided in § 1.170A-14(g)(4)(ii), the regulations apply to contributions made on or after December 18, 1980, and are effective on December 18, 1980.

FOR FURTHER INFORMATION CONTACT: Ada S. Rousso of the Legislation and Regulations Division, Office of Chief Counsel, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224 (Attention: CC:LR:T), Telephone 202-588-3287 (not a toll free call).

SUPPLEMENTARY INFORMATION:

Background

On May 23, 1983, the Federal Register (48 FR 22940) published proposed amendments to the Income Tax Regulations (26 CFR Part 1) and Estate and Gift Tax Regulations (26 CFR Parts 20 and 25) under sections 170(h), 2055 and 2522 of the Internal Revenue Code of 1954 (Code). The amendments were proposed to conform the regulations to section 6 of the Temporary Tax Provisions, Extension (Pub. L 96-541, 98 Stat. 3206). A public hearing was held on September 15, 1983. Subsequent to the hearing, section 170(h)(5) of the Code was amended by section 1035(a) of the Tax Reform Act of 1964 (Pub. L. 98-309, 98 Stat. 1042). On December 10, 1984, the Service issued a news release (IR-84- 125) reminding taxpayers claiming deductions for donations of conservation easements that such deductions are limited to the fair market value of the easement at the time of the contribution. The news release further indicated that if the donation of the easement does not decrease the value of the property on which the easement is granted, the fair market value of the easement, and thus, the deduction, is zero.

After consideration of all comments regarding the proposed amendments and of the revision made by the Tax Reform Act of 1984, those amendments are adopted as revised by this Treasury decision.

Summary of Comments

Qualified Contribution of Entire Interest of Donor Other Than Qualified Mineral Interest

In response to many comments, regarding the donation of an entire interest of the donor other than a qualified mineral interest, proposed § 1.170A-14(b) has been revised to provide that section 170(h) will not disallow a deduction for a conservation contribution where the donor has previously transferred a portion of the entire interest unless the donor has purposefully reduced his interest before the contribution is made, for example. by transferring a portion to a related person in order to retain control of more than a qualified mineral interest.

Access

The final regulations have been revised to clarify the extent of public access required for each type of qualified conservation contribution under section 170(h). Thus, in order to qualify for a deduction under section 170(h), donations of property to preserve land areas for outdoor recreation by or for the education of the general public, for the preservation of a view, for the preservation of land pursuant to a governmenal conservation policy, or for the preservation of historic structures or land areas must provide for either physical or visual access. Examples have been included to clarify the public access requirement in specific circumstances.

Inconsistent Use

Section 1.170A-14(e)(2) provides that a deduction will not be allowed if a contribution would accomplish one of the enumerated conservation purposes but would permit impairment of other enumerated conservation interests. However, inconsistent use of the property is permitted if that use is necessary for the protection of the conservation interests that are the subject of the contribution. Commenters felt that the proposed regulations were not specific enough regarding permitted inconsistent uses. Therefore, the final regulations have been revised to include examples of certain uses that are not prohibited if, under the circumstances, they do not impair significant conservation interests. See § 1.170A-14(e)(2).

Third Party Mineral Rights

The proposed regulations provided that the interest in property that is retained by the donor (and the donor's successor in interest) must be subject to legally enforceable restrictions that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation. In addition, there was a prohibition against any method of mining on property that is the subject of a gift that would be inconsistent with the conservation purposes of the donation. Furthermore, a contribution was disallowed if at any time there may be surface mining on the property.

Many comments were received requesting relief from this rule because in many areas of the country, the mineral rights are not and may never have been owned by the donor; thus the donor cannot ensure that a third party owner of the mineral rights will not engage in surface mining on the property that is the subject of the gift.

Subsequent to publication of the proposed regulations, section 1035(a) of the Tax Reform Act of 1984 amended section 170(h)(5)(B) (relating to surface mining) to provide an exception to the general rule precluding a deduction for a conservation contribution if there is any likelihood of surface mining occurring at any time on the property to which the contribution relates. For conservation contributions made after July 18, 1984, the general rule with respect to surface mining will not apply to preclude a deduction if the surface estate and mineral interests were separated before June 13, 1976, remain so separated up to and including the time of the gift, and the probability of surface mining occurring on the property is so remote as to be negligible. Factors that may be considered in determining if the probability of surface mining is so remote as to be negligible are provided in the final regulations. In addition, the regulations provide that no deduction for a conservation contribution of the surface estate is permitted under this exception if the present owner is related to the owner of the surface estate at the time of the gift. Finally, these regulations clarify that any person may retain the mineral interest so long as the donor can guarantee observance of the restrictions to protect the conservation interests. See § 1.170A-14(g)(4) and the example thereunder.

Preservation of Open Space

In general, the statute provides that a donation of real property to preserve open space for conservation purposes (including farmland and forestland) will qualify as a deductible contribution if either of two tests are met: (1) The preservation must be pursuant to a clearly delineated governmental policy and must yield a significant public benefit, or (2) the preservation must be for the scenic enjoyment of the general public and must yield a significant public benefit. In connection with the first test. the final regulations retain the "sliding scale" approach adopted in the proposed regulations which is used to establish a relationship between the two requirements. Thus, although the requirements of governmental policy and public benefit must be met independently, the more specific the governmental policy with respect to a particular site to be protected, the more likely the governmental decision, by itself, will tend to establish the significant public benefit associated with the donation.

Commenters felt the regulations did not sufficiently clarify the standards under which deductions are allowed for the preservation of open space. Many of the comments received suggested revisions in the final regulations to provide donors with procedural “safe harbors” to avoid uncertainty regarding the deductibility of their donations. Commentators believed that without safe harbors, donors either will have to bear the expense of seeking advance rulings, or will risk additional tax liability if their deductions are later disallowed. Generally, the commenters suggested the following:

(1) A declaration by a unit of government identifying a particular property as worthy of protection should meet the clearly delineated governmental policy test and thus be sufficient to eliminate the need to meet the significant public benefit test.

(2) Acceptance of a donation by a unit of government (federal, state or local) or a duly constituted commission of such unit of government, should establish both a clearly delineated governmental policy and significant public benefit.

(3) A sliding scale approach should be extended to the relationship between scenic enjoyment of the general public and significant public benefit. Thus, the more scenic the view and the more people who see it. the more it tends to confer a significant public benefit.

(4) The regulations should encourage donations of farmland for agricultural uses by expanding references to the preservation of farmland to uses other than just the preservation of farmland pursuant to a state program for flood prevention and control. See § 1.170A-14(d)(4)(iv)(B). Commenters believed the reference was misleading because it implied that such

is the only use for which there can be a deductible donation of farmland.

(5) Acceptance of a donation by a qualified conservation organization should be conclusive evidence of deductibility. Because the Internal Revenue Service lacks the expertise to make the subjective determinations of "significant public benefit" and "scenic enjoyment", that responsibility should be delegated to either a private organization or to another governmental agency with acknowledged expertise in this area.

In general, the rules in the proposed regulations relating to open space easements have been retained in the final regulations. However, in response to the comments, some clarifications have been made regarding such easements. First, the fact that a unit of government has identified a particular property as worthy of protection does not by itself show the existence of a clearly delineated governmental policy, and thus, the significant public benefit associated with the donation must be independently demonstrated. Second, when there is a rigorous review of a donation by a unit of government or a duly constituted commission of a unit of government, the acceptance of a donation by such unit or commission of government tends to establish the clearly delineated governmental policy.

An example of a rigorous review process has been included in the final regulations. The more specific the governmental policy with respect to a particular site to be protected, the more likely it is that the governmental decision to accept the donation will tend, by itself, to establish the significant public benefit associated with the donation. A degree of certainty is available to donors in jurisdictions that have clearly articulated preservation policies, but as with any subjective test, there must ultimately be some exercise of judgment and responsibility by both donors and donees. Third, the terms "significant public benefit" and "scenic enjoyment" necessarily require a case-by-case factual determination and hence cannot be defined precisely. The list of factors included at 1.170A-14(d)(4)(iv) with respect to "significant public benefit" and § 1.170A-14(d)(4)(ii) with respect to "scenic enjoyment" are intended to be illustrative, rather than all-inclusive. In a particular case, other facts and circumstances may be relevant. Fourth, the regulations clarify that farmland, as recognized by the statute, is merely a category of open apace that must meet either of the two prescribed tests in order to be a deductible contribution. Finally, acceptance of a donation by a qualified organization is not conclusive evidence of the deductibility of a donation. The Internal Revenue Service has the responsibility for making final determinations as to the deductibility of donations. That responsibility cannot be delegated to a private organization or to another governmental agency, although the Service accords substantial weight to the determinations of qualified organizations and governmental agencies in its decision-making process.

Donations of Mortgaged Property

Section 170(h)(5) provides that the conservation purposes of the donation must be protected in perpetuity. The proposed regulations did not specifically address how this requirement applies to mortgaged property.

In response to comments received, the final regulations clarify that when a contribution of mortgaged property is made to a qualified organization, the mortgagee must subordinate its rights under the mortgage to the right of the qualified organization to enforce the conservation purposes of the gift in perpetuity. However, since certain donees, unaware of this clarification, accepted (or will have accepted) contributions of mortgaged property prior to February 12, 1986, without requiring subordination of the mortgagee's rights in the property, a donor will be allowed a deduction for such a contribution provided that the donor can demonstrate that the conservation purposes of the gift are protected in perpetuity absent subordination.

Valuation

Section 1.170A-14(h)(3)(i) of the final regulations has been revised to indicate that increases in the value of *any* property owned by the donor or a related person—not just contiguous property—resulting from the granting of a perpetual conservation restriction must be taken into account in determining the amount of the deduction.

Paperwork Reduction Act

The collection of information requirements contained in these regulations have been submitted to the Office of Management and Budget in accordance with the requirements of the Paperwork Reduction Act of 1980. These requirements have been approved by OMB.

Special Analyses

The Commissioner of Internal Revenue has determined that this final rule is not a major rule as defined in Executive Order 12291 and that a Regulatory Impact Analysis is therefore not required. Although a notice of proposed rulemaking which solicited public comments was issued, the Internal Revenue Service concluded when the notice was issued that the regulations are interpretative and that the notice and public comment procedure requirement of 5 U.S.C.

553 did not apply. Accordingly, the final regulations do not constitute regulations subject to the Regulatory Flexibility Act (5 U.S.C. chapter 6).

Drafting Information

The principal author of these regulations is Ada S. Rousso of the Legislation and Regulations Division of the Office of Chief Counsel, Internal Revenue Service. However, personnel from other offices of the Internal Revenue Service and Treasury Department participated in developing the regulations, both on matters of substance and style.

List of Subjects

26 CFR 1.61-1–1.281-4

Income taxes, Taxable income, Deductions, Exemptions.

26 CFR Part 20

Estate taxes.

26 CFR Part 25

Gift taxes.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR Parts 1, 20, 25, and 602 are amended as follows:

* * *

§ 1.170A-14 Qualified conservation contributions.

* * *

(g) *Enforceable in perpetuity.*—

* * *

(3) *Remote future event.* A deduction shall not be disallowed under section 170(f)(3)(B)(iii) and this section merely because the interest which passes to, or is vested in, the donee organization may be defeated by the performance of some act or the happening of some event, if on the date of the gift it appears that the possibility that such act or event will occur is so remote as to be negligible. See paragraph (e) of § 1.170A-1. For example, a state's statutory requirement that use restrictions must be rerecorded every 30 years to remain enforceable shall not, by itself, render an easement nonperpetual.

* * *

(6) *Extinguishment.* (i) In general. If a subsequent unexpected change in the conditions surrounding the property that is the subject of a donation under this paragraph can make impossible or impractical the continued use of the property for conservation purposes, the conservation purpose can nonetheless be treated as protected in perpetuity if the restrictions are extinguished by judicial proceeding and all of the donee's proceeds (determined under paragraph (g)(6)(ii) of this section) from a subsequent sale or exchange of the property are used by the donee organization in a manner consistent with the conservation purposes of the original contribution.

(ii) *Proceeds.* In case of a donation made after February 13, 1986, for a deduction to be allowed under this section at the time of the gift the donor must agree that the donation of the perpetual conservation restriction gives rise to a property right, immediately vested in the donee organization with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, hears to the value of the property as a whole at that time. See §1.170A-14(h)(3)(iii) relating to the allocation of basis. For purposes of this paragraph (g)(6)(ii), that proportionate value of the donee's property rights shall remain constant. Accordingly, when a change in conditions give rise to the extinguishment of a perpetual conservation restriction under paragraph (g)(6)(i) of this section, the donee organization, on a subsequent sale, exchange, or involuntary conversion of the subject property, must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction, unless state law provides that the donor is entitled to the full proceeds from the conversion without regard to the terms of the prior perpetual conservation restriction.