Preservation Easements, Preservation Laws, Property Rights & the Appraisal Process: Lessons from New Orleans, Nashville (and New York City)

Richard J. Roddewig, JD, MAI – Jones Lang LaSalle
Leah Tubbs – Preservation Resource Center of New Orleans
Jennifer Harrman – Historic Nashville, Inc.
Robin Zeigler – Nashville Metro Historic Zoning Commission
Preservation Easements and Preservation Ordinances

**QUESTION:** Why is the issue as to whether a preservation easement is stronger than a local landmark law so critical?
Preservation Easements and Preservation Ordinances

ANSWER: Such a comparison has been a critical part of the appraisal process since the early 1980s and was recognized in the first Tax Court case dealing with valuation of a preservation easement -- *Hilborn* decision in 1985 -- as a key element of the valuation analysis.
Preservation Easements & Preservation Ordinances

- Session Overview
  - Preservation Easements – Property Rights Affected
  - Central Highest and Best Use Issues in Preservation Easement Appraisals
  - The New Orleans & Nashville Experiences with the Interplay Between Easements & Preservation Codes
  - Legal Permissibility – Easements & Ordinances Compared – Lessons from NYC
Preservation Easements: Topic One
What Is a Historic Preservation Easement?

UTOPIA HOTEL
ADDED TO HISTORIC NASHVILLE’S LIST OF PRESERVATION EASEMENTS
Topic 1: What is a Historic Preservation Easement?

- What is a preservation easement?
  - Essential legal element – gives a third party (other than an adjacent property owner) some control over or use of another’s property
  - Other names – easement in gross, equitable servitude, preservation covenant, preservation restriction
  - Terminology varies from state to state depending on state law
Topic 1: What is a Historic Preservation Easement?

- What is a preservation easement?

  - Typical provisions
    - Review of exterior alterations
    - Review of proposed demolitions
    - Review of additions – vertical & horizontal
    - Mandatory scheduled inspections
    - Mandatory insurance coverage
    - No hardship exception
    - Legal right to enforce terms in court of law
Topic 1: What is a Historic Preservation Easement?

- What is a preservation easement?
  - Contractual agreement – signed by property owners and easement holder
  - Recorded in the title record
  - “Runs with the land” – binds future owners
  - Gives the easement holder a legally enforceable “real property interest”
  - Imposes obligations on property owner
Topic 1: What is a Historic Preservation Easement?

☐ What is a preservation easement?

- Contractual agreement – can be for a few weeks, a few months, a few years, or “in perpetuity”
- DOES NOT HAVE TO BE IN PERPETUITY
- Must be in perpetuity in order to take a charitable contribution deduction for the effect of the easement on the value of the historic property
Preservation Easements: Topic Two
Highest and Best Use Issues
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Four Elements of Highest and Best Use Analysis
  - What uses are legally permissible?
  - What uses are physically possible?
  - What uses are financially feasible?
  - Of the physically possible, legally permissible & financially feasible uses, which use provides the highest present value? (and is reasonably probable)
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Highest and Best Use Analysis must be conducted both “before” and “after” considering the provisions in the Historic Preservation Easement – at least in appraisals to support the value of the charitable donation of the easement
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Many preservation easement appraisal assignments involve properties already protected by local historic preservation codes.
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Critical HABU Question 1 – Does the preservation easement merely duplicate restrictions on property rights already imposed by the local historic preservation code?
Topic 2: Highest and Best Use in Preservation Easement Appraisals

Appraisals and legally permissible uses

- Compare the types of changes, alterations and repairs made reviewable by landmark laws to those reviewable under the easement

- Compare enforcement authority and process

- Compare past pattern of enforcement of landmark laws to effectiveness of monitoring and enforcement by holder of the preservation easement
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Critical HABU Question 2 – Do preservation easement provisions prohibiting/limiting vertical or horizontal additions merely duplicate property right restrictions already created by the local historic preservation code or imposed by the existing local zoning code?
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

Appraisals and legally permissible uses

- Compare the pre-easement zoning & historic preservation restrictions to the additional restrictions imposed by the easement

- Are there:
  - Additional restrictions on height and setbacks?
  - Additional restrictions on front, side, and rear yards?
  - Additional restrictions on subdivision?
  - Restrictions on right to sell or transfer development rights?
  - Additional restrictions on uses?
Topic 2: Highest and Best Use Issues in Preservation Easement Appraisals

- Downtown zoning FAR provisions typically allow new buildings much taller & bulkier than historic structures.
Preservation Easements: Topic Three – Easement Programs & Preservation Codes in Nashville & New Orleans: Some Comparisons
Topic 3: Preservation Easements in New Orleans & Nashville

- Questions for the Panel
  - How many easements do PRC & Historic Nashville hold?
  - What types of properties are protected? Primarily residential? Primarily commercial? Both?
  - Does your organization have a regular monitoring process & schedule?
  - Can your organization enter the property to check structural integrity?
  - Do your organizations have an endowment fund to monitor & enforce the easements?
  - Is there a dedicated staff responsible for monitoring?
Topic 3: Preservation Easements in New Orleans & Nashville

Questions for the Panel

- Are any of your easements in locally designated historic districts or on locally designated individual landmarks?
- If so, what is the definition of “alterations” reviewable under the easement and what “alterations” are reviewable by the local historic preservation commission?
- When reviewable by both the easement holder and the local preservation commission, is there coordination between the two bodies in the review process?
- Has there ever been disagreement between the two bodies – e.g., easement holder rejects a proposed alteration but the preservation board OKs it?
Topic 3: Preservation Easements in New Orleans & Nashville

Questions for the Panel

- Has there ever been disagreement between the two bodies – e.g., easement holder rejects a proposed alteration but the preservation board OKs it?
Topic 3: Preservation Easements in New Orleans & Nashville

Questions for the Panel

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Topic 3: Preservation Easements in New Orleans & Nashville

Questions for the Panel

- Can owners of easement properties seek relief from your easement based on “economic hardship”?
- Can owners of locally designated historic properties seek relief from the local preservation code based on a claim of “economic hardship”?
- Has an owner of an easement property ever requested your organization to extinguish the easement?
- Has an owner of a locally designated historic property ever requested to be “de-designated”?
- Has your easement organization ever gone to court to enforce an easement? Or stop the city from issuing a permit to an easement protected property?
Topic 3: Preservation Easements in New Orleans & Nashville

Questions for the Panel

- Can enforcement costs be imposed on owners of easement protected properties?
- Can the local preservation board impose enforcement costs on owners of locally designated properties?
Preservation Easements: Topic Four – Lessons from New Orleans & Nashville
Topic 4: Preservation Easements: Lessons from New Orleans & Nashville

 Leah Tubbs – Preservation easement enforcement in New Orleans in the wake of Hurricane Katrina
Topic 4: Preservation Easements: Lessons from New Orleans & Nashville

- Robin Zeigler – Historic Zoning in Nashville

HANDBOOK AND DESIGN GUIDELINES
Preservation Easements: Topic Five – The Courts and the IRS Positions on Property Rights in Easement Appraisals

Form 8283
(Rev. December 2014)
Department of the Treasury
Internal Revenue Service
IRS contends that preservation easements merely duplicate protections already provided by local historic preservation laws and landmark designation.
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- This IRS contention first appeared in 2005 IRS release on alleged easement abuses
- Then IRS market studies in New York City and Washington, D.C. reiterated this point
- IRS has more recently made this contention in briefs, filings and oral arguments in Tax Court cases
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- IRS NYC & D.C. studies claim:
- Easements have “zero value”
- Easements merely duplicate local preservation laws
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

Key Tax Court Question -- Do preservation easements have an adverse effect on market value even if the property is already protected by a local historic preservation law?

Inconsistent Tax Court Case Law Answers
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

Do Preservation Easements Affect Value Even When Locally Protected?

- Griffin v. Commissioner -- Yes (1990) (Mixed Use)
- Dorsey v. Commissioner – Yes (1990) (Office)
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

Do Preservation Easements Affect Value Even When Locally Protected?

- Simmons v. Commissioner – Yes (2011) (Res. Townhouse)
- Reisner v. Commissioner – No (2014) (Res. Townhouse)
- Scheidelman v. Commissioner - No (2014) (Res. Townhouse)
- Whitehouse Hotel v. Commissioner – Yes (2014) (Hotel/Retail)
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- **Hilborn v. Commissioner case, 1985**
  - First Tax Court case involving valuation of a preservation easement
  - Tax Court ruled that a New Orleans preservation easement on a property already protected by strong historic preservation laws resulted in a 10% impact on value
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- **Hilborn** case from 1985
  
  Tax Court stressed that in analyzing value after the easement: “The easement’s terms and covenants are examined, individually and collectively, and compared to existing zoning regulations and other controls (such as local historic preservation ordinances) to estimate whether, and the extent to which, the easement will affect current and alternative future uses of the property.”
Topic 5. Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- **Whitehouse Hotel LP case**

- **Tax Court decision:**
  - Landmark designation and easements
    - Landmark designation may adversely impact value pre-easement
    - A 10% adjustment to comparables based on difference in landmark designation status is appropriate
Topic 5. Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- **Whitehouse Hotel LP case (cont.)**

- **Tax Court decision:**
  - Tax Court easement value conclusion is equivalent to a 14.82% impact on “before” easement value
  - Court applied this only to a portion of the complex
  - Court did not consider impact on highest and best use as Ritz-Carlton Hotel
Topic 5. Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- *Simmons v. Commissioner*
  - Two rowhouses in D.C.
  - Both in designated D.C. historic districts
  - Easements donated to L’Enfant Trust
  - Photo: 17 Logan Circle
Simmons v. Commissioner

IRS Position

- Zero value to easements
- Because both rowhouses already protected by D.C. preservation laws
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- *Simmons v. Commissioner*

- **Tax Court Ruling**
  - L’Enfant Trust’s easement imposes “higher level of enforcement” than D.C. preservation laws
  - A zero valuation appraisal is NOT “credible”
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

- *But see Chandler v. Commissioner*
  - Tax Court Ruling

- Despite legal differences between Boston’s preservation code & the easement, “a typical buyer would perceive not differences between the two sets of applicable restrictions.”

- Similar conclusion in *Kaufman v. Comm’n.*
Topic 5: Preservation Easements & Preservation Ordinances: The Courts & the IRS Position

Given the Tax Court inconsistency, what should appraisers do?

- Research the protections & policies of the local preservation board or commission
- Research the manner in which the easement holder has monitored/enforced easements
- Compare the two programs – are there situations similar to New Orleans?
- If there are differences, analyze the market effect using “paired sales” analysis
Topic Six: Preservation Easements & Preservation Ordinances: Lessons from the New York City Experience
Topic 6: Lessons from New York City Experience

- IRS New York City market study conclusion about the legal comparison
  - “The presence of a façade easement on a residential property located in a historic district does not excuse the property owner from maintaining and performing repairs on the façade in accordance with regulations imposed by the New York City Landmarks Preservation Commission and New York City Department of Buildings. Overall, the cost burden is no less than if the façade easement did not exist.”
Topic 6: Lessons from new York City Experience

- IRS New York City market study legal conclusions (continued)
  - “All the owners of residential properties located in New York City who have made façade easement donations are subject to existing regulations addressing façade maintenance and preservation rules established by the New York City Landmarks Preservation Commission and New York City Department of Buildings that, for all intent and purposes, are no less onerous than those made by the donation receiving party.”
Topic 6: Lessons from New York City Experience

- Easement organization rebuttal to the IRS New York City market study legal conclusions

RESPONSE TO THE METROPOLITAN VALUATION SERVICES REPORT:

“Study on the Impact of a Façade Easement on the Fair Market Value Of a Townhouse-Type Property in the City of New York For calendar Years 2003 Through 2007”

Prepared For
Dana M. Fidazzo
Venable LLP
750 East Pratt Street, Suite 900
Baltimore, Md. 21202
Topic 6: Lessons from New York City Experience

• Rebuttal Report

• “IRS Valuation Study is seriously flawed”

• IRS study “contains a great deal of misinformation about the workings of both the LPC and the Trust, and omits much important information about both organizations.”
Topic 6: Lessons from New York City Experience

• Rebuttal Report (cont.)
• Most significant difference between preservation easements and NYC Preservation Commission rules “is the discretion reserved for the LPC’s Commissioners.”

• That discretion “can have a significant impact on how a property may be developed.”
Topic 6: Lessons from New York City Experience

• Rebuttal Report (cont.)
• The NYC landmarks law “explicitly defers to the commissioners’ discretion—which supersedes rules, guidelines, and staff recommendations.”

• “There is no equivalent to this discretion in the case of . . . preservation easements.”
Topic 6: Lessons from New York City Experience

- Rebuttal Report (cont.)
- Compares NYC landmarks law & Title 63 regs to easements on such issues as:
  - Vertical (rooftop) additions
  - Modifications of doorways & windows
  - Demolition approvals
  - Projects approved by LPC then disapproved by National Architectural Trust
Topic 6: Lessons from New York City Experience

• Rebuttal Report (cont.)

• Hearst International Building (951-969 Eighth Avenue 36-story addition – Commission approved it because the original 6-story base was designed with “structural support for the addition of several stories”
Topic 6: Lessons from New York City Experience

- Rebuttal Report (cont.)
- 1217 Park Avenue – addition approved by LPC
Topic 6: Lessons from New York City Experience

• Rebuttal Report (cont.)

• Upper East Side rowhouse example

• March 2007 LPC issues a C of A for exterior alterations including installation of new cast-stone cornice & relocation of main entrance – work would be compatible with other buildings in district

• Building also subject to a preservation easement but work began before easement holder knew about the permit

• NAT issues a stop work order – NAT disapproved the work under Secretary of the Interior’s Standards
Topic 6: Lessons from New York City Experience

- Rebuttal Report (cont.)

- Upper East Side Historic District rowhouse example

[Images: Existing condition and Proposed condition]
Topic 6: Lessons from New York City Experience

- Rebuttal Report (cont.)
- Upper West Side/Central Park West Historic District rowhouse example
  - Owner changes an original doorway without a permit
  - LPC issues a warning letter in March 2007
  - April 2007 LPC issues a Permit for Minor Work to legalized the prior work
  - Property protected by an easement – owner had not sought NAT approval
  - Building also subject to a preservation easement but work began before easement holder knew about the permit
  - NAT issues a stop work order – required owner to replace the improper door approved by the LPC with a door that matched the original removed door
Topic 6: Lessons from New York City Experience

- Rebuttal Report (cont.)

- Upper West Side/Central Park Historic District rowhouse example

- NAT required unauthorized door to be replaced

Removed door

Unauthorized door
Topic 6: Lessons from New York City Experience

- Amster Yard
- Protected by New York Landmarks Conservancy Easement
- Buyer demolished rear portion without approval from Conservancy
Topic 6: Lessons from New York City Experience

- Amster Yard (cont.)
- NY Landmarks Conservancy enforced the easement & required the demolished section to be rebuilt according to original plans and photos
Topic 6: Lessons from New York City Experience

- Other New York City issues related to protection provided by landmarks law & Title 63 rules
  - LPC staff & budgetary shortages
  - Sheer number of protected buildings (in excess of 24,000) – but only two full-time enforcement staff
  - Unable to monitor/inspect buildings on a regular basis
  - Demolition by neglect
  - Building Department “snafus”

- By contrast, easement holders monitor & inspect every easement protected building annually
Topic 6: Lessons from New York City Experience

- Building Department “snafus” and confusion
- 54 State Street, Brooklyn Heights District
- Building Department in 2006 failed to note it was in a district – granted permit for demolition of stoop, front entryway, windows, & interior occurred without review by LPC
Topic 6: Lessons from New York City Experience

- Other New York City issues related to protection provided by landmarks law & Title 63 rules
  - Politics and economic development issues can outweigh preservation issues
  - 17 successful “hardship” applications
  - 9 designated landmarks have been demolished following hardship hearings

- By contrast, owners of easement protected buildings cannot seek exceptions based on economic hardship
Topic Seven: Preservation Easements & Preservation Ordinances: Summary of the Legal Differences Between Preservation Easements and Preservation Ordinances
Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

- Is the IRS contention that preservation easements merely duplicate protections already provided accurate?

- AI Easement Book has detailed comparison list
## Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

<table>
<thead>
<tr>
<th>Landmark Laws</th>
<th>Historic Easements</th>
</tr>
</thead>
<tbody>
<tr>
<td>□ Subject to amendments and repeal</td>
<td>□ Typically not subject to amendment/repeal</td>
</tr>
<tr>
<td>□ Include right to appeal denial of an alteration or demo permit</td>
<td>□ No right to appeal denial of an alteration or demo request</td>
</tr>
<tr>
<td>□ Typically not recorded</td>
<td>□ Recorded restriction</td>
</tr>
<tr>
<td>□ Subject to economic hardship exceptions</td>
<td>□ Not subject to any hardship exception</td>
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### Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

<table>
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<th><strong>Landmark Laws</strong></th>
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<tbody>
<tr>
<td>□ Enforcement costs paid by local government</td>
<td>□ Enforcement costs paid by property owner</td>
</tr>
<tr>
<td>□ Outside legal standing to enforce is limited</td>
<td>□ Standing to enforce due to recorded deed</td>
</tr>
<tr>
<td>□ Legal right to require restoration following casualty is limited</td>
<td>□ Absolute right to require restoration following casualty</td>
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### Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

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<thead>
<tr>
<th>Landmark Laws</th>
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<tbody>
<tr>
<td>- No mandatory inspection by licensed professional</td>
<td>- Mandatory licensed professional inspection on regular schedule</td>
</tr>
<tr>
<td>- No interior inspections</td>
<td>- Interior inspections</td>
</tr>
<tr>
<td>- No right to require insurance</td>
<td>- Mandatory insurance requirements</td>
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<td>- Typically no restriction on subdivision</td>
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<td>Mandatory licensed professional inspection on regular schedule</td>
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<td>No interior inspections</td>
<td>Interior inspections</td>
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<th>Historic Easements</th>
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</thead>
<tbody>
<tr>
<td>□ Do not create a “property interest”</td>
<td>□ Create a “property interest”</td>
</tr>
<tr>
<td>□ Subject to constitutional challenges based on due process, equal protection, &amp; regulatory taking claims</td>
<td>□ Not subject to constitutional challenges</td>
</tr>
<tr>
<td>□ Politics involved</td>
<td>□ Not subject to politics</td>
</tr>
</tbody>
</table>
Topic Eight: Conclusion – Preservation Easement Appraisals Today
Topic 8: Preservation Easement Appraisals Today

- Appraising Preservation Easements Today
  - Especially challenging
  - High likelihood of IRS review
  - Risk of overvaluation penalties
  - Due to number of easement properties, research and analysis of actual sales of easement properties increasingly possible
Topic 8: Preservation Easement Appraisals Today

To understand effect of a preservation easement on “fair market value” the appraiser must:

Compare the legal restrictions “before” imposition of the easement to any additional legal restrictions imposed by the preservation easement

Determine how the marketplace of buyers and sellers react – in terms of prices paid -- to legal restrictions imposed by preservation laws to those imposed by preservation easements

As part of the “before and after” approach to value
Topic 8: Preservation Easement Appraisals Today

Appraisals and legally permissible uses

- Compare the types of changes, alterations and repairs made reviewable by landmark laws to those reviewable under the easement
- Compare enforcement authority and process
- Compare past pattern of enforcement of landmark laws to effectiveness of monitoring and enforcement by holder of the preservation easement
Topic 8: Preservation Easement Appraisals Today

- Key questions related to strength of an easement program
  - How strong financially is the organization?
  - How many easements does it hold?
  - How long has it had an easement program?
  - What are the criteria for easement acceptance?
  - What are the enforcement policies?
  - Does the group have a dedicated endowment for enforcement?
Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

- Key questions related to strength of an easement program (cont.)
  - Does the group have an easement committee?
  - Who enforces the easement? Paid staff?
  - Does it have the financial and professional resources to enforce its easements?
  - How effectively has it managed its program and enforced easements in the past?
  - Does it meet with potential buyers of easement encumbered properties?
Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

“Matched pairs” analysis can now be done in many cities given the number of preservation easements

- New Orleans
- New York City
- Chicago
- Charleston
- Boston
- Many others
Topic 7: Legal Differences Between Preservation Easements and Preservation Ordinances

“Matched pairs” & Sale/Resale analysis

**Discussion Question 10-1.3.** Based on your analysis of the marketplace, you prepare the following adjustment grid for the paired sales. Calculate the easement impact as indicated by each sales comparison, and fill in the chart. What is the indicated range in impact of the easement from the paired sales adjustment grid?

<table>
<thead>
<tr>
<th>Address</th>
<th>Easement Sale: 1100 Highlands</th>
<th>Paired Sale No. 1: 1050 Oak</th>
<th>Paired Sale No. 2: 910 Oak</th>
<th>Paired Sale No. 3: 900 Highlands</th>
<th>Paired Sale No. 4: 1210 Highlands</th>
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<tbody>
<tr>
<td>Sale</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
<td>No</td>
<td>No</td>
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<tr>
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<td>$750,000</td>
<td>$850,000</td>
<td>$900,000</td>
<td>$773,000</td>
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<tr>
<td>Date</td>
<td>3 months ago</td>
<td>6 months ago</td>
<td>1 year ago</td>
<td>Current</td>
<td>18 months ago</td>
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<tr>
<td>Market</td>
<td>3.0%</td>
<td>6.0%</td>
<td>12.0%</td>
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<td>18%</td>
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<td>Conditions</td>
<td>Adjustment</td>
<td>Time Adjusted Price</td>
<td>$901,250</td>
<td>$795,000</td>
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<tr>
<td>Lot Size</td>
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<td>Zoning</td>
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<td>Same</td>
<td>Same</td>
<td>Accounted for in Lot Adjustment</td>
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<tr>
<td>Garage</td>
<td>NA</td>
<td>Same</td>
<td>-$10,000</td>
<td>-$20,000</td>
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<tr>
<td>Condition &amp;</td>
<td>NA</td>
<td>Same</td>
<td>Same</td>
<td>-$40,000</td>
<td>+$30,000</td>
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<tr>
<td>Age Adjustments</td>
<td>-$10,000 for Corner lot</td>
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<td>None</td>
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<td>Indicated</td>
<td>Easement Impact</td>
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**Discussion Question 10-1.5.** Based on the paired sales analysis, what would be your conclusion concerning the impact of the preservation easement? How would you incorporate the result of your analysis into a “Sales Comparison Approach” after considering the preservation easement on the 565 Maple Street property that is the actual subject of the appraisal?
Topic 8: Preservation Easement Appraisals Today

- Where Are We Today and What Is Still Needed to Be Done?

- Preservation easements will continue to be an important tool for saving and protecting significant historic and architectural treasures.
Topic 8: Preservation Easement Appraisals Today

Where Are We Today and What Is Still Needed to Be Done?

The appraisal courses and the Appraisal Institute book should become more of a guide for both the IRS and taxpayer appraisers (as well as Tax Court judges) to lessen controversies over appraisal issues.