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Conservation Easement Appraisals and Highest and Best Use Analysis: Lessons from Recent US Tax Court Decisions

Abstract

In recent years, the number of charitable donations of conservation easements has surged. Much of the activity has involved syndicated conservation easements. Each donation requires an appraisal to support the value of the gift. Both Congress and the Internal Revenue Service as well as the US Department of Justice have challenged appraisal reports supporting these values in hundreds of recent syndicated conservation easement donations. The highest and best use analysis is the central focus in many of the challenges. This article revisits the 2020 US Senate Report concerning abusive appraisals supporting syndicated conservation easements; it then discusses the "before" value highest and best use issues raised in three recent US Tax Court cases involving donations of conservation easements. The article then addresses sources of information for appraisers asked to undertake conservation easement appraisals and concludes with a summary of ten lessons for appraisers regarding highest and best use issues in the three tax court decisions.

Introduction: Types of Properties Qualifying for a Charitable Gift of a Conservation Easement

Prior to 1976, federal tax laws made it difficult to donate a partial interest in real property, such as an easement, and take a charitable contribution deduction for the value of the donation. Amendments to the Internal Revenue Code in 1969 had limited the charitable deduction involving real property—with only a few exceptions—to situations in which the donation involved the taxpayer's entire interest in the property. However, the Tax Reform Act of 1976 modified the charitable donation rules to allow a charitable contribution deduction for a "lease,…option to purchase, or easement" to a qualifying organization "exclusively for conservation purposes." I.R.C. § 170(f)(3)(B)(iii).[1]

The "conservation purposes" for which an easement may be donated include the preservation of land areas for outdoor recreation, the protection of ecosystems or natural habitats, open space preservation for scenic enjoyment of the public, and the preservation of a "historically important land area" or a "certified historic structure."[2] As a result of the inclusion of historically important land areas and some types of historic structures in the allowable conservation purposes, donations of historic preservation easements are also covered under the definitions of a "perpetual conservation restriction" in the Internal Revenue Code and its implementing Treasury Regulations.[3]

1. For more information on these early easement acquisition programs, see Richard J. Roddewig and Charles T. Brigden, *Appraising Conservation and Historic Preservation Easements*, 2nd ed. (Appraisal Institute and Land Trust Alliance, 2020), Chapter 2, p. 9, citing William H. Whyte's seminal book, *The Last Landscape*.
2. See IRC Code 170(h)(4)(A) and Treas. Reg. § 1.170A-14(d).
3. See 26 CFR § 1.170A-14(b).

To better assure the quality and essential content of conservation and historic preservation easement appraisal reports, the Tax Reform Act of 1984 included language requiring every charitable donation of a conservation restriction with a value in excess of $5,000 to be supported by a "qualified appraisal" report completed by a "qualified appraiser."[4] A 2023 article in *The Appraisal Journal* discussed the minimum content that an appraisal must contain to meet the "qualified appraisal" requirements.[5]

Syndicated Conservation Easement Donations and IRS Notice 2017-10

In 2016, the Internal Revenue Service (IRS) noticed a significant increase in the number of individual tax returns claiming a charitable deduction for the donation of a conservation easement. IRS reviews of 2015 and 2016 tax returns identified more than 400 syndicated partnerships in which the partners were claiming a share of a charitable deduction of the value of a conservation easement.[6] IRS staff review appraisers became concerned about the content of many of the appraisal reports supporting those syndications.

As a result of those concerns, the Treasury Department issued IRS Notice 2017-10 in December of 2016.[7] That notice described syndicated conservation easement donations as "tax avoidance transactions" and classified them as "listed transactions," a designation that creates significant reporting requirements for the syndicators and their "material advisors."[8] According to the Internal Revenue Service in IRS Notice 2017-10, an essential element of the promotional tax avoidance scheme is an appraisal "that greatly inflates the value of the conservation easement based on unreasonable conclusions about the development potential of the real property."[9]

The 2020 Senate Committee on Finance Report on Inflated Appraisals in Syndicated Conservation Easement Donations

In March of 2019, the Senate Committee on Finance launched its own investigation into syndicated conservation easements and issued its report in August of 2020. The report states that "an inflated appraisal" is the "engine of every syndicated conservation easement transaction."[10] Actual conservation easement appraisal reports

4. Although the terms "qualified appraisal" and "qualified appraiser" were added to the Tax Code in 1984, it was not until the Treasury Department later issued implementing regulations that the minimum content of a "qualified appraisal" was clearly set forth. The regulations related to those terms could be found at Treas. Reg. §1.170A-13(c) (3) and (c)(5) until July 30, 2018, and are now at §1.170A-17(a) and (b).

5. See Richard J. Roddewig and Anne S. Baxendale, "The Evolution of Land Trust Responsibilities in Reviewing Conservation Easement Appraisals," *The Appraisal Journal* (Issue 2–3, 2023): 116.

6. Committee on Finance, United States Senate, "Syndicated Conservation-Easement Transactions: Bipartisan Investigative Report as Submitted by Chairman Grassley and Ranking Member Wyden," August 2020, 116th Congress, 2nd Session, S. Rpt. 116-44, at 3. Available at bit.ly/49aEfaY.

7. In November of 2022, the US Tax Court set aside Notice 2017-10 because, in the court's opinion, the IRS had not complied with proper administrative procedures before issuing the notice. See *Green Valley Investors, LLC v. Commissioner*, 59 T.C. No. 5. The IRS has responded with proposed regulations that restate the essence of Notice 2017-10 and are being proposed in accordance with the Administrative Procedures Act.

8. All "material advisors" involved in listed transactions must file an IRS Form 8918 Material Advisor Disclosure Statement. Information to be provided to the IRS and IRS Notice 2017-10 requires material advisors involved in conservation easements "to report to the IRS any conservation easement transactions that include (1) promotional materials, (2) pass-through entity attracting investors, and (3) charitable contributions that equal or exceed 250% of the investors' initial investment as well as (4) the contribution and deduction." Also, "'material advisors' are defined as those who provide 'material aid, and assistance or advice' about the transaction and receive at least $10,000 in compensation." Roddewig and Brigden, *Appraising Conservation and Historic Preservation Easements*, 2nd ed., at page 30, citing 26 CFR 301.6111-3(b)(3)(i)(B).

9. Internal Revenue Service. Listing Notice—Syndicated Conservation Easement Transactions. Notice 2017-10, at page 2. Available at bit.ly/4nkfGfl.

10. See Committee on Finance, United States Senate, "Syndicated Conservation-Easement Transactions: Bipartisan Investigative Report as Submitted by Chairman Grassley and Ranking Member Wyden," August 2020, 116th Congress, 2nd Session, S. Rpt. 116-44, at 6. Available at: bit.ly/4ozcjCc.

were critiqued in detail by the committee. The most common red flag in those appraisals indicating a likely overvaluation was "a consistent pattern of land (or interest in a partnership holding land) sold in an arm's length transaction, followed shortly thereafter by an appraisal asserting land values multiple times higher than the value established in that prior arm's length transaction." That, according to the Senate Committee on Finance, "clearly calls into question the accuracy of these appraisals."[11]

The Senate Committee on Finance Report pointed to the following three components of the faulty appraisals it reviewed as driving the overvaluations: (1) failure to properly summarize and analyze the recent purchase price of the land; (2) an improper claim that some type of land development was the highest and best use; and (3) supporting the value for development with a faulty discounted cash flow (DCF) analysis.[12]

This article addresses how those three aspects of faulty conservation easement appraisals identified by the Senate Committee on Finance Report play out in three recent US Tax Court cases that reviewed the "before" value highest and best use analyses in conservation easement appraisal reports.

Recent US Tax Court Cases Involving Internal Revenue Service Challenges to Conservation Easement Valuations

In the aftermath of IRS Notice 2017-10 and the Senate Committee on Finance Report, the Internal Revenue Service (IRS) has reviewed hundreds of partnerships related to syndicated conservation easements. As of October 2024, the chief judge of the US Tax Court estimated there were over 1,000 docketed cases in the US Tax Court involving conservation easements.[13] While the focus of many of the cases is a challenge based on alleged lack of compliance with various reporting requirements related to the tax returns themselves or whether the donation meets the "conservation purposes" test, challenges based on the highest and best use issues identified in the Report of the Senate Committee on Finance are at the heart of many of the cases.

The US Tax Court has begun to hear those cases, and the decisions of the court have begun to emerge. Among those recent decisions[14] are the following three discussed in this article:

- *Savannah Shoals, LLC, Green Creek Resources, LLC, Tax Matters Partner, Petitioner v. Commissioner of Internal Revenue*, United States Tax Court, Served May 17, 2024, T.C. Memo. 3412-12
- *Green Valley Investors, LLC, Petitioner, et al. v. Commissioner of Internal Revenue*, United States Tax Court, Served February 11, 2025, T.C. Memo. 2025-15
- *Ranch Springs, LLC, Ranch Springs Investors, LLC, Tax Matters Partner, Petitioner v. Commissioner of Internal Revenue*, United States Tax Court, Docket No. 11794-21, Filed March 31, 2025

The *Savannah Shoals* Case, the *Green Valley* Case, and the *Ranch Springs* Case: An Introduction

The decisions in the three cases discussed in this article are complex. This article focuses on aspects of the decisions related to highest and best use analysis. There is much more in each of the cases related to the details in the appraisals submitted by the appraisers and other experts for the taxpayers and the IRS at the trials related to the fair market value of the donated conservation easements.

11. See Committee on Finance (August 2020), id., at 11.

12. For more on the Senate Finance Committee Report and its detailed discussion of an actual appraisal report involving a conservation easement donation in Alabama, see Roddewig and Baxendale, "Evolution of Land Trust Responsibilities," 116, at 124–125.

13. Jason Hanson, "Easement Bottleneck Confuses Path to Settlement or Litigation," *Bloomberg Tax* (December 3, 2024), bit.ly/3WdmvEi (accessed October 20, 2025).

14. Among the other tax court decisions issued since January of 2024 involving the valuation of conservation easement donations are the following: *Oconee Landing Property, LLC, Oconee Landing Investors, LLC, Tax Matters Partner v. Commissioner of Internal Revenue*, T.C. Memo. 2024-25; *Buckelew Farm, LLC v. Commissioner of Internal Revenuer*, T.C. Memo. 2024-52; *Excelsior Aggregates, LLC, Big Escambia Ventures, LLC, Tax Matters Partners, et al. v. Commissioner of Internal Revenue*, T.C. Memo 2024-60; *Corning Place Ohio, LLC, Corning Place, Ohio Investment, LLC, Tax Matters Partners v. Commissioner of Internal Revenue*, T.C. Memo. 2024-72; *Jackson Crossroads, LLC, Greencone Investments, LLC, Tax Matters Partner v. Commissioner of Internal Revenue*, T.C. Memo. 2024-111; and *Seabrook Property, LLC, Seabrook Manager, LLC, Tax Matters Partner v. Commissioner of Internal Revenue*, United States Tax Court, Filed January 21, 2025.

A 2023 article in *The Appraisal Journal* discussing land trust responsibilities when reviewing conservation easement appraisals summarized the four-step process involved in highest and best use analysis as follows:

> Highest and best use analysis in both the "before" and "after" easement valuation scenarios involves answering the following questions:
> 1. What uses are physically possible?
> 2. Of the physically possible uses, which ones are legally permissible?
> 3. Of the physically possible and legally permissible uses, what uses are financially feasible?
> 4. And, finally, which of the uses that are physically possible, legally permissible, and financially feasible results in the "highest present value"?[15]

Sometimes the sequence starts with legally permissible uses rather than physically possible uses. The result of that analysis is the use that would result in the "most probable" price that a "willing buyer would pay a willing seller," and that most probable price equates to the fair market value of the property. That type of four-step process is completed both "before" considering the provisions in the conservation easement document and then again "after" considering the easement document.

In each of the three cases, the appraisals submitted by the taxpayer to support the donation claimed to utilize the "before and after" approach to value. In that method, the highest and best use and market value of the entire property is first analyzed "before" considering the provisions in the recorded conservation easement. The provisions in the easement document are then considered, and the highest and best use and market value are reconsidered. The difference between the "before" value (disregarding the provisions in the easement document) and the "after" value (considering the easement provisions) is the fair market value of the conservation easement donation. The three tax court decisions discuss whether that method was properly applied by the taxpayer's appraiser in each case.

There are a number of commonalities between the three cases, including the following four items:

- First, the taxpayer's appraisal in each of the three cases concluded that quarrying was the highest and best use of the property before considering the conservation easement, but the tax court disagreed with that conclusion.
- Second, in each of the three cases, the taxpayer's appraiser applied a DCF analysis to support the "before" value of the property and the feasibility of limestone or granite quarrying as the highest and best use. According to the US Tax Court, the taxpayer's appraiser in each of the three cases then based the "before" value on the going concern value of the business that could be conducted on the property rather than on the value of the real estate on which the business would be conducted.
- Third, each of the cases involved appraisals or valuation testimony at trial that the tax court concluded disregarded prices paid for properties in the same market area that also were located above the same type of granite or limestone.
- Fourth, in all three cases the tax court concluded that the 40% overvaluation penalty for a "gross valuation misstatement" should be imposed on the taxpayer.[16]

The conservation easement in the *Savannah Shoals* case was donated in December of 2017 on 103 acres in Hart County, Georgia. The appraisal completed to support the charitable donation indicated a "before" value of $23.1 million based on a conclusion that the highest and best use of the property was as an aggregate quarry. The fair market value conclusion "after" considering the conservation easement was $103,000, indicating an easement value of $23 million.[17] At the tax court trial, the taxpayer's appraisal expert testified that the "before" easement value was $21,075,000 based on quarrying as the highest and best use, and the "after" value was $290,000, indicating an easement value of $20,785,000.[18]

The conservation easement in the *Green*

15. Roddewig and Baxendale, "Evolution of Land Trust Responsibilities," 126.
16. Treasury Regulations § 6662(h) imposes a 40% penalty on the taxpayer for a gross valuation misstatement when the claimed value is 200% or more of the amount determined by the tax court to be the correct value.
17. T.C. Memo. 3412-12, 13.
18. *Ibid*., 15.

Valley case was donated in December of 2014 on 136.12 acres in Chatham County, North Carolina. The appraisal completed to support the charitable donation indicated a "before" value of $22,559,000 based on a conclusion that the highest and best use of the property was as an aggregate quarry. The fair market value conclusion "after" considering the conservation easement was $250,000, indicating an easement value of $22,310,000, rounded.[19]

The tax court's thumbnail summary of the "before" values involved in the *Ranch Springs* case donation is as follows:

> [The] LLC had acquired the land for $6,500 per acre in December 2016. In December 2017 an appraiser hired by LLC valued the land at $236,673 per acre, asserting that its highest and best use (HBU) was limestone mining. Relying on this appraisal, LLC on its 2027 return claimed a charitable contribution deduction of $25,814,000 for a qualified conservation contribution under I.R.C. § 170(h).[20]

"Before" Value Highest and Best Use Issues in the *Savannah Shoals* Case

Physically Possible Use Issues

There is little focused discussion in the *Savannah Shoals* opinion on issues related to the physically possible uses "before" considering the easement. The property was "heavily wooded with rolling to steep terrain" and had no public road frontage. It was accessed "by a right of way via a dirt road."[21] A previously planned development project had failed on the larger parcel that included the 103 acres on which the easement was donated. The failed development plan had proposed a 325-lot subdivision on the entire larger parcel. The development had received county approvals, and some grading had been done and a guard house built. However, only five lots had been sold, and no homes had been built. There had been no physical work done to the 103-acre portion of the entire property.[22] The work had stopped as a result of the 2008 recession, resulting in the inability of the developer to obtain financing.

As to the physical possibility of aggregate mining, some exploration work had been done. Four exploratory test holes had been drilled on the property, and core samples of the underlying rock were tested. One of the experts for the taxpayer concluded that the testing indicated the rock "met the South Carolina and Georgia Departments of Transportation's requirements for crushed rock aggregate that is used for road base."[23] At trial, there was testimony based on the prior analysis that there were approximately 32 million tons of "subsurface aggregate" under the surface and that the "proposed quarry could produce 19.6 million tons of aggregate over 30 years."[24] Another earlier report referenced in the decision indicated that a "40-acre quarry could produce 10.5 million tons of aggregate over 25 years."[25]

The tax court decision does not discuss the implications of the testing and testimony concerning the underlying "subsurface" for a highest and best use analysis and conclusion. However, the court stated in a footnote that it was inappropriate for one of the geology experts to describe the aggregate on the property as a "mineral reserve" or "mineral resource." Both of those terms, the court said, "have special meanings in the mining industry," and can only be applied if a "feasibility study" has been completed. The court stated that the drilling and testing that had been done on the core samples "do not satisfy the industry guidelines for a feasibility study that is required to declare either a mineral resource or a mineral reserve."[26]

Legally Permissible Use Issues

The "legal permissibility" prong of the four-step highest and best use test is only briefly discussed in the tax court's decision in the *Savannah Shoals* case. The decision describes Hart County, where the property is located, as "largely rural and agricultural," and indicates that the county did not have any zoning laws and had no ordinances on

19. T.C. Memo. 2025-15, 8, 20.

20. 164 T.C. No. 6, Filed March 31, 2025, 1.

21. T.C. Memo. 3412-12, 3.

22. *Ibid*., 3.

23. *Ibid*., 6–7.

24. *Ibid*., 14.

25. *Ibid*., 7.

26. *Ibid*., 7, n. 11.

the books that prohibited or regulated mining. As a result, an aggregate quarry was a "legally permissible use" of the property on the date that the easement was donated. The county approved developments as they were proposed based on "land use ordinances" that seem, from the court's brief reference, to be enacted based on each particular development that is proposed. The court stated that "[t]he county might have imposed a 120- to 180-day moratorium so that it could enact an ordinance regulating mining."[27]

However, the State of Georgia had significant permitting requirements for mining, and the county would "defer" to the state's procedures related to mining permits.[28] The court summarized those state requirements as follows:

> The county would defer to the procedures of the Environmental Protection Division (EPD) of the Georgia Department of Natural Resources to regulate the development and operation of a quarry. Shoals would have been required to obtain EPD permits including permits relating to stormwater and wastewater discharge, surface and ground water withdrawal, and air quality to operate a quarry.[29]

The decision did not include any further discussion of the likelihood that the state would or would not issue its required permits or the probability that the county would adopt an ordinance allowing mining. Instead, it moved on to a discussion of the financial feasibility of aggregate mining on the subject property.

Financially Feasible Use Issues

The tax court said the following about the aggregate mining financial feasibility analyses submitted by the taxpayer's appraisal and mining experts:

> We find that petitioner's experts severely overestimated demand for aggregate and failed to account for existing supply in the market. Accordingly, we find that their production and sales projections far exceeded likely production and sales. Petitioner's experts failed to account for the fact that competing quarries had substantial delivered price advantages over the proposed quarry because of their locations. As a result, petitioner's experts' production and sales projections were overly optimistic. We find that it is highly unlikely that the market would have supported their profitability conclusions. We find that a proposed quarry was not financially feasible.[30]

Discounted Cash Flow Analysis Issues

The taxpayer's appraisal and mining experts based the "before" value conclusion on a DCF analysis. An IRS quarrying expert at trial critiqued the DCF analysis of the taxpayer's expert. The taxpayer's DCF analysis indicated a "net present value ranging from $21.1 to $27.6 million," while the IRS expert's critique resulted in a "net present value of $2.9 million."[31] The differences were based on disagreements related to "production and sales projections, the amount of overburden that would need to be removed and the costs to remove and store it, the time required to obtain mining permits and its impact on production and sales in the first year of the proposed quarry, the quality of the aggregate, operating costs, and capital costs."[32]

Based on a comparison of the DCF analyses of the competing experts, the tax court concluded that it found "significant flaws in the discounted cash flow analyses performed by petitioner's experts, and the quarry was not financially feasible."[33] However, the tax court opinion does not discuss those flaws in any detail because it concluded that the basic problem in the taxpayer's DCF analysis was that it "overestimated demand for aggregate and failed to account for existing supply in the market."[34] It summarized the basis for that conclusion as follows:

> Petitioner's experts failed to account for the fact that competing quarries had substantial delivered price advantages over the proposed quarry because of their locations. As a result, petitioner's experts' production and sales projections were overly optimistic. We find it

27. *Ibid*., 8.
28. *Ibid*., 8.
29. *Ibid*., 8.
30. *Ibid*., 38.
31. *Ibid*., 38.
32. *Ibid*., 38.
33. *Ibid*., 38.
34. *Ibid*., 38.

> is highly unlikely that the market would have supported their profitability projections.[35]

In a footnote, the court noted that the taxpayer's DCF analysis resulted in a 67% operating profit margin compared to an industry average profit margin of only 24%.[36] The court also commented in another footnote that given the population living within a 25-mile radius of the property, the proposed quarry would have had to capture between 40% and 60% of the demand for aggregate, a target that the court described as "unlikely."[37]

Those deficiencies in the DCF analysis stemmed from the failure of the taxpayer's DCF analyses to take into account five important factors:

1. Competition from other quarries located closer to the population centers generating the demand for aggregate
2. The aggregate prices at the competing quarries that were lower than the prices in the taxpayer's DCF analysis
3. The transportation cost advantage of those competitive quarries located closer to their target market
4. The excess capacity at one of the principal competitive quarries
5. An overly optimistic estimate of the demand for aggregate in the target market.[38]

"Before" Value Highest and Best Use and Market Value Conclusion by the Tax Court

The tax court in the *Savannah Shoals* case concluded that the highest and best use before considering the conservation easement was "low-density residential and recreational uses" and not aggregate mining. Based on actual sale prices for land in the county where the property was located as well as on the actual price of $515,000 paid for a 92% interest in the 103-acre property, the tax court concluded that the fair market value "before" considering the conservation easement was $580,000[39] and not $21,075,000, as claimed based on quarrying as the highest and best use as asserted by the appraisal expert for the taxpayer.

"Before" Value Highest and Best Use Issues in the *Green Valley* Case and Tax Court Decision

Legally Permissible and Physically Possible Use Issues

The *Green Valley* court referenced testimony from various geology and mining experts presented by both the taxpayer and the IRS and concluded that the testimony indicated "no genuine dispute" that aggregate mining on the Green Valley property was both physically and legally possible. The court added the following explanation:

> The parties agree that construction aggregate of sufficient quality exists on this property and that rezoning the property was a strong possibility. Accordingly, we will accept that a construction aggregate mine at the Green Valley property is a physical and legal possibility.[40]

The court did state, however, that on the date the easement was donated, the property did not have a mining permit although it had applied for one from the State of North Carolina, but that application was subsequently withdrawn.[41] The only statement about applicable zoning as it relates to mining in the decision is a simple statement by the court that the "Green Valley property had no zoning limits."[42]

Financially Feasible Use Issues

To determine whether the Green Valley property's highest and best use was as a construction aggregate mine, the court looked carefully at the testimony related to whether the property's use for quarry operations was financially feasible. The court concluded that the annual production estimate of one of the taxpayer's mining experts was not supportable because the radius of the primary

35. *Ibid*., 38.
36. *Ibid*., 43, n. 41.
37. *Ibid*., 42, n. 40.
38. *Ibid*., 42.
39. *Ibid*., 47.
40. T.C. Memo. 2025-15, 25.
41. *Ibid*., 32, 7.
42. *Ibid*., 31.

market area was significantly smaller than estimated by the taxpayer's expert.[43] The court also emphasized the "difficulty" of "entry into the construction aggregate market…due to the sensitivity of construction aggregate pricing and competition from large, experienced companies."[44] The court also described as "compelling" the testimony of a geologist from the Department of the Interior who stated "abundant competition" and "high transportation costs of aggregate were significant entrance barriers to the development" of the Green Valley property as an aggregate quarry.[45]

Discounted Cash Flow Analysis Issues

The *Green Valley* court says it made some "conservative adjustments" to the DCF analysis submitted at trial by an expert for the taxpayer that decreased the net present value result from $23 million to $10 million, and after making further adjustments, "the net present value is reduced to nearly zero."[46] However, the tax court decision does not explain the adjustments it made, so how the court arrived at a net present value close to zero cannot be determined from the decision.

The tax court also describes some of the inputs in a DCF analysis done by an appraiser retained by the taxpayer who testified at trial. That DCF resulted in a net present value before considering the conservation easement of $15,900,000.[47] Once again, however, the tax court does not discuss how it would have adjusted the inputs into that DCF analysis to arrive at a conclusion that the net present value should have been close to zero.

"Before" Value Highest and Best Use Conclusion by the Tax Court

The tax court in the *Green Valley* case concluded that there was no "adequate proof" that the "proposed development of this [Green Valley] property as a quarry mine is both financially feasible and maximally productive," and in such a situation when there is no "adequate proof" then the "property's highest and best use is presumed to be its current use."[48] As a result, the court concluded that the highest and best use of the Green Valley property before considering the conservation easement "remains its current agricultural/residential/recreational use with knowledge of minerals on the site and the opportunity to seek entitlements allowing for mining on the site." Based on actual sale prices for unpermitted land sales with the potential for mining, the tax court concluded that the fair market value "before" considering the conservation easement was between $1,371,000 and $1,426,699 and not $15.9 million to $23.9 million as claimed in the two appraisal reports relied on by the taxpayer and based on a highest and best use for quarrying.[49]

"Before" Value Highest and Best Use Issues in the *Ranch Springs* Case and Tax Court Decision

The tax court judge hearing the *Ranch Springs* case described the fact pattern as "painfully familiar."[50] As in both the *Savannah Shoals* and *Green Valley* cases, the taxpayer's appraisal claimed the highest and best use of the 110-acre farmland property before the donation of the conservation easement was development as a quarry.[51]

Legally Permissible Use Issues

The "legal permissibility" prong of highest and best use analysis was the focus of much of the tax court's opinion. These involved first, the reasonable probability of obtaining a zoning change to allow mining, and second, the reasonable probability of obtaining the needed approvals from various state and federal agencies.

43. *Ibid*., 26–27.

44. *Ibid*., 26.

45. *Ibid*., 28.

46. *Ibid*., 26.

47. *Ibid*., 18.

48. *Ibid*., 29.

49. *Ibid*., 33.

50. 164 T.C. No. 6, Filed March 31, 2025, 3.

51. *Ibid*., 3.

The zoning of the property, however, permitted only "agricultural and light residential use."[52] No application for a rezoning to allow limestone mining was ever filed. Instead, the taxpayer commissioned a letter from a law firm that stated "'there is a reasonable probability that the Property can be rezoned to M-1 [Industrial] and issued a special exception that allows for mining, as long as there is not strong neighbor opposition to the mining request.'" That letter also indicated that the prospect for approval of the zoning change and special exception application "would be 'influenced heavily by the amount of support or opposition by neighbors of the subject Property.'"[53]

Despite the importance of support or opposition of neighboring property owners to the mining approval process, neither the property owner nor "its agents" "did any outreach to immediate neighbors" or other residents of the area to gauge the level of support or opposition.[54]

Permits to operate a quarry were also needed from the Alabama Department of Environmental Management (ADEM) as well as from the US Environmental Protection Agency and the US Fish and Wildlife Service. The property owner never applied for those required approvals.

The appraisal report filed with the IRS to support the $25.8 million easement value did not discuss any of these zoning and permitting issues. Instead, according to the tax court, the appraisal included the "'extraordinary assumption' that 'all necessary permits including those related to zoning could be obtained to operate a mine on the property.'"[55]

At the trial, two members of the zoning commission as well as the mayor testified that there would have been strong opposition by neighboring property owners to a quarry.

Based on all that, the tax court concluded that obtaining rezoning was not reasonably probable.

Physically Possible Use Issues

The tax court decision does not specifically comment on physically possible issues related to the Ranch Springs property. It does, however, discuss the investigation into the limestone deposits on the property. At trial, the IRS submitted testimony from two geologists who agreed that the "modest exploratory work" that had been done involving "data from drilling nine boreholes and one corehole to a depth of 225" indicated that "the limestone beneath the Ranch Springs Property could be classified only as an 'inferred mineral resource.'"[56]

Financially Feasible Use Issues

The tax court concluded that "use of the property as a limestone quarry was not financially feasible" because the income and expense projections in the feasibility study submitted to support the "before" value were "wildly optimistic."[57] The court reviewed information submitted at trial related to the other competing quarries in the surrounding counties that indicated there was "plenty of unused production capacity"[58] and that "existing players can capture new demand much faster and more easily than a greenfield site—i.e., raw land that had never been mined—that would take years to get up and running."[59]

The tax court also pointed to inaction by the owners of the Ranch Springs property involving other nearby properties they owned as evidence that limestone mining was *not* financially feasible. The owners had experience in mining, owned mining equipment, and had access to capital, but never pursued permits for limestone mining on "any of the ten nearby properties they acquired,

52. *Ibid.*, 3.

53. *Ibid.*, 14–15.

54. *Ibid.*, 16.

55. *Ibid.*, 24.

56. *Ibid.*, 49.

57. *Ibid.*, 46.

58. The tax court decision referenced trial testimony indicating that one nearby competitive quarry could only sell 85% of the limestone it could produce and another nearby quarry was operating at only 55% to 60% of capacity two years before the date of the easement donation and "well below capacity" in 2016 when the Ranch Springs property sold for only $6,500 per acre. (164 T.C. No. 6, Filed March 31, 2025, 46)

59. 164 T.C. No. 6, Filed March 31, 2025, 46.

all of which were situated over the same limestone formation."[60]

Discounted Cash Flow Analysis Issues

The taxpayer's appraiser "constructed a DCF spreadsheet to estimate the *NPV* [net present value] of operating a limestone business on the property for 35 years."[61] The tax court in the *Ranch Springs* decision does not adequately explain the various revenue and expense inputs that went into the model, nor does it discuss the discount rate used. Because it had already decided that quarrying was not "reasonably probable" in the near future under its analysis of the legally permissible uses in its highest and best use analysis, it did not have to critique the DCF model itself.

It did, however, include a detailed discussion of other tax court cases discussing the appropriateness of DCF analysis. It described the DCF method attempted by the appraiser for the property owner as a variant on the "income capitalization method" and then said the following about its appropriate use:

> The income method is most reliable when used to determine the value of an existing business, with a track record of growth, income, expenses, and profits. A historical track record of this sort provides a plausible basis for projecting future revenue. The income approach is rarely appropriate when seeking to determine the value of raw land or other undeveloped property with no existing cashflow.[62]

Equating the Value of a Future Operating Quarry with the Value of the Land

The three cases have another aspect in common that is also an issue in many if not most of the recent syndicated conservation easement valuation cases in the tax court. In each case, the taxpayer claimed a deduction based on the value of something that did not yet exist. For example, in the *Ranch Springs* decision, the tax court said the taxpayer and its appraiser were "[e]quating the assumed value of the hypothetical mining business to the value of the land."[63] The court said such an "equation defies economic logic and common sense."[64]

In fact, the attorneys for the taxpayer in the *Ranch Springs* case argued to the tax court that such a deduction was indeed appropriate because the "'willing buyer/willing seller' test, which governs the valuation of property for charitable contribution purposes generally, does not apply when the donated property is a conservation easement."[65] Instead, the taxpayer's attorneys argued that the fair market value of a perpetual conservation restriction is the value of the "'property rights sacrificed,'" and that equated to the value of the "right to construct and operate a limestone quarry." Therefore, according to the taxpayer, the value of the easement should be the value of the "hypothetical limestone quarry."[66]

The court summarily dismissed that argument, stating there is no case law precedent for such a position and stating that the "willing buyer/willing seller" test has been cited in "dozens of cases dating back many decades."[67] The Treasury regulations require the deduction to be based on a comparison of the "before and after" value of the land itself. It is not based on the property rights that the owner of the land has theoretically "lost" as measured by the value of the business that might have been conducted by the donor in the absence of the conservation easement.

The *Ranch Springs* court summed up its review of the valuation method and conclusions in the taxpayer's appraisal report as "'an outrageous overstatement' wholly untethered from reality."[68]

In the *Green Valley* case, the tax court empha-

60. *Ibid*., 46.
61. *Ibid*., 55.
62. *Ibid*., 55.
63. *Ibid*., 55.
64. *Ibid*., 57.
65. *Ibid*., 62.
66. *Ibid*., 63.
67. *Ibid*., 63.
68. *Ibid*., 3.

sized the connection between highest and best use analysis and selection of the appropriate valuation method:

> We find the question of income approach versus sales comparison approach is largely predicated upon our determination of the property's highest and best use. In other words, our conclusion as to the property's highest and best use and whether the property is income producing (hypothetically or not) will lead to a more informed conclusion as to whether the income approach or a different approach to value is most appropriate.[69]

Sources for Information on Generally Accepted Methods of the Appraisal Profession Related to Conservation Easement Appraisal

Appraisers involved in conservation easement appraisal assignments must look to standards of professional practice for the appropriate methods to apply. Standards Rule 1-1 of the Uniform Standard of Professional Appraisal Practice (USPAP) states clearly that "In developing a real property appraisal, an appraiser must: (a) be aware of, understand, and correctly employ those recognized methods and techniques that are necessary to produce a credible appraisal."

The Comment to Standards Rule 1-1 states the following:

> Changes and developments in the real estate field have a substantial impact on the appraisal profession….To keep abreast of these changes and developments, the appraisal profession is constantly reviewing and revising appraisal methods and techniques and devising new methods and techniques to meet new circumstances. For this reason, it is not sufficient for appraisers to simply maintain the skills and knowledge they possess when they become appraisers. Each appraiser must continuously improve his or her skills to remain proficient in real property appraisal.[70]

The Scope of Work Rule of USPAP sets forth the requirement that an appraiser must "determine and perform the scope of work necessary to develop credible assignment results." The Scope of Work Rule then states that the appraisal methods applied must not simply be based on what the appraiser has done in the past. Instead, the appraisal must be performed based on "what an appraiser's peers' actions would be in performing the same or a similar assignment."[71]

How does an appraiser determine what the actions of the peers would be? Frequently Asked Question 170 in the *USPAP Guidance and Reference Manual* asks that question and then states that "[i]n USPAP, 'appraiser's peers' has a specific meaning." It goes on to state that USPAP defines this meaning as "other appraisers who have expertise and competency in a similar type of assignment," and adds the following explanation:

> Knowledge about what an appraiser's peers would do in a similar assignment comes through being a participant in the profession. Typical forums that allow appraisal professionals to share information about practice include appraisal journals and publications, professional meetings and conferences, education through courses and seminars, and appraisal discussion groups.[72]

Between the 1930s and 1970s, there was little in the appraisal literature related to the appropriate techniques for the appraisal of conservation and historic preservation easements. That changed dramatically in the late 1970s and early-to-mid 1980s in the wake of a series of changes to the Internal Revenue Code allowing for the donation of partial interests in properties, including conservation easements donated in perpetuity.[73] Articles began to appear on a

69. T.C. Memo. 2025-15, 25.

70. The Appraisal Foundation, *Uniform Standards of Professional Appraisal Practice (USPAP)*, effective January 1, 2024 (The Appraisal Foundation, 2024), 18, lines 500–510.

71. The Appraisal Foundation, *USPAP* (effective January 1, 2024), 20.

72. The Appraisal Foundation, *USPAP Guidance and Reference Manual*, effective January 1, 2024 (The Appraisal Foundation, 2024), 212.

73. The sequence of legislation resulting in this change included the Tax Reform Act of 1976, additional legislation in 1977, and the Tax Treatment Extension Act of 1980. That last bill required that conservation easements be donated in perpetuity to be deductible.

regular basis in *The Appraisal Journal*,[74] and conservation and historic preservation groups joined with the American Bar Association to hold annual legal continuing education programs focused (in part) on appraisal issues involved in supporting conservation easement donations.[75] In addition, the appraisal profession and the land trust movement jointly published a booklet entitled *Appraising Easements: Guidelines for Valuation of Historic Preservation and Land Conservation Easements*.[76]

Ten Lessons for Conservation Easement Appraisers in the Three Recent Tax Court Decisions

There are various lessons that conservation easement appraisers should take away from a review of these tax court decisions.

Lesson 1: Consider All Four Steps in Highest and Best Use Analysis

Although the tax court in each of the three cases discussed in this article does not specifically address the "physically possible use" element of a proper highest and best use analysis, there is discussion of physically possible uses buried in the discussion of the other elements of highest and best use analysis. Physically possible use issues may be more central in other types of conservation easement valuation assignments, such as in assignments in which subdivision development is a possible "before" value highest and best use. Other tax court decisions involving conservation easements claimed to limit subdivision of the property have focused on physical aspects of the property that affect subdivision analysis.[77]

Lesson 2: Do Not Confuse the Highest and Best Use "Before" Considering the Easement with the Potential Future Value of a Development Project on the Property[78]

The *Ranch Springs* decision made it very clear that the fair market value of the conservation easement is not equal to the value of the "property rights sacrificed." It is the effect of the restrictions in the conservation easement document on the value of the land on which the easement is imposed. Although the easement may prohibit all kinds of development opportunities, the prices paid for land with similar physical characteristics and development possibilities determine how the marketplace values those future possibilities.

Lesson 3: Do Not Confuse the Value of a Future Business with the Current Value of the Land on Which the Future Business Will Operate

Lesson 3 is a variant on Lesson 2. Distinguishing between the value of a business operated on a parcel of real property and the value of the real property itself has long been a thorny issue in real estate appraisal theory and practice. Hotel and motel appraisal assignments are the most common situations in which issues related to the distinction between business value and real estate value can be central. Much has been written over

74. See, for example, Judith Reynolds, "Preservation Easements," *The Appraisal Journal* (July 1976): 355; Ralph Brown and Jerome Schmitz, "Appraising Wetland Easements," *The Appraisal Journal* (April 1978): 175; Jared Shlaes and Richard J. Roddewig, "Appraising the Best Tax Shelter in History," *The Appraisal Journal* (January 1982): 25; Lawrence J. Golicz, "Historical Façade Easements: the Impact of Future Costs," *The Appraisal Journal* (January 1984): 9; Richard J. Roddewig and Jared Shlaes, "Preservation Easements Reconsidered: An Alternative Approach to Value," *The Appraisal Journal* (July 1984): 325; and Max J. Derbes, Jr., "Façade Easement Valuation Methodology," *The Appraisal Journal* (January 1988): 60. One earlier *Appraisal Journal* article appeared in the 1960s that was also influential: Howard Williams and W. D. Davis, "Effects of Scenic Easements on the Market Value of Real Property," *The Appraisal Journal* (January 1968): 15. See also William Cantrell, "Scenic Easements: Evaluation Considerations," *The Real Estate Appraiser and Analyst* (Summer 1983): 61.

75. For a discussion of some of these various conferences and programs, see Roddewig and Brigden, *Appraising Conservation and Historic Preservation Easements*, 377–379.

76. The National Trust for Historic Preservation and the Land Trust Exchange, *Appraising Easements: Guidelines for Valuation of Historic Preservation and Land Conservation Easements* (Preservation Press, 1984).

77. See, for example, *Thayer v. Commissioner*, T.C. Memo 1977-3120, one of the earliest tax court cases involving the valuation of a conservation easement; *Boltar, et al. v. Commissioner*, 136 T.C. No. 14; and *Mountanos v. Commissioner*, T.C. Memo 2013-138.

78. Another recent US Tax Court decision involving the donation of a historic preservation easement also has significant commentary on this issue. The fair market value of the easement was based on what the court in that decision described as a "structurally impossible" and "economically unsound" hypothetical 34-story addition to an existing 11-story historic building. *Corning Place Ohio, LLC, v. Commissioner of Internal Revenue*, T.C. Memo. 2024-72.

the past three decades on that issue in hotel and motel valuation assignments.[79]

The same considerations apply when considering a future business that might be conducted on a parcel of land. The net income of the future business, even when properly analyzed to deduct stabilized operating costs, return to improvements, and entrepreneurial profit, may not necessarily equate to the market value of the underlying land as determined by prices paid for land with the potential to be developed for such a business use.

For sand and gravel or hard rock or aggregate quarry properties, such as those considered to be the highest and best use before the easement in the three cases discussed in this article, the royalty rate method is typically used to determine the contributory value of the underlying land to the value of the mining or quarry business. "The royalty is a dollar amount per ton of extracted material."[80]

Although the royalty rate method of valuing land devoted to quarrying was not discussed in either the *Savannah Shoals* or *Green Valley* decisions, it was discussed in some detail in the *Ranch Springs* decision. One of the experts who testified in the *Ranch Springs* case explained how the method would be applied as follows:

> The royalty income method, he explained, values the property by 'discount[ing] the stream of projected royalty income to a present value.'" To implement this methodology, '[a]n appropriate royalty rate and associated discount rate must be extracted from the market and used to capitalize the royalty income.[81]

The tax court indicated that the application of that method would result in a land value that was 10% or less of the "before" value of the property as determined by the experts for the taxpayer based on future development as a quarry. The court then concluded that it was demonstrated that "[N]o rational mine operator would pay the entire *NPV* of the prospective mining business to purchase the land if he could acquire access to the minerals by lease for 10% or less of that sum."[82]

The *Ranch Springs* court, however, did not then conclude that the easement value should be about 10% of the quarry-based "before" value conclusion in the taxpayer's appraisal report. The reason for not using such a royalty rate analysis discounted to a present value is due to the skepticism about the reliability in general of the DCF method expressed by the tax court judges in all three cases.

Lesson 4: The Owner of the Easement-Protected Property Is Not Entitled to a Charitable Donation Deduction for Potential Future Lost Profits from a Hypothetical Future Business

Lesson 4 is related to the prior two lessons.

In Footnote 17 in the *Green Valley* decision, the tax court repeated language from the *Savannah Shoals* decision that fair market value must be based on "the price that a willing buyer and a willing seller would agree to," and it was "not convinced that a quarry operator would pay the aggregate's net present value for the land as there would be no means for a profit." In doing that, the court said, the taxpayer's appraisal "ignored the regulatory definition of fair market value."[83]

In the *Ranch Springs* decision, the tax court commented that the price paid for "raw land" is just one of the costs "that would need to be incurred in constructing the hypothetical mining business" and then asked the following rhetorical question: "Why would a rational investor pay the entire *NPV* [net present value] of the mine's future operations in order to defray one component cost?"[84]

Those comments by the tax court judges should be a warning to appraisers to carefully compare the result of an income capitalization approach to value with the prices paid for properties in the market area with a similar highest and best use as a check on their value conclusion.

79. See, for example, Stephen Rushmore and Karen E. Rubin, "The Valuation of Hotels and Motels for Assessment Purposes," *The Appraisal Journal* (April 1984): 270–288; and William D. Siegel, "Separating Business Enterprise Value from Real Estate Value," in David C. Lennhoff (ed.), *A Business Enterprise Value Anthology*, 2nd ed. (Appraisal Institute, 2011), 93–95.

80. Thomas W. Hamilton and Jan A. Sell, "Use of the Income Approach in Valuing a Sand and Gravel Property in a Condemnation Proceeding," in Lennhoff (ed.), *A Business Enterprise Value Anthology*, 2nd ed., 211.

81. 164 T.C. No. 6, Filed March 31, 2025, 59.

82. *Ibid*., 59.

83. T.C. Memo. 2024-35, 45.

84. 164 T.C. No. 6, Filed March 31, 2025, 57.

Lesson 5: Be Extra Careful When Relying on Discounted Cash Flow Analysis

Discounted cash flow analysis is defined in *The Dictionary of Real Estate Appraisal* as follows:

> The procedure in which a discount rate is applied to a set of projected income streams and a reversion. The analyst specifies the quantity, variability, timing, and duration of the income streams and the quantity and timing of the reversion, and discounts each to its present value at a specified yield rate.[85]

There is nothing inherently wrong with using DCF analysis in an appraisal report on land that has some development potential, such as for residential subdivision development, and the Appraisal Institute's book *Appraising Conservation and Historic Preservation Easements*, Second Edition, recognizes its importance in appropriately supported feasibility analysis.[86]

Advisory Opinion 33 in USPAP says the following about the importance of DCF analysis:

> DCF analysis has become a requirement of many real property clients and other intended users. These users of appraisal services favor the inclusion of DCF analysis as a management tool in projecting cash flow and return expectations, capital requirements, refinancing opportunities, and timing of future property dispositions. DCF analysis is regarded as one of the best methods of replicating steps taken to reach many investor buy/sell/hold decisions and is often a part of the exercise of due diligence in the evaluation of an asset.[87]

The tax court decision in the *Savannah Shoals* case and in the *Green Valley* case did not reject DCF analysis as an inappropriate method to apply in a conservation easement valuation appraisal. It simply noted flaws in methods as applied in the taxpayer's appraisal reports in both cases.[88] The *Ranch Springs* decision, however, went further and said DCF analysis "is rarely appropriate when seeking to determine the value of raw land or other undeveloped property with no existing cash-flow."[89] Note that the court did not say DCF analysis is *never* appropriate to use but instead is *rarely* appropriate to use. In a footnote, the tax court provided some more context to its view as to when the discounted present value resulting from a DCF analysis is appropriate and when it is not:

> Theoretically, an *NPV*-oriented method might be employed in an effort to estimate the value of the land, but only if all other value inputs were stripped out so as to isolate the value of the land. But it would seem illogical to conjure an imaginary business with myriad hypothetical inputs and outputs just to back into a purported value for the land. An objective appraiser would not turn to an *NPV*-oriented method given its inherent uncertainties, especially where comparable land sales are plentiful.[90]

The *Ranch Springs* decision also describes the application of the DCF method to be "inherently speculative and unreliable" when there is "the absence of a financial track record" related to the business income generated by the property being appraised.[91] However, in other cases, the tax court has approved a DCF analysis[92] even in at least some situations where there was no existing track record of income generated by the subject property. For example, in *Trout Ranch v. Commissioner*,[93] the lot sales that went into the DCF analysis of both experts and the tax court itself were not from the subject property on which the easement was granted but instead from sales at another subdivision project in the same market

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85. Appraisal Institute, *The Dictionary of Real Estate Appraisal*, 7th ed. (Appraisal Institute, 2022), 54.
86. Roddewig and Brigden, *Appraising Conservation and Historic Preservation Easements*, 2nd ed., 165–167.
87. The Appraisal Foundation, *USPAP Guidance and Reference Manual*, 2024 ed. (The Appraisal Foundation, 2024), 96.
88. T.C. Memo. 3412-12, 38; and T.C. Memo. 2025-15, 31.
89. 164 T.C. No. 6, Filed March 31, 2025, 55.
90. *Ibid*., 60, n. 23.
91. *Ibid*., 41.
92. Chapter 22 of *Appraising Conservation and Historic Preservation Easements*, 2nd ed. (2020) lists the following cases in which the tax court's valuation conclusion was based in whole or in part on a DCF analysis: *Symington v. Commissioner* (87 T.C. 892); *Stotler v. Commissioner* (T.C. Memo 1987-275); *Clemens v. Commissioner* (T.C. Memo 1992-436); *Schwab v. Commissioner* (T.C. Memo 1994-232); *Kiva Dunes Construction LLC v. Commissioner* (T.C. Memo 2009-145); *Trout Ranch v. Commissioner* (T.C. Memo 2010-283); *Crimi v. Commissioner* (T.C. Memo 2013-51); and *Schmidt v. Commissioner* (T.C. Memo 2014-159).
93. T.C. Memo. 2010-283.

area. In fact, in the *Trout Ranch* decision, the tax court judge constructed his own DCF analysis based on pieces of information in both the taxpayer and IRS expert testimony.

The lesson from the three cases is, at least in conservation easements involving mining or quarrying, that appraisers should be extra cautious in relying on a DCF analysis as the primary valuation method. Although the decision does not discuss why the tax court judge in the *Trout Ranch* case considered it appropriate to apply a DCF analysis even when the subject property had no track record of sales, perhaps the court was influenced by the proximity of sales of subdivided parcels that could easily compare to the potential subdivided parcels at the *Trout Ranch* easement property.

In the *Savannah Shoals* case, the tax court mentioned evidence presented at trial indicating that other mining companies purchasing properties for aggregate mining did not use the DCF analysis when making an offer in an area where subsurface aggregate was so abundant.[94] To buttress use of a DCF analysis, appraisers in conservation easement assignments should perhaps include information that confirms purchasers in the relevant market utilize DCF analysis when analyzing a potential purchase.

Lesson 6: Include a Realistic Supply and Demand Analysis (Marketability Study) to Support Any Conclusion That Some Type of Land Development Is the "Before" Value Highest and Best Use

All three of the cases discussed in this article involve tax court consideration of supply and demand factors related to the quarry project claimed to be the highest and best use before considering the easement. In two of the cases (*Savannah Shoals* and *Ranch Springs*), the tax court concluded there already was sufficient supply available from existing quarries, and in all three cases the courts concluded that the taxpayers' estimates of production from the future quarry were not supportable. *The Appraisal of Real Estate* and *The Dictionary of Real Estate Appraisal* differentiate between a *market study* and a *marketability analysis*, which is sometimes also called a "marketability study." A marketability analysis focuses on the particular property that is the subject of the appraisal, while a market study is more general in its discussion and analysis of supply and demand factors.[95]

The lesson from the three cases is that appraisers need to be realistic in any supply and demand analysis in their conservation easement appraisal reports. Most conservation easement appraisal assignments involve analyzing the effect of restrictions on future subdivision of the protected property. *Appraising Conservation and Historic Preservation Easements*, Second Edition, includes a six-page example of a market study and a market analysis that includes analysis of building permits issued, construction activity, and home and lot prices in the general competitive market as well as home and lot prices, absorption rates, and trends in the subdivisions that would compete with the subject property if it was subdivided.[96]

Lesson 7: Include Detailed Support for a Conclusion That a Zoning Change or Development Permit Is "Reasonably Probable"

The Appraisal of Real Estate states that an appraisal report conclusion that rezoning is reasonably probable must be supported by market evidence such as "rezoning applications, zoning hearings, actions by municipalities, and interviews with planning and zoning officials."[97] All three of the tax court decisions discussed in this article discuss testimony related to the issuance of zoning and mining permits for quarrying.

While the *Savannah Shoals* decision states that Hart County, Georgia, did not have any zoning laws that prohibited or regulated mining, it emphasized that the State of Georgia had significant permitting requirements for mining and the county would "defer" to the state's procedures related to mining permits.[98] However, the court

94. T.C. Memo. 3412-12, 46.

95. *The Dictionary of Real Estate Appraisal*, 7th ed. (Appraisal Institute, 2022), 115, includes the following definition: "*marketability analysis*. The study of how a specific property is expected to perform in a specific market. A marketability analysis expands on a market analysis by addressing a specific property. *See also* market analysis."

96. Roddewig and Brigden, *Appraising Conservation and Historic Preservation Easements*, 2nd ed., 170–175.

97. Appraisal Institute, *The Appraisal of Real Estate*, 15th ed. (Appraisal Institute, 2020), 309.

98. T.C. Memo. 3412-12, 8.

did not address the reasonable probability of obtaining a permit from the state because it concluded that mining was not financially feasible, so it did not have to address the probability of obtaining a state mining permit.

In the *Green Valley* case, there was "no genuine dispute" concerning the likelihood that zoning and mining permits could be obtained. As a result, the court does not include any significant discussion about the necessary steps in the approval process.

The *Ranch Springs* decision emphasizes the importance of including information from local zoning officials about the likelihood of obtaining zoning and planning approval. The tax court heard trial testimony from the local mayor as well as from two members of the zoning commission indicating there would be strong opposition from neighboring property owners to an application for a mining permit. That was enough for the tax court to conclude that rezoning for mining was not reasonably probable.

Lesson 8: Be Sure to Include a Discussion of the Recent Price Paid for the Subject Property

As discussed previously, the Senate Committee on Finance report stated that the most common red flag indicating a faulty conservation easement appraisal and a likely overvaluation was "a consistent pattern of land (or interest in a partnership holding land) sold in an arm's length transaction, followed shortly thereafter by an appraisal asserting land values multiple times higher than the value established in that prior arm's length transaction." That, according to the Senate Committee on Finance, "clearly calls into question the accuracy of these appraisals."[99]

The *Savannah Shoals*, *Green Valley*, and *Ranch Springs* cases each involved appraisals or valuation testimony that disregarded actual pre-donation prices paid for each subject property. In each case, the tax court compared those pre-easement purchase prices with the claimed pre-donation values in the taxpayers' appraisal testimony. The discrepancies were glaring. In the *Savannah Shoals* case, a 92% interest in the property had been obtained for $515,000, or approximately $5,000 per acre, in November of 2017. When the conservation easement was donated one month later in December of 2017, the taxpayer's appraisal stated that the pre-donation market value of the land was $23.1 million. In the *Ranch Springs* case, the taxpayer purchased the land for $6,500 per acre in December of 2016. One year later (in December of 2017), the appraisal to support the charitable donation claimed the market value was more than $236,000 per acre.

According to the tax court, the appraiser who completed the *Savannah Shoals* easement valuation report did not know that a 92% interest in the property had recently sold for only $515,000. The tax court emphasized the missing analysis in the taxpayer's appraisal report and referenced the statement in that appraiser's report "that there are no known sales of the easement property within four years of the valuation date and no current agreement to sell it."[100]

The *Green Valley* decision discusses two transactions in 2011 involving the assemblage of the land holding on which the conservation easement would later be donated. The combined purchase price was $2,237,600. The decision references an appraisal done in December of 2013, less than three years after the 2011 acquisition. That report concluded that an aggregate quarry was the highest and best use and that the property had a value of $22.0 million.[101] The tax court does not indicate how that 2013 appraisal report considered or reconciled the $2.24 million purchase price in 2011 with the $22.0 million value conclusion.

A 95% interest in the *Green Valley* property was subsequently sold for $5.0 million to the syndicated conservation easement investment group on December 29, 2014. One day later, the conservation easement was donated. The same appraisal firm that completed the earlier 2013 report completed the appraisal report for the actual easement donation. Again, however, the tax court does not indicate how that 2014 appraisal report considered or reconciled the value conclusions in it with the prices paid in the prior transactions.

99. See Committee on Finance (August 2020), id., at 11.

100. T.C. Memo. 2024-35, 12.

101. T.C. Memo. 2025-15, 6.

That discussion of prices paid and comparisons with the claimed easement donation values indicate how important it is for appraisers to make inquiries about recent transactions involving the subject properties in assignments to support the value of a conservation easement donation. Those prices need to be investigated and then discussed in the appraisal report. At a minimum, inquiries about prior transactions need to be made with the owner of the property making the donation. It may also be necessary to search the recorded deeds for the property if there is any concern about a recent transaction.[102]

Lesson 9: Be Sure to Include an Analysis of Land Prices Paid for Similar Properties Located in the Vicinity of the Easement-Protected Property

In each of the three cases, the tax court also criticized the disregard for prices paid for properties in the same market area located above deposits of rock similar to that on the subject properties. In each case, the tax court held that, in the case of raw unimproved land, the sales comparison method is generally the most reliable "before" easement valuation method.

Lesson 10: Become Thoroughly Familiar with Tax Court Decisions Related to Conservation Easement Appraising

The three cases demonstrate the importance of reading past tax court decisions as part of the research before completing an appraisal report to support a conservation easement valuation. Familiarity with the case law can assist an appraiser in identifying the basis for potential challenges by the IRS to a conservation easement appraisal. The importance of knowing the case law and referencing tax court decisions as a "check" on the accuracy of the valuation methods and analysis in a conservation easement report has also been emphasized in *Appraising Conservation and Historic Preservation Easements*, Second Edition. Chapter 24 in that book is devoted to how to use case law decisions in a conservation easement appraisal assignment. It emphasizes that knowing the case law "is extremely important because there is a high likelihood that the case law will come into play in the majority of conservation and historic preservation easement assignments."[103] The chapter includes citations to many of the tax court decisions issued before the 2020 date of publication of that book.

The book then lists a number of ways in which the case law can be used as a check on the content and analysis in the conservation easement valuation appraisal report. In that list are ways the case law can be helpful in the "before" value highest and best use analysis, such as in comparing the restrictions created by the conservation easement, and "the otherwise applicable land use, zoning, or historic preservation restrictions" affecting the property.

However, the second edition of *Appraising Conservation and Historic Preservation Easements* also includes an important warning about too much reliance on the case law. Simply looking at the percentage impacts on "before" values in the reported cases is not an acceptable appraisal method. The case law should only be referenced as a "check on the results of the actual valuation methods used to value the conservation or historic preservation easement," and "[i]t is not appropriate to rely on the percentage determinations of easement value in the case law as a valuation method or technique."[104]

Conclusion

The three cases referenced in this article are only a few of the many recent US Tax Court cases involving the charitable donation of syndicated conservation easements. In all three cases, the court concluded there was a "gross valuation overstatement" and imposed a 40% overvaluation penalty on the taxpayer. The size of those penalties give emphasis to the necessary depth of analysis and quality of the appraisal report supporting a conservation easement donation valuation.

102. In the case of the *Savannah Shoals* appraisal, however, it is not clear if a search of the public records would have helped. The decision indicates that the appraisal report for the taxpayer was dated December 1, 2017, but the deed related to the $515,000 transaction was not recorded until December 6, 2017. (T.C. Memo 2024-35, 10)

103. Roddewig and Brigden, *Appraising Conservation and Historic Preservation Easements*, 2nd ed., 455.

104. *Ibid*., 456.

The ten lessons for conservation easement appraisers provided in this article highlight four important appraisal principles:

1. Undertake a thorough and well-supported highest and best use analysis that includes detailed support for any conclusion that development of the property before considering the easement is legally permissible and financially feasible.
2. Do not confuse the value of the future business that might be conducted on the property with the value of the real property itself.
3. Always consider and discuss the most recent purchase price paid for the property as well as prices paid for similar properties in the local market area.
4. If working on assignments in this realm of appraisal practice, stay up to date on recent case law decisions and Treasury Department regulations related to the content and analysis necessary to support a conservation easement donation.

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Disclosure: JLL Valuation and Advisory Services works on conservation easement assignments for both taxpayers as well as federal government agencies including the Internal Revenue Service and the US Department of Justice.