Charitable Contributions: Acknowledgements, Appraisals and the IRS’s Strict Rules

UPON AUDIT, IF A TAXPAYER DOES NOT HAVE A CONTEMPORANEOUS WRITTEN ACKNOWLEDGMENT WITH ALL THREE ITEMS OF INFORMATION REQUIRED, THE ENTIRE CHARITABLE CONTRIBUTION IS DENIED.

Acknowledgements Requirements
Tax season has begun, and it is crucial for any taxpayer claiming a charitable contribution deduction to be aware of the acknowledgment rules. Before the taxpayer files a tax return claiming a charitable deduction of $250 or more, the taxpayer must receive from the charitable organization a contemporaneous written acknowledgement of the contribution in order for the deduction to be allowed. The written acknowledgement must set forth: (a) the amount of cash contributed or a description of any property other than cash contributed; (b) the date of the contribution; and (c) whether the charitable organization provided any goods or services in consideration for the property or cash received. If goods or services were provided, there must be a description and good
faith estimate of their value or a statement that the goods or services consist solely of intangible or religious benefits. I.R.C. § 170(f)(8)(A) and (B). The acknowledgement must be received by the taxpayer by the earlier of the date on which the taxpayer files a return for the year in which the contribution was made or the due date (including extensions) for filing the return. I.R.C. § 170(f)(8)(C). Recent cases make it clear that the rules are being applied in a draconian manner — i.e., upon audit, if the taxpayer does not have a contemporaneous written acknowledgement with all three items of information required, the entire charitable contribution is denied. Thus, even if a taxpayer has a written acknowledgement, but the acknowledgment does not have the “no goods or services” language, no charitable deduction can be claimed.

There is a long line of cases that strictly construe the acknowledgement rules. For example, in Gomez v. Commissioner, T.C. Summary Opinion 2008-93 (2008), the taxpayers had 10 cancelled checks each in excess of $250, for a total of $6,100 that was paid to their church in 2005. At trial, even though the IRS admitted that the payments had been made to the church, the taxpayers received no deduction because they failed to receive a contemporaneous written acknowledgement from the church. The taxpayers received a letter from the church in 2008 acknowledging the contribution, but the Tax Court held that the letter was provided too late and did not satisfy the contemporaneous requirement. The letter also lacked the statement that no goods or services were provided in exchange for the donations.

A recent Tax Court case, 15 West 17th Street, LLC v. Commissioner, 147 T.C. No. 19 (2016), reinforces the need to obtain from the charitable organization a contemporaneous written acknowledgement that contains all of the required provisions. In the case, 15 West 17th Street, LLC (the LLC) donated a conservation easement on property it owned in New York City to the Trust for Architectural Easements (the Charitable Organization). The LLC claimed a $64.5 million charitable contribution deduction for the contribution of the easement on its partnership return. Prior to filing its income tax return for the year of the gift, the LLC received a letter from the Charitable Organization acknowledging the gift. However, the acknowledgement did not have the required “no goods or services” language. The IRS disallowed the deduction for several reasons, including (1) the acknowledgement lacked the “no goods or services” language and (2) the IRS believed the value of the easement and, consequently, the amount of the gift, was overstated.

After the LLC filed its Tax Court petition, the Charitable Organization filed an amended Form 990 information tax return. The amended return described the gift and stated that no goods or services were provided in consideration for the easement donation. Under Internal Revenue Code section 170(f)(8)(D), an acknowledgment is not required if a
contribution is reported by the charitable donee on a return in a form that is in accordance with regulations that the Secretary of the Treasury may prescribe. The IRS contended that the reporting by the Charitable Organization on its Form 990 could not be used to satisfy the acknowledgment rules because no regulations had been promulgated under this Code section, whereas the LLC argued that it was not necessary for regulations to be promulgated for the Code section to be operative. The Tax Court sided with the IRS, holding that the Code section was not self-executing and thus was not in force unless the Treasury actually issued regulations. Therefore, even though the Charitable Organization filed an amended return to attempt to correct the failure of the contemporaneous written acknowledgement to include the “no goods or services” language, the amended return was not effective. As a result, the LLC was allowed none of its $64.5 million charitable contribution deduction. The dissenting opinions stated that the plain language of the statute should be followed regardless of whether the Treasury issued regulations, and that the deduction should have been allowed. The end result is that a $64.5 million charitable contribution deduction was denied for failure to satisfy one element of the contemporaneous written acknowledgement requirement.

When real estate or a conservation easement is contributed to a charity, if the agreement or deed contains all of the requisite information and is executed by the charity, the agreement or deed may constitute a contemporaneous written acknowledgement. In R.P. Golf, LLC, T.C. Memo 2012-282, 104 CCH TCM 413 (2012), the taxpayer contributed a conservation easement to a charity and did not obtain an acknowledgment. However, the Tax Court held that the agreement between the taxpayer and the charity satisfied the acknowledgment rules because it was signed by the representative of the charity, was contemporaneous with the donation of the easement, and provided a detailed description of the property and the easement. Despite these features, the IRS claimed that the agreement was not a proper acknowledgment because it lacked the “no goods or services” statement. The court held for the taxpayer, stating as follows:

The agreement in this case states that the easement contribution is made “in consideration of the covenants and representations contained herein and for other good and valuable consideration”. The agreement then describes the property’s conservation value as its aesthetic, open space, scenic, recreational, and natural resource values but does not include consideration of any value other than the preservation of the property. Finally, the agreement states that it constitutes the entire agreement between the parties regarding the contribution of the conservation easement. The Court therefore holds that the agreement, taken as a whole, states that no goods or services were received in exchange for the contribution. Accordingly, the agreement satisfies the substantiation requirements of section 170(f)(8).
In French Bayne, T.C. Memo 2016-53, 111 CCH TCM 1241 (2016), the taxpayers contributed a conservation easement, and the IRS challenged the deduction for the taxpayer’s failure to obtain a contemporaneous written acknowledgment. The taxpayers received a letter from the charity after they filed their tax return, which the Tax Court held was not contemporaneous. The taxpayers contended that the conservation deed satisfied the acknowledgment requirement, and the controversy involved whether the “no goods or services” language was included in the deed. The Tax Court held that, when a deed of conservation does not explicitly state whether the donee provided goods or services, the deed taken as whole must be examined to determine if the deed is in compliance with this requirement. The two factors that support compliance are that the deed recites no consideration other than the preservation of the property and that the deed includes a provision stating that the deed is the entire agreement of the parties. Because the deed failed to contain the latter provision, the court held that the deed did not confirm that the preservation of the property was the only consideration. On that basis, the taxpayers lost and consequently received no deduction.

The contemporaneous written acknowledgement requirement applies to all charitable gifts, including gifts to private foundations. Consequently, if you have made a charitable contribution to your private foundation, the private foundation must provide you with a contemporaneous written acknowledgement, identifying the gift, the amount of the gift and the date of the gift and stating whether any goods or services were received in return (and their value if any were provided).

**IRS Attacks Appraisal on Account of Minor Deficiencies**

To claim a charitable deduction for a gift of property in excess of $5,000, a taxpayer must obtain a qualified appraisal and submit with the taxpayer’s tax return an appraisal summary on Form 8283. The IRS has been attacking conservation easement transactions for a number of years by challenging appraisals as not meeting the rules for a “qualified appraisal” under Internal Revenue Code section 170(f)(11). The courts have ruled on whether an appraisal obtained by a taxpayer is a “qualified appraisal” with differing results.

The IRS’s nitpicking attacks on appraisals are demonstrated in the taxpayer-friendly case of Cave Buttes, L.L.C., 147 T.C. No. 10 (2016). In that case, the Tax Court held that the appraisal substantially complied with all of the requirements for a qualified appraisal, even though there were some deficiencies. Cave Buttes owned a property in the Phoenix, Arizona, area that it sold to Maricopa County in a bargain-sale transaction.
The question for the court was whether Cave Buttes attached a qualified appraisal to its tax return for the year in which the charitable deduction was claimed. To be a qualified appraisal under Proposed Treasury Regulation section 170A-17, the appraisal must satisfy certain requirements. The following five deficiencies were alleged by the IRS in the Cave Buttes case:

1. The appraisal was not prepared by a qualified appraiser and did not include the qualifications of the appraiser who prepared the report.

2. The appraisal did not include a sufficiently detailed or accurate description of the property.

3. The appraisal did not include a statement that the appraisal was prepared for income tax purposes.

4. The date of valuation was not the date of the purported contribution.

5. The appraisal’s definition of fair market value was not the same definition as in Treasury Regulation section 1.170A-1(c)(2).

As to the first requirement, the regulations set forth a number of rules that must be satisfied for an appraiser to constitute a qualified appraiser. The regulations further provide that, if two appraisers contribute to a single appraisal, each must comply with the rules for the appraisal to be qualified. The IRS claimed that neither of the two appraisers who wrote the appraisal report was qualified. As to one, the IRS claimed that he lacked personal knowledge about the property and the comparables used in the appraisal and that he didn’t personally sign the appraisal. As to the other appraiser, the IRS claimed that he was not qualified because he signed the appraisal but did not sign Form 8283 and his qualifications were not included in the appraisal.

The court dismissed these objections by noting that both appraisers signed the appraisal report, even though both did not sign Form 8283. Moreover, the fact that one appraiser’s qualifications were omitted from the appraisal did not detract from the fact that, taken as whole, there was sufficient compliance with the regulations.

The court also dismissed the IRS’s claim that the description of the property was not sufficiently specific. The IRS contended that the appraisal was based on erroneous information about access to utilities and access to the property. The court held that these arguments “miss the point” of the requirement of the regulations that an appraisal
describe the property and held that the description in the appraisal that included the address and characteristics of the property was enough to strictly comply with the regulations.

Another IRS attack was its claim that the appraisal did not contain a statement that the appraisal was prepared for income tax purposes. The court noted that the appraisal said that it was prepared “to estimate the current Market Value of the fee simple interest in the subject property as of the date of valuation for filing with the IRS.” The statement, the court held, was sufficiently close to “prepared for income tax purposes,” which is the language required by the regulations. The court added that there are no “magic words” necessary to fulfill this requirement.

The IRS faulted the appraisal for having a date that varied from the date of the closing. The court found that having a valuation date that was off by between 11 and 21 days in a deal with a number of moving parts and a somewhat vague closing date enabled the appraisal to substantially comply with the regulations.

The final IRS challenge was that the appraisal did not use the definition of “fair market value” contained in the regulations, which is “the price at which the property would change hands between a willing buyer and a willing seller, neither under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.” Instead, the appraisal used a different standard that is contained in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. It states that market value is:

The most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated

2. Both parties are well informed or well advised and are acting in what they consider their best interest

3. A reasonable time is allowed for exposure in the open market

4. Payment is made in cash in United States dollars or terms of financial arrangements comparable thereto, and
5. The price represents normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

The court found that each element of the definition contained in the regulations was met in the definition used. Thus, despite the IRS attack, the appraisal was a qualified appraisal. In a touch of irony, the court observed that the IRS's own appraisal used the same definition as was used in the taxpayer's appraisal.

The IRS continues to challenge appraisals for noncompliance with the strict rules, and it has prevailed in some of the cases. These results reinforce the need to comply strictly with the regulations and requirements of Internal Revenue Code section 170.

**Syndicated Conservation Easement Transactions**

Another IRS challenge to conservation easements is its recent guidance identifying some syndicated conservation easement transactions as listed transactions for the purposes of Treasury Regulation section 1.6011-4(b)(2) and Internal Revenue Code sections 6111 and 6112. In Notice 2017-10, 2017-4 I.R.B. 544, the IRS described syndicated conservation easement transactions as transactions in which a promoter offers prospective investors in a pass-through entity the possibility of a charitable deduction for a conservation easement. In many instances, the amount of the charitable contribution deduction is at least 2.5 times the amount of the investment by the individual in the pass-through entity. After the individual invests in the pass-through entity, the entity donates a conservation easement to a charitable organization. The promotor has obtained an appraisal that greatly inflates the value of the conservation easement, based on unreasonable conclusions about the property's development potential. The Notice states that the IRS intends to challenge the tax benefit from those transactions.

The consequences of entering into a listed transaction include that individuals must file disclosure statements regarding these transactions, material advisers have disclosure and list maintenance obligations, potentially higher scrutiny by the IRS, and potentially higher and more penalties being assessed for failure to follow the myriad rules surrounding listed transactions.

**Pepper Perspective**

Whenever making a charitable contribution, make sure you receive a contemporaneous written acknowledgment that includes all three components of information: (a) the amount of cash contributed or a description of any property other than cash contributed (if the property value is stated as more than $5,000, a qualified appraisal must also be
submitted); (b) the date of the contribution; and (c) whether the charitable organization provided any goods or services in consideration for the property or cash received, and, if they did provide anything, the value of the goods or services that the charity provided. The contemporaneous written acknowledgement must be received prior to the earlier of the filing of the tax return for the year in which the charitable contribution is made and the due date for the return with extensions.

If you fail to obtain the acknowledgement, or if the acknowledgment does not contain the “no goods or services” language (or a qualified appraisal, if required), upon audit, your contribution will be completely disallowed, even if you have proof that the charity received the contribution. The contemporaneous written acknowledgement requirement applies to all charitable gifts, including to private foundations, so make sure your private foundation provides you with a compliant contemporaneous written acknowledgement. A large conservation easement deduction will likely result in an audit of the tax return; thus, strict compliance with the appraisal rules to support the deduction is necessary.