

TAX UPDATE

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PODCAST

'The New Tax Landscape
for Investment Management'

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Joan C. Arnold
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ARTICLES IN THIS ISSUE

Combatting Foreign Tax Evasion With New Filing Requirements for Foreign-Owned Disregarded Entities

Page 2

***Temple-Inland* Decision Leads to Proposed Delaware Escheat Reform Legislation**

Page 4

Practical Partnership Tips: Electronic K-1s and Addressing New Partnership Audit Rules

Page 8

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

Page 11

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Combatting Foreign Tax Evasion With New Filing Requirements for Foreign-Owned Disregarded Entities



Morgan L. Klinzing | klinzingm@pepperlaw.com

THE NEW REGULATIONS EXPAND THE FILING REQUIREMENTS FOR FORM 5472 TO INCLUDE DISREGARDED ENTITIES WITH FOREIGN OWNERS WHEN THERE ARE CERTAIN REPORTABLE TRANSACTIONS.

If a non-U.S. person (individual or corporation) owns 100 percent of the stock of a U.S. corporate subsidiary, the subsidiary needs to obtain an employer identification number (EIN) and maintain adequate books and records to be able to prepare its tax return and Form 5472 (*Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business*), on which the ownership of the non-U.S. owner is reported, along with certain related party transactions. New reporting requirements finalized on December 13, 2016¹ now extend those rules to disregarded entities. A “disregarded entity” is a company, other than a corporation formed under state law, with a single owner that is not treated as an entity separate from its owner for U.S. federal tax purposes. For example, an LLC with only one owner is disregarded for U.S. federal tax purposes, unless it elects to be classified as a corporation.

Foreign investors often use an LLC to buy assets in the United States. Investors typically do this for the limited liability benefit and the privacy it allows. If a foreign investor used an LLC to simply buy and hold property without renting it, prior to the new rules, the investor did not need to enter the U.S. tax system until the property was sold. This could allow foreign investors to hide assets and income from their local tax authorities and opened a potential avenue for using the disregarded LLC as a money-laundering vehicle.

The new regulations expand the filing requirements for Form 5472 to include disregarded entities with foreign owners when there are certain “reportable transactions.” Reportable transactions include property sales, licenses, leases, loans and payments in connection with forming, acquiring or disposing of the entity.

The IRS can then use the information provided on Form 5472 to enforce U.S. tax laws. Also, the Department of the Treasury can exchange the information with other governments under tax treaties, inter-governmental agreements (e.g., information exchange agreements entered into under the Foreign Account Tax Compliance Act) and other taxpayer information exchange agreements, decreasing the likelihood of foreign tax evasion.

In addition to filing Form 5472, the disregarded entity will also be required to maintain records and obtain an EIN. Disregarded entities will be required to keep records to establish the proper treatment of reportable transactions. The application for an EIN will also require the disregarded entity to identify a responsible party, which is generally the individual who has control or manages the entity. The regulations do provide exceptions for certain small corporations and *de minimis* transactions.

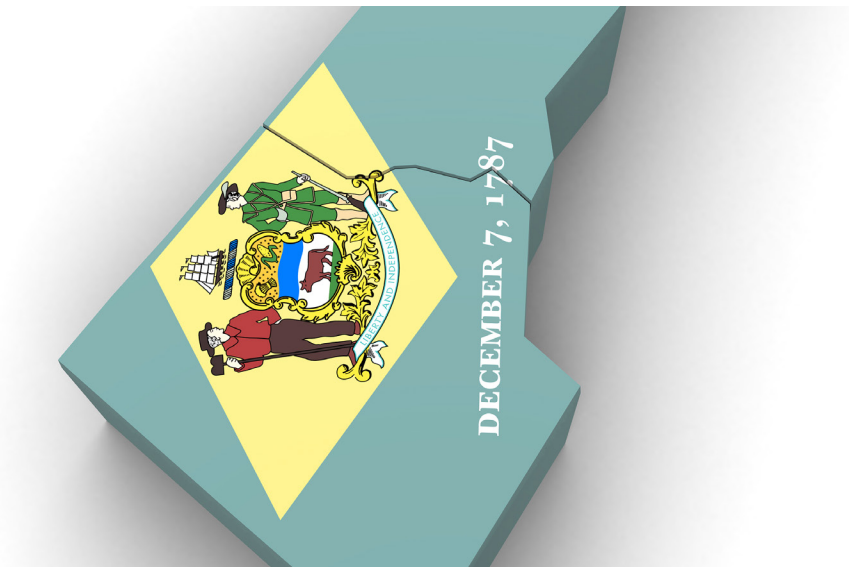
Pepper Perspective

These new reporting requirements are effective for taxable years beginning on or after January 1, 2017 and ending on or after December 31, 2017. Foreign-owned disregarded entities should obtain advice regarding whether they have any reporting requirements and to ensure they are maintaining appropriate records, and should obtain an EIN if they have not yet done so.

Endnote

1 T.D. 9796, 81 FR 89849 (Dec. 13, 2016).

***Temple-Inland* Decision Leads to Proposed Delaware Escheat Reform Legislation**



Lance S. Jacobs | jacobsls@pepperlaw.com

THE PROPOSED REFORMS ARE A WELCOME CHANGE, SPECIFICALLY AS THEY RELATE TO LOOKBACK PERIODS, ELECTRONIC FILING AND LIMITED COMPLIANCE REVIEWS.

As a result of what some might view as a scathing decision by the U.S. District Court for the District of Delaware in *Temple-Inland, Inc. v. Cook*, 192 F. Supp. 3d 527 (D. Del. 2016), Delaware has proposed comprehensive unclaimed property legislative reform. This reform could impact any corporation formed in Delaware, without regard to state of activity. Delaware still retains its status as one of the most favorable jurisdictions within which to incorporate, and the unclaimed property priority rules require escheat of property to the state of incorporation when the last-known address of the rightful owner is unknown. As a result, changes to the Delaware unclaimed property laws have nationwide implications for Delaware-incorporated businesses. This article reviews the *Temple-Inland* decision as well as the proposals on the table in Delaware SB 13, which was introduced in the general assembly on January 12, 2017.

Temple-Inland Decision

Temple-Inland is a Delaware corporation that manufactures corrugated packaging, with its principal places of business in Texas and Indiana. In 2008, the Delaware state escheator notified the company of an impending audit. The audit was completed by a third-party auditor retained by the state to conduct its escheat audits. As a result of the audit, Temple-Inland was assessed more than \$2 million, attributable to escheatable but dormant accounts payable and payroll. Once Temple-Inland exhausted its administrative remedies, it filed suit challenging the constitutionality of the assessment in U.S. district court, rather than litigating the assessment in the Delaware Court of Chancery.

The district court granted Temple-Inland's motion for summary judgment in part on substantive due process grounds. These substantive due process claims are reviewed below, followed by the proposed changes in the law in light of the decision.

The district court noted that Delaware's actions during the audit "shocked the conscience," so as to constitute a due process violation. The court found that Delaware's attempts to audit a full 22-year lookback period violated the explicit terms of the statute, which provided for a six-year statute of limitations, and that the state could only go back through the entire lookback period if Temple-Inland had not filed escheat returns. Delaware made an impermissible assumption that the reports had not been filed when, in fact, they might have been filed and subsequently destroyed under standard record-retention policies. Additionally, Delaware's policy on "negative reports" — those reports that show zero escheatable property — was that no filing was necessary, which also would have explained the lack of documentation for certain years. Additionally, unlike many states, the Delaware statutory scheme did not mandate a certain period for record retention, a failure of due process in that it did not put Temple-Inland on notice that it had to retain its records for a certain period of time.

The court also took issue with Delaware's attempt to apply a 2010 amendment to the escheat statutes retroactively to allow estimation of liability to years prior to the amendment. In viewing and using this technique as a revenue raiser, the court said it violated substantive due process and was inherently inconsistent with the escheat statute's stated goal of reuniting property with its rightful owner. Additionally, the estimation methodology chosen used a sample that was based on all escheatable property, rather than limiting the sample in such a way to arrive at an estimation of Delaware escheatable property, which violated substantive due process. Finally, the estimation methodology used by Delaware presented a real risk that the same property could be escheatable to multiple

states based on the estimation rule being applied to the primary rule (that property is escheatable to the state of the last-known address of the owner), rather than strictly to the secondary rule (that property should be escheated to the state of incorporation of the holder if the last-known address of the owner could not be ascertained).

Proposed Reforms

In response to the *Temple-Inland* decision, Delaware has proposed legislative reforms that include the below seven key components.

Shortened Lookback Period

When the law is enacted, the audit lookback period will be limited to 10 years plus the period of dormancy — *i.e.*, how long a piece of property must go unclaimed before it is escheatable; it is five years for most property — from the date of the audit letter. This lookback period will apply to pending but uncompleted audits at the time of enactment as well.

One-Time Voluntary Disclosure Agreement Election

After the enactment, those entities under audit may make a one-time election to enter into the unclaimed property voluntary disclosure agreement (VDA) program. The election must be made by July 1, 2017. Any unclaimed property liability would be settled through the secretary of state's VDA program, rather than with the third-party contract auditors working with the Delaware Department of Finance. To the extent that the audit is a part of a larger, multistate audit, the election would only apply to the Delaware portion. Any holder that makes this election and resolves the VDA in accordance with the secretary of state's time limits would avoid interest and penalties.

Option to Expedite Audit

This election, also to be made prior to July 1, 2017, allows a holder to elect an expedited resolution of its audit. Like the VDA program, a holder resolving an expedited audit within the time period set forth under the terms of its expedited audit would avoid interest and penalties.

Compliance Review

Meant as a kinder, gentler audit, the compliance review would be less intrusive than a full-blown audit and would be limited to the contents of the filed report and its supporting documents. The state would nonetheless retain its ability to conduct a full-blown audit of a holder, but it presents a possibility of an easier resolution.

Due Diligence

Historically, only securities-related property subject to escheat required statutory due diligence to identify the owner. The proposed bill extends the diligence requirements to any property held by a holder prior to the holder escheating the property to Delaware.

Increased Interest and Penalties

Current law limits interest on unclaimed property to 0.5 percent per month to a cap of 25 percent of the amount of the unclaimed property. The proposed reform would increase the cap to 50 percent, and it would also reestablish the failure-to-pay penalty, at a rate of 0.5 percent per month up to 25 percent of the total liability. Fraud penalties (up to 75 percent of the underlying liability) and purposeful evasion and willfulness penalties of up to 25 percent of the underlying liability are also proposed. While penalties historically were negotiated as the result of state settlements, the early indication is that Delaware will automatically impose and attempt to collect those penalties.

Electronic Filing

After March 1, 2018, all Delaware annual unclaimed property reports will be required to be filed electronically. Delaware will develop and implement a web-based portal to accomplish this new requirement.

Pepper Perspective

As a preferred state of formation for entities as a result of its favorable corporate law provisions, Delaware long enjoyed the benefit of the second priority rule for escheatable property. Holders would have to remit to Delaware, as the state of incorporation, any property for which they could not identify the owner's last-known address. Delaware used this as a source of revenue; as a result, the unclaimed audit process could be difficult and lead to arbitrary results, as it did for Temple-Inland. The proposed reforms are a welcome change, specifically as they relate to the lookback periods, electronic filing and the limited compliance reviews, but also as they relate to the one-time only options, which give entities currently under audit an opportunity to close the audit amicably. The increased penalties and interest should drive compliance higher as a detriment to holders avoiding their responsibilities. Implementation of the spirit of the proposed reforms by the Department of Finance upon passage will be critical to avoid the sometimes difficult and contentious audit process.

Practical Partnership Tips: Electronic K-1s and Addressing New Partnership Audit Rules



Jennifer A. O'Leary | olearyj@pepperlaw.com

PARTNERSHIPS AND LIMITED LIABILITY COMPANIES SHOULD BEGIN THINKING ABOUT ADDRESSING THE ISSUES PRESENTED BY THE NEW PARTNERSHIP LAW IN THEIR AGREEMENTS, EVEN IF FURTHER CHANGES WILL BE NECESSARY ONCE REGULATIONS ARE ISSUED.

Electronic K-1s

Many partnership and limited liability agreements provide that the partnership or limited liability company taxed as a partnership will deliver K-1s electronically. Some provide that partners and members are consenting to this delivery by signing the agreement. Is this sufficient to comply with the requirements to deliver a K-1 to partners and members?

Unfortunately, it is not. In order to avoid the significant penalties that may apply if K-1s are not delivered to partners of partnerships and members of limited liability companies, the partnership or limited liability company must receive consent electronically to the electronic delivery of K-1s. That electronic consent must demonstrate that the partner or member can access the electronic format in which the K-1s are delivered. If consent

to electronic delivery is received in paper form, then an additional confirmation of that consent must be received in a manner that demonstrates that the partner or member can access the electronic format in which the K-1s will be delivered.

Thus, if consent to electronic delivery is received in paper form, then an additional electronic confirmation of that consent is still needed. Based on the rules, it appears that a consent given when accessing the secure website to download or print the K-1s should be sufficient.

The rules also require that, if the electronic method of delivery changes materially, new consent to electronic delivery is required in a manner that demonstrates that the partner or member can access the new method. It is not clear what amounts to a material change, but, if the partnership or limited liability company is in any doubt regarding it, obtaining a new consent when accessing the system makes sense. It may be more practical to simply obtain consent each year. The partnership or limited liability company must also inform the partners or members of how to print the K-1s and of the date when the K-1s will no longer be available on the website.

Additionally, the rules require that partners or members be able to withdraw consent and that the partnership or limited liability company will then be required to deliver paper K-1s. Partners and members must be informed that, if they do not consent or if they withdraw consent, paper K-1s will be provided. Even electronic K-1s must provide all required information and comply with all the instructions and rules applicable to substitute K-1s. Further, the partnership or limited liability company must provide notice when the K-1s are available. If the notice is delivered via email and is returned as undeliverable, paper notice must be provided within 30 days.

Therefore, although electronic delivery of K-1s is permitted, certain rules must be followed in order to avoid penalties for failing to deliver K-1s.

New Audit Rules

Beginning in 2018, new audit rules will apply to partnerships and limited liability companies taxed as partnerships. The default under these new rules will be that the partnership or limited liability company will pay any tax assessed on audit. We have been waiting for the regulations implementing this new law, and many of those proposed regulations were issued in late January. However, the proposed regulations were then promptly withdrawn as part of the Trump administration's freeze on new regulations. At this time, it is unclear when those regulations will be reissued or if replacement regulations will be issued.

One item that the proposed regulations reserved on, and sought comments regarding, was whether partnerships could elect to issue “statements” that are essentially amended K-1s through multiple tiers of partnerships. If these types of “statements” were allowed and a partnership undergoes an audit resulting in an assessed adjustment, that partnership could elect to issue statements to its partners, rather than paying the tax due at the partnership level. One potential result of this method is that the partners would pay a higher tax. However, if that partnership has other partnerships or limited liability companies as its partners, the now-withdrawn proposed regulations did not permit the partnership-partner to itself issue statements. Instead, comments were being sought regarding this issue. The IRS and the Department of the Treasury are concerned about the costs and effects on compliance of permitting statements to be issued through tiers of pass-through entities. Thus, this remains an issue for tiered partnership structures.

Pepper Perspective

As it is not clear when proposed regulations will be issued, and the effective date of the law is fast approaching, partnerships and limited liability companies should begin thinking about addressing the issues presented by the new partnership law in their agreements, even if further changes will be necessary once regulations are issued. One way to deal with the partnership’s or limited liability company’s paying the tax may be through the same mechanism that the entity currently uses to deal with required withholding taxes. It may make sense to wait a few more months before implementing any changes, however, in the hope that regulations will be issued in that time period, unless the entities subject to the new law are already in the process of creating or amending their agreements.

EVENT

**Proposed Tax Legislation:
What It Might Mean To You
(New York)**

**Joan C. Arnold
Morgan L. Klinzing
Todd B. Reinstein**

Thursday, March 2, 2017

EVENT

**Proposed Tax Legislation:
What It Might Mean To You
(Philadelphia)**

**Joan C. Arnold
Morgan L. Klinzing
Todd B. Reinstein**

Wednesday, March 1, 2017

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



W. Roderick Gagné | gagner@pepperlaw.com
Lisa B. Petkun | petkunl@pepperlaw.com

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 by the church 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 promoter 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.

EVENT

Tax Executives Institute

'International Tax Update'

**Joan C. Arnold
Todd B. Reinstein**

Thursday, February 16, 2017

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FEDERAL AND INTERNATIONAL TAX ISSUES

Annette M. Ahlers | ahlersa@pepperlaw.com

Joan C. Arnold | arnoldj@pepperlaw.com

Steven D. Bortnick | bortnicks@pepperlaw.com

W. Roderick Gagné | gagner@pepperlaw.com

Howard S. Goldberg | goldbergh@pepperlaw.com

Morgan Klinzing | klinzingm@pepperlaw.com

Jennifer A. O'Leary | olearyj@pepperlaw.com

Lisa B. Petkun | petkunl@pepperlaw.com

Delaram Peykar | peykard@pepperlaw.com

Thomas D. Phelan | phelant@pepperlaw.com

Todd B. Reinstein | reinsteint@pepperlaw.com

STATE AND LOCAL TAX ISSUES

Lance S. Jacobs | jacobsls@pepperlaw.com

EMPLOYEE BENEFITS ISSUES

David M. Kaplan | kapland@pepperlaw.com

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WEBINAR

**Restoring Clarity to a
Muddied Funds Landscape**

**Julia D. Corelli
Steven D. Bortnick**

**Presented by
Financial Executives
Alliance**

**March 21, 2017
1:00 PM**

EVENT

Private M & A

**Terrence R. Allen
Steven D. Bortnick**

**Presented by
Financial Executives
Alliance**

**March 16, 2017
Los Angeles, CA**

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