

1 UNITED STATES COURT OF APPEALS
2 FOR THE DISTRICT OF COLUMBIA CIRCUIT
3

4
5 COMMISSIONER OF INTERNAL
6 REVENUE SERVICE,

7 Appellant,

No. 10-1063

8 v.

9 DOROTHY JEAN SIMMONS,

10 Appellee.
11

12 Friday, February 4, 2011

13 Washington, D.C.

14 The above-entitled matter came on for oral
15 argument pursuant to notice.

16 BEFORE:

17 CIRCUIT JUDGES GINSBURG AND GARLAND AND
18 SENIOR CIRCUIT JUDGE SILBERMAN

19 APPEARANCES:

20 ON BEHALF OF THE APPELLANT:

21 PATRICK J. URDA, ESQ.

22 ON BEHALF OF THE APPELLEE:

23 ROBERT J. ONDA, ESQ.
24
25

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P R O C E E D I N G S

THE CLERK: Case number 10-1063, Commissioner of Internal Revenue Service, Appellant v. Dorothy Jean Simmons. Mr. Urda for the Appellant; Mr. Onda for the Appellee.

ORAL ARGUMENT OF PATRICK J. URDA, ESQ.

ON BEHALF OF THE APPELLANT

MR. URDA: May it please the Court, Patrick Urda for the Commission of Internal Revenue. Your Honors, this case involves the deductibility of the donation of facade easements to L'Enfant over property in Logan Circle. The Tax Court erred in two respects in its decision, first, the donations were not made exclusively for conservation purposes as necessary to qualify for the deduction; secondly, tax payer failed to obtain qualified appraisals as required by DEFRA, and the relevant Treasury regulations.

This morning I'd like to discuss each of these issues in turn, turning first to whether there was a qualified charitable contribution in this case.

JUDGE SILBERMAN: Counsel, let me ask you a question at the outset. Although this is phrased as just an individual case doesn't it implicate thousands of tax deductions across the District of Columbia?

MR. URDA: Yes, this does, Your Honor.,

JUDGE SILBERMAN: That means it's a fundamental change in policy on the part of the IRS then, is that correct?

1 MR. URDA: No, that's not correct. There has been
2 no change in policy, Your Honor.

3 JUDGE SILBERMAN: But there are thousands of these
4 easements across the District of Columbia similar to these,
5 isn't that correct?

6 MR. URDA: That's certainly correct, Your Honor, but
7 the question is whether this type of easement and this type of
8 language in particular qualifies for a charitable contribution
9 deduction.

10 JUDGE SILBERMAN: I understand. Is this any
11 different than thousands of others in the District of
12 Columbia?

13 MR. URDA: Well, Your Honor, based on -- I can only
14 speak to this language. I'm not --

15 JUDGE SILBERMAN: Well, can you? Is that true? Is
16 that -- I mean, I know the IRS is a little different from
17 other agencies and they proceed individually, but I remember
18 reading a few years ago a Washington Post story about these
19 easements across the District of Columbia, and I gather
20 they're quite common, and that this conservation group is not
21 much different than any others.

22 MR. URDA: That's correct, Your Honor, and that's
23 why it's so important to focus on the language to actually see
24 whether these types of easements actually qualify for the
25 deduction. This is really coming up right now as people are

1 taking deductions for --

2 JUDGE SILBERMAN: But this has been going on for
3 decades, isn't that correct?

4 MR. URDA: That's correct.

5 JUDGE SILBERMAN: So, all of a sudden the IRS is
6 challenging the position?

7 MR. URDA: Well, all of a sudden deductions are
8 being taken, so the IRS is --

9 JUDGE SILBERMAN: No, if I remember the Washington
10 Post story almost 10 years ago these deductions have been
11 going on for a long, long time.

12 MR. URDA: I can only say, Your Honor, that the IRS
13 has taken a position based on this type of language in this
14 easement which it finds does not qualify for a qualified
15 charitable contribution.

16 JUDGE SILBERMAN: So, you're not willing to tell the
17 Court whether this is a change in position of the IRS and
18 whether this is the first time they've challenged this type of
19 easement?

20 MR. URDA: Well, I know that there have been a
21 number of challenges in the Tax Court for the last 20 years to
22 try to figure out what exactly is acceptable language. This
23 is one of those cases where the IRS has believed that the
24 language does not comply.

25 JUDGE GINSBURG: You keep saying language, what are

1 we talking about?

2 MR. URDA: Okay. We're --

3 JUDGE GINSBURG: Perpetuity, is that the issue?

4 MR. URDA: Excuse me?

5 JUDGE GINSBURG: Is perpetuity the issue?

6 MR. URDA: Yes --

7 JUDGE GINSBURG: Okay.

8 MR. URDA: -- perpetuity is the issue. Because as
9 the Code requires these have to be exclusively for
10 conservation purposes.

11 JUDGE GARLAND: Can I just back up on the question
12 Judge --

13 MR. URDA: Sure.

14 JUDGE GARLAND: -- Silberman asked? This language
15 appears to be standard language. Has the IRS ever challenged
16 this language before?

17 MR. URDA: I'm not sure if the IRS has ever
18 challenged this particular language before, but I'm not sure
19 if this language has ever been before the IRS before.

20 JUDGE GARLAND: Are there any other historical
21 easements in the District of Columbia where the IRS has
22 challenged?

23 MR. URDA: I'm not sure, Your Honor.

24 JUDGE GARLAND: Well, then it seems like --

25 JUDGE SILBERMAN: Why are you not sure?

1 JUDGE GARLAND: -- it seems like a rather
2 significant question.

3 JUDGE SILBERMAN: Yes. Why are you not sure?

4 MR. URDA: I can tell you that this is the first
5 time that the, as far as my research went that this type of
6 language has been challenged in the District of Columbia, but
7 it could very well be the first time this language has come
8 up. And this language is, the problematic portion of this
9 language is that it doesn't restrict the interest to one that
10 would preserve the conservation purposes in perpetuity as is
11 required under the Code, or as the IRS has articulated in its
12 regulation --

13 JUDGE GARLAND: What is it about it --

14 JUDGE GINSBURG: What's the problem with it? Yes.

15 JUDGE GARLAND: What is it about it that doesn't
16 restrict it to conservation purposes?

17 MR. URDA: Well, the language is nothing herein
18 contained shall be construed to limit the grantees right to
19 give its consent, e.g. to changes in a facade, or to abandon
20 some or all of its rights hereunder.

21 JUDGE GARLAND: Yes. But then you have paragraph C
22 which says grantor agrees that any rehabilitation work or new
23 construction work on the facade whether or not grantee has
24 given consent will comply with the requirements of all
25 applicable federal and state government laws, and particularly

1 addressing the Secretary of the Interior's standards for
2 rehabilitating historic buildings. So, I appreciate that you
3 have another argument about whether there's anything given
4 here more than the law, but that's not what I'm focusing on,
5 I'm focusing on the words conservation purposes. They have
6 agreed here that all construction work will comply with a
7 series of laws that deal with conservation purposes, is that
8 right?

9 MR. URDA: That's correct.

10 JUDGE GARLAND: So, then how can you say that it is
11 not -- there isn't an agreement in perpetuity with respect to
12 conservation purposes?

13 MR. URDA: Because conservation purposes isn't the
14 only defined term under the Code. It's --

15 JUDGE GARLAND: You read me a sentence.

16 MR. URDA: Yes.

17 JUDGE GARLAND: You said the sentence is will
18 prevent uses of the retained interest inconsistent with the
19 conservation purposes, is that it?

20 MR. URDA: That's correct.

21 JUDGE GARLAND: Okay. That's the only phrase in
22 that sentence.

23 MR. URDA: I think that that's the sentence that you
24 read. Yes.

25 JUDGE GARLAND: Yes. I'm sorry, which were you

1 reading?

2 MR. URDA: My sentence is on A109-118, nothing
3 herein contained shall be construed to limit the grantee's
4 right to give its consent.

5 JUDGE GARLAND: No, I'm sorry.

6 MR. URDA: Yes.

7 JUDGE GARLAND: We're talking past each other.

8 MR. URDA: Yes. Sorry.

9 JUDGE GARLAND: Which provision of the Code or the
10 regulation were you reading a few moments ago?

11 MR. URDA: That's 170(h)(5).

12 JUDGE GARLAND: Right.

13 MR. URDA: Conservation, in order to be exclusively
14 for conservation purposes the conservation purpose has to be
15 protected in perpetuity. So --

16 JUDGE GARLAND: Right. So, this --

17 JUDGE SILBERMAN: It's your regulation you're
18 relying on.

19 MR. URDA: No, that's 170(h)(5). We also rely on
20 the regulation which gives --

21 JUDGE GARLAND: No.

22 JUDGE SILBERMAN: Well, where does the perpetuity
23 come from? Where is that language?

24 MR. URDA: 26 U.S.C. 170(h)(5).

25 JUDGE GARLAND: (5)(a), that's --

1 JUDGE SILBERMAN: Right.

2 JUDGE GARLAND: -- the Code, right?

3 MR. URDA: That's correct.

4 JUDGE GARLAND: Okay. So, that's what I'm focusing
5 on. The conservation purpose they are agreeing to be bound by
6 in perpetuity, that purpose being protected by at the minimum
7 the Secretary of the Interior's regulations and the laws
8 regarding historic preservation.

9 MR. URDA: I actually think, Your Honor, as L'Enfant
10 itself admits in the Amicus brief that they have an unfettered
11 ability because the language of the easement says nothing
12 herein contained shall be construed to limit the grantee's
13 right to consent to changes in a facade, for example. So --

14 JUDGE GARLAND: Yes. But it says in (c) whether or
15 not the grantee has given consent it will comply.

16 MR. URDA: I think that that's a fair point, Your
17 Honor, but I think that looking back at the regulation which
18 gives a little bit more information on --

19 JUDGE GARLAND: All right, which part --

20 MR. URDA: -- this is --

21 JUDGE GARLAND: Where do you want me to look now?

22 MR. URDA: 1.170A-14(g)(1), it says any interest
23 retained by the donor must be subject to legally enforceable
24 restrictions that will prevent uses of the retained interest
25 inconsistent with conservation purposes of the donation. I'm

1 not sure that that language actually complies with the
2 regulation. So, you have two problems, there's no perpetuity
3 under the Code as well as under the regulation. Now, this
4 isn't --

5 JUDGE GARLAND: What's --

6 JUDGE GINSBURG: Let me ask this question. If this
7 provision were not there would there be anything that would
8 compel a grantee to enforce the easement? No.

9 MR. URDA: No.

10 JUDGE GINSBURG: And would there be anyone with
11 standing other than the grantee to enforce the easement?

12 MR. URDA: Definitely not.

13 JUDGE GINSBURG: Definitely not?

14 MR. URDA: Right.

15 JUDGE GINSBURG: So, this adds nothing. No easement
16 can be, you can't make any grantee qualified regardless of
17 what's in the easement enforce it if they don't want to.
18 That's what you're telling me.

19 MR. URDA: Well, I think that's partially right.

20 JUDGE GINSBURG: So, this is just a recognition of
21 reality.

22 JUDGE SILBERMAN: Wait a minute. Wait a minute.
23 You said it's partially right, why is it only partially right?

24 MR. URDA: Well, I think that obviously the District
25 of Columbia and many other jurisdictions have their own set of

1 laws that --

2 JUDGE GINSBURG: That's different than the easement.

3 MR. URDA: That's correct.

4 JUDGE GINSBURG: Okay. So, who can enforce the
5 easement?

6 MR. URDA: Well, actually only the grantee can
7 enforce the --

8 JUDGE GINSBURG: Okay. So, if the grantee chooses
9 not to enforce an easement, or becomes lax, or is overloaded
10 and doesn't enforce it --

11 MR. URDA: That's precisely the problem.

12 JUDGE GINSBURG: -- wait a minute, the easement is
13 still in perpetuity if it has the qualifying provisions.

14 MR. URDA: Well, except the way that perpetuity is
15 defined by the Code is that it will prevent uses of the
16 retained interest inconsistent. In your example, Judge
17 Ginsburg, I'm not sure that that will actually happen.
18 Remember, the --

19 JUDGE GINSBURG: Well, I think you're quibbling over
20 something that's ephemeral here. You've got a more
21 interesting point and less time to deal with it, 14 seconds.
22 So, we'll give you a little extra time. Why don't you move on
23 to that?

24 MR. URDA: Okay. Moving on to the more interesting
25 point, the appraisal issue. Under DEFRA a qualified appraisal

1 actually is defined in large part by the Secretary of the
2 Treasury and how he defines it in regulations. The Secretary
3 of the Treasury defined it here in 1.170-(13) as one that
4 shall include a valuation method for fair market values and
5 specific basis for evaluation. The appraisals here did not
6 comply with either of these two requirements. Quite frankly,
7 the appraisals speak only in general language --

8 JUDGE SILBERMAN: Is that a mixed question of fact
9 and law?

10 MR. URDA: I believe so, Your Honor.

11 JUDGE SILBERMAN: Don't we have to give deference to
12 the Tax Court then?

13 MR. URDA: Unless it's a clear error, and I think
14 that here it is a clear error because --

15 JUDGE SILBERMAN: Well, deference, of course,
16 doesn't mean that you automatically approve, but we do have to
17 defer, don't we?

18 MR. URDA: Certainly, Your Honor.

19 JUDGE SILBERMAN: Okay.

20 JUDGE GINSBURG: Which is to say it may error but
21 only if it's clearly erred can we reverse it.

22 MR. URDA: That's correct, Your Honor.

23 JUDGE GINSBURG: Okay.

24 MR. URDA: Now, and of course, the regulation itself
25 because it filled a gap left by Congress is entitled to

1 controlling weight.

2 JUDGE GARLAND: But it doesn't say, it's vague
3 itself, that is it says the method of appraisal, well, you may
4 not like the method of appraisal which appears to be a
5 different issue, but it does give the method of appraisal.
6 And it actually says specifically what it did. Now, it may
7 have not done very much, but what if it specifically said I
8 didn't do very much? That's quite specific. So, now there's
9 no question of substantial compliance, they've complied.

10 MR. URDA: I think that that's a fair point. The
11 question is what is a method? You know, can you just say my
12 method is throwing a dart against a wall?

13 JUDGE GARLAND: Well, but that's not, that obviously
14 is not their method.

15 MR. URDA: Of course not. I'm just --

16 JUDGE GARLAND: So, let me ask you another question.

17 MR. URDA: Okay.

18 JUDGE GARLAND: In addition to the issue you have
19 here which is whether it's deductible at all, does the IRS
20 have the right to challenge the amount of the deduction?

21 MR. URDA: Not in this proceeding. The IRS is not
22 challenging the valuation, the IRS is saying that there was an
23 earlier error --

24 JUDGE GARLAND: Yes, but could it have challenged
25 the amount of the deduction?

1 MR. URDA: Certainly.

2 JUDGE GARLAND: So, your overall point here, which
3 is gee, they didn't get much more than the law would have
4 limited them anyway --

5 MR. URDA: Right.

6 JUDGE GARLAND: -- and therefore it's not worth very
7 much. You could have challenged that a different way in a
8 different kind of proceeding?

9 MR. URDA: Yes, Your Honor.

10 JUDGE GARLAND: Just explain to me, I'm --

11 MR. URDA: Well, I mean, we did challenge that
12 valuation in the Tax Court. That was actually the second part
13 of the Tax Court's opinion --

14 JUDGE GARLAND: Yes, so that --

15 MR. URDA: -- when they were talking about the --

16 JUDGE GARLAND: So, you did challenge that part?

17 MR. URDA: That's right.

18 JUDGE GARLAND: So, but here I thought there's a
19 part of your brief where you say five percent wasn't good
20 enough.

21 MR. URDA: Well, we were explaining -- to give a
22 little back story on why when you have a method that doesn't
23 give you any sort of guidance what kind of trouble it is to
24 review.

25 JUDGE GARLAND: I see. But so if we thought that

1 there wasn't a violation either of the statute or the
2 regulations about qualified appraisals that would be the end
3 of it from your point of view, we couldn't agree with you that
4 this doesn't seem to be worth five percent, or whatever,
5 right? That couldn't be sent back?

6 MR. URDA: I think that the Court could send back
7 the case, in fact, I think we have a footnote in our reply
8 brief saying that because the Tax Court actually had no basis
9 for its opinion based on the fact that there was no qualified
10 appraisal it would be appropriate for the Court to send it
11 back.

12 JUDGE GARLAND: But it's either, it's really on or
13 off switch here, it's not a dispute about whether they were
14 arbitrary and capricious in how much they allowed.

15 MR. URDA: I think that if I'm understanding you
16 right, Judge --

17 JUDGE GARLAND: Well, I'm not sure. Sometimes what
18 you're saying sounds like it's arbitrary and capricious to
19 have picked five percent, and sometimes it sounds like all
20 you're saying is they had no basis for five percent, therefore
21 it's not a qualified appraisal. Those seem like two different
22 questions to me.

23 MR. URDA: I'm sorry for my lack of clarity. I
24 think it's, my argument is because they had, they didn't
25 comply with the regulations -

1 JUDGE SILBERMAN: Wait a minute. The problem is
2 you're both using they --

3 MR. URDA: I'm sorry, that --

4 JUDGE SILBERMAN: -- into that. Well, are you
5 talking about the tax payer, are you talking about the IRS,
6 are you talking about the Tax Court, which are you referring
7 to?

8 MR. URDA: I'm sorry, Judge Silberman. I'm
9 referring to the appraisals obtained by tax payer did not
10 comply with the regulation because it did not give a method or
11 substantial basis besides very general language. That led to
12 both tax payer's own appraisal having no grounding, but in the
13 Tax Court's decision --

14 JUDGE SILBERMAN: What was missing in the appraisal
15 as a matter of law?

16 MR. URDA: Well, I think what was missing was any
17 sort of basis that a reviewing court, or the IRS could
18 determine how the appraiser reached his conclusion, instead
19 the language --

20 JUDGE SILBERMAN: Well, hypothetically what is
21 missing? The appraiser tried to calculate what the value of
22 the easement was, he pointed out that there were very few
23 sales that he could compare it to so he had to make a rough
24 judgment, well, how else could he do it?

25 MR. URDA: Well, he could have actually given some

1 flesh to those bones. He could have said here's who I talked
2 to, this is somebody active in the market, and this is what
3 this person had found. Instead he says I considered
4 subjective and conjectural factors. We don't know what
5 factors he considered.

6 JUDGE GARLAND: You mean if he gave the names of the
7 real estate agents he spoke with that would have done it for
8 you?

9 MR. URDA: I'm not sure what would have done it for
10 us, but --

11 JUDGE SILBERMAN: Wait a minute, you can't do that.

12 MR. URDA: Okay.

13 JUDGE SILBERMAN: You can't say that.

14 MR. URDA: Okay.

15 JUDGE GINSBURG: Sure you are, you got the Walman
16 (phonetic sp.) appraisal.

17 MR. URDA: That's right.

18 JUDGE GINSBURG: Well, that does it for you, right?

19 MR. URDA: Yes, it does.

20 JUDGE GINSBURG: And that doesn't say speculative
21 and conjectural matters, it says that talk with other agents
22 in the market --

23 MR. URDA: Right.

24 JUDGE GINSBURG: -- identified comps, including
25 comps for eased properties subject to this kind of an

1 easement, right?

2 MR. URDA: Yes.

3 JUDGE GINSBURG: So, that's your model of what's
4 appropriate.

5 MR. URDA: That's correct.

6 JUDGE GINSBURG: All right. Now, before you sit
7 down I want to --

8 MR. URDA: Okay.

9 JUDGE GINSBURG: -- just clarify one thing. Judge
10 Garland asked you, and I don't think you settled this, but
11 your footnote seems to me clear that your objection to the, or
12 your reference to the five percent is only meant to illustrate
13 the lack of guidance derived from the tax payer's appraisal
14 and not an independent basis for objecting to the judgment and
15 asking us to remand it for this --

16 MR. URDA: That's right.

17 JUDGE GINSBURG: Okay. Thank you very much.

18 MR. URDA: Okay. Thank you.

19 JUDGE GINSBURG: Mr. Onda.

20 ORAL ARGUMENT OF ROBERT J. ONDA, ESQ.

21 ON BEHALF OF THE APPELLEE

22 MR. ONDA: May it please the Court, I am Robert
23 Onda, and I represent the Appellee, Dorothy Jean Simmons, in
24 this case.

25 Your Honor, based upon the discussions we had regarding

1 qualified easements I will not address that, I believe you
2 understand our argument. I would like to address today the
3 point regarding the qualified appraisals, and why --

4 JUDGE GARLAND: Can I just pass on the qualified
5 easement for one second? The question that --

6 MR. ONDA: Yes.

7 JUDGE GARLAND: -- Judge Silberman began with, are
8 you any more familiar than opposing counsel is with whether
9 there are identical easements that the IRS has let pass in the
10 past?

11 MR. ONDA: Your Honor, there are, the way I should
12 answer that is there are over 1,100 easements that the
13 L'Enfant Trust has, they all take substantially the same form
14 as this easement. There are cases in the Tax Court that the
15 IRS, or there are cases that the IRS has examined with these
16 easements. I am not familiar with any case that has directly
17 pointed to this language to say that this is a basis for
18 saying that this does not qualify, a qualified conservation
19 easement.

20 JUDGE GINSBURG: Does or does not?

21 MR. ONDA: Does -- I am not aware of any.

22 JUDGE GINSBURG: Either way.

23 MR. ONDA: The basis of attack seems to be that
24 number one --

25 JUDGE SILBERMAN: Wait a minute. And also there are

1 other conservation organizations that have similar easements
2 throughout the District, right?

3 MR. ONDA: Throughout the District, Your Honor, and
4 throughout --

5 JUDGE SILBERMAN: And throughout the country.

6 MR. ONDA: -- the United States.

7 JUDGE SILBERMAN: Yes.

8 MR. ONDA: Quite a few.

9 JUDGE SILBERMAN: Is this the first case that's come
10 to any Court of Appeals on this?

11 MR. ONDA: This is the first case before the Court
12 of Appeals dealing with this issue. Now, there was another
13 case, the White House cases down in New Orleans in the Fifth
14 Circuit that dealt with a valuation issue on these cases. But
15 this is the first case dealing with this issue.

16 JUDGE GARLAND: And there are no advisory letters or
17 anything like that from the IRS on this topic?

18 MR. ONDA: Dealing with the conversation easement?
19 The conversation --

20 JUDGE GARLAND: Yes.

21 MR. ONDA: -- purpose? No, Your Honor.

22 JUDGE GINSBURG: Mr. Onda, was Mr. Donnelly, your
23 appraiser, in some way specially qualified by the IRS or
24 otherwise to do easement appraisals?

25 MR. ONDA: Your Honor, his experience would have

1 provided him the knowledge to do this type --

2 JUDGE GINSBURG: So, there's no special
3 certification or anything like that?

4 MR. ONDA: At that time there was not, Your Honor.

5 JUDGE GINSBURG: There is now.

6 MR. ONDA: In fact, there was no special rules. If
7 you looked at the valuation treaties at that time it was a
8 before and after basis, and there was really no comparable
9 sale --

10 JUDGE GINSBURG: Okay.

11 MR. ONDA: -- method in which to do the after
12 valuation method.

13 JUDGE GINSBURG: All right. Now, there was the --
14 as of the time these appraisals were done there was this piece
15 on the website of the --

16 MR. ONDA: That's correct, Your Honor.

17 JUDGE GINSBURG: -- Revenue Service --

18 MR. ONDA: Yes.

19 JUDGE GINSBURG: -- giving some guidance, since
20 repudiated or withdrawn, at least, establishing a range of 10
21 to 13 percent as the ordinary parameters for a facade
22 easement, right?

23 MR. ONDA: Yes.

24 JUDGE GINSBURG: Your two properties came in with
25 suggested percentages of 11 and 13.

1 MR. ONDA: Yes.

2 JUDGE GINSBURG: What in the record is there to
3 explain the difference between those two percentages?

4 MR. ONDA: The differences between those two?

5 JUDGE GINSBURG: Yes.

6 MR. ONDA: I believe that during Mr. Donnelly's
7 testimony in the Tax Court what he had indicated, and I
8 believe Ms. Simmons also had indicated was that the valuation
9 of the Logan Circle property was a greater value because of
10 the view the Logan Circle property had with respect to the --

11 JUDGE GINSBURG: Well, that went into the I thought
12 the value of the property.

13 MR. ONDA: Yes, Your Honor.

14 JUDGE GINSBURG: But I'm talking about the
15 percentage.

16 MR. ONDA: Well, the Logan Circle property is also a
17 detached structure, so that it would have more, it would have
18 four sides in which you would have to maintain.

19 JUDGE GINSBURG: Well, is the facade more than the
20 front?

21 MR. ONDA: Yes, Your Honor, this is an envelope
22 facade. This encompasses the entire --

23 JUDGE GINSBURG: Okay.

24 MR. ONDA: -- property. The entire --

25 JUDGE GINSBURG: Okay. That's a more adequate

1 answer. I didn't --

2 MR. ONDA: Thank you, Your Honor.

3 JUDGE GINSBURG: -- realize that. Thank you. As
4 for the substantiality of the basis here of the stated method
5 required --

6 MR. ONDA: Yes.

7 JUDGE GINSBURG: -- your appraiser does say, you
8 know, I talked to some folks, I looked at some pieces, I had
9 some conjectural and speculative considerations, doesn't tell
10 us who, doesn't tell us where, doesn't tell us what those
11 considerations were. It seems like a fragile point in the
12 appraisal.

13 MR. ONDA: Your Honor, I would agree, except for the
14 fact that that's all that the regulation requires is the
15 disclosure of that method. And if you look at the intent of
16 Congress in --

17 JUDGE GINSBURG: Well, I mean, if that's the method,
18 pardon me, that's like saying I used a comparable properties
19 method and --

20 MR. ONDA: Yes.

21 JUDGE GINSBURG: -- not telling us what the
22 properties are.

23 MR. ONDA: But, Your Honor, you're right. But the
24 purpose of this regulation was, the substantiation regulation,
25 was to provide a tool for the IRS, a mechanism so that they

1 would have information with which to determine the correctness
2 of a valuation.

3 JUDGE GINSBURG: Well, you can do that --

4 MR. ONDA: That tool --

5 JUDGE GINSBURG: -- on the face of the page if you
6 lay out the comps, as Walman did in his appraisal.

7 MR. ONDA: That's correct.

8 JUDGE GINSBURG: But if you say I had subjective and
9 speculative considerations involved how does the IRS evaluate
10 it?

11 MR. ONDA: Well, the IRS -- well, number one, Your
12 Honor, the return information that's submitted with the return
13 is an appraisal summary that's signed by the appraiser. It
14 doesn't need to include the valuation method, the specific
15 basis, or anything else. They are required to maintain a
16 qualified appraisal in the records. This appraisal was
17 maintained. The IRS looked at that appraisal, if they had
18 questions regarding the method or whatever else they should
19 have asked the appraiser --

20 JUDGE GINSBURG: Well, the purpose of these --

21 MR. ONDA: -- for his file.

22 JUDGE GINSBURG: -- the purpose of these regulations
23 is so that they don't have to ask a tax payer, right? You're
24 supposed to supply all the information so they can look at it.

25 MR. ONDA: No, that's not correct, Your Honor. The

1 only information to be supplied with the return is the
2 appraisal summary, and that's the form 8283.

3 JUDGE GINSBURG: And that doesn't call for the
4 stated evaluation method?

5 MR. ONDA: No, it does not, Your Honor.

6 JUDGE GARLAND: So, that comes --

7 JUDGE GINSBURG: Okay.

8 JUDGE GARLAND: -- during an audit, or something
9 like that --

10 MR. ONDA: That comes during --

11 JUDGE GARLAND: -- is that right? So --

12 MR. ONDA: -- an audit, Your Honor. Yes.

13 JUDGE GARLAND: -- you have filed the IRS form with
14 your tax return --

15 MR. ONDA: Yes.

16 JUDGE GARLAND: -- it says the appraisal approves
17 this amount --

18 MR. ONDA: And the appraiser signs that.

19 JUDGE GARLAND: Yes, I understand. And then if the
20 IRS thinks that looks funny, or if they have an automatic
21 program, or whatever else causes an audit, during the audit
22 they can look at all the work papers, is that right?

23 MR. ONDA: That's correct.

24 JUDGE GARLAND: All right.

25 JUDGE SILBERMAN: Counsel, the truth of the matter

1 underlying all of this is there's no way on God's green earth
2 anybody can figure out what the real reduction in value is on
3 the part of these easements, isn't that true?

4 MR. ONDA: I would agree with that, Your Honor.

5 JUDGE SILBERMAN: And all this talk about making a
6 comparative sales, comparative, is really bologna because
7 nobody can figure out what the decrease in value is, isn't
8 that the truth?

9 MR. ONDA: I think it's very difficult to determine
10 the value.

11 JUDGE SILBERMAN: Right. And that's one of the
12 reasons why these easements are so attractive, because the
13 truth of the matter is for most people giving up the easement
14 is giving up very little, they don't want to change the brick
15 facade of a Colonial style house, nobody does, so they don't
16 want to put up a glass window or something like that. So,
17 that's why they're so attractive. But the problem is Congress
18 and the IRS, and your position is basically that an honest
19 appraisal is not, appraiser is not going to be able to really
20 come up with comparables that make any sense at all.

21 MR. ONDA: I think you can have five appraisers that
22 will come up with five different answers.

23 JUDGE GINSBURG: Well, Walman came up with
24 comparables for properties subject to easement, right? And
25 looked at before and after transactions.

1 MR. ONDA: He said we had differences as to whether
2 those were truly comparables, but even in his appraisal, Your
3 Honor, as we discussed in our brief, when you look at his --
4 when you utilize the Donnelly before value which was adopted
5 by the Tax Court, and then you utilize Walman's after value
6 there isn't a value decrease.

7 JUDGE GINSBURG: That's an interesting point. Is
8 that in your brief?

9 MR. ONDA: Yes, it is, Your Honor.

10 JUDGE GINSBURG: Okay. That's --

11 JUDGE GARLAND: Can I ask the question I was trying
12 to ask before? So, and maybe the IRS did take this approach
13 below, instead of saying this is completely out because it's
14 not a qualified appraisal, or because it's not a conservation
15 purpose in perpetuity, they had simply said, you know,
16 Walman's value is better, your value is not supported, the
17 difference between agreeing to be bound by the law and
18 agreeing to be bound by an easement is not much of a
19 difference, and so you're only entitled to X rather than Y,
20 they could have done that during the audit and simply
21 disallowed as of some smaller amount of the deduction, or
22 could they not have done that?

23 MR. ONDA: Yes, they could, Your Honor.

24 JUDGE GARLAND: And is that the kind of approach
25 they also took in the Tax Court in addition to the attack on

1 being able to make any deduction at all?

2 MR. ONDA: They took the approach that the value was
3 zero, so there was no --

4 JUDGE GARLAND: I see. So, it's all or nothing,
5 basically?

6 MR. ONDA: It was an all or nothing approach, Your
7 Honor.

8 JUDGE GARLAND: But they could have simply said
9 along the lines of what Judge Silberman's saying that well,
10 these particular tax payers, and I'm not saying this is true,
11 but if they thought it they could say these particular tax
12 payers have not actually agreed to very much, they wouldn't
13 have made much of a difference, and therefore their deduction
14 is only, I don't know, \$10,000?

15 MR. ONDA: Correct.

16 JUDGE GARLAND: And then the tax payers could have
17 challenged that valuation, and that's what would have been
18 before the Court?

19 MR. ONDA: That's correct. The one point I would
20 like to come back to, Your Honor, is that you talk about that
21 there's not much difference, I think in this case, and I think
22 that actually depends upon the organization, in this case I
23 think the record was very clear that L'Enfant Trust is very
24 active in their enforcement, so, and I think the Tax Court did
25 find that as result of that there was additional financial

1 burdens imposed on the tax payer in this case.

2 JUDGE GINSBURG: Isn't that a rather transient
3 consideration to say well, the District doesn't enforce its
4 laws as vigorously as the Trustee does?

5 MR. ONDA: Well, it's an issue of valuation, and I
6 think that if you have an organization that is going to impose
7 a higher standard, so if we say that you cannot, you know, you
8 need our approval to replace a window --

9 JUDGE GINSBURG: Well, that's different, but insofar
10 as the substantive burdens are the same, part of your argument
11 was that L'Enfant is more vigorous in enforcing them, and that
12 the District has only a reactive program if someone complains.

13 MR. ONDA: That is correct. That's part of the
14 argument. The second part of that argument is that the
15 standards in which L'Enfant requires changes to be made is a
16 higher standard than that required by the District.

17 JUDGE GINSBURG: There's the color of the door and a
18 couple of other things, right?

19 JUDGE SILBERMAN: Well, a comparable analogy would
20 be suppose you paid for a private contractor to police your
21 brick sidewalk because it's often crumbling, one could argue
22 the city has an obligation to fix that, but you'd still have
23 to pay a lot of money to have a private contractor police that
24 because the city is not as zealous as a private contractor
25 would be.

1 MR. ONDA: That's correct.

2 JUDGE SILBERMAN: As a matter of fact, that
3 hypothetical is real.

4 MR. ONDA: Yes. Your Honor, I guess the last point
5 I would like, one of the last points I'd like to make on the
6 qualified easement is that it is, that affirming the Tax Court
7 decision is I think consistent with the legislative intent
8 behind DEFRA and the substantiation regulations. As I said,
9 the mechanism, or the, there were two competing goals there,
10 the first was to prevent the prevalent use of these over-
11 valuations, and Congress could have done that by simply saying
12 with respect to appreciated property the donor gets a
13 deduction for the adjusted basis, and not the fair market
14 value, that would have eliminated the problem. However,
15 Congress was concerned about the charities that depend upon
16 these types of properties for their exempt purposes and for
17 fund raising purposes. They wanted to maintain that benefit
18 so that these charities would benefit by donations of
19 appreciated property. So, what they did is they enhanced the,
20 they enacted the substantiation requirements to provide a tool
21 which the IRS never had to evaluate these appraisals. They
22 also enhanced the penalty provisions, they now made a penalty
23 for a valuation over statements instead of a graduated 10, 20
24 and 30 percent, if it's an over-valuation in a charitable
25 contribution setting it's a flat 30 percent if it's in excess

1 of 150 percent of the value. So, no graduated percentage as
2 in other situations a flat 30 percent.

3 JUDGE GARLAND: Say it again, a flat 30 percent for
4 what?

5 MR. ONDA: For the understatement that's caused by
6 an over-valuation.

7 JUDGE GINSBURG: That's the penalty.

8 JUDGE GARLAND: You mean the penalty?

9 MR. ONDA: The penalty.

10 JUDGE GARLAND: Yes.

11 MR. ONDA: That's correct. And then finally, by
12 requiring the appraiser to sign the appraisal summary the
13 appraiser was now subject to abating penalties under 6701, so
14 now the appraiser if he falsified an appraisal, or potentially
15 did something wrong he was subject to penalties. So, it was a
16 two-prong attack, stronger substantiation requirements,
17 enhanced penalties. But the substantiation requirements were
18 not meant to eliminate the need of the Internal Revenue
19 Service to go in and evaluate these appraisals and take that
20 second step, and that's what I believe the Government would
21 like us to say. They never cross-examined Mr. Donnelly during
22 the trial, never asked him a question regarding his
23 valuations.

24 JUDGE GINSBURG: Thank you, Mr. Onda.

25 MR. ONDA: Thank you, Your Honors.

1 JUDGE GINSBURG: Mr. Urda, you've more than used
2 your time, but we'd like to give you a minute to reply.

3 ORAL ARGUMENT OF PATRICK J. URDA, ESQ.

4 ON BEHALF OF THE APPELLANT

5 MR. URDA: Thank you, Your Honors. I think that the
6 colloquy between you, Judge Silberman, and opposing counsel
7 hit it right on its head, five appraisers could come up with
8 five different numbers, that's precisely why it's so important
9 to have this specific basis for these appraisals so that the
10 IRS can figure out what's right and what's wrong, or at least
11 have some clue to it.

12 JUDGE SILBERMAN: I think it's an illusion, I don't
13 think it's possible to have a real persuasive appraisal of the
14 difference in value of these easements. I think it's -- and I
15 think we're all kidding ourselves, and probably the IRS ought
16 to handle it by just saying this is a flat figure we'll
17 accept, which is what the IRS originally did.

18 MR. URDA: That might be the case, Judge, but under
19 DEFRA they do have these regulations --

20 JUDGE SILBERMAN: Yes, I --

21 MR. URDA: -- and this did not comply.

22 JUDGE SILBERMAN: All right.

23 JUDGE GARLAND: Can I ask one -- I'm sorry --

24 MR. URDA: Certainly, Judge.

25 JUDGE GARLAND: -- that's just before, this is on

1 the lender subordination.

2 MR. URDA: Certainly.

3 JUDGE GARLAND: You are still maintaining that the
4 lender didn't subordinate here?

5 MR. URDA: Certainly.

6 JUDGE GARLAND: And what do you do with this part D
7 of the easement that says lender hereby subordinates and then
8 the lender acknowledgment on the next page?

9 MR. URDA: I think that the lender acknowledgment,
10 without knowing that the lender is -- he acknowledged that
11 there is going to be an easement, but from how I read the
12 acknowledgment it's not clear that the lender acknowledged to
13 be bound.

14 JUDGE GARLAND: So, this is a question of District
15 of Columbia property law, not really a question of IRS at all?
16 If you have an easement in which it says you agree to be
17 subordinated, and then you sign an acknowledgment on the next
18 page that's a question of basically property or contract law,
19 isn't it?

20 MR. URDA: That small point, yes, it might be.

21 JUDGE GARLAND: So, this is just a small -- that's
22 not the --

23 MR. URDA: That's right.

24 JUDGE GARLAND: It's appropriate to describe this as
25 a small point, is that right?

1 MR. URDA: That's correct.

2 JUDGE GINSBURG: Why does any lender agree to be
3 subordinate?

4 MR. URDA: Beg your pardon?

5 JUDGE GINSBURG: Why does a lender ever agree to be
6 subordinated?

7 MR. URDA: Well, Judge, that's an interesting
8 question. Maybe there isn't too much there that he's
9 subordinated to.

10 JUDGE GINSBURG: So, he thinks that there's a very
11 slight diminution, or maybe an increase in value?

12 MR. URDA: I think that that might be as the
13 Treasury regulations themselves provide.

14 JUDGE GINSBURG: Any indication that some lenders
15 are compensated for subordination?

16 MR. URDA: I don't believe that there's any in this
17 record.

18 JUDGE GINSBURG: But that's not beyond the realm of
19 possibility in other cases?

20 MR. URDA: I don't think it's beyond the realm of
21 possibility at all.

22 JUDGE GINSBURG: Okay.

23 MR. URDA: I'm sure there are lots of assurances
24 going on.

25 JUDGE GINSBURG: Thank you --

1 MR. URDA: Thank you.

2 JUDGE GINSBURG: -- Mr. Urda. Mr. Onda, thank you.

3 Case is submitted.

4 (Recess.)

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DIGITALLY SIGNED CERTIFICATE

I certify that the foregoing is a correct transcription of the electronic sound recording of the proceedings in the above-entitled matter.



Paula Underwood

February 13, 2011

DEPOSITION SERVICES, INC.