United States Tax Court

T.C. Memo. 2026-68

MALIBU VALLEY LAND, LLC, SPECTRUM DEVELOPMENT, INC., TAX MATTERS PARTNER,
Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

Docket No. 20442-19. Filed August 17, 2026.

Vivian D. Hoard and *Adam R. Young*, for petitioner.

Lori A. Amadei, *Henry C. Bonney*, *Paulmikell A. Fabian*, *Virgil C. Southall*, and *Richard L. Wooldridge*, for respondent.

MEMORANDUM FINDINGS OF FACT AND OPINION

GREAVES, *Judge*: This case involves a noncash charitable contribution deduction reported for tax year 2014. Malibu Valley Land, LLC (MVL), reported a deduction of $32,075,000 for its grant to the Mountain Recreation & Conservation Authority (MRCA) of a perpetual conservation easement over 297.84 acres of real property with entitled development rights (conservation easement) on December 30, 2014 (donation date). In a Notice of Final Partnership Administrative Adjustment (FPAA), the Internal Revenue Service (IRS or respondent) disallowed the deduction for failure to comply with the technical requirements of section 170.[1] In the alternative, respondent asserts that the conservation easement was worth $4,650,000.

[1] Unless otherwise indicated, statutory references are to the Internal Revenue Code, Title 26 U.S.C. (Code), in effect at all relevant times, regulation references are

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[*2] The parties agree that in this case the income approach provides credible evidence of value, distinguishing this case from recent conservation easement cases before this Court. The wide valuation gap between the parties turns largely on a single issue: the property's development potential. The record leaves no question that the property has development potential and attendant value. The property is the subject of one of the oldest vesting tentative tract maps in the State of California and enjoys a location that is far superior to large-acre tracts just miles away. Determining the extent of that value, however, requires us to delve into underdeveloped portions of California land-use law stretching back nearly four decades.

FINDINGS OF FACT

The following facts are derived from the pleadings, the stipulation of facts with attached exhibits, and the testimony of fact and expert witnesses admitted into evidence at trial. MVL was a California limited liability company that is subject to TEFRA for its taxable year ending December 31, 2014.[2] Spectrum Development, Inc. (petitioner or Spectrum), was MVL's tax matters partner. MVL had its principal place of business in California when the petition was filed. After concessions, the issues before the Court are (1) whether MVL had the requisite donative intent to claim a charitable contribution deduction for the conservation easement, (2) the value of the conservation easement, (3) whether the investment interest limitations apply to $450,000 of interest MVL paid to a creditor, and (4) whether accuracy-related penalties apply.[3]

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to the *Code of Federal Regulations*, Title 26 (Treas. Reg.), in effect at all relevant times, and Rule references are to the Tax Court Rules of Practice and Procedure.

[2] Before its repeal, the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), Pub. L. No. 97-248, §§ 401–407, 96 Stat. 324, 648–71, governed the tax treatment and audit procedures for many partnerships, including MVL.

[3] In its petition, petitioner also argues that respondent erred in adjusting the amounts of capital contributions and distributions for MVL. However, petitioner failed to address these adjustments to any meaningful extent at trial or on brief. We therefore conclude that petitioner has abandoned any arguments or contentions related to these issues. *See Thiessen v. Commissioner*, 146 T.C. 100, 106 (2016) ("[I]ssues and arguments not advanced on brief are considered to be abandoned."); *Mendes v. Commissioner*, 121 T.C. 308, 312–13 (2003); *Nicklaus v. Commissioner*, 117 T.C. 117, 120 n.4 (2001); *see also* Rule 151(e)(4) and (5) (requiring that a party's brief set forth and discuss the points and arguments on which the party relies). Respondent

[*3] I. *Location, Location, Location*

The Santa Monica Mountains region of Los Angeles (LA) County, California, offers a retreat for the wealthy looking to escape the hustle and bustle of the city. Those who have sought this refuge include King Gillette, a business tycoon of the shaving industry; equestrian aficionados looking for large rural estates; and hip-hop star Ye (previously known as Kanye West).

The 297.84 acres over which MVL granted the conservation easement and a contiguous 18.43 acres sit within the Santa Monica Mountains region (together, subject property). The subject property is approximately 3 miles south of Calabasas, 6 miles north of Malibu, and 25 miles from downtown LA. The region is serviced by four major highways that connect to the Ventura Freeway and the Pacific Coast Highway. The subject property is approximately four miles south of the Ventura Freeway and abuts Mulholland Highway, a secondary scenic highway that provides access to the interior of the region.

A portion of the subject property lies within the Mulholland Scenic Corridor. Since at least 1981, LA County has imposed additional safeguards to restrict development in this scenic corridor to preserve the character of the area. The subject property also hosts rare species of plants and animals. LA County designated southern portions of the subject property as areas containing sensitive environmental resources of the highest significance, rarity, and diversity (H1) and sensitive environmental resources of high significance, rarity, or diversity (H2).

Aside from a few high-end subdivisions, the area surrounding the subject property remains largely undeveloped as of the donation date because of long-running conservation efforts to preserve the area's beauty and resources by the State of California, LA County, and private donors. One such resource is the Stokes Canyon watershed, one of the most pristine watersheds in the Santa Monica Mountains region. To protect this watershed and other resources, state and local government agencies purchased and dedicated open spaces in the area to public recreation. One of the subject property's largest neighbors is the King Gillette Ranch, a 588-acre parcel now part of the Malibu Creek State Park. The King Gillette Ranch is owned by MRCA, a quasi-

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has conceded that MVL satisfied the other technical requirements of section 170 and that the property was not inventory.

All dollar amounts have been rounded to the nearest whole dollar.

[*4] governmental entity charged with preservation and education. MRCA purchased the ranch in the 2000s for $33 million and converted it into a recreational and educational destination.

The subject property features varied topography, including rugged peaks and ridges, steep canyons, rolling hills, and pastoral valleys. Much of the property is sloped, and in 2004 LA County designated several of its slopes as significant ridgelines.[4] These ridgelines offer views of the surrounding mountains, canyons, and valleys. The ocean is not visible from the subject property.

II. *Ownership and Development of a Vesting Tentative Tract Map*

A. *Acquisition and Entitlement*

Brian Boudreau's involvement with the subject property started in 1978 when he was 11 years old. His father, Charles Boudreau, was a highly experienced real estate advisor and dealer in the Santa Monica Mountains region. He bought attractive land, perfected entitlements to build on the land, and flipped the now-entitled land to developers.

Charles was also a religious man, and he took his son with him to weekly services at the Claretian Theological Seminary located near the subject property. The Claretian Theological Seminary had substantial land holdings in the area. Given Charles's knowledge of real estate, the Claretian Theological Seminary asked him to act as its real estate advisor.

In this role Charles became friends with the Claretian Theological Seminary's trust advisor. They worked together to manage the church's property holdings for over six years. Eventually, the pair determined that the church should dispose of most of its real estate. For a buyer, they looked no further than Charles.

On May 22, 1978, the Claretian Theological Seminary sold 443 acres in the Santa Monica Mountains region (Boudreau Family Land) to Malibu Valley Farms, Inc., an entity owned by Charles. Charles took the most logical step with his background: He considered adding entitlements to the land for future development. In 1984 the California legislature adopted the vesting tentative tract map scheme, which, as

[4] A significant ridgeline is one that has been identified as a scenic resource because it is highly visible and dominates the landscape. LA County, Cal., LA County, Cal. Planning and Zoning Ord. 2004-0072, § 1 (Dec. 7, 2004).

[*5] discussed *infra*, generally permits developers, upon approval of a vesting tentative map, to rely on the local ordinances in effect when the subdivision application was deemed completed, rather than ordinances adopted later in the development process. *See* Cal. Gov't Code § 66498.9(b) (West 2014); *see also id.* §§ 66498.1 through 66498.9. Charles set his sights on this new entitlement.

The Subdivision Map Act generally requires approval of subdivision applications, subject to limited exceptions that are not relevant here. *Id.* § 66426. It establishes a two-step approval process. First, the subdivider submits a tentative map proposing the division of property into five or more lots. *Id.* The local agency reviews the tentative map for compliance with applicable local law. *Id.* §§ 66473.5, 66474. In LA County, the tentative tract map is reviewed by the County Board of Supervisors. Approval of a tentative map does not create legal lots; it merely establishes a framework for future development. *Id.* § 66429.

Legal lots are created in the second step, when the subdivider submits a final map for approval and recordation. This final map is more detailed than the tentative map and must depict the required infrastructure and improvements to serve the new lots. *Id.* §§ 66456, 66456.2, 66457. It must substantially conform to the approved tentative map, satisfy any conditions that the local agency placed on the tentative map, and comply with subdivision ordinances applicable when final approval is sought. *Id.* § 66458(a). In LA County, the final map is reviewed by the County Board of Supervisors. A subdivider may not sell lots before the final map is recorded. *Id.* § 66499.30(a).

Because development and final approval of the subdivision can take years—and local ordinances may change during that time—the legislature adopted the vesting tentative tract map scheme.[5] *See id.* § 66498.9(b); *see also id.* §§ 66498.1 through 66498.9. A vesting tentative tract map generally "locks in" the local ordinances, policies, and standards in effect when the application is deemed complete. *Id.* § 66498.1(b). Vesting tentative maps apply only to residential

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[5] The rights conferred by a vesting tentative tract map have not materially changed since the statute was adopted.

It is unclear from the record what, if any, additional application requirements applied to a vesting tentative tract map as compared to a tentative tract map at the time Charles applied. As of the donation date, the LA County Code required only that the map be labeled with "Vesting Tentative Map." LA County, Cal., Code § 21.38.040 (2014).

[*6] subdivisions and may be filed whenever the Subdivision Map Act requires a tentative map, that is, in step 1 of the approval process. *Id.* §§ 66498.7, 66498.1(a). Much as with a tentative tract map, the local agency reviews the application to determine compliance with local ordinances, policies, and standards in effect at the time the application was complete. *Id.* §§ 66498.1(b), 66474.2(a). If approved, the vesting tentative tract map confers the right to proceed with development in "substantial compliance with the [local] ordinances, policies, and standards" in effect when the application was complete, subject to reasonable conditions imposed before recordation. *Id.* §§ 66498.1(b) and (c), 66498.6.

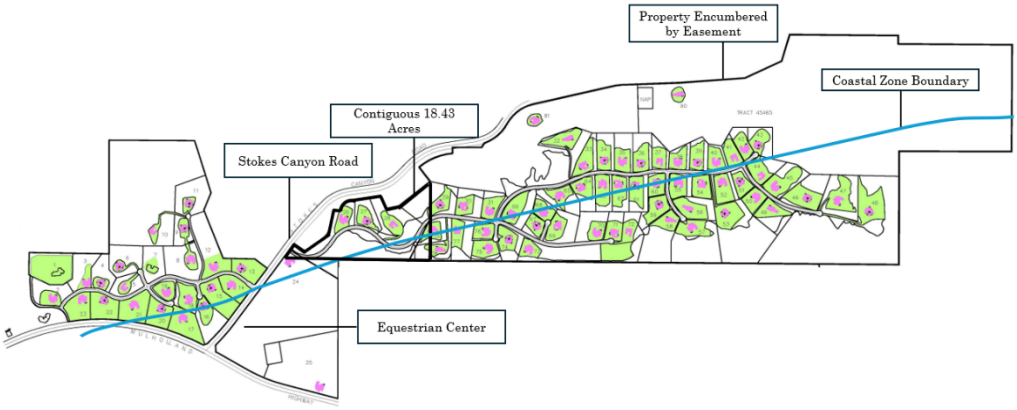
The vested rights conferred by a vesting tentative tract map are limited. *Id.* § 66498.6(b). A subdivider receives no vested development rights with respect to state or federal law. *Id.* In addition, the vested development rights do not last indefinitely. The vesting tentative tract map has an initial life of at least one year, as set by the local agency, but it may be extended for various reasons including progress in recording a portion of the map, permitting delays, or litigation. *Id.* § 66498.5(b) and (c). If a subdivider satisfies the conditions of approval and complies with the local law in effect when the vesting tentative tract map was approved, the local agency must approve and record a final map that substantially conforms with the vesting tentative tract map. *See id.* § 66474.1. Because the vesting tentative tract map does not create legal lots, the lots proposed on a vesting tentative tract map cannot be sold until the final map is recorded. *Id.* § 66499.30(a).

B. *Drafting of Vesting Tentative Tract Map 45465*

Charles, through his entity Malibu Valley Farms, Inc., retained HMK Engineering to prepare Vesting Tentative Tract Map 45465 (VTTM) that covered a portion of the Boudreau Family Land, including the subject property. On July 15, 1987, HMK Engineering provided Charles with a draft VTTM setting forth 81 proposed lots. HMK Engineering made subsequent amendments to the map before it was completed in 1988. The VTTM is depicted below, as amended in 1988:[6]

[6] This depiction, offered by petitioner, matches the plans HMK Engineering designed in 1987 and amended in 1988. We have superimposed the coastal zone boundary from other maps in evidence. This map is offered solely for illustrative purposes.

[*7]



The VTTM area is bisected by Stokes Canyon Road, a two-lane paved roadway that runs diagonally through the tract. This road serves as the primary dividing line for purposes of our discussion. The portion of the VTTM area west of Stokes Canyon Road consists of 23 lots, each planned for a single-family residence. Development activity before the donation date was concentrated on this western portion. Although it is not part of the subject property, the western portion provides useful information regarding the procedures and costs associated with development in accordance with the VTTM. Its topography is comparable to the rest of the VTTM area.

Our focus is on the portion of the VTTM area east of Stokes Canyon Road. This area includes the subject property and an equestrian center. In total, the VTTM shows 56 lots east of Stokes Canyon Road on the subject property, each intended for a single-family residence. The contiguous 18.43-acre portion of the subject property is a triangular parcel immediately east of Stokes Canyon Road. The VTTM depicts three lots on this contiguous portion. Immediately east of this parcel lies the 297.84-acre portion encumbered by the conservation easement. This portion is irregularly shaped and is depicted on the VTTM as containing 53 lots. Finally, south of the subject property, near the intersection of Stokes Canyon Road and Mulholland Highway, is an equestrian center. The equestrian center predates the VTTM and did not receive entitlements under the VTTM because it is a commercial property.

The final feature of note is the line running diagonally across the property. This line marks the boundary of the coastal zone established under the California Coastal Act (Coastal Act). The subject property

[*8] south of the line is within the coastal zone (southern portion),[7] while the subject property north of the line lies outside of it (northern portion).[8] The California Coastal Commission (Coastal Commission) has primary authority over development within the coastal zone. Cal. Pub. Res. Code §§ 30300, 30330. On the subject property, 22 lots are in the northern portion[9] and 34 lots are in the southern portion.[10]

The northern portion is approximately 191.65 acres, and the southern portion is approximately 124.35 acres.[11] As of the donation date, the northern portion was zoned A1 (Light Agricultural), while the southern portion was primarily zoned RL20, which permits one single-family residence per 20 acres. A small section of the southern portion was zoned RL10, which permits one single-family residence per 10 acres.

As discussed in greater detail *infra*, subdivision within the coastal zone is complicated and expensive. Accordingly, subdividers seek to avoid it where possible. The Coastal Act nevertheless provides a

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[7] The coastal zone generally extends from the coast to 1,000 yards from the mean high tide line of the sea. Cal. Pub. Res. Code § 30103(a) (West 2014). In significant habitat or recreation areas, it extends inland to the lesser of the first major ridgeline or five miles from the mean high tide line of the sea. *Id.*

[8] The unincorporated area north of the coastal zone to approximately the 101 Freeway is referred to as the "North Area" and is subject to specific provisions governing development. *Land Use Pres. Def. Fund v. Cnty. of L.A.*, No. B190846, 2007 WL 686733, at *1 n.2 (Cal. Ct. App. Mar. 8, 2007).

[9] These lots are designated by the following numbers: 26–43, 64, 65, 80, and 81. On average these lots are 8.7 acres with a 1.02-acre building pad. Lots 80 and 81 are the largest lots at 112.96 acres and 34.25 acres, respectively.

[10] The following 13 lots are bisected by the coastal zone boundary: 44, 54, 55, 60–63, 66–68, 76, 77, and 79. We include these lots in the southern portion. The portions of these lots located within the coastal zone are governed by the Coastal Act. *Sierra Club v. Cal. Coastal Comm'n*, 111 P.3d 294, 303 (Cal. 2005) (holding that when a lot straddles the coastal zone boundary, the Coastal Commission retains jurisdiction over development for the portion of the lot within the coastal zone). Petitioner provided no analysis on the process of reconfiguring these lots to exclude the portions located in the coastal zone, which can be a years-long process. Nor did any expert opine on whether LA County would review the necessary lot adjustments as in substantial compliance with the VTTM. Consequently, we will treat these 13 lots as part of the southern portion of the subject property.

[11] Neither party provided us with the exact acreage of either part of the subject property. To determine the approximate acreage in the northern portion, we added together the sizes of the lots identified as being located in the northern portion. Our estimate is consistent with estimates from LA County in the record.

Even though the northern portion contained more acreage, it had fewer lots than the southern portion because of its difficult terrain.

[*9] procedure to request an adjustment to the coastal zone boundary from the Coastal Commission. Cal. Pub. Res. Code § 30103(b). In 1987 Charles invoked that procedure and asked the Coastal Commission to move the coastal zone boundary line such that the lots proposed on the property to the west of Stokes Canyon Road would be outside the coastal zone.

The Coastal Commission denied this request, concluding that the proposed boundary adjustment would be inconsistent with the policies of the Coastal Act. The Commission found that moving the boundary would place a portion of the proposed development beyond the Coastal Commission's jurisdiction, and ultimately beyond LA County's oversight. Without that oversight, the Coastal Commission explained that it could not preserve scenic and visual resources, protect environmentally sensitive areas, or limit development consistent with applicable density policies. The Coastal Commission determined that any further subdivision of the affected land would require participation in its transfer development credit program[12] to limit new development in the region and ensure that the proposed boundary adjustment would be consistent with the Coastal Act.

C. *Submission and Approval of the VTTM*

In 1987 Malibu Valley Farms, Inc., submitted applications for the VTTM, a conditional use permit, and an oak tree permit.[13] As discussed above, approval of the VTTM entitles the developer to build in accordance with the approved map, subject to any conditions expressly reserved in the VTTM. Cal. Gov't Code §§ 66498.1(b) and (c), 66498.6. A conditional use permit was required to grade slopes exceeding 25%.

The oak tree permit was required to remove any oak trees within the VTTM area. LA County, Cal. Planning and Zoning Ord. 82-0168, § 2 (July 20, 1982). In the unincorporated area of LA County, a landowner generally may not remove or damage any oak tree with a circumference of 25 inches or more, nor may a landowner grade, pave, trench, or

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[12] As discussed in greater detail *infra*, the transfer development credit program generally requires a developer to retire parcels of land that could otherwise be developed in exchange for the opportunity to record new lots in the coastal zone. Generally, these programs are created in local coastal plans. *See* LA County, Cal., Code § 22.44.1230. The Coastal Commission also had its own transfer development credit program.

[13] The exact date that Malibu Valley Farms, Inc., submitted its application is unclear.

[*10] otherwise disturb soil within an oak tree's canopy. *Id.* §§ 1 and 2. The oak tree permit application required property and construction information, a site plan identifying the location of all oak trees, and an oak tree report evaluating their health. *Id.* LA County could also require planting replacement oak trees elsewhere on the property. *Id.* An oak tree permit expired on the date specified on the permit, or if no date was specified, one year after issuance, and could be extended for one additional year. *Id.* The oak tree permit application submitted with the VTTM sought approval to remove between 52 and 78 oak trees—less than 3% of the oak trees within the VTTM area.

LA County reviewed the VTTM and associated permit applications for compliance with all applicable state and local laws and to ensure adequate environmental protection. This review process was largely driven by the California Environmental Quality Act. This Act requires California public agencies, including the LA County Board of Supervisors, to conduct an environmental review of any discretionary project and to prepare an environmental impact report (EIR) for any project that may have a significant effect on the environment. Cal. Pub. Res. Code § 21100(a). The VTTM qualified as a "project" under the California Environmental Quality Act and was therefore subject to the Act's requirements. *See id.* § 21065(c).

In March 1988 LA County began to prepare a draft EIR for the proposed VTTM, conditional use permit, and oak tree permit. The draft EIR concluded that the proposed development would not result in any significant environmental impacts. It further determined that the land covered by the VTTM was not designated as a significant ecological area or buffer area and that the proposed density complied with zoning requirements.

LA County further found that the VTTM complied with all applicable local ordinances, policies, and standards in effect as of the application date, including the LA County General Land Use Plan and the Malibu/Santa Monica Mountains Interim Area Plan (1981 Interim Area Plan) and the Malibu Local Coastal Program Land Use Plan (1986 Malibu LCP LUP). At the time the application was deemed complete, development in the northern portion was governed primarily by the 1981 Interim Area Plan, which emphasized preservation of the area's scenic resources and natural terrain. LA County, 1981 Interim Area Plan 3 (1981). The 1981 Interim Area Plan included policies addressing wildlife habitat and oak tree preservation and identified scenic highways, including Mulholland Highway. *Id.* The plan's map of

[*11] significant environmental areas did not designate any portion of the VTTM area as a significant environmental area. *Id.*, Natural and Historic Resources Map. LA County concluded that the proposed VTTM complied with these requirements.

LA County also reviewed the VTTM for consistency with the 1986 Malibu LCP LUP, which was one piece of the regulatory scheme of the Coastal Act. At the time, the Coastal Act governed development in the southern portion. Several Coastal Act provisions were particularly relevant, including protections for environmentally sensitive habitat areas, standards governing the location of new residential development, and requirements to protect scenic and visual resources by minimizing alterations of natural landforms.

The Coastal Act contemplates significant reliance on local governments through local coastal programs, which consist of a land use plan and implementing ordinances referred to as local implementation plans.[14] When the Coastal Commission certifies both the local land use plan and the local implementation plan, it delegates its authority over development in the coastal zone to the local jurisdiction. Cal. Pub. Res. Code § 30519(a). In 1986 the Coastal Commission certified the 1986 Malibu LCP LUP, but no local implementation plan had been certified.

The 1986 Malibu LCP LUP included policies requiring protection of environmentally sensitive habitat areas, minimizing grading, designing development to reduce impacts to physical features, and preserving scenic and visual resources, including limiting skyline intrusion in highly scenic areas. It also reflected concern with excess development in the coastal zone and identified several strategies to limit development and encourage lot retirement.

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[14] The land use plan is a set of policies related to the Coastal Act and is part of the local government's general plan. Cal. Pub. Res. Code § 30108.5. The local implementation plan provides zoning ordinances and standards to implement the policies of the land use plan. *Id.* § 30108.4. For example, a land use plan may provide the general goal of preserving the scenic resources of an area. The local implementation plan would then provide the specific building requirements that effectuate this policy such as a prohibition of building on scenic ridgetops.

When a local jurisdiction completes either part of its local coastal program, that section is submitted to the Coastal Commission for certification. *Id.* §§ 30510, 30512(a), 30513(a). The Coastal Commission will conduct a public hearing and review the land use plan and/or the local implementation plan for their compliance with the Coastal Act. *Id.* §§ 30512(a), 30513(b). The Coastal Commission then votes on whether to certify the portion of the local coastal program. *Id.* §§ 30512(a), 30513(b).

[*12] LA County found that the proposed VTTM was compatible with the 1986 Malibu LCP LUP. In the draft EIR, LA County noted that 126 acres would be graded but concluded that the proposed grading and development were consistent with applicable ordinances and plans including those governing scenic resource protection in the Mulholland Scenic Corridor. The County also found that the VTTM was consistent with current zoning requirements, and that, with mitigation, the project would not result in significant environmental impacts.

Consistent with the California Environmental Quality Act, LA County circulated the draft EIR to interested agencies for review and comment. Eight agencies commented on the draft EIR, none of which recommended denying the VTTM. The Las Virgenes Municipal Water District raised concerns regarding the water and sewage capacity and recommended conditioning recordation of any final map on upgrading the public systems. LA County adopted the recommendation.

The Coastal Commission also commented on the draft EIR, raising concerns regarding density, cumulative impact of development in the region, grading, impacts to environmentally sensitive areas, removal of native vegetation, and adverse effects on visual resources. LA County made minor revisions to the draft EIR but rejected most of these criticisms. LA County also conditioned the approval of final maps in the coastal zone on obtaining "any permit required for the subdivision under the provisions of the California Coastal Act of 1976" (coastal development permit) or demonstrating that the subdivision was exempt.[15] Because the area lacked a fully certified local coastal program at the time, jurisdiction over any required coastal development permit would have rested with the Coastal Commission.[16]

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[15] Coastal development permits are the primary mechanism used to regulate development in the coastal zone and must be obtained before subdivision may occur in the coastal zone. Cal. Pub. Res. Code § 30600(a).

[16] Before the certification of the local coastal program, the Coastal Commission processes coastal development permits for coastal zone land within the local government's jurisdiction. Cal. Pub. Res. Code § 30604(a). Once the Coastal Commission certifies a local coastal program, the Coastal Commission delegates primary jurisdiction to issue coastal development permits to the local jurisdiction. *Id.* § 30519(a). This delegation means that the certified local coastal program and permits issued pursuant thereto are "not solely a matter of local law, but embody state policy." *See Pac. Palisades Bowl Mobile Estates, LLC v. City of L.A.*, 288 P.3d 717, 721 (Cal. 2012) (quoting *Charles A. Pratt Constr. Co. v. Cal. Coastal Comm'n*, 76 Cal. Rptr. 3d 466, 471 (Ct. App. 2008)). Regardless of whether the primary authority to issue coastal

[*13] The California Environmental Quality Act's final substantive step is certification of the final EIR. Cal. Pub. Res. Code § 21100.1(a). After holding a public hearing, LA County certified the final EIR and approved the VTTM, Conditional Use Permit 87-058, and Oak Tree Permit No. 87-058, finding that the project would not have a significant environmental effect. Certification of the final EIR in 1988 presumptively satisfied the California Environmental Quality Act for purposes of proceeding with the approved project; a subsequent EIR would be required only if there were substantial project changes, changed circumstances, or new information that warranted major revisions. *See id.* § 21166.

LA County initially approved the VTTM for two years, but this period was extended each time a new final map was recorded and for other delays. *See* LA County, Cal., Code § 21.38.060 (2014). The VTTM remained in effect through the donation date.

D. *Brian Takes the Reins*

Where Charles was drawn to real estate, his son Brian found his passion in horses. From a young age Brian spent his free time mucking out stalls at the equestrian center on the Boudreau Family Land. While working at the equestrian center, Brian met Robert Levin, the only other person living on the land covered by the VTTM at that time. The two developed a close friendship through their shared interest in horses.

Around this time, Brian moved to Kentucky to pursue a career in the horse industry. There he boarded horses and dabbled in the bloodstock business by purchasing, selling, and breeding thoroughbreds.

One of his earliest friends in Kentucky was Jack Preston. Mr. Preston made his fortune in real estate and oil, and he used that wealth to support his interest in horses. Mr. Preston's horses later won major races, including the Kentucky Derby, the Belmont Stakes, and the Breeders' Cup. Through his relationship with Mr. Preston, Brian gained access to lucrative opportunities. In one instance, Mr. Preston offered Brian shares in award-winning horses. Brian purchased shares for $50,000 to $100,000 each and later sold them for $2.5 million each.

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development permits is held by the Coastal Commission or the local jurisdiction, the Coastal Commission has the ultimate authority to ensure coastal development permits are issued consistent with Coastal Act policies. Cal. Pub. Res. Code § 30330.

[*14] Around 1990 Charles's health began to decline, and Brian returned to California to help manage the Boudreau Family Land. As part of his estate planning, Charles began transferring property to Brian as Trustee of the Boudreau Trust of 1990. With these transfers, Brian soon discovered that his father had obtained loans secured by the Boudreau Family Land ranging from several hundred thousand dollars to over $1 million, and most of the property was heavily mortgaged. He turned to his friends for financial advice.

One such friend was Mr. Levin. In 1991 Mr. Levin lent Charles and Brian $100,000 secured by a portion of the subject property. But this would not be the only loan from Mr. Levin. A couple of months later, Mr. Levin lent the pair an additional $150,000 secured by the same portion of the subject property. Charles passed away on December 18, 1992.

Charles's death marked the beginning of a difficult period for Brian. In addition to the emotional toll of his father's passing, Brian soon fell behind on payments to his father's creditors. Those creditors ultimately foreclosed on substantial portions of the Boudreau Family Land, including the subject property. Brian fought tirelessly to reclaim the property. As he had before, he turned to friends for help. Mr. Preston answered his call. Together they formed Malibu Canyon LP, and with Mr. Preston's financial backing the partnership reacquired portions of the Boudreau Family Land, including the subject property. The two then turned their attention to preserving the VTTM entitlements.

Other portions of the Boudreau Family Land, however, were lost. In 1996 Mr. Levin foreclosed on the parcel east of Stokes Canyon Road where the equestrian center was located. Shortly after Mr. Levin took ownership, the equestrian center burned down. In 1998 Brian helped Mr. Levin rebuild it after a years-long regulatory fight.

E. *North Area Plan*

In 2000 the LA County Board of Supervisors adopted the Santa Monica Mountains North Area Plan (North Area Plan) to replace the 1981 Interim Area Plan. LA County Dep't of Reg'l Plan., North Area Plan I-1 (2000). The North Area Plan continued LA County's emphasis on habitat protection and hillside management. As compared to the 1981 Interim Area Plan, the North Area Plan operationalized the general policies into detailed development requirements.

[*15] The North Area Plan established several policies related to preservation, including requiring developments to protect and preserve significant, viable habitat areas and linkages in their natural condition. *Id.* IV-19. It also aimed to ensure that hillside areas retain their natural topography and limited development on ridgelines visible from key public lands and scenic highways. *Id.* IV-21. To achieve this, the North Area Plan sought to limit grading where possible and severely limit grading in areas of 50% or greater slope. *Id.* Additionally, it established policies to prohibit skyline development and required structures to be set back sufficiently to avoid obstructing the natural skyline. *Id.* IV-22.

In 2002 the Board of Supervisors established the North Area Community Standards District to implement the North Area Plan through zoning regulations. LA County, Cal., Code § 22.44.133. In 2004 the LA County Board of Supervisors amended the district to include additional grading and ridgeline controls. Among other requirements, the amended regulations required a conditional use permit for grading exceeding 5,000 cubic yards and imposed development setbacks from significant ridgelines with variances available only upon specified findings. LA County, Cal., Planning and Zoning Ord. 2004-0072, § 1 (Dec. 7, 2004).

F. *The First Final Map*

As with the changing development standards, ownership of the Boudreau Family Land looked much different from that in the period before Charles's death. Soka University owned the land west of Stokes Canyon Road. Malibu Canyon LP, with Mr. Preston and Brian as partners, owned the land east of Stokes Canyon Road except for the equestrian center, which Mr. Levin owned. The VTTM remained active but was nearing expiration.

By 2004 LA County had extended the expiration date of the VTTM several times under the vesting provisions of the Subdivision Map Act. To obtain another extension, Brian had to record a final map. Recording a final map, however, required satisfying conditions imposed under the VTTM, including, for the majority of lots, upgrading the water and sewage systems needed to support the proposed subdivision.

On May 26, 2004, Soka University authorized Brian, through his development entity Malibu Canyon Development, Inc., to construct water and sewer lines to service the VTTM area in the existing utility right of way along Mulholland Highway and Stokes Canyon Road. On

[*16] June 4, 2004, Malibu Canyon Development, Inc., applied for a coastal development permit waiver to replace existing lines located within the coastal zone. The application represented that the project would not require grading, affect public access or views, or require removal of oak trees. It also stated that the work would not conflict with the Coastal Act and that the lines would serve a parcel outside of the coastal zone. On November 22, 2004, the Coastal Commission granted permit waivers, determining that the lines would "serve development and fire hydrants also located outside the coastal zone along Stokes Canyon Road."

In 2005 Soka University decided to divest its holdings in the Santa Monica Mountains region and offered Brian an opportunity to repurchase the land west of Stokes Canyon Road. Seeing a chance to reunite the VTTM areas, he quickly agreed. On February 19, 2005, Soka University sold that property to Malibu Canyon LP for $12 million.

Brian turned his sights to recording the first final map from the VTTM. He applied for a final map numbered 45465-01. LA County recorded this first final map on March 16, 2005.[17] It created a single lot on a portion of the VTTM west of Stokes Canyon Road that was not subject to the coastal permitting requirements applicable to land within the coastal zone.

G. *The Long and Costly Trail to a Second Final Map*

Fresh off recording the first final map, Brian wanted to maintain the momentum to record more final maps on the VTTM. At the same time, the ghosts of his father's debt continued to haunt Brian. Brian sold an unrelated San Diego property for less than the outstanding balance of the loan that his father took out from Mr. Levin. Brian agreed to secure the over $1 million balance of this loan with the subject property.[18]

In 2008 Brian approached Mr. Levin for additional financing to prepare another final map for submission. Mr. Levin saw continued value in the land and happily agreed. In April 2008 Malibu Canyon LP borrowed an additional $4 million that was again secured by the subject

[17] The sewer and water line upgrades were not complete by this point. However, because this lot had a pre-existing single-family residence, that condition did not apply.

[18] At the time he sold the San Diego property, Brian had paid off Mr. Levin's previous loans secured by the subject property.

[*17] property. This increased the debt secured by this property to over $5 million.

The infusion of cash did not solve Malibu Canyon LP's financial problems. On May 19, 2008—the day the VTTM was set to expire—Malibu Canyon LP submitted a second final map to LA County. The map sought to record seven lots west of Stokes Canyon Road. LA County rejected the submission, concluding that Malibu Canyon LP had failed to obtain a grading permit from the Regional Water Board. Malibu Canyon LP strongly disagreed because this permit was not made a condition when the VTTM was approved, but the decision could only be challenged in court.

By then, Mr. Preston had invested over $18 million in preserving the VTTM and had no appetite for protracted litigation. He chose to cut his losses and relinquish his interest in Malibu Canyon LP.[19] Mr. Levin got spooked by Mr. Preston's departure, and he requested a deed in lieu of foreclosure for the property east of Stokes Canyon Road. Brian complied.

Despite the setback, Brian continued preservation efforts for the VTTM. He sued LA County, and the court issued a writ of mandamus directing LA County to record the second final map. After the litigation concluded, the second final map was recorded on June 2, 2010, reviving the VTTM and extending its expiration through 2014.

Malibu Canyon LP was not the only party reacting to the VTTM's survival. German American Bank had acquired a note that was secured by the land west of Stokes Canyon Road. Once the VTTM was reinstated, the bank moved to foreclose, alleging delinquent payments. The dispute settled in 2011 with Malibu Canyon LP agreeing to pay the bank $3 million by June 2012 in exchange for the land.

The short turnaround to pay $3 million appeared fatal. Malibu Canyon LP had lost its principal financing partner and depleted its resources through litigation. Brian sought financing from local brokers to no avail. Then, seven days before the $3 million was due, an unexpected visitor arrived at Brian's front door. Don Hankey, a billionaire who made his fortune on subprime car loans, had heard about

[19] Malibu Canyon LP continued in existence after Mr. Preston relinquished his interest because Brian's other entities owned partnership interests.

[*18] Brian's predicament from local bankers. He came to Brian's house to discuss funding the settlement.

Mr. Hankey ultimately lent Malibu Canyon LP $4.2 million to satisfy the German American Bank obligation and finance development on the land west of Stokes Canyon Road. The loan came with a condition: Mr. Hankey insisted that Brian begin building homes on the lots created by the second final map to ensure repayment. Brian had never built a house, but he needed the financing and remained determined to see the project through. Malibu Canyon LP began constructing homes on several of the seven lots using construction loans:

Parcel	*Details*
1	Pre-existing single-family home built before the second final map.
2	Malibu Canyon LP built a single-family home on this lot in 2017 that sold in the same year.
3	Transferred to Malibu Valley Partners, LLC.[20] Vacant as of trial.
4	Transferred to Malibu Valley Partners, LLC. Malibu Valley Partners, LLC, built a single-family home on this parcel in 2023 that sold in 2024.
5	Malibu Canyon LP built a single-family home in 2017. Occupied by Brian after his house burned down.
6	Transferred to Malibu Valley Partners, LLC. Malibu Valley Partners, LLC, built a single-family home on this parcel in 2021 that sold in 2022.
7	Malibu Canyon LP built a single-family home on this lot in 2017 that sold in 2019.

These lots shared topography similar to that of the subject property, including slopes exceeding 25% and 50%.

H. *Creation of MVL and Talk of an Easement*

The sun was shining again on the Boudreau Family Land: Malibu Canyon LP had a new financial partner in the form of Mr. Hankey and the VTTM was active. Mr. Levin saw this as an opportunity to move

[20] Malibu Valley Partners, LLC, is a California limited liability company associated with Brian.

[*19] onto greener pastures and focus on raising his daughter after a contentious divorce. He had substantial wealth and was not concerned about recovering his full investment in the land. Mr. Levin offered Brian the property east of Stokes Canyon Road—excluding the equestrian center—for $1.5 million, a price he considered below market. He did not seek other potential buyers, list the property for sale, contract with a broker, or have the property appraised before selling it to Brian.

Brian jumped at the opportunity to acquire the subject property. In April 2013 Mr. Levin sold the property to Diamond West Realty, Inc., a brokerage firm Brian owned. In exchange, Mr. Levin received two notes with face values of $944,700 and $555,300, respectively (Levin notes). Each note carried 10% interest and was payable on March 31, 2016. Even if paid early, the notes required payment of all interest that would have accrued through March 31, 2016.

On November 25, 2013, Brian formed MVL, a partnership for federal tax purposes, with Brian owning 99% and his wholly owned corporation Spectrum owning 1%. On December 2, 2013, Diamond West Realty, Inc., transferred the subject property to MVL in exchange for MVL's assumption of the Levin notes.

Managing the Boudreau Family Land was stressful for Brian, but it also gave him the ideal setting to pursue trail riding. Around 2013 Mr. Hankey, also an avid horseman, began joining Brian on rides across the subject property. Mr. Hankey was struck by the surrounding Santa Monica Mountains, which offered some of the most pristine trails in the country. During one ride with Brian, Mr. Hankey raised the idea of placing a conservation easement on the subject property. Mr. Hankey was interested in a conservation easement both for tax reasons and to preserve the land for his continued enjoyment.

Around the same time, Mr. Hankey and his son purchased land adjacent to the subject property. Mr. Hankey had been in contact with Forever Forests, LLC, a conservation consulting firm, and he asked Brian to speak with them. At first, this disheartened Brian. He had hoped that Mr. Hankey would fund development of the subject property, but Mr. Hankey saw personal use of the subject property as more valuable than the returns from large-scale development. Brian was torn. He wanted to carry on his father's vision of recording the entire VTTM, but he also felt obligated to repay Mr. Levin. Seeing no other viable option, Brian reluctantly agreed.

[*20] III. *Conservation Easement Donation*

A. *Transfer Development Credits*

Throughout the conservation easement process, Brian kept his eye on developing the remainder of the Boudreau Family Land. By the donation date, however, the regulatory landscape governing development in the Santa Monica Mountains had materially changed. On October 10, 2014, the Coastal Commission certified the Santa Monica Mountains Local Coastal Program (2014 LCP), including its land use plan and implementing provisions. Following certification of the 2014 LCP, development within the coastal zone required a coastal development permit consistent with the certified 2014 LCP and the Coastal Act. Cal. Pub. Res. Code § 30604(a). Although authority to grant coastal development permits was delegated to LA County, the Coastal Commission retained appellate jurisdiction. *Id.* § 30603(a)(2), (4).

As relevant here, the 2014 LCP imposed substantial additional constraints on subdivision within the coastal zone as compared to the 1986 Malibu LCP LUP. The program requires a subdivider to obtain one transfer development credit for each newly created lot within the coastal zone. One transfer development credit generally requires retirement of approximately 20 acres of qualifying coastal land. Transfer development credits are awarded only after the director of the Department of Regional Planning certifies compliance with all requirements to obtain the transfer development credit, including retirement of the identified lots. LA County, Cal., Code §§ 22.44.1230(F)(3)(b), 22.44.630.[21] Moreover, under the 2014 LCP, a developer could not build a structure within 50-foot horizontal and vertical setbacks from significant ridgelines, build within 100 feet from designated H1 habitat areas, or grade on steep slopes. *Id.* §§ 22.44.2040(B)(3), 22.44.1900(A), 22.44.1260(J).

Given the acreage retired through the conservation easement, Brian hoped the donation would generate transfer development credits that could be used to record new lots in the coastal zone. Before the donation, Beth Palmer, Brian's longtime real estate attorney, sent the draft conservation easement deed to the LA County Department of Regional Planning to determine whether MVL would be eligible for the

[21] This section of the LA County Code was codified in 2015 after the Board of Supervisors approved the LCP in 2014. The 2015 codification matches the LCP and therefore, for clarity, this Opinion will cite the 2015 LA County Code where relevant.

[*21] transfer development credits. She did not hear back until after the donation deed was executed.

In its response, the LA County Department of Regional Planning stated that because the lots were on an approved tentative tract map—not a final map—it could not determine whether the lots qualified for the transfer development credits. It added, however, that if the easement were recorded in the same form, it would qualify for a transfer development credit for each 20 acres retired in the coastal zone. It remains unclear whether MVL was ultimately entitled to credits, though Ms. Palmer later cited the response as evidence that MVL obtained them.

B. *Preparation and Recording*

On April 9, 2014, MVL and Forever Forests, LLC, entered into a conservation consulting services agreement. Forever Forests, LLC, agreed to guide MVL through the conservation easement process, including identifying a donee organization and obtaining a valuation. On May 2, 2014, MVL, through Forever Forests, LLC, retained Thomas Erickson to appraise the subject property. Mr. Erickson had over 40 years of experience appraising property in LA County.

Mr. Erickson met with Brian and Ms. Palmer to discuss the property and its development potential. Using the information provided, Mr. Erickson valued the conservation easement at $32,075,000. Brian believed that the valuation was low because of his experience selling other undeveloped lots in the area. But he concluded he could never use the full deduction during his lifetime. He therefore did not challenge the appraisal and proceeded with the donation.

During this time, Forever Forests, LLC, contacted the MRCA to determine whether it would accept the conservation easement. MRCA welcomed the opportunity to neutralize the unique development rights. By then, the VTTM was unusual even among the limited number of vesting tentative tract maps in LA County. A report from the LA County Department of Regional Planning showed only a small number of vesting tentative tract maps that entitled a developer to subdivide such a large piece of property into so many estate-sized lots, and few of those predated the North Area Plan.

MVL's ownership changed before the donation date. On September 26, 2014, Mr. Hankey purchased a 75% limited partner interest from Brian for $3.55 million. Mr. Hankey paid $1.55 million of

[*22] that amount directly to Mr. Levin to satisfy the outstanding debt and accrued interest on the Levin notes. By the donation date, MVL's ownership was as follows: Spectrum (0.225%), Brian (22.275%), Beth Palmer (2.5%), and Mr. Hankey (75%).

On December 30, 2014, MVL recorded a grant of a conservation easement over the subject property to MRCA. On March 16, 2015, Lisa Soghor, MRCA's deputy executive officer, executed a letter titled "Acknowledgement of Charitable Donation," confirming MRCA's receipt of the easement and stating that MVL received no goods or services in exchange.

IV. *Events Surrounding the Subject Property After the Donation*

Before turning to tax reporting and procedural history, we note several relevant postvaluation events. After the donation, Brian and his entities continued development of the additional portions of the VTTM area.

In 2021 Malibu Valley Partners sought LA County approval to amend a portion of the VTTM covering the area west of Stokes Canyon Road. The amendment proposed relocating four lots out of the coastal zone and adjusting the corresponding lot sizes, lot lines, and grading volumes. Malibu Valley Partners submitted this request to the LA County Department of Regional Planning. In response, LA County prepared and certified an addendum to the final EIR addressing the amendment's incremental environmental effects.[22] This addendum was not circulated for public review. Cal. Code Regs. tit. 14, § 15164(b) and (c) (2014). A hearing officer approved the amendment on July 28, 2021, finding it consistent with the North Area Plan and the 2014 LCP.

Concerned citizens appealed the hearing officer's decision to the LA County Regional Planning Commission (RPC). After receiving public comments and holding a hearing, the RPC considered whether the North Area Plan and the 2014 LCP applied to the proposed development. If these more recent laws applied, the proposed development in the amendment might conflict with these laws. The RPC expressly determined that they did not apply to the amendment because the VTTM locked in the development laws in 1988. On November 3, 2021, the RPC approved the amendment.

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[22] The record does not identify which office of LA County prepared the addendum.

[*23] The decision was then appealed to the LA County Board of Supervisors, the highest level within the LA County Department of Regional Planning. After a public hearing, the Board of Supervisors denied the appeal and approved the application on July 26, 2022. In its written findings, the Board of Supervisors agreed with the RPC that the North Area Plan and the 2014 LCP did not apply. It also found the addendum to the final EIR sufficient because no statutory trigger required preparation of a new EIR. All proposed development in these phases would occur outside the coastal zone.

The final event of note after the donation date was that around 2022, Mr. Levin sold the equestrian center to Brian.

V. *Tax Reporting*

On March 24, 2015, Mr. Erickson finalized his appraisal report. MVL then turned to Cherri Skoczek, Brian's certified public accountant for over 30 years, to prepare its tax return. Ms. Skoczek prepared MVL's Form 1065, U.S. Return of Partnership Income, for the short tax year ending December 31, 2014. She did not advise on the reasonableness of the appraisal or the deductibility of the conservation easement donation.

MVL timely filed Form 1065 for the tax year beginning September 26, 2014, and ending December 31, 2014, and attached Form 8283, Noncash Charitable Contributions, to the return.[23] On Form 8283 MVL reported a $32,075,000 conservation easement donation; the value was based on Mr. Erickson's appraisal. MVL also attached MRCA's contemporaneous written acknowledgment and Mr. Erickson's appraisal report. In addition to the noncash charitable contribution deduction, MVL reported $450,000 of interest expense related to the Levin notes that were paid off using Mr. Hankey's capital contribution.

VI. *Audit and Tax Court Petition*

Respondent selected MVL's 2014 information return for examination. The audit was assigned to Revenue Agent (RA) Yan Zhao, who enlisted the help of IRS Engineer Peter Crane to prepare an appraisal valuing the conservation easement. After determining that the charitable contribution deduction should be disallowed for failure to

[23] It is unclear who prepared the Form 8283, though Ms. Skoczek acknowledged that she reviewed the Form 8283 and stated that she would have informed Ms. Palmer or Brian if anything appeared incorrect.

[*24] comply with the technical requirements of section 170, RA Zhao turned her attention to penalties. By June 6, 2018, RA Zhao began drafting Form 886–A, Explanations of Items, determining the applicability of accuracy-related penalties under section 6662 for a gross valuation misstatement, a substantial valuation misstatement, and negligence. She also considered the penalty for a substantial understatement of income tax and concluded no partnership-level defenses would apply.

RA Zhao also prepared Form 5701, Notice of Proposed Adjustment (NOPA), addressing penalties. On December 19, 2018, she submitted the NOPA to Team Manager Johnson for approval. The NOPA referenced Form 886–A and stated that penalties would be determined at the partner level. Team Manager Johnson signed the NOPA on the same day and returned it to RA Zhao. RA Zhao compiled the appraisal, the signed NOPA, and Form 886–A into the 30-day package and sent it to MVL.

On August 21, 2019, respondent issued an FPAA disallowing the conservation easement deduction in full. Respondent also determined an accuracy-related penalty for a gross valuation misstatement, and, in the alternative, an accuracy-related penalty for negligence or a substantial understatement of income tax would apply. Respondent further disallowed MVL's interest expense deduction for lack of substantiation and, alternatively, contended that the expense should have been added to MVL's basis in the subject property.

Petitioner filed a petition with this Court for readjustment. On January 17, 2020, respondent filed his answer in which IRS Attorney Lori Amadei asserted an alternative accuracy-related penalty for a substantial valuation misstatement. Her immediate supervisor, Associate Area Counsel Aely Ullrich, signed the answer.

VII. *Trial*

The parties presented the following expert witnesses at trial to address the value of the easement. Each expert's report was received as the witness's direct testimony under Rule 143(g)(2).

[*25] A. *Petitioner's Experts*

1. *Charles Hewlett*

Charles Hewlett, the managing director of a real estate consulting company, was qualified as an expert in real estate market analysis and financial feasibility analysis for single-family subdivisions. In his opening report Mr. Hewlett addressed the highest and best use of the subject property and market feasibility for the residential lots. He concluded that the highest and best use was a 56-lot residential community of large custom homes. He based this conclusion on the rights conveyed under the VTTM, strong buyer demand, and rising home values. Using eight comparable lots, he estimated that as of December 30, 2014, the average lot on the subject property would sell for $1,417,000 with annual appreciation. He also provided an absorption schedule and projected land appreciation rates.

Mr. Hewlett's rebuttal report criticized Stuart DuVall's valuation report, challenging Mr. DuVall's selection of comparable properties and his market-trend adjustments. He also faulted Mr. DuVall's assumption of a flat 3% annual appreciation in lot values after the donation date.

2. *William Cunningham*

William Cunningham is a professional civil engineer employed by Diamond West, Inc.[24] Mr. Cunningham has worked on the VTTM since 2013 as the engineer of record. At trial, he was qualified as an expert in land development, civil engineering, engineering for the VTTM, engineering cost estimates, and VTTM-related land use permitting.

Mr. Cunningham's opening report addressed the physical feasibility of subdividing the subject property under the VTTM. He prepared final engineering plans consistent with the VTTM and developed direct cost estimates. He estimated total engineering costs, including grading and other lot improvements, at $17,121,708, or approximately $305,745 per lot. He also opined that it would take one year to obtain clearances necessary to record final maps and that this process could overlap with the coastal development permit request process.

[24] Diamond West, Inc., and Diamond West Realty, Inc., are two separate entities. While Brian initially owned an interest in Diamond West, Inc., he divested his interest after the donation around 2017.

[*26] Mr. Cunningham's rebuttal report challenged Mr. DuVall's assumptions regarding applicable land use policies and the lot configuration used in Mr. DuVall's valuation. Mr. Cunningham specifically opined that the North Area Plan and the 2014 LCP do not apply to the VTTM.

3. *Peter Gutierrez*

Peter Gutierrez, a California land use attorney, was qualified as an expert in LA County land use approval procedures, the final map permitting process in southern California, and the coastal development permit process in southern California.[25]

Mr. Gutierrez's opening report addressed whether it was reasonably probable that MVL could obtain approval to record a final map reflecting the 56 lots shown on the VTTM. He opined that MVL could satisfy the conditions necessary to record the final map before the VTTM expired. He further opined that, although a 56-lot subdivision would not likely have been approved in 2014 absent the VTTM, development could proceed in substantial compliance with the policies and ordinances in effect in 1988. With respect to the coastal development permit, Mr. Gutierrez opined that LA County would process the permit and could rely on its findings in the final EIR. He estimated that obtaining the coastal development permit would take approximately two years.

Mr. Gutierrez's rebuttal report criticized Mr. DuVall's application of land use laws adopted after the VTTM. He also stated that in 1988 LA County did not require transfer development credits for coastal zone development. At trial, however, he acknowledged that the Coastal Commission had its own transfer development credit requirement at the time of the donation.

4. *Thomas Erickson*

Mr. Erickson, a certified land appraiser with experience appraising property in LA County, was qualified as an expert in LA County real estate valuation.

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[25] We have disregarded Mr. Gutierrez's reports to the extent they express legal conclusions. *See Alumax Inc. & Consol. Subs. v. Commissioner*, 109 T.C. 133, 171 (1997) (stating that legal conclusions are not proper expert testimony), *aff'd*, 165 F.3d 822 (11th Cir. 1999).

[*27] In his opening report, Mr. Erickson concluded that the conservation easement was worth $27,425,000 as of the donation date. He determined that the subject property's highest and best use before the donation was a 56-lot residential development under the VTTM. He valued the subject property at $31 million before the conservation easement and $3,575,000 after.[26] Mr. Erickson conducted both a market approach, yielding an estimated $30 million, and an income approach, yielding $31 million. He considered the income approach more reliable because of the lack of close comparable sales.

5. *David Williams*

David Williams, a valuation services director with Colliers International Valuation & Advisory Service, was qualified as an expert in real estate valuation in Southern California, including LA County.

In his opening report Mr. Williams valued the conservation easement at $24.4 million as of the donation date. He concluded that the subject property's highest and best use before the donation was a 56-lot residential development under the VTTM. He valued the property at $29.8 million before the conservation easement and $5.4 million after. Mr. Williams conducted both a market approach, yielding $30 million, and an income approach, yielding $28.7 million. He reconciled the two by giving greater weight to the market approach, resulting in a $29.8 million before value.

In rebuttal, Mr. Williams criticized Mr. DuVall's assumption that the land use laws in effect on the donation date governed the property. Mr. Williams asserted that Mr. DuVall's failure to account for the development rights under the VTTM—specifically that the North Area Plan and the 2014 LCP did not apply—led Mr. DuVall to an incorrect highest and best use determination. This error spilled into Mr. DuVall's selection of comparable property sales and valuation. Mr. Williams also challenged Mr. DuVall's income approach assumptions, including his growth and discount rates.

[26] Respondent conceded the after value of the land and therefore, we need not dive deeper into how the parties' experts calculated the after value of the subject property.

[*28] B. *Respondent's Experts*

1. *Daniel Cooper*

Daniel Cooper, the president of an ecological consulting firm specializing in LA County natural resources, was qualified as an expert in conservation biology with a focus on assessing resources in the Santa Monica Mountains since 2009. His opening report addressed only issues that respondent has since conceded.

Mr. Cooper's rebuttal report challenges Mr. Gutierrez's time estimate for securing the permits required to record the final map from a biological perspective. He criticized Mr. Gutierrez's estimate that MVL could obtain a coastal development permit within two years. Mr. Cooper states that a project of the scale contemplated by the VTTM would be unprecedented in the Santa Monica Mountains and noted that smaller single-family home projects in the region have taken significantly longer, frequently requiring multiple redesigns before approval.

Mr. Cooper further explained that, in his experience, LA County began applying the requirements of the draft 2014 LCP to development in the area in 2013. He also opined that LA County would likely require a new EIR before a final map was recorded. In addition, he concluded that LA County would not rely on the final EIR in connection with MVL's oak tree permitting. He estimated that obtaining an oak tree permit for removal associated with a 56-lot subdivision would require at least 12 months, including preparation for a new oak tree report and submission of a new permit application.

2. *Matthew Jewett*

Matthew Jewett, a land use consultant, was qualified as an expert in land use planning and entitlement in the Santa Monica Mountains Coastal Zone.

Mr. Jewett's rebuttal report addressed Mr. Gutierrez's land use analysis for the southern portion of the property located within the coastal zone. Mr. Jewett opined that it would be nearly impossible for MVL to obtain a coastal development permit for that portion of the property. He further determined that even if approval were possible, the permitting process would far exceed Mr. Gutierrez's two-year estimate. Mr. Jewett also stated that the 2014 LCP would apply to development under the VTTM as a matter of state law and was not

[*29] frozen in place by the VTTM. As a result, he concluded that MVL would be required to comply with the transfer development credit requirements; consequently, anything more than minimal development on the southern portion would be financially infeasible. Finally, he opined that if LA County required a new EIR before final approvals, this alone could add at least one additional year to the process.

3. *Stuart DuVall*

Stuart DuVall, a certified general real estate appraiser with experience appraising land in California, was qualified as an expert in real estate valuation.

In his opening report, Mr. DuVall concluded that the value of the conservation easement was $4.65 million. He determined that the property's highest and best use before the donation was a 21-lot rural residential subdivision with associated open space on the southern portion of the property. He valued the property at $6.65 million before the conservation easement and $2 million after. To estimate the before value, Mr. DuVall applied both a market approach ($6.95 million) and an income approach ($6.645 million). He assigned greater weight to the income approach and ultimately adopted a before value of $6.65 million.

Mr. DuVall attached two appendices to his opening report. One appendix, prepared by Brent Caldwell, a civil engineer, consisted of handwritten calculations and unexplained Excel spreadsheets purporting to estimate engineering costs associated with Mr. DuVall's alternative development map. The second appendix, prepared by Mr. Jewett, addressed whether the VTTM complied with the 2014 LCP and the North Area Plan. Mr. Jewett also estimated the cost to record the final map for Mr. DuVall's alternative development map. Both appendices were marked as drafts. Neither was separately offered into evidence, and neither author was cross-examined regarding the contents. At trial, Mr. DuVall appeared unfamiliar with the underlying work reflected in the appendices. For example, he could not explain whether Mr. Jewett's analysis considered the applicable law at the time the VTTM application was deemed complete.

Mr. DuVall's rebuttal reports addressed the appraisal reports of Mr. Erickson and Mr. Williams. He challenged their highest and best use conclusions, their selection of comparable property sales, and the variables used in their respective income approaches.

[*30] OPINION

I. *Burden of Proof*

Generally, the Commissioner's adjustments in an FPAA are presumed correct, and the taxpayer bears the burden of proving them wrong. *See Welch v. Helvering*, 290 U.S. 111, 115 (1933); *Crescent Holdings, LLC v. Commissioner*, 141 T.C. 477, 485 (2013); *see also* Rule 142(a)(1). The taxpayer bears the burden of proving entitlement to any deduction claimed. *See INDOPCO, Inc. v. Commissioner*, 503 U.S. 79, 84 (1992). Section 7491(a) provides that if, in any court proceeding, a taxpayer introduces credible evidence with respect to any factual issue relevant to ascertaining the taxpayer's liability for any tax imposed by subtitle A or B and meets other prerequisites, the Commissioner shall have the burden of proof with respect to that issue. *See Higbee v. Commissioner*, 116 T.C. 438, 440–41 (2001).

We need not decide whether the burden shifts to respondent under section 7491 because the parties have provided sufficient evidence to enable us to decide all issues by a preponderance of the evidence. *See Knudsen v. Commissioner*, 131 T.C. 185, 189 (2008), *supplementing* T.C. Memo. 2007-340. In this case we discerned no evidentiary tie on any material issue of fact. *See, e.g.*, *id.*

II. *Technical Requirements for a Charitable Contribution Deduction*

Section 170(a)(1) allows a deduction for a charitable contribution. Section 170(c) defines a charitable contribution as including a "contribution or gift" to or for the use of a qualified charity. "The *sine qua non* of a charitable contribution is a transfer of money or property without adequate consideration." *United States v. Am. Bar Endowment*, 477 U.S. 105, 118 (1986). If a transaction with a charity is structured as a quid pro quo exchange—i.e., if the taxpayer receives property or services equal in value to what it conveyed—there is no "contribution or gift" within the meaning of the statute. *Hernandez v. Commissioner*, 490 U.S. 680, 701–02 (1989). To the extent that a taxpayer receives a quid pro quo, a charitable contribution deduction is permitted only to the extent that the value of the transferred property exceeds the value of the benefits received. *See Addis v. Commissioner*, 374 F.3d 881, 885 (9th Cir. 2004), *aff'g* 118 T.C. 528 (2002).

In assessing whether a transaction constitutes a quid pro quo exchange, we give the most weight to the external features of the transaction to avoid imprecise inquiries into a taxpayer's subjective

[*31] motivations. *See Hernandez v. Commissioner*, 490 U.S. at 690–91. If a transaction is structured such that it is understood that the taxpayer's money or property will not pass to the charitable organization unless the taxpayer receives a specific benefit in return—or the taxpayer cannot receive the benefit unless it pays the required price—then the transaction does not qualify for a deduction under section 170. *Graham v. Commissioner*, 822 F.2d 844, 849 (9th Cir. 1987), *aff'g* 83 T.C. 575 (1984), *aff'd sub nom. Hernandez v. Commissioner*, 490 U.S. 680; *see also Costello v. Commissioner*, T.C. Memo. 2015-87, at *27. By contrast, if the benefit received is merely incidental to a charitable purpose, the deduction is allowable. *See McGrady v. Commissioner*, T.C. Memo. 2016-233, at *25 (citing *McLennan v. United States*, 24 Cl. Ct. 102, 107 (1991), *aff'd*, 994 F.2d 839 (Fed. Cir. 1993)); *see also Collman v. Commissioner*, 511 F.2d 1263, 1265–69 (9th Cir. 1975) (holding that a taxpayer had the requisite donative intent when he donated property to the county to widen the road even though he benefited from this activity because widening the road was required to rezone his property), *aff'g in part, rev'g in part, and remanding* T.C. Memo. 1973-93.

Respondent argues that MVL is not entitled to a charitable contribution deduction because it received transfer development credits as a result of the donation. As discussed above, transfer development credits are awarded through an independent regulatory process as part of a coastal development permit application. LA County, Cal., Code § 22.44.1230(F)(3)(b). Transfer development credits may be awarded for retiring lots in the coastal zone under the 2014 LCP and are required to record a new legal lot in the coastal zone. *Id.* §§ 22.44.1230(D)(2), 22.44.1230(B)(1)(a).

The external features of MVL's conveyance do not support respondent's characterization of the donation as a quid pro quo exchange. There is no evidence that MVL's conservation easement donation was contingent on securing transfer development credits. In fact, the letter from the LA County Department of Regional Planning regarding the potential for transfer development credits is dated after the conservation easement was recorded. *Cf. Triumph Mixed Use Invs. III, LLC v. Commissioner*, T.C. Memo. 2018-65, at *35–40 (determining that there was a quid pro quo exchange when the donor expressly negotiated with the donee for the exchange of real property for approval of a concept plan). In any event, the letter did not guarantee that MVL would receive transfer development credits for the conservation easement donation. Accordingly, it cannot be said that MVL's donation was contingent on the receipt of the transfer development credits. *See*

[*32] *Graham v. Commissioner*, 822 F.2d at 849. If anything, the possibility of transfer development credits was a mere incidental benefit. *See Collman v. Commissioner*, 511 F.2d at 1265–69.

Respondent likens the transfer development credits to the favorable land entitlements received upon the donation of a facade easement in *Seventeen Seventy Sherman Street, LLC v. Commissioner*, T.C. Memo. 2014-124. In *Seventeen Seventy Sherman*, we denied a charitable contribution deduction because the taxpayer received consideration in exchange for its donation and failed to establish the value of that consideration. *Id.* at *28–32. There, the taxpayer sought a zoning variance and entered into an agreement with a community development organization under which the taxpayer would donate an easement to the organization in exchange for a favorable recommendation from the organization to the local planning board in support of the variance. *Id.* at *9–10. Although the local planning board was not required to accept the recommendation, it did so in approximately 90% of cases. *Id.* at *30. We held that the donation was a quid pro quo exchange because the recommendation would not have been provided without the easement and the taxpayer expected the recommendation to substantially increase the likelihood of approval. *Id.* at *30–32. We have similarly denied a charitable contribution deduction where a taxpayer treated the grant of a conservation easement to a county "as a bargaining chip" to obtain a subdivision exemption from the county that it initially refused to grant. *Pollard v. Commissioner*, T.C. Memo. 2013-38, at *22–25.

Respondent's comparisons put the cart before the horse. In *Seventeen Seventy Sherman* and *Pollard*, the taxpayer's transfer was structured as the price of a specific benefit, and the benefit was provided as part of an integrated arrangement involving the donee (or another party acting in concert with the donee). Here, respondent does not contend, nor does the record show, that MRCA provided any benefit to MVL in exchange for the conservation easement. MRCA was not involved in any determination to award transfer development credits, did not offer to assist MVL in obtaining them, and did not provide any recommendation or other advocacy to LA County. *Cf. Stubbs v. United States*, 428 F.2d 885, 887–88 (9th Cir. 1970) (determining that the quid was assistance in obtaining favorable zoning provided by the donee); *Hernandez v. Commissioner*, 819 F.2d 1212, 1217 (1st Cir. 1987) (determining that the quid was religious "auditing" services provided by the donee), *aff'd*, 490 U.S. 680; *Murphy v. Commissioner*, 54 T.C. 249, 253 (1970) (determining that the quid was adoption services provided by

[*33] the donee); *DeJong v. Commissioner*, 36 T.C. 896, 899–900 (1961) (determining that the quid was education services provided by the donee), *aff'd*, 309 F.2d 373 (9th Cir. 1962). Nor did the Board of Supervisors compel the donation to a donee of its choice. *Cf. Triumph Mixed Use Invs. III, LLC*, T.C. Memo. 2018-65, at *35–40 (determining that there was a quid pro quo exchange when the donor expressly negotiated with the donee for the exchange of real property for approval of a concept plan).

In sum, the record does not show that MVL's conveyance was conditioned on receiving transfer development credits. Any such benefit was therefore not bargained for with MRCA and was not part of a quid pro quo exchange. At most, the possibility of transfer development credits was an incidental consequence of MVL's donation. Accordingly, MVL had the requisite donative intent to claim a charitable contribution deduction.

III. *Valuation of the Easement*

Having determined that MVL satisfied the threshold requirements for a charitable contribution deduction, we now consider the amount of the deduction to which MVL is entitled. If a taxpayer makes a gift of property other than money, the amount of the contribution generally equals the property's fair market value at the time of the gift. *See* Treas. Reg. § 1.170A-1(c)(1). The regulations define fair market value as "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts." *Id.* subpara. (2).

Valuation is not a precise science. The value of property on a given date is a question of fact to be resolved on the basis of the entire record. *See Kaplan v. Commissioner*, 43 T.C. 663, 665 (1965). Because there is rarely a substantial market for sales of easements comparable to the donated easement, courts typically value conservation easements indirectly using a "before and after" approach. *See Ranch Springs, LLC v. Commissioner*, 164 T.C. 93, 128 (2025); Treas. Reg. § 1.170A-14(h)(3)(i). Under that approach, the value of an easement equals the fair market value of the property immediately before the easement was granted (before value) minus the fair market value of the property as encumbered by the easement (after value). *Browning v. Commissioner*, 109 T.C. 303, 320–24 (1997). Treasury Regulation § 1.170A-14(h)(3)(i) provides that, where a donor grants a perpetual conservation restriction

[*34] covering only a portion of the contiguous property owned by the donor, the fair market value of the restriction is the difference between the fair market value of the entire contiguous parcel before and after the restriction is granted. Both parties apply this rule and value the conservation easement with reference to the 316.27-acre subject property. We will do the same.

The parties rely on several experts to value the easement. We evaluate an expert's opinion in the light of the expert's qualifications and the evidence in the record. *See Helvering v. Nat'l Grocery Co.*, 304 U.S. 282, 295 (1938); *Estate of Mellinger v. Commissioner*, 112 T.C. 26, 39 (1999). The persuasiveness of an expert's opinion depends largely on the facts and assumptions on which it is based. *Estate of Davis v. Commissioner*, 110 T.C. 530, 538 (1998). We are not bound to accept an expert's opinion in whole or in part and may accept those portions we find reliable. *Helvering v. Nat'l Grocery Co.*, 304 U.S. at 295; *Estate of Hall v. Commissioner*, 92 T.C. 312, 338 (1989). We also "may determine fair market value on the basis of our own examination of the evidence in the record." *Savannah Shoals, LLC v. Commissioner*, T.C. Memo. 2024-35, at *35, *aff'd*, No. 24-12661, 2026 WL 2056291 (11th Cir. July 16, 2026); *see also Jackson Crossroads, LLC v. Commissioner*, T.C. Memo. 2024-111, at *35, *aff'd*, Nos. 25-10744, et al., 2026 WL 822261 (11th Cir. Mar. 25, 2026); *Buckelew Farm, LLC v. Commissioner*, T.C. Memo. 2024-52, at *51, *aff'd*, No. 24-13268, 2025 WL 2502669 (11th Cir. Sep. 2, 2025).

A. *"Before Value" of the Subject Property*

1. *Prior Transactions Involving the Subject Property*

The best evidence of a property's fair market value is the price at which it changed hands in an arm's-length transaction reasonably close in time to the valuation date. *Ranch Springs*, 164 T.C. at 128–29. Prior sales of the subject property therefore may be highly probative. In addition, we have held that the purchase of a partnership interest may provide useful evidence of value where the interest acquired is nearly 100% and the partnership's only asset is the subject property. *Buckelew Farm*, T.C. Memo. 2024-52, at *56; *see also Oconee Landing Prop., LLC v. Commissioner*, T.C. Memo. 2024-25, at *71–72, *supplemented by* T.C. Memo. 2024-73.

Respondent points to two transactions as evidence of the subject property's fair market value before the conservation easement donation:

[*35] (1) the 2013 transfer of the subject property from Mr. Levin to Diamond West Realty, Inc., for $1.5 million and (2) Mr. Hankey's 2014 purchase of a 75% interest in MVL for $3.55 million. We are not persuaded that either transaction provides reliable evidence of fair market value because both were intertwined with preexisting relationships and other business dealings.

a. *2013 Transfer from Mr. Levin to Diamond West Realty, Inc.*

The 2013 sale occurred in the context of a longstanding personal and financial relationship between Mr. Levin and Brian. Mr. Levin and Brian's decades-long friendship appears to have animated their business dealings, particularly when it came to the VTTM. Time and time again—even after Brian had previously defaulted on loans—Mr. Levin stood ready to lend Brian money to preserve the VTTM's development rights, often without seeking additional collateral. The record reflects that Mr. Levin repeatedly provided Brian and his father financing over the years to preserve the development rights associated with the VTTM, including loans ranging from $100,000 to $4 million. The mixing of business and friendship was not one sided on the part of Mr. Levin. After the equestrian center burned down, Brian stood by Mr. Levin's side during a years-long regulatory battle to rebuild it. This history indicates that their dealings were not purely market driven.

The circumstances of the 2013 sale likewise do not reflect an arm's-length transaction. Mr. Levin did not list the property, solicit other buyers, or otherwise test the market. Instead, he sold the property directly to Brian's entity at a price that, on this record, appears substantially below market. In fact, even the comparable large tract sales offered by respondent—of tracts which are significantly inferior to the subject property—would suggest a much higher value for the subject property. Mr. Levin credibly explained that, after a difficult divorce, he sought to simplify his life, divest certain holdings, and focus on raising his daughter. He was satisfied with the wealth he had already accumulated. We find that explanation credible, and it reinforces the conclusion that the sale price reflected personal considerations rather than market forces.

Respondent argues that Mr. Levin's earlier decision to take the property back in 2009 by deed in lieu of foreclosure shows that Mr. Levin separated friendship from business. We disagree. That episode does not negate the evidence that, by 2013, Mr. Levin's priorities had shifted and

[*36] that the sale was motivated in substantial part by personal considerations.

Respondent also argues that Mr. Levin's retention of the equestrian center until 2022 undermines his testimony that he wished to divest his California real estate interests. We are not persuaded. The record shows that the equestrian center and the subject property were treated as distinct assets, particularly because the VTTM did not confer any entitlements on the equestrian center. Mr. Levin credibly testified that he viewed them as separate properties, and his decision to retain one does not materially undermine his testimony regarding the other.

On this record, we find that the 2013 sale price was materially influenced by personal considerations and was not the product of arm's-length bargaining. We therefore give it little weight in determining the subject property's fair market value.

b. *2014 Purchase of 75% of MVL*

We likewise are not persuaded that Mr. Hankey's 2014 purchase of a 75% interest in MVL for $3.55 million reliably reflects the subject property's before value. The record indicates that the transaction occurred against a backdrop of personal relationships and intense financial pressure. By the time of this transaction, Brian found himself once again in a financial pinch: The Levin notes were coming due soon and Brian felt a personal obligation to repay his longtime friend. He did not have the financial resources to repay the loans himself or through his development entities. Nor could Brian rely on third-party financing as apparent from his failed attempts to secure funding to satisfy the German American Bank obligation.

Brian's only remaining reliable option to repay the Levin notes was Mr. Hankey, but as before, his capital came with a condition. Through riding on the subject property with Brian, Mr. Hankey came to appreciate the recreational value of the property. Mr. Hankey credibly testified that he valued the ability to ride horses on the land and enjoy it as an extension of his nearby residence, and that his personal benefit outweighed potential development profit. Consequently, he conditioned his financing on the preservation of his personal enjoyment in the property. Faced with the pressure of satisfying the Levin notes, Brian had no alternative but to accept Mr. Hankey's terms. Therefore, this price reflects idiosyncratic motivations and financial pressure rather

[*37] than market value and explains the discrepancy between the partnership purchase price and the valuation supported by the record.

In addition, this transaction involved a significantly lower ownership interest than we have previously used as a proxy for the value of land in other cases and is further complicated by the indebtedness secured by the property. *See, e.g.*, *Seabrook Prop., LLC v. Commissioner*, T.C. Memo. 2025-6, at *67 (using a sale of a 99% partnership interest as evidence of fair market value of a property); *J L Mins., LLC v. Commissioner*, T.C. Memo. 2024-93, at *57 (using a sale of a 98% partnership interest as evidence of fair market value of a property); *Oconee Landing Prop.*, T.C. Memo. 2024-25, at *71–72 (using a sale of a 97% partnership interest as evidence of fair market value of a property). As the ownership percentage falls below 100%, the purchase price becomes less directly comparable to the value of the underlying real estate because marketability and control considerations can materially affect the value of the interest acquired. *See Astleford v. Commissioner*, T.C. Memo. 2008-128, slip op. at 19–20 (applying a lack-of-marketability discount and a lack-of-control discount to the sale of a limited partnership interest); *Estate of McCormick v. Commissioner*, T.C. Memo. 1995-371 (applying a lack of marketability and control discounts to a limited partner interest). Accordingly, we give the 2014 partnership-interest transaction little weight as evidence of the subject property's before value.

2. *Other Valuation Methods*

In the absence of reliable arm's-length transactions involving the subject property, courts typically consider one or more accepted valuation approaches to determine fair market value: (1) the market approach, (2) the income approach, and (3) an asset-based approach.[27] *See Bank One Corp. v. Commissioner*, 120 T.C. 174, 306 (2003), *aff'd in part, vacated in part, and remanded on another issue sub nom. JPMorgan Chase & Co. v. Commissioner*, 458 F.3d 564 (7th Cir. 2006). The usefulness of any approach depends on the nature of the property and the facts of the case. *See Chapman Glen Ltd. v. Commissioner*, 140 T.C. 294, 325–26 (2013).

Under the market approach, an appraiser estimates fair market value by reference to arm's-length sales of comparable properties

[27] Neither party uses the asset-based approach to value the easement. We agree that the asset-based approach is not appropriate.

[*38] occurring reasonably close in time to the valuation date. *See id.* at 326. Because no two properties are identical, the appraiser must make adjustments to account for differences such as size, location, development potential, and conditions of sale. *Wolfsen Land & Cattle Co. v. Commissioner*, 72 T.C. 1, 19 (1979). The reliability of a comparable property sales analysis depends on the comparability of the selected properties and the reasonableness of the adjustments made. *Id.* at 19–20.

Under the income approach, an appraiser estimates fair market value by discounting to present value the expected future cashflows that the property would generate. *See, e.g.*, *Chapman Glen Ltd.*, 140 T.C. at 327; *Marine v. Commissioner*, 92 T.C. 958, 983 (1989), *aff'd*, 921 F.2d 280 (9th Cir. 1991) (unpublished table decision). This approach is most reliable where the projections rest on a credible foundation, including market data and supportable assumptions about cost, timing, and risk. *Ranch Springs*, 164 T.C. at 151; *Excelsior Aggregates, LLC v. Commissioner*, T.C. Memo. 2024-60, at *33.

Both approaches must be applied in a manner consistent with the property's highest and best use. *See Mitchell v. United States*, 267 U.S. 341, 344–45 (1925); *Stanley Works & Subs. v. Commissioner*, 87 T.C. 389, 400 (1986); Treas. Reg. § 1.170A-14(h)(3)(ii). A property's highest and best use is the most profitable use that is legally permissible, physically possible, financially feasible, and maximally productive. *Olson v. United States*, 292 U.S. 246, 255 (1934); *Symington v. Commissioner*, 87 T.C. 892, 897 (1986). The highest and best use is presumed to be the property's current use absent proof to the contrary. *Mountanos v. Commissioner*, T.C. Memo. 2013-138, at *7, *supplemented by* T.C. Memo. 2014-38, *aff'd*, 651 F. App'x 592 (9th Cir. 2016); *Esgar Corp. v. Commissioner*, T.C. Memo. 2012-35, slip op. at 20, *aff'd*, 744 F.3d 648 (10th Cir. 2014). If a proposed highest and best use differs from the current use, it must be reasonably probable and not speculative. *Hilborn v. Commissioner*, 85 T.C. 677, 689 (1985).

The experts on both sides agree that the highest and best use of the subject property is residential subdivision development. Each side also relies upon both the market and the income approach. While we agree that both approaches are relevant to determine the value of the subject property before the easement, each side's application falls short of the finish line.

[*39] Petitioner's experts assumed that the entire subject property could be developed without meaningful constraints from the North Area Plan and the 2014 LCP. Respondent's expert Mr. DuVall adopted the opposite assumption: The VTTM conferred no meaningful development entitlements. These competing assumptions materially affect both the number and the character of the lots that could be developed and substantially reduce the reliability of each expert's comparable property sales analysis and cashflow projections.

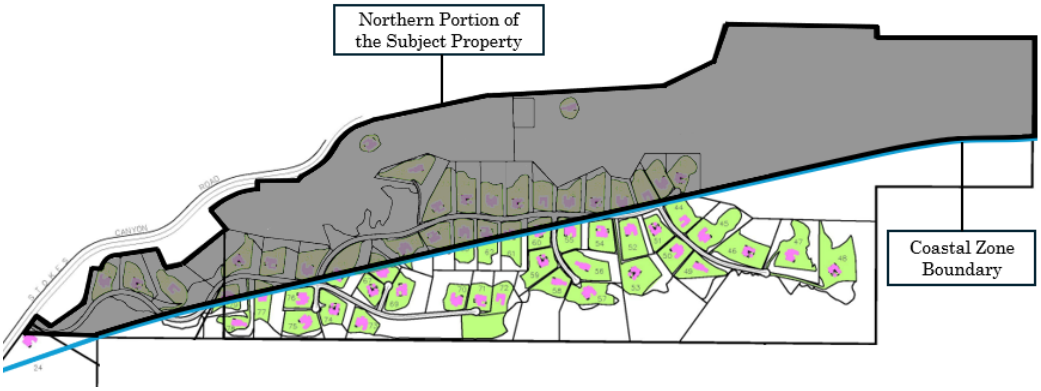
As discussed *infra*, the subject property does not fit either extreme. The VTTM likely preserves preexisting development standards for the northern portion, while development in the southern portion remains tightly constrained by the 2014 LCP. Because different regulatory regimes govern different portions of the property, and because neither side offered reliable comparables capturing this patchwork, we cannot reliably value the property as a single undifferentiated whole.

Accordingly, the most reliable method on this record is to value the subject property as the sum of its parts. We therefore determine the fair market value of the northern and southern portions separately—considering both the market and income approaches for each portion—and then add the resulting values. *See Champions Retreat Golf Founders, LLC v. Commissioner*, T.C. Memo. 2022-106, at *41 (determining the fair market value of a property by first determining the value of different portions of the property that had varying highest and best uses), *supplementing* T.C. Memo. 2018-146.

3. *Northern Portion*

The northern portion lies north of the coastal zone boundary and is highlighted below on the relevant portion of the VTTM:

[*40]



a. *Highest and Best Use*

As noted above, a property's highest and best use must be (1) legally permissible, (2) physically possible, (3) financially feasible, and (4) maximally productive. *Buckelew Farm*, T.C. Memo. 2024-52, at *52. Both parties agree that the highest and best use of the northern portion is residential subdivision development. Petitioner contends that 22 lots may be developed in their entirety in the northern portion. Respondent contends that 21 lots may be developed in the northern portion. Comparing petitioner's 22 lots to respondent's 21 lots, the dispute is not primarily over density, but over lot configuration—an issue driven by which development standards apply.

i. *Parties' Lot Configurations*

Petitioner's proposed lots generally track the VTTM, placing lots and building pads on ridge tops and other premium locations. Petitioner acknowledges that this configuration would not comply with the development ordinances in effect by 2014 but contends that the VTTM vests the development standards in place when the map was deemed complete in 1988. Petitioner's expert Mr. Cunningham testified that the differences between petitioner's proposed map and the VTTM are minor and remain in substantial compliance with the VTTM.

Respondent's expert Mr. DuVall prepared an alternative plat map that relocates lots and building pads to conform to the development standards applicable in 2014. Respondent does not dispute the physical possibility or financial feasibility of petitioner's proposed subdivision in

[*41] the northern portion; the dispute concerns the legal permissibility of petitioner's lot configuration.

ii. *Effect of North Area Plan on VTTM*

By 2014 the laws around development in the North Area had changed dramatically from the time when Charles obtained the VTTM. The stricter North Area Plan, rather than the 1981 Interim Area Plan, governed development in the North Area. Given these changes, we must determine whether development of the northern portion is governed by the standards in effect when the VTTM was deemed complete in 1988 or by the standards later adopted under the North Area Plan. This issue determines the legal permissibility of each party's proposed subdivision.

The answer follows from the vesting provisions applicable to the VTTM. A vesting tentative tract map generally confers the right to proceed in substantial compliance with the ordinances, policies, and standards in effect when the local agency deemed the application complete. Cal. Gov't Code §§ 66498.1(b) and (c). The local ordinances, policies, and standards in effect at the time the VTTM was deemed complete were the 1981 Interim Area Plan and its implementing ordinances. Respondent makes no persuasive argument that the VTTM failed to vest the 1988 development standards for the northern portion. We therefore conclude that the VTTM locked in the application of the 1981 Interim Area Plan and the implementing ordinances in effect when the VTTM application was complete. The later passage of the North Area Plan and corresponding implementing zoning ordinances did not affect the vested rights.

Whether the VTTM complied with those standards was determined by LA County in 1988 when it certified the final EIR and approved the map. LA County found that the VTTM complied with the applicable ordinances, policies, and standards, and that environmental impacts were mitigated to less-than-significant levels. We see no reason to second guess LA County's determination. Accordingly, development of the northern portion may proceed in substantial compliance with the VTTM.

iii. *"Substantial Compliance" with VTTM*

The remaining issue is whether petitioner's proposed lot configuration is in "substantial compliance" with the VTTM. Petitioner's proposed map is reproduced below; our discussion focuses on the shaded northern portion:

[*42]



Whether this map is in substantial compliance with the VTTM is ultimately determined through LA County's subdivision approval process. *See* Cal. Gov't Code § 66474.1; *see also Youngblood v. Bd. of Supervisors*, 586 P.2d 556, 562 (Cal. 1978) ("Approval of the final map thus becomes a ministerial act once the appropriate officials certify that it is in substantial compliance with the previously approved tentative map."). For valuation purposes, however, the relevant question is whether development in substantial compliance with the VTTM was reasonably probable as of the donation date. The record does not supply a bright-line definition of "substantial compliance" in this context, and the inquiry is necessarily fact dependent. We therefore look at the evidence, including testimony from professionals experienced in LA County subdivision practice.

Petitioner's engineering expert, Mr. Cunningham, opined that the lot configuration set forth in his expert report is in substantial compliance with the VTTM. Respondent does not meaningfully dispute that opinion. Mr. Cunningham's proposed lot layout is nearly identical to that set forth in the VTTM, and the differences appear only minor, including slight lot-line adjustments to lot 64 and 65 to remove them entirely from the coastal zone. On this record, we find it reasonably probable that petitioner's lot configurations in the northern portion could be developed in substantial compliance with the VTTM.

Accordingly, development of the northern portion in accordance with the VTTM is legally permissible, physically possible, financially feasible, and maximally productive. We conclude that the highest and best use of the northern portion is a 22-lot large lot subdivision consistent with the VTTM. With that conclusion in mind, we turn to the valuation approaches.

[*43] b. *Market Approach*

The market approach estimates fair market value by comparing the subject property to similar properties sold in arm's-length transactions reasonably close in time to the valuation date. *Savannah Shoals*, T.C. Memo. 2024-35, at *36. This approach is often the most reliable indicator of value when there is sufficient market data for comparable properties. *See Whitehouse Hotel Ltd. P'ship v. Commissioner*, 139 T.C. 304, 324–25 (2012) (holding that other valuation methods are "not favored if comparable-sales data are available"), *supplementing* 131 T.C. 112 (2008), *aff'd in part, vacated in part and remanded*, 755 F.3d 236 (5th Cir. 2014); *Estate of Rabe v. Commissioner*, T.C. Memo. 1975-26, 1975 Tax Ct. Memo LEXIS 348, at *11 ("In the case of vacant, unimproved property the 'market data' or 'comparable sales' approach is generally the most reliable method of valuation, the rationale being that the marketplace is the best indicator of value, based on the conflicting interests of many buyers and sellers."), *aff'd*, 566 F.2d 1183 (9th Cir. 1977) (unpublished table decision). The parties offered the opinion of three experts to assist in our market analysis. As applied to the northern portion, however, the market approach suffers from fundamental limitations that materially reduce its reliability.

The principal value-driving attribute of the northern portion is the VTTM. The VTTM is significant because it predates the adoption of the North Area Plan and therefore preserves development rights that are materially more favorable than those available for most large tracts in the area by the donation date. Properties with comparable vested subdivision rights are rare. A report from the Department of Regional Planning indicates that only a limited number of vesting tentative tract maps remained active for large-lot subdivision development in the region, and even fewer predate the North Area Plan. This unusual feature complicates the application of the market approach, which rests on the principle of substitution.

None of the experts identified a sale that closely resembled the hypothetical sale of the northern portion as of the donation date. The only expert who offered a sale involving properties entitled under a vesting tentative tract map was Mr. Williams. But the record lacks sufficient information to evaluate whether the vesting rights in that transaction were comparable to those conferred by the VTTM. For example, the report does not identify when the vesting tentative tract

[*44] map was approved, which prevents us from assessing whether it likewise predates the North Area Plan.

Moreover, the purported comparable properties involved materially different development rights. It contemplated approximately 314 single-family residences on lots ranging from 5,000 square feet to 0.5 acre—an intensity of development far exceeding that contemplated in the northern portion. Without reliable evidence to quantify how differences in density, lot size, and resulting end-product values would affect price, we would be left to speculation in attempting to adjust that sale to the subject property.

We do not require perfectly comparable properties. But we do require sufficient market evidence to make reasoned and supportable adjustments. *Wolfsen Land & Cattle Co.*, 72 T.C. at 19. Here, the experts did not provide a reliable basis to adjust the proffered sales to account for the VTTM's unique development entitlements and the substantial differences in density and lot characteristics. Accordingly, we give little weight to the market approach in valuing the northern portion. *See Champions Retreat Golf Founders*, T.C. Memo. 2022-106, at *28–29 (rejecting the market approach when the record lacked information sufficient to "determine whether the lots sold were comparable, how they might have been similar or different, and whether (or what) adjustments were necessary to make those lots comparable to the property at issue in this case"); *Glade Creek Partners, LLC v. Commissioner*, T.C. Memo. 2020-148, at *37–40 (rejecting the market approach when the experts provided poor comparable properties and failed to provide reliable adjustments to account for differences in the properties), *supplemented by* T.C. Memo. 2023-82, *aff'd in part, vacated in part, and remanded*, No. 21-11251, 2022 WL 3582113 (11th Cir. Aug. 22, 2022); *Estate of Wineman v. Commissioner*, T.C. Memo. 2000-193, slip op. at 29–30 (rejecting an expert's valuation approach because it was "far too conclusory," suffered "generally from a dearth of data," and "lack[ed] an adjustment grid" that would enable the Court to analyze the sale of comparable properties).

c. *Income Approach*

The income approach estimates the fair market value of property by discounting to present value the future cashflows the property is expected to generate. *See Chapman Glen Ltd.*, 140 T.C. at 327; *Marine*, 92 T.C. at 983; *Champions Retreat Golf Founders*, T.C. Memo. 2022-106, at *21. For undeveloped land intended for subdivision, appraisers

[*45] commonly apply a variation of the income approach known as the subdivision development method. *See Champions Retreat Golf Founders*, T.C. Memo. 2022-106, at *22; *Crimi v. Commissioner*, T.C. Memo. 2013-51, at *64–65. That method values raw land by modeling the property as if it were subdivided, improved, and sold as finished lots over an absorption period. *Champions Retreat Golf Founders*, T.C. Memo. 2022-106, at *22; *Crimi*, T.C. Memo. 2013-51, at *64–65.

The subdivision development method generally requires the following inputs: (1) the number of finished lots; (2) the projected retail value of each finished lot, derived from comparable lot sales; (3) the development and absorption schedule; (4) direct and indirect development costs, including permitting and infrastructure; and (5) a market-derived discount rate to convert net proceeds to present value. *See Crimi*, T.C. Memo. 2013-51, at *64–65 n.28 (citing Appraisal Institute, *The Appraisal of Real Estate* 370–76 (13th ed. 2008)). Depending on the circumstances, the model may also include appropriate adjustments for marketability and development risk. *See id.*

We have observed that the income approach is often most reliable when applied to an existing income-producing business with a track record of revenues and expenses. *See Ranch Springs*, 164 T.C. at 151. When applied to vacant land, the approach can be highly sensitive to assumptions, and unsupported projections have undermined income analyses in many conservation easement cases. *See, e.g.*, *Savannah Shoals*, T.C. Memo. 2024-35, at *36 ("Income valuation methods are not favored when valuing vacant land with no income-producing history because they are inherently speculative and unreliable."). For that reason, we must carefully examine the plausibility of the critical assumptions underlying the model. *See Ranch Springs*, 164 T.C. at 151; *Kiva Dunes Conservation, LLC v. Commissioner*, T.C. Memo. 2009-145, slip op. at 10–11.

This case presents unusual features that support consideration of the subdivision development method. Both parties' experts applied the method, and respondent defended its use on brief. More importantly, the key income and expense variables are grounded in real-world development experience. Although the northern portion itself had not been developed as of the valuation date, Brian and his entities had development experience with the VTTM, including construction of finished lots and homes west of Stokes Canyon Road on terrain with similar hillside constraints. The cost estimates relied upon by petitioner

[*46] were also supported by Mr. Cunningham, who worked directly on development of the VTTM and other projects in the region. In addition, after the valuation date, the subject property was further developed into finished and recorded lots, providing additional real-world context for development costs and timing. *Cf. Ranch Springs*, 164 T.C. at 151–53 (criticizing the income method when the experts had to estimate income and expenses without any basis in reality); *Seabrook Prop.*, T.C. Memo. 2025-6, at *66 (rejecting cost estimates that left "ample room to doubt the costs").

The revenue side of the model is likewise more supportable than in many cases. The experts agree that comparable sales of large undeveloped tracts with similar highest and best use are scarce in the area, particularly given the VTTM's unique vesting characteristics. Nevertheless, the experts were able to identify sales of finished lots that more closely resemble the lots contemplated for the northern portion (northern portion lots). Those finished-lot comparables provide a firmer basis for estimating retail lot values than the sales of large, unentitled tracts.

Finally, the income approach is more manageable here because the development and absorption period is relatively short. The experts' models do not require projecting costs and revenues decades into the future; as discussed below, the relevant period is approximately four years. The parties also agree that most development costs can be modeled on a per-lot basis, which allows us to adopt reliable components of each model and adjust them to reflect our findings regarding permissible lot yield.

For these reasons, we consider the income approach, using the subdivision development method, to determine the fair market value of the northern portion. We therefore turn to the specific variables used in the parties' models.

i. *Number and Character of Lots*

As discussed in our highest and best use analysis, development of the northern portion may proceed in substantial compliance with the VTTM as drawn by Mr. Cunningham. We therefore use 22 lots as the lot-yield input in our income approach. Mr. Cunningham's plan—and the VTTM—contemplate a gated subdivision. Other than the gate, no community amenities are included in the subdivision design.

[*47] ii. *The Value of Each Lot*

Having determined that 22 ridgeline and otherwise desirable lots are feasible on the northern portion, we turn to the value of each finished lot.[28]

a) *Mr. Erickson's Comparable Lot Sales*

Petitioner's expert Mr. Erickson relied on sales of finished lots in three nearby communities that he considered comparable to the lots contemplated for the northern portion: (1) The Estates at the Oaks of Calabasas (The Estates), (2) Hidden Hills, and (3) County Ridge.

The Estates is a gated enclave within the larger Oaks of Calabasas development, approximately three to four miles north of the subject property. It consists of 55 homes on large lots and sits approximately 250 to 400 feet higher in elevation than the subject property. The Estates includes such substantial amenities as a clubhouse, a pool, tennis courts, and a gym, as well as convenient access to Ventura Freeway and nearby retail.

- Estates 1 (April 2014): 1.72-acre vacant finished lot; 1-acre (43,560 sf) building pad; panoramic hilltop views; sold for $2.675 million ($61/sf of building pad).

- Estates 2 (July 2013): 1.63-acre vacant finished lot; 1-acre (43,560 sf) building pad; panoramic hilltop views; sold for $2.6 million ($60/sf of building pad).

- Estates 3 (August 2013): 1.75-acre vacant finished lot; 0.95-acre (41,382 sf) building pad; panoramic hilltop views; sold for $2.6 million ($63/sf of building pad).

- Estates 4 (April 2013): 0.83-acre vacant finished lot; building pad took up the entire lot; interior location with partial mountain view; sold for $1.85 million ($51/sf of building pad).

Hidden Hills is a gated community of more than 300 homes, roughly five to six miles north of the subject property, with an

[28] The experts based their income approach on all the lots in their proposed subdivision. We have renumbered the comparable lots continuously for added clarity in our analysis.

[*48] equestrian focus. It offers extensive amenities, including three equestrian arenas, tennis courts, a pool, a recreation center, and a movie theater.

- Hidden Hills 1 (December 2013): 1.55-acre vacant finished lot; 1.1-acre (47,916 sf) building pad; good valley/mountain views; sold for $3.25 million ($68/sf of building pad).

- Hidden Hills 2 (December 2013): 1.98-acre vacant finished lot; 1.25-acre (54,450 sf) building pad; good valley/mountain views; sold for $3.75 million ($69/sf of building pad).

- Hidden Hills 3 (October 2013): 1.03-acre vacant finished lot; building pad comprised the entire lot; no view; sold for $1.925 million ($43/sf of building pad).

- Hidden Hills 4 (July 2012): 7.07-acre vacant finished lot; 3.53-acre (153,767 sf) building pad; sold for $3.55 million ($23/sf of building pad).

County Ridge is a small nine-lot subdivision just north of the subject property on Stokes Canyon Road. It is not gated, offers no amenities, and comprises lower-value homes.

- Subdivision 1 (January 2014): 5.24-acre partially graded vacant lot; 0.7-acre (30,492 sf) building pad; no paved access; not on a ridgeline; sold for $850,000 ($28/sf of building pad).[29]

Mr. Erickson compared these sales to the lots contemplated for the northern portion, evaluating factors including amenities, views, topography, building-pad size, and development synergy. He classified most sales in The Estates and Hidden Hills as superior, primarily because of their amenity packages and established community character. He treated Hidden Hills 4 as similar on the theory that its unusually large size captured reverse economies of scale. He classified Subdivision 1 as inferior because it lacked a guarded gate and was associated with lower value homes.

On the basis of this set of sales and his qualitative adjustments, Mr. Erickson concluded that the northern portion lots should be valued above $28 per square foot of building pad (Subdivision 1) and below the

[29] Mr. DuVall opined that this sale price should be adjusted upward to $1 million to account for market trends.

[*49] amenity-rich sales in The Estates and Hidden Hills. He then grouped the 56 VTTM lots into clusters based on acreage and building pad size, and he then priced them primarily as a function of building-pad area. He valued lots between $30 and $40 per square foot of building pad but did not explain how he selected a particular figure within that range for any given cluster. For the largest lots, he applied $30 per square foot to the building pad area and then assigned the remaining acreage a value of $10,000 per acre, again without clearly explaining the basis for that residual acreage value. Using this methodology, Mr. Erickson derived an average lot value of $1,890,803.

b) *Mr. Williams's Comparable Lot Sales*

Petitioner's expert Mr. Williams relied on four finished lot sales drawn from a wider geographic area.

- Subdivision 2 (April 2015): 1.15-acre vacant finished lot with a net acreage[30] of 0.5 acre; sold for $1.47 million. The lot was in Malibu Park, a luxury coastal community approximately 9.3 miles southwest of the subject property within the coastal zone. It had mountain and ocean views and included an active building permit and architectural plans for a 6,700-square-foot residence.

- Subdivision 3 (July 2014): 1.91-acre lot with an approximately 0.49-acre (21,344 sf) developable flat pad; sold for $1.175 million. The property was in San Diego, approximately 114.8 miles southeast of the subject property.

- Subdivision 4 (October 2013): 3.02-acre vacant finished lot with approximately 1.02 acres of net developable area; sold for $1.28 million. The lot was approximately 8.3 miles southwest of the subject property and had ocean views. It was also subject to a partial trail easement on the southern end.

- Subdivision 5 (July 2013): 2.07-acre vacant finished lot with approximately 0.44 acre of net developable area; sold for $1.33 million. The lot was in the gated Country Estate subdivision approximately 51 miles east of the subject property in San Diego County.

[30] It is unclear from Mr. Williams's report whether net acreage refers to the building pad size.

[*50] Mr. Williams compared these lots to the northern portion lots, considering lot size, views, neighborhood characteristics, location, and market conditions. He performed a qualitative ranking of each lot and sale as superior, similar, or inferior and then derived a per-lot value for the northern portion lots.

He treated Subdivision 2 as slightly superior because it had ocean views and active building permits, though he considered its smaller size to be an offsetting factor. Mr. Williams treated Subdivision 4 and Subdivision 5 as similar to the northern portion lots, reasoning that their superior views and gated settings were offset by inferior location, market conditions, and lot characteristics. These sales bracketed his indicated per-lot value between $1.28 million (Subdivision 4) and $1.33 million (Subdivision 2). On the basis of this set of sales, Mr. Williams concluded that the northern portion lots should be valued at $1.3 million per lot.

c) *Mr. Hewlett's Comparable Lot Sales*

Rounding out petitioner's experts, Mr. Hewlett likewise identified sales he considered relevant to finished-lot pricing. Unlike the remaining experts, Mr. Hewlett does not offer an appraisal report. Consequently, we will not rely on the sales he identified in our market analysis. Instead, his report focuses on quantifying the effects of various qualities of the comparable property sales, including appreciation due to the passage of time, effect of ZIP Code on prices, and the effect of size on the price per acre.

d) *Mr. DuVall's Comparable Lot Sales*

Respondent's expert Mr. DuVall searched for sales of finished lots in 2013 and 2014 and identified ten transactions, including Subdivision 1, which we discussed *supra*.

i) *Large Tract Transaction*

Mr. DuVall also relied on a bulk tract transaction involving approximately 67 acres about 0.7 miles north of the subject property. The tract had entitlements for seven single-family residences. Dry utilities were available from the street, and rough grading of the building pads had been completed.

[*51] In June 2013 the tract owner (a real estate company) entered a joint venture with the buyer (a homebuilder). The buyer acquired the tract and borrowed development funds from the tract owner. The parties agreed to an average price of $656,000 per finished lot and estimated lot-finishing costs of $177,000 per lot. On the basis of these terms, Mr. Duvall inferred a tract value of approximately $3.35 million after accounting for the parties' cost estimates. In another portion of the record, Mr. Williams also referenced this transaction and calculated a purchase price of $4.6 million, though he did not disclose his methodology.

ii) *Individual Lot Sales*

- Subdivision 6 (January 2014): 25.26-acre vacant finished lot approximately four miles southeast of the subject property; sold for $1 million. The lot had two graded building pads (1 acre (43,560 sf) and 0.5 acre (21,780 sf)). Mr. DuVall calculated a combined price of approximately $15 per square foot of building pad. The property included a meadow in the southern portion and steep sloping hills/mountains in the northern portion. It was in the coastal zone.

- Subdivision 7 (December 2013): 24.5-acre vacant finished lot with a 1.5-acre (65,340 sf) graded building pad on top of a knoll; sold for $1.25 million ($19/sf of building pad). The lot was in The Reserve at Lobo Canyon, approximately 6.5 miles west of the subject property, and was subject to the North Area Plan. At the time of sale it had approved plans for a large house, a guest house, and a six-car garage.

- Subdivision 8 (April 2014): 16.5-acre unfinished lot; sold for $600,000. The lot was subject to the North Area Plan.

- Subdivision 9 (May 2014): 10.3-acre vacant unfinished lot; sold for $450,000. It included an approximately 0.25-acre (10,890 sf) building pad and was adjacent to the VTTM area west of Stokes Canyon Road. The lot was primarily hillside.

- Subdivision 10 (February 2014): 10.3-acre finished lot in the Abercrombie Estates subdivision; approximately 1-acre (43,560 sf) building pad; sold for $1.25 million ($29/sf of building pad). The lot was approximately three miles west of the subject property in the coastal zone. At the time of sale the Coastal Commission had approved plans for an 8,000-square-foot

[*52] residence. A stream on the lot separated the building pad from hillside terrain. The building pad had uphill views.

- Subdivision 11 (March 2014): 5.4-acre semifinished vacant lot in Palo Comado Estates, an equestrian-oriented community; sold for $1.35 million. The property consisted of two legal lots that together were restricted to one single-family residence under a conditional use permit. It was approximately five miles northwest of the subject property in Agoura Hills. The lot included a large, level building area, a stream, oak woodland, and hillside terrain. The rear quarter of the lot was deed restricted as open space.

- Subdivision 12 (May 2014): 4.25-acre lot consisting of two contiguous tracts; sold for $882,000. The parties allocated $332,000 to a 1.57-acre tract with a 0.3-acre (13,068 sf) building pad and $550,000 to a 2.68-acre tract with a 0.75-acre (32,670 sf) building pad. Together these lots sold for $19/sf of building pad. These lots were not finished.

- Subdivision 13 (March 2013): 3.5-acre finished lot with an approximately 2-acre (87,120 sf) graded building pad in the Vintage at Hidden Park subdivision; sold for $725,000 ($8/sf of building pad).[31] The lot was approximately 4.5 miles west of the subject property in the Santa Monica Mountains, was subject to the North Area Plan, and had panoramic views of Malibu Creek.

For these transactions, Mr. DuVall emphasized the sales of finished and mostly finished lots. He gave the greatest weight to Subdivision 1 and Subdivision 10. He considered Subdivision 10 superior because it had a large, level building pad. On the basis of this analysis, Mr. DuVall concluded that the northern portion lots should be valued at $1.1 million per lot.

e) *Our Analysis*

The record describes numerous lot sales offered by the parties as evidence of the value of the northern portion lots. We must determine which sales provide the most reliable guidance.

[31] Mr. DuVall applied a 20% upward adjustment for the value of this lot to account for market trend.

[*53] Under Mr. Cunningham's design, the 22 lots on the northern portion average 8.7 acres in gross area with an average building pad of approximately 1.02 acres (43,996 sf).[32] These lots are generally larger than the lots emphasized by petitioner's experts and smaller than several lots emphasized by respondent's expert. None of the appraisal experts provided consistent quantitative adjustments that would allow us to reconcile the comparable sales to the subject lots with precision. The testimony nevertheless supports several valuation principles that guide our analysis.

First, the experts generally agree that larger lots tend to sell for less on a per-acre basis than smaller lots—a phenomenon often described as reverse economies of scale. The principle reflects diminishing marginal utility: Once a buyer has sufficient land to accommodate a residence and desired privacy, additional acreage typically contributes less to value than the first acre or two. This concept is well established in valuation practice and caselaw. *See Oconee Landing Prop.*, T.C. Memo. 2024-25, at *71 ("It is also well established that smaller parcels (other things being equal) generally sell for higher per-acre prices than larger parcels."); *see also Estate of Giovacchini v. Commissioner*, T.C. Memo. 2013-27, at *96; *Estate of Kolczynski v. Commissioner*, T.C. Memo. 2005-217, slip op. at 16. However, the record reflects that small properties that do not have meaningful excess acreage beyond the building pad sell for significantly less than properties with some excess acreage.

Second, location is critical. The Santa Monica Mountains constitute a distinct high-end market characterized by limited supply of finished lots and strong demand driven by natural amenities, views, proximity to preserved open space, and privacy. This area was a magnet for celebrities and other high net worth individuals. Comparable property sale prices from materially different markets therefore warrant caution. Third, the record supports the general proposition that finished lots in established gated communities tend to command a

[32] Lots 80 and 81 were significantly larger than the remaining lots on the northern portion and pull the average lot size higher. The only expert that attempted to price these lots separately from the remaining lots was Mr. Erickson. However, his analysis and selection of a price of $10,000 per acre for the excess acreage was wholly without support in his report or the record more broadly. Therefore, we are without a sufficient basis to price these lots separately. Our approach of determining the price per average lot adequately compensates for any distortion these lots would otherwise have on the valuation.

[*54] premium over standalone lots, reflecting community, character, security, and amenity package.

Fourth, the record also supports adjusting comparable property sale prices. Although Mr. Hewlett did not prepare an appraisal report and we do not rely on his sales analysis, he offered several calculations that are useful for limited purposes. He provided a quantitative illustration of reverse economies of scale. His reverse-economies analysis supports the general proposition that differences in lot size can materially affect unit pricing.[33] He also provided and estimated market trend appreciation rates for the subject property's ZIP Code that respondent's expert Mr. DuVall agrees are reasonable. We agree and adjust the comparable sale prices below to reflect those time trends.[34]

Mr. Hewlett also attempted to quantify location premiums by comparing sales of four-bedroom homes across ZIP Codes and subdivisions. While that analysis provides a general sense of the magnitude of potential neighborhood effects, it has limited utility here because the subdivisions used in his analysis do not align consistently with the finished-lot comparables offered by the other experts. We therefore do not apply a separate location premium adjustment, though we consider location qualitatively in weighing the comparable property sales.

With these principles in mind, we first exclude certain sales. We give no weight to the sales of Subdivision 3 and Subdivision 5, which are in the San Diego region and therefore reflect different market forces. We likewise give no weight to the sale of Subdivision 2, which is in a coastal-zone market and included active permits and architectural plans. The record does not allow us to isolate the value of those permits and plans from the land value, and the permitting premium is likely substantial in the coastal zone.

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[33] We do not apply the formulas he derived but instead use them to assist in our qualitative analysis.

[34] Mr. Hewlett provided appreciation rates for select months in 2013 and 2014: April 2013 at 19%; July 2013 at 14%; November 2013 at 6%; December 2013 at 4%; March 2014 at 4%; and October 2014 at 1%. For the appreciation rates not expressly provided by Mr. Hewlett, we have assumed constant linear appreciation between the two closest months. For example, Mr. Hewlett did not provide appreciation rates for the three months between July 2013 and November 2013. Between July and November 2013 the rate of appreciation declined by 8%. We have assumed appreciation declined over this time by 2% monthly such that the appreciation rates were 12% for August 2013, 10% for September 2013, and 8% for October 2013.

[*55] Neither do we give weight to the Large Tract joint venture transaction. Unlike the other transactions, it was not a straightforward land sale. The parties structured it as a joint venture with seller financing and development cost assumptions. Mr. DuVall and Mr. Williams derived materially different implied prices for the tract ($3.35 million and $4.6 million, respectively), reflecting the uncertainty inherent in extracting a land value from the transaction terms. On this record, we cannot reliably determine the price at which the tract changed hands.

Finally, we give no weight to the sales of Subdivision 8, Subdivision 9, and Subdivision 12. These lots are unfinished and therefore are poor comparisons to the northern portion lots. As discussed *infra*, the fact that development in the region is costly and takes several years would significantly reduce the prices of these comparable property sales as compared to the northern portion lots.

We therefore focus on the remaining finished and semifinished lot sales. The experts valued the northern portion lots using two related metrics: (1) price per square foot of building pad and (2) price per finished lot. We begin with the building-pad metric.[35]

i) *Price per Square Foot of Building Pad*

Both parties envision a luxury residential community with large custom homes on each lot. Large custom homes require an adequate building pad to support the intended development. The average building pad on the northern portion lots is 43,996 square feet. The comparable lots offered by the experts include building pads ranging from approximately 30,000 square feet to over 150,000 square feet.

The record does not establish the average building pad size required to support a large custom home. Given the wide range of building pad sizes in the comparable properties, we focus initially on the extreme outliers to determine whether building pad size appears to materially affect the price per square foot. Hidden Hills 4,

[35] Only Mr. Erickson determined a price of the subject property based on the size of the building pad. On occasion, the other experts offered the size of the building pad located on their selected comparable lots. To the extent we can determine the size of the building pad, we consider these other comparable property sales in this analysis. The information regarding the following comparable lot sales is not sufficient to be useful: Subdivision 4, Subdivision 8, and Subdivision 11.

[*56] Subdivision 6, Subdivision 7, and Subdivision 13 have the largest building pads among the filtered comparables, each in excess of 65,000 square feet. These sales reflect the lowest price per square foot of building pad by a substantial margin. This suggests diminishing marginal returns once a building pad reaches a certain size. Accordingly, we do not rely on the sales of Hidden Hills 4, Subdivision 6, Subdivision 7, and Subdivision 13 in valuing the northern portion lots as a function of building pad size.

Excluding these outliers leaves the sales of the following comparable properties for consideration: Estates 1, Estates 2, Estates 3, Estates 4, Hidden Hills 1, Hidden Hills 2, Hidden Hills 3, Subdivision 1, and Subdivision 10. Because the appraisal experts did not quantify adjustments according to building pad size, we likewise take a qualitative approach. We discuss the remaining comparable property sales in descending order of superiority to the sales of the northern portion lots.

The sales of Estates 1, Estates 2, Estates 3, Hidden Hills 1, and Hidden Hills 2 are far superior. These lots have roughly comparable building pad sizes but substantially less excess acreage. When a buyer is purchasing a luxury lot primarily to be able to build a large custom home, the building pad is the principal driver of value, and additional acreage beyond the pad contributes less on a unit basis. We therefore would expect the northern portion lots—each with substantial excess acreage—to sell for a lower price per square foot of building pad than these comparable sales.

These developments also offered superior views due to elevation and, more significantly, high-end gated amenities such as recreation facilities, equestrian areas, and community centers. Mr. Erickson opined that these amenities would not warrant a material adjustment because purchasers of large lots tend to build their own amenities. We are not persuaded. Mr. Erickson did not cite any market data supporting that proposition. Moreover, the amenities in these developments go beyond what could reasonably be recreated on an individual's lot. For example, the Estates included a substantial community center, and Hidden Hills had multiple equestrian arenas. The amenities add value to these lots that cannot be ignored. We therefore find that the amenities materially contribute to the value of these lots and render them significantly superior to the northern portion lots. After adjustments for market conditions, these sales reflect prices between $63 and $72 per square foot of building pad. We would expect

[*57] the northern portion lots to sell for less than the low end of that range.

The sales of Estates 4 and Hidden Hills 3 present a different story. Like the prior lots, these lots benefit from superior community amenities. However, unlike the prior lots, their lot characteristics are inferior to the northern portion lots. Both are on flatter terrain and lack ridgeline mountain views. In addition, their configuration provides little or no excess acreage beyond the building pad itself. Balancing these factors, we find these sales are only slightly superior to the sales of the northern portion lots. After adjustments for market conditions, Estates 4 sold for $61 per square foot of building pad, and Hidden Hills 3 sold for $46 per square foot of building pad. We would expect the northern portion lots to sell for slightly less than $46 per square foot of building pad.

The sale of Subdivision 10 is inferior to the sales of the northern portion lots. This lot is broadly similar in finished condition and has a comparable building pad size. It is also in a gated community without meaningful amenities. However, its views are inferior because the building pad is adjacent to the road and lacks the ridgeline mountain views that distinguish the northern portion lots. Subdivision 10 also benefited from Coastal Commission approved building plans. We do not view that factor as increasing its value relative to the northern portion lots. The northern portion lots lie outside the coastal zone and would not require Coastal Commission approval. Both would still require ordinary local permitting. Moreover, as discussed above, application of the coastal zone development regulations, such as the setback ordinance, would reduce a lot's market value relative to an otherwise similar lot outside the coastal zone. After adjustments for market conditions, Subdivision 10 sold for $30 per square foot of building pad. We would expect the northern portion lots to sell for more than this.

The sale of Subdivision 1 is also inferior to the sale of the northern portion lots. Although geographically close to the subject property, it was only partially finished and lacked necessary road improvements. It was not in a gated community and did not offer the ridgeline views that are a key feature of the northern portion lots. We therefore would expect the northern portion lots to sell for more than Subdivision 1 on a price-per-square-foot building pad basis.

Considering the above sales, we find that the price of the northern portion lots is best supported by a range between approximately $46

[*58] (Hidden Hills 3) and $30 (Subdivision 10) per square foot of building pad. We select $40 per square foot of building pad. Neither Hidden Hills 3 nor Subdivision 10 captures the ridgeline views that are the primary selling feature of the northern portion lots. The record supports the conclusion that views materially increase the price per square foot of building pad in luxury subdivisions. Within the luxury subdivision sales, lots with meaningful views sold for approximately $15 more per square foot of building pad than lots without comparable views. Comparing sales within the same development controls for many external variables, including subdivision location and shared amenities. Although we cannot factor in every lot-specific variable (such as configuration), the consistent magnitude of this differential supports a meaningful upward adjustment for the northern portion lots' superior views. Applying $40 per square foot of building pad to the average building pad size of 43,996 square feet yields an indicated value of $1,759,840 per lot.

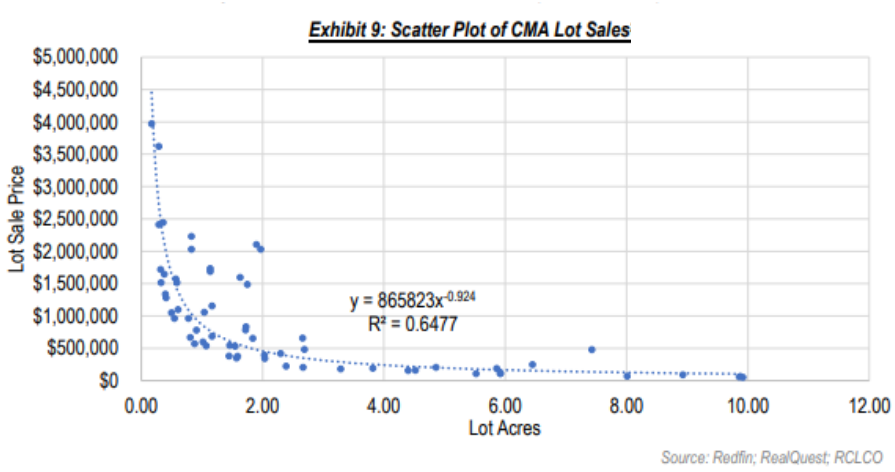
ii) *Price per Lot*

Mr. Williams and Mr. DuVall estimated the value of the northern portion lots by comparing each lot as a whole to the comparable lot sales. The average northern subject property lot is 8.7 acres. Reviewing the comparable sales on a per-lot basis, we find that much of our analysis above remains applicable.

The sales of Estates 1, Estates 2, Estates 3, Hidden Hills 1, and Hidden Hills 2 are all superior to the sales of the northern portion lots because those developments offer high-end amenities. However, those lots are substantially smaller than the northern portion lots, and lot size is expected to affect the per-lot purchase price. The question is the magnitude of that effect. Mr. Williams opined that small lots generally sell for less than large lots. This is a commonsense proposition. But Mr. Williams did not provide a quantitative framework to measure how much lot size affects per-lot pricing in this market.

Mr. Hewlett picked up the reins and offered a useful illustration of the relationship between lot size and pricing through his market data. Mr. Hewlett analyzed sales in the area between 2010 and 2014 for properties priced over $500,000 that consist of 10 acres or less. His scatter plot graph showed a strong negative exponential relationship between lot size and price per acre: The smallest lots sell at the highest prices per acre, and the price per acre declines rapidly as lot size

[*59] increases to approximately two acres. Beyond that point, the decline levels off. His scatter plot is reflected below:



Although Mr. Hewlett's analysis was expressed on a per-acre basis, it is useful in understanding how lot size affects the overall per-lot purchase price. For small lots, a high price per acre may still yield a modest per-lot price because the buyer is purchasing less acreage. For larger lots, a lower price per acre is offset by the buyer's purchasing more acres. But as lot size increases, the incremental effect of additional acreage diminishes.

Mr. Hewlett's examples illustrate the point. Under his model, a two-acre lot would sell for $912,657, while an eight-acre lot would sell for $1,014,061—an increase of only about $100,000. Thus, while smaller lots generally sell for less than larger lots, the per-lot price differential narrows substantially once lots exceed roughly two acres. With these principles in mind, we return to the comparable property sales.

The sales of Estates 1, Estates 2, Estates 3, Hidden Hills 1, and Hidden Hills 2 remain far superior. In addition to the superior amenities, these lots are around two acres—substantially smaller than the 8.7-acre northern portion lots. Mr. Hewlett's data indicates that increasing lot size from roughly two acres to nine acres has only a modest effect on per-lot price. Thus, the size difference does not overcome the substantial superiority of the amenities in these developments. After adjustments for market conditions, the lowest-priced lot among these sales sold for $2,768,625. We would expect the northern portion lots to sell for less.

[*60] The sale of Hidden Hills 4 is likewise superior. It shares the high-end amenities of the other Hidden Hills and Estates sales, but unlike the two-acre lots discussed above, it is 7.07 acres—closer in size to the northern portion lots. The slightly smaller size would tend to reduce its price relative to an otherwise similar 8.7-acre lot. But the superior amenities substantially outweigh any modest size adjustment. After adjustments for market conditions, Hidden Hills 4 sold for over $4 million. We would expect the northern portion lots to sell for significantly less.

The sales of Estates 4 and Hidden Hills 3 are only slightly superior. Like the other Estates and Hidden Hills, these lots benefit from superior amenities. But as discussed above, these lots also have material drawbacks relative to the northern portion lots, including inferior views and lot configurations that provide little to no excess land beyond the building area. These lots are also smaller—approximately one acre—which would tend to reduce their per-lot price. After adjustments for market conditions, the lowest priced lot sold for $2,079,000. We would expect the northern portion lots to sell for slightly less.

The sale of Subdivision 11 is slightly inferior. Although Subdivision 11 is in an equestrian-oriented subdivision, it was only semifinished and offered stream and woodland views rather than ridgeline mountain views. It is also smaller than the northern portion lots at approximately five acres. After adjustments for market conditions, it sold for approximately $1.4 million. We would expect the northern portion lots to sell for more.

The sale of Subdivision 4 is also slightly inferior. Subdivision 4 is similar in finished condition and development potential. It also offers ocean views, which could be superior to the average buyer. However, it was subject to a partial easement crossing the front of the lot and was not in a gated community. Moreover, it is smaller than the northern portion lots at 3.02 acres. On balance we find the sale of Subdivision 4 inferior to the sales of the northern portion lots. After adjustments for market conditions, it sold for approximately $1.38 million. We would expect the northern portion lots to sell for more.

The sale of Subdivision 10 is slightly inferior. The lot lacks ridgeline views and instead offers inferior stream views and uphill rear exposure. However, it is larger than the northern portion lots at 10.3 acres. We would expect the larger size to increase its per-lot price,

[*61] though Mr. Hewlett's data indicates the magnitude of that size effect is modest at these acreage levels. The size difference offsets some, but not all, of the inferiority resulting from weaker views. We therefore treat this sale as slightly inferior and would expect the northern portion lots to sell for more.

The sale of Subdivision 13 is inferior. Although the lot is finished, located in a gated community, and has Santa Monica Mountain views, it does not appear to offer the ridgeline views that are a defining feature of the northern portion lots. It is also smaller at approximately three acres. Subdivision 1 is also inferior. Subdivision 1 is only semifinished, lacks ridgeline views, is not gated, and is smaller. We would expect the northern portion lots to sell for more than these.

Finally, Subdivision 6 and Subdivision 7 are too large to provide useful guidance. At approximately 24.5 and 25.26 acres, these sales exceed the size range of Mr. Hewlett's analysis and do not provide a reliable basis for quantifying the effect of lot size at that scale. Moreover, sales of larger lots in the record suggest pricing below $10,000 per acre, indicating that different market dynamics may apply at those acreage levels. We therefore do not rely on these sales.

Considering the above sales, we find that the per-lot price of a northern portion lot is between $1.404 million (Subdivision 11) and $2.079 million (Hidden Hills 3). We select a price of $1.8 million per lot. A value closer to that of Hidden Hills 3 is warranted because the competing strengths and weaknesses of that lot more closely resemble the northern portion lots than do the inferior lots at the low end of the range. Subdivision 11, for example, is only partially finished, and finishing a lot in this market is expensive and time consuming under the assumptions of the hypothetical sale. Subdivision 11 is also inferior in view and smaller in size. Hidden Hills 3 reflects a luxury-market purchaser, and its lot-specific disadvantages (inferior views and configuration) help balance its superior subdivision amenities. We therefore conclude that a value modestly below the sale's price of Hidden Hills 3, and well above the price of the inferior sales, best reflects the fair market value of the northern portion lots.

iii) *Reconciled Price*

We must now reconcile the differing per-lot values indicated by the two pricing frameworks discussed above. Valuing the northern portion lots as a function of building pad size yields an indicated value

[*62] of $1,759,840 per lot. Valuing the lots as a whole yields an indicated value of $1.8 million per lot.

We find both approaches informative and assign them equal weight. The building-pad approach captures the value attributable to the home sites, which are a principal driver of demand, but it tends to understate the contribution of the substantial acreage beyond the pad. The per-lot approach better reflects how the market prices large luxury lots, including the value of excess land, but it does not isolate the contribution of the building pad. Giving each approach equal weight, we determine a reconciled price of $1,779,920 per lot for use in our income approach.

iii. *Absorption Rate*

The absorption rate reflects the number of lots expected to sell each year. *See Lake Jordan Holdings, LLC v. Commissioner*, T.C. Memo. 2025-123, at *20; *Trout Ranch, LLC v. Commissioner*, T.C. Memo. 2010-283, slip op. at 20, *aff'd*, 493 F. App'x 944 (10th Cir. 2012). Developers of large subdivisions commonly begin marketing before the subdivision is completed or the final map is recorded. The experts agree that several lots would sell during a pre-sale period and that, after the initial surge, the remaining inventory would sell at a steady rate. They disagree, however, on the number of pre-sale lots and the annual absorption rate.

Mr. Erickson opined that 15 lots would sell during the pre-sale period and that the remaining inventory would sell at a rate of one lot every two months, or six lots annually. He based his pre-sale estimate on Brian's prediction, which he believed was reasonable. He based his absorption rate on the marketing history of seven custom lot sales between 2012 and 2014 in The Estates and Hidden Hills developments, which sold between 1 month and 11 months after listing. Mr. Erickson opined that the sales would proceed more quickly in a new subdivision because coordinated marketing typically increases initial sale velocity.

Mr. Williams adopted Mr. Hewlett's absorption rate analysis. Mr. Hewlett opined that between 10 and 16 lots would sell during the pre-sale period, and Mr. Williams selected 10 lots. For the absorption rate, Mr. Hewlett relied primarily on household income concentration and building permit activity in Calabasas and Hidden Hills, which increased sharply during periods when new inventory entered the market. On the

[*63] basis of those calculations, he estimated absorption at eight lots per year.

Mr. DuVall opined that five lots would sell during the pre-sale period and that sales would proceed at 12 lots annually. He did not explain his pre-sale assumption. He derived his absorption rate from the sales pace of finished homes in The Vintage at Hidden Park subdivision and increased that rate according to his expectation of improved market conditions, without explaining the magnitude of that adjustment.

We adopt Mr. Erickson's assumptions: 15 pre-sale lots and an absorption rate of 6 lots per year. Although 15 pre-sale lots is substantial, it is well within the historic trends of the region. As Mr. DuVall explained, in 2013, 10 vacant lots over 5 acres were sold in the unincorporated area in the Santa Monica Mountains National Recreation Area between Calabasas and Malibu. He reported that in 2014, the sales increased to 17 vacant lots. We would expect the total number of sales to increase beyond this trend because of the pent-up demand in the market. As explained in Mr. Hewlett's report, building permit data likewise reflects sharp increases when new inventory entered the market, supporting the existence of pent-up demand that would further increase the total number of sales in the region. Mr. Erickson's pre-sale estimate also falls within Mr. Hewlett's stated range. Consequently 15 pre-sale lots is reasonable.

We find Mr. Erickson's absorption rate better supported because it is grounded in comparable vacant lot sales in similar luxury subdivisions. By contrast, Mr. Hewlett's multistep model does not adequately explain how its inputs translate into a reliable absorption rate. We likewise reject Mr. DuVall's absorption rate because it relies on finished homes sales, and the record does not support treating demand for finished homes as a proxy for demand for high-end custom lots.

Accordingly, for our income approach, we assume 15 lot sales during the pre-sale period with the remaining lots selling at a rate of six lots per year.

iv. *Expenses*

We turn next to the development costs for the proposed 22-lot subdivision in the northern portion. The parties presented competing

[*64] estimates of the direct and indirect costs associated with construction, permitting, and sales.

a) *Petitioner's Experts*

Both Mr. Erickson and Mr. Williams relied heavily on cost estimates prepared by Mr. Cunningham, who based his construction cost projections on his development experience on other portions of the VTTM property. Mr. Cunningham estimated construction costs for the full 56-lot subdivision at $17,121,708, or $305,745 per lot. He based that estimate on 11 years of development experience, including work developing the VTTM property west of Stokes Canyon Road.

For indirect costs, Mr. Erickson and Mr. Williams performed their own analysis. With respect to real property taxes, both assumed that the property would not be reassessed until the first lot sale. Under that assumption, taxes would increase only by the statutory 2% annual cap set forth in California law. After the first lot sale, both assumed that LA County would reassess the remaining property to reflect the value of the infrastructure improvements. Thereafter, the total property tax burden would decline as lots were sold and associated property tax obligations shifted to the buyers.

For the remaining indirect costs, Mr. Erickson and Mr. Williams determined the following costs were appropriate:

Indirect Costs	*Mr. Erickson*	*Mr. Williams*
Insurance	$265,000 lump sum to cover construction phase	2% of sales
Supervision/Project Management	$250,000 lump sum	$200,000 lump sum
Financing	8% annual interest on 60% outstanding balance with a 1.5% loan origin fee	8% through the three years after construction[36]
Sales & Marketing	5% of sales	5% of sales
General & Administrative	$0	2% of sales starting with first lot sale
Entrepreneurial Incentive	12% of sales	10% of sales

b) *Respondent's Expert*

Mr. DuVall likewise relied in part on third-party materials to estimate the cost of developing the lots. For direct construction costs, he relied on a report by Mr. Caldwell—who was not admitted as an expert and did not testify. For planning and permitting costs, he relied on a report by Mr. Jewett. Both materials were labeled draft reports subject to change, and neither contained sufficient detail for us to evaluate how the authors derived the cost figures. Mr. DuVall performed his own estimates of certain indirect costs based on a survey of subdivisions in LA County and Ventura County.

For property taxes, Mr. DuVall assumed that the property would be reassessed on the donation date to fair market value, which he derived from his market approach. He further assumed that the property would be reassessed again at the sale of the first lot to reflect the value of the infrastructure improvements. He then assumed taxes would decline ratably as lots were sold. He applied the following additional costs:

[36] It is unclear from his report to what base Mr. Williams applies the 8% rate.

[*66]

Indirect Cost	*Cost*
Administrative & Overhead	1% of sales
Market, Sales & Escrow	5% of sales

c) *Our analysis*

Although neither party separately calculated all expenses specifically for a 22-lot subdivision, the record supports allocating subdivision-related expenses on a per-lot basis. The parties agree that a ratable allocation across the lots is reasonable. We therefore compare the parties' positions on a per-lot basis.

Petitioner offered the only testimony supporting a direct construction cost estimate. Mr. Cunningham has substantial development experience in the region, including experience developing the VTTM. That experience bolsters the reliability of his cost estimate. We therefore adopt Mr. Cunningham's construction cost estimate, adjusted on a per-lot basis for the 22-lot subdivision. This method yields direct costs of $305,745 per lot.

We recognize that Mr. Cunningham's estimate may include certain permitting costs that would not apply to the northern portion. But any such items appear minor relative to the overall estimate and, in any event, would be offset by other permitting costs that are required for the northern portion but were not separately quantified in petitioner's model (such as oak tree permitting and replacement requirements). We therefore find Mr. Cunningham's estimate a reasonable proxy for the direct permitting and construction costs of the northern portion.

By contrast, respondent offered no expert testimony to support direct cost estimates. Mr. DuVall relied on draft third-party reports from individuals who did not testify as to those reports, and those materials provide insufficient detail on their face for us to evaluate their reliability. We therefore give them no weight.

We turn next to indirect development costs, including property taxes, insurance, supervision and project management, sales and marketing, administrative expenses, and financing costs. We start with the sales and marketing expenses. All experts assumed sales and

[*67] marketing costs of 5% of gross sales. We find that assumption reasonable and adopt it. The parties dispute the remaining costs.

For property taxes, the parties agree that the property would be reassessed at the sale of the first lot to reflect the value of the infrastructure improvements. They disagree, however, on how property taxes should be calculated between the donation date and the first lot sale.[37] Petitioner assumed that the property would not be reassessed on the donation date and that taxes would continue to be based on the historical assessed value, subject to the 2% annual cap under California law. Respondent assumed that the donation date would trigger reassessment of fair market value, which he derived from his market approach, before reassessment again at the first lot sale to reflect infrastructure improvements.

We adopt petitioner's approach. The record does not establish that a reassessment would occur on the donation date. Furthermore, petitioner's method is grounded in the historical assessment of the subject property and reflects established assessment practices in LA County. We therefore adopt petitioner's assumption for purposes of this income approach. Mr. DuVall's method, by contrast, rests on a substantial and inadequately supported assumption that the property would be reassessed to fair market value on the donation date. *See Whitehouse Hotel Ltd. P'ship*, 139 T.C. at 323 (discussing the risk of even small errors in the variables input into the income method). It also depends on Mr. DuVall's market-approach valuation, which we rejected, *supra*. Because we do not adopt respondent's market approach valuation nor did we calculate our own market approach valuation, we have no reliable basis to estimate the amount of any reassessment on the donation date. Respondent also failed to identify any authority supporting reassessment as of the donation date under these circumstances.

Accordingly, through the first lot sale we assume taxes are based on the historical assessed value (adjusted by the statutory 2% annual cap and excluding the ratable portion attributable to the southern portion not included in the northern portion). At the first lot sale, we

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[37] The method advanced by each party appears permissible under the Uniform Standards of Professional Appraisal Practice. Appraisal Found., Appraisal Standards Bd., *Uniform Standards of Professional Appraisal Practice*, Standards Rule 1-4 (2014 ed.) (requiring that an appraiser weigh historic information and trends with anticipated future events in determining expense statements).

[*68] assume reassessment to reflect infrastructure improvements. Thereafter, the tax burden declines as lots are sold.

We turn now to insurance. We adopt Mr. Erickson's insurance estimate. Mr. Erickson's model of insurance costs as a construction-period cost is supported by his analysis. Respondent did not separately model construction insurance. We reject Mr. Williams's estimate that insurance would equal 2% of sales because he provided no support for that assumption and because insurance costs are not properly modeled as a percentage of future sale proceeds. Under Mr. Erickson's estimate, insurance costs are $4,732 per lot during the construction period.

We will likewise adopt Mr. Erickson's cost estimates for supervision/project management and construction financing. On a per-lot basis, supervision and project management costs are $4,464 per lot. Mr. Erickson estimated construction financing costs of 8% annual interest with a 1.5% loan origination fee.

Mr. DuVall and Mr. Williams also included an administrative and overhead line item. Neither expert explained what expenses were included in that or whether those expenses were captured elsewhere in the discounted cashflow model. Because we cannot determine whether this line item duplicates other costs, we do not adopt it.

Finally, the parties differ on how they treat entrepreneurial profit. Petitioner treated entrepreneurial incentive as a separate line-item expense. Respondent incorporated it into the discount rate. As discussed more *infra*, market sources commonly treat entrepreneurial incentive as part of the overall discount rate rather than as a separate line item. We therefore consider entrepreneurial incentive as part of our discount rate analysis rather than as a distinct expense.

v. *Development Timeline*

We must next determine the development timeline, including the permitting process through construction of finished lots and recordation of the final map. A lot cannot be sold until the final map is recorded. Cal. Gov't Code § 66499.30(a). The timeline adopted in this section therefore determines when the pre-sale lots discussed above will be sold.

a) *Expert Opinions*

Mr. Erickson assumed a two-year entitlement period followed by one year of construction. He derived the entitlement period from the

[*69] opinions of Mr. Gutierrez and Mr. Cunningham. Mr. Gutierrez addressed the permitting required to record a final map and opined that the process would take approximately two years, largely because of the time required to obtain a coastal development permit. Mr. Cunningham addressed the timing of civil engineering and revision cycles. On the basis of his experience with the VTTM and other developments, he estimated that the preparation of the final tract map, final engineering plans, and required hydrology and hydraulics reports would take approximately three months, followed by a nine-month revision and resubmission process. Mr. Williams likewise assumed a two-year permitting period, on the basis of Mr. Gutierrez's opinion, and assumed construction would take three years.

Mr. DuVall assumed three years for planning and nine months for construction. He based those estimates on a draft appendix prepared by Mr. Jewett.

Respondent also offered testimony from Dr. Cooper regarding the permitting timeline. Dr. Cooper opined that LA County would likely require a new EIR because the final EIR was not adequately supported. He also opined that it was unclear whether LA County would allow oak tree removal under the prior permit or would instead require a new application supported by an updated oak tree survey. He further opined that a complete oak tree survey of the entire subject property could take 12 months or longer.

b) *Our Analysis*

We begin with the permitting timeline. We do not rely on Mr. DuVall's permitting estimates because they are based on a draft report prepared by Mr. Jewett, who did not testify and whose methodology was not disclosed. This leaves the opinions of Mr. Gutierrez, Mr. Cunningham, and Dr. Cooper. As discussed above, we assume that the northern portion is outside the coastal zone. We therefore do not include the coastal zone development permit process in our timeline. The coastal permit was, by all accounts, the most time-consuming component of Mr. Gutierrez's schedule. Removing that component materially shortens the permitting period.

It is helpful to briefly summarize the steps required for MVL to record a final map. As of the valuation date, the property was entitled to development in substantial compliance with the VTTM. To obtain recordation of a final map, MVL would need to demonstrate that: (1) the

[*70] final map is in substantial compliance with the approved VTTM, (2) the conditions of approval have been satisfied, and (3) the project complies with applicable laws that LA County is required to apply under the vesting provisions of the Subdivision Map Act.

Whether a proposed final map is in substantial compliance with the VTTM is a determination made by LA County. For the reasons discussed *supra*, we find it likely that the map prepared by Mr. Cunningham would be found in substantial compliance. Once substantial compliance is established, LA County's approval becomes ministerial. *Youngblood*, 586 P.2d at 562; *Ailanto Props., Inc. v. City of Half Moon Bay*, 48 Cal. Rptr. 3d 340, 362 n.17 (Ct. App. 2006) (holding that recording the final map for a vested tentative tract map is ministerial rather than discretionary). If MVL satisfies the conditions of approval and the applicable vesting requirements, LA County must approve the final map.

Mr. Cunningham estimated that preparation of the final tract map, engineering plans, and required hydrology and hydraulics reports would take approximately three months, followed by nine months of revisions and resubmissions. We find that estimate reasonable and adopt it. Accordingly, we assume that the civil approval process required to record the final map would take one year.

Dr. Cooper opined that LA County would require a new EIR because the prior report was inadequately supported. If required, this would greatly extend the permitting time because the subsequent EIR is subject to the same notice and public review as the initial EIR. Cal. Code Regs. tit. 14, § 15162(d). We disagree. LA County certified the final EIR when it approved the VTTM. The report is presumptively adequate. The California Environmental Quality Act permits a county to request a subsequent or supplemental environmental impact report only in limited circumstances, such as substantial changes to the project, substantial change in circumstances, or new information that could not have been known at the time of certification. Cal. Pub. Res. Code § 21166; Cal. Code Regs. tit. 14, § 15162; *Laurel Heights Improvement Assn. of S.F., Inc. v. Regents of Univ. of Cal.*, 864 P.2d 502, 507–08 (Cal. 1993). Respondent has not shown that any of those circumstances would apply here.

Petitioner's development assumptions contemplate only minor lot-line adjustments, not a materially different project. The passage of time, standing alone, does not require a new EIR. *Comm. For*

[*71] *Re-Evaluation of T-Line Loop v. S.F. Mun. Transp. Agency*, 211 Cal. Rptr. 3d 902, 917 (Ct. App. 2016). Nor do subsequent changes in local regulations override the vesting protections applicable to the VTTM. *See Concerned Dublin Citizens v. City of Dublin*, 154 Cal. Rptr. 3d 682, 698 (Ct. App. 2013) (holding that new threshold requirements for greenhouse gases were not new information requiring a supplemental environmental impact report because the potential environmental impacts of greenhouse gases were known as of the date the final environmental impact report was certified).

To the extent LA County required additional environmental documentation, the county could prepare an addendum rather than a new EIR. Cal. Code Regs. tit. 14, § 15164(a). An addendum is not circulated for public review and therefore would not create the same delay as a new report. *Id.* subdiv. (c). We therefore do not assume that a new EIR would be required.

Dr. Cooper also raised concerns regarding oak tree permitting. The record does not establish that the oak tree issues would delay recordation of the final map beyond the one-year civil approval period described above. In any event, to the extent additional oak tree permitting work were required, that work could proceed in parallel with the civil engineering revision process. We therefore conclude that the permitting and final-map recordation process would take one year.

We next consider the construction period. Respondent assumed nine months, where petitioner's assumptions ranged from one year to three years. We find one year a reasonable construction period for the 22-lot northern subdivision. It is modestly longer than respondent's estimate, which is appropriate given the topography and grading required for the northern portion lots. It is also materially shorter than the three-year construction period assumed for the full 56-lot subdivision.

We therefore assume a development timeline of two years: one year for permitting and final-map recordation, followed by one year of construction. We further assume, consistent with the experts' models, that the first lot sales occur upon completion of construction and recordation.[38] Accordingly, the lots sold during the pre-sale period

[38] Mr. Williams opined that sales will start after the construction plans are approved but before construction has started or finished. Because petitioner primarily advances Mr. Erickson's income approach, we will disregard Mr. Williams's timeline.

[*72] would close at the end of the two-year development period, in December 2016.

vi. *Appreciation and Cost Inflation*

The revenue and expense figures discussed above are stated in 2014 dollars. Under our adopted timeline, development and sales will span just over four years—two years for permitting and construction and approximately two additional years to sell the inventory. Over that four-year period, lot prices and development costs will change. We therefore must account for appreciation in lot values and inflation in construction costs.

For lot appreciation, petitioner and respondent diverge significantly on the appropriate rate of appreciation.[39] Petitioner's expert Mr. Williams relied on variable appreciation rates derived by Mr. Hewlett, which are based on historical LA County home price data and on projected forecasts in the local market:

Year	*2015*	*2016*	*2017*	*2018*
Projected Growth	7.7%	6.4%	4.8%	0.5%

Respondent's expert Mr. DuVall, by contrast, applied a flat 3% annual appreciation rate based on a national investor survey and long-term inflation data.

We adopt Mr. Hewlett's variable appreciation rates. Appreciation of high-end residential lots in LA County is driven primarily by local market conditions, not by national inflation measures. Mr. Hewlett's approach is grounded in local price data and contemporaneous market forecasts. Mr. DuVall's flat 3% rate is not.

Moreover, Mr. DuVall's rate is inconsistent with his own market analysis. In adjusting comparable sales that occurred shortly before the valuation date, he applied substantially higher appreciation adjustments—for example, approximately 20% for a sale occurring 1.5 years before the valuation date and approximately 10% for a sale occurring one year before. He offers no persuasive explanation for why appreciation would abruptly decline to 3% annually after the valuation

[39] Mr. Erickson did not consider appreciation of the lots in his analysis.

[*73] date despite upward market trends. We therefore reject his flat 3% appreciation rate.

With respect to construction cost, only Mr. DuVall modeled cost inflation during the development period. He assumed that direct construction cost would increase by 2% annually. That assumption is modest and consistent with contemporaneous cost trends. We adopt a 2% annual inflation rate for construction costs.

For purposes of the income approach, we apply Mr. Hewlett's variable appreciation rates to projected lot sales and a 2% annual inflation rate to construction costs.

vii. *Discount Rate*

The discount rate converts projected future cashflows to present value and reflects both the time value of money and the risk inherent in the project. *See Trout Ranch*, T.C. Memo. 2010-283, slip op. at 21. The experts generally agree that a discount rate near 20% is consistent with market data for comparable development projects. The dispute concerns treatment of entrepreneurial incentive. Petitioner models entrepreneurial incentive as a separate expense and applies a lower discount rate. Respondent incorporates entrepreneurial incentive into a single discount rate.

We adopt respondent's approach. The market reports relied upon by the experts apply a unified discount rate reflecting total required return. None of those sources divide entrepreneurial incentive into a separate line item while simultaneously reducing the discount rate. Using these sources as petitioner has understates the effective rate and inflates present value. The distortion is illustrated simply. Discounting $100 receivable two years in the future to present value at 20% yields a present value of approximately $69. If the return is divided into separate components and the cashflow is discounted at only 10% with a 10% line-item expense, the present value increases to approximately $74—equivalent to applying an effective discount rate of roughly 16% rather than 20% as set forth by petitioner's expert. The divergence widens as the projection period lengthens. Modeling entrepreneurial incentive separately as an item of expense therefore reduces the effective discount rate and overstates value. *See Glade Creek Partners*, T.C. Memo. 2020-148, at *50 (rejecting a line-item expense for developer profit and increasing the discount rate to account for this elimination).

[*74] A 20% discount rate is also appropriate in the light of the risks identified above. The project involves a multiyear entitlement and construction period, exposure to market absorption risk, substantial upfront capital investment, and uncertainty regarding time of approvals. These factors justify a market-level required return at the upper end of the range supported by the developer surveys in the record.

We therefore apply a single 20% discount rate and do not include a separate line item for entrepreneurial incentive.

viii. *Conclusion as to Value*

After careful consideration of the record, including the expert testimony and supporting documentation, we conclude that the fair market value of the northern portion shall be determined under the income approach using the variables and assumptions set forth above and subject to computations under Rule 155.

In reaching this conclusion, we adopted the following variables. A reconciled per-lot value of $1,779,920 as of 2014. This price should be increased annually by the appreciation values in Mr. Hewlett's report. The sale of 15 lots at the conclusion of the two-year development period, with the remaining lots absorbed at six lots per year thereafter.

On the expense side of the ledger, we adopted Mr. Cunningham's direct development costs of $305,745 per lot, increased 2% annually for construction-cost inflation. As for indirect costs, we adopt the following costs:

[*75]

Category	*Expense Per Lot*
Direct Costs	$305,745
Sales and Marketing	5% of sales
Property Taxes	To be calculated assuming no reassessment on donation date as discussed above.
Insurance	$4,732
Supervision	$4,464
Construction Financing	8% annual interest with a 1.5% loan origin fee
Entrepreneurial Incentive	None

We assume the indirect costs are evenly divided over the two years for permitting and construction with the exception of sales and marketing and property taxes that will continue until all lots are sold. The net income from each year will be discounted to the donation date with a 20% discount rate, inclusive of entrepreneurial incentive.

This valuation reflects the risk inherent in the entitlement and development process, the absorption characteristics of the local luxury-lot market, and the time required to complete and sell the subdivision. It also reflects our rejection of unsupported assumptions regarding reassessment, permitting delays, and discount-rate modeling. We leave the exact calculation of the value to the parties in accordance with the findings and conclusions of the Court under Rule 155. It is sufficient for our remaining analysis to estimate the value of the northern portion as approximately $20.4 million. *See Green Valley Invs., LLC v. Commissioner*, T.C. Memo. 2025-15, at *33 n.19 (using an estimated value to determine the applicability of gross valuation misstatement and substantial valuation misstatement penalties).

4. *Southern Portion*

The southern portion lies south of the coastal zone boundary, as highlighted below on the VTTM:

[*76]



a. *Highest and Best Use*

Petitioner contends that the highest and best use of the southern portion was development of 34 lots in accordance with the VTTM. Respondent argues that no development was reasonably probable and that the highest and best use was to hold the land as open space for the benefit of neighboring property owners. Resolution of this dispute turns primarily on the application of the regulatory regime governing development in the coastal zone as of October 10, 2014, when the Coastal Commission certified the 2014 LCP.

Following certification of the 2014 LCP, development within the coastal zone required a coastal development permit consistent with both the 2014 LCP and the Coastal Act. Cal. Pub. Res. Code § 30604(a). Although authority was delegated to LA County, the Coastal Commission retained appellate jurisdiction.[40] On appeal, the Coastal

[40] The appellate structure varies depending on whether the local government has a certified local coastal program in effect. If there is no certified local coastal program, any local government action with respect to a coastal development permit may be appealed to the Coastal Commission. Cal. Pub. Res. Code § 30602. If a certified local coastal program is in effect, the issuance of a coastal development permit is appealable if the permit relates to a development within 100 feet of any stream or if the approved development is not designated as the principal permitted use under zoning ordinances. *Id.* § 30603(a)(2), (4). Whichever standard applies, LA County's issuance of a coastal development permit to MVL would be appealable to the Coastal Commission. Both Josh Huntington, an LA County Department of Regional Planning employee, and Mr. Gutierrez confirmed that the Coastal Commission would have appellate jurisdiction over a coastal development permit issued for the subject property.

Even to the extent that LA County's decision regarding the coastal development permit was not appealable to the Coastal Commission, aggrieved parties

[*77] Commission reviews coastal development permit decisions de novo and must determine whether the proposed development conforms to the certified 2014 LCP and the Coastal Act. *Redondo Beach Waterfront, LLC v. City of Redondo Beach*, 265 Cal. Rptr. 3d 556, 564, 569 (Ct. App. 2020). It would not be bound by LA County's prior determination. *Id.* The Coastal Commission has final interpretive authority over the 2014 LCP. *Charles A. Pratt Constr. Co.*, 76 Cal. Rptr. 3d at 473.

Accordingly, even if LA County were the initial coastal development permit decisionmaker and approved the coastal development permit under the 1986 Malibu LCP LUP, any approval would remain subject to multiple avenues for appellate review under the 2014 LCP. The certified 2014 LCP imposed substantial constraints. As relevant here, each newly created lot within the coastal zone requires a transfer development credit. One transfer development credit generally requires retirement of approximately 20 acres of qualifying coastal land. Moreover, structures must observe 50-foot horizontal and vertical setbacks from significant ridgelines, development is prohibited within 100 feet of designated H1 habitat areas, and grading on steep slopes is significantly restricted. LA County, Cal., Code §§ 22.44.2040(B)(3), 22.44.1900(A), 22.44.1260(J).

The experts agreed that development of 34 coastal zone lots in accordance with the VTTM would not comply with the 2014 LCP. A 34-lot subdivision would require 33 transfer development credits necessitating retirement of approximately 660 acres of qualifying coastal land. The record does not establish that such credits were available or reasonably obtainable. In addition, several proposed building pads appear to encroach upon ridgeline setbacks and habitat buffer areas, and the VTTM contemplated substantial grading in areas subject to slope limitations. Given these requirements, petitioner has not shown that development of the southern portion in accordance with the 34-lot VTTM configuration was reasonably probable under the 2014 LCP.

Petitioner argues that the VTTM conferred vesting rights insulating the project from application of the 2014 LCP. California law does not support this interpretation. A certified local coastal program is "not solely a matter of local law, but embod[ies] state policy." *See Pac.*

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would not be without recourse. In that case, LA County's decision could be appealable in court. *Id.* § 30803.

[*78] *Palisades Bowl Mobile Estates*, 288 P.3d at 721 (quoting *Charles A. Pratt Constr. Co.*, 76 Cal. Rptr. 3d at 471). Therefore, the VTTM did not "lock in" application of the 1981 Malibu LUP LCP. *See* Cal. Gov't Code § 66498.6(b). California caselaw confirms that the Coastal Commission may apply a later-certified local coastal program in its appellate review of a coastal development permit. *See Charles A. Pratt Constr. Co.*, 76 Cal. Rptr. 3d at 471–72.[41] In fact, the Coastal Commission is statutorily obligated to review coastal development permits for compliance with the Coastal Act and certified local coastal programs when exercising appellate jurisdiction. Cal. Pub. Res. Code § 30603(b)(1). Petitioner therefore has not established that vesting would have insulated the southern portion from application of the 2014 LCP, especially on appellate review by the Coastal Commission.

Petitioner relies on (1) the final EIR, (2) the 2004 coastal development permit waivers for water and sewer lines, and (3) the 2022 action by the LA County Board of Supervisors to show that the Coastal Commission approved development in the coastal zone. The final EIR reflects LA County's conclusion that the VTTM complied with then-applicable coastal policies. The Coastal Commission submitted detailed comments on the draft EIR raising concerns regarding development density, cumulative impacts, grading, habitat encroachment, vegetation removal, and visual impacts. Although LA County responded to those comments, the record does not establish that the Coastal Commission formally endorsed those responses. In any event, determinations made in 1988 do not bind the Coastal Commission when applying subsequently certified coastal regulations. *Redondo Beach Waterfront*, 265 Cal. Rptr. 3d at 564, 569.

The 2004 coastal development permit waivers concerned limited utility improvements within an existing right-of-way and were granted on representations that the work would not involve grading, habitat impacts, or public access concerns. The waivers also expressly found that the improvements were to service development outside of the coastal zone. Those waivers do not establish that a 34-lot coastal subdivision would have been approved under the 2014 LCP. Finally,

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[41] To the extent *Redondo Beach Waterfront*, 265 Cal. Rptr. 3d at 568–69, could be read to suggest to the contrary, that decision focused on whether a *local jurisdiction*—not the Coastal Commission—was bound to the local implementation plan in effect when the application became complete. Even assuming LA County was bound to apply earlier local provision in its initial review, any coastal development permit approval would remain subject to appeal and de novo review by the Coastal Commission under the 2014 LCP.

[*79] petitioner cites a 2022 Board of Supervisors action stating that the 2014 LCP did not apply to the VTTM. That action occurred eight years after the valuation date and does not control our analysis of reasonable probability as of 2014. *See Estate of Spruill v. Commissioner*, 88 T.C. 1197, 1233 (1987) ("[S]ubsequent events are generally not relevant in fixing a property's fair market value on a given date . . . ."). Moreover, LA County's position cannot bind the Coastal Commission in the exercise of its appellate jurisdiction. *Redondo Beach Waterfront*, 265 Cal. Rptr. 3d at 564, 569. None of the evidence in the record establishes that issuance of a coastal development permit for the 34-lot VTTM configuration was reasonably probable as of the valuation date.

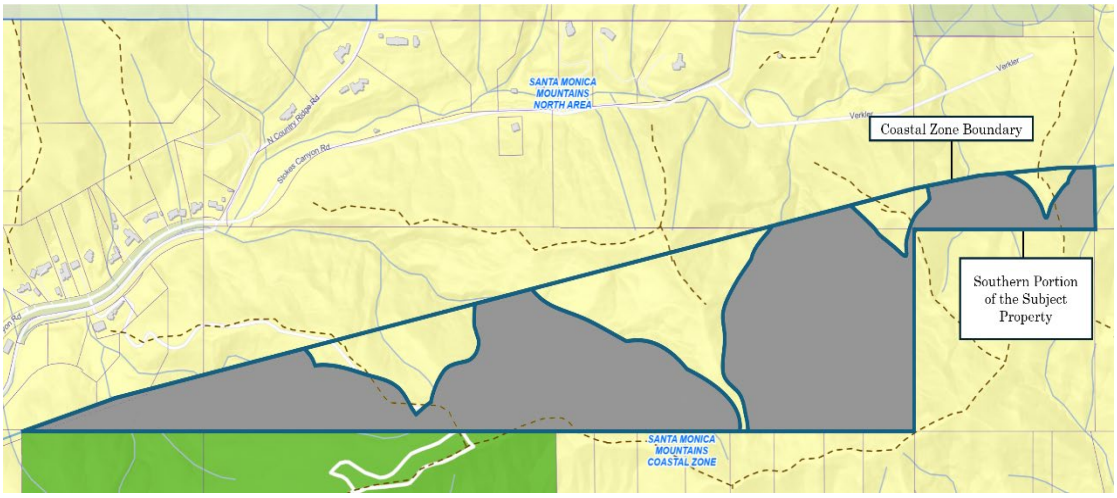
Even if the 1986 Malibu LCP LUP applied, petitioner has not shown that development of 34 coastal zone lots would have been financially feasible. In 1987 the Coastal Commission indicated its intent to apply the financially prohibitive transfer development credit to development on the VTTM when Malibu Valley Farm, Inc., sought to move the coastal zone boundary. A 34-lot coastal zone subdivision would therefore have required acquisition and retirement of substantial acreage. Petitioner has not demonstrated that this obligation would have been economically feasible. Accordingly, even under the earlier regulatory regime, development of the southern portion in accordance with the 34-lot VTTM configuration was not shown to be financially feasible.

Development of the southern portion as a 34-lot subdivision under the VTTM in the coastal zone was not reasonably probable and likely to occur within a reasonable time as of the valuation date. The 2014 LCP imposes substantial constraints, including transfer development credit requirements, ridgeline setbacks, habitat buffers, and grading limitations. These restrictions materially limit the buildable area and introduce significant regulatory uncertainty, particularly in the light of the Coastal Commission's appellate authority.

At the same time, respondent's proposed highest and best use—holding the land solely as passive open space—fails to account for the property's residual zoning density and remaining, though constrained, development potential. The record establishes that the southern portion retained some possibility of limited coastal development, even if the scope and timing of such development were uncertain. As of the valuation date, the property was zoned for one single-family residence per 20 acres. On approximately 124.35 acres, that zoning would

[*80] theoretically permit up to six lots. The practical number would likely be lower.

Each new lot would require a transfer development credit, and substantial portions of the property are constrained by ridgeline setbacks, H1 habitat buffers, and slope limitations. These restrictions materially reduce the buildable area and increase entitlement uncertainty. The H1 habitats and quiet zones are shaded below and the significant ridgelines are highlighted with dotted lines:



The record reflects that market participants may assign value to property subject to regulatory uncertainty. Uncertainty does not eliminate value, though it materially diminishes it. Respondent's assumption of no possible future development is not maximally productive.

Accordingly, the presumption that a property's existing use reflects its highest and best use controls. *Mountanos*, T.C. Memo. 2013-138, at *7. As of the valuation date, the southern portion was held as an investment with limited and uncertain coastal development potential. That use constitutes its highest and best use.

b. *Market Approach*

We turn to determining the value of the southern portion under the market approach. The market approach estimates value by comparing the subject property to similar properties sold in arm's-length transactions near the valuation date. *Savannah Shoals*, T.C. Memo. 2024-35, at *36. When sufficient data exists, this method generally provides the most reliable indication of fair market value. *See*

[*81] *Whitehouse Hotel Ltd. P'ship*, 139 T.C. at 324–25 (holding that other valuation methods are "not favored if comparable-sales data are available"). We consider the comparable tract sales identified by the experts and rely primarily on those identified by Mr. DuVall, because they most closely resemble the southern portion in size, entitlement posture, and regulatory setting.[42]

- Comparable 1 (July 2014): 703-acre tract of land approximately 8 miles southwest of the subject property within the coastal zone; sold for $12 million ($17,070 per acre) to a conservation group. It was subdivided into 24 legal lots supported by certificates of compliance permitting sale. The tract was ocean facing and had electricity available at the property boundary.

- Comparable 2 (April 2014): 416-acre tract of land approximately 15 miles southwest of the subject property in the coastal zone; sold for $5.3 million ($12,740 per acre) to a conservation organization. Mr. DuVall determined that low-density zoning would result in a maximum of six lots (one residence per 30 acres). Utilities were several miles away. The property had not been subdivided into legal lots.

- Comparable 3 (September 2014): 60-acre rugged tract; sold for $450,000, or $7,500 per acre. The property is 0.25 miles north of the subject property. Access was via an adjoining easement. Zoning permitted one single-family residence per 40 acres. The tract included a 1.5-acre building pad and the remains of a residence that had burned down.

- Comparable 4 (August 2014): 39.61-acre steep hillside tract; sold for $125,000 ($3,156 per acre). Zoning permitted one dwelling per 20 acres, although the topography significantly limited development feasibility.

Because the record does not support quantitative adjustments, we conduct a qualitative analysis consistent with the parties' approach at trial.[43] The southern portion contains approximately 124.35 acres. Its highest and best use is as an investment with limited and uncertain low-density development potential. Zoning permits one single-family

[42] We have renumbered the comparable tracts continuously for added clarity in our analysis.

[43] We will not apply Mr. Hewlett's timing adjustment to these tracts of land because his appreciation rates were derived from smaller lot sales.

[*82] residence per 20 acres, suggesting a theoretical maximum of six lots. In practice, development would likely yield fewer lots because of the need for the costly transfer development credits and grading and other restrictions imposed by the 2014 LCP.

Mr. Erickson and Mr. Williams valued the property on a per-acre and per-lot basis. Mr. DuVall relied solely on a per-acre analysis. We reject any per-lot methodology. The number of potential lots was uncertain as of the valuation date, particularly in the light of the recently certified 2014 LCP. Indeed, when faced with similar uncertainty in analyzing comparable sales, petitioner's experts declined to rely on per-lot pricing. We agree that a per-acre analysis is more reliable and better reflects the market's pricing of similarly constrained tracts. We address the comparables in descending order of superiority.

The sale of Comparable 1 is superior to the sale of the southern portion. Although both properties were within the coastal zone, Comparable 1 had already been subdivided into 24 legal lots. A purchaser therefore would not have needed transfer development credits and could have immediately marketed individual lots. It also possessed superior ocean views. These advantages outweigh the downward pressure on price attributable to its large size and earlier sale date. We conclude the southern portion would sell for less than $17,070 per acre and treat that figure as an upper boundary rather than a direct indicator of value.

The sale of Comparable 2 is broadly similar. Like the southern portion, the lot had not been subdivided and would have required transfer development credits to create legal lots. Its zoning permitted up to six lots, subject to practical reductions from coastal restrictions. It benefited from ocean views, but its lower density (one residence per 30 acres), earlier sale date, and larger size offset that advantage. We view $12,740 per acre as a reasonable upper indicator, though somewhat overstated relative to the southern portion given its superior views and development posture.

Comparable 3 is geographically the closest sale and therefore particularly useful in capturing localized market forces. It has more limited zoning density (one dwelling per 40 acres), but it included a level 1.5-acre building pad, making development more feasible and reducing grading constraints. The southern portion would require substantial grading and compliance with restrictive 2014 LCP requirements to create pads. Comparable 3 is also smaller, which tends to increase

[*83] per-acre pricing due to reverse economies of scale, and its sale occurred three months before the valuation date. On balance, these characteristics largely offset one another. We treat $7,500 per acre as a reasonable lower indicator, though likely somewhat conservative given the southern portion's greater theoretical density.

The sale of Comparable 4 is inferior. The lot's steep topography substantially impaired development potential, rendering it less valuable than the southern portion. We therefore would expect the southern portion to sell for more than $3,156 per acre and treat that figure as a floor rather than a meaningful valuation benchmark.

The sales of Comparable 2 and Comparable 3 provide the most probative benchmarks. The sale of Comparable 2 captures the incremental value attributable to limited multilot development potential. The sale of Comparable 3 captures the hyperlocal market conditions and the value of constrained development in the immediate vicinity. We do not mechanically average sales; rather, we weigh the evidence. The sale of Comparable 2 likely overstates value because of its superior views and relatively stronger development profile. The sale of Comparable 3 likely understates value because of its lower density allowance, though its proximity enhances its probative value. The midpoint between these indicators best reflects the southern portion's constrained yet meaningful development potential while accounting for regulatory uncertainty.

Averaging $12,740 and $7,500 yields $10,120 per acre. We find that figure to be supported by the preponderance of the evidence and consistent with the qualitative comparisons discussed above. Applying that figure to the 124.35 acres results in a value of $1,258,422 for the southern portion.

c. *Income Approach*

As discussed *supra*, the income approach estimates value by discounting projected future cashflows to present value. *See Chapman Glen Ltd.*, 140 T.C. at 327; *Marine*, 92 T.C. at 983; *Champions Retreat Golf Founders*, T.C. Memo. 2022-106, at *21. The reliability of that method depends on the plausibility of the underlying assumptions. *See Ranch Springs*, 164 T.C. at 151; *Kiva Dunes Conservation*, T.C. Memo. 2009-145, slip op. at 10–11. The income approach does not provide a reliable indicator of the fair market value of the southern portion.

[*84] As we explained in our highest and best use analysis, development in accordance with the VTTM is not reasonably probable with respect to the southern portion. Unlike the northern portion, which could support 22 lots, the southern portion could theoretically support no more than six lots under existing zoning. In practice, the number would likely be fewer because subdivision would require transfer development credits and compliance with grading and other restrictions imposed by the 2014 LCP.

The parties did not provide credible, record-based estimates of the costs required to obtain transfer development credits, secure coastal approvals, construct infrastructure, or create compliant building pads. Any income approach would therefore require substantial assumptions regarding yield, timing of approvals, absorption costs, and discount rates. Those assumptions would be speculative on this record. We therefore decline to rely on the income approach in valuing the southern portion.

5. *Putting It All Together for the Before Value*

As set forth *supra*, the most reliable method to price the subject property is as a sum of its parts. We determined the value of the southern portion under the market approach to be $1,258,422. We determined that the income approach provides the most reliable indication of value for the northern portion. The precise amount shall be computed by the parties under Rule 155 consistent with our findings and conclusion. The sum of (1) the Rule 155 value of the northern portion and (2) $1,258,422 for the southern portion constitutes the fair market value of the subject property before the easement grant.

B. *After Value of the Subject Property and Valuation Conclusions*

Respondent argues that the fair market value of the subject property after the conservation easement grant was $2 million. That amount is lower than the after values opined by petitioner's experts. Respondent has not argued for a higher after value. We therefore treat $2 million as conceded and find that to be the fair market value of the subject property after the easement grant. *See Seabrook Prop.*, T.C. Memo. 2025-6, at *76.

The value of the easement equals the difference between the before value and the after value. The parties shall compute the before value under Rule 155 consistent with this Opinion and subtract

[*85] $2 million to determine the value of the easement. By our estimate, the easement is worth approximately $19.7 million.

IV. *Interest Expense*

For 2014 MVL reported a $450,000 deduction for interest paid on indebtedness secured by the subject property. The indebtedness arose from the Levin notes assumed by MVL, which it later satisfied, including accrued interest.

A. *Statutory Framework*

Section 163(a) allows a deduction for interest paid or accrued within the taxable year on indebtedness. For noncorporate taxpayers, however, section 163(h)(1) disallows a deduction for personal interest. Personal interest does not include interest properly allocable to a trade or business or to investment property. § 163(h)(2). Investment interest is deductible only to the extent of the taxpayer's net investment income. § 163(d)(1). Investment interest means any interest paid or accrued on indebtedness properly allocable to property held for investment. § 163(d)(3)(A). Property is held for investment if it produces gain or loss not derived in the ordinary course of a trade or business. §§ 163(d)(5)(A), 469(e)(1). The amount of investment interest that exceeds the taxpayer's investment income is carried forward. § 163(d)(2). Thus, the deductibility of interest depends on whether MVL held the subject property in a trade or business or for investment.

B. *TEFRA Jurisdiction*

Respondent argues that section 163(d) requires disallowance at the partnership level because MVL had no investment income. That argument misconstrues the TEFRA framework. Under TEFRA, partnership tax matters are resolved in two stages: (1) a partnership-level proceeding to determine partnership items and (2) a partner-level proceeding to determine affected items and compute the partners' tax liabilities. §§ 6221, 6226(f), 6231(a)(3).

In a partnership-level proceeding, our jurisdiction is limited to readjusting partnership items, the proper allocation of those items among the partners, and the applicability of penalties relating to partnership items. § 6226(f). Treasury regulations provide that partnership items include the partnership's aggregate and each partner's share of items of income, gain, loss, deduction, or credit and

[*86] characterization of those items. *See* Treas. Reg. § 301.6231(a)(3)-1(a)(1)(i). Whether the interest expense is properly characterized as trade-or-business interest or investment interest depends on the character of the property in the hands of the partnership. *See Miller v. Commissioner*, 70 T.C. 448, 453–58 (1978) (characterizing interest as investment interest by considering the partnership's relationship to the expense); *cf. Terry v. Commissioner*, T.C. Memo. 1984-442 (finding that the characterization of loss as ordinary or capital is a partnership item). That determination is therefore a partnership item.

By contrast, the application of the section 163(d) limitation—including whether a particular partner has sufficient net investment income—is a partner-level affected item determination. *See* § 702(a)(7) (requiring a partner to separately account for "other items of . . . deduction . . . to the extent provided by regulations prescribed by the Secretary"); Treas. Reg. § 1.702-1(a)(8)(iii) ("Each partner shall aggregate the amount of his separate deductions or exclusions and his distributive share of partnership deductions or exclusions separately stated in determining the amount allowable to him of any deduction or exclusion under subtitle A of the Code as to which a limitation is imposed."); Rev. Rul. 84-131, 1984-2 C.B. 37 (explaining that limitation prescribed by section 163(d)(1) applies at the partner level).[44] Accordingly, we decide only whether the interest is investment interest or trade-or-business interest. Any limitation under section 163(d) will be applied, if necessary, at the partner level.

C. *Trade or Business vs. Investment*

Whether property is held for sale to customers in the ordinary course of a trade or business is a factual determination. *See Polakis v. Commissioner*, 91 T.C. 660, 669–70 (1988). In cases involving undeveloped real property, courts consider the following factors: (1) the purpose for which the property was held, (2) the duration of ownership, (3) the continuity and frequency of sales, (4) the extent of development and improvement activities, (5) advertising and sales efforts, and (6) the relationship of real estate sales to the taxpayer's other income-producing activities. *Id.* at 670. No single factor controls.

[44] Although respondent's informal guidance is not binding on this Court, we will not permit respondent to argue contrary to his published guidance. *See Rauenhorst v. Commissioner*, 119 T.C. 157, 171–73 (2002); *Walker v. Commissioner*, 101 T.C. 537, 550–51 (1993).

[*87] The record establishes that MVL did not hold the subject property in the ordinary course of a trade or business. MVL acquired the property after nearly two decades of unsuccessful development efforts by Brian and his father. The transfer to MVL occurred in connection with the easement transaction, not as part of an ongoing real estate development enterprise. MVL did not market the property for sale. It undertook no advertising or solicitation efforts. It engaged in no sales activity. It did not subdivide, improve, or otherwise develop the property for sale to customers. Petitioner does not contend that MVL operated a real estate development business with respect to the property, and the record contains no evidence of such activity. These facts weigh decisively against dealer treatment. *See Cardulla v. Commissioner*, T.C. Memo. 2023-89, at *25–27 (determining that interest paid by a partnership on debt secured by property was investment interest where the partnership obtained the property when the investors "lost faith in its potential" and did not undertake any sale or development activities), *aff'd*, No. 24-31, 2025 WL 1984265 (9th Cir. July 17, 2025); *Conner v. Commissioner*, T.C. Memo. 2018-6, at *26–31 (determining that interest paid by various entities on debt secured by property was investment interest when only preliminary development steps were taken and no sales activities occurred), *aff'd*, 770 F. App'x 1016 (11th Cir. 2019).

Petitioner suggests that respondent advances a "novel" statutory interpretation. The argument is unpersuasive. The inquiry under section 163(d) into whether property is held for investment substantially overlaps with the inquiry under section 1221(a)(1) into whether property is held for sale to customers in the ordinary course of a trade or business. Courts have long applied the same factual framework in both contexts because the characterization of the property controls the result. *See, e.g.*, *Glade Creek Partners*, T.C. Memo. 2023-82, at *23.

D. *Conclusion*

We conclude that MVL held the subject property for investment. Accordingly, the $450,000 interest expense constitutes investment interest. The deductibility of that interest is subject to the limitations of section 163(d), which shall be applied at the partner level.

V. *Penalties*

Respondent determined an accuracy-related penalty for a gross valuation misstatement under section 6662(a), (b)(3), and (h) with respect to MVL's charitable contribution deduction. In the alternative,

[*88] respondent determined an accuracy-related penalty on the grounds of a substantial valuation misstatement under section 6662(a), (b)(3), and (e); a substantial understatement of income tax under section 6662(a), (b)(2), and (d); or negligence under section 6662(a) and (b)(1).[45]

Under TEFRA, the applicability of penalties relating to an adjustment to partnership items is determined at the partnership level. *See* §§ 6221, 6226(f); *Dynamo Holdings Ltd. P'ship v. Commissioner*, 150 T.C. 224, 233 (2018). The section 7491(c) burden of production rule does not apply in a TEFRA partnership-level proceeding because the Court does not determine an individual partner's liability. *Dynamo*, 150 T.C. at 236–37. Accordingly, respondent does not bear a burden of production with respect to penalties. The partnership bears the burden of proving any defenses to penalties, including reasonable cause and good faith.[46]

A. *Accuracy-Related Penalties*

Section 6662(a) imposes a 20% penalty on any portion of an underpayment attributable to specified grounds, including negligence or disregard of rules and regulations, a substantial understatement of income tax, and a substantial valuation misstatement. § 6662(b)(1)–(3). Negligence includes any failure to make a reasonable attempt to comply with the Code or exercise ordinary and reasonable care in the preparation of a tax return. Treas. Reg. § 1.6662-3(b)(1).

A misstatement is "substantial" if the value of the property claimed on a return equals or exceeds 150% of the correct amount. § 6662(e)(1)(A). The penalty increases to 40% in the case of a "gross valuation misstatement," which occurs when the claimed value equals or exceeds 200% of the correct value. An understatement of income tax is substantial if it exceeds the greater of 10% of the tax required to be shown on the return or $5,000. § 6662(d).

MVL reported the conservation easement contribution at $32,075,000. Therefore, to the extent that the easement is valued at $16,037,500 or less, MVL partners will be liable for gross valuation

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[45] Respondent did not meaningfully develop on brief whether accuracy-related penalties related to other adjustments in the FPAA, and therefore we deem this issue conceded. *See Thiessen*, 146 T.C. at 106; *see also* Rule 151(e)(4) and (5).

[46] We need not determine whether any of the asserted penalties were timely approved under section 6751(b)(1) because we determine that gross valuation misstatement penalties do not apply and that to the extent any other accuracy-related penalty applies, MVL had reasonable cause.

[*89] misstatement penalties. The precise penalty applicable depends on the value of the easement as ultimately computed under Rule 155. *Clay v. Commissioner*, 152 T.C. 223, 246 (2019) (conditioning the application of substantial understatement of income tax accuracy-related penalties on the results of the parties' Rule 155 computations), *aff'd*, 990 F.3d 1296 (11th Cir. 2021); *Bergquist v. Commissioner*, 131 T.C. 8, 24, 25 (2008) (conditioning the application of substantial valuation misstatement accuracy-related penalties on the results of the parties' Rule 155 computations). However, even our preliminary approximations of the easement's value demonstrate a value of approximately $19.7 million. This is far in excess of the approximately $16 million value that would trigger gross valuation misstatement penalties. Therefore, gross valuation misstatement penalties do not apply.[47] Because we find that MVL had reasonable cause for the underpayment, we need not consider whether the alternative penalties apply.

B. *Reasonable Cause and Good Faith*

Section 6664(c)(1) provides that no accuracy-related penalty applies to any portion of an underpayment for which the taxpayer shows reasonable cause and good faith. *See Higbee*, 116 T.C. at 448. Reasonable cause is determined case by case, considering all pertinent facts and circumstances. Treas. Reg. § 1.6664-4(b)(1). The inquiry focuses on whether the taxpayer exercised ordinary business care and prudence at the time the return was filed. *See Neonatology Assocs., P.A. v. Commissioner*, 115 T.C. 43, 98 (2000), *aff'd*, 299 F.3d 221 (3d Cir. 2002).

Reliance on professional advice may establish reasonable cause where the taxpayer proves: (1) the adviser was a competent professional with sufficient expertise, (2) the taxpayer provided necessary and accurate information, and (3) the taxpayer actually relied in good faith on the adviser's judgment. *Neonatology Assocs., P.A.*, 115 T.C. at 99; *Higbee*, 116 T.C. at 446–47 (holding that, in a situation such as here, the taxpayer bears the burden of proof with regard to issues of reasonable cause); *see also* Treas. Reg. § 1.6664-4(c)(1) (providing additional rules for establishing reliance on the advice of others).

[47] We have previously found it adequate to determine the applicability of gross valuation misstatement penalties based on an estimated value. *See Green Valley Invs.*, T.C. Memo. 2025-15, at *33 n.19.

[*90] Section 6664(c)(3) imposes additional requirements for valuation misstatement penalties. The defense applies only if the valuation was based on a qualified appraisal by a qualified appraiser and the taxpayer made a good-faith investigation of value. The reasonable cause defense does not apply to gross valuation misstatement penalties. § 6664(c)(3).

Respondent does not dispute that MVL obtained a qualified appraisal prepared by a qualified appraiser, Mr. Erickson. The dispute concerns whether MVL conducted a good-faith investigation of value. The record demonstrates that MVL made a good-faith investigation of the value of the contributed property.

MVL retained Mr. Erickson, a certified appraiser with decades of professional experience. He was provided access to relevant documents and information concerning the property. After completion of the appraisal, MVL's partners reviewed and relied upon it in reporting the charitable contribution deduction. In preparing the appraisal, Mr. Erickson relied extensively on information provided by Brian and Ms. Palmer concerning the VTTM and the property's development history. That reliance was reasonable. The interaction between vested subdivision rights and evolving coastal development regulations presents unusually complex land-use questions. Brian had more than 20 years of direct involvement with the VTTM, and Ms. Palmer had professional experience addressing its regulatory implications. Even witnesses that worked for LA County demonstrated uncertainty regarding how these legal regimes interacted.

Although we ultimately reach different conclusions regarding development potential, disagreement with an appraisal does not establish a lack of good faith. The imposition of penalties does not turn on whether the appraisal ultimately proved correct. The relevant inquiry is whether at the time the return was filed MVL reasonably relied on professional advice that was based on information then available. A valuation later rejected by the Court does not, by itself, establish lack of reasonable cause. *See Murfam Enters. LLC v. Commissioner*, T.C. Memo. 2023-73, at *17–18 (rejecting the valuation set forth by the taxpayer but determining that reasonable cause existed because the taxpayer acted in good faith with respect to its valuation and reporting of the easement donation).

Respondent argues that the appraisal merely adopted MVL's preferred conclusions and conflicted with the prior sale of a 75% partnership interest to Mr. Hankey. As explained *supra*, that

[*91] transaction was not an arm's-length indicator of fair market value and does not undermine MVL's reliance on the appraisal. While this sale is not a reliable indicator of the value of the property, the record contains several other indicators that demonstrate a higher value for the subject property. Brian fought to retain ownership of the VTTM with efforts that would make John Dutton in *Yellowstone* look yielding. Year after year Brian fought to keep the property. He did not do this for sentimental attachment purposes. Instead, he saw the value of the VTTM. Importantly, throughout this entire time, people were lining up to give Brian money to finance the VTTM. If anything, the history of the VTTM including the subject property supported a high valuation for the property. MVL made a good-faith investigation of the value of the subject property.

We find that MVL and its partners actually and in good faith relied on Mr. Erickson's appraisal in determining the value reported on the return. Considering the record as a whole, MVL exercised ordinary business care and prudence and conducted a good-faith investigation of value. We therefore find that MVL had reasonable cause and acted in good faith within the meaning of section 6664(c).

CONCLUSION

We conclude that MVL is entitled to a charitable contribution deduction for the donation of the conservation easement. As discussed *supra*, the precise value of the easement shall be determined through Rule 155 computations consistent with this Opinion. The value of the easement equals the fair market value of the subject property before the easement minus the after value of $2 million. A gross valuation misstatement penalty is not applicable and no other accuracy-related penalties are applicable because MVL has demonstrated reasonable cause and good faith.

To reflect the foregoing,

Decision will be entered under Rule 155.