

Publications

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90 Days, 10%: IRS Opens New Easement Settlement Window

Key Takeaways:

- The IRS has opened a limited settlement window for eligible conservation and historic preservation easement disputes, with a reduced 10% gross valuation misstatement penalty available during the first 90 days. The initiative applies only to partnerships that receive individualized settlement letters from the IRS.
- The new program offers substantially more favorable terms than the 40% penalty the IRS has frequently pursued in syndicated easement litigation. Partnerships that miss the initial 90-day window may face a higher 20% penalty and less favorable settlement treatment after 135 days.
- Partnerships, investors and representatives should review any IRS settlement correspondence promptly and evaluate whether participation makes sense under the circumstances.

The IRS has announced a new time-limited settlement opportunity for eligible conservation easement and historic preservation easement disputes. The initiative creates a narrow opportunity for eligible partnerships to resolve long-running easement disputes on significantly more favorable terms before penalties increase and settlement leverage shifts back to the government. For taxpayers who qualify, the key takeaway is simple: the most favorable settlement terms are available for only 90 days, and during that first window, the IRS will apply a reduced 10% gross valuation misstatement penalty.

Key Terms of the IRS Settlement Initiative

Under the new initiative, eligible partnerships will receive individualized settlement letters from the IRS. The 90-day clock starts on the postmark date or electronic transmission date of that letter. During that 90-day period, the partnership may settle on terms that include no charitable contribution deduction for the easement donation, an “other deduction” generally tied to the partnership’s estimated out-of-pocket costs, a 10% gross valuation misstatement penalty and statutory interest.

The 10% penalty is the most important feature of the early settlement window. It is far lower than the 40% gross valuation misstatement penalty the IRS has often pursued, and that courts have frequently sustained, in syndicated easement cases.

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There is also a significant timing consequence. If an eligible partnership does not accept within the first 90 days, there is a second 45-day window, but the penalty increases from 10% to 20%. The IRS has stated that there will be no extensions.

After the full 135-day period expires, the special settlement terms disappear. At that point, the IRS says cases generally will be resolved only based on litigation hazards. In practical terms, the IRS has indicated that this may mean allowing only about 5% to 7% of the claimed deduction and imposing a 40% gross valuation misstatement penalty, plus interest.

Many Eligible Partnerships Can Defer Payment Under the New Process

Another important change is that many partnerships will not have to make an upfront payment when electing into the settlement program. Instead, the liability will be addressed through the IRS's normal post-settlement assessment and collection procedures. This may make the program more workable for partnerships that previously had difficulty coordinating payment among investors.

The settlement opportunity is not available in every easement case. Certain cases are excluded, including cases that have already been tried and are awaiting an opinion, cases on appeal, cases that have already settled, certain test cases and cases with trial scheduled to begin within 30 days of the announcement. Eligibility will be determined by the IRS based on the status and facts of each case.

Partnerships That Delay Could Face Higher Penalties

For investors, partnerships and their representatives, the practical message is this: watch for IRS correspondence and act quickly. The best settlement terms are available only during the first 90 days after the IRS issues the individualized letter. Missing that window could double the penalty from 10% to 20%, and waiting beyond 135 days could expose the case to a much harsher settlement or litigation posture.

Any taxpayer, partnership representative, or investor who receives an IRS settlement letter, partnership notice, or related communication should have it reviewed promptly. The decision whether to participate will depend on the specific settlement terms, the partnership's tax year, the investor's share of the adjustment and whether the case is governed by TEFRA or the BBA partnership audit rules.

Polsinelli's government investigations, tax and business attorneys have extensive experience with conservation easements and are prepared to assist with tax compliance or any potential enforcement action by the government. Should you have questions regarding the information discussed, please reach out to Lauren DeSantis-Then, Bill Sanders or your preferred Polsinelli attorney.