

IRC § 6695A APPRAISER PENALTIES

What does it mean to you?

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WHAT ARE THEY?

(Start from the back)

- **Pension Protection Act of 2006 (PL 109-280), § 1219**
 - Added IRC § 6695A, Appraiser Penalty
 - Redefined terms (lowered thresholds)
 - “Substantial Valuation Misstatement” – IRC §§ 6662(e)(1) & (2)
 - “Substantial Estate and Gift Tax Valuation” IRC § 6662(g)
 - “Gross Valuation Misstatement” – IRC § 6662(h)(2)
 - Eliminated Reasonable Cause Exception for Gross Valuation Misstatements – IRC § 6664(c)(2)
 - Amended IRC § 170(f)(11)(E)
 - Defined “Qualified Appraisal” – IRC § 170(f)(11)(E)(i)
 - Defined “Qualified Appraiser” – IRC §§ 170(f)(11)(E)(ii) & (iii)
- **Small Business Work Opportunity Tax Act of 2007 (PL 110-28)**
- **Tax Technical Corrections Act of 2007 (PL 110-172)**

IRC § 6695A

Appraiser Penalty Defined

SEC. 6695A. SUBSTANTIAL AND GROSS VALUATION MISSTATEMENTS ATTRIBUTABLE TO INCORRECT APPRAISALS

(a) Imposition of Penalty- If—

(1) a person prepares an appraisal of the value of property and such person knows, or reasonably should have known, that the appraisal would be used in connection with a return or a claim for refund, and

(2) the claimed value of the property on a return or claim for refund which is based on such appraisal results in a substantial valuation misstatement under chapter 1 (within the meaning of section 6662(e)), or a gross valuation misstatement (within the meaning of section 6662(h)), with respect to such property, then such person shall pay a penalty in the amount determined under subsection (b).

(b) Amount of Penalty- The amount of the penalty imposed under subsection (a) on any person with respect to an appraisal shall be equal to the lesser of—

(1) the greater of—

(A) 10 percent of the amount of the underpayment (as defined in section 6664(a)) attributable to the misstatement described in subsection (a)(2), or

(B) \$1,000, or

(2) 125 percent of the gross income received by the person described in subsection (a)(1) from the preparation of the appraisal.

(c) Exception- No penalty shall be imposed under subsection (a) if the person establishes to the satisfaction of the Secretary that the value established in the appraisal was more likely than not the proper value.

IRC § 6695A

To Which Taxes Does It Apply?

- **Income Taxes**
- **Estate & Gift Taxes**
 - **not for appraisals prepared before May 25, 2007**
 - **for appraisals prepared on or after May 25, 2007, effective date of SBWOTA (per AM 2007-0017), if appraisal results in a gross valuation misstatement**
 - **For all appraisals prepared on or after December 29, 2007, effective date of Tax Technical Corrections Act of 2007**

IRC § 6695A

To Whom Does It Apply?

- **No Definition of “person”**
 - Only refers to “any person who knows or reasonably should have known that appraisal would be used in connection with a return or claim for refund”
- **Appraisers?**
 - Qualified and non-qualified?
- **Person per IRC § 7701?**
- **Fiduciary?**
 - Trustee?
 - Personal Representative?
- **Other Professional Adviser?**
 - Realtor?
 - Insurance Broker?
 - Accountant?
 - Attorney?

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IRC § 6695A

To What Does It Apply?

- **“Appraisal”**
 - not “Qualified Appraisal”
 - not defined
- **“Prepare”**
 - Not defined

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IRC § 6695A(c)

Exception

- **No penalty will be imposed under Section 6695 if the “person” establishes that the value set forth in the appraisal was “more likely than not the proper value”**
 - More likely than not = greater than 50% chance
- **But must be established to the satisfaction of the Secretary of the Treasury**

IRC § 6662

New Definitions

- **Substantial Valuation Misstatement**
 - IRC §§ 6662(e)(1) & (2)
- **Substantial Estate and Gift Tax Valuation**
 - IRC § 6662(g)
- **Gross Valuation Misstatement**
 - IRC § 6662(h)(2)

IRC §§ 6662(e)(1) & (2)

Substantial Valuation Misstatement Defined

- If value of property (or the adjusted basis of any property) claimed on an income tax return is 150% or more than the amount determined to be the correct amount of such valuation or adjusted basis
 - pre-PPA = 200%
- *de minimis* exception - no penalty imposed if the portion of the underpayment for the taxable year attributable to the substantial valuation misstatement is \$5000 or less

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IRC § 6662(g)

Substantial Estate or Gift Tax Valuation Understatement Defined

- If the value of any property claimed on an estate, gift or GST tax return is 65% or less of the amount determined to be the correct amount of such valuation
 - Pre-PPA = 50%
- *de minimis* exception – no penalty imposed if the underpayment attributable to the substantial estate and gift valuation understatements for the taxable period is \$5000 or less

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IRC § 6662(h)(2)

Gross Valuation Misstatements Defined

- **Income Tax**
 - Substitute 200% for 150%
- **Estate Tax**
 - Substitute 40% for 65%
- **Penalty increases to 40% from 20% for taxpayer**
 - But penalty stays same for appraiser

IRC § 6664(c)(2)

Reasonable Cause Exception

- **IRC § 6664(c)(1) states that no penalty will be imposed under IRC § 6662 “if it is shown that there was a reasonable cause for [an underpayment] and that the taxpayer acted in good faith.”**
- **However, IRC § 6664(c)(2) excepts out underpayments attributable to (1) any gross valuation overstatements and (2) substantial valuation overstatements unless (A) the claimed value of the property was based on a qualified appraisal and (B) in addition to obtaining such appraisal, the taxpayer made a “good faith” investigation of such value.**

NEW DEFINITIONS
“QUALIFIED APPRAISAL”
&
“QUALIFIED APPRAISER”

- **IRC § 170(f)(11)(E) defines both terms**
- **Definitions also applicable to IRC § 6662 understatement penalties (per IRC §§ 6664(c)(3)(B) & (C))**

IRC § 170(f)(11)(E)(i)
“Qualified Appraisal”

- **(I) appraisal must be within Treasury Regulations**
 - Appraisal must comply with all requirements if Treas. Reg. 1.170A-13(c) (Notice 2006-96, 2006-46 IRB 902)
- **(II) appraisal must be conducted by a “qualified appraiser” in accordance with generally accepted appraisal standards and Treasury Regulations**
 - Uniform Standards of Professional Appraisal Practice (“USPAP”) is sole example of generally accepted appraisal standards given in Notice 2006-96, §.02(2)

IRC §§ 170(f)(11)(E)(ii) & (iii) **“Qualified Appraiser”**

Appraiser must:

- **have earned an appraisal designation from a “recognized professional appraiser organization” OR has otherwise met minimum education and experience requirements set forth in Treasury Regulations ((ii)(I))**
- **regularly perform appraisals for which he or she receives compensation ((ii)(II))**
- **meet other Treasury Regulation requirements ((ii)(III))**
- **demonstrate verifiable education and experience in valuing the type of property subject to the appraisal ((iii)(I))**
- **Not have been prohibited from practicing before the IRS in the three prior years ((iii)(II))**

Treasury Regulations – Notice 2006-96 **“Appraisal Designation”**

- **“Appraisal designation from recognized professional appraiser organization” must be “awarded on the basis of demonstrated competency in valuing the type of property for which the appraisal is performed.” (§.03(1))**

Treasury Regulations – Notice 2006-96 “Education and Experience”

- To meet “demonstrated verifiable education and experience” requirement, appraiser must make a declaration in the appraisal “that, because of the appraiser’s background, experience, education, and membership in professional associations, the appraiser is qualified to make appraisals of the type of property being valued.” (§.03(2))

QUALIFIED APPRAISER “Minimum Education & Experience”

- **Real Property (§.03(3)(a))**
 - On or before 10/19/2006 – Treas. Reg. § 1.170A-13(c)(5)
 - After 10/19/2006 – appraiser must be licensed or certified for the type of property being appraised in the state in which the real property is located
- **Other Property (§.03(3)(b))**
 - On or before 2/16/2007 – Treas. Reg. § 1.170A-13(c)(5)
 - After 2/16/2007 – Appraiser must:
 - Have successfully completed college or professional-level coursework that is relevant to the property being valued;
 - Have two years experience in the trade or business of buying, selling or valuing the type of property being valued; and
 - Fully describe in the appraisal his or her education or experience that qualifies him or her to value the type of property being valued.

POST-PPA

What's an Attorney to Do?

- **Who hires the appraiser?**
- **Can you rely on others' statements when planning?**
- **Should attorneys file tax returns?**
- **How do we advise clients regarding valuation discounts?**
- **How does client go beyond valuation?**
- **How much due diligence is required regarding appraiser?**
- **How advise client as to choosing an appraiser?**
- **Circular 230?**