

Appraisal Requirements for Charitable Contribution Deductions

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MOST TAXPAYERS ARE FAMILIAR WITH THE BENEFIT of charitable contribution deductions, as provided under the federal income tax law, Code Section 170.¹ These deductions have been in existence for many decades, and most taxpayers recognize the importance of taking what can be significant deductions on their federal and state tax returns.

When donating to charity, assuming the gift is otherwise qualified,² taxpayers generally are able to deduct the fair market value of the contribution. The definition of what is “fair value,” or “fair market value,” along with other related questions as to value, the type of value, etc., is a major issue in federal tax law, as it is within the appraisal industry. However, the summary position is that the meaning of fair market value involves an exchange between a willing buyer and willing seller, without undue pressure. This approach has come from case law. The tax code has no singular definition of fair market value for all purposes.

Generally speaking, one of the major concerns with a charitable gift is determining the fair market value on the date of the charitable contribution, since the fair market value is normally the amount that can be deducted for federal tax purposes.³ The fair market value is the crucial consideration as to the amount of the deduction; thus the requirements to determine fair market value must be met.

The Code §170 regulations specify the requirements for supporting the deduction relative to a proper appraisal. There have been many articles and discussions on these regulations as to what constitutes a proper appraisal as well as the issue of who is an approved appraiser for purposes of the tax requirements.⁴ Not surprisingly,

valuation issues spawn much controversy. The regulations, under Treasury Reg. §1.170A-13, and generally under Code §170, attempt to place more controls on the valuation issue because of the importance of this deduction and the concern as to what constitutes fair value.

Valuation of specific property has been in the news of late regarding gifts of paintings, conservation easements,⁵ and even contributions of automobiles to charities. In the latter case, Congress recently saw fit to provide additional legislation which limits the deductibility of contributions of automobiles, especially because of what were thought to be abuses.⁶

Although Congress attempted to tighten the restrictions of charitable contribution deductions in some cases, along with the Treasury’s issuing Treasury Reg. §1.170A-13 on substantiation of the fair market value of a charitable contribution, there continues to be additional concern with such contributions, and the determination of the fair market value of the gifts. As a result, the IRS promulgated additional Proposed Regulations on the subject of the charitable contribution deduction and substantiation

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requirements. Some of the original Regulations (§1.170A-13) were generated by the Treasury as a result of Acts by Congress, which were passed in 2004 and 2006. These Acts attempted to strengthen the requirements for such deductions.⁷ The Proposed Regulations under Treasury §1.170A-17 go further to strengthen the requirements.

PROPOSED REGULATIONS ON SUBSTANTIATION AND REPORTING FOR NON-CASH CHARITABLE CONTRIBUTIONS

Under the Proposed Regulations,⁸ the Treasury states:

“These Proposed Regulations provide guidance concerning substantiation and reporting requirements for cash and non-cash charitable contributions under Section 170 of the Internal Revenue Code.” In particular, the Proposed Regulations were issued in response to additional requirements for substantiation and support for charitable contributions that were provided for under the American Jobs Creation Act of 2004⁹ and under the Pension Protection Act of 2006. The Proposed Regulations are intended to apply to contributions that occur after the date the regulations are published as Final Regulations. Therefore, until such time, one could consider these Proposed Regulations as guidance under Treasury Reg. §1.170A. Tax practitioners typically follow Proposed Regulations with very few exceptions as they give notice of the government’s position. There is authority for the position that the Proposed Regulations are not binding on the taxpayer; however, most taxpayers are advised to follow them.

The Proposed Regulations provide specific requirements for the deduction of a contribution of real or personal property where the amount claimed for the deduction is in excess of \$5,000.¹⁰ One of the requirements in Code §170 and the Proposed Regulations, along with the prior regulations, is to attach a “Qualified Appraisal” (as that term is used and discussed below), where the amount claimed for the deduction is in excess of \$5,000.¹¹ If the appraisal involves a return filed after Aug. 17, 2006, there are specific requirements as to what constitutes a “Qualified Appraisal” and a “Qualified Appraiser.”¹²

Code §170 provides that an individual will not meet the requirements to be a “Qualified Appraiser” unless that person: “...(1) demonstrates verifiable education and experience in valuing the type of property subject to the appraisal; and (2) the individual has not been prohibited from practicing before the Internal Revenue Service ...”¹³

This requirement of the appraiser to not only show proper education, as defined in the regulations, but also experience in valuing the type of property in question, should be recognized by any appraiser who attempts to undertake the appraisal and by those who claim the deduction.

Appraisers and others working in the fields of appraising and taxation must remember that the definitions used in the tax regulations are *different* from those used in many professional appraisal organizations and overseeing bodies in the appraisal field. For example, under the Uniform Standards of Professional Appraisal Practice (USPAP), within the Definitions section of the 2008–09 edition, an “appraiser” is “one who is expected to perform valuation services competently and in a manner that is independent, impartial and objective.”

The same issue as to definitional differences applies to an appraisal. That is, the Proposed Regulations have a stated definition of an appraisal (Qualified Appraisal), as noted above. Under Code §170(f)(11)(E)(i), the Qualified Appraisal is defined as an appraisal that: “(1) is treated ... as a qualified appraisal under regulations or other guidance prescribed by the Secretary [of the Treasury]; and (2) is conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance prescribed ...” by the Secretary.

However, in contrasting the differences of the Proposed Regulations and USPAP, note that USPAP defines the appraisal as:

(Noun) the act or process of developing an opinion of value; an opinion of value.

(Adjective) of or pertaining to appraising and related functions such as appraisal practice appraisal services.

Many organizations refer to the USPAP definition of an appraisal.

Since 2006, the federal government, for tax purposes, has attempted to give definitional support for a number of the terms noted, such as Qualified Appraisal, Generally Accepted Appraisal Standards, Appraisal Designation, Education and Experience and Minimum Education and Experience.¹⁴ Without attempting to detail all of the requirements for the Qualified Appraisal and the

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Qualified Appraiser, it should be noted that there are many requirements under the Regulations and Proposed Regulations to substantiate the position for the Qualified Activity, including, for example, proper record keeping.¹⁵

In Proposed Regulation §1.170A-17, there are additional requirements for Qualified Appraisals. As stated in these regulations, the Appraisal Document must be prepared by the Qualified Appraiser in accordance with “Generally Accepted Appraisal Standards.” The Proposed Regulations make reference to USPAP.¹⁶ The Proposed Regulations are in line with Notice 2006-96. However, the Proposed Regulations now require compliance with “Qualified Appraisals.”

Consistent with the prior rules, but slightly modified, the Proposed Regulations emphasize the time frames that must be met for the appraisal in conjunction with the gift that is made. One cannot, for example, simply have an appraisal that was made two years before the gift was made to the charity and validly claim the deduction. Rather, the Proposed Regulations provide that the effective date for the appraisal, which is the date to which the value opinion would apply, must be the date of the contribution, in most cases. There is a 60-day window from the time of the appraisal to the actual date of the contribution.¹⁷ Thus, although appraisers will often refer to an “effective date” as used in USPAP, the date that is important for federal tax law is normally the date of the contribution. And, the controlling date for the qualified appraisal under Treasury Regs. Section 1.170-13(c)(3) and Proposed Treasury Regs. 1.170A-17(a)(4) must be “... not earlier than 60 days prior to the date of contribution ...” Thus, although most real estate appraisers will be guided by USPAP when distinguishing between an effective date and report date, the federal tax law is looking to the definition noted above.

Filings must be made with the tax return when claiming the charitable contribution deduction of property valued in excess of \$5,000. IRS Form 8283 must be attached to the tax return, evidencing the deduction.

As to an appraiser’s education and experience, the Proposed Regulations delineate “Minimum Education Requirements” more thoroughly, to assure that the Appraisal and the Appraiser are “Qualified.”¹⁸ Although there are other ways to satisfy requirements for education, the Proposed Regulations add that an individual has what

is called “Verifiable Education and Experience” if the appraiser in question has completed professional or college-level course work relevant to valuing the type of property in question. Further, there is a statement as to “Minimum Education,” requiring two or more years of experience in valuing “That Type of Property.”¹⁹ It appears there will be more discussion and regulations issued to determine what “Education and Experience” is necessary for given types of property.

Individuals seeking education and/or designations may be advised to choose professional organizations that follow the requirements of USPAP—although not all organizations connected with appraisals follow USPAP, and clearly the federal tax code, as to charitable contributions, does not refer to a requirement to follow USPAP. Under IRS Notice 2006-96, real estate appraisers have sufficient education and experience if one holds a proper license or certification in the state where the property is located.²⁰ Thus, indirectly, because of state licensing bodies, USPAP and other standards may be relevant, but the federal tax Code does not directly cite nor rely on such organizations for purposes of Code Section 170 contributions.

The Proposed Regulations emphasize there is no absolute safe harbor to guarantee a deduction simply because one is using a “Qualified Appraisal” and/or “Qualified Appraiser.” The statement in the Treasury Regulations notes: “Taxpayers are reminded that the IRS may challenge the amount of a claimed deduction, even if the donor substantiates the amount of the deduction with a Qualified Appraisal prepared by a Qualified Appraiser.”²¹

SUBSTANTIATION

The essence of the Code §170 requirements, the existing Regulations and the Proposed Regulations, along with other releases and positions by the Treasury and the IRS, support the position that the key concern is to substantiate the fair market value of the property that is being claimed as a charitable deduction. Such substantiation focuses not only on the number that is concluded to be the fair market value, but also how that number was calculated and supported in the “Qualified Appraisal” and by the “Qualified Appraiser.” Such discussion and position are contained in the Code and the Regulations as well as the Proposed Regulations.²²

In particular, the new substantiation requirements are more burdensome; they require stronger documentation

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when the amount of the deduction is in excess of \$5,000 and involves property other than cash. (See Form 8283, which is utilized with the tax return to help substantiate the claimed deduction, along with other support documentation, including the “Qualified Appraisal.”)²³

Specifically, Treas. Regs. Section 1.170-13(c) states that the substantiation requirements include attaching to the donor’s tax return a “fully completed appraisal summary” (as defined in the Code).

FORM 8283:

The substantiation under Code §170 for the requirements of documentation for a gift in excess of \$5,000 provides for written acknowledgment, via the Qualified Appraisal, and support for the Qualified Appraiser. This form illustrates some of the requirements necessary to support the tax deduction. These relate to: (1) timing; (2) details on the Qualified Appraiser and the Qualified Appraisal; (3) description of the property being contributed; (4) the fair market value claimed; (5) detail as to the property that is being contributed; (6) information as to the donor and donee; (7) basis of the property; and (8) statements about the contribution itself, such as whether the contribution is a part sale (bargain sale) transaction; relationships, if any, between the donor and donee; declaration as to an understanding by the appraiser of the requirements in connection with the appraisal, including potential penalties that one can incur for improper actions; and so forth.

There is a requirement for the donee to acknowledge the gift in question and to disclose other information as to relationships, if any, between the donee and the donor. Information as to the manner of acquisition of the property and timing of the gift are also noted in Form 8283.

SUMMARY

A qualified charitable contribution offers the taxpayer a deduction equal to the fair market value of the property, as well as avoidance of the current income tax that would be generated if one sold the property at fair market value for an amount in excess of the basis. To support the good faith positions of determining fair market value, the Proposed Regulations amend the existing Regulations and delineate requirements under Code §170, the charitable contribution deduction section, and attempt to implement additional restrictions on such contributions as covered by the American Jobs Creation Act of 2004 and the Pension Protection Act of 2006.

Proposed Regulations under §1.170A-17 adds to the requirements of determining what constitutes a “Qualified Appraiser” as well as what constitutes a “Qualified Appraisal.” The Proposed Regulations require a higher level of expertise and experience from the Qualified Appraiser and require documentation of such activity and experience, as well as more information on the property being contributed.

Although the Proposed Regulations are not adding new concepts, they require additional substantiation and documentation for a Qualified Appraisal used to support the claim of a deduction under rules of Code §170. Although we cannot know when or if the Proposed Regulations will become final, they are supported by Code Section 170 and the cautious appraiser will follow them. ■

ENDNOTES

1. See Internal Revenue Code 26 U.S.C.A. Annotated, Code Section 170, herein also referred to as “Code § 170.”
2. For details on charitable contributions, see Levine, Mark Lee and Segev, Libbi Levine, *Real Estate Transactions, Tax Planning and Consequences*, Thomson-West (2009 edition). See Chapter 13 of text §234, page 376. See also the article by Harmelink, Philip, and Nichols, Nancy, “Various Motivations Behind Family Charitable Contributions,” *Tax Notes* 205 (1/15/2007).

See also IRS Publication 78, which details the basic rules for charitable contribution deductions.

See also the Levine text, cited in this note, for a discussion of the tax value issue. In particular, see Chapter 41; see also Internal Revenue Code Section 2512 as one example of the valuation issue as to gifts and gift taxation.

3. There are exceptions to the deductibility of the fair market value of the property. For example, if the item that is given to charity, had it been sold, would generate long-term capital gain, the general rule is that fair market value can be deducted. However, if the item, when sold, would not generate a long-term capital gain deduction, such as a property that is inventory, and would generate ordinary income on a sale, the deduction is generally limited to the adjusted basis of the taxpayer. See Murrills, David, “Donating Inventory: Section 170(e)(3) and Fair Market Value,” *Tax Notes* 655 (Feb. 1, 2003). See also Code §170(e) in general for the rules as to when a fair market value deduction is allowed. See also the Levine and Segev text, cited *supra*, Endnote 2, Text §236.
4. See the Levine and Segev text, cited *supra*, Endnote 2. See also the specific regulations for determining a qualified charitable contribution under the valuation issues contained in the Code §170 regulations. In particular, see Treasury Reg. §1.170A-13(c).

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See Levine, Mark Lee, "Appraisers' Exposure In Charitable Contributions: Final Regulations," *Journal of R.E. Appraisal & Economics* (1988).

See Levine, Mark Lee, "Appraisers' Exposure In Connection With Charitable Contributions – Revisited," *The Appraisal Journal* (January 2002).

See Levine, Mark Lee, "A Refresher and Tax Baedeker On Charitable Contributions After the JGTRR Act of 2003," *Exchanging Real Estate* (2008). See Levine, Mark Lee, "A Refresher and Tax Baedeker On Charitable Contributions After the JGTRR Act of 2003," *Real Estate Transactions, Tax Planning*, Thomson-West (2004).

See Levine, Mark Lee, "Charitable Contributions of the Automobile: Riding To A Deduction," *Real Estate Transactions, Tax Planning*, Thomson-West (2005).

See Levine, Mark Lee, "Appraisal Update: New Requirements for Charitable Deductions Put Appraisers At Risk," CIREI-Commercial Investment Real Estate Institute (January-February 2007).

5. See Code §170(h). See also *Turner v. CIR*, 126 T.C. 299 (2006 WL 1330084), See *Glass v. CIR*, 124 T.C. 258 (2005 WL 1231654). See Gerzog, Wendy, "Conservation Easement Under *Turner* and *Glass*," *Tax Notes* 179 (July 10, 2006).
6. See IRS Publication 4303, *A Donor's Guide To Car Donations*. See Levine, Mark Lee, and Segev, Libbi Levine, "Charitable Contributions of the Automobile: Riding To A Deduction," *Real Estate Transactions, Tax Planning*, Chapter 13, Text §243.5, Note 15.
7. The American Jobs Creation Act of 2004 and the Pension Protection Act of 2006.
8. See Proposed Regulations Reg-140029-07 on the issue of substantiation and reporting requirements for cash and non-cash charitable contribution deductions. These Proposed Regulations were issued in connection with Treasury Reg. §1.170A15-18.
9. Public Law 108-357.
10. Code §170(f)(11).
11. Code §170(f), Treasury Reg. §1.170A-13, and Proposed Treas. Regs. Section 1.170A-17.
12. Code §170(f)(11)(E).

Under Code §170(f)(11)(E)(i), the Qualified Appraisal is defined as " ... an appraisal that is (1) treated as a qualified appraisal under regulations or other guidance prescribed by the Secretary (of the Treasury) and (2) conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance prescribed by the Secretary (of the Treasury)."

However, the term "Qualified Appraiser" has a distinct meaning within the Regulations, because of the concern to be assured that the person undertaking the appraisal has certain education and training. As such, the Proposed Regulations provide: " ... the term 'qualified appraiser' means an individual who (1) has earned an appraisal designation from a recognized professional appraisal organization or has otherwise met minimum education and experience requirements set forth in Regulations prescribed by the Secretary; (2) regularly performs appraisals for which the individual receives compensation, and (3) meets such other requirements as may be prescribed by the Secretary ..." See Code §170(f)(11)(E)(ii).
13. Code §170(f)(11)(E)(ii).
14. IRS Notice 2006-96.
15. See these details in REG-140029-07.
16. See Title XI of the Financial Institution Reform, Recovery and Enforcement Act of 1989, Public Law 101-73, 103 Stat. 183 (12 U.S.C. 3331-3351).
17. For example, the Proposed Regulations provide that the date the "Qualified Appraiser" signs the "Appraisal Report," known as the "Appraisal Report Date" can be no earlier than sixty (60) days before the date that the contribution actually occurs. It cannot be later than the due date, including extensions of the tax return, where the deduction is to be claimed. See also Treasury Reg. §1.170A-13 and Proposed Treas. Regs. Section 1.170A-17.
18. Treasury Reg. §170(f)(11)(E)(iii)(I).
19. "That Type of Property" is the specific language of the Regulations.
20. Notice 2006-96, Section 3.03(a)(ii).
21. Proposed Regulations contained in REG-140029-07.
22. Code §170, existing Treasury Reg. §1.170A and the Proposed Regulations under Proposed Amendment 1.170A-16, contained within the earlier-cited REG-140029-07.
23. IRS Form 8283, as well as Treasury Reg. §1.170(f)(8) and Treasury Reg. §1.170A-13(f).