

# Valuing your valuables: the IRS way

You make a gift of a valuable work of art. Or donate it to a favored charity. Perhaps, at your death, your executor needs to put prices on your holdings for estate tax purposes. How does the Internal Revenue Service determine whether the value indicated on a tax return reflects the true, fair market value of a work of art?

## **Appraising the appraisal system**

The answer, interestingly enough, is the little-known IRS Commissioner’s “Art Advisory Panel.”

The Panel, generally consisting of somewhere between 16 to 21 members, depending upon the year, is empowered to guide the IRS in valuation by reviewing and evaluating the acceptability of art appraisals submitted by donors and executors in support of their claims as to the property’s fair market value. All tax returns selected for audit that include artwork or cultural property with a claimed value of \$20,000 or more are referred to the IRS National Office Art Appraisal Services for review by the Panel.

The Panel is composed of distinguished museum directors and curators, art historians and scholars, and dealer experts—often some of the best-known professionals in their field of expertise, and all of whom serve without compensation. They meet in Washington, D.C., usually once or twice a year in each of several specialty areas.

## **Behind the scenes**

Prior to the meetings, staff appraisers send photographs and written materials to the panelists concerning the artwork to be reviewed. The written material is likely to include information from the taxpayer’s appraisal—the size, medium, physical condition of the work—as well as the staff’s own market research, including information on public and private sales of relevant art. Often, one or more of the panelists or staff will have seen the property, but a visual inspection is not required. To ensure objectivity, the panelists are not advised of the nature of the taxable transfer—in other words, they have no indication of whether an item is being donated to a charity or is part of a private family collection being passed down to another generation.

At the meetings, which are closed to the public, the Panel examines the taxpayer's appraisal and any supporting evidence provided, along with the staff's research and findings. After discussion—often lively, according to insiders, as a result of the different perspectives of the various experts—consensus usually can be reached. Often, the fair market value of a particular work of art may have a “plus-or-minus factor” or a range in values. And, occasionally, additional information on a particular work is needed, requiring a postponement of the appraisal until the information is obtained.

### **After the evaluation**

The Panel's conclusions and recommendations are reviewed by the office of Appraisal Services. A copy of the resulting report detailing the Panel's determination, together with a list of the participating panelists, is sent to the taxpayer. The taxpayer may ask for reconsideration of the Panel's findings of fair market value of the item only if additional information or new probative evidence can be furnished. If such information is supplied to the Panel, reconsideration may take place at a subsequent meeting. Appeal can take place at either the IRS administrative level or like most tax disputes, in court. In the event of a court battle, the IRS will rely upon the Art Appraisal Services and Art Advisory Panel's assistance in court papers, and panels will often appear as expert witnesses for the IRS valuation.

### **Inaccurate appraisals can be costly**

You may be liable for a penalty if you overstate the value or adjusted basis of your donated property. The penalty is 20% of the underpayment of tax related to the overstatement, if the value or adjusted basis claimed on your tax return is 150% or more of the correct amount, and you underpaid your tax by more than \$5,000 as a result of the overstatement. The penalty is 40% if the value or adjusted basis is 200% or more of the correct amount, and you underpaid your tax by more than \$5,000.

Appraisers who prepare an incorrect appraisal may have to pay a penalty when they know, or should have known, that the appraisal would be used in connection with a tax return or claim for refund, and the appraisal results in the imposition of the 20% or 40% penalty. The penalty may be either 10% of the underpayment because of the

misstatement, \$1,000, or 125% of the income received for the appraisal. In the case of fraud, an appraiser may be subject to a civil penalty for aiding and abetting an understatement of tax liability, and may have his or her appraisal disregarded.

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Any developments occurring after January 1, 2009, are not reflected in this article.