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Importance of “Qualified Appraisals” by “Qualified Appraisers”

-by Neil E. Harl*

The rapid run-up in farm and ranch land values in recent years¹ has focused attention on land appraisal for purposes of developing an investment strategy, evaluating offers to buy or to sell and supporting deductions claimed for charitable gifts of property. Land value increases have also boosted the stakes for valuations of property for federal estate purposes,² generation-skipping transfer tax purposes³ and for gifts to non-charitable donees.⁴ The importance of accurate and supportable appraisals has never been greater than at present.

Wherever tax considerations are involved, “qualified appraisers” and “qualified appraisals” have become matters of significant concern.⁵

The basic statutory framework

The authority for requiring “qualified appraisals” by “qualified appraisers” for property transfers under certain circumstances dates from the *Pension Protection Act of 2006*.⁶ The Internal Revenue Service promptly issued *Notice 2006-96*⁷ which stated that the Notice was serving as “transitional guidance” and regulations would be issued.

Additional guidance

*Notice 2006-96*⁸ stated that individuals would be required to obtain a “qualified appraisal” for donated property with a deduction of greater than \$5,000 and pointed out that newly enacted I.R.C. § 6695A imposes a civil penalty on one who prepares an appraisal that results in a substantial or gross valuation misstatement.⁹ The civil penalty is the greater of 10 percent of the amount of the underpayment or \$1,000, or 125 percent of the gross income received by the appraiser from the preparation of the appraisal.¹⁰ The penalty is not to be imposed if the value established in the appraisal is “. . . more likely than not the proper value.”¹¹

The term “qualified appraisal” (for purposes of *this paragraph* – limited to paragraph 11 in I.R.C. § 170(f)) is defined as an appraisal “. . . which (I) is treated . . . as a qualified appraisal under regulations or other guidance . . . “ from the Department of the Treasury and “. . . (II) is conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance. . . “ from the Department of the Treasury.¹² An appraisal is treated as having been conducted in accordance with generally accepted appraisal standards if, for example, the appraisal is consistent with the substance and principles of the Uniform Standards of Professional Appraisal Practice as developed by the Appraisal Standards Board of the Appraisal Foundation.¹³

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The term “qualified appraiser” (again, for purposes of *this paragraph* – limited to paragraph 11 in I.R.C. § 170(f)), on the other hand, means an individual who “. . . (I) has earned an appraisal designation from a recognized professional organization or has otherwise met minimum education and experience requirements set forth in regulations . . . ; (II) regularly performs appraisals for which the individual receives compensation, and (III) meets such other requirements as may be prescribed . . . “ by the Department of the Treasury.¹⁴ The individual must – (1) demonstrate verifiable education and experience in valuing the type of property subject to the appraisal and (2) has not been prohibited from practicing before the Internal Revenue Service during the three-year period ending on the date of the appraisal in question.¹⁵

An appraiser must include a declaration, in the appraisal statement, that the appraiser may be subject to a penalty if a substantial or gross valuation misstatement results from an appraisal of the property that the appraiser knows, or should have known, would be used in connection with a tax return or claim for refund.¹⁶

Important point for farm and ranch appraisals (and appraisers)

*Notice 2006-96*¹⁷ makes it clear that an appraiser is treated as having earned an appraisal designation from a recognized professional appraisal organization if the appraisal designation is awarded on the basis of demonstrated competency in valuing the type of property for which the appraisal is performed. Also, the education and experience requirements are likewise associated with the type of property being valued. Thus, appraisers of farm and property are not judged by the competency of appraisers of urban property.

ENDNOTES

¹ See Duffy, *Iowa Farmland Survey*, Iowa State University Extension, December 2012.

² See I.R.C. § 2001(a). See generally 5 Harl, *Agricultural Law*, Chapters 42-45 (2013); Harl, *Agricultural Law Manual* § 5.03 (2013).

³ See I.R.C. § 2601. See generally 5 Harl, *Agricultural Law* § 44.08 (2013).

⁴ See I.R.C. § 2501(a). See generally 6 Harl, *Agricultural Law* Ch. 46 (2013).

⁵ See I.R.C. §§ 170(f)(11)(E), 6695A.

⁶ Pub. L. No. 109-280, 120 Stat. 780 (2006), adding I.R.C. § 170(f)(11)(E) and I.R.C. § 6695A (penalties).

⁷ 2006-2 C.B. 902.

⁸ 2006-2 C.B. 902.

⁹ I.R.C. § 6695A(a).

¹⁰ I.R.C. § 6695A(b).

¹¹ I.R.C. § 6695A(c).

¹² I.R.C. § 170(f)(11)(E)(i).

¹³ Notice 2006-96, 2006-2 C.B. 902.

¹⁴ I.R.C. § 170(f)(11)(E)(ii).

¹⁵ I.R.C. § 170(f)(11)(E)(iii).

¹⁶ Notice 2006-96, 2006-2 C.B. 902.

¹⁷ 2006-2 C.B. 902.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

BANKRUPTCY

CHAPTER 12

ELIGIBILITY. We have been informed by one of the attorneys in the case that the IRS has decided not to appeal the following case. The debtor had farmed with a brother in a partnership from 1993 through 2010 when the partnership was dissolved. The dissolution agreement split some of the farm equipment but the brother assumed the partnership liabilities and paid cash for the value of the debtor's partnership interest. The debtor's share of farming income for 2007 through 2010 exceeded 50 percent of the debtor's total income. After the dissolution and up to the bankruptcy petition, the debtor continued to farm alone in a much smaller operation. The debtor filed for Chapter 12 in 2011 and federal and state tax claims arising from the dissolution of the partnership were filed in the debtor's bankruptcy case and the IRS argued that the debtor was not eligible for Chapter 12 because the debtor did not have farm income for at

least three years before the filing of the petition, because the debtor changed farming operations in 2010. The IRS argued that the farm income eligibility requirements had to be met by the debtor in the farming operation active when the petition was filed; therefore, the debtor's income from the partnership could not be considered. The court disagreed and held that the farm income requirement did not require that the income come solely from the operation active when the debtor filed the petition and could be combined with all farm activity during the three years prior to the petition. Because the debtor's farming income in two of the pre-bankruptcy years exceeded non-farm income, the debtor was eligible for Chapter 12. *In re Hemann*, 2013 Bankr. LEXIS 1385 (Bankr. N.D. Iowa 2013).

USE OF ESTATE PROPERTY. The debtors, husband and wife, owned and operated a dairy farm through a limited liability company. The debtors had purchased the dairy farm with a real estate mortgage and commercial security agreement with a bank which provided for a blanket security interest on the land, equipment, livestock, and milk and cattle sale proceeds. The debtors had suffered losses to their cows from stray electricity and sought