

Office of Chief Counsel
Internal Revenue Service
Memorandum

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to: Program Manager, Estate & Gift Tax Program
(Small Business/Self-Employed)

from: Associate Chief Counsel
(Procedure & Administration)

subject: Applicability of Section 6695A Penalty to Estate & Gift Appraisals

This memorandum addresses the applicability of the penalty under I.R.C. § 6695A to appraisals used in connection with estate or gift tax returns and whether there is a period of limitations on assessment that applies to this penalty.

ISSUES

(1) Whether the section 6695A penalty may be assessed against an appraiser who prepared an appraisal used in connection with an estate or gift tax return or claim for refund that results in a substantial or gross valuation misstatement.

(2) What is the period of limitations applicable to assessment of the section 6695A penalty?

CONCLUSIONS

(1) The Service may assess a section 6695A penalty against an appraiser for appraisals prepared after May 25, 2007 that are used in connection with an estate or gift tax return or claim for refund or credit that results in a gross valuation misstatement.

(2) There is no period of limitations applicable to the assessment of a penalty under section 6695A. To the extent practicable, however, the Service should assess the section 6695A penalty within 3 years after the filing of the return or claim for refund on

which the penalty is based in order to minimize the ability of an appraiser to argue that the assessment was not made on a timely basis.

LAW AND ANALYSIS

The Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780, was enacted on August 17, 2006. Section 1219(b)(1) of the PPA added section 6695A to the Code, which provides:

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).

Section 6695A(a).

The penalty is the greater of \$1,000 or 10% of the amount of the underpayment attributable to the misstatement (but in no event more than 125% of the gross income received by the appraiser for preparing the appraisal). Section 6695A(b). The penalty does not apply if the appraiser establishes to the satisfaction of the Secretary that the value established in the appraisal was more likely than not the proper value. Section 6695A(c).

Section 1219(b)(2) of the PPA also amended section 6696, which contains rules regarding the application of sections 6694, 6695, and 6695A. Section 6696, as amended after the PPA, provides, in part:

(d) Periods of limitation.

(1) Assessment. The amount of any penalty under section 6694(a) or under section 6695 shall be assessed within 3 years after the return or claim for refund with respect to which the penalty is assessed was filed, and no proceeding in court without assessment for the collection of such tax shall be begun after the expiration of such period. In the case of any penalty under section 6694(b), the penalty may be assessed, or a proceeding in court for the collection of the penalty may be begun without assessment, at any time.

(2) Claim for refund. Except as provided in section 6694(d), any claim for refund of an overpayment of any penalty assessed under section 6694, 6695, or 6695A shall be filed within 3 years from the time the penalty was paid.

(e) Definitions. For purposes of sections 6694, 6695, and 6695A --

(1) Return. The term "return" means any return of any tax imposed by subtitle A.

(2) Claim for refund. The term "claim for refund" means a claim for refund of, or credit against, any tax imposed by subtitle A.

Section 6696(d) & (e).

Section 6695A is generally effective for appraisals prepared with respect to returns or submissions filed after August 17, 2006. If, however, the appraisal relates to a facade easement donation, the effective date is for returns filed after July 25, 2006. The Joint Committee Explanation describing the PPA states that "[t]he provision establishes a civil penalty on any person who prepares an appraisal that is to be used to support a tax position if such appraisal results in a substantial or gross valuation misstatement." Technical Explanation of H.R. 4, JCX-38-06 at 311 (August 3, 2006).

The Small Business and Work Opportunity Tax Act of 2007, Public Law 110-28, 121 Stat. 190, was enacted on May 25, 2007. Section 8246(a) of the SBWOTA amended several provisions of the Code, including section 6696(e), to extend the income tax return preparer penalties to all tax return preparers. Section 6696(e), as amended after the SBWOTA, now provides:

(e) Definitions. For purposes of sections 6694, 6695, and 6695A --

(1) Return. The term "return" means any return of any tax imposed by this title.

(2) Claim for refund. The term "claim for refund" means a claim for refund of, or credit against, any tax imposed by this title.

This amendment to section 6696(e) is applicable to returns prepared after May 25, 2007.

I. Applicability of Section 6695A to Estate and Gift Tax Cases

The statutory language in section 6695A(a) includes penalties for returns or claims for refund based on appraisals that result in gross valuation misstatements within the meaning of section 6662(h). Section 6662(h)(2)(C) defines gross valuation misstatement to include certain estate and gift tax valuation understatements, as well as certain valuation misstatements under chapter 1 and certain overstatements of pension liabilities. Prior to amendment by the SBWOTA, however, the PPA had amended

section 6696(e) to define “return” and “claim for refund” for purposes of sections 6694, 6695, and 6695A to include only tax imposed by subtitle A, i.e., income taxes. The plain reading of former section 6696(e) meant that the section 6665A penalty was imposed only with respect to appraisals relating to returns or claims for refund of income taxes. The express language of former section 6696(e), therefore, does not give the Service the authority to assess the section 6695A penalty with respect to estate and gift tax appraisals prepared before May 25, 2007, the effective date of the amendments to section 6696(e) by the SBWOTA. Notwithstanding the inapplicability of section 6695A to these returns and refund claims, other civil and criminal penalties (including the section 6701 penalty for aiding and abetting understatement of tax liability) apply to false and fraudulent estate and gift tax appraisals that fall within this time frame.

The language of section 6696(e), as revised by the SBWOTA amendments, changes the definition of “return” and “claim for refund” for purposes of section 6695A to include returns and refund claims for any tax imposed by Title 26. As a result, under current law, the section 6695A penalty applies to an appraiser who prepares an appraisal used in connection with an estate or gift tax return or claim for refund or credit that results in a gross valuation misstatement.

This change is effective for “returns prepared after May 25, 2007.” SBWOTA section 8346(c). The preparation of an appraisal to be used with a return which results in a gross valuation misstatement can be considered part of the preparation of the return itself. Cf. Treas. Reg. § 301.7701-15(b)(1) (“A person who renders advice which is directly relevant to the determination of the existence, characterization, or amount of an entry on a return or claim for refund, will be regarded as having prepared that entry.”). Thus, the Service should assess a section 6695A penalty against an appraiser only for appraisals prepared after May 25, 2007.

II. Period of Limitations on Assessment for Section 6695A

There is no period of limitations applicable to the assessment of a penalty under section 6695A. Section 6696 provides, in general, the rules applicable to sections 6694, 6695, and 6695A. Section 6696(d)(1) specifically provides a 3 year period of limitations on assessment of the section 6694(a) and 6695 penalties, but does not provide for a limitations period for section 6695A penalty. Section 6696(d)(2) specifically provides a 3 year period of limitations on a claim for refund of an overpayment of any penalty assessed under section 6694, 6695 or 6695A. The general period of limitations under section 6501(a), which provides that tax must be assessed within 3 years after the return was filed, does not apply to the section 6695A penalty. Section 6501 explicitly provides that the term “return” means the return required to be filed by the taxpayer. Section 6501(a). Because an appraiser is not required to file the return giving rise to the penalty, section 6501(a) does not apply. Cf. Sage v. United States, 908 F.2d 18, 25 (5th Cir. 1990) (holding that section 6501 does not apply to the assessment of penalties under sections 6700 and 6701 because no return is filed by the person subject to penalty.); Kuchan v. United States, 679 F. Supp. 764 (N.D. Ill. 1988) (same).

Accordingly, there is no period of limitations that applies to the assessment of penalties under section 6695A. The section 6695A penalty may be assessed at any time. In order to minimize the ability of an appraiser to argue that an assessment has not been made on a timely basis, however, the Service should assess the section 6695A penalty, to the extent practicable, within 3 years after the filing of the return or claim for refund on which the penalty is based.

Please call me at (202) 622-3400 if you have any further questions.

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