Deconstruction, Appraiser, Appraisal, and Tax-Related Matters

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Donating Building Materials to Charity through "Deconstruction"

Within the Internal Revenue Code, tax policy aligning with environmental initiatives is a wonderful and rare occurrence. An individual may choose to deconstruct, or "un-build" a structure and donate the materials to charity. As opposed to demolishing and sending materials to the landfill. When donated to a 501(c)3 charity or governmental entity, a tax deduction can be taken for the IRS defined *Fair Market Value* of the materials, fixtures, furnishings, appliances and other property salvaged from the deconstruction. **These materials and property have solid value on the secondary retail "resale" market.**

To substantiate the tax deduction, an individual, pass-through entity, or corporation must obtain an IRS defined **Qualified Appraisal** by a **Qualified Appraiser** if the value of the donation exceeds $5,000. This simple stipulation, like all things tax, is not so simple.

Form 8283

A donor must submit IRS Form 8283 *Noncash Charitable Contributions* to substantiate the donation. The form was updated in December 2020 moving critical information found in Section B, Part I to the front page instead of hidden on p. 2. This section must be filled out by the taxpayer **in its entirety**:

Section B. Donated Property Over $5,000 (Except Publicly Traded Securities, Vehicles, Intellectual Property or Inventory Reportable in Section A)—Complete this section for one item (or a group of similar items) for which you claimed a deduction of more than $5,000 per item or group (except contributions reportable in Section A). Provide a separate form for each item donated unless it is part of a group of similar items. A qualified appraisal is generally required for items reportable in Section B. See instructions.

Part I Information on Donated Property

2 Check the box that describes the type of property donated.

a ☐ Art* (contribution of $20,000 or more)	**e** ☐ Other Real Estate	**i** ☐ Vehicles
b ☐ Qualified Conservation Contribution	**f** ☐ Securities	**j** ☐ Clothing and household items
c ☐ Equipment	**g** ☐ Collectibles**	**k** ☐ Other
d ☐ Art* (contribution of less than $20,000)	**h** ☐ Intellectual Property	

* Art includes paintings, sculptures, watercolors, prints, drawings, ceramics, antiques, decorative arts, textiles, carpets, silver, rare manuscripts, historical memorabilia, and other similar objects.

** Collectibles include coins, stamps, books, gems, jewelry, sports memorabilia, dolls, etc., but not art as defined above.

Note: In certain cases, you must attach a qualified appraisal of the property. See instructions.

3	(a) Description of donated property (if you need more space, attach a separate statement)	(b) If any tangible personal property or real property was donated, give a brief summary of the overall physical condition of the property at the time of the gift.	(c) Appraised fair market value
A			
B			
C			

	(d) Date acquired by donor (mo., yr.)	(e) How acquired by donor	(f) Donor's cost or adjusted basis	(g) For bargain sales, enter amount received and attach a separate statement.	(h) Amount claimed as a deduction (see instructions)	(i) Date of contribution (see instructions)
A						
B						
C						

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 62299J Form **8283** (Rev. 12-2020)

This is one of the few IRS forms, that brings two additional independent party's attestations onto an individual's tax return form—the appraiser and the nonprofit. Both must sign the form on page 2 parts IV and V:

Part IV Declaration of Appraiser

I declare that I am not the donor, the donee, a party to the transaction in which the donor acquired the property, employed by, or related to any of the foregoing persons, or married to any person who is related to any of the foregoing persons. And, if regularly used by the donor, donee, or party to the transaction, I performed the majority of my appraisals during my tax year for other persons.

Also, I declare that I perform appraisals on a regular basis; and that because of my qualifications as described in the appraisal, I am qualified to make appraisals of the type of property being valued. I certify that the appraisal fees were not based on a percentage of the appraised property value. Furthermore, I understand that a false or fraudulent overstatement of the property value as described in the qualified appraisal or this Form 8283 may subject me to the penalty under section 6701(a) (aiding and abetting the understatement of tax liability). I understand that my appraisal will be used in connection with a return or claim for refund. I also understand that, if there is a substantial or gross valuation misstatement of the value of the property claimed on the return or claim for refund that is based on my appraisal, I may be subject to a penalty under section 6695A of the Internal Revenue Code, as well as other applicable penalties. I affirm that I have not been at any time in the three-year period ending on the date of the appraisal barred from presenting evidence or testimony before the Department of the Treasury or the Internal Revenue Service pursuant to 31 U.S.C. 330(c).

Sign Here	Appraiser signature ▶	Date ▶
	Appraiser name ▶	Title ▶
Business address (including room or suite no.)		**Identifying number**
City or town, state, and ZIP code		

Part V Donee Acknowledgment

This charitable organization acknowledges that it is a qualified organization under section 170(c) and that it received the donated property as described in Section B, Part I, above on the following date ▶

Furthermore, this organization affirms that in the event it sells, exchanges, or otherwise disposes of the property described in Section B, Part I (or any portion thereof) within 3 years after the date of receipt, it will file **Form 8282**, Donee Information Return, with the IRS and give the donor a copy of that form. This acknowledgment does not represent agreement with the claimed fair market value.

Does the organization intend to use the property for an unrelated use? . . . . ▶ ☐ **Yes** ☐ **No**

Name of charitable organization (donee)	**Employer identification number**	
Address (number, street, and room or suite no.)	City or town, state, and ZIP code	
Authorized signature	Title	Date

Form **8283** (Rev. 12-2020)

Bridging the Cost Gap Between Deconstruction and Demolition

The tax deduction can bridge the gap between more expensive and labor intensive deconstruction over the slash-and-burn demolition practices typically costing less. In fact, in our experience, close to 95% of residential homeowners who undertook deconstruction over demolition did so because of the tax deduction. Again, it is fantastic when tax policy aligns with sound environmental practices. However, these tax deductions are wrought with challenges and under-qualified appraisers put taxpayers at risk of losing these deductions in their entirety **if the appraisal is not produced correctly**.

No Licensure for Personal Property Appraisers

The deconstruction appraiser pool was small and insular for the past few decades; there are only a handful of appraisers producing the majority of deconstruction appraisals nationwide.

To help raise appraiser standards and deliver superior appraisals, we opened our doors in September 2019, and ***I am the 100% owner of our company***. As signatory on every appraisal, nothing is sent to a client without my writing and review. Along with my CPA and MS in Accounting, training, and ongoing education, I also completed the full education courses for all three personal property appraisal organizations along with 400+ hours of continuing education. As a CPA who has produced many business valuations, the valuing of personal property assets is quite similar to the Market Value of depreciable assets under FAS 157. ***Our team's overriding goal is to ensure 100% compliance with IRS, appraisal organization, and USPAP compliance.***

There is no licensure, either state or federal, for personal property appraisers. There are standards set forth by the IRS but the education and experience requirements have had the proverbial truck driven through them. **Experience producing erroneous appraisals for decades does not an IRS Qualified Appraiser make.** To practice as a CPA, I had to obtain a master's degree and then sit for a two day grueling CPA examination, in four sections, which I am proud to say I passed all four on the first go-round, mostly because I never wanted to take that test again. Taxpayers have no such standard upon which they can judge an appraiser.

Longevity in this industry does not equate with expertise and competence. There are <u>no licenses or specific certifications for deconstruction appraisers</u>, architectural reuse appraisers or any other name for these types of

appraisals. Additionally, claiming to have had zero audits in decades of appraisal production is an inaccurate claim. Clients not appraisers are audited. Clients may not inform the appraiser if they are audited. Given the high number of retrospective appraisals we produce, there have been plenty of disallowed deconstruction appraisals, further detailed below.

Personal Property Appraisal Organizations

However, there are three personal property appraisal organizations who sponsor the congressionally organized Appraisal Foundation, a nonprofit helping to heighten appraiser education and standards. They also promulgate USPAP, the Uniform Standards of Professional Appraisal Practice. At a minimum, **ensure your appraiser is an accredited member of one of the following organizations.** If they are not, ask them why. Sound valuation methodology reaches across appraisal disciplines and the foundational valuation concepts offered by these organizations cannot be learned without rigorous study and examinations.

American Society of Appraisers (ASA)
Appraisers Association of America (AAA)
International Society of Appraisers (ISA)

What is the Correct Valuation Methodology?

There are three valuation methods to be applied when appraising. Each must be considered in an appraisal with the appraiser determining if one or more applies to the given assignment. These include:

Sales Comparison Approach (Market-based Approach)
Cost Approach
Income Approach

The Sales Comparison Approach is used for the **overwhelming majority** of all personal property appraisals prepared to substantiate an income tax deduction for a charitable contribution. This method includes the research and documentation of consummated sales and offers of sale for comparable property in a relevant time frame and in the relevant market.

The Cost Approach estimates the replacement cost of property and is used primarily for insurance appraisals.

The Income Approach calculates the present value of future cash flow from income producing property and is typically used for financial planning and business valuation purposes.

The Sales Comparison Approach should be used for the vast majority of appraisals for charitable contributions as taught by the three organizations. Arguing against this would run parallel to a CPA arguing that the definition of accrual accounting does *not* mean that income must be recognized when earned or expenses when incurred. Using other methods as a shortcut to a faster or inflated appraisal contradicts the decades-long approaches of accredited appraisal organizations and valuation theory. Other approaches also lack common sense, and can lead to disallowed deductions, fines, and later repayment of tax benefits.

Important Tax Court Cases

In the recent *Mann v. United States* case, the federal court of appeals set important precedent in determining how deconstructed and donated building materials, furnishings, and fixtures should be valued in line with IRS defined *Fair Market Value*. Along with proper and accurate valuation comes two equally important issues: what does and does not constitute an IRS defined *Qualified Appraisal* and *Qualified Appraiser*? We first provide an overview of deconstruction and its tax implications, and then address the impact of the *Mann* case.

The *Mann* case provides several examples of what not to do to obtain a *Qualified Appraisal*. In *Mann*, the appraiser did not produce a *Qualified Appraisal*, with the appeals court providing the following analysis:

> *Finally, the $313,353 appraisal used to claim the deduction was not a qualified appraisal of the contributed property under 26 U.S.C. § 170(f)(11)(C). See 26 C.F.R. § 1.170A-13(c)(3)(ii)(I). The appraisal assumed that every component of the house would be severed and donated to Second Chance for reuse. Based on that assumption about the property contributed and recognizing that many of those components lacked a resale market, the appraisal used a "cost approach to value." The appraiser determined the value of new and uninstalled versions of the building's components and depreciated that value by 17%, a value calculated based on the components having "60-years of economic life with an effective age of 10." The appraiser determined that this represented the*

components' current value based on the largely unexplained assumption that the 10-year-old materials, now cut to the appropriate size and installed in the house, were worth 83% of their new and uninstalled values. Aggregating the value of each such component — including substantial amounts even for the value of the house's foundation and drywall — the appraisal determined that the value of the entire house was $313,353, and that was the amount that the Manns claimed as a charitable deduction on their amended return.

The district court found this appraisal flawed because not every component was donated to Second Chance, stating that "a valuation of over $300,000 based on the extraction and resale of all building materials does not properly value the donation in light of the conditions placed on the conveyance." Mann , 364 F. Supp. 3d at 564; cf. Rolfs v. Comm'r, 668 F.3d 888, 895 [109 AFTR 2d 2012-828] (7th Cir. 2012) (disallowing deduction based on taxpayers' donation of a house to a local fire department for the house's destruction in a training exercise where "[n]one of the value of the house, as a house, was actually given away"). The court did note that a "proper way" to value the donation would have been "based on the resale value of the specific building materials and contents" that Second Chance removed from the premises. Mann, 364 F. Supp. 3d at 564. The appraisal never provided the IRS with an estimate of the value of those materials.

There are several important takeaways from this case. First, the appraiser used the cost approach to value claiming there was not a resale market, which is false. Second, the appraiser made the "unexplained assumption" about the life of the materials in their current installed form. Third, the appraiser aggregated the value of each component calculated using software and included amounts for foundation and drywall which were never donated. Finally, the court did not find their valuation method proper because it was not "based on the resale value of the specific building materials and contents."

Chirelli v. Commissioner, T.C. Memo 2021027 March 3rd, 2021, is another tax court case in which a taxpayer lost their non-cash charitable contribution due to lack of substantial compliance by the appraiser in producing an IRS Qualified Appraisal. There are important takeaways from this case to help protect taxpayers from losing their deductions and the subsequent paying of fines and interest should their appraisals not meet IRS standards. **The IRS is serious about ensuring appraisers comply with the Internal Revenue Code and adhere to the strict definition of both Qualified Appraiser and Qualified Appraisal.**

Please find a copy of the case text here:
https://casetext.com/case/chiarelli-v-commr-1

1. Like *Loube v. Commissioner,* 2020, Form 8283 was not filled out completely and signed by the taxpayer, nonprofit and appraiser. (See link for full case text: https://casetext.com/case/loube-v-commr)

2. One of the appraisals grouped items into general categories without specifically describing them. As appraisers, one of our primary functions is to observe and identify what we are appraising. Accurate and detailed descriptions do just that. The case notes that the taxpayer did "not otherwise provide reliable written records credibly identifying the individual items donated, their values or condition, the manner of acquisition, the donation dates, or his bases in the property."

3. The condition was also not specified, with a general category of "excellent" noted. Again, the appraiser did not back-up their work.

4. The Contemporaneous Written Acknowledgement letter (CWA), receipts, and accompanying substantiation were found lacking.

Choosing the wrong appraiser can compromise not just the tax deduction but trigger underpayment fines and penalties. There is an accuracy penalty assessed to the appraiser at times, but the major negative implications hit the taxpayer.

John D. Russell, J.D. of The American Society of Appraisers offers a great write-up of the case here:
https://www.appraisers.org/docs/default-source/discipline_pp/recent-court-case-illustrates-importance-of-retaining-qualified-appraisers.pdf?sfvrsn=9d7e6ad4_4

Peter J. Reilly with Forbes also offers an insightful look at the Chirelli case:
https://www.forbes.com/sites/peterjreilly/2021/03/07/with-large-charitable-contributions-aim-for-more-than-substantial-compliance/?sh=c0e65247d232

What Makes an Accurate Appraisal?

<u>Step One:</u> *Literal Description*—The first step to be taken is for an appraiser to give a literal description of the donated property. Let's take the example of a donated door. A literal description of the door would be:

> *Six-panel door, manufactured of pine and painted white, having a solid core with six beveled frames, devoid of hardware and without inclusion of the door jamb. Dimensions: 80"H x 36"W. The door is in overall good condition with noted signs of chipped paint along the bottom.*

<u>Step Two:</u> *Comparable Sales*—The appraiser should present comparable sales to substantiate their concluded value. In this case, a comparable sale could be included with the following description:

> *Comparable 1: This is a sale of a similar six-panel door, also in pine but having an unfinished rather than painted exterior. The door has the same dimensions and is in used good condition, with similar wear evident along the interior*

*edges. The sale occurred at **Sample Retail** on 12/31/20 for $105. The sale included antique style brass hardware including a knob and hinges as well as the door jamb.*

<u>Step Three:</u> *Adjustments to Value*—The appraiser then makes adjustment to the comparable sale to conclude final value.

In concluding value, I considered this sale as relevant due to the following factors: The door is of similar dimensions and the lack of paint does not appear to affect value after a review of other comparable sales. The door is in similar condition to the appraised but requires adjustments downward due to the inclusion of hardware, hinges, and a door jamb. The sale occurred within close proximity to the effective valuation date. The appraised value is adjusted downward to $85.

Then, a copy of the comparable sale should be included within the appraisal.

This is a simple example. Some properties require the review of many comparable sales to conclude value with lengthy descriptions and detailing of comparable property characteristics. However, the valuation methodology, which requires researching consummated sales on the open market and making adjustments to value, is the same whether we are appraising this door or a Louis XVI fauteuil.

Additionally, **current market conditions** need to be researched and documented. This is especially pertinent in the economically volatile times in which we currently find ourselves. Modern art prices has proven to be inelastic on the auction market but furniture from the French Empire style has taken a dive. It is a great time to procure a Napoleonic Egyptian style bureau plat!

How do you know if Your Appraiser is Qualified?

1. Check the appraiser's education. IRS counsel presenters have communicated that they often first review the appraiser's CV to determine education and competence. Ask the following questions:

    a. What level of college education does the appraiser hold and in what subject? Does that subject lend itself to valuation methodology?

    b. From which of the three personal property appraiser organizations did the appraiser complete their education? **Per above, there is no license or certification for deconstruction or reuse appraisers.** The three personal property appraisal organizations sponsoring The Appraisal Foundation are:

i. American Society of Appraisers (ASA)
ii. Appraisers Association of America (AAA)
iii. International Society of Appraisers (ISA)

c. Finally, ensure the appraiser is **accredited** with one of the three organizations. This means that they went through an appraiser education program, which included extensive coursework, exams, and appraisal reviews and includes extensive continuing education requirements.

2. Peruse the appraiser's website and review articles written by the company's appraisers. Check their social media for educational content. Review where they have presented their appraisal knowledge and established themselves as experts.

3. **Ask for a sample appraisal** and review the following:

   a. Do they use correct valuation methodology? In 99% of personal property appraisals, the market-based or Sales Comparison Approach should be used.

   b. How many comparable sales do they review for each piece of property? Do they include the comparable sales data within the report?

   c. Do they provide a larger macroeconomic market evaluation along with the microeconomic evaluation for the property's specific market?

   d. Review the appraiser's CV. As stated above, determine their level of education and accreditation to ensure they comply with the IRS definition of a Qualified Appraiser. What continuing education courses have they completed?

4. The appraiser or owners of the firm must not be precluded from preparing appraisals for the IRS as detailed in IRS Circular 230, found here:

   https://www.irs.gov/pub/irs-pdf/pcir230.pdf. Appraisers prepare documentation "relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service." They are held to the same standards as attorneys, CPAs and other enrolled agents presenting documentation to the IRS. It sounds obvious but a quick criminal record check never hurts.

§ 10.51 Incompetence and disreputable conduct.

(a) *Incompetence and disreputable conduct.* Incompetence and disreputable conduct for which a practitioner may be sanctioned under §10.50 includes, but is not limited to —

5. Ensure the appraiser was not involved in the two tax court cases: *Mann v. US*, and *Loube v. Commissioner.*

Here is a link to Publication 561 from the IRS with the definition of Qualified Appraisers and Qualified Appraisals. Per the standards, the appraiser needs college or equivalent relevant education and training in the type of appraisals being completed. Expansive education is found through the three personal property education organizations AAA, ASA, and/or ISA. There is no on-the-job training commensurate with this standard or training through a deconstruction trade organization that meets the IRS definition:

https://www.irs.gov/publications/p561#en_US_201911_publink1000258036

IRS Appraisals

Perhaps it is my nineteen years as a CPA that have drummed into my head that the IRS needs substantiation for *everything*. The appraisals we produce at The Green Mission Inc. are laid out like detailed research papers, walking the IRS through our evaluation of the current market and arguing our cases for the values we assign to every single piece of property. We leave nothing to the imagination.

Donating building materials, appliances, fixtures, furnishings and other home contents can be a tax savvy strategy to lower taxes while contributing to worthy organizations and keeping waste from landfills.

Contact our offices with questions about your potential deconstruction donation. We provide a quoted value range, without charge, based on a review of comparable sales, to help you make an informed choice when choosing deconstruction over demolition. We can also send a sample appraisal demonstrating our detailed and extensive research conducted for our clients.

Please reach out to our Director of Business Development, Jennie Lumpkin:
Jennie@TheGreenMissionInc.com, (540) 322-3884.

References:

IRS form 8283: https://www.irs.gov/pub/irs-pdf/f8283.pdf

IRS Qualified Appraisal and Qualified Appraiser criteria:
https://www.irs.gov/publications/p561

The Appraisal Foundation: https://www.appraisalfoundation.org/

USPAP:
https://www.appraisalfoundation.org/imis/TAF/Standards/Appraisal_Standards/Uniform_Standards_of_Professional_Appraisal_Practice/TAF/USPAP.aspx

American Society of Appraisers: https://www.appraisers.org/

Appraisers Association of America: https://www.appraisersassociation.org/

International Society of Appraisers: https://www.isa-appraisers.org/