**The Perils of a Discredited Appraisal**
**Critical Insights on *Kollsman v. Commissioner***

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A US Tax Court ruling has brought the perils of a discredited art appraisal into sharp focus. In the *Estate of Kollsman v. Commissioner,* the court rejected a premiere auction house appraisal for bias and absence of objective support. Relying almost exclusively on the IRS expert, the court concluded a $2,400,000[1] value for the disputed artwork.

*Kollsman* illustrates that preeminence in the auction business, or in another art-related profession, is not adequate assurance of appraisal expertise or competency. As Keith Fogg thoughtfully covered in a previous *Procedurally Taxing* blog post, an expert who has or is seeking any involvement in the sale or purchase of the subject of an appraisal can signal an obvious and avoidable conflict of interest.

Beyond bias, this post explores exposure in failing to select a relevantly credentialed expert, who will submit fully supported, impartial testimony and reports, allowing their opinions to be confidently embraced by the IRS and the courts. Those who practice tax law where the value of art is at issue may be held liable for failing to secure a qualified expert who can competently support contested value. Therefore, lawyers offering estate planning services should be familiar with established, meaningful, credible and defined appraiser qualification criteria when vetting personal property appraisal experts.

In contrast to the disregarded expert witness offered by the estate in Kollsman, the IRS expert whose opinion prevailed and was found qualified[2] was a properly credentialed appraiser. Credentialed appraisers are trained and tested in appraisal standards, ethics and methodology, have had sample reports vetted through peer review, and are more likely to submit a full and impartial expert analysis.

In rejecting the appraisal offered by the estate in Kollsman as "unreliable and unpersuasive", the court found profound deficiencies in competency as well as independence:

- **Absence of comparable market data**: The court found it "remarkable" that the opinion was not supported by the comparable sales price data consistently found to be significant in prior cases, or that "any objective support" was offered to support the valuation figures. "He effectively urges the Court to accept them on the basis of his experience and expertise. We have no basis for doing so".
- **Exaggerated discount for condition.** In rejecting the wholly unsupported opinion of diminution of value based on condition, the court believed any reasonable investigation of condition impacts on value would, at a minimum, include an opinion from a qualified conservator.
- **Direct conflict of interest:** The expert provided his fair market value estimates simultaneously with a solicitation for exclusive rights to auction the paintings if they were to be sold. The court found this to be a "significant conflict of interest that could cause a reasonable person to question his objectivity".
- **Direct financial incentive**: The court believed the expert was acting with incentive to undervalue estate tax liability in exchange for an agreement to benefit from selling the property. Judge Gale's language was strong on this point, finding: "a direct financial incentive to curry favor" by providing "*lowball* estimates that would lessen the Federal estate tax burden borne by the estate".

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[1] The estate valued the artwork at $600,000, the IRS at $2,600,000. In affording the estate testimony and report "very little weight", the court applied a modest discount to the IRS opinion, concluding value at $2,400,000.
[2] The appraisal credential of the IRS expert in *Kollsman* was referenced in the opinion.

**The Appraisal Foundation's 2018 Personal Property Appraiser Qualification Criteria**

The appraisal of art is a recognized professional discipline, distinct from other types of art market expertise, with clearly defined credentialing standards. When engaging an art appraisal expert it's critical to assert the same diligence employed in engaging any other expert witness, which includes understanding the professional criteria specific to the discipline of appraising.

In the United the States, The Appraisal Foundation (TAF) is the foremost authority on the valuation profession. Under the *Financial Institutions Reform, Recovery, and Enforcement Act* (FIRREA), Congress authorized The Appraisal Foundation as the source of appraisal practice standards and qualifications. TAF's Appraiser Qualifications Board (AQB) is responsible for developing appraiser qualification standards for the real estate, personal property and business valuation professions. TAF's Appraisal Standards Board (ASB) issues and updates The Professional Standards of Professional Appraisal Practice (USPAP). Together these standards and practices help ensure a trustworthy level of professional competency. After five years of research and analysis, including input from the credentialing sponsoring organizations, the TAF issued an updated and more stringent Personal Property Appraiser Qualification Criteria, which is in effect as of January 1, 2018.

TAF sponsoring professional personal property organizations are required to adhere to these criteria when credentialing members. The International Society of Appraisers, The Appraisers Association of America, and The American Society of Appraisers maintain public online registries where the expert's specialization, level of credentialing and current USPAP compliance may be accessed and confirmed.

## Suggested Standards of Professional Responsibility in Vetting Appraisers and Expert Reports

1. **Require a current credential issued by one of the three TAF sponsoring personal property appraisal organizations.** Members of the qualifying organizations earn their credentials through a rigorous admissions, training and testing process. They are required to comply with IRS and TAF/AQB guidelines, adhere to a code of ethics, are subject to oversight, and continuing education requirements. Before attaining Accredited or Certified status, members must submit appraisal reports to a stringent peer review process. These qualifications support competency, accountability and a commitment to professionalism. Consult the public registries of the qualifying organizations to ensure current credentialing. The International Society of Appraisers, the Appraisers Association of America, and The American Society of Appraisers

2. **Appraisal reports should be well-supported.** Every appraisal submitted to assist in determining tax liability has the potential to become the subject of litigation. The IRS Art Appraisal Services[2] is staffed by TAF credentialed appraisers tasked with protecting the public from abuse in valuation resulting from inadequately supported appraisal reports.

   Reports for objects of significant value should be supported by comparable sales data, relevant expert opinions, and a well-reasoned objective justification for each value conclusion. In response to IRS guidance, this is a required reporting component of all three TAF qualifying organizations for any object valued above $50,000. At a minimum, all appraisal reports should also disclose the approach to valuation and methodology employed, intended use, definition of value, markets explored, any conditions limiting assignment results, extraordinary assumptions, and scope of work.

3. **Appraisal reports should be comprehensive.** IRS Publication 561, *Determining the Value of Donated Property*, outlines a *Preferred Object Identification Format for Art*[3] *Valued over $50,000*. The appraisal must

3 The IRS Art Appraisal Services is distinct from the IRS Art Advisory Panel. The members of the Art Advisory Panel are renown art experts, scholars and gallerists who serve without compensation. The IRS Art Appraisal Services is part of the Office of Appeals, staffed by TAF qualified appraisers.

4 On this document the IRS defines "Art" as including paintings, sculptures, watercolors, prints, drawings, ceramics, antiques, decorative arts, textiles, carpets, silver, rare manuscripts, historical memorabilia, and other similar objects.

include professional quality photographs, and contain a complete physical description of the object, including size, materials or medium, subject matter, name, nationality and life dates of the artist, signatures or other identifying inscriptions or markings, date of creation, provenance (history of ownership), condition, literature references and exhibition history. The IRS also expects the appraiser to exercise due diligence in confirming authenticity.

4. **Appraisals submitted to the IRS should address how the appraiser meets the IRS Appraiser Qualification Criteria, and acknowledge civil liabilities associated with a grossly inaccurate valuation.** The Pension Protection Act of 2006 ((PPA), P.L. 109-280, at §170(f)(11)(E)), codified the definition of a qualified appraiser and qualified appraisal report. The PPA strengthened the professional requirements a qualified appraiser must meet, specifically identifying organizational credentials, experience, and professional-level coursework. All IRS appraisals are required to include a statement of how the appraiser meets the IRS qualification criteria.

5. **Appraisals should include a signed and dated certificate of compliance with the Uniform Standards of Professional Appraisal Practice (USPAP).** This certification must disclose conflicts or bias to the subject property or parties and confirm that the assignment was not predicated on a pre-determined result. The certification should include a statement that the appraiser is compliant with the current version of USPAP (2018-19)

6. **The Uniform Standards of Professional Appraisal Practice (USPAP) is not a credential.** USPAP sets critical ethics and reporting standards, but it is not a credential. An individual who promotes as "USPAP Certified" displays a superficial understanding of the standards of their own profession, because USPAP does not certify. The qualifying personal property organizations issue credentials. USPAP training and compliance is a 15-hour foundational course with a 7-hour bi-annual continuing education requirement. It is a required, but rudimentary component in achieving and maintaining a TAF/AQB compliant credential.

7. **Experts should be objective and disinterested.** The PPA specifically disqualifies individuals who would have a conflict of interest in the outcome of the appraisal. An expert should do nothing that would cast doubt on the impartiality of their opinion. Experts with a past, present or potential future interest in the appraised property should be avoided.

8. **Contingent fees are prohibited by USPAP.** The Ethics Rule of USPAP prohibits contingent fees without exception. An appraiser must not accept an assignment, or have a compensation arrangement for an assignment, that is contingent on a predetermined value result, based on a percentage of value, or attainment of any advantage (e.g., the appraiser will broker or sell the subject property).

In summary, preeminence in art sales or other art-related professions is not assurance of appraisal expertise or competency. In fact, an expert's involvement in the sale and purchase of the subject artwork can undermine the perception of objectivity. Further, to manage the risk of a disqualified expert, appraisers should meet recognized professional standards for qualification and competency, including active credentialed membership in one of the three TAF qualifying organizations.

Professional Qualification Criteria for Personal Property Appraisers are developed by The Appraiser Qualifications Board of The Appraisal Foundation. The standard is rigorous, meaningful, easily accessible to opposing parties, and is clearly defined. TAF/AQB qualification is the accepted minimum professional standard. The three major appraisal organizations (TAF Sponsors) have united in a collaborative effort to inform the public of meaningful qualification standards. The Appraisal Foundation is in the process of developing a public campaign to promote these standards. Increasingly, it will be difficult for allied professionals to credibly overlook the qualifying standard of experts they customarily engage.

In the wake of Kollsman, it is critical for tax lawyers who rely on expert appraisals to be familiar with appraiser qualification and reporting standards. Assertively vetting experts illustrates an advanced level of diligence, providing a critical, and often overlooked layer of protection for the clients we mutually serve.

**About the Author:** Cindy Charleston-Rosenberg, ISA CAPP, is a past President and Certified Member of the International Society of Appraisers (ISA), the largest professional organization of qualified appraisers in the United States and Canada. She is an experienced expert witness and writes and presents widely on advanced appraisal methodology issues. Cindy has won numerous awards for her thought leadership in the personal property appraisal profession and currently serves as Chair of ISA's Specialty an Advanced Studies Committee. She is active in industry activities to raise awareness of the critical importance of meaningful appraiser qualification standards.