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## MEMORANDUM

To: Mark Judge, Office of Exemption Determinations (OED)  
Employee Benefits Security Administration  
U.S. Department of Labor

From: Peter Barash<sup>1</sup>  
Legislative & Regulatory Government Relations Consultant To  
The American Society of Appraisers

Date: July 21, 2011

Subject: Recommended Changes to the Valuation Provisions of OED's Rulemaking On  
Prohibited Transaction Exemption Procedures

On behalf of my client, the American Society of Appraisers (ASA), I greatly appreciate the opportunity to provide several informal – but I believe extremely important – comments on the proposed rulemaking referenced above. ASA is the nation's leading multi-discipline professional appraisal organization. It teaches, tests and credentials its members for professional appraisal practice in the areas of business valuation, commercial and residential real property and in personal property valuation (including fine arts and machinery and technical specialties). ASA has worked closely and successfully with many federal agencies over the years (including IRS in

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<sup>1</sup> By way of personal background, my firm, Peter Barash Associates, has provided government relations services for a number of years to ASA on legislation and regulation which impact the appraisal profession. I have been providing those services since I left Capitol Hill as Staff Director of a major House Subcommittee with jurisdiction over financial services issues, including valuation. I was the principal drafter of legislation to professionalize appraisal practice in federally-related transactions, which became Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA). Title XI, among other things, established a requirement that real estate appraisers must be state licensed or certified and adhere to the Uniform Standards of Professional Appraisal Practice (USPAPA) as preconditions for providing their services to the federal government.

connection with tax-related valuations), to improve the reliability and integrity of valuations in federally-related transactions.

If you conclude that the comments and recommendations in this Memorandum are worth further exploration, I am authorized to state that ASA's leadership would be pleased to meet with you; and, given the relevancy to your rulemaking of uniform valuation standards and appraiser qualifications, you might consider meeting with representatives of The Appraisal Foundation: the not-for-profit federally recognized organization which promulgates the Uniform Standards of Professional Appraisal Practice (USPAP) and professional appraiser qualifications.

As you may know, ASA submitted written comments to EBSA and testified at EBSA's hearing in strong opposition to its proposed "appraiser-as-fiduciary" rule. ASA's comment letter and hearing testimony proposed an alternative approach to improving the quality and reliability of ESOP-related valuations – an approach that is widely and successfully utilized throughout the federal government. Of particular interest to us was that the basics of this alternative approach (reliance on Qualified Appraisers to ensure valuation competency and on Qualified Appraisals to ensure that those performing them adhere to generally-accepted standards of practice) were already incorporated in your proposed rulemaking on "Prohibited Transaction Exemption Procedures."

ASA observed in its comments and testimony that with a very few perfecting changes to the exemption procedures rule – changes which we believe are totally consistent with its letter and spirit – the resulting appraisal reform system could also work effectively for all ERISA required valuations. ASA's praised the thrust and many of the details of the proposed exemption procedures rulemaking; but did suggest several important changes to the proposal that we believe are necessary to more effectively protect the interests of pension plan beneficiaries.

Regrettably, ASA was so focused on the "appraiser-as-fiduciary" rulemaking that we failed to communicate our suggestions directly to the Office of Exemption Determinations in connection with its rulemaking. Nevertheless, given the importance of our suggested changes – which we believe will substantially improve the rulemaking and are necessary to conform it to existing federal law as well as the appraisal reform systems in place throughout the government (including specifically the IRS which shares ERISA enforcement responsibility with EBSA) we hope and trust that your Office will be able to consider them. An outline of our suggested changes – respectfully submitted – follows:

**I. OED's Proposed Definition of "Qualified Independent Appraiser" Fails To Require The Use Of A State Certified Or State Licensed Appraiser For Valuations of Real Estate; And Its Qualification Requirements For Other Categories of Property Needs To Be Strengthened**

(A) **REAL PROPERTY**: ASA recognizes that appraisals covered by ERISA's prohibited transaction exemption requirements can involve major categories of property other than real estate and real property. While OED's proposed definition of "Qualified Independent Appraiser" contains many of the elements included in the professional appraiser requirements of IRS and other federal agencies, it fails to require the use of state certified and state licensed appraisers to value real property – a central and indispensable component of real property valuation requirements throughout the rest of the federal government. Virtually all other federal agencies with responsibility for overseeing real estate valuations require that they be performed only by individuals who are state licensed or certified.

IRS' iteration of this state certification/licensing requirement can be found in SECTION 3.03(3) of its Notice 2006-96 (issued November 13, 2006; Part III – Administrative, Procedural, and Miscellaneous; the entire IRS Notice is attached to this Memo). This provision requires that for tax returns filed after October 19, 2006, real estate appraisals must be performed by an "appraiser [who] is licensed or certified for the type of property being appraised in the state in which the appraised real property is located." The phrase, "for the type of property being appraised" is used for the purpose of distinguishing between various subcategories of real property appraisal (e.g., commercial properties; residential properties; complex real estate properties).

We acknowledge and appreciate the provision in the exemption procedures proposal that an individual performing a real property appraisal "...shall submit a written representation that he or she is a member of a professional organization of appraisers that can sanction its members for acts of malfeasance." While ASA is supportive of this provision with respect to non-real property appraisal disciplines, it has very limited relevancy in a world with real property appraiser licensing systems in the 50 states and territories (these state licensing agencies supervise the conduct and competency of their licensees; and sanction them for USPAP violations or other misconduct). A requirement that real estate valuations in connection with exemption transactions only be performed by state licensed or certified appraisers is a much more effective protection for pension beneficiaries, as general matter, than the currently proposed provision. It is especially superior because about 75% of the nation's real estate appraisers (all of whom are state licensed or certified) are not members of any "professional appraisal organization" and could not, therefore, be sanctioned by them.

On the other hand, virtually all professional appraisers who practice in the business valuation or personal property arenas are members of professional appraisal organizations, like ASA and others, which credential them for professional appraisal practice. These individuals can be sanctioned – and are sanctioned – by the professional appraisal organizations which award designations based on demonstrated competency and adherence to ethics requirements.

**(B) PROPERTY OTHER THAN REAL PROPERTY:** While we believe the proposed rule's "Qualified Independent Appraiser" definition for non-real property valuations has merit, we also believe that pension plan beneficiaries would be far better protected from unreliable appraisals if the definition was strengthened.

The definition, as proposed, requires that a "Qualified Independent Appraiser" "must represent in writing its qualifications to serve in that capacity.... and must demonstrate that he/she has experience in valuing assets of that type." We also recognize, however, that the definition does not establish any objective standards regarding qualifications and experience. Under the proposed definition, an individual can simply self-represent (based on subjective criteria) that he or she is qualified to value the particular type of property at issue. By contrast, IRS Guidance for valuations of non-real property for non-cash charitable contributions (and for other Income and Estate tax purposes) sets forth specific and objective appraiser qualification requirements, as follows:

IRS Notice 2006-96 states, in pertinent part, that:

"The term 'Qualified Appraiser' means an individual who (1) has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the Secretary... [A]n individual will not be treated as a qualified appraiser unless that individual (1) demonstrates 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...at any time during the 3-year period ending on the date of the appraisal."

The proposed definition of "Qualified Independent Appraiser" in the exemption procedures rule contains elements similar to those in the IRS Guidance; but, we believe the IRS definition requires a more objective and reliable demonstration of competency to value a particular category of property.

## **II. OED's Proposed Definition of a "Qualified Appraisal Report" Fails To Require Adherence To Generally-Recognized Appraisal Standards (i.e., USPAP)**

We believe that the absence of any requirement in the proposed prohibited transaction exemption proposal that appraisers adhere to generally-accepted appraisal standards is an extremely serious omission. Merely requiring that the appraiser "describe the methods used in determining fair market value" is insufficient to ensure that the appraiser is adhering to

generally-recognized valuation standards of care and practice. All professional appraisers in any discipline is required to adhere to generally-recognized valuation standards. That means the Uniform Standards of Professional Appraisal Practice (USPAP) or standards that are fully consistent with the substance and principles of USPAP. IRS's qualified appraisal requirements spell this out, as follows:

#### IRS "Qualified Appraisal" Standards

"An appraisal will be treated as a 'Qualified Appraisal'...if the appraisal complies with all the requirements of Section 1.170A-13(c) of the existing regulations...and is conducted by a qualified appraiser in accordance with generally accepted appraisal standards... An appraisal will be 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 (USPAP), as developed by the Appraisal Standards Board of the Appraisal Foundation."

Unless your final regulations require adherence to USPAP's uniform appraisal standards, some individuals may be tempted to pick and choose standards that are most likely to produce a desired fair market value outcome. Moreover, a requirement for adherence to uniform appraisal standards requirement is most likely to permit successful enforcement actions against those who violate such standards. Adherence to USPAP is required of all state licensed/certified real estate appraisers as well as by those with designations from professional appraisal organizations; and most sanctions applied by state licensing agencies and by the professional organizations are based on USPAP violations.

As stated above, ASA appreciates the very important steps taken by the Office of Exemption Determinations, in its rulemaking proposal, to improve the reliability and integrity of appraisals performed in connection with the exemption procedures. At the same time, however, we are concerned that it falls short in a couple of very important areas. We believe that with a handful of easily accomplished changes, the final regulations will much more effectively protect the interests of pension plan beneficiaries.

## Part III - Administrative, Procedural, and Miscellaneous

### Guidance Regarding Appraisal Requirements for Noncash Charitable Contributions

Notice 2006-96

#### SECTION 1. PURPOSE

This notice provides transitional guidance relating to the new definitions of “qualified appraisal” and “qualified appraiser” in § 170(f)(11) of the Internal Revenue Code, and new § 6695A of the Code regarding substantial or gross valuation misstatements, as added by § 1219 of the Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (2006) (the “PPA”).

The Service and the Treasury Department expect to issue regulations under § 170(f)(11). Until those regulations are effective, taxpayers may rely on this notice to comply with the new provisions added by § 1219 of the PPA.

#### SECTION 2. BACKGROUND

A deduction for charitable contributions is generally permitted under § 170(a), subject to certain limitations depending on the type of taxpayer, the nature of the property contributed, and the type of donee organization. Section 170(f)(11), as added by § 883 of the American Jobs Creation Act of 2004, Pub. L. No. 108-357, 118 Stat. 1418 (2004), contains reporting and substantiation requirements relating to the allowance of deductions for noncash charitable contributions. In particular, under § 170(f)(11)(C), taxpayers are required to obtain a qualified appraisal for donated

property for which a deduction of more than \$5,000 is claimed. Under § 170(f)(11)(D), in certain cases the qualified appraisal must be attached to the tax return. For appraisals prepared with respect to returns filed on or before August 17, 2006, existing Treasury Regulations provide a definition of the terms “qualified appraisal” and “qualified appraiser” for purposes of § 170(f)(11).

Section 1219 of the PPA amends § 170(f)(11)(E) and provides statutory definitions of a qualified appraisal and qualified appraiser for appraisals prepared with respect to returns filed after August 17, 2006.

Section 170(f)(11)(E)(i) provides that the term “qualified appraisal” means an appraisal that is (1) treated as a qualified appraisal under regulations or other guidance prescribed by the Secretary, and (2) conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance prescribed by the Secretary.

Section 170(f)(11)(E)(ii) provides that the term “qualified appraiser” means an individual who (1) has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the Secretary, (2) regularly performs appraisals for which the individual receives compensation, and (3) meets such other requirements as may be prescribed by the Secretary in regulations or other guidance. Section 170(f)(11)(E)(iii) further provides that an individual will not be treated as a qualified appraiser unless that individual (1) demonstrates 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 by the Secretary under § 330(c) of Title 31 of the United States Code at any time during the 3-year period ending on the date of the appraisal.

Section 1219 of the PPA also adds a new penalty provision. If the claimed value of property based on an appraisal results in a substantial or gross valuation misstatement under § 6662, a penalty is imposed by new § 6695A on any person who prepared the appraisal and who knew, or reasonably should have known, the appraisal would be used in connection with a return or claim for refund.

### SECTION 3. TRANSITIONAL GUIDANCE

#### *.01 In general*

The Service and the Treasury Department expect to issue regulations under § 170(f)(11), as amended by the PPA. The terms in section 3 of this notice apply to contributions of property (other than readily valued property within the meaning of § 170(f)(11)(A)(ii)(I)) by individuals, partnerships, or corporations for which a deduction of more than \$5,000 is claimed on returns filed after August 17, 2006, and before the effective date of the regulations that the Service and the Treasury Department expect to issue. Until regulations are effective under § 170(f)(11), as amended by the PPA, an appraisal that meets the requirements of this notice shall be treated as a qualified appraisal for purposes of § 170(f)(11). The determination of whether an appraiser is qualified under section 3.03 of this notice must be based on the appraiser's qualifications as of the date the appraisal is made.

#### *.02 Transitional terms-qualified appraisal*



(1) *Qualified appraisal.* An appraisal will be treated as a qualified appraisal within the meaning of § 170(f)(11)(E) if the appraisal complies with all of the requirements of § 1.170A-13(c) of the existing regulations (except to the extent the regulations are inconsistent with § 170(f)(11)), and is conducted by a qualified appraiser in accordance with generally accepted appraisal standards. See sections 3.02(2) and 3.03 of this notice.

(2) *Generally accepted appraisal standards.* An appraisal will be treated as having been conducted in accordance with generally accepted appraisal standards within the meaning of § 170(f)(11)(E)(i)(II) if, for example, the appraisal is consistent with the substance and principles of the Uniform Standards of Professional Appraisal Practice (“USPAP”), as developed by the Appraisal Standards Board of the Appraisal Foundation. Additional information is available at <http://www.appraisalfoundation.org>.

.03 *Transitional terms – qualified appraiser*

(1) *Appraisal designation.* An appraiser will be treated as having earned an appraisal designation from a recognized professional appraiser organization within the meaning of § 170(f)(11)(E)(ii)(I) if the appraisal designation is awarded on the basis of demonstrated competency in valuing the type of property for which the appraisal is performed.

(2) *Education and experience in valuing the type of property.* An appraiser will be treated as having demonstrated verifiable education and

experience in valuing the type of property subject to the appraisal within the meaning of § 170(f)(11)(E)(iii)(I) if the appraiser makes a declaration in the appraisal that, because of the appraiser's background, experience, education, and membership in professional associations, the appraiser is qualified to make appraisals of the type of property being valued. See also § 1.170A-13(c)(5).

(3) *Minimum education and experience.* An appraiser will be treated as having met minimum education and experience requirements within the meaning of § 170(f)(11)(E)(ii)(I) if –

(a) *For real property*

(i) For returns filed on or before October 19, 2006, the appraiser is qualified as a “qualified appraiser” within the meaning of § 1.170A-13(c)(5) to make appraisals of the type of property being valued.

(ii) For returns filed after October 19, 2006, the appraiser is licensed or certified for the type of property being appraised in the state in which the appraised real property is located.

(b) *For property other than real property –*

(i) For returns filed on or before February 16, 2007, the appraiser is qualified as a “qualified appraiser” within the meaning of § 1.170A-13(c)(5) to make appraisals of the type

of property being valued.

(ii) For returns filed after February 16, 2007, the appraiser has (A) successfully completed college or professional-level coursework that is relevant to the property being valued, (B) obtained at least two years of experience in the trade or business of buying, selling, or valuing the type of property being valued, and (C) fully described in the appraisal the appraiser's education and experience that qualify the appraiser to value the type of property being valued.

*.04 Applicability of reporting and substantiation regulations*

*(1) In general*

The requirements of § 1.170A-13(c) of the existing regulations concerning qualified appraisals and qualified appraisers continue to apply to all taxpayers, including those to whom the transitional guidance in this section may apply, except to the extent the regulations are inconsistent with the provisions of § 170(f)(11). In particular, all taxpayers are required to comply with §§ 1.170A-13(c)(3), (c)(5), (c)(6) and (c)(7).

*(2) Revision to appraiser declaration*

For returns filed after February 16, 2007, the declaration required under § 1.170A-13(c)(5)(i) must include an additional statement that the appraiser understands that a substantial or gross valuation misstatement resulting from an appraisal of the value of property that the appraiser knows, or reasonably should have

known, would be used in connection with a return or claim for refund, may subject the appraiser to a civil penalty under § 6695A. See also § 1.170A-13(c)(3)(iii).

#### SECTION 4. REQUEST FOR COMMENTS

The Service and the Treasury Department invite comments containing suggestions for future guidance under § 170(f)(11), including regulations. In particular, comments are requested concerning the definition of the following terms: (1) "generally accepted appraisal standards" in § 170(f)(11)(E)(i)(II); (2) "appraisal designation from a recognized professional appraisal organization" in § 170(f)(11)(E)(ii)(I); (3) "minimum education and experience requirements" in § 170(f)(11)(E)(ii)(I); and (4) "verifiable education and experience in valuing the type of property subject to the appraisal" in § 170(f)(11)(E)(iii)(I). Comments also are requested on the potential impact any guidance under § 170(f)(11) may have on small businesses. Comments should refer to Notice 2006-96 and be submitted by January 17, 2007, to:

Internal Revenue Service  
P.O. Box 7604  
Ben Franklin Station  
Washington, D.C. 20044  
Attn: CC:PA:LPD:PR  
Room 5203

Alternatively, comments may be submitted electronically via e-mail to the following address: [Notice.Comments@irs.counsel.treas.gov](mailto:Notice.Comments@irs.counsel.treas.gov). All comments will be available for public inspection and copying.

#### SECTION 5. PAPERWORK REDUCTION ACT

The collections of information in this notice have been reviewed and approved by

the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545-1953.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collections of information in this notice are in section 3 of this notice. The collections of information are required from donors to satisfy the substantiation requirements of § 170(f)(11). The collections of information are required from donors to obtain a benefit. The likely respondents are individuals, partnerships, and corporations.

The estimated total annual reporting burden is 161,571 hours.

The estimated annual burden per respondent varies from 5 minutes to 5 hours, with an estimated average of approximately 3.5 hours. The estimated number of respondents is 46,285.

The estimated annual frequency of responses (used for reporting requirements only) is once per year.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and return information are confidential, as required by § 6103.

## SECTION 6. DRAFTING INFORMATION

The principal author of this notice is Susan J. Kassell of the Office of Associate Chief Counsel (Income Tax & Accounting). For further information regarding this notice contact Susan J. Kassell at (202) 622-5020 (not a toll-free call).