IN THE OREGON TAX COURT
MAGISTRATE DIVISION
Income Tax

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| DAVID A. GRADIN and BRENDA C. GRADIN, Plaintiffs, | ) | TC-MD 050026C |
| v. | ) | |
| DEPARTMENT OF REVENUE, State of Oregon, Defendant. | ) | **DECISION** |

At issue is the deductibility of a non-cash contribution made by Plaintiffs to a qualifying nonprofit organization in 2001. The appeal involves tax years 2001 and 2002, because there was a carryover from the 2001 deduction. Trial was held April 19, 2005. David Gradin (Gradin) appeared for Plaintiffs. Keith Shribbs (Shribbs) appeared for Defendant.

## I. STATEMENT OF FACTS

The property that formed the basis of the deduction is a 1,280 square foot, 1992 Guerdon manufactured home. The home was purchased in December 1991 by Rodney Gradin. The home was placed on a two-acre parcel and valued separately by the county assessor's office as personal property. Plaintiffs purchased the home from Rodney Gradin in January 1995 for $38,950.

Plaintiffs subsequently decided to build a stick-built home on their property. Building regulations required that the manufactured home be moved within 30 days of the final inspection of the new home. A local church was looking for a home for its pastor. Plaintiffs donated the property to the church on October 2, 2001. Plaintiffs do not attend the church to which the manufactured home was donated.

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As Gradin was preparing Plaintiffs' 2001 return in January 2002, he discovered that he needed an appraisal to establish the amount he could deduct for the contribution. Gradin contacted a realtor who opined that the tax assessment should be adequate for that purpose, but suggested he meet with an appraiser in the county assessor's office. Gradin met with Karla Hartenberger (Hartenberger), an "Appraiser 1" in the assessor's office. Gradin testified that Hartenberger researched the assessor's valuation records for the subject property and printed certain relevant information. Hartenberger then completed certain portions of Internal Revenue Service (IRS) Form 8283,[1] including the appraised fair market value (FMV) of the manufactured home, which she determined to be $48,240. Hartenberger's FMV estimate matched the real market value (RMV) in the assessor's ad valorem tax records ($48,240). Hartenberger signed the form, provided her title, indicating "Appraiser 1 Clackamas County," her address, and an appraisal date of February 13, 2002. Plaintiffs' Form 8283 provides a description of the home as "92 Guerdon home lic: X 216135, acct: 01504312." The condition of the home was reported as "very good." The form indicates that the donor (Plaintiffs) acquired the property January 30, 1995 by "purchase" for $38,950. The donee of the property, Fellowship Baptist Church, completed Part IV of the form on February 14, 2002.

Plaintiffs reported a total non-cash charitable contribution of $48,240, but due to limitations for charitable contributions in IRC section 170(b),[2] they spread that amount over two years, claiming $30,936 (rounded) on their 2001 return, and a carryover deduction of $17,304 on their 2002 return. Plaintiffs contend the county appraiser's value estimate and the assessment history for the home support the reported deduction.

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[1] See Plaintiffs' Exhibit 3-10.

[2] References to the Internal Revenue Code (IRC) are to 2001.

The assessor placed a RMV of $41,280 on the home for the 1995-96 tax year, which had a July 1, 1995, assessment date. ORS 308.210 (1993).[3] Plaintiffs appealed the 1995-96 tax assessed value of the home to the county board of property tax appeals (board). The assessor requested that the value be sustained, based on the sales of two similar manufactured homes for $51,400 and $52,500. (Ptfs' Ex. 7.) The board sustained the value. Plaintiffs appealed the board's decision to the Oregon Department of Revenue (department) and, prior to the hearing, the parties agreed to settle for a value of $37,000.[4] The county assessor increased the value of the home each year thereafter until tax year 2000-2001. The value that year was $48,240. The assessor placed the same value on the property for the following year (tax year 2001-02). (Ptfs' Ex. 6-1.)

Defendant audited the returns and disallowed the deductions for tax years 2001 and 2002. The IRS questioned the carryover deduction for 2002 and, after receiving additional information from Plaintiffs related to the 2001 return, including Form 8283, the IRS allowed the deduction.

Defendant insists Plaintiffs are not entitled to the deduction because they did not obtain a "qualified appraisal" to determine the fair market value of the property, as required by Treas. Reg. § 1.170A-13(c)(2)(A). In its Answer, Defendant argues that "[t]he IRS did not examine the 2001 federal tax return in regards to the non-cash charitable contribution of the [manufactured] home so the letter received by the plaintiffs from the IRS (EX 5) has no relevance on the matter before the court."

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[3] Oregon Revised Statutes.

[4] Plaintiffs contend that the department contacted them prior to the hearing and "offered" to settle based on a value of $37,000. However, the department's role was to determine the value of the property based on the evidence presented at the hearing, and the court assumes that the settlement offer was made by the assessor's office.

## II. ISSUE

Is a donor of property valued in excess of $5,000 absolutely required to obtain a qualified appraisal, and, if so, does the doctrine of substantial compliance entitle Plaintiffs to claim the deduction?

## III. ANALYSIS

### A. *Qualified Appraisal*

Internal Revenue Code (IRC) section 170(a)(1) allows a deduction for charitable contributions "only if verified under regulations prescribed by the Secretary." According to the regulations, the deduction is based on the FMV of the item at the time of the contribution. Treas. Reg. § 1.170A-13(c)(3)(ii)(I). Treas. Reg. § 1.170A-13(c)(1) requires substantiation of contributions exceeding $5,000, pursuant to the provisions in Treas. Reg. § 1.170A-13(c)(2).

The substantiation requirements set forth in Treas. Reg. § 1.170A-13(c)(2)(i), provide that "a donor who claims or reports a deduction with respect to a charitable contribution to which this paragraph (c) applies **must** comply with the following three requirements:

> "(A) Obtain a qualified appraisal (as defined in paragraph (c)(3) of this section) * * *.
>
> "(B) Attach a fully completed appraisal summary (as defined in paragraph (c)(4) of this section) to the tax return * * * on which the deduction for the contribution is first claimed (or reported) by the donor.
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> "(C) Maintain records containing the information required by paragraph (b)(2)(ii) of this section."

(Emphasis added.)

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The appraisal requirements are mandatory, as evidenced by a use of the word "must" in the regulation. The regulation comports with Congress's intent that the appraisal requirements be mandatory. The House Report for the Deficit Reduction Act of 1984 provides in relevant part:

> "[T]he conference agreement requires * * * that the treasury department must issue temporary or final regulations under section 170 before January 1, 1985 incorporating the substantiation requirements as set forth in this section of the conference agreement. Accordingly, pursuant to present law (sec. 170(a)(1)), which expressly allows a charitable deduction only if the contribution is verified in the manner specified by treasury regulations, *no deduction is allowed for a contribution of property for which an appraisal is required under the conference agreement unless the appraisal requirements are satisfied*."

HR Conf. Rep. No. 98-861, at 995 (1984) (emphasis added); *see Hewitt v. C.I.R.*, 166 F3d 332, WL 802042, at *2 (4th Cir 1998) (unpub'd op) (quoting conference report and concluding that appraisal requirement is mandatory). It is clear from the regulations that Plaintiffs were required to obtain a qualified appraisal.

A "qualified appraisal" is an appraisal document that is made at the time of the donation; is prepared, dated, and signed by a "qualified appraiser;" includes certain required information specified in paragraph (c)(3)(ii); and does not involve a prohibited appraisal fee. Treas. Reg. § 1.170A-13(c)(3)(i).[5] A "qualified appraiser" is an individual who "either holds himself or herself out to the public as an appraiser or performs appraisals on a regular basis [;]" is professionally qualified in terms of background, experience, education, etc., to make appraisals

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[5] The official definition of a "qualified appraisal" in Treas. Reg. section 1.170A-13(c)(3)(i) is as follows:

"(i) In general. For purposes of this paragraph (c), the term "qualified appraisal" means an appraisal document that –
"(A) Relates to an appraisal made not earlier than 60 days prior to the date of the contribution of the appraised property nor are later than the date specified in paragraph (c) (3) (iv) (B) of this section [the due date of the return on which the deduction is first claimed];
"(B) Is prepared, signed and dated by a qualified appraiser * * *;
"(C) Includes the information required by paragraph (c)(3)(ii) of this section; and
"(D) Does not involve an appraisal fee prohibited by paragraph (c)(6) of this section."

of the type of property being valued and sets out those qualifications in the appraisal; is not prohibited by paragraph (c)(5)(iv) from appraising the property [as the donor, donee, an employee of the donor or donee, etc.]; and is aware of the sanctions for making intentionally false or fraudulent overstatements of value. Treas. Reg. § 1.170A-13(c)(5).

The 11 specific items of information required by Treas. Reg. § 1.170A-13(c)(3)(ii) for a qualified appraisal include the following:

> "*Information included in a qualified appraisal*. A qualified appraisal shall include the following information:
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> "* * * * *
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> "(F) The qualifications of the qualified appraiser who signs the appraisal, including the appraiser's background, experience, education, and membership, if any, in professional appraisal associations * * * [,]
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> " * * * * *
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> "(J) The method of valuation used to determine the fair market value, such as the income approach, the market-data approach, and the replacement-cost-less-depreciation approach [,] and
>
> "(K) The specific basis for the valuation, such as specific comparable sales transactions or statistical sampling, including a justification for using sampling and an explanation of the sampling procedure employed."

(Emphasis in original.)

The regulations define an "appraisal summary" as "a summary of a qualified appraisal that (A) [i]s made on the form prescribed by the [IRS]; (B) [i]s signed and dated * * * by the donee * * *; (C) [i]s signed and dated by the qualified appraiser * * * ; and [i]ncludes [certain required information]." Treas. Reg . (4)(i)(A)(B)(C). The appraisal summary is just that; a summary of a complete appraisal made in accordance with the regulations.

Plaintiffs do not have a qualified appraisal. They have a Form 8283, which the IRS

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prescribed to be used as the appraisal summary. *See Jorgensen v. C.I.R*, TC-Memo 2000-38, WL 134332 (Feb 7, 2000). Plaintiffs attached Form 8283 to their 2001 return. As indicated above, the appraisal requirement is mandatory, and to universally accept the appraisal summary (Form 8283) in the place of a full-blown appraisal made by a qualified appraiser would render the regulatory requirement of an appraisal superfluous.

B. *Substantial Compliance*

Plaintiffs argue that they are entitled to the deduction based on the doctrine of substantial compliance, *citing Bond v. Commissioner of Internal Revenue*, 100 TC 32 (1993). Plaintiffs contend they have satisfied the regulatory substantiation requirements by submitting a copy of Form 8283, which is signed by a county appraiser who attested to a value of $48,240, and by providing a value history for the property from the county assessment and tax records. Defendant responds that Plaintiffs did not substantially comply: Plaintiffs' appraiser did not value the property, but rather merely certified the roll value, and there is no evidence Plaintiffs' appraiser was qualified under the regulations.

In *Bond*, the United States Tax Court analyzed the appraisal requirements in the treasury regulations under the doctrine of substantial compliance set forth in *Taylor v. Commissioner*, 67 TC 1071, 1077-1078 (1977), and concluded that "the reporting requirements are directory and not mandatory[,]" because they do not "relate to the substance or essence of whether or not a charitable contribution was actually made." *Bond*, 100 TC at 40-41. The taxpayers in *Bond* donated two airships (blimps) that had been appraised by an eminently qualified appraiser; however, the appraiser never completed a document sufficient to meet the definition of a qualified appraisal set forth in the treasury regulations. The appraiser inspected the airships and made written computations, calculations, and other notes in arriving at his $60,000 opinion of

value, although the appraiser subsequently misplaced his notes. *Bond*, 100 TC at 33-34. The appraiser completed Form 8283, which the taxpayers attached to their income tax return. In completing the form, the appraiser described the donated property, stated the property's value, summarized the overall physical condition of the property, and attested that he was not the donor, the donee, etc. The appraiser attested that he held himself out to the public as an appraiser qualified to make appraisals of the type of property being valued, and that the property was donated to a qualified recipient. During the federal audit process, the appraiser sent a letter to the IRS setting forth in detail his appraiser qualifications. *Id*. at 41. The court concluded that the taxpayers substantially complied with the applicable regulations and allowed taxpayers the full amount reported on their return. In arriving at that conclusion, the court stated that the taxpayers "* * * met all of the elements required to establish the substance or essence of a charitable contribution, but merely failed to obtain and attach to their return a separate written appraisal containing the information specified in respondent's regulations * * *." *Id*.

Four years after *Bond*, the United States Tax Court explained its holding in *Bond*, and, although it did not expressly overrule its earlier decision, the court narrowed considerably its view of the substantial compliance doctrine. In *Hewitt v. CIR*, 109 TC 258, 263-64 (1997), *aff'd* 166 F3d 332 (1998), the Tax Court stated that in *Bond*:

> "* * * we concluded that the reporting requirements of section 1.170A-13, Income Tax Regs, were directory, not mandatory, and therefore, that these requirements could be met by substantial, rather than strict, compliance. *Bond v. Commissioner*, 100 TC at 41. In effect, we held that the appraisal summary itself constituted the required appraisal. In this connection we note that the appraisal requirements may not be entirely procedural so as to justify the application of the substantial compliance rules under any and all circumstances. (Citation omitted. Emphasis omitted.)"
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> "*We find nothing in Bond v. Commissioner, supra, which relieves petitioners of the requirement of obtaining a qualified appraisal***.** Such a requirement is statutorily imposed by section 155(a)(1)(A) * * *[of the Tax Reform Act of 1984,

> Pub.L. No. 98-369, § 155, 98 Stat. 494, 691 (1984)]." 109 TC at 263-64 (emphasis added).

The taxpayers in *Hewitt* did not attempt to obtain an appraisal of the stock they donated and did not attach appraisal summaries to their returns. *See Hewitt v. Commissioner*, 166 F3d 332, WL 802042, at *1 (4th Cir 1998) (unpub'd op). The commissioner conceded the values reported by taxpayers represented fair market value, but allowed deductions only to the extent of basis. *Id*. In affirming the Tax Court, which held that the taxpayers were not entitled to deduct amounts in excess of those allowed by the commissioner, the Court of Appeals noted that Congress intended the appraisal requirement to be mandatory and that deductions are a matter of legislative grace. *Id*. WL 802042, at *2, 3 (4th Cir 1998) (unpub'd op). The court then stated that "*Bond* does not suggest that a taxpayer who completely fails to observe the appraisal regulations has substantially complied with them. *Id*., at *3. *See also D'Arcangelo v. Commissioner*, 68 TCM (CCH) 1223 (1994) (obtaining an appraisal from a nonqualified appraiser does not constitute substantial compliance)." *Hewitt*, 166 F3d 332, WL 802042, at *3 (emphasis added).

The taxpayers in *D'Arcangelo* were denied a $40,000 deduction for art supplies donated to a high school that then either gave away or discarded the supplies. *D'Arcangelo*, TC Memo 1994-572 (1994) (unrept'd op). The taxpayers in that case attached to their tax return a Form 8283, and a letter of appraisal from the principal of the high school. The principal was not a qualified appraiser. The court stated that "[u]nlike the taxpayers in *Bond*, in the instant case, petitioners did not merely fail to attach evidence of a qualified appraisal, *they altogether failed to obtain a qualified appraisal*." *Id*., at 7. (Emphasis added.)

In this case, Plaintiffs' efforts to comply with the regulations fall somewhere between *Bond*, on the one hand, and *Hewitt* and *D'Arcangelo,* on the other. Plaintiffs' compliance falls

short of the taxpayers in *Bond*, who engaged the services of an eminently qualified appraiser who inspected the donated property; calculated the value based on computations, schedules, and notes; and filled out in detail the taxpayers' Form 8283, setting forth a description of the property, the value, the overall physical condition, the appraiser's general qualifications, and other information required in a qualified appraisal under the applicable regulations. As the court noted in *Hewitt*, "the taxpayers [in *Bond*] made a good faith effort to comply with the appraisal requirement." *Hewitt*, WL 802042, at *4. Plaintiffs did more than the Hewitts, who completely ignored the regulatory appraisal requirements. The facts in this case are most closely analogous to those in *D'Arcangelo*, where the taxpayers submitted a Form 8283 with their return, along with a letter of value, albeit written by an unqualified individual.

To the extent that this case is similar to *Bond*, in that Plaintiffs obtained a value estimate from an appraiser, it is unclear whether Plaintiffs' appraiser is "qualified" under the regulations. Additionally, Plaintiffs' appraiser did not personally inspect the property, and it appears that Plaintiffs, rather than their appraiser, determined the condition of the property to be "very good." Hartenberger did not see the home, and the handwriting on Form 8283 appears to match Gradin's, not Hartenberger's. Property inspection is a fundamental aspect of property appraisal. Without an inspection, there is no way to verify the condition of the property. Plaintiffs may have removed valuable components such as cabinets and windows before giving the property away. Without an inspection conducted contemporaneous with an appraisal, there is insufficient evidence for the court to know what was actually donated. Moreover, the regulations require that the appraiser state the method of valuation used (*e.g.*, cost approach or market approach) and the basis for the valuation (e.g., comparable sales). Treas. Reg. § 1.170A-13(c)(3)(ii)(J) and (K). Plaintiffs' appraisal summary lacks that information. Additionally, the appraiser's stated

qualifications must include the appraiser's background, experience and education. *Id*. at (F). Without that information, the court is unable to evaluate the evidence and determine an appropriate value to be allowed as a deduction.

Other than *Bond*, Plaintiffs have not cited, nor is the court aware of, any judicial pronouncements of substantial compliance where the taxpayers did not obtain a qualified appraisal prepared by a qualified appraiser. The Seventh Circuit Court of Appeals has ruled that the doctrine of substantial compliance should be "interpreted narrowly," being limited to cases where "the taxpayer had a good excuse (though not a legal justification) for failing to comply with either an unimportant requirement or one unclearly or confusingly stated in the regulations or the statute." *Prussner v. United States*, 896 F2d 218, 224 (1990). The appraisal requirement associated with code section 170 is not unimportant; it exists to avoid fraud. Nor is the requirement stated unclearly or confusingly. Finally, Plaintiffs do not have a good excuse for failing to obtain a qualified appraisal. Accordingly, under the Seventh Circuit's test, Plaintiffs cannot invoke the doctrine of substantial compliance to escape the appraisal requirement.

Although it is a close call, the court concludes that Plaintiffs have failed to substantially comply with the regulations. That conclusion makes it unnecessary to discuss the cases cited by Plaintiffs regarding the use of assessed values in determining the value of the donated property.

The court acknowledges the apparent harshness of the result, given that there is no dispute as to whether Plaintiffs donated the property or whether the recipient was a qualified donee. Plaintiffs have a value history for the property based on county property assessment and tax records and a value estimate by an appraiser who completed Form 8283. They do not, however, have a qualified appraisal. Additionally, there is no information to determine whether

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the appraiser who completed the appraisal summary is qualified. Finally, there is insufficient information to determine the true condition and value of the property.

## IV. CONCLUSION

After a careful review of IRC section 170 and the regulations promulgated thereunder, and with due consideration for applicable case law, the court concludes that Plaintiffs are not entitled to the disputed section 170(a)(1) non-cash charitable contribution deduction, because they failed to obtain a qualified appraisal and did not substantially comply with the regulations. Now, therefore,

IT IS THE DECISION OF THIS COURT that Plaintiffs' appeal is denied.

Dated this _____ day of November 2005.

DAN ROBINSON
MAGISTRATE

***If you want to appeal this Decision, file a Complaint in the Regular Division of the Oregon Tax Court, by mailing to: 1163 State Street, Salem, OR 97301-2563; or by hand delivery to: Fourth Floor, 1241 State Street, Salem, OR.***

***Your Complaint must be submitted within 60 days after the date of the Decision or this Decision becomes final and cannot be changed.***

***This document was signed by Magistrate Dan Robinson November 10, 2005. The Court filed and entered this document November 10, 2005.***