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The Value of an Expert's Appraisal is Usually Worth The Price

By Alexander A. Bove, Jr.

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A cynic, said Oscar Wilde, knows the price of everything and the value of money. Presumably he meant that the value of a thing is relative, depending on the impact it has to the person affected and not by the price.

Obviously, Wilde did not have taxes in mind when he pondered over this pronouncement, since gift and estate tax laws take a much less philosophical approach. And no doubt he would characterize writers of the tax law as true cynics, since they basically equate price to value and value to price – provided that we take the right value at the right time.

For both gift tax and estate tax purposes, the law requires that the gift or the estate property be valued as of a certain date, to determine the tax consequences of the transaction. For a gift, the controlling date is the date the gift is made, and for estate purposes, the date is either the date of death or, at the choice of the executor, an alternate valuation date (generally six months after the date of death). In either case, the proper valuation of the asset is critical, and so the question becomes, how do you establish a value acceptable to the IRS?

The IRS says to use the fair market value, defined briefly as what a willing buyer would pay and a willing seller would accept. But how do you arrive at that number without actually selling the property? Generally, the answer is by an independent appraisal, and, as a rule, the more expert and professional the appraisal, the more likely the value will be upheld – but more about that later.

For some gift or estate property, no independent appraisal is necessary. For instance, the value of publicly traded stocks or bonds is seldom in question; their market values can easily be ascertained, as can the value of certificates of deposit and bank or money market accounts.

When there is no ready market, however, an independent expert appraisal becomes essential to support the value used by the donor of the gift or executor of the estate to determine the tax.

Being arbitrary or casual about such valuations can be costly. For instance, say that Dad (a widower) has a small business he feels is worth \$1.5 million, despite outside opinions that it may be worth considerably more. Dad felt he knew the value of his business better than anyone and refused to pay an appraiser an outrageous fee just to have the appraiser tell Dad what he already knew. Using his own valuation, Dad gives 45 percent of the business to his daughter and values the gift at 45 percent x \$1.5 million or \$675,000. Because he is entitled to give up to \$675,000 without paying a gift tax, Dad reports the gift but pays no gift tax.

The IRS, however, does not agree with Dad's valuation. After looking at the financial statements for Dad's business, the IRS comes up with its own valuation of \$3 million, advising Dad he owes them over \$270,000 in gift taxes, plus interest.

Upon hearing this and realizing he had no support for his valuation, Dad drops dead of shock. In due time Daughter files an estate tax return showing the remaining 55 percent of the business (among other assets) in Dad's estate. This time, however, Daughter gets an independent expert appraisal of the business, ready and equipped to argue the case if the IRS doesn't accept their valuation.

While most experienced estate planners appreciate the value of an expert appraisal, the fact is that most individuals, like Dad, do not. The fees for expert appraisals of businesses or other property can easily range from \$2,500 to \$25,000 and more, depending on the size and complexity of the interest being valued. But such a cost can be well worth it, especially when the gift or estate is in the high numbers. In Dad's case it could well have saved some or all of the quarter million dollar tax.

In fact, an expert appraisal might have caused Dad to reduce the amount of his gift, or caused the IRS to hesitate auditing him or reduce its own valuation, or it even may have staved off the audit altogether.

In high-stakes cases, the best appraisers are in great demand and even the IRS will strategize to hire a top appraiser in a particular field to prevent the taxpayer from hiring the same appraiser, or to take advantage of the expert's knowledge.

Think about it - if the IRS itself feels an independent expert appraisal is worth the price, it is telling us that the value of such an appraisal is greater than the price. In other words, don't be a cynic.

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