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Appraising Real Estate

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Appraising real estate is more art than science and the process became more difficult with the passage of the Pension Protection Act of 2006 (PPA) which set by statue the definition of a qualified appraiser.

The goal of all appraisals is to determine the property fair market value (FMV), what a willing buyer and seller would agree is a fair transaction. Real estate appraisals are typically performed for outright gifts, life income gifts, conservation easements when the FMV is $5,000 or more. Unlike tangible personal property gifts there is no requirement the real estate must be used to further a charities exempt purpose to be fully deductible for income, gift and estate tax purposes.

Under PPA an appraiser must have an appraisal designation from a recognized appraiser organization or have met minimum education and experience requirements. The appraiser must regularly perform appraisals and be compensated for them. The PPA also instituted penalty provisions for excessive appraisals.

Finding a Qualified Appraiser

If your charity does not have appraiser relationships or the property is out of your area consider reviewing the American Society of Appraisers (ASA) listings at www.apraisers.org
The Society has a "Find an Apprisal Expert" section where you can choose from several specialties and search by States. If this search proved futile try a Google search for "Appraisers in (State)." This yielded several options and revealed appraisers listed by county.

Charities should look for appraisers who have the MAI designation certifying they are members of the Appraisal Institute. MAI members have met rigorous requirements relating to education, experience and use the Uniform Standards of Professional Appraisal Practice procedures.

It is wise to ask the potential appraiser to submit a list of previous clients, references and a sample of a recent appraisal.

Appraisal Timing and Filing Requirements

Appraisal requirements apply to gifts of property from individuals, partnerships and corporations.

To claim a charitable deduction the apprisal must be made no earlier than 60 days prior to the transfer and not later than the date the federal tax return is due.

IRS publications 561 provides guidance on “Determining the Value of Donated Property” but it is the donor’s responsibility to file IRS Form 8283 to substantiate the charitable deduction. Publication 561 should be reviewed before proceeding with real estate gifts.

IRS Form 8283 will list the type of property, the condition of the property, the cost basis, how acquired and the FMV determined by appraisal. The appraiser must sign (IRS Form 8283, Section B, Part III) attesting to the appraisal’s validity and indicating he/she has not received a prohibited appraisal fee. A prohibited appraisal fee is an arrangement where the fee would be a percentage of the appraisal amount or the final allowable charitable deduction.

The charity must sign the form attesting receipt of the gift. It is not necessary to submit the appraisal document unless the gift is over $500,000.

Appraisal Techniques

There are three main approaches to real estate appraisals. First is the comparable sales approach which compares the subject property to other similar properties that have been sold. There are adjustments applied to compensate for differences in sale date, size, condition, location and local market variables.

The second method used, if the property produces income, is to compare the rate of income to a comparable return from other investments. It answers the question, “If I put my funds into this property am I getting a fair return compared to where else I could invest?”

The third method is to determine the FMV based upon what it would cost to reproduce the current property including the land and/or buildings.

Together these three techniques are designed to indicate the fair market value of the property.

If the appraisal indicates potential environmental issues the charity may commission an environmental impact survey to determine if the liability risks override the financial benefits of the gift.

Subsequent Sale or Transfer

When a charity disposes of the property, within three years of the date of the gift, by sale or other transfer it is required to report the transaction, within 125 days, to the IRS using form 8282 “Donee Information Return,” and supply a copy to the donor.