TAX COURT CASE UPDATE

Citation:

Joseph Mohamed, Sr. and Shirley Mohamed v. Commissioner, T.C. Memo 2012-152, May 29, 2012.

Overview:

The Tax Court has denied a real estate appraiser's charitable contribution deduction for millions of dollars of properties donated to a charitable remainder unitrust (CRUT). Although the Court acknowledged that the donations were made, and speculated that the taxpayer's self-appraisals actually undervalued the real estate, the deductions were denied because he failed to satisfy the substantiation requirements under Code Section 170 and its regulations.

The Facts:

Joseph Mohamed, Sr. is a real estate broker, certified real estate appraiser, and entrepreneur. He and his wife formed a CRUT in 1998 and donated five properties to it in 2003. Mr. Mohamed completed their 2003 tax return himself, including the Form 8282, Noncash Charitable Contributions. He admitted that he did not read the instructions before completing the form because it seemed self-explanatory. In section B, the Appraisal Summary, he used his own appraisals of the parcels, reporting that he had donated "4 parcels of land, 2 with improvements," worth $1,010,388, and a "40 acre parcel of vacant land," worth $14,873,921. He did not report his basis, but stated that he had bought all the properties in the 1970s and 1980s. He left the Declaration of Appraiser blank because it stated "I declare that I am not the donor, the donee, a party to the transaction," but he did sign the Donee Acknowledgment saying that the CRUT was a qualified organization under Code Section 170(c) and that it had actually received the donations. He also attached two statements to the tax return providing additional information about the properties, including property descriptions and values. Mr. Mohamed signed the second document, and under his signature indicated that his title was "Real Estate Broker/Appraiser." He says he claimed a lower value on the Form 8283 than he thought might be justified because he didn't want to risk overvaluing the property.

In 2004, the Mohameds donated another property to the CRUT, and Mr. Mohamed again filled out the return and Form 8283 in a similar fashion to 2003. He attached a statement with information on when he purchased the land and made improvements to it. There was also a second statement listing the property's income and expenses and computing its market value, which he signed as "Owner and Licensed Real Estate Broker." Mr. Mohamed claimed that it was attached to the 2004 return, but the IRS denied receiving it until 2006.

The IRS disputed Mr. Mohamed's self-appraisal of the properties in 2005, so the Mohameds hired independent appraisers. The independent appraisals were similar to, and overall somewhat higher than, Mr. Mohamed's own figures. The actual sales prices of the properties when sold by the CRUT in arms-length transactions were also relatively consistent with Mr. Mohamed's values. The IRS then realized that the Mohameds had made several mistakes in filing their Form 8283 for 2003 and 2004, and asserted that these mistakes compelled denying

the Mohameds any charitable deductions.

Discussion:

The Tax Court addressed each of the Mohameds' arguments and ultimately agreed that they were not entitled to their claimed charitable deductions.

The Tax Court agreed with the IRS that the Mohameds did not comply with the substantiation requirements for claiming a charitable deduction. Notably, Mr. Mohamed was not an eligible "qualified appraiser" because he was the donor and the taxpayer claiming the deductions, and was also the donee in his capacity of trustee of the CRUT. Additionally, the appraisal summary was missing key information such as his bases in the properties. The Court also concluded that the Mohameds did not qualify for relief under Reg. § 1.170A-13(c)(4)(iv)(H) (which allows a donor to provide a forgotten appraisal summary within 90 days of the IRS's request without penalty) because the original appraisal was not a qualified appraisal completed before the due date of the return and the subsequent independent appraisals were untimely.

The Tax Court then turned to the Mohameds' challenge of the validity of the regulations, in which they claimed that the statute only permits the IRS to disallow unverified donations. However, they claim that the regulations go beyond the statute and disallow deductions for verified and substantiated deductions. They argued that the regulations are arbitrary and capricious, in that a taxpayer that follows the procedures but overvalues his donation can keep some of the deduction, but a taxpayer that accurately values his donation but fails to follow the procedures loses the entire deduction.

The Court looked to the statutory language of Code Section 170 and found that it contained an express delegation of authority for the IRS to create rules about how a donation is to be "verified." Further delegation was found in the Deficit Reduction Act of 1984, which instructed the IRS to issue regulations requiring taxpayers to get a qualified appraisal and attach an appraisal summary for donations of property worth over $5,000. DEFRA also mandated that the appraiser be someone other than the taxpayer or donee. The Court found that, although the regulation is "complicated," it comports with Congress interpretation and is not arbitrary or capricious.

The Mohameds argued that, even if the regulation is valid, their deductions should be upheld because they substantially complied with the rules. The Tax Court disagreed, providing a survey of substantial-compliance-related case law which made clear that a qualified appraisal is required for the doctrine to successfully apply. The Court also addressed the particular deficiencies with respect to each individual property and found that none of the original or subsequent independent appraisals substantially complied with the regulation

Finally, the Tax Court rejected the Mohameds' arguments that Form 8283 for 2003 and 2004 did not indicate anywhere on it that an independent appraisal was necessary and had conflicting information about what could be filled out by the taxpayers and what required an appraiser's signature. Although the Court acknowledged that the forms were potentially confusing (especially to someone who did not read the instructions), and that the IRS has since revised them to reduce confusion, it stated that any failings in the forms were an insufficient basis to allow the deductions because "the authoritative sources of Federal tax law are in the statutes, regulations, and judicial decisions and not in such informal publications."

Conclusion:

The Court recognized that its complete denial of the Mohameds' deductions was “harsh,” but found that Congress was specific about how deductions were to be substantiated in light of problems and potential abuses regarding misvalued property, and that these rules could not be undermined “in a single sympathetic case.”