



June 16, 2020

The Honorable David J. Kautter
Assistant Secretary for Tax Policy
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

The Honorable Charles P. Rettig
Commissioner
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC 20224

The Honorable Michael J. Desmond
Chief Counsel
Internal Revenue Service
1111 Constitution Ave, NW
Washington, DC 20224

Ms. Holly Porter
Associate Chief Counsel
Passthrough & Special Industries
Internal Revenue Service
1111 Constitution Ave, NW
Washington, DC 20224

**RE: IRS Memorandum on Interim Guidance on Internal Revenue Code Section 6695A
Penalty Case Reviews (Control Number: LB&I-20-0120-001, January 22, 2020)**

Dear Messrs. Kautter, Rettig, and Desmond, and Ms. Porter:

The American Institute of CPAs (AICPA) is concerned about the recently issued Department of the Treasury (“Treasury”) and the Internal Revenue Service (IRS) [Memorandum](#) dated January 22, 2020 from Commissioner Douglas W. O’Donnell and Commissioner Eric Hylton that eliminated the previously existing multi-tiered review process set forth in [Internal Revenue Manual \(IRM\) 20.1.12.7.4](#)¹ for Internal Revenue Code section² 6695A penalty case reviews. Under this part of the IRM, the review process included at least two qualified knowledgeable IRS appraisers. We suggest that IRS return to the prior review process requiring at least two qualified knowledgeable IRS appraisers.

Background

One of the six goals included the [IRS Strategic Plan for the years 2018-2022](#) is the following: “Collaborate with external partners proactively to improve tax administration.” As the national organization representing in excess of 400,000 members in the United States, the AICPA has implemented a specialized training and credentialing program for professionals desiring to specialize in the valuation of a business, fractional interest in a business, security or intangible asset. Many of the valuation analysts affected by the recent IRS action are valuation analysts

¹ See [IRM 20.1.12.1.7.4](#) (as of 12-18-2017) Review Manager and Appraiser Procedures for IRC 6695A Penalty Case.

² Unless otherwise indicated, hereinafter, all section references are to the Internal Revenue Code of 1986, as amended, or to Treasury Regulations promulgated thereunder.

holding the Accredited in Business Valuation (ABV) credential sponsored by AICPA. As ABV credential holders and CPAs (“valuation analysts” or “appraisers”), our members are qualified to practice before the IRS and hence, are bound by the rules set forth in Circular 230. Consequently, the IRS and AICPA share common goals of reasonableness and ethical behavior in the discharge of responsibilities in the valuation discipline.

AICPA Observations and Recommendations

We were not aware of any notice to the AICPA or to our affected members that a change of process was forthcoming, and we express our disappointment in this fact. We hope this was an oversight, as we view ourselves as “external partners” and value the collaborative working relationship between our organizations that was forged over many years. We welcome the opportunity to engage in dialogue with the IRS to understand the reasons for such action and to explore the possibility of workable alternatives.

The AICPA shares the concern of the IRS that the marketplace contains valuation analysts who are not properly trained or experienced, or who take unreasonable valuation positions when preparing valuations that taxpayers will use to support an IRS filing. We understand and support all efforts to eradicate bad valuations, whether done with intent and motive, or due to incompetence. However, we believe the recent IRS action to eliminate the multi-tiered review process could have a harmful effect on the valuation profession and negative unintended consequences on the IRS’s efforts to promote quality valuations and allocate its limited resources towards vetted and informed enforcement actions.

The AICPA was one of seven valuation accrediting organizations that testified before the IRS Office of Servicewide Penalties and Appraiser Organizations in the wake of the passage of section 6695A in the Pension Protection Act of 2006. The AICPA also met with representatives of the Office of Professional Responsibility, which oversees compliance with Circular 230 by professionals licensed to practice before the IRS. As a consequence of these interactions, the IRS agreed it was necessary to have five individuals, at least two of them independent IRS appraisers, review a case before contacting the appraiser with a Letter 4477 advising the appraiser that his/her appraisal was selected for audit. This process of review and concurrence was intended to assure the application of proper technical knowledge, fairness, and objectivity to the review and selection process.

Valuation Expertise for IRS Professionals is Critical

The AICPA is concerned that the elimination of the collaboratively developed multi-tiered review process, which in essence challenges a valuation analyst on a competency standard, will result in IRS agents, who may have limited training and experience in valuation, initiating a section 6695A penalty case against a valuation analyst without the critical input and concurrence from an independent IRS appraiser.

The field of valuation has many subjective factors requiring the judgment of the valuation analysts. These subjective factors lead to legitimate differences of opinion, even among people who are knowledgeable and experienced, as reasonable people often disagree. The application of

recognized methodologies, the rigorous analysis of the subject company or interest, and the application of professional judgment developed over many years of training and experience that are applied to each engagement's unique set of facts and circumstances establish the foundation for a thoroughly supported conclusion of value.

AICPA Observations and Recommendations

It is necessary for IRS professionals who decide whether to initiate the section 6695A process to have, at a minimum, the requisite skills, experience and training the IRS requires for qualified appraisers in order to ensure that legitimate differences of opinion are discussed and resolved in a manner that results in better valuations and a stronger profession.

The change implemented by the IRS removes an essential check and balance that has operated effectively for nearly 15 years. The removal will result in valuation analysts who have prepared high quality valuations that have complied in all respects with the AICPA's valuation standards (recognized by the IRS as a generally accepted appraisal standard) as subject to the section 6695A penalty proceedings who otherwise would not have been subject under the multi-tiered review process.

Effect on Professional Reputation

Our members who prepare valuations to support IRS filings are concerned that the elimination of the multi-tiered review process creates an opportunity for IRS to expand its ability to initiate section 6695A penalty proceedings that could negatively affect individual practitioners as well as the valuation profession as a whole.

Many of our members who are valuation analysts offer testimony on conclusions of value before triers of fact in federal, state, and local venues where professional reputation, experience, and credentials are essential to establish and maintain credibility within a field or discipline. The receipt of a Letter 4477, informing a valuation analyst of the possibility of penalty imposition, is discoverable information in the civil, commercial, or criminal litigation context and does not become "undiscoverable" with the passage of time. A litigant can use Letter 4477 against a valuation analyst in any litigation setting as a means to call into question the valuation analyst's reputation and credibility even when the outcome of the section 6695A penalty proceedings resulted in no sanctions or findings against the valuation analyst (i.e., the work was performed in accordance with IRS requirements).

AICPA Observations and Recommendations

Some form of review and concurrence process is necessary *before* a section 6695A penalty process is initiated and Letter 4477 is sent. This process must include at least two IRS professionals with the requisite education, training, and experience requirements that are set forth in the "qualified appraiser" requirements of the IRS. Otherwise, we are concerned that experienced and qualified valuation analysts who perform high quality valuations (i.e., that meet or exceed IRS requirements and are in compliance with AICPA valuation standards) will elect to stop preparing valuations for IRS filings because the risk to their business and professional reputation and credibility is too high.

If the purpose of the penalty provisions is to increase compliance with the tax laws, and in this case with the rules regarding appraisals, unintended consequences may result from these changes. As mentioned above, if appraisals are more difficult to obtain and more expensive as a result of the changes in the administration of the penalty provisions of section 6695A, taxpayers will submit returns to the IRS without the benefit of a qualified appraisal. Taxpayers will derive valuations based on their own experience and based on their individual limited experience. These self-appraisals will not have the benefit of the experience, perspective and knowledge of the rules that a qualified appraiser brings to the tax compliance process. Self-appraisals will result in less accurate appraisals and more work for the IRS in the long term.

The intent behind the IRS action to eliminate the tiered review was not to stop valuation professionals who are performing high quality valuations; however, feedback received from members suggests if the IRS action is not revised with the recommendations this letter has provided, qualified experienced valuation analysts may cease performing tax valuations.

Eliminating the multi-tiered approach will potentially make the tax administrative process more difficult and backlogged as the revised process for initiating section 6695A cases creates the potential for an influx of valuation cases that may or may not have failed to meet the IRS requirements but all of which will require the use of the IRS's limited resources.

Effect of Litigation on Valuations

In the estate and gift tax area, taxpayers often retain estate/gift tax lawyers for advice and planning and retain a valuation analyst to conduct a valuation and produce a report containing an opinion of value. This opinion of value is attached to the Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, or Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return. If that Form 706 or 709 is selected for audit by IRS, the taxpayer will more likely than not retain the estate/gift tax lawyer to represent them before IRS in the examination process. Once the examination begins, the IRS and the taxpayer generally have one objective: to resolve the matter expeditiously to avoid the cost of the appeals process and potential litigation in Tax Court. If the issue is valuation related, often the IRS and taxpayer's legal counsel negotiate a value without the knowledge or involvement of the valuation analyst in an effort to resolve and close the matter.

AICPA Observations and Recommendations

An IRS agent untrained in valuation theory may take an unreasonable valuation position, causing the taxpayer and his/her representative to agree to a negotiated amount that, under the mechanical measures of section 6695A, qualify for the imposition of an appraiser penalty. We do not recognize a value that is negotiated in the tax administration process as the "proper" or "correct" amount as those terms are used in section 6695A and consequently, the IRS agent should not use it for the imposition of an appraiser penalty.

Due to the concerns raised in this letter, we recommend that IRS return to the prior review process requiring at least two qualified knowledgeable IRS appraisers before issuing a Letter 4477.

The AICPA is the world's largest member association representing the accounting profession with more than 429,000 members in the United States and worldwide, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses. We appreciate your consideration of these comments and welcome the opportunity to discuss these issues further. The AICPA stands ready to work collaboratively with the IRS in addressing the tax laws of the United States, including the issues addressed in this correspondence. If you have any questions, please contact Eva Simpson, AICPA Director – Valuation, at (919) 402-4508 or eva.simpson@aicpa-cima.com; Eileen Sherr, AICPA Senior Manager – Tax Policy & Advocacy, at (202) 434-9256 or eileen.sherr@aicpa-cima.com; or either Chris Hesse at (612) 397-3071 or Chris.Hesse@CLAconnect.com or Annette Stalker at (916) 710-8333 or Annette@StalkerForensics.com.

Sincerely,



Christopher W. Hesse, CPA
Chair, AICPA Tax Executive Committee



Annette Stalker, CPA, CFF
Chair, AICPA Forensic & Valuation Services
Executive Committee

cc: Mr. Douglas W. O'Donnell, Commissioner, Large Business and International Division
Mr. Eric Hylton, Commissioner, Small Business/Self-Employed Division
Mr. William (Tim) Brittain, Internal Revenue Service
Ms. Catherine Veihmeyer Hughes, Estate and Gift Tax Attorney Adviser, Office of Tax
Legislative Counsel, Office of Tax Policy, Department of the Treasury