
Another Ethical Dilemma

By Charles M. Lax

Michigan certified public accountants are subject to the *AICPA Code of Professional Conduct*. Additionally, those same practitioners are governed by *Treasury Department Circular 230* ("Circular 230") if they practice before the Internal Revenue Service. This article will briefly touch the ethical dilemma a practitioner faces when they may not agree with their client over the use of information or documentation provided by the client to sustain a tax position. As I have done in the past, the issues will be presented through a case study methodology, which will include a set of facts, a description of the issues, the applicable authority, and a suggested resolution.

CAN YOU TRUST YOUR CLIENT?

You are the new certified public accountant for a corporate client. In preparing your first year end financial statement and tax return, you learn that the corporation distributed a piece of vacant real estate to the corporation's owner during the year. The real estate was acquired more than 10 years ago. You ask the client about the property. He indicates that it was a great investment since he "paid next to nothing for it." You tell him that it should be appraised in order to report the transaction. He tells you that since there is no market for the property, you should use the original cost. He assures you the original cost is still a good value.

Can you rely on the client's determination of value?

Section 10.34(c) of Circular 230 generally allows a practitioner to rely upon information furnished by a client without verification, but the practitioner cannot ignore what he knows. Furthermore, Section 10.34(b) of Circular 230 provides that a practitioner must make reasonable inquiry if the information appears incorrect, incomplete, or inconsistent with another fact. In this case, the client is not a real estate appraiser. It is also unreasonable to believe that the value of the real estate has not changed in 10 years.

Under these circumstances, at a minimum the practitioner should make reasonable inquiry concerning the real estate valuation. Tax bills should be obtained. Furthermore, inquiry should be made about the development and/or sale of adjacent real estate or other real estate in that geographic area. The best approach, of course, would be to insist upon a third party appraisal. It is not uncommon for practitioners and their clients to have a different view of the same facts. While not wanting to jeopardize the relationship with the client, the practitioner must balance that against their obligations under Circular 230. In this case an appraisal should be obtained.

CAN YOU TRUST THE THIRD PARTY “EXPERT”

You continue to insist on obtaining an appraisal. The client relents and a few days later he sends you a one paragraph document called an “Appraisal.” It basically contains a street address for the property and the fact that the property is vacant. It is signed by “Tom Smith, Licensed Real Estate Broker.” On the letterhead you see that Mr. Smith is a residential real estate broker. The value reported in the Appraisal is the original purchase price.

Can you now use the cost as its current value under these circumstances?

Under Section 10.22(b) of Circular 230, a practitioner may generally rely upon the work product of others, if reasonable care is used in evaluating the work product and the person providing the work product. In this case, while a third party appraisal has now been provided, the question remains: *Is it reasonable to use this appraisal?*

Too often, practitioners feel they are getting a “free pass” when they are provided with an opinion, documentation, or appraisal from a third party. Unfortunately, Circular 230 requires more. In this case, the appraisal is provided by a residential broker even though the property is commercial in nature. At a minimum, the practitioner should make further inquiry concerning Mr. Smith’s appraisal credentials. Possibly, he has other credentials and experience with regard to commercial property. Furthermore, the practitioner should contact Mr. Smith to discuss the appraisal and how he arrived at the valuation. Once again, this may not make the client happy, but it may well be required under Circular 230.

