

Cite as Det No. 08-0169, 28 WTD 25 (2009)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund and)	<u>D E T E R M I N A T I O N</u>
Correction of Assessment of)	
)	No. 08-0169
...)	
)	Registration No. . . .
)	Document No. . . .
)	Docket No. . . .
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RCW 82.45.030, RCW 82.45.033: REET – CONTROLLING INTEREST – MEASURE – VALUE. When a corporation sells a controlling interest in a limited partnership owning real estate, REET is calculated using the value of the real estate owned by the partnership. Absent other evidence, the market value assessment for the property maintained on the county property tax rolls should be used as the measure of the REET.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

M. Pree, A.L.J. – A corporate taxpayer requests a refund of additional real estate excise tax (REET) it paid under protest on its sale of the controlling interest of a limited partnership, which owned real estate in Washington. The corporation contends REET should have been measured by the partnership’s value, which included encumbered real estate. The market value assessment for the property maintained on the county property tax rolls was the appropriate measure of REET. Petition denied in part and granted in part, with a partial refund.¹

ISSUE

Under RCW 82.45.030, when a corporation sells a controlling interest in a limited partnership owning real estate encumbered by a nonrecourse loan, how is REET calculated?

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

FINDINGS OF FACT

[Taxpayer] owned a controlling interest of a Washington limited partnership . . . (LP). LP owned real estate in Washington subject to a nonrecourse loan.

[In] 2008, the taxpayer sold [more than 50]% of its interest in LP to [an LLC] for \$40,000. Using the \$40,000 sales price, the taxpayer calculated the value on 100% of LP [and paid REET calculated on that amount]. The taxpayer submitted the payment with a Controlling Interest Affidavit, which explained the real property parcel owned by the LP had an assessed value of [more than \$1 million] subject to a lien in excess of [\$2 million].

The Miscellaneous Tax Section of the Department of Revenue, reviewed the taxpayer's affidavit. On February 29, 2008, the Miscellaneous Tax Section wrote the taxpayer, and explained the taxpayer owed \$. . . additional REET based on the real property's assessed value The taxpayer paid [the assessment] and appealed for a refund.

LP's real estate parcel actually had an assessed fair market value . . . on the county property tax rolls at the time of the transfer [that was somewhat less than the assessed value stated on the taxpayer's Controlling Interest Affidavit and used to calculate the assessment]. The Miscellaneous Tax Section acknowledges that, because the assessed value per county tax rolls was [less than the value used to calculate the assessment], the total REET should have been [lower than the amount assessed]. Consequently, based on the lower valuation, \$. . . should be refunded to the taxpayer. . . . We do not have an appraisal of the real property.

According to the taxpayer, the outstanding balance on the mortgage was [more than \$2 million]. . . . LP's . . . 2008 balance sheet listed the real estate: land (\$. . .), buildings (\$. . .), and building improvements (\$. . .) separately as fixed assets. Fixed assets also included furniture and fixtures (\$. . .) as well as office equipment – partners (\$. . .). The balance sheet also listed current assets (\$. . .) and funded reserves (\$. . .). Accumulated depreciation offset the asset totals. Total liabilities of \$. . . exceeded the total assets of \$. . . resulting in a negative equity of \$. . . . Yet, the taxpayer received \$40,000 for its [more than 50%] interest of LP. Consequently, we find LP's book value did not reflect its fair market value.

ANALYSIS

REET is imposed upon the sale of real property in Washington. RCW 82.45.060. "Real property" means any interest, estate, or beneficial interest in land or anything affixed to land, including the ownership interest or beneficial interest in any entity which itself owns land or anything affixed to land. RCW 82.45.032(1). The term "sale" includes the transfer or acquisition of a controlling interest in any entity with an interest in real property located in this state for a valuable consideration. RCW 82.45.010(2).

RCW 82.45.033(2) defines "Controlling interest" in the case of a partnership as: ". . . fifty percent or more of the capital, profits, or beneficial interest in such partnership." The taxpayer

owed REET because it sold over a 50% interest in LP, a partnership, which owned real estate in Washington, for valuable consideration, \$40,000.² Our issue involves the measure of the REET. The REET rate is multiplied by the “selling price” to determine the amount of tax due. *See* RCW 82.45.060. RCW 82.45.030 defines “Selling price” for controlling interest sales as:

(2) If the sale is a transfer of a controlling interest in an entity with an interest in real property located in this state, the selling price shall be the true and fair value of the real property owned by the entity and located in this state. If the true and fair value of the real property located in this state cannot reasonably be determined, the selling price shall be determined according to subsection (4) of this section....

(4) If the total consideration for the sale cannot be ascertained or the true and fair value of the property to be valued at the time of the sale cannot reasonably be determined, the market value assessment for the property maintained on the county property tax rolls at the time of the sale shall be used as the selling price.

RCW 82.45.030(2) specifically addresses the sale of controlling interests, “the selling price shall be the true and fair value of the real property owned by the entity and located in this state.” The transferee paid the taxpayer \$40,000 for LP, an entity with assets other than the real estate, and substantial liabilities. In the sale of an entity, the value taxed is not the consideration paid, but the value of the real estate owned by the entity. *McFreeze Corp. v. Dep’t of Revenue*, 102 Wn. App. 196, 200, 6 P.3d 1187 (2000); Det. No. 98-083, 17 WTD 271 (1998). In fact, because LP had other assets in excess of \$40,000, and a negative equity of \$. . . , the fair value of the real property owned by LP cannot be reasonably determined from the \$40,000 received by the taxpayer, nor LP’s balance sheet. The transfer of the controlling interest in LP cannot be based on the \$40,000 taxpayer received as this amount does not represent the true and fair market value of the real property. We cannot determine the value of the real estate.

Because the true and fair value of the real property cannot reasonably be determined, RCW 82.45.030(2) directs us to RCW 82.45.030(4). We cannot ascertain the total consideration for the property. Therefore, under RCW 82.45.030(4), we conclude that the . . . market value assessment for the property maintained on the county property tax rolls should be used as the selling price to measure the REET. . . . [Because the taxpayer paid REET calculated on an amount in excess of the market value assessment for the property maintained on the county tax rolls at the time of sale, the taxpayer is entitled to a partial refund.]

² We understand neither the taxpayer nor LP were liable for the nonrecourse loan and, therefore, the transfer of the real property encumbered by the loan may not constitute consideration to the taxpayer for the purpose of determining whether a sale occurred and REET was due. *See* WAC 458-61A-103(2). Because the taxpayer received \$40,000 consideration, REET does apply. Our issue is the measure of REET regarding the transfer of a controlling interest, which is not addressed in WAC 458-61A-103.

DECISION AND DISPOSITION

We grant the petition in part. \$. . . plus interest will be refunded to the taxpayer.

Dated this 8th day of July, 2008.