

Cite as Det. No. 97-240R, 21 WTD 145 (2002)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of)	<u>F I N A L</u>
Assessment of)	<u>D E T E R M I N A T I O N</u>
)	No. 97-240R
)	
...)	Real Estate Excise Tax
)	Audit No. . . .
)	

WAC 458-61-374, WAC 458-61-030; RCW 82.45.010: REET – CONSIDERATION – EXEMPT TRANSFERS – NONRECOURSE DEBT. Real Estate Excise Tax (REET) is due when a purchaser in exchange for an undivided interest in real property agrees to make payment on certain nonrecourse debts and also takes the property subject to an underlying recourse debt.

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.

NATURE OF ACTION:

Real property owner seeks reconsideration of a determination affirming the assessment of real estate excise tax (REET) on the transfer of an undivided interest in the property.¹

FACTS:

Mahan, A.L.J. -- On . . . , 1996, the taxpayer purchased real property for \$[13x] [Bank] financed the purchase and the taxpayer executed a promissory note in the amount of \$[9x] in favor of the bank. The note was secured by a Deed of Trust on the property. The seller also took back a promissory note for \$[1.5x], which was secured by a second deed of trust, and a promissory note for \$[1x], which was secured by a third deed of trust. The second and third promissory notes were nonrecourse in nature.

On . . . , 1996 the taxpayer, by statutory warranty deed, transferred an undivided . . . % interest in the property to [a purchaser.] The taxpayer executed Real Estate Excise Tax Affidavit # . . . and

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

claimed an exemption to REET under WAC 458-61-374. The Purchase and Sale Agreement for the transaction provided that the purchase price was \$[2x], with the purchaser taking the undivided interest in the property subject to the nonrecourse in that amount and making payments on that debt. The taxpayer agreed to continue making payments on those debts for the amounts that were in excess of the purchase price. The agreement further provided that the taxpayer would continue to be liable for the [Bank] debt and that the purchaser was not responsible for that debt.

The Department of Revenue (Department) denied the claimed exemption and stated:

This liability of the First Deed of Trust Extended to the entire property, both the . . . percent retained by [the taxpayer] and the . . . percent undivided interest transferred to [the purchaser.] For this reason the transfer fails to meet the criteria for tax exemption under WAC 458-61-374, i.e., the . . . undivided interest transferred to [the purchaser] was encumbered by debt for which the grantor was liable.

In its petition the taxpayer contends that

The only consideration given by [the purchaser] was taking the interest in the property subject to the obligation to pay the Non-recourse Notes in the amount of the purchase price. This transfer should thus be exempt under WAC 458-61-374.

At the hearing, the taxpayer stated that the only benefit it received in the transfer was that it did not need to pay that portion of the nonrecourse debt that the purchaser agreed to pay. It further argued that such a transfer does not involve any additional consideration, relying on the gift exemption provided under WAC 458-61-410. In relevant part it provides:

When any consideration other than love and affection is present in the transfer, the transaction is taxable to the extent of the consideration present. Consideration includes the indebtedness balance of any real property transferred which is encumbered by a lien securing an indebtedness.

...

(iii) Example 3. No consideration is given by B. A has \$175,000 equity and an underlying mortgage of \$25,000, on which A continues to make the payments. This is a gift by A to B of the \$175,000 and the payments on the underlying debt. It is exempt from the real estate excise tax.²

² As stated in the original determination, these gift provisions are distinguishable. Under the gift provisions, the party liable under the promissory note is effectively making a gift of the payments as they come due, and it is not being relieved of any debt, as occurred in this case.

On reconsideration, the taxpayer further asserts that it should be treated as if it had, in effect, transferred property subject only to nonrecourse debt because of the lack of any potential liability should the transferee default. It makes this argument in response to a comment in the original determination. The taxpayer further explains that any deficiency is unlikely because:

The seller is a limited liability company and its only asset in the case is the property. The first deed of trust holder would most likely choose a non-judicial foreclosure because a deficiency judgment on the promissory note would be pointless. The first deed of trust is thus, in effect, nonrecourse.

ISSUE:

Is REET due when a purchaser in exchange for an undivided interest in real property agrees to make payment on certain nonrecourse debts and also takes the property subject to an underlying recourse debt?

DISCUSSION:

REET is imposed upon sales of real property. RCW 82.45.060. A sale of real property is defined for REET purposes as follows:

As used in this chapter, the term "sale" shall have its ordinary meaning and shall include any conveyance, grant, assignment, quitclaim, or transfer of the ownership of or title to real property, including standing timber, or any estate or interest therein for a valuable consideration

RCW 82.45.010. Under this statutory framework, there are two prerequisites for imposition of the tax: (1) the transfer of an interest in real property; and (2) consideration paid or contracted to be paid in exchange for the transfer. State ex rel Namer, Inc. v. Williams, 73 Wn.2d 1, 435 P.2d 975 (1968); AGLO 1977 No. 6.

In a similar manner, WAC 458-61-030(8)(d) provides that the term "sale" does not include:

those real property transfers which are excluded from the definition of "sale" and exempted from the real estate excise tax by RCW 82.45.010 and this chapter, including transfers where no valuable consideration is present. See also WAC 458-61-225, Assumption of debt, and WAC 458-61-374, Exemption--Transfers "subject to."

As referenced in this provision, WAC 458-61-374 (Rule 374) provides:³

³ As further referenced in this provision, WAC 458-61-225 (Rule 225) provides:

(1) In addition to other circumstances where valuable consideration passes between the parties, the real estate excise tax applies to transfers of real property when an underlying debt on the property is assumed by the grantee.

A transfer of real property subject to an underlying debt when the grantor is not personally liable for the debt and when no other consideration is given for the transfer is exempt from the real estate excise tax.

In general, the measure of the tax is based on the "selling price", which is defined to include the "total consideration paid or contracted to be paid." RCW 82.45.060; 030. The term "consideration" is defined to include "money or anything of value, paid or delivered or contracted to be paid or delivered in return for the sale and shall include the amount of any lien, mortgage, contract indebtedness, or other incumbrance, either given to secure the purchase price, or any part thereof, or remaining unpaid on such property at the time of sale." RCW 82.45.030(3); see also WAC 458-61-030(3).

In this case, the taxpayer continued to be personally liable under the first deed of trust, which was secured by the entire property. It received consideration in being relieved of a portion of its debt on the entire property. As such REET would be due on the transfer unless there is a specific exemption available. In considering this issue we are mindful of the requirement that exemption provisions must be narrowly construed. Taxation is the rule and exemption is the exception. Budget Rent-a-Car, Inc. v. Department of Rev., 81 Wn.2d 171, 174, 500 P.2d 764 (1972).

Here, the taxpayer does not meet the express exemption allowed under Rule 374. The property transferred was subject to the first deed of trust, a debt upon which the grantor was liable. Accordingly, the transaction does not qualify for the exemption.

In the final analysis, whether the taxpayer is potentially liable should a default occur is not relevant to whether the exception applies. Following the decision in Groesbeck v. Department of Rev., 63 Wn. App. 371, 818 P.2d 1121 (1991), RCW 82.45.010 was amended to remove from the definition of "sale" the exclusion for transactions in which the only consideration was the assumption of the balance owing on obligations secured by the real property transferred. As a result, the only related exception remaining is with respect to transfers subject to nonrecourse debt under Rule 374.

In order for us to include the taxpayer's transaction, which involved a transfer subject, in part, to a recourse debt, we would have to rewrite the Rule 374 exception. This we cannot do. See, e.g., State v. Mollich, 132 Wash. 2d 80, 87, 936 P.2d 408, 411 (1997) ("[The court has] no license to rewrite explicit and unequivocal statutes."); Soundgarden v. Eikenberry, 123 Wash. 2d 750, 766, 871 P.2d 1050 (1994). In general, a court refrains from adding to, or subtracting from, the language of a statute unless imperatively required to make it rational. Applied Indus. Materials

(2) The measure of the tax is the combined amount of the debt and any other additional consideration.

(3) See WAC 458-61-374 for the transfers made when the grantor has no personal liability for the underlying debt.

Corp., 74 Wn. App. at 79 (citing McKay v. Department of Labor & Indus., 180 Wash. 191, 194, 39 P.2d 997, 98 A.L.R. 990 (1934)). Rules of statutory construction apply to the interpretation of administrative rules and regulations. Multicare Medical Ctr. v. Department of Social & Health Services, 114 Wn.2d 572, 591, 790 P.2d 124 (1990).

Accordingly, the taxpayer's petition for reconsideration is denied.

DECISION AND DISPOSITION:

This matter is remanded to the Miscellaneous Tax Division for collection of any outstanding amounts.

Dated this 29th day of January 1999.