

Cite as Det. No. 05-0064, 24 WTD 447 (2005)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Refund by)	<u>D E T E R M I N A T I O N</u>
)	
...)	No. 05-0064
)	
)	Registration No.
)	Docket No.
)	

- [1] RCW 82.45.010: REAL ESTATE EXCISE TAX (REET) – DEFINITION OF SALE. A valid and binding real estate contract can qualify as a sale for REET purposes, even if no instrument is recorded for the transfer.
- [2] WAC 458-61-100, WAC 458-61-590: REET – REFUND—RESCINDED TRANSACTIONS. If a real estate transaction is completely rescinded, the reconveyance is exempt from REET. However, there is no REET refund for the initial conveyance of the rescinded transaction.

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.

STATEMENT OF THE CASE

Nguyen, A.L.J – . . . (Taxpayer) requests refund of the real estate excise tax (REET) that she paid on account of an unrecorded transaction that was subsequently rescinded.¹

We hold that the initial transaction qualified as a taxable sale for REET purposes notwithstanding any subsequent rescission.

ISSUES

1. Does the initial transaction qualify as a sale for REET purposes?
2. Does Taxpayer qualify for a refund under the rescinded sale exception of former WAC 458-61-100(5)?

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

3. Does the Department have the authority to waive the REET if rigid application of the tax would impose significant hardship on Taxpayer?

FINDINGS OF FACT

In 2003, Taxpayer entered into a contract for the sale of her real property . . . located in [Washington]. There was no closing, and the sale was not recorded. In June 2004, Taxpayer and the buyers agreed to rescind the sale contract and restore the parties to their original positions.

. . . Taxpayer and the buyers signed [a rescission contract] in June 2004. In the recitations, Taxpayer is identified as “Seller” and the buyers, a married couple, are identified collectively in the singular as “Buyer.” The parties entered into a contract in 2003 for the sale and purchase of certain real property . . . collectively called the “sale property.” At the time of the 2003 transaction, the buyers were managing the sale property for Taxpayer, and leasing part of the property for use as pasture and hayfield. . . .

The parties agreed to rescind the unrecorded Sales and Purchase Agreement, released each other from their obligations under the rescinded contract, and restored the payments, expenses and benefits in accordance with the terms of the rescission agreement.

After the rescission, Taxpayer submitted a request to the Department asking for a full refund of the REET that she had paid based on the unrecorded initial sale contract.² The Special Programs Division of the Department denied the refund request on July 7, 2004. Taxpayer timely petitioned the Appeals Division for a review of the refund request.

In her petition, Taxpayer argues that the unrecorded contract did not qualify as a sale, and therefore should not be subject to REET. In addition, Taxpayer argues that she qualifies for a refund under the rescinded sales exception of former WAC 458-61-100(5). Taxpayer also argues that a rigid application of REET in this case would be a significant hardship for her.

ANALYSIS

1. The initial transaction qualifies as a sale for REET purposes.

[1] REET is imposed as “an excise tax upon each sale of real property.” RCW 82.45.060. For this purpose, the term “sale” is defined in part as follows:

(1) 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

² According to . . . attorney for Taxpayer, Taxpayer paid the real estate excise tax based on the advice of [Escrow Agent] . . . [Escrow Agent] informed Taxpayer that in order to formalize the transaction, she would also need to pay the real estate excise tax.

interest therein for a valuable consideration, **and any contract for such conveyance, grant, assignment, quitclaim, or transfer**, and any lease with an option to purchase real property, including standing timber, or any estate or interest therein or other contract under which possession of the property is given to the purchaser, or any other person at the purchaser's direction, and title to the property is retained by the vendor as security for the payment of the purchase price. The term also includes the grant, assignment, quitclaim, sale, or transfer of improvements constructed upon leased land.

RCW 82.45.010(1) (emphasis added).

Taxpayer argued that there was no sale for REET purposes because Taxpayer did not sign or record any conveyance, assignment, quitclaim, or transfer instrument. There was no settlement or closing, and the sale contract was never recorded. Taxpayer pointed out that REET is generally paid when a real estate contract is recorded at the consummation of a sale. Because the sale transaction in this case was never consummated, Taxpayer argued that no REET was ever due or owing.

We give due weight to the thoughtful arguments presented by Taxpayer. However, after consideration of applicable law, we cannot treat the transaction as a non-sale for REET purposes for the following reasons:

- An unrecorded conveyance is still valid between the parties, even if it is void against a subsequent good faith purchaser. RCW 65.08.070 (unrecorded conveyance is void against subsequent purchaser in good faith); *Chelan County v. Wilson*, 49 Wn. App. 628, 632, 744 P.2d 1106 (1987) (“The intention of the recording act is to require persons claiming an interest in real property to record such instrument as will give notice of their claims. Unrecorded conveyance of realty, however, is valid as between the parties.” (Citations omitted).)
- A real estate contract by itself, even if unrecorded, transfers an equitable interest in the property and confers in the buyer certain substantial rights with respect to the possession, control and legal title to the property. *Chelan County*, 49 Wn. App. at 632.
- The REET statute defines “sale” to include any contract for the conveyance, grant, assignment, quitclaim, or transfer of the ownership of or title to real property. RCW 82.45.010(1). Moreover, the statute does not require that the contract be fully performed to qualify as a sale.
- Taxpayer does not dispute that the initial contract, at the time of its execution in 2003, was a valid and binding agreement for the sale of the property. In fact, both parties acted accordingly. The parties took affirmative steps to carry out the signed contract, which include, among other things, several payments and significant investment of money and effort by the buyers to maintain and improve the property.

- The REET statute specifically provides for the reporting and payment of tax where no instrument is recorded in the county real property records. RCW 82.45.090(2). This provision shows that the tax, if otherwise applicable, is due even in the absence of any real estate recording.

Taxpayer noted that because the buyers were already managing and leasing the sale property, the sales contract did not significantly change their right of possession of the property. Although there might have been no practical difference in the short term, the signed contract clearly put the parties in very different legal positions, with very different future expectations.

All things considered, we find that the 2003 real estate sale contract by itself qualifies as a taxable sale under RCW 82.45.010(1), even if the parties did not go through a formal closing process.

2. Taxpayer does not qualify for a refund under the rescinded sale exception of former WAC 458-61-100(5).

Taxpayer argues that she is entitled to a refund of the REET based on the rescinded sale exception under former WAC 458-61-100. That former rule provides as follows (emphasis added):

- (5) The authority to issue tax refunds under this chapter is limited to:
 - (a) **Transactions that are completely rescinded as defined in WAC 458-61-590**

By contrast, the current WAC 458-61-100 provides (emphasis added):

- (5) Circumstances under which a refund of tax is authorized. The authority to issue tax refunds under this chapter is limited to:
 - (a) **The conveyance back to the grantor for transactions that are completely rescinded as defined in WAC 458-61-590**

Taxpayer contends that former WAC 458-61-100(5)(a) applies to her because: (i) the original sale transaction happened, and the REET was paid, prior to September 25, 2003, the effective date of the new WAC 458-61-100; and (ii) the original sale transaction was “completely rescinded” pursuant to WAC 458-61-590.

In support of her argument, Taxpayer also cited two published determinations suggesting that under former WAC 458-61-100, the Department would allow refund of any REET paid on account of a transaction if it was completely rescinded: Det. No. 88-365, 6 WTD 403 (1988); Det. No. 87-43, 2 WTD 207 (1986).

In both the cited determinations, the Department found that there was no rescission and, consequently, never reached the issue of refund for any REET paid on the original transaction.

Because the determinations discussed the question of rescission in general terms, they might have raised the expectation that a REET refund might be available for the original transfer as well as for the second transfer in a rescinded sale transaction. However, the 2003 amendment of WAC 458-61-100 clarified that no refund is due on the original transaction.

By its terms, WAC 458-61-100 is not an exemption provision; it merely establishes the procedure for requesting a REET refund. In particular, section (5) of former WAC 458-61-100 limits the authority to grant REET refunds, but it does not affirmatively establish any exemptions, except as provided by the statute or other applicable administrative rules. Even if we assume that former WAC 458-61-100 applies to the transaction at issue, we still have to determine whether there is a statutory provision or rule that exempts a transaction if it is subsequently rescinded.

WAC 458-61-590, to which subsection (5)(a) of both the current and former WAC 458-61-100 refers, specifically provides that (emphasis added):

(1) The real estate excise tax does not apply to a reconveyance of property pursuant to a rescission.

(2) In order to qualify for exemption under this section, all consideration paid toward the selling price must be returned by the grantor to the grantee.

(a) A grantor may retain interest paid by the grantee without disqualifying the rescission.

(b) The payment of a reasonable reimbursement for site improvements will not disqualify the rescission.

WAC 458-61-590 expressly deals with the “reconveyance” of real property “pursuant to a rescission.” It does not apply to REET paid on the initial conveyance of property but only provides an exemption from REET upon the “reconveyance” of the property. Thus, WAC 458-61-590 does not apply to this case, because the transaction at issue is a conveyance, not a reconveyance.³

WAC 458-61-590 is based on the statutory exemption provided in RCW 82.45.010(3)(c), which excludes from the definition of sale “[a] cancellation or forfeiture of a vendee’s interest in a contract for the sale of real property, whether or not such contract contains a forfeiture clause, or deed in lieu of foreclosure of a mortgage.” In contrast, there is no statutory provision allowing a refund of REET paid upon the initial real estate sale contract when there is a subsequent cancellation, forfeiture, or rescission of that contract.

3. Applicable case law does not allow REET refund for rescinded transaction.

³ In the present case, the rescission agreement was recorded on June . . . , 2004. The . . . County authorities properly stamped “Not Subject to Excise Tax” on that document the same day it was recorded. It is this second transaction that is exempt from REET pursuant to RCW 82.45.010(3)(c) and WAC 458-61-590, not the original sale agreement.

The above interpretation of the rescission rule is consistent with long-standing case law on the application of REET to a rescinded sale transaction.

In *Perkins v. King County*, 51 Wn.2d 761, 762-63, 321 P.2d 903 (1958), the Washington Supreme Court considered a similar situation. Perkins sold a hotel on a real estate contract and paid the applicable REET on the sale. Thereafter, a dispute arose between Perkins and buyer, and Perkins sued for forfeiture of the contract. The parties later reached an agreement under which the contract was rescinded and the lawsuit was settled. Perkins then applied to the county for a refund of the REET paid on the original conveyance. The court held that Perkins was not entitled to a refund of the REET.

The court explained its decision in *Perkins* as follows:

In the instant case, the appellant urges that rescission of the contract vitiated the sale completely,--in legal effect as though it had never occurred; and that, under the doctrine of unjust enrichment, the tax should be refunded by the county. The argument is an ingenious and superficially persuasive one. However, it is indigenous to the field of contract law. There, it is homogeneous, its thesis workable and proper. We are not able to comprehend its applicability in the field of taxation--at least, under the facts of the instant case.

The actions of the parties in rescinding the real estate contract certainly altered their legal relationships and, fictionally, may have vitiated the sale as far as their legal responsibilities were concerned. However, taxwise, their actions did not alter the facts of life: a sale, as defined by RCW 28.45.010, had been consummated, and a so-called taxable event or incident had occurred within the contemplation of the statute. The tax accrued. It was paid by the real-estate vendor to the proper county official. That should be--and as far as we are concerned it is--the end of the matter, because the legislature made no provision in the tax statute for a refund of the excise imposed and collected under the circumstances involved in the instant case. Whether the statute as written and presently administered should be changed, is a matter of tax policy that must be determined by the legislature, not by the courts.

Id. at 763.

Although the REET statute has been re-codified and amended since the date of the *Perkins* decision, the legislature still has not provided any exemption for transactions that are subsequently rescinded, nor excluded such rescinded transactions from the definition of "sale."

4. The exemption for inadvertent recording does not apply.

At the hearing, Taxpayer also compared this case to the situation in (the new) WAC 458-61-100(5)(c) (emphasis added):

(5) The authority to issue tax refunds under this chapter is limited to: . . .

(c) **The initial conveyance recorded in error by an escrow agent before the closing date, provided the property is conveyed back to the grantor**

It is our view that the situation in WAC 458-61-100(5)(c) only applies to inadvertent and premature recordings by an escrow agent before a closing date, which would need to be undone by a reconveyance in order to correct the transaction. We do not believe that it properly applies to the facts of this case. In fact, the initial sale was not recorded at all. Although the parties subsequently rescinded the entire transaction, that was because they did not wish to go through with the sales contract, not because the transfer was in error and needed to be corrected.

5. The Department has no authority to waive the REET despite any economic hardship.

As the court noted at the end of the *Perkins* decision, “[w]hether the statute as written and presently administered should be changed, is a matter of tax policy that must be determined by the legislature, not by the courts.” *Id.* at 763. Although the legislature may some day agree with Taxpayer that it is harsh to impose tax on a rescinded transaction, it has not yet changed the law to provide for an appropriate exemption.

In the absence of any applicable statute, the Department has no authority to grant a refund request in this case, notwithstanding any economic hardship.

DECISION AND DISPOSITION

For the reasons stated in this determination, Taxpayer's petition for refund is denied.

Dated 4th day of April, 2005.