

Cite as Det. No. 14-0233, 34 WTD 220 (2015)

BEFORE THE APPEALS DIVISION
 DEPARTMENT OF REVENUE
 STATE OF WASHINGTON

In the Matter of the Petition for)	<u>D E T E R M I N A T I O N</u>
Correction of Assessment of)	
)	No. 14-0233
)	
...)	Registration No. . . .
)	
)	

[1] WAC 458-61A-101; RCW 82.45.030: REAL ESTATE EXCISE TAX (REET) - CONTROLLING INTEREST TRANSFER - TRUE AND FAIR VALUE. In a sale of controlling interest in an entity that holds title to real property, the measure of the REET is determined by the true and fair value of the real property conveyed. Where the assessed value of property maintained on the county property tax rolls at the time of the controlling interest transfer reflects the impact of a permanent easement, this value reflects to true and fair value of the property.

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.

Kreger, A.L.J. – An LLC owning real property appeals a Real Estate Excise Tax Assessment (REET) on a controlling interest transfer, asserting that assessed value of the property or the selling price of the interest represents the true and fair value of the property in light of a permanent conservation easement, which significantly limits the use of the property. As the assessed value of the property on the county tax rolls reflects the true and fair value of the land under RCW 84.34.060, we conclude this value should have been used. Taxpayer’s petition is granted.¹

ISSUE

Where RCW 84.34.060 [determines the] true and fair value of open space land [for property tax purposes], and this value is reflected in the taxable assessed value used by the county, does this value also establish the true and fair value of the property under RCW 82.45.030(2)?

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

FINDINGS OF FACT

[Taxpayer] is a Washington limited liability company formed in 2006. The Taxpayer was formed primarily to hold two parcels of real property located in . . . Washington.

The property at issue was previously owned by [the previous owners]. In 1996 the [previous owners] entered into a permanent conservation easement (the Easement) with the United States Department of Agriculture. In exchange for the warranty easement deed, the [previous owners] received consideration of \$. . . . The Taxpayer provided a copy of the Easement at issue.

The Easement is authorized by the Wetlands Reserve Program under Title XII of the Food Security Act of 1965, as amended (16 U.S.C. 3837). The purpose and intent of the Easement is specified as:

To restore, protect, manage, maintain, and enhance the functional values of wetlands and other lands, and for the conservation of natural values including fish and wildlife habitat, water quality improvement, flood water retention, groundwater recharge, open space, aesthetic values, and environmental education.

Easement, second paragraph.

The easement runs with the land in perpetuity and binds the landowners as well as their “heirs, successors, assigns, lessees and any other person claiming under them.” Easement, third paragraph. This easement limits the uses of the property with the intent that the property eventually revert to its natural state. The landowners retain the right to access the property, and make undeveloped recreational use of the property, including hunting and fishing. The landowners have also expressly reserved the right to maintain a barn/storage shed on the property for the purpose of storing hay and farm equipment, and to maintain a bridge that crosses a portion of the . . . Slough. Easement Parts II & VIII. The landowners are specifically prohibited from:

1. Haying, moving, or seed harvesting for any reason;
2. Altering of grassland, woodland, wildlife habitat, or other natural features by burning, digging, plowing, disking, cutting or otherwise destroying the vegetative cover;
3. Dumping refuse, wastes, sewage, or other debris;
4. Harvesting wood products;
5. Draining, dredging, channeling, filling, leveling, pumping, diking, impounding, or related activities, as well as altering or tampering with water control structures or devices;
6. Diverting or causing or permitting the diversion of surface or underground water into, within, or out of the easement area by any means;
7. Building or placing building or structures on the easement area;
8. Planting or harvesting any crop; and
9. Granting or allowing livestock on the easement area.

Easement Part III.

As indicated by the terms of the easement and the relatively substantial sum paid to the [previous owners], the restrictions the Easement place on the property limit its value as it cannot be developed or built upon but is restricted to recreational access. The Taxpayer indicates that they primarily use the property to exercise dogs and for limited hunting activities.

In 1997 [the subsequent owners] acquired the property from the [previous owners]. The Taxpayer specifies that the value of the property at the time of that transfer was determined to be approximately \$. . . . The Statutory Warranty Deed filed with that transfer specified \$10 cash and other valuable consideration in return for the exchange. In 2006 the [subsequent owners] conveyed the property to the Taxpayer, listing a gross selling price on the property of \$. . . . The REET affidavit filed in conjunction with the transfer indicated that the property is classified as open space and lists a gross selling price of \$. . . , and REET excise tax was paid on this amount.

The Taxpayer originally had three members [Partner A, Partner B and Partner C]. In 2013 [Partner B] and [Partner C] each sold their 1/3 interest to [Partner A] for \$. . . , or a total of \$. . . . The Taxpayer filed a REET affidavit listing a value of \$. . . for the property.

Upon examination, the Special Programs Division of the Department of Revenue (Department) found that the amount reported on the REET affidavit as the value of the property was lower than the market value maintained on the county tax rolls. On June 27, 2013, Special Programs issued an assessment for an additional \$. . . , based on difference between the amount maintained as the market value on the county tax rolls of \$. . . and the \$. . . listed in the Taxpayer's affidavit. (We note that the assessment was imprecise in its description of the county tax information. The REET assessment states that the amount reported was lower than the county "assessed value," which is not accurate. In this case the county was actually assessing the property at the current use value, which under the 2013 assessed value of the properties totals to \$. . . . The REET assessment should have indicated that it was the "market value" on the county tax rolls that Special Programs relied upon.) The Taxpayer timely appealed the assessment.

The assessed value is consistent with the value of the property subject to the Easement. The Taxpayer believes that the difference between the assessed and market value in the . . . Country records may be due to a mistaken impression that the Easement is temporary rather than perpetual, so that the listed market value reflects the value of the properties were they not subject to the Easement at issue.

The Taxpayer stated that the property is its primary asset. Other than some equipment, which it estimates has a value of approximately \$. . . , the Taxpayer does not have any assets beyond the property itself.

ANALYSIS

The Taxpayer asserts that the current use value on the county tax rolls accurately reflects the value of the property, or alternatively that the sales price for 2/3 LLC interest establishes the current market value for the proportionate interest in the properties.

Chapter 82.45 of the Revised Code of Washington imposes an excise tax on every sale of real property located within this state unless the sale is specifically exempted from the tax. RCW

82.45.060; WAC 458-61A-100. The term “sale” for REET purposes “shall have its ordinary meaning and shall include any conveyance, grant, assignment, quitclaim, or transfer of the ownership of or title to real property . . . for a valuable consideration.” RCW 82.45.010(1). “The term ‘sale’ also includes the transfer or acquisition within any twelve-month period 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). In the case of a partnership, association, trust, or other entity a “controlling interest” means “fifty percent or more of the capital, profits, or beneficial interest in such partnership, association, trust, or other entity.” RCW 82.45.033(2); WAC 458-61A-101(2)(a)(ii).

With a controlling interest transfer, the measure of the tax is the “true and fair value” of the Washington real property owned by the entity. RCW 82.45.030(2) and WAC 458-61A-101(4); *McFreeze Corp. v. State, Dep’t of Revenue*, 102 Wn. App. 196, 201, 6 P.3d 1187, 1190 (2000) (In the sale of a controlling interest of a corporation, partnership, or other entity that owns Washington real property, “the value taxed is not the consideration paid, but the value of the real estate owned by the entity.”). As we explained in Det. No. 98-083, 17 WTD 271, 276 (1998), with respect to the sale of an interest in an LLC that owned Washington real property:

[T]he tax at issue . . . bears no relation to the funds received by the taxpayers for [their] interest in the LLC. Rather, the incident giving rise to the tax is the transfer of the beneficial ownership in real property located in this state. Accordingly, the amount of the tax is based on the value of the real property, not the interest in the LLC that was transferred.

It is also well settled that the tax is not prorated by the percentage of the interest being sold. *McFreeze Corp.* at 201, 6 P.3d at 1190 (“[N]othing in the statutes authorizes the taxpayer to apportion the tax. . . . [I]f the sale is 50 percent or more [of the entity], tax is on the full value of the real estate owned by the entity.”); Det. No. 00-083, 19 WTD 1037, 1040 (2000) (“Under the applicable provisions, the measure of the tax is the value of the real property, not the proportionate amount of the beneficial interest that was transferred.”); Det. No. 98-083, 17 WTD 271, 276 (1998). Accordingly, we conclude that the Taxpayer erred in reporting tax on the selling price of the \$. . . paid for the 2/3 interest rather than on the true and fair value of the real property.

In this case, because of the impact of the conservation easement the property fits within the definition of “open space land” under RCW 84.34.020.² The county tax rolls indicate that the current use of the property as having an approved open space restriction.

²RCW 84.34.020 provides:

(1) "Open space land" means (a) any land area so designated by an official comprehensive land use plan adopted by any city or county and zoned accordingly, or (b) any land area, the preservation of which in its present use would (i) conserve and enhance natural or scenic resources, or (ii) protect streams or water supply, or (iii) promote conservation of soils, wetlands, beaches or tidal marshes, or (iv) enhance the value to the public of abutting or neighboring parks, forests, wildlife preserves, nature reservations or sanctuaries or other open space, or (v) enhance recreation opportunities, or (vi) preserve historic sites, or (vii) preserve visual quality along highway, road, and street corridors or scenic vistas, or (viii) retain in its natural state tracts of land not less than one acre situated in an urban area and open to public use on such conditions as may be reasonably required by the legislative body granting the open space classification, or (c) any land meeting the definition of farm and agricultural conservation land under subsection (8) of this section. As a

The true and fair value of open space land is specifically defined by statute:

In determining the true and fair value of open space land and timber land, which has been classified as such under the provisions of this chapter, the assessor shall consider only the use to which such property and improvements is currently applied and shall not consider potential uses of such property.

RCW 84.34.060.

Having found that the records available are sufficient to detail the true and fair value of the property it is not necessary to address the Taxpayer's assertion that the sales price for the LLC interests may be used to establish the selling price for the property.

Because the conservation easement significantly limits the use of the property and was sufficient for the county to characterize it as open space property, the true and fair value of the property is prescribed by RCW 84.34.060. This amount in turn is also the true and fair value of the real property, for purposes of measuring the tax for the controlling interest transfer under RCW 82.45.030(2). Having found evidence of the true and fair value of the property, it is unnecessary to turn to the alternate valuation measures in RCW 84.45.030(4).

In this case under the statutes detailed above the true and fair value of the property at issue is the current use value,³ which is also the current assessed value. Accordingly, we conclude that the true and fair value of the open space, real property owned by the Taxpayer is the current assessed value of \$. . . . The Taxpayer's petition is granted.

DECISION AND DISPOSITION

The Taxpayer's petition is granted.

Dated this 21st day of July, 2014.

condition of granting open space classification, the legislative body may not require public access on land classified under (b)(iii) of this subsection for the purpose of promoting conservation of wetlands.

³ [In this case, on these facts, we conclude that the true and fair value of the property is the current use value. However, this determination cannot be cited as authority that any property subject to an easement in an open space program can, as a matter of law, use the current use valuation for REET purposes. That is not our holding. There must be an independent determination of the "true and fair value of the property" for each individual controlling interest transfer subject to REET, and that true and fair value may not always correspond to the current use value.].