

Cite as Det. No. 20-0100, 41 WTD 73 (2022)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 20-0100
)	
)	
...)	Registration No. ...

WAC 458-61A-101(2)(c); RCW 82.45.030: REAL ESTATE EXCISE TAX (REET) – MEASURE OF THE TAX – SELLING PRICE – NOMINAL SALE – PANIC SALE. The measure of REET is the true and fair value of the property conveyed, represented by the selling price. If property has been conveyed in an arm’s length transaction, a rebuttable presumption exists that the selling price is equal to the total consideration paid or contracted to be paid to the transferor. Evidence that a seller is under great pressure to sell the property quickly suggests they are not “a willing, but unobligated, owner,” making it likely the sale price does not reflect the 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.

LaMarche, T.R.O. – Taxpayer disputes the assessment of Real Estate Excise Tax (REET) on its purchase of certain real property located in Washington, arguing that the Department overstated the fair market value of the property for REET purposes, because it used the county assessed value on the tax rolls rather than the sale price that was negotiated between the parties. We deny the petition.¹

ISSUE

Under RCW 82.45.010, RCW 82.45.030, and WAC 458-61A-102, for purposes of assessing REET, was the selling price listed on the REET affidavit the “true and fair value” of the real property conveyed?

FINDINGS OF FACT

... (Grantor) entered into a purchase and sales agreement with ... (Grantee) on November 8, 2018, for the purchase of real property ... located at ... , in ... , Washington (the Property).² The Grantor filed a Real Estate Excise Tax affidavit (REET Affidavit) with ... County, Washington,

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

² Legal Description: Parcel No. ... , ... County, Washington. Property description: ...

dated . . . 2018, and listed a gross selling price of \$. . . , on which Grantor paid \$. . . ³ in state REET, \$. . . in local REET, and a \$. . . state technology fee, for a total of \$. . .

The Department of Revenue reviewed the REET Affidavit, and noted that the sales price of \$. . . was significantly lower [less than half] than the 2018 County's assessed value of \$ The Department concluded that the sale was a "nominal sale," and audited the transaction. It found that Grantor and Grantee were both listed as "Registered Agent/Governor" on a notice from the City of . . . dated . . . 2018. The Department's tax examiner contacted the County's Assessor's Office, which said that Grantor and Grantee were affiliates. The Assessor's Office told the examiner that Grantor had never appealed the tax assessed value of the Property. For these reasons, the Department concluded that the sale was not an arm's length transaction and the \$. . . selling price did not accurately reflect the true market of the Property.

Grantor contended to Audit that the \$. . . sale price was the true and fair value for the Property, explaining in its April 29, 2019, narrative provided during the audit that it sold the Property largely due to lack of capital needed to make substantial repairs mandated by the City. Grantor stated that the City had condemned the parking lot on the Property, and had posted notices about the dangerous condition of a retaining wall, which resulted in the Property's tenants ceasing to pay rent.

Grantor said that because of the condition of the Property, it was unable to obtain financing to make repairs, and believed it was highly unlikely any buyer could obtain financing through normal channels to purchase the Property. Grantor also stated that it was running out of time to pay a promissory note that was coming due. For these reasons, Grantor stated, it was left only with the option of selling it to a cash buyer who could immediately comply with the City's requirements, which Grantor estimated would cost more than \$. . . [a quarter of the 2018 County assessed value]. There is no indication that Grantor offered the Property for sale to the general public.

During the audit, Grantor did not provide proof of repair costs, and did not provide a copy of a professional appraisal. Grantor also indicated that it did not allocate assets under section 1060 of the Internal Revenue Code of 1986 (as amended).

The Department concluded that the evidence did not support Grantor's claim that the selling price of \$. . . reflected the true and fair market value for the Property, and assessed REET on the difference between the County's 2018 assessed value of \$. . . and the selling price of \$. . . , or \$ The Department issued a balance due notice on May 13, 2019, Letter ID . . . , totaling \$. . . ,⁴ which consisted of \$. . . in REET, and \$. . . in interest. Grantor did not pay the assessment, but timely filed a petition for review.

Grantor states that its owner and Grantee's owner are friends. Grantor says that its owner is a mortgage broker, whose intent was to purchase the Property, make repairs, and "flip" it for a profit. In email correspondence on September 16, 2019, Grantor stated that it had been in negotiations with Grantee for the purchase of the Property for several months.

³ All figures are rounded unless otherwise noted.

⁴ One dollar difference is due to rounding.

Grantor contends that although there was tacit agreement that Grantee would purchase the property, Grantee had to obtain funding for the purchase from hard money lenders due to the condition of the Property. Grantor states that pending the sale it agreed to make Grantee its property manager, and believes this was the basis for what it claims was the County's erroneous statement to the auditor that the parties were affiliated.

There are several documents pertinent to this case, detailed as follows.

Purchase and Sale Agreement. The purchase and sale agreement in dispute between Grantor and Grantee dated . . . 2018 (Purchase and Sale Agreement), shows the purchase price of \$. . . for the Property, and on Form . . . , Section . . . , at . . . , states: "4. buyer is buying in as is condition including retaining wall issue."

Settlement Statement. The final settlement statement shows a settlement and disbursement date of . . . 2018. The statement lists the sale price of the Property as \$. . . The statement indicates that nearly all of the proceeds, \$. . . , were paid to . . . [Entity A], LLC. . . . [Entity A], LLC was a Washington company whose sole governing member was . . . (Attorney), Grantor's representative in this case. As described in more detail below, . . . [Entity A], LLC had loaned money to Grantor on the Property.

County valuation and prior sales information. The Assessor's website⁵ indicates that the Property was valued at \$. . . [an amount 60 percent higher than 2018 sales price] in 2016, \$. . . in 2017, \$. . . in 2018, and \$. . . in 2019 [an increase of approximately 15-20 percent per year]. The sales history for the Property listed on the website indicates that the Property was sold for \$. . . [an amount approximately 60 percent higher than 2018 sales price] in June 2005 to . . . [two individuals], then quitclaimed to . . . (Prior Owner) alone for \$0 in September 2005, who then sold it to Grantor for \$. . . [an amount approximately 20 percent higher than 2018 sales price] in May 2017. The May 2017 sale is memorialized in a statutory warranty deed dated May . . . , 2017. Although requested to do so, Grantor has provided no information about its May 2017 purchase.

Ownership interests of Grantor and Grantee. Grantee provided documents from the Washington Secretary of State dated September . . . , 2017, which included a copy of its annual report. The annual report indicates that Grantor's sole governing member is Owner, and that Owner is the sole registered agent. The Secretary of State [documents] indicate that the sole governing member of Grantee is Grantee's Owner, and its registered agent has always been Attorney.

Deed of Trust and promissory note between Grantor and [Entity A], LLC. County records show Grantor conveyed a deed of trust, recorded on October . . . , 2017, to Attorney as Trustee, on behalf of beneficiary [Entity A], LLC. The deed secures a \$. . . promissory note [approximately in the same amount as the 2018 sales price] between Grantor and [Entity A], LLC, dated May . . . , 2017. Secretary of State records show, as indicated above, that Attorney was the sole governing member of the lender, [Entity A], LLC.

⁵ The . . . County Assessor's website address is

The promissory note states that \$. . . [approximately 66 percent] of the loan is for closing on the Property, and \$. . . [approximately 34 percent] is for repairs. The promissory note states there is no debt on the Property at the time of the agreement. The deed of trust to [Entity A], LLC was recorded on October . . . , 2017.

. . . **2018 Notice to Comply.** The City’s Police Department’s Code Enforcement Unit issued a notice to Grantor [in] . . . , 2018 (2018 Notice to Comply). The notice was addressed to both Grantor in care of . . . , Grantor’s owner, and Grantee as Grantor’s “Registered Agent/Governor.” The 2018 Notice to Comply indicates that the Code Enforcement Unit inspected the Property and found that it required significant repairs, including repair or replacement of a handicapped ramp; repair to the Property’s right of way; and repair or replacement of the retaining wall along the Property’s east alleyway supporting the elevated parking area. The notice described the retaining wall as being in a “dangerous condition,” and said that it showed deterioration in the form of buckling, cracking, leaning, and crumbling, to the extent that the retaining wall was beginning to detach from the parking lot slope.

The Code Enforcement Unit stated that Grantor was in violation of several city ordinances, and had until [one month later in] . . . , 2018, to take corrective action, or be subject to a hearing before the city’s hearing examiner and an assessment of fines and/or costs. The notice stated that the retaining wall section of the property had been condemned in . . . , 2014, on the basis that it was not safe for motor vehicle use, including parking.

. . . **2018 letter to City.** Attorney wrote a letter to the Code Enforcement Unit [one month later in] . . . , 2018, stating: “My client, . . . [Grantee] has just entered into agreement to purchase [the Property] from . . . [Grantor]. It is expected we will be closing on sale at the end of this month.”

. . . **[Second] 2018 Notice to Comply.** The Code Enforcement Unit issued a second notice [later in] . . . , 2018 ([Second] 2018 Notice to Comply). The notice was addressed to three parties, as follows:

Property Owner:

. . . [Grantor]

Registered Agent/Governor: . . . [Grantor’s owner]

[Grantor’s address]

Property Associate pays City of . . . Water Services:

. . . [Grantee’s Owner]

[Grantee’s Owner’s address]

Property Owner Attorney Representative:

[Attorney]

[Attorney’s address]

The [Second] 2018 Notice to Comply indicated that the Code Enforcement Unit had re-inspected the property after it received a new complaint, and found no repairs had commenced. The notice gave Grantor until [the end of] . . . , 2018, to obtain all permits required to bring the Property into

compliance with city code and the International Property Maintenance Code, and to remove, repair, or replace the handicapped ramp.

. . . **2015 City code violation order.** The code violations listed in the 2018 Notice to Comply sent to Grantor had originally been observed in 2015, when the Property was owned by Prior Owner. City Code Enforcement sent a notice to comply to Prior Owner, who failed to make the required repairs. The City held a violation hearing, and the Violations Hearing Examiner found that Prior Owner was in violation of City code. The Examiner issued an order [in] . . . , 2015 (2015 Code Violations Order), which fined Prior Owner, and ordered him to complete all repairs to the Property by August . . . , 2015. The order stated that failure to comply with the order would be a misdemeanor. The order further provided that if Prior Owner failed to comply, the City was authorized to undertake and complete abatement of the violations at the full expense of Prior Owner. The 2015 Code Violations Order and related documents were recorded on the Property [in] . . . , 2015.

Geo-tech report. Grantor provided a geo-technology (geo-tech) engineering firm's report dated April . . . , 2018. The Geo-tech Report described the conditions noted in the City's notices, proposed retaining wall designs for the Property, and listed the scope of repairs. The report did not contain a bid or other indication of cost.

Retaining wall repair bids. Grantor provided a copy of an undated bid given to Grantee that estimated that repairs to the two retaining walls described in the Geo-tech Report, including preparation, back fill, and grading, would cost \$. . . [approximately 38 percent of the 2018 sales price]. This excluded permits and engineering costs. A second bid dated . . . , 2018, estimated repairs to the retaining walls, and building of drainage system at \$. . . [approximately 45 percent of the 2018 sales price], not including engineering, permits, sales tax, paving, or material disposal.

After filing its petition, Grantor stated that after the sale Grantee had made the repairs required by the City; however, Grantor did not provide evidence showing the actual amount paid for the repairs. Taxpayer also submitted an estimate of costs for a professional appraisal of the Property, but no appraisal was ever provided.

Median home prices in . . . County, where the Property is located, rose 12.5% in one year from \$. . . in Quarter 2, 2017 (Q2 2017) to \$. . . n Q2 2018.⁶ . . .

⁶ University of Washington and Washington State Department of Licensing Real Estate Commission, Washington Center for Real Estate Research, Washington State's Housing Market, 2nd Quarter 2018, *Median Home Prices, State of Washington and Counties Time Trend*, at 15, <http://realestate.washington.edu/wp-content/uploads/2018/08/2018Q2WSHMR.pdf> (last accessed November 26, 2019).

ANALYSIS

REET is imposed upon the sale of real property in Washington. RCW 82.45.060. REET is measured by the “selling price.” RCW 82.45.030; WAC 458-61A-102(22) (REET Rule 102).

RCW 82.45.030 defines “selling price” as follows:

(1) As used in this chapter, the term “selling price” means the true and fair value of the property conveyed. If property has been conveyed in an arm's length transaction between unrelated persons for a valuable consideration, a rebuttable presumption exists that the selling price is equal to the total consideration paid or contracted to be paid . . .

(Emphasis added.)

Secretary of State records do not indicate that Grantee and Grantor, and their respective owners, had common ownership interests. We also note Grantor’s explanation that although Grantee was listed as “governor/registered agent” on the City’s . . . 2018 Notice to Comply, Grantee acted only as the property manager. This is supported by the [Second] 2018 Notice to Comply, which lists Grantee’s owner as “Property Associate pays City of . . . Water Services.” Other factors, though, indicate that the sale may not have been an arm’s length transaction.⁷

However, assuming, solely for purposes of argument and without deciding, that the transaction was made at “arm’s length,” this gives rise to a *rebuttable* presumption that the \$. . . sales price reflected the “true and fair value” of the Property. We turn now to whether the facts presented rebut the presumption in RCW 82.45.030(1).

We cannot determine true and fair value based on speculation, but must look to the objective evidence. *See In re Westlake Ave.*, 40 Wash. 144, 150, 82 P.279 (1905). As the court stated in *In re Westlake*, market value is not limited to the value of the property to the owner. Instead,

The market value of property is the price which it will bring when it is offered for sale by one who desires, but is not obliged, to sell it, and is bought by one who is under no necessity of having it. In estimating its value, all the capabilities of the property, and all the uses to which it may be applied or for which it is adapted, are to be considered, and not merely the condition it is in at the time and the use to which it is then applied by the owner. It is not a question of the value of the property to the owner

⁷ Grantor’s owner and Grantee’s owners are admittedly friends. Alone, this factor does not mean a transaction cannot be at arm’s length between the parties. However, Attorney, through his solely-owned LLC, [Entity A], loaned Grantor \$. . . [approximately the same amount as the 2018 sales price in] . . . , 2017, which was secured by the Property, and [Entity A], LLC was repaid out of the sale proceeds. Attorney was the registered agent for Grantee, and represented both parties during the course of the disputed transaction. Moreover, the evidence indicates Grantor did not advertise the Property to the general public, or take other steps to find buyers, other than offering the Property for sale directly to Grantee. These factors indicate that this was not a typical sale. Taken together with the unusually low sales price, the facts indicate that, more likely than not, the sale was not an “arm’s length” transaction between “unrelated parties.” RCW 82.45.030(1). However, as we will discuss, we do not base our decision on this finding.

Id. (Emphasis added.) See also *Donaldson v. Greenwood*, 40 Wn.2d 238, 252, 242 P.2d 1038 (1952) (“‘Fair market value’ means neither a panic price, auction value, speculative value, nor a value fixed by depressed or inflated prices. We have defined it as the amount of money which a purchaser willing, but not obliged, to buy the property would pay an owner willing, but not obliged, to sell it.”) (Emphasis added.)

The court’s analysis in *Westlake* is reflected in WAC 458-61A-101(2)(c) (REET Rule 101), which states that “true and fair value” is defined as “market value, which is the amount of money that a willing, but unobliged, buyer would pay a willing, but unobligated, owner for real property, taking into consideration all reasonable, possible uses of the property.” REET Rule 101(2)(c) (emphasis added).

Here, Grantor indicates that it was under great pressure to sell the property quickly—essentially the “panic sale” the court describes in *Donaldson*, 40 Wn.2d at 252. Also, Grantor indicates that it offered the Property for sale only to Grantee. These factors indicate that at the time of sale, Grantor was not “a willing, but unobligated, owner,” making it likely the \$. . . sale price did not reflect the true and fair value of the Property. REET Rule 101(2)(c).

Further, although the condition of the Property required repairs, “all of the capabilities of the property and the uses to which it could be applied, . . . not merely the condition it is in at the time” indicate that the true and fair value of the Property should reflect the value of the Property as improved and put to use as a fully tenanted rental property. *In re Westlake Ave.*, 40 Wash. 144, at 150 (emphasis added); REET Rule 101(2)(c).⁸

Grantor argues that at the very least, approximately \$. . . in estimated repairs should be subtracted from the county assessed value of the Property for REET purposes. However, we note that the condition of the Property was described in the City’s hearing order recorded on the Property in 2015 that required Prior Owner to make the repairs, and the Assessor would likely have been aware of those issues when valuing the Property in subsequent years. The Assessor also likely would have been aware that Grantee had applied for building permits, which would indicate that an adjustment to the county assessed value might be needed to account for improvements. The Assessor increased the assessed value of the Property by exactly \$. . . [the same amount as the estimated amount of repairs and approximately 50 percent of the 2018 sales price] the year after the disputed sale, to \$. . .

The \$. . . increase in value on the county rolls is a significant departure from the prior value, and although Grantor has provided no proof of the actual cost of repairs, this is approximately the same amount the contractors bid to complete the repairs required by the City. . . . The preceding factors

⁸ We note that Grantee purchased the Property “as is.” Given that immediately prior to the sale the City could force Grantor to make repairs to the Property or make those repairs itself at Grantor’s expense, as well as impose fines on Grantor for failure to make the repairs, purchasing the Property “as is” could be construed as Grantee’s assumption of that substantial liability. As an owner of the Property, Grantee would be legally required to make the repairs after the sale, and Grantee was aware of this when entering into the sales agreement. RCW 82.45.030(3) provides that assumption of liability is also a form of “total consideration paid or contracted to be paid” that is included in the measure of REET. This further indicates that \$. . . [2018 sales price] does not reflect the true and fair value of the Property.

indicate it is more likely than not that the Assessor took the poor condition of the Property into account when determining the 2018 assessed value.

Grantor argues further that its purchase from the Prior Owner for \$. . . in 2017 supports a lower true and fair market value for the sale at issue here. However, the only evidence in the record about that sale is the sales price listed on the county assessor's website. Although the Department requested documentation to support Grantor's claim that the prior sale of \$. . . supported a lower fair market value, Grantor provided no evidence about that prior sale, including whether other forms of consideration were exchanged.

It is clear, however, that at the time of the sale, Previous Owner was in violation of the 2015 Code Violations Order because he had failed to complete the mandated repairs by August . . . , 2015. Previous Owner's failure to comply constituted a misdemeanor, and gave the City the authority to undertake the repairs itself at his expense, and take other enforcement actions against him, including imposing additional fines. At the time of sale to Grantor, Prior Owner had been in violation of the order for more than nine months. Like the "panic sale" described in *Donaldson*, 40 Wn.2d at 252, Prior Owner was under significant duress to sell quickly, which makes it more likely than not that the \$. . . selling price in the transaction between Grantee and Previous Owner in May 2017 did not reflect the true and fair value of the Property.

In addition to the considerations above, the evidence also indicates that the disputed selling price of \$. . . is a "nominal sale" that does not reflect the true and fair value of the Property.

RCW 82.45.100(4) states:

If upon examination of any affidavits or from other information obtained by the department or its agents it appears that all or a portion of the tax is unpaid, the department must assess against the taxpayer the additional amount found to be due plus interest and penalties.

(Emphasis added.)

WAC 458-20-303 (REET Rule 303), the Department's administrative rule that addresses REET affidavits, requires that affidavits be "complete," stating:

[A]n affidavit is incomplete if any required information is omitted or obviously incorrect, such as the use of a nominal selling price. A nominal selling price is an amount stated on the affidavit that is so low in comparison with the fair market value assessment stated on the property tax rolls that it would cause disbelief by a reasonable person. In the case of a nominal selling price, the county assessed value will be used as the selling price, unless there is an independent appraisal showing a greater value.

REET Rule 303(6)(b) (emphasis added).

As we discuss above, the REET Affidavit showed a selling price of \$. . . in 2018 for [the Property], which was listed on the 2018 County rolls at \$. . . [more than twice the selling price]. The \$. . . sales price is only approximately 44% of the \$. . . county assessed value that year. We note that the Property's value on the tax rolls increased to \$. . . [an amount 63 percent higher than selling

price] the following year, and the median residential home price in the County for the second quarter of 2018 was \$. . . [an amount 57 percent higher than selling price]. Moreover, real estate prices in the area were rising rapidly and there was limited inventory and a strong “seller’s market” for properties in the County at the time of sale.

For these reasons, we find the selling price to be “nominal,” because it “is so low in comparison with the fair market value assessment stated on the property tax rolls that it would cause disbelief by a reasonable person.” REET Rule 303(6)(b). As indicated above, in the case of a nominal sale, the REET is based on the value listed in the county tax rolls, as was done in the audit, or the value shown in an independent appraisal, if it shows a higher value. REET Rule 303(6)(b). [Here, Taxpayer did not provide an appraisal.]

In conclusion, we find that the \$. . . sale price for the Property does not reflect the “selling price” under RCW 82.45.030(1) for REET purposes, and conclude that the Department properly assessed tax based on the \$. . . value listed the County’s tax rolls for 2018. RCW 82.45.060; REET Rule 101(2)(c); REET Rule 102(22); REET Rule 303; *In re Westlake Ave.*, 40 Wash. 144; *Donaldson v. Greenwood*, 40 Wn.2d 238. Accordingly, we deny the petition.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 25th day of March 2020.