

FINAL BILL REPORT

HB 1664

C 209 L 99

Synopsis as Enacted

Brief Description: Preventing the use of step transactions to avoid real estate excise tax.

Sponsors: Representatives Dickerson, Thomas and Dunshee; by request of Department of Revenue.

House Committee on Finance
Senate Committee on Ways & Means

Background:

The real estate excise tax (REET) is imposed on each sale of real property. The state tax rate is 1.28 percent. Additional local taxes are allowed. Cities and counties may impose an additional 0.25 percent tax for capital improvements. Cities and counties may also impose a second 0.25 percent tax for capital projects specified in a city or county's comprehensive plan. An additional tax of 0.5 percent is available for cities and counties not imposing the second 0.5 percent of the local sales tax. A county may impose an additional 1 percent tax for acquisition and maintenance of conservation areas if this rate is approved by voters.

The seller of real property pays REET, except the one percent county conservation rate which is paid by the buyer.

REET applies when a sale occurs. A sale is defined as any conveyance, grant, assignment, quitclaim, or transfer of the ownership of or title to real property. A sale of a controlling interest in a partnership or corporation is generally treated as a sale of the real estate owned by the partnership or corporation for the purposes of REET. However, REET does not apply to real property transfers resulting from the formation, liquidation, dissolution, or reorganization of entities if the transactions do not result in federal income tax liability.

It is possible to transfer effective control of real estate without REET liability using a "step transaction." A buyer can contribute capital to a corporation or partnership to dilute the current owner's interest to less than 50 percent. The buyer can then purchase the minority interest and liquidate the business. Since real property transfers involving formation, liquidation, dissolution, or reorganization of entities are not subject to the real estate excise tax, the result is the transfer of real property without payment of the tax.

Summary:

The exemption from the real estate excise tax for real property transfers involving the formation, liquidation, dissolution, or reorganization of partnerships and corporations is narrowed. Under this narrower exemption, the tax applies if all of the following conditions are met:

- there is more than one of these formation, liquidation, dissolution, or reorganization transactions within a 12-month period;
- the result is the transfer of a controlling interest in any entity with an interest in real property in this state; and
- one or more persons previously holding a controlling interest in the entity receive cash or property for the interest.

When these conditions are met, real estate excise tax is due from the person who previously held the controlling interest in the entity.

However, tax does not apply to a person who receives real property that the person originally contributed to the entity, a person who did not contribute real property to the entity, or a person that did not have an interest in the entity when real property was purchased.

Votes on Final Passage:

House 96 0
Senate 47 2

Effective: July 25, 1999