




STATE OF WASHINGTON  
DEPARTMENT OF REVENUE

DATE: January 12, 2009

TO: County Treasurers  
Administrators of the Real Estate Excise Tax

FROM: Stuart Thronson, Assistant Director, Special Programs Division 

SUBJECT: Application of the Real Estate Excise Tax on "Short Sales"

This correspondence is in follow up to my January 8, 2009 memorandum on "short sales" and the relief of debt in calculating the Real Estate Excise Tax (REET). On January 9, 2009 the Department held a meeting with over 40 representatives from the escrow and title industries, as well as realtors and real estate attorneys from around Washington State. The purpose of the meeting was for the Department to learn more about how "short sales" and debt forgiveness transactions work in the current market in order to determine proper calculation of the REET

The meeting was helpful in providing additional input about the nature of these transactions and the Department has carefully reconsidered its interpretation of the applicable statutes.

Background

All sales of real property are subject to the REET unless specifically exempted by statute. The measure of the tax is based on the total selling price of the property conveyed. RCW 82.45.030 defines "selling price" as 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 to the transferor, or to another for the transferor's benefit." The same statute goes on to define the term "total consideration paid or contracted to be paid" as including "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 encumbrance, either given to secure the purchase price, or any part thereof, or remaining unpaid on such property at the time of sale." (Emphasis added)

Application to Short Sale Transactions

Short sales are distinguishable from other transactions involving the forgiveness of debt because the seller negotiates separately with the lender for any debt reduction/forgiveness.

Ordinarily, if a homeowner owed \$350,000 on his/her mortgage, but sold the house for \$300,000, he/she would still be liable for the remaining amount due on the debt. However, in the "short sale" situation, the financial institution may agree to forgive the remaining amount it is owed. The seller has been spared upwards of \$50,000 in personal liability. Alternatively, the financial institution may simply release their lien on the property, but require a personal note from the seller for repayment of the balance.

In either scenario, if the purchase price in a short sale transaction is the fair market value for the property, the amount of the debt owed by the seller exceeding the purchase price is not deemed consideration, because **it is not paid or delivered in return for the sale of the property**. The escrow agent, title company or others involved in the sale may or may not know whether the remaining debt owed by the seller is forgiven or converted to another instrument at closing. The forgiveness of debt in this case is a negotiated transaction between the seller and the financial institution independent of the sale of the property. This important element distinguishes these transactions from other transfers of property involving the forgiveness of debt.

#### Refund Process

Sellers who previously paid REBT on the amount of the forgiven debt in a short sale transaction may be entitled to a refund of the excess tax paid. Forms and instructions for requesting a refund can be found on the department's web site at:

<http://dor.wa.gov/Docs/forms/RealEstExcsTx/RealEstExTxRefundReq.pdf>

cc: Cindi Holmstrom, Director  
Leslie Cushman, Deputy Director  
Tremaine Smith, Senior Assistant Director  
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