

Let's do the math on price vs. assessed value

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For some time, you have been looking to purchase an office building to expand your business. After investigating the market, you locate the perfect building and negotiate a purchase price of \$7.5 million. You are delighted with the price because it is less than the tax-assessed value of the property, which is \$9.6 million.

The discount from the tax-assessed value reflects in part the need for improvements to the office building, but also the decline in market values that has taken place during the recent recession.

At closing, you review the settlement statement and discover that the Virginia recording taxes have been calculated using the tax-assessed value of the office building rather than your purchase price. You ask the settlement agent which value should be used, and the response is that the clerk's office requires the use of the greater of the tax-assessed value or the purchase price.

You ask your settlement agent what is the difference between the amount of recording taxes using the tax-assessed value and the purchase price and learn that the difference is about \$9,000 for the state and local recording taxes and the Virginia grantor's tax. Puzzled about the difference, you ask your lawyer which value should be used.

The Virginia code states that the state recording tax is based on "the consideration of the deed or the actual value of the property conveyed, whichever is greater."

In our example, the purchase price (consideration) negotiated between the seller and the buyer is less than the tax-assessed value of the office building. The question is whether the purchase price negotiated between the parties or the tax-assessed value more properly reflects the "actual value" of the property for purposes of calculating the Virginia recording tax.

The Virginia attorney general and tax commissioner have both concluded that "actual value" as used in the Virginia code is synonymous with fair market value and is not necessarily equal to the tax-assessed value of a property.

If "actual value" is synonymous with fair market value, then in an arm's-length transaction negotiated between disinterested and unaffiliated parties, the recording tax should be based on the purchase price for the property, even if the purchase price is less than the tax-assessed value. In a real estate market with declining property values, it is not uncommon for the negotiated purchase price to be less than the tax-assessed value. Adjustments in tax-assessed values often lag behind changes in the marketplace, and negotiated purchase prices may reflect more accurately the fair market value.

Both the attorney general and the tax commissioner have identified circumstances in which the stated consideration in the deed for a property should not be used for calculating recording taxes.

Examples of four such situations are transfers of property arising out of foreclosure sales, transfers of property between affiliated persons or family members, bulk sales of properties and transfers for only nominal consideration.

In each situation, the consideration paid for the transfer of the property may be less than the fair market value of the property and thus should not be used to calculate recording taxes. In the absence of any other indication of fair market value - such as an appraisal - the tax-assessed value of the property may be a better indicator of fair market value and may be used to calculate recording taxes.

In our example, the seller and purchaser of the office building are not affiliated with or related to each other, and the purchase and sale of the office building have been negotiated at arm's length. The fact that the purchase price is less than the tax-assessed value for the office building reflects both the condition of the office building and the decline in property values that has occurred during the recent recession. In this situation, the consideration of \$7.5 million is a better indicator of fair market value than is the \$9.6 million tax assessment.

If the Virginia General Assembly had intended that recording taxes be based on tax-assessed values, the legislature could have easily stated this rule. The Virginia General Assembly has not taken this approach, however, and has stated that the recording tax should be based on the greater of the purchase price of the deed or the actual value of the property. Absent any special factors to indicate the purchase price does not reflect fair market value - like those identified by the attorney general and tax commissioner - the purchase price should be used for calculating Virginia recording taxes.

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