

Tax Tips

Potential Tax Trap: Real Estate Transfer Taxes and Entity Acquisitions

State and local real estate transfer taxes can be a significant and sometimes overlooked cost in certain acquisition transactions. In many states, including Illinois, the transfer of a controlling interest in an entity that owns real estate can trigger a real estate transfer tax, even though the real estate itself is not transferred. Currently, 16 states impose some sort of a real estate transfer tax upon the transfer of a controlling interest in an entity that owns real estate located in that state.

The transfer of a controlling interest for real estate transfer tax purposes typically means a transfer of “control,” which can be as little as 50 percent and as high as 90 percent, depending on the real estate transfer tax laws of the relevant state. Many states aggregate certain transfers of interests occurring within a particular time frame in determining whether there is a transfer of “control.” Illinois, for example, aggregates certain transfers that occur over a two-year period. Additionally, many states require that the entity be a “real estate entity” in order to impose a real estate transfer tax upon a transfer of control. A “real estate entity” generally means an entity engaged in a real estate business where a certain minimum percentage of its income and assets are derived from or consist of real estate.

Certain real estate transfers (including certain transfers of a controlling interest in a real estate owning entity) are exempt from real estate transfer taxes. Although the laws vary from state to state, exempt transfers typically include: (i) an exchange of interests in an entity in order to effectuate a mere change of identity or form of ownership or organization where there is no actual change in beneficial ownership, (ii) transfers involving a parent and subsidiary, (iii) mergers between

corporations and (iv) transfers of interests in publicly traded companies. The types of exemptions and the legal conditions for claiming exemptions differ greatly from state to state and require an analysis of the relevant state’s real estate transfer tax laws in order to properly ascertain whether a real estate transfer tax may be due.

As more and more states look to increase revenues, the trend will be for more states to expand the application of real estate transfer taxes to transfers of controlling interests in real estate owning entities. Accordingly, more and more acquisition transactions involving the transfer of a controlling interest in an entity are likely to trigger real estate transfer taxes. Clients engaged in an acquisition transaction should be made aware of the potential costs resulting from an imposition of real estate transfer taxes and should take these costs into consideration when evaluating the overall cost of the acquisition and in allocating these costs among the parties to the acquisition.

If you have any questions or need assistance regarding the possible imposition of real estate transfer taxes in acquisition transactions, please contact **David P. Dorner** at +1 (312) 609 7764 or **Timothy W. O’Donnell** at +1 (312) 609 7683.

FEDERAL TAX NOTICE: Treasury Regulations require us to inform you that any federal tax advice contained herein is not intended or written to be used, and cannot be used, by any person or entity for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code.

Principal Tax Members of the Tax & Estate Planning Group

Denise L. Blau +1 (212) 407 7755	Daniel T. Sherlock, <i>Co-Chair</i> +1 (312) 609 7551	Amy E. Lewis +1 (312) 609 7837
Jonathan H. Bogaard +1 (312) 609 7651	Robert F. Simon +1 (312) 609 7550	Peter T. Wynacht +1 (312) 609 7965
Matthew P. Larvick +1 (312) 609 7970	William F. Walsh +1 (312) 609 7730	
Timothy W. O'Donnell, <i>Co-Chair</i> +1 (312) 609 7683	David P. Dorner +1 (312) 609 7764	

VEDDER PRICE®

222 NORTH LASALLE STREET

CHICAGO, ILLINOIS 60601

T: +1 (312) 609 7500 | F: +1 (312) 609 5005

1633 BROADWAY, 47TH FLOOR

NEW YORK, NEW YORK 10019

T: +1 (212) 407 7700 | F: +1 (212) 407 7799

1401 I STREET NW, SUITE 1100

WASHINGTON, D.C. 20005

T: +1 (202) 312 3320 | F: +1 (202) 312 3322

200 ALDERSGATE

LONDON EC1A 4HD

T: + 44 (0)20 3440 4680 | F: + 44 (0)20 3440 4681

www.vedderprice.com

The Vedder Price Tax & Estate Planning Group

Business Tax Planning & Compliance

Due to the complexity and constantly changing nature of the federal, state and local tax laws, the tax aspects of almost every type of business and personal transaction require scrutiny by a tax attorney. At Vedder Price, this experience is provided by the members of the tax group, each of whom has had substantial formal tax education, including in some cases advanced degrees in taxation, as well as practical experience in resolving tax problems.

In addition to advising the firm's business clients with respect to the tax issues involved in the everyday operation of a corporation, limited liability company, partnership or sole proprietorship, Vedder Price's tax attorneys plan for and provide advice on the tax aspects of taxable and nontaxable acquisitions of business entities, mergers, recapitalizations, the organization and liquidation of entities, taxable and nontaxable sales and exchanges of assets, foreign operations, redemptions, distributions, and the public and private offering of securities.

Besides representing corporations, limited liability companies, partnerships and sole proprietorships, members of Vedder Price's tax group have substantial experience with respect to a wide variety of other entities, including S corporations, professional service corporations, regulated investment companies, real estate investment trusts and unit investment trusts, and provide advice regarding the desirability of using these entities and the special tax issues encountered by each of them.

About Vedder Price

Vedder Price is a business-oriented law firm composed of more than 265 attorneys in Chicago, New York, Washington, D.C. and London. The firm combines broad, diversified legal experience with particular strengths in commercial finance, corporate and business law, financial institutions, labor and employment law and litigation, employee benefits and executive compensation law, occupational safety and health, general litigation, environmental law, securities, investment management, tax, real estate, intellectual property, estate planning and administration, health care, trade and professional associations and not-for-profit organizations.

Tax Tips is published periodically by the law firm of Vedder Price P.C. It is intended to keep our clients and interested parties generally informed on tax issues and developments. It is not a substitute for professional advice. For purposes of the New York State Bar Rules, this bulletin may be considered ATTORNEY ADVERTISING. Prior results do not guarantee a similar outcome.

Vedder Price P.C. is affiliated with Vedder Price LLP, which operates in England and Wales.

© 2011 Vedder Price P.C. Reproduction of this bulletin is permissible only with credit to Vedder Price. For additional copies, an electronic copy of this bulletin or address changes, please contact us at info@vedderprice.com.