August 10, 2012

[redacted]

Re: **Redacted Formal Ruling 2012-06**

Dear [redacted]:

This is a formal ruling for [redacted] regarding the applicability of property transfer tax to its proposed transfer of property. This ruling is based upon representations in your letter of [redacted]

RULING

Based upon the facts presented, it does not appear that the proposed transfer falls under any exemption from the property transfer tax.

FACTS

[redacted] is the municipal housing authority for the [redacted], created under Chapter 113 of Title 24 of the Vermont Statutes Annotated.

The [redacted] is an exempt organization under Section 501(c)(3) of the Internal Revenue Code, organized to provide housing to low income residents of the [redacted].

[redacted] and [redacted] co-own a property at [redacted] in a joint venture to provide low-income housing opportunities. That [redacted] property is valued by the City of [redacted] at over [redacted].

[redacted] and [redacted] also co-own [redacted], a limited liability company which is wholly-owned and operated by [redacted] and [redacted]. [redacted] owns and operates several low-income housing projects. [redacted] is not a 501(c)(3) exempt organization.

[redacted] and [redacted] are considering the transfer of their [redacted] for financial reasons and to increase efficiency of operations of the three entities. The transfer of the [redacted] property will not be a transfer made at the time of formation of [redacted]. The transfer will be without consideration other than assumption by [redacted] of the debt which is secured by the property and assumption of the Federal Housing and Urban Development contract obligations related to the property. After the transfer, the [redacted] property will continue to be used as affordable housing.

DISCUSSION

You have asked for a ruling on whether Vermont's property transfer tax will apply to the transfer of the [redacted] property from [redacted] and [redacted] to their wholly-owned limited liability company [redacted].

Vermont's property transfer tax is generally imposed at the rate of one and one-quarter percent of the value of property transferred. 32 V.S.A. § 9602. Where the transfer is for nominal consideration, the taxable value is the fair market value. 32 V.S.A. § 9601(6). Since your transfer will be for nominal consideration, the taxable value would be the fair market value. The tax is imposed upon the transferee, which in your case is [redacted]. 32 V.S.A. § 9604.

The transfer tax law exempts certain specified types of transfers, but none of these exemptions would apply to exempt your transfer to [redacted].

The one exemption which is somewhat relevant to this transfer is in Subsection (20), as follows:

> § 9603. Exemptions
>
> The following transfers are exempt from the tax imposed by this chapter:
>
> * * *
>
> (20) Transfers made to organizations qualifying under Section 501(c)(3) of the Internal Revenue Code of 1986 or to a wholly-owned subsidiary corporation of such an organization provided one of the stated purposes of the transferee is:
>
> (A) to acquire property in order to preserve housing for low-income families or. . . .

32 V.S.A. § 9603(20). This exemption does not apply to your case, because the transferee [redacted] is not a 501(c)(3) and is not a wholly-owned subsidiary corporation of such an organization.

You have suggested that it is unclear that the transfer meets the specific legal requirements for exemption from the transfer tax and that it might meet the "spirit" of the exemption.

Unfortunately, the spirit of the language of Subsection (20) would not support a broadening of the exemption to the transfer you propose.[1]

We note first that tax exemption statutes are strictly construed against the taxpayer, and any doubts as to their application will be interpreted against the exemption. Hopkinton Scout Leaders Ass'n v. Town of Guilford, 2004 VT 2, 6, 176 Vt. 577, 578 (2004). The exemption must be strictly construed against the party claiming the exemption unless such a construction would produce irrational results or defeat the purposes of the statute. Tarrant v. Department of Taxes, 169 Vt. 189, 206 (1999). No claim of exemption can be sustained unless within the express letter or necessary scope of the exemption clause. Pizzagalli Construction Co. v. Department Taxes, 132 Vt. 496, 499 (1974).

As in all tax cases, however, the substance of the transaction may govern. Sherburne Corp. v. Town of Sherburne, 124 Vt. 481, 483 (1965). And the Supreme Court has, in a property transfer tax case, held that a statutory exemption should not be applied mechanically where a "transfer is, in substance, eligible for exemption." Wetherbee v. State, 132 Vt. 165, 168 (1974). The analysis of the Wetherbee case, however, is inapplicable to this case.

In Wetherbee, the Court considered the scope of a subsection which exempted generally "(3) Transfers to secure a debt or other obligation." Id. at 167. The taxpayers wished to obtain a bank loan for improvements to their incorporated catering business. Taxpayers owned the real property location of their business. To obtain the loan, the bank required the taxpayers to first transfer their real property to their corporation, followed by a mortgage deed from the corporation to the bank to secure the loan, followed by a deed from the corporation back to the taxpayers, subject to the new mortgage. All transfers were made at the same time. The Court viewed all three transfers as so closely related to the loan transaction that they were "in substance" three steps under the general heading of "to secure a debt," and therefore all exempt.[2]

The Wetherbee analysis does not apply to your case, however. In your case, the language of the statutory exemption (20) in question is not general, but is narrow and explicit, and applies to transfers "to organizations qualifying under Section 501(c)(3) of the Internal Revenue Code. . .or to a wholly-owned subsidiary corporation of such an organization. . . ."

The first clause of the exemption is explicit in requiring 501(c)(3) status of the transferee. [redacted] is not a 501(c)(3) organization, nor could it be said that [redacted] is "in substance" a 501(c)(3) organization.

Next, the second clause of the exemption requires that the transferee be a "wholly owned subsidiary corporation" of a 501(c)(3). [redacted] is not wholly-owned by a 501(c)(3), because it has two owners, and one [redacted] is not a 501(c)(3). Unlike the general wording of the exemption

[1] This analysis focuses on Subsection (20), which addresses transfers to a subsidiary entity. You have suggested that [redacted] own exemption as a transferee would derive from 24 V.S.A. § 4020 or 32 V.S.A. § 9603(2), but neither of these sections contemplate transfers to subsidiary corporations. Your letter concedes that Subsection (11), which exempts certain transfers at the time of a corporation's formation, is inapplicable.

[2] The Legislature later amended the language of the exemption from "transfers to secure a debt" to "transfers directly to the obligee to secure a debt." 32 V.S.A. § 9603(3); No. 225 of the Acts of 1974 (Adj.), §§ 3-9.

in Wetherbee for transfers "to secure a debt," the exemption in Subsection (20) is very specific in its reference to 501(c)(3) organizations, and does not refer generally to tax-exempt organizations. Because the language is specific, it cannot be read to include other types of exempt organizations. In addition, a reading of Subsection (20) in the context of the entire Section 9603 emphasizes that the Legislature intended Subsection (20) to be specific to 501(c)(3) organizations: The Legislature was clearly aware, when it enacted Subsection (20), that there were other types of exempt organizations, because it created a separate exemption in Subsection (22) for transferees who are exempt under 501(c)(2). In other words, when it specified 501(c)(3) in exemption (20), it expressly was excluding other types of exempt organizations. As noted, there is no general language in Subsection (20), as there was in the Wetherbee case, that would allow for exemption of a transfer to an LLC co-owned by a 501(c)(3) and a non-501(c)(3) entity. And there is no general language in Subsection (20) that would exempt a transfer to an LLC co-owned by two entities which are exempt under some other law. And finally, it cannot be said that [redacted] meets the requirements of exemption (20) as an "organization *qualifying* under Section 501(c)(3)" [but which hasn't applied yet for 501(c)(3) status], because a housing authority would not qualify for 501(c)(3) status.[3]

In short, the transfer to [redacted] does not fit within the language or the substance of exemption (20). Since there is no property transfer tax exemption which would apply to the proposed transfer to [redacted], the transfer would be subject to the property transfer tax.

GENERAL PROVISIONS

This ruling will be made public after deletion of the parties' names and any information which may identify the parties. A copy of this ruling showing the proposed deletions is attached, and you may request within 30 days that the Commissioner delete any further information that might identify the parties. The final discretion as to deletions rests with the Commissioner.

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[3] If [redacted] were an organization "qualifying under Section 501(c)(3)," then [redacted] would be wholly-owned by one 501(c)(3) and one organization qualifying under 501(c)(3). It is possible, but not clear, that transfer to a subsidiary with two such owners would meet the requirements for the Subsection (20) exemption. But that issue is moot, since it appears that [redacted] would not qualify under 501(c)(3). The Internal Revenue Service has recognized that in some cases a "state or municipal instrumentality" may qualify as an exempt organization under 501(c)(3). Rev.Rul. 60-384, 1960-2 C.B. 172 (1960). If, however, the entity has powers which exceed those prescribed for an exempt entity in Section 501(c)(3), the entity will not qualify under that section:

> If the organization . . . is clothed with powers other than those described in section 501(c)(3) it would not be a clear counterpart of a section 501(c)(3) organization. For example, where [it] exercises enforcement or regulatory powers in the public interest such as health, welfare, or safety, it would not be a clear counterpart of an organization describe in section 501(c)(3) . . . since it has purposes or powers which are beyond those described in section 501(c)(3).

Id; *See also* Rev.Rul. 74-14, 1974-1 C.B. 125 (1974). [redacted] has powers which exceed those prescribed for a 501(c)(3), because it has the power to exercise "public and essential governmental functions" and specifically, has authority for clearance of substandard and decadent areas for the public health and welfare, and to aid in this mission, it has the power of eminent domain. 24 V.S.A. §§ 4001(4), 4002(10), 4008(1), (2), (4); Davis v. Cain, 127 Vt. 296, 299 (1968). [redacted] is therefore not a "clear counterpart" of a 501(c)(3) organization and is "clothed with powers beyond those" of such an organization. Since [redacted] is not a qualifying organization under 501(c)(3), [redacted] is not wholly-owned by two qualifying 501(c)(3) organizations, and the transfer to it could not be exempt under Subsection 9603(20). This ruling does not address whether [redacted] qualifies as a state or municipal instrumentality.

This ruling is issued solely to the taxpayer and is limited to the facts presented, as affected by current statutes and regulations. Other taxpayers may refer to this ruling, when redacted to protect confidentiality, to determine the department's general approach, but the Department will not be bound by this ruling in the case of any other taxpayer or in the case of any change in the relevant statutes or regulations.

Emily Bergquist

Date

Approved:

Mary N. Peterson
Commissioner of Taxes

Date