

Ruling 97-10

Vermont Department of Taxes

Date: December 30, 1997

Written By: Mary L. Bachman, General Counsel

Approved By: Edward W. Haase, Commissioner of Taxes

You have requested a ruling that the transfer of real property by an existing partnership to a new limited partnership upon formation is exempt from Vermont property transfer tax. This ruling relies on the information conveyed in your letters of [dates].

Facts [Owners], both of [town], Vermont, have been in the business of developing real estate for [number] years under the name [Partnership] (the "Partnership"). The partners will transfer approximately sixty percent of the Partnership's real property to the [Limited Partnership] (the "Limited Partnership"). The properties to be transferred to the Limited Partnership are long-term rental properties and one parcel of undeveloped land, with a total approximate value of [dollar amount]. The assets remaining in the Partnership are primarily properties being developed or with the potential for development in the near future.

Initially the Partnership will be the general partner and a limited partner of the Limited Partnership. [Owners] will be limited partners of the Limited Partnership. Subsequently, the Partnership will distribute (transfer) its general partnership and limited partnership interests in the Limited Partnership to [Owners] so that they will be general and limited partners of the Limited Partnership and general partners of the Partnership.

The properties being transferred to the Limited Partnership are currently being refinanced on a long-term basis and the transfer to the Limited Partnership will permit the [owners] to shield the rental property from direct risks associated with the real property development business currently being conducted and planned by the Partnership. The Limited Partnership will also allow an opportunity to transfer interests in the long-term investment properties to family members both in order to shift income to the family members and to avoid the sale of the business properties to pay estate taxes on the deaths of [owners].

Ruling Vermont imposes a tax upon the transfer by deed of title to property located in the state. 32 V.S.A. § 9602. The law exempts certain transfers from the tax, including "[t]ransfers made to a partnership at the time of its formation, pursuant to which transfer no gain or loss is recognized under section 721 of the Internal Revenue Code, except where the commissioner of taxes finds that a major purpose of such transaction is to avoid the property transfer tax." 32 V.S.A. § 9603(15).

Section 721 of the Internal Revenue Code provides that no gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership.¹ That is the situation which has been described herein and thus it appears that there will be no recognition of gain at the federal level associated with this transfer.

The anti-abuse provision of the exemption allows the commissioner to treat a transfer to a new partnership as taxable if the transaction was structured as an initial partnership contribution only to accomplish an otherwise taxable transfer in an exempt manner. In this situation two non tax-avoidance reasons for the transfer exist: first, separation of the real estate ownership will serve to shield the long-term real estate investments to be held by the Limited Partnership from some risks associated with the development activities of the Partnership; second, the Limited Partnership will be a vehicle for shifting income to other family members (presumably through limited partnership interests). A third reason for the transaction is avoidance of probate and sale of the Limited Partnership assets upon the deaths of [owners]. Avoidance of estate tax as a motivation for the transfer does not disqualify it from the exemption. Since it appears that there are sufficient business and estate planning reasons for the transfer to the new Limited Partnership, the transfer is exempt from property transfer tax under the provisions of 32 V.S.A. § 9603(15).

This ruling is issued solely to your business and is limited to the facts presented as affected by current statutes and regulations. Other taxpayers may refer to this ruling 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 statute or regulations.

¹An exception from the nonrecognition rule concerning a partnership which would be treated as an investment company if incorporated does not apply to these facts.