REDACTED VERSION

[Date]

[Address]

Re: Formal Ruling 18-05

Dear [Deleted]:

This is a formal ruling for your client, [Taxpayer], regarding Taxpayer's request that the Commissioner of Taxes certify Taxpayer's subsidiary as eligible for various tax advantages which accrue to a 501(c)(3) organization. This ruling is based upon representations in your letter dated [date], and your enclosed materials.

RULING

The tax advantages you request under Vermont law for your subsidiary are available only to organizations which qualify for tax-exempt status under Section 501(c)(3) of Federal income tax law. The Commissioner of Taxes has no authority to qualify an entity as tax-exempt under Federal law. If your subsidiary obtains Federal qualification as a 501(c)(3), it may then be eligible for tax advantages available under Vermont law to 501(c)(3) organizations, assuming all other requirements of the Vermont laws are also met.

FACTS

The facts as you state them are as follows:

Taxpayer, [Taxpayer], is a Vermont nonprofit corporation recognized by the Internal Revenue Service ("IRS") as exempt from Federal income tax, under Section 501(c)(3) of the Internal Revenue Code ("IRC") ("501(c)(3)").

Taxpayer intends to create a subsidiary in the form of a Vermont limited liability company ("LLC"). Taxpayer will be the sole member of the LLC. Both the parent corporation and its subsidiary LLC will be operated on a nonprofit basis, even though an LLC cannot not be an express nonprofit entity under Vermont law.

You state,

> The IRS will recognize LLCs as tax exempt under Section 501(c)(3) so long as the LLC is . . . a "disregarded entity" . . . OR . . . a qualified tax exempt organization that meets 12 conditions designed by the IRS to ensure the LLC is organized and operated exclusively for tax exempt purposes and precludes private inurement of net earnings.

Taxpayer's Request Letter, p. 3. Taxpayer intends that its LLC will meet the twelve IRS conditions for exempt status.

Taxpayer will transfer to its subsidiary LLC fee interests in some or all of its real property. The interests to be transferred will include [parcel types]. Some of the parcels may be [deleted]. Holding the properties in the LLC will protect the parent Taxpayer's assets from liability for lawsuits related to the properties owned by the subsidiary LLC.

Taxpayer requests that the Commissioner of Taxes "recognize the status" of the proposed LLC as qualified for favorable property tax treatment under Chapter 155 of Title 10, and also as qualified for favorable property transfer- and land gains-tax treatment under Title 32.

DISCUSSION

Qualification for Title 10 property tax advantages

Chapter 155 of Title 10 provides property tax reduction or exemption for conservation land held by a "qualified organization" if the Commissioner of Taxes certifies the land as "being held and maintained for the purposes" stated in Chapter 155:

> (b)(1) The Commissioner of Taxes may certify that real property acquired **by a qualified organization** under this chapter is being held and maintained for the purposes expressed in section 6301 of this title. As a condition of that certification, the Commissioner may require that the qualified organization provide adequate assurances that the property is being so held and maintained, including written agreements with the Department of Taxes, deeds, covenants or other conveyances. Property which is so certified:
>
> (A) if in the nature of an interest in fee simple, shall be assessed on the basis of its actual use, or may be enrolled by the qualifying organization in a current use program under 32 V.S.A. chapter 124; or
>
> (B) shall be exempt from assessment and taxation, if in the nature of an interest other than fee simple.

10 V.S.A. § 6306(b) (bold typeface added). As this section shows, the Commissioner may only certify land held by a "qualified organization."

A "qualified organization" is defined as one which qualifies under 501(c)(3) of Federal law, is not a "private foundation" under Federal law, and is certified by the Commissioner of Taxes as "principally engaged in the preservation of undeveloped land":

> (2) "Qualified organization" means:
>
> (A) an organization qualifying under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended, which is not a private foundation as defined in Section 509(a) of the Internal Revenue Code, and which has been certified by the Commissioner of Taxes as being principally engaged in the preservation of undeveloped land for the purposes expressed in section 6301 of this title.

10 V.S.A. § 6301a(2)(A). That is, the Vermont statutes require that, before the Commissioner may certify an entity as principally engaged in land preservation, the entity must qualify under

501(c)(3) of the Federal tax law.[1] The Commissioner has no authority to determine whether an entity meets the requirements of Federal tax law. Therefore, before your LLC can be a "qualified organization" under Title 10, the LLC must first obtain IRS recognition that it qualifies under Federal 501(c)(3).

Once your LLC is recognized by the IRS as a 501(c)(3) and is certified by the Commissioner of Taxes as "principally engaged in the preservation of undeveloped land," it will be a "qualified organization." At that point, it may seek certification by the Commissioner that its land is "being held and maintained for the purposes" specified in Chapter 155 of Title 10. 10 V.S.A. § 6306(b)(1). After that certification, the land may be treated favorably for property tax purposes. If owned in fee simple, it will be exempt from property tax; if other than a fee simple interest, the property will be assessed at its "actual use" value or may be enrolled in the current use (UVA) program in Title 32, assuming it meets the requirements of the UVA program. 10 V.S.A. § 6306(b)(1)(A), (B).

Additional requirements for enrollment in current use

Note that the UVA statutes contain additional eligibility requirements for enrollment of land certified under Title 10. For managed forestland, one of these requirements is that at the time of enrollment the LLC will have been a 501(c)(3) for at least five years:

> (9) "Managed forestland" means:

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[1] A "qualified organization" may also be a 501(c)(2) under Federal law:

> (2) "Qualified organization" means:
>
> * * *
>
> (B) an organization qualifying under Section 501(c)(2) of the Internal Revenue Code of 1986, as amended, provided such organization is controlled exclusively by an organization or organizations described in subdivision (2)(A) of this section.

10 V.S.A. § 6301a(2)(B). It is not known whether your proposed LLC might qualify under 501(c)(2) of Federal law:

> (2) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt under this section . . . .

26 U.S.C. § 501(c)(2).

(A) any land, exclusive of any house site, which is at least 25 acres in size and which is under active long-term forest management for the purpose of growing and harvesting repeated forest crops in accordance with minimum acceptable standards for forest management. Such land may include eligible ecologically significant treatment areas in accordance with minimum acceptable standards for forest management and as approved by the Commissioner; or

(B) any land, exclusive of any house site, which is:

(i) **certified under 10 V.S.A. § 6306(b)**;

(ii) is owned by an organization that was **certified by the Commissioner of Taxes as a qualified organization as defined in 10 V.S.A. § 6301a** and **for at least five years preceding its certification was determined by the internal revenue service to qualify as a Section 501(c)(3) organization** which is not a private foundation as defined in 26 U.S.C. § 509(a); and

(iii) is under active conservation management in accord with standards established by the Commissioner of Forests, Parks and Recreation.

32 V.S.A. § 3752(9).

Other Vermont tax advantages for a 501(c)(3)

Vermont law provides additional favorable tax treatment for 501(c)(3) organizations: Certain transfers of property to or from a 501(c)(3) are exempt from property transfer tax, or in some cases, the tax is deferred; and are exempt from land gains tax. 32 V.S.A. §§ 9603(14)(A)(B), 10002 (e), (i), (j), (l) (o). But for these tax advantages, too, your LLC would first have to obtain IRS recognition as a 501(c)(3).

"Disregarded entity" status and Federal recognition of an LLC as a 501(c)(3)

You mention that Taxpayer's LLC will be a "disregarded entity." Federal income tax law allows the owners of a limited liability company to choose whether to treat it for Federal income tax purposes as a corporation or a partnership. Since an entity owned by only one person cannot be a "partnership," a single-member LLC must choose whether to be taxed as a corporation or as a "disregarded entity." Federal income tax regulations provide that disregarded entity status is the

default; the choice to be treated as a corporation must be affirmatively elected. U.S. Treas. Reg. §§ 301.7701-3.

You suggest that Taxpayer's disregarded-entity LLC will qualify for 501(c)(3) status, based on the IRS guidance materials you submitted with your ruling request (IRS "LLC guide sheet" and "2001 EO CPE Text, Section B. *Limited Liability Companies as Exempt Organizations - Update*"). Whether the LLC will qualify in future is insufficient. The LLC must already qualify as a 501(c)(3) entity in order to obtain the Vermont tax benefits you seek.

The Department of Taxes is not authorized to provide Federal tax advice, and the IRS guidance materials are not binding tax advice from the IRS. The guidance materials, however, suggest that your LLC likely will not qualify as a 501(c)(3). They state that if a qualified 501(c)(3) organization is the sole owner of a disregarded-entity LLC, the disregarded LLC is not eligible for its own 501(c)(3) designation. Instead, the disregarded LLC is treated as having no separate existence from its owner, and the LLC's activities are treated simply as activities of its owner. 2001 EO CPE Text, Section 2. In your case, Taxpayer's disregarded LLC would be ignored as a separate entity for income tax purposes, and all of its activities would be viewed as activities of Taxpayer.

The IRS guidance materials do state that an LLC may qualify on its own as a 501(c)(3) entity if it meets twelve listed conditions. But this option is apparently allowed only for an LLC "*other than* . . . a disregarded entity with a sole exempt organization owner." 2001 EO CPE Text, Section 3.B (emphasis added). This means that Taxpayer's solely-owned disregarded LLC would not have the option of qualifying under the twelve-conditions test.

Disregarded entity status under income tax law has no bearing on an LLC's status as a separate entity under other laws. Londen Land Co., LLC v. Title Res. Guar. Co., WL 3034871 at *3 (D. Ariz. Aug. 3, 2010); *aff'd* 467 F. App'x 708, 709 (9th Cir. 2012) ("[D]isregarded entity

. . . election has nothing to do with other legal matters - such as member liability or property ownership."). Under Vermont LLC law, "A limited liability company is a legal entity distinct from its members." 11 V.S.A. § 4021. This rule applies to all LLCs, including single-member LLCs. Under *Londen*, this "distinct entity" Vermont status is unaffected by the LLC's income tax status. This means that once Taxpayer transfers real property to its LLC, the LLC - as a distinct Vermont entity - would require its own 501(c)(3) designation in order to qualify for the Vermont tax advantages sought; and this is the result whether or not the LLC is disregarded for income tax purposes.

GENERAL PROVISIONS

Issuance of this ruling is conditioned upon the understanding that neither the taxpayer nor a related taxpayer is currently under audit or involved in an administrative appeal or litigation concerning the subject matters of the ruling. 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 see 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.

This ruling will be made public after deletion of the taxpayer's name and any information which may identify the taxpayer. 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 taxpayer. The final discretion as to deletions rests with the Commissioner.

You have the right to appeal this ruling within 30 days. 3 V.S.A. §§ 808, 815.

_____ _____

Emily Bergquist Date

Approved:

Commissioner signed the original ruling on July 31, 2018.

_____ _____

Kaj Samsom Date

Commissioner of Taxes