VERMONT DEPARTMENT OF TAXES
TECHNICAL BULLETIN

TAX: LAND GAINS TB-34

SUBJECT: LAND GAINS TAX ALLOCATIONS ISSUED: January 16, 2007
(Supercedes Guidelines dated July 2001)

REFERENCE: 32 V.S.A. § 10005

A. Introduction

The land gains tax is imposed on the gains from the sale or exchange of land in Vermont. 32 V.S.A. § 10001. "Land" does not include buildings or other structures. 32 V.S.A. § 10002(a). This Technical Bulletin provides guidance for taxpayers in determining the amount of gains subject to land gains tax where there is a sale or exchange of land which includes buildings, structures or other improvements.

B. Relevant Statute

32 V.S.A. § 10005 provides in pertinent part as follows:

(a) The provisions of the Federal Internal Revenue Code shall determine the basis of land sold or exchanged except basis for land transferred by a mortgagee who acquired the land by foreclosure or transfer in lieu of foreclosure shall be the amount of debt due the mortgagee, increased by the costs of acquisition, and decreased by the amount of any tax benefit due to bad debt loss on the mortgage debt.
(b) The amount realized from the sale or exchange shall be the full actual consideration therefor, paid or to be paid, including the amount of any liens or encumbrances on the land existing before the sale or exchange and not removed thereby. The amount realized from the sale or exchange shall be the gross amount thereof, reduced by any reasonable expenses of sale and commissions. However, if the seller has owned the land for less than one year, the amount realized from the sale or exchange shall be the gross amount thereof, reduced by no more than a total of 12 percent by any expenses of sale and commissions. In the event that a sale includes land and buildings or other structures, the amount realized shall be allocated between the land and the buildings or other structures on the basis of fair market value.
(c) The taxable gain from the sale or exchange is the amount realized minus the basis of the land as determined under subsection (a) of this section. No gain shall be recognized in cases where gain is not recognized under the Federal Internal Revenue Code, as amended, in relation to the sale or exchange of capital assets.

C. Allocation Between Land and Buildings

For both the convenience of taxpayers and ease of administration, Vermont Tax Form LG-2 and instructions are designed to allow taxpayers to use a simplified method for determining the allocation of the *amount realized* to land on which a building is situated. Instead, the total *gain* (as defined in 32 V.S.A. § 10005(c)) may be allocated based on relative fair market value of the land and buildings. The reason for allowing this simplified method is because allocation of *amount realized* cannot be accurately determined without a qualified appraisal of both the land and buildings at the time of sale. Allocation of *gain* is usually more easily determined based upon information already available to the seller at the time of closing, and is consistent with the statutes since in most cases the relative fair market value of land to building does not change between the acquisition of the property and its subsequent sale.

It is not mandatory that taxpayers use the Form LG-2 and instructions for allocation based on *gain.* However, their use will usually expedite the processing of returns and result in less audit follow-up by the Department.

(1) Allocation based upon the *amount realized*

If taxpayers elect to allocate the *amount realized*, the allocation must be based upon a complete appraisal(s) which fully complies with USPAP (Uniform Standards of Professional Appraisal Practice) showing value both at the time of acquisition and upon subsequent sale. The appraisal(s) must be conducted prior to the sale, and separately state the values of the land and the buildings. A summary of appraisal (i.e., a cover letter from the appraiser merely stating value) will not be accepted. The complete appraisal(s) must be attached to the LG-2 return. The allocation must be calculated based on the following substitute Schedule A (instead of the regular Schedule A lines 24 through 28) and this substitute schedule also must be attached to the LG-2.

SUBSTITUTE SCHEDULE A -- FOR USE WHEN ALLOCATION IS BASED ON AMOUNT REALIZED:

A. Total amount realized (adjusted selling price from line 11)	$______
B. Fair market value of land (per attached appraisal)	$______
C. Fair market value of total property (per attached appraisal)	$______
D. Percentage of value realized on land (divide line B by line C)	______
E. Equals amount realized on land (multiply line A by line D)	$______
F. Basis of land (from line 12)	$______
G. Gain on sale of land (subtract line F from line E)(if less than 0 enter 0) (enter on line 28)	$______

(2) Allocation based upon *gain*

For allocation between land and buildings based on *gain* instead of *amount realized*, taxpayers may continue to use the current form LG-2 Schedule A and either of the following methods to arrive at the fair market value of land:

(a) Taxpayers may use the town listed value of land and land improvements (water, sewer, etc.) divided by the town listed value of land, land improvements and buildings. These values are usually available on the lister cost sheet (also known as the property value card) of the municipality in which the property is located. Multiply the result by the total sales price and enter on line 24.

(b) In most cases, taxpayers may use the following percentages to complete Schedule A. If used, skip lines 24 and 25 on Schedule A and use the percentages on line 26.

1. City of Burlington & South Burlington……………………35%
2. Condominiums & timesharing intervals (statewide) ………10%
3. Lakeshore lot with average camp…………………………..45%
4. Other (Statewide except Burlington & South Burlington)
    A. up to 1.9 acres……………………….………………. 25%
    B. 2 acres to 10.9 acres…………………..………... 30%
    C. 11 acres to 25 acres……………………….…… 35%

NOTE: Any of the above methods chosen by taxpayers are subject to review and audit by the Department. If a Taxpayer elects to calculate the allocation percentage based on either of the above two methods based on *gain,* the percentages must be generally consistent with ratios derived for similar properties in the area based on the lister cost sheets.

The Department will normally not accept a claimed loss on the sale of land (zero dollars on line 15 and Schedule A line 27 or Substitute Schedule A line G) absent special circumstances which convincingly demonstrate a decrease in land value upon sale (for example, extraordinary acquisition costs, distress sale, sale of polluted land, etc.). If such special circumstances exist, they should be explained on an attachment to Form LG-2.

D. Allocation of Cost

When the property being sold is a portion of a larger property, the manner of allocating cost may vary depending upon the type of property being sold. The following methods will be accepted by the Department.

(1) Mandatory cost allocation (for estate property and other situations where I.R.S. mandates allocations)

Where the Internal Revenue Code mandates the use of an allocation derived from actual past events, that allocation must be used for the Land Gains Tax allocations.

For example, a sale of property acquired from a decedent may be separately valued on the Federal Estate Tax Return (706). If this is the case, the allocated basis must be that value. Thus, Federal Estate Tax Return 706 (Schedule A) shows as follows:

Lot 1 (20 acres) ....$ 6,000
Lot 2 (100 acres).. 20,000
Lot 3 (house, barn & 40 acres) 100,000

And if Lot 1 is sold, cost basis is $6,000.

NOTE: If the lot is not separately valued on the Federal Estate Tax Return, the appraisal for the estate may contain a breakdown of the total used to prepare the return.

(2) Average cost allocation

The Department will accept an average per acre cost allocation.

Example:

100 acres purchased for $30,000
Acquisition legal fees 275
Property transfer tax 150
Total cost $30,425
10 acres sold

$$\text{Total cost} \ldots \left(\frac{\$30{,}425}{100}\right) = \$304.25 \text{ average cost per acre}$$
$$\text{Total acres} \ldots \quad \times 10 \text{ acres sold}$$
$$\$\,3{,}042.50 \text{ Cost allocated to sale}$$

If structures were purchased along with the 100 acres for a total of $100,000, the allocated cost of the buildings is first subtracted from the $100,000, and then the average cost per acre is calculated in the following manner:

$$\left(\frac{\text{listed value of structures per town Listers}}{\text{listed value of total property}^{1}}\right) \times \text{total cost} = \text{allocated cost of structures}$$

Example:

Total cost $100,000
Less allocated cost of structures .... - 70,588 *
Allocated cost of land .... $\left(\frac{29{,}412}{100}\right)$ = $294.12 average cost per acre
Number of acres ....

* $\left(\frac{\text{Listed value of structures} \ldots\ \$60{,}000}{\text{Listed value of total property} \ldots\ \$85{,}000}\right)$ x $100,000 = $\underline{\$\,70{,}588}$ allocated cost of structures

(3) Graded cost allocation

If the parcel being sold is of a substantially better quality than the balance of the land, the average cost may be adjusted by a grade factor not to exceed 2.

Example:

100 acres purchased for $30,000 (no buildings)
20 acres prime house sites
80 acres swampy unusable land
10 acres of prime land sold

$$\text{Total cost} \ldots \left(\frac{\$30{,}000}{100}\right) = \$\,300 \text{ per acre (average cost)}$$
$$\text{Total acres} \ldots \quad \times\ 2 \text{ grade}$$
$$\$\,600 \text{ per acre – graded cost per acre}$$
$$\times\ 10 \text{ acres sold}$$
$$\$6{,}000 \text{ cost allocated to sale.}$$

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[1] Listed value of total property is the listed value of land, land improvements and structures.

(4) Fair market value cost allocation to portion of a larger property

The most commonly used method of allocating cost to a portion of a larger property being sold is as follows:

$$\left(\frac{\text{sales price of property sold}}{\text{fair market value entire property}}\right) \text{ x original cost basis} = \text{cost allocated to property sold}$$

Example:

100 acres purchased (no buildings) for	$30,000
Acquisition legal fees	275
Property transfer tax	+ 150
Original cost basis	$30,425

The property is subdivided into 10 lots with varying sales prices. The projected total combined sales price for all lots is $130,000. Lot 1 is being sold for $18,000.

$$\begin{array}{l} \text{Sales price of Lot 1} \\ \text{Total projected sales price} \end{array} \left(\frac{\$18{,}000}{\$130{,}000}\right) \text{ x \$30,425 original cost} = \underline{\$4{,}212.70} \text{ Allocated cost of Lot 1}$$

NOTE: Improvement costs since acquisition are separately allocated to the lots to which they apply. For example, new road costs are allocated to the lots served by the new road.

(5) Use of specified percentages from paragraph C(2)(b) for allocation of cost.

Assuming the buildings are useable and in good condition cost may be allocated as follows:

Example:

A house & 3 acres were purchased for $45,000;
1 acre is being sold

Cost of house and 3 acres	$ 45,000
Acquisition legal fees	250
Property transfer tax	+ 225
Total cost	$ 45,475
Percentage for 3 acres *	x 30%

$$\begin{array}{l} \text{Allocated cost all land} \\ \text{Number of acres} \end{array} \left(\frac{\$13{,}643.00}{3}\right) = \text{\$4,548 allocated of 1 acre}$$

* percentage in Paragraph C(2)(b) for 2 to 10.9 acres.

(6) Farms

Where part of an operating farm is sold, cost may need to be allocated. In most cases, there is a breakdown of cost between the realty, livestock and equipment.

Example:

Buildings & 400 acres purchased for $400,000
Acquisition legal fees 500
Property transfer tax .... + 2,000
Total cost of realty $402,500

25 acres of field land being sold

Step 1. First allocate out cost of buildings
Original total cost of realty $402,500
Less allocated cost of buildings...................- 233,329 *
Cost allocated to land...................................$ 169,171

$$* \quad \frac{\text{Listed value of structures}}{\text{Listed value of total property}} \ldots\ldots \left(\frac{\$173{,}910}{\$300{,}000}\right) \times \$402{,}500 = \$233{,}329 \text{ allocated cost of structures}$$

Step 2. Determine cost allocated to type of land being sold.
Per Town Lister:
100 acres fields @$400 per acre ....$ 40,000
100 acres crop land @$380 per acre..........................38,000
75 acres pasture @$250 per acre 18,750
125 acres woodland @$235 per acre................... + 29,340
Land valuation total $126,090

$$\left(\frac{40{,}000}{126{,}090}\right) \times \$169{,}171 \text{ (cost)} = \$53{,}667 \text{ cost allocated to 100 acre fields}$$

Step 3. Determine cost allocated to sale.

$$\left(\frac{53{,}667}{100}\right) = \$536.67 \text{ average cost allocated to field}$$

$536.67 x 25 A = $13,416.75 cost allocated to sale

(7) Treatment of personal property

Taxpayers may not take a "double deduction" for personal property. If Taxpayers deduct the consideration received for the personal property from the selling price, Taxpayers must then deduct the cost of the personal property from the cost of the property sold.

Signed: ______________________________
Danforth Cardozo, III

Approved: ___________________________
Commissioner of Taxes