STATE OF VERMONT

SUPERIOR COURT
Chittenden Unit

CIVIL DIVISION
Docket No. S1297-11 CnC

In re: Colchester Leased Land Appeals

DECISION ON CROSS-MOTIONS FOR PARTIAL SUMMARY JUDGMENT

In these consolidated cases, the owners of buildings (mainly cottages and camps) located on lakeshore lands they lease from third parties have appealed, pursuant to 32 V.S.A. § 4461(a), the Town of Colchester Board of Civil Authority's (BCA) decisions with respect to 2011 assessed value of the buildings. The owners of the buildings (Appellants) contend that the Town of Colchester (the Town) has impermissibly assessed the buildings they own by including with those assessments a sum described as the "land/amenity" value.[1] The Town maintains that the "land/amenity" values incorporate into the value of the buildings the attributes of the buildings' respective locations (such as views or lake proximity or access), and that doing so is necessary to arrive at the fair market value for those buildings. Appellants contend that the Town has no statutory basis upon which to tax them for the "land/amenity" value. Appellants and the Town have each filed motions for partial summary judgment on the issue of whether the Town's inclusion of the "land/amenity" values is proper.

BACKGROUND

The facts material to the issues presented are undisputed and relatively straightforward. The Appellants own camps or cottages near Lake Champlain within the Town of Colchester. The camps or cottages are located on land leased from third parties. In 2011, Colchester completed a town-wide reappraisal of real estate in the Town for the 2011–2012 tax year.

The re-appraised values for the *buildings* on the leased lands at issue in these cases are the sum of two values: (1) what the Town calls the "building" value and (2) what the Town calls the "land" or "land/amenity" value.[2] The "building" value is derived by calculating the building's replacement cost new, but less depreciation. The "land/amenity" value is supposed to be the "intangible locational value" or "intangible amenity value" associated with the building's location. The Town calculates the "land/amenity" value by applying a variety of factors to a "unit price" of $100,000. For example, a building located on a parcel that has superior views and lake access might be

[1] Several Appellants are also appealing the Town's assessment of the fair market value of their buildings, apparently arguing that even if the "land/amenity" value is not included, the value for the building itself is still too high.

[2] The latter value has been described using a variety of terms. For simplicity the court will simply refer to it as the "land/amenity" value.

assigned factors that magnify the $100,000 resulting in a "land/amenity" value of $220,000. A building located on a parcel with no views and less-than-excellent lake access might be assigned factors that bring the "land/amenity" value down to less than $100,000.

The re-appraised values for the *lands* underlying the buildings are calculated based on the land's income value to the owners of the land (i.e., the average annual rent the owners receive from the lessees).

ANALYSIS

There are five basic questions that could be asked with respect to property taxes: who, what, when, why, and how much? The answer to the "why" question is a philosophical and policy question not at issue here, although the basic idea, of course, is that the property taxes supply funding for bodies of government to carry out various functions. The answers to "who" and "when" are relatively straightforward in these cases.[3] The more difficult questions in these cases are "what" and "how much?"[4]

The court begins with the relevant statutory provisions. The court's goal is to "discern and implement legislative intent." *Garbitelli v. Town of Brookfield*, 2011 VT 122, ¶ 12, available at http://info.libraries.vermont.gov/supct/current/op2011-020.html. In doing so, the court may look to "the words of the statute itself, the legislative history and circumstances surrounding its enactment, and the legislative policy it was designed to implement." *Id.* (quoting *Perry v. Med. Practice Bd.*, 169 Vt. 399, 406 (1999)).

As mentioned above, the owner or possessor of "taxable real estate" is responsible for the real estate taxes on such real estate. See 32 V.S.A. § 3651 ("Taxable real estate shall be set in the list to the last owner or possessor thereof on April 1 in each year in the town, village, school and fire district where it is situated."). "Real estate" includes land. 1 V.S.A. § 132. In addition, pursuant to 32 V.S.A. § 3608, "[b]uildings on leased land or on land not owned by the owner of the buildings shall be set in the list as real estate." As the Supreme Court has explained, "[b]y enacting § 3608, the Legislature specifically included buildings on leased land in the definition of taxable real estate, and recognized that a building can be taxed separately from the land upon which it sits." *Gordon v. Bd. of Civil Auth. for Town of Morristown*, 2006 VT 94, ¶ 8, 180 Vt. 299. "Section 3608

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[3] The owner or possessor of "[t]axable real estate" is responsible for the real estate taxes on such real estate. See 32 V.S.A. § 3651 (general rule); *Gordon v. Bd. of Civil Auth. for Town of Morristown*, 2006 VT 94, ¶ 11, 180 Vt. 299. Not all real estate is *taxable* real estate. For example, some real estate is not taxable by operation of an exemption under chapter 125 of Title 32. At least for present purposes, these cases do not present any question of exemption. Sections 3482 and 3651 also answer the "when" question, indicating that the "record date," in a sense, for property taxation is April 1 of each year.

[4] The Town maintains that these cases present a question of valuation. Appellants say that the questions raised in these cases are questions of statutory construction and authority to tax, rather than valuation. The court concludes that, in this case, "valuation" and "taxability" are two sides of the same coin. Defining precisely *what* is being taxed in these cases will bring the "how much" question into focus.

contemplates two separate listings when a building is located on land not owned by the owner of the building: one for the building, and one for the land." *Id.* ¶ 10.

The owner or possessor of "taxable real estate" pays real estate taxes based on the real estate's value. A tax rate determined by a municipality (in the case of the municipal property tax) or the State (in the case of the education property tax) is applied to the listed value on the grand list. See 17 V.S.A. § 2664 (authorizing towns to tax real estate within their boundaries based on their grand lists); 32 V.S.A. § 5402(a) (setting rates for the statewide education property tax).[5] Section 3481 states that the "listed value" is 100% of the "appraisal value," and the "appraisal value" is, in most cases, "the estimated fair market value." 32 V.S.A. § 3481(1), (2). The "estimated fair market value," in turn, is:

> the price which the property will bring in the market when offered for sale and purchased by another, taking into consideration all the elements of the availability of the property, its use both potential and prospective, any functional deficiencies, and all other elements such as age and condition which combine to give property a market value.

Id. § 3481(1). In short, property tax in Vermont is, as in most states, an *ad valorem* levy.

The parties have diametrically opposed views as to how to assign values to the improvements on the land and to the land itself. Appellants maintain that, by the plain terms of 32 V.S.A. § 3608, they are only liable to pay taxes on the value of their "buildings," and that the Town may not tax them for the "land/amenity" value or any other value related to their leasehold interest. The Town agrees with Appellants that it may only assess buildings on leased land against the building's owner, but asserts that in order to do that, it must include the significance of each building's location in the fair market value of the building itself. Appellants contend that the value of a particular location inheres in the real property itself and not in the structures added to that property.

Listing the building on leased land as its own unit of "real estate" separate from the land itself requires the Town to assign independent values to integral components of a larger unit. Joan M. Youngman, *Defining and Valuing the Base of the Property Tax*, 58 Wash. L. Rev. 713, 803 (1983). This is no easy task. See *id.* at 805 ("What is the value of the left-hand member of a pair of $4 gloves?" (quoting 1 J. Bonbright, *The Valuation of Property* 76 (1937)); *City and Cnty. of Denver v. Bd. of Assessment Appeals of the State of Colorado*, 848 P.2d 355, 359 (Colo. 1993) (noting the difficulty of ascertaining the individual value of separate interests). Vermont's statutory scheme, however, requires it. To do that, it becomes necessary to define very precisely what the subjects of taxation are in these cases.

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[5] There are two types of property tax in Vermont: municipal property taxes and a statewide education property tax. *In re HS-122*, 2011 VT 138, ¶ 1 (mem.), available at http://info.libraries.vermont.gov/supct/current/eo2011-128.html.

Section 3608 explicitly states that "buildings" on leased land are "taxable real estate." "The term 'building' is often used in a broad sense, referring to any structure enclosing a space or sheltering contents." *Gordon*, 2006 VT 94, ¶ 9. The statute does not say that anything besides "buildings" on leased land is taxable to the building's owner. Most importantly, it does not say that the building owner's *leasehold interest* in the underlying land is a subject of taxation. See *Sherburne Corp. v. Town of Sherburne*, 145 Vt. 581, 586 (1985) ("The Town cites no statutory authority for a system of taxation in which each person with an interest in real property is taxed on the value of that interest."). Where the Legislature has intended to tax a leasehold interest, it has done so explicitly. See 32 V.S.A. § 3610 (perpetual leases). Here, however, the only "real estate" taxable to Appellants are the "buildings" they own.

This result is consistent with the court's conclusion in *Lesage v. Town of Colchester*, No. S1417-03 CnC, http://www.vermontjudiciary.org/TCDecisionCvl/2005-8-17-3.pdf. In that case, as here, the appellants owned a lakeshore cottage but not the land on which it was located. The Town initially listed the value of the cottage as of April 1, 2003 at $80,200. Of that sum, $60,200 was attributable to the cottage itself and $20,000 was a value assigned to the appellants' leasehold interest. The Colchester Board of Civil Authority reduced the value by $20,000 (the leasehold value). The appellants challenged the resulting $60,200 value of the cottage, and the court held a de novo trial. At trial, the Town did not attempt to include the leasehold interest with the value of the building. In fact, the Town calculated the value of the cottage by subtracting the value of the average leasehold interest in comparable cottages ($46,000) from the average time-adjusted selling price of comparable cottages on leased land ($121,100). The result was approximately $75,000, which this court found to be the fair market value of the cottage.[6]

In short, § 3608 does not provide authority to tax Appellants' leasehold interests, and the practice, as demonstrated by *Lesage*, has been not to do so. The intangible "amenity" values in these cases must be assigned to the land itself, not to the buildings. See *In re Wine*, 260 P.3d 1234, 1239 (Kan. Ct. App. 2011) (finding no error in Court of Tax Appeals' conclusion that location "must be considered an attribute of the land, not the improvements"). Appellants' leasehold interest in the land has no effect on the value assigned to the buildings Appellants own. See *Cove Sportsmans Club v. Dep't of Revenue*, 11 Or. Tax. 40, 41 (Or. T.C. 1988) ("The question, then, is: What effect does the short-term interest in the land have on the assessed value to be put on the buildings? For purposes of ad valorem taxation the court finds none.").

Consistent with *Cove Sportsmans Club*, all of the *building* value is indeed assessable to the building owners. Understanding that the "land/amenity" values are assigned to the land itself, it becomes clear that the Town must not consider those intangible values when assessing the fair market value of the buildings in these cases.

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[6] The civil suit apparently caused the Town to employ what it called a more "precise" approach to valuation, apparently involving comparables different than those (if any) that were used to arrive at the $60,200 figure. The Town's $75,000 figure still did not include the appellants' leasehold interest.

Here, as in *Wine*, the tenants' interests have been overvalued because they include the value of the tenants' leasehold interests. 260 P.2d at 1237.

The court's conclusion does not mean that the Town is unable to capture the intangible value of lakefront properties in its tax base. Here again, as in *Wine*, the landowners' interests have been undervalued by attributing the value of the leased interest to the lessees rather than assessing the value of the land's undivided fee simple estate and using that single figure to determine the landowners' tax bases. See *id.* That imbalance is corrected when the value of the intangibles is assessed to the owner of the underlying land. The landowners and the building-owners will apportion between themselves—by way of the leases into which they enter—who is to pay how much for the intangibles. It is possible that both types of owners will bear some of the tax burden for the "land/amenity" values. The market will ultimately sort out what proportion each must bear.

The Town asserts that market data supports its appraisal methodology, noting that buyers are motivated to pay more for a camp in a prime location than for a camp set farther from the lake. The Town compares two buyers of similar camps but for quite different prices.[7] One camp had lake access and fetched $270,000 in 2010, whereas another camp located away from the lake in a wooded setting sold for only $125,000 in 2010. The Town maintains that the only conclusion possible is that the location of the building, and its fair market value, is inextricably intertwined with the building itself. The court disagrees. The difference is not in the value of the *building* but in the value of the *leasehold interest* that is likely to come with it. And leaseholds are not subject to the property tax except when they are perpetual.

Neither does assessing the landowner for the intangibles violate 32 V.S.A. § 3608. The Town contends that it would because § 3608 "does not require that a building's intangible location value . . . be set in the list to the owner of the underlying land." Town's Mot. for Partial Summ. J. at 12 n.3 (filed Feb. 1, 2012). In fact, § 3608, as discussed above, only authorizes taxing "buildings." The "land/amenity" values are taxable to the owners of the underlying land.

ORDER

The Appellants' Motion for Partial Summary Judgment (filed Dec. 21, 2011) is granted. The Town's Cross-Motion for Partial Summary Judgment (filed Feb. 1, 2012) is denied. This ruling does not dispose of all of the appeals, since some of the Appellants also seek review of the Town's assessment of the fair market value of the buildings themselves. The court will set a hearing to discuss whether final judgment can be entered

[7] The properties in the Town's example are not under appeal, but are in the same general area as Appellants' properties.

as to some of the appeals, the form of any such judgment, and the way forward with respect to the portions of those appeals that are not resolved by this ruling.

Dated at Burlington this 3 day of April 2012.

Geoffrey W. Crawford
Superior Court Judge