Morash v. Department of Taxes, No. 715-10-07 Rdcv (Teachout, J., Sept. 5, 2008)

STATE OF VERMONT
RUTLAND COUNTY

CARYL MORASH,	)	
Taxpayer-Appellant,	)	**Rutland Superior Court**
	)	**Docket No. 715-10-07 Rdcv**
v.	)	
	)	
DEPARTMENT OF TAXES,	)	
Appellee.	)	

DECISION
Appeal of Tax Commissioner's Denial of Renter Rebate Claim

Appellant Caryl Morash is a 76-year-old taxpayer who resides in a dwelling located on the green in East Poultney, Vermont. Her home is owned by the Morash Family Irrevocable Living Trust, and Ms. Morash is the sole beneficiary of the trust during her lifetime. In 2000, Ms. Morash applied for a property tax rebate, which was denied because she is not the owner of the dwelling. In 2002, 2003, and 2004, Ms. Morash applied for—and received—a renter rebate after indicating that she had entered into a rental transaction with the Trust, and paid rent in the form of property taxes.

In June 2005, the Department of Taxes notified Ms. Morash that it had adjusted her renter rebate downward for the years 2002, 2003 and 2004 based on a new determination that her rental transaction was not arms length. After Ms. Morash appealed that adjustment to the Tax Commissioner, the Department requested a copy of her trust, and subsequently notified her that it was further adjusting her renter rebate to $0.00 for the years 2002, 2003 and 2004 because her dwelling was owned by an irrevocable living trust for which she was the sole beneficiary. Based on this information, the Department concluded that Ms. Morash was ineligible to claim the renter rebate under 32 V.S.A. § 6062(e), which defines when dwellings owned by a trust constitute "homesteads" for purposes of the renter rebate. Ms. Morash appealed this adjustment to the Tax Commissioner as well.

The Tax Commissioner determined that Ms. Morash was not entitled to claim the renter rebate. The Commissioner reasoned that (1) to claim the renter rebate, the renter must rent a "homestead" on the last day of the taxable year under 32 V.S.A. § 6066(b); (2) when the renter is the sole beneficiary of the trust that owns the dwelling, the

dwelling is not the "homestead" of the renter-beneficiary unless one of the conditions set forth in 32 V.S.A. § 6062(e) are met; and (3) Ms. Morash is the sole beneficiary of the trust that owns her dwelling, but does not meet one of the conditions in § 6062(e). The commissioner accordingly affirmed the denial of Ms. Morash's renter rebate claim, and did not reach the question of whether her rebate should adjusted downward because the rental transaction was not arms' length. Ms. Morash appealed this determination to the Rutland Superior Court. 32 V.S.A. § 5885(b).

On appeal, Ms. Morash argues that the Tax Commissioner erred by denying her renter rebate claim on the basis of 32 V.S.A. § 6062(e). She contends generally that § 6062(e) should be interpreted as defining the circumstances under which a dwelling owned by a trust constitutes a "homestead" for purposes of the homeowner's property tax rebate, but not as applying to renter rebate claims, and advances several arguments in support of this contention. For this reason, Ms. Morash seeks reversal of the commissioner's determination, and remand so that the commissioner may consider the other bases for adjustment of her rental rebate claim.

Oral argument was heard on July 30, 2008. Ms. Morash was represented by Vermont Legal Aid Staff Attorney Jacob S. Speidel, Esq. The Department of Taxes was represented by Assistant Attorney General Timothy Collins, Esq.

This appeal requires the court to interpret the statutory scheme administering the statewide education property tax and two income-sensitive tax-adjustment programs—the property tax rebate available to homeowners, and the renter rebate—in relation to a trust beneficiary's claim of entitlement to a renter rebate. In interpreting these statutes, the court looks to "the whole statute, the subject matter, its effects and consequences, and the reason and spirit of the law," and gives the statutes a reasonable construction "so that they will neither be rendered ineffectual nor lead to irrational consequences." *In re R.S. Audley, Inc.*, 151 Vt. 513, 517 (1989) (citations omitted). The analysis begins with a review of the history of the legislative enactments relevant to this appeal.

In February 1997, the Vermont Supreme Court invalidated the then-existing system for financing public education through local property tax revenues. *Brigham v. State*, 166 Vt. 246 (1997). As a result, the Legislature was required to swiftly create a new system of statewide education funding, which it did by enacting "Act 60" in June 1997. Otherwise known as the "Equal Education Opportunity Act," Act 60 established several new mechanisms for funding schools on a statewide basis including, in pertinent part: (1) a new statewide Education Property Tax, which was imposed on all non-residential and homestead property at the same statewide rate, in Part 2 of the Act, "Property Taxation," and codified at 32 V.S.A. **ch. 135**, §§ 5401–5412; and (2) an Income-sensitive Property Tax Adjustment designed to provide relief from the new statewide property tax to income-eligible homeowners and renters, in Part 3 of the Act, "Income and Franchise Taxes, codified at 32 V.S.A. **ch. 154**, §§ 6061–6074.

The income-sensitive property tax adjustment involved two different tax rebates: (1) a property tax rebate for homeowners, which linked the amount of property tax paid

by the homeowner to the homeowner's income; and (2) a renter rebate, which recognized that a portion of rent paid by tenants to landlords is used to pay property taxes, and which is claimed as a state income tax credit by income-eligible renters for "rent constituting property taxes." 32 V.S.A. § 6066(b). The provisions governing both rebates are set forth in Title 32, Chapter 154, and the eligibility requirements for both the homeowner rebate and the renter rebate are set forth in § 6066(a) for homeowners and § 6066 (b) for renters.

Both the homeowner rebate and the renter rebate have certain eligibility requirements based on income and documentation, and both rebates require that the claimant have occupied a "homestead." Specifically, the homeowner's property tax rebate requires that the claimant have "owned the homestead on April 1 of the year in which the claim is filed." 32 V.S.A. § 6066(a). For the renter rebate, the claimant must have "rented the homestead on the last day of the taxable year." *Id*. § 6066(b).

At the time of Act 60's enactment in 1997, the term "homestead" was defined in two places. The first definition was set forth within the statutes establishing the statewide Education Property Tax (**ch. 135)**, and it defined a "homestead" as "the principal dwelling owned and occupied by a resident individual." 1997, No. 60, § 45 (codified as amended at 32 V.S.A. § 5401(7)). This definition of "homestead" said nothing about renters, which makes sense because this is a definition for purposes of **ch. 135** on the Education Property Tax, and renters do not directly pay the statewide property tax—the property tax is paid by owners.

The second definition of "homestead" was set forth in the statutes establishing the Income-sensitive Tax Adjustment programs (**ch. 154**), and explained that for purposes of income-sensitive tax relief, a "homestead" was "a dwelling as defined in section 5401(7) of this title, which is owned *or rented* by the claimant as the principal residence." 1997, No. 60, § 51 (originally codified at 32 V.S.A. § 6061(2)) (emphasis added). In other words, this "second definition" clarified that, for purposes of the renter rebate, the "homestead" is the principal dwelling rented by the claimant.

At the time of Act 60's enactment in 1997, the income-sensitive tax adjustment statutes did not address whether the beneficiary of a trust was entitled to claim either the homeowner rebate or the renter rebate when her principal dwelling was owned by the trust. The practical effect was that the beneficiary was never entitled to claim the homeowner rebate (because the trust, not the beneficiary, was the "owner" of the property), but there were no categorical restrictions upon the ability of a beneficiary/tenant to claim the renter rebate.

This situation changed in 1999, when the Legislature made a number of changes to the education funding laws. In pertinent part, the Legislature amended 32 V.S.A. § 6062, which contains several miscellaneous provisions pertinent to the income-sensitive tax adjustment. The following provision, 32 V.S.A. § 6062(e), was added. It defined when a dwelling owned by a trust qualified as a "homestead" of the trust beneficiary/claimant:

> (e) A dwelling owned by a trust is not the homestead of the beneficiary unless the claimant is the sole beneficiary of the trust and:
>
> (1) the claimant or the claimant's spouse was the grantor of the trust, and the trust is revocable or became irrevocable solely by reason of the grantor's death; or
>
> (2) the claimant is the parent, grandparent, child, grandchild or sibling of the grantor, the claimant is mentally disabled or severely physically disabled, and the grantor's modified adjusted gross income is included in the household income calculation.

The general rule established by § 6062(e) is that "a dwelling owned by a trust is not the homestead of the beneficiary" unless the conditions set forth in subsections (e)(1) or (e)(2) are met. Thus, although the general rule provides categorically that trust beneficiaries cannot claim income-sensitive tax relief for dwellings owned by the trust, subsections (e)(1) and (e)(2) establish situations when tax relief *is* available. The statute therefore has the effect of *expanding eligibility for the homeowner rebate*, for which trust beneficiaries were previously totally ineligible. The central question in this case is whether the statute was also intended to have the effect of categorically *limiting eligibility for the renter rebate by trust beneficiaries* unless they fall within the narrow categories defined in subsections (e)(1) or (e)(2).

The Commissioner determined that "the plain statutory language found in 32 V.S.A. § 6062(e) limits those instances where the beneficiary of an irrevocable trust, such as Ms. Morash, may receive a homestead property tax adjustment, whether as a homeowner or as a renter." Determination, page 4. Ms. Morash argues that this determination was erroneous, for three reasons. First, she argues that the structure and effect of § 6062(e) shows that the Legislature intended only to define when beneficiaries of grantor trusts may claim the homeowner rebate, and that it is unreasonable and counterproductive to interpret § 6062(e) as defining when beneficiaries of other trusts may or may not claim the renter rebate. Second, she argues that the Legislature has amended the definition of "homestead" at other times only in relation to the homeowner rebate, without also intending to alter eligibility for the renter rebate. Finally, she argues that the Department's interpretation is unreasonable because it could have the effect of precluding income-sensitive tenants who rent from charitable housing trusts to claim the renter rebate.

Whether § 6062(e) applies to renter rebate claims

Ms. Morash argues first that the language, structure, and effect of § 6062(e) show that the Legislature intended only to address the treatment of grantor trusts for purposes of the homeowner rebate, and did not intend for the statute to apply to renter claims.

Subsection (e)(1), which provides that a dwelling owned by a trust can be the "homestead" of the sole beneficiary if the claimant or the claimant's spouse was the grantor of a revocable trust, or if the claimant's spouse was the grantor of an irrevocable trust that became irrevocable solely by reason of the spouse's death, shows that one circumstance that the Legislature meant to address was the treatment of "grantor trusts" for purposes of income-sensitive tax relief.

Grantor trusts are trusts in which the grantor or creator of the trust has retained a significant degree of control over the trust assets. Because the grantor retains such control, the grantor (rather than the trust as a separate entity) is often treated as the "owner" of the trust property for purposes of federal and state income taxes. See I.R.C. §§ 671–77 (addressing federal tax treatment of grantor trusts); 32 V.S.A. § 5824 (adopting federal income tax laws for purposes of computing Vermont tax liability). Prior to 1999, although grantors were often treated as "owners" of the trust property for income tax purposes, they were not eligible to claim the homeowner rebate. For this reason, it is reasonable to interpret § 6062(e)(1) as a legislative attempt to identify those beneficiaries of grantor trusts who are treated as "owners" of the trust property for income tax purposes, and make income-sensitive property tax relief available to them.

It does not necessarily follow, however, that the Legislature intended § 6062(e) to address only how "grantor trusts" would be treated. Indeed, the scope of § 6062(e) is not limited to grantor trusts. Subsection (e)(2) addresses certain types of special-needs trusts, and provides that a dwelling owned by a trust may qualify as the "homestead" of the beneficiary if the claimant is mentally disabled or severely physically disabled, and the trust was settled by a close family member whose income is included in the household income calculation. Such trusts could be irrevocable ones, such as the one for Ms. Morash, rather than grantor trusts.

In other words, subsection (e)(2) can be reasonably interpreted, based on its language and structure, to make the renter rebate available to mentally disabled or severely physically disabled trust beneficiaries who fall within the defined category, but unavailable to other trust beneficiaries of non-grantor trusts who do not. It should be noted that in the circumstance of subsection (e)(2), the income of both the claimant and grantor are calculated together in order to determine eligibility for an income-sensitivity adjustment.

Ms. Morash argues that the statute does not specifically demonstrate an intent to deny access to the rebate to trust beneficiary tenants such as herself, and therefore the effect of the statute should be limited. The Department argues that the Legislature "specifically intended" to make the renter rebate unavailable to trust beneficiaries in order to avoid collaborative collusion problems between trusts and trustees. The language does not show such a specific intent. The Department has not provided any legislative history. The record provides no information one way or another as to whether the Legislature had any intentions at all except in relation to the two situations described in § 6062(e) (1) and (2).

There is nonetheless a rational basis for concluding that the construction of the statute described above--that beneficiaries are not eligible to claim the renter rebate when their dwelling is owned by a trust except as specifically described--is also supported by policy reasons. When a trust is well-funded, it is likely to pay the property tax and related expenses, and there is no need for either the claimant or the grantor to be seeking income-sensitive tax relief. Allowing beneficiaries of well-funded trusts to claim the renter rebate creates the potential for collusion between the beneficiary and the trustee in structuring an arrangement that may not serve the policy goals of income sensitivity, and it may be expensive for the Department to detect such situations.

When a trust is modestly funded, there could also be significant administrative costs in determining whether tax relief would serve the purposes of income sensitivity. For example, the Morash Trust has multiple grantors. The incomes of all grantors may have to be reviewed in order to determine eligibility for an income-sensitivity adjustment. There could also be issues in verifying whether income-sensitivity goals are being met in a trust with multiple beneficiaries, particularly where a trustee has discretion with respect to distribution of income. Again, the opportunity for collusion would be available, whereas the costs to the Department in verifying eligibility for income-sensitivity treatment could be great. While the statute makes income sensitivity available in non-grantor trusts in the limited circumstance of a special needs trust with certain characteristics, it is a reasonable legislative policy to make income sensitivity categorically unavailable to trust beneficiaries except in circumstances that are specifically identified.

Ms. Morash credibly asserts that there is not enough trust money available to pay property taxes in her case, and that the statute is having the effect of denying income sensitive property tax relief where it is needed. The situation is a sympathetic one. The solution to this problem is subject to legislative decision-making and line-drawing, however. The role of the court is to apply statutes as they are written if doing so is reasonable, and, for the reasons discussed above, it is reasonable to conclude that § 6062(e) defines the only circumstances under which a dwelling owned by a trust is a "homestead" for purposes of both the homeowner rebate and renter rebate.

Whether other amendments to Act 60 show that the Legislature did not intend to amend the definition of "homestead" for purposes of the renter rebate

Ms. Morash argues next that the history of legislative amendments to Act 60 shows that the Legislature has, at other times, amended the definition of "homestead" for purposes of the homeowner rebate without also intending to amend the definition for purposes of the renter rebate. The most pertinent example occurred in 2003, when the Legislature overhauled the statewide property tax to eliminate a controversial revenue-sharing pool and created a "split grand list" that taxed non-residential property at a significantly higher rate than homestead property. See generally 2003, No. 68 ("Act 68"); see also Laurie Reynolds, *Skybox Schools: Public Education as Private Luxury*, 82 Wash. U. L.Q. 755, 793 (2004) (describing the controversy surrounding Act 60's revenue-sharing pool, and the new funding mechanisms of Act 68). As part of

implementing the new property tax scheme, the Legislature significantly amended the definition of "homestead" for purposes of the statewide property tax, created the new term "housesite" to define the portion of a homestead eligible for property-tax relief, and (probably inadvertently) repealed as redundant the "second definition" of "homestead" in the income-sensitive tax-adjustment chapter that had made clear that a homestead could be "rented" for purposes of the renter rebate.[1]

The 2003 amendments are persuasive evidence that, when the Legislature was enacting and implementing Act 68, it intended to affect only the portions of the statewide property tax and income-sensitive tax relief programs that applied to homeowners, and that any effect the amendments had on the renter rebate program were inadvertent. However, the 2003 amendments were a response to a specific controversy involving the statewide property tax, and are not persuasive evidence that the Legislature had a similar intent in 1999 when it enacted 32 V.S.A. § 6062(e), which defines the circumstances under which a dwelling owned by a trust qualifies as a "homestead" for purposes of income-sensitive tax relief.

Furthermore, the court is not persuaded that the 2003 repeal of the definition of "homestead" means that Ms. Morash should receive a renter rebate for the tax year 2004. There is no evidence that the Legislature meant by this (probably inadvertent) amendment to eliminate the requirement that the claimant rent a "homestead" in order to be eligible for the renter rebate, and there is nothing unreasonable about inferring from § 5401(7)—the operative definition of "homestead" during the year 2004—that a "homestead" meant the principal dwelling rented by a claimant for purposes of the renter rebate.

Whether the Tax Commissioner's interpretation is unreasonable as applied to tenants of charitable housing trusts

Ms. Morash argues that the Tax Commissioner's interpretation of § 6062(e) threatens the ability of low-income tenants to claim the renter rebate when they rent property owned by a charitable housing trust, because charitable housing trusts often have broad "beneficiary" designations such as the "people of Vermont." Aside from going far beyond the facts of this case, this argument is not persuasive because, unlike private trusts, charitable trusts are not required to have definite or definitely ascertainable beneficiaries. Restatement (Second) of Trusts § 364. "In the case of a charitable trust the persons who are to receive benefits from the trust need not be designated; the beneficial interest is not given to individual beneficiaries, but the property is devoted to the accomplishment of purposes beneficial to the community." *Id.*, comment *a*. In short, § 6062(e) defines when a dwelling owned by a trust is the homestead of "the

[1] The Legislature corrected this oversight in 2005, No. 94 (Adj. Sess.), § 8, by amending the definition of "homestead" contained in the statewide property tax chapter, 32 V.S.A. § 5401(7). Therefore, the term "homestead" is presently defined in only one place in the tax statutes, and it means "the principal dwelling and parcel of land surrounding the dwelling, owned and occupied by a resident individual as the individual's domicile, or for purposes of the renter property tax adjustment under subsection 6066(b) of this title, rented and occupied by a resident individual as the individual's domicile." 32 V.S.A. § 5401(7)(A).

beneficiary," and charitable trusts do not name an individual beneficiary. For this reason, the court does not perceive an inherent problem in applying § 6062(e) to renter rebate claims.

Conclusion

For the foregoing reasons, the court concludes that it is reasonable to interpret 32 V.S.A. § 6062(e) as defining the only circumstances under which a dwelling owned by a trust is the "homestead" of the beneficiary for purposes of the renter rebate. The Tax Commissioner's Determination is accordingly affirmed.

ORDER

The Determination of the Tax Commissioner is *affirmed*.

Dated at Rutland, Vermont this ____ day of August, 2008.

_____
Hon. Mary Miles Teachout
Presiding Judge