

Taxes and Second Homes

Natural Resources, Fish, and Wildlife Committee

Graham Campbell, Senior Fiscal Analyst, JFO

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Background

- Vermont has a lot of seasonal/second homes
 - According to Census 2020, over 55,000 housesites were seasonal/recreational/occasional use (16.6% of total housesites)
 - “Vacant Homes” in Census
 - 62,428 homes in 2020 Census (18.6% of housesites)
 - 66,097 in 2010 Census (20.4% of housesites)
 - 53,748 in 2000 Census (18.2% of housesites)
 - IPX1031 estimates 17% of homes are vacation homes (2nd in the country)
- “Second Home” has many definitions:
 - Census definition is very broad: seasonal, temporary, occasional, recreational
 - Includes detached homes, condos, apartments, camps, lake houses, cottages, etc...



Background: Vermont Department of Taxes

- Any home that is not a homestead is considered nonhomestead
 - Nonhomestead includes second homes, seasonal rentals, etc, but it also includes commercial, industrial, business, farms, etc...
- 18 different property categorizations
- R1, R2: Residential properties
- S1, S2: Seasonal properties
- S1, S2 properties are generally those who have seasonal home characteristics deemed by the assessor
 - Lack of insulation, heat, on a concrete slab
- Normal, non-seasonal homes that are used as a second residence are likely captured as a R1 or R2
- In short: there is no great way in the current property tax system to identify second homes, especially those that are limiting housing supply in Vermont.



Taxes and Second Homes

- Generally, the Federal and Vermont tax codes do not have strict definition of “second home” or “vacation home”
- Most of the time, the tax code distinguishes between primary and secondary/other residences.
- Overall, there are few to no provisions in either Vermont or Federal tax code that benefit second homes relative to primary homes
- But: many second homeowners can utilize many of the tax benefits that are provided to real estate in the tax code.



Taxes for Second Homes: Personal Income Tax

- Federal tax code:
 - Itemized deductions
 - Home mortgage interest deduction: individual can deduct the interest on mortgages up to \$750,000 of debt.
 - State and local tax deduction: taxpayers can deduct property taxes paid on first or second homes (as well as state and local income and sales taxes) up to \$10,000
 - These deductions most likely benefit second homeowners more than single-home homeowners because higher income households are much more likely to itemize
 - Deductions for Rental Property
 - Many second homes operate as rental properties, ie, like a business
 - Mortgage interest cost and taxes are deductible expenses under Federal tax code
 - Capital Gains
 - 1) Capital gains exclusion of \$500k for a primary residence. If owner lives in second home two of past five years, they can claim this exclusion
 - 2) For those second homeowners who do owe capital gains, they pay lower rates on capital gains relative to regular income



Taxes and Second Homes: Personal Income Tax

- Vermont
 - In general, Vermont does not provide any specific tax benefits to second homeowners that don't apply to primary homeowners.
 - Federal deduction flow-through
 - Because Vermont income taxes start with AGI, if a rental property deducts mortgage or tax expenses, that deduction flows through to Vermont
 - Capital Gains Exclusion
 - Vermont picks up the Federal capital gains exclusion for the sale of primary residence
 - Vermont's Capital Gains Exclusion: VT-specific exemption that allows \$5,000 of capital gains to be excluded from taxation.



Taxes and Second Homes: Property Tax

- Second homes are classified as nonhomestead property
- Generally, the legislature sets the yields for both types of properties, so levels and changes are similar to prevent distortions:
 - FY2022: \$1.523 for homestead, \$1.612 for nonhomestead.
- Homestead owners benefit from the Property Tax Credit and second homeowners do not:
 - PTC reduces homestead property taxes by about \$170 per year



Taxes and Second Homes: Other

- Use Value Appraisal
 - Second homeowners with large landholding likely benefit from the property tax savings from UVA, but it's not a special benefit relative to primary homeowners.
 - JFO does not have data on the number of parcels enrolled that contain a housesite *and* is owned by a nonresident owner.
- Property Transfer Tax
 - Vermont levies transfer of property by deed or controlling interest.
 - Paid by the buyer. Buyers and sellers indicate what they intend to property for
 - If transferee uses it for principal residence: lower tax rate. Otherwise, 1.25% on entire transfer

VT Property Transfer Tax Table		
Property Type	First \$100K	Over \$100K
Principal Residence	0.50%	1.25%+ 0.2% (CWS)
VHFA, VHCB, USDA (first \$110K)	No Tax	1.25% + (0.2% CWS on amounts above \$200k)
All Other	1.25% +(0.2% CWS)	

CWS: Clean Water Surcharge

VHFA: Vermont Housing Finance Agency

VHCB: Vermont Housing and Conservation Board

USDA: U.S. Department of Agriculture



Considerations for second homes and the tax code

- Definition of second home is very nuanced. What is the target?
- Build a new tax system or use an existing system?
 - **Property tax:** would probably require a declaration of non-occupied housesite, similar to homestead declaration
 - Compliance and administration could be an issue.
 - **Income tax:** Vermont does not offer much in the form of incentives to take away. Most benefits are Federal.
 - **Property Transfer Tax:** Probably the easiest, most straightforward because buyer and seller list their uses of the property, but it is only collected once



What do other states do?

- JFO could not find state taxes on second homes specifically
- Washington DC levies a higher property tax on vacant properties.
 - Tax is \$5 per \$100 of assessed value. Ordinary property is about \$0.85
- Vancouver BC has a vacant property tax of 3% on the value of the home that is not a primary residence.
 - Requires a declaration by the owner

