Department of Legislative Services

Maryland General Assembly
2014 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 709 (Senator Dyson, *et al.*)

Budget and Taxation Rules and Executive Nominations

Income Tax Credit - Preservation and Conservation Easements

This bill alters the existing preservation and conservation easement income tax credit by shifting the program from a traditional tax credit program to a tax credit program subject to an aggregate limitation administered by the Maryland Environmental Trust (MET). MET must award credits on a first-come, first-served basis. The bill also expands the program by (1) allowing pass-through entities to claim a credit of up to $10,000 in a taxable year and (2) allowing an easement conveyed to the Department of Natural Resources (DNR) to qualify for the credit. The Comptroller's Office, in consultation with MET, is required to adopt regulations implementing the bill.

The bill takes effect July 1, 2014, and applies to tax year 2014 and beyond.

Fiscal Summary

State Effect: General fund revenues may decrease beginning in FY 2015 to the extent the bill increases the amount of credits claimed in a tax year and if credits are claimed against the estate tax. Expenditures are not affected.

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill alters the preservation and conservation easement income tax credit by shifting the program from a traditional tax credit program to a tax credit program subject to an aggregate limitation administered by MET. MET must award credits on a first-come, first-served basis. Subject to availability, MET must award a tax credit certificate to each person who has demonstrated that an easement conveyance was approved by the Board of Public Works. Tax credit certificates must state the total credit that can be claimed, the maximum amount that can be claimed in each year, and the earliest and last tax year the credit may be claimed. The amount of certificates issued by MET may not exceed an amount that would allow more than $250,000 in credits to be claimed in a single year.

A tax credit certificate may be transferred to specified individuals, and the Comptroller may charge a fee of 3% of the value of the credit to pay the cost of administering the transfer of tax credit certificates. Any fees must be distributed equally between the Comptroller and MET. The Comptroller's Office, in consultation with MET, must adopt regulations implementing the bill and to specify the procedures for transferring credits.

The bill expands the tax credit program by allowing easements conveyed to DNR to qualify for the tax credit. In addition, the maximum value of the tax credit that can be claimed in each year is increased from $5,000 to $10,000 if the taxpayer is a pass-through entity with more than one member or the taxpayer's filing status is spouse filing a joint return, head of household, or surviving spouse. If a taxpayer dies, any unused amount of the credit may be claimed against the decedent's Maryland estate tax liability.

It is the intent of the General Assembly that the issuance of tax credit certificates as provided by the bill may not adversely impact the annual budgets of State agencies or programs that purchase or acquire conservation easements or property, including DNR and the Maryland Agricultural Land Preservation Fund. For the purposes of transferred tax credits, MET must (1) use best efforts to obtain donated easements in those areas targeted for preservation, including GreenPrint and AgPrint and (2) report, in consultation with DNR, by December 1, 2016 to the General Assembly on the effectiveness of transferred tax credits in encouraging the conveyance of easements.

Current Law:

Preservation and Conservation Easements Tax Credit

Individuals who donate or sell a perpetual easement to the Maryland Environmental Trust or Maryland Agricultural Land Preservation Foundation (MALPF) can qualify for a State income tax credit. The easement must be accepted and approved by the Board of Public Works.

The amount of the credit allowed is the amount by which the fair market value of the property before the conveyance of the easement exceeds the fair market value of the property after the conveyance of the easement. The fair market value of the property before and after the conveyance of the easement is substantiated by an appraisal prepared by a certified real estate appraiser. The amount of the credit is reduced by the amount of any payment received for the easement. The amount of the credit allowed for any taxable year may not exceed the lesser of the State income tax liability or $5,000. Any unused credit may be carried forward for up to 15 years, but may not exceed the lesser of the State tax or $5,000 in any taxable year. The credit may not be claimed for a required dedication of open space for the purpose of fulfilling density requirements to obtain a subdivision or building permit.

Federal and State Tax Treatment of Easements and Farm Property

Donors of conservation easements may claim a federal income tax deduction. The donation must be exclusively for conservation purposes and the easement must be conveyed to a governmental unit or a qualified organization that is a 501(c)(3) charitable organization with the commitment and resources to enforce the easement's restrictions. An enhanced deduction was available in tax years 2006 through 2013. This deduction reduces federal adjusted gross income, which in turn will reduce any State and local taxes by flowing through to Maryland adjusted gross income.

Federal estate tax law provides for additional estate tax relief for small businesses and farms to address concerns that the federal estate tax could hinder families who wish to pass on a farm or small business to their heirs. These benefits include special-use valuation and exclusion for conservation easements as described below. Most of these provisions allow for a reduction in the value of the estate for federal estate tax purposes; this reduction generally flows through to the Maryland estate tax and can result in a reduction in State tax liability. In addition, special rules apply under the Maryland estate tax for qualified agricultural land. Chapters 448 and 449 of 2012 exempt from the State estate tax up to $5.0 million in qualified agricultural property.

The federal Taxpayer Relief Act of 1997 allows farmers and other landowners to exclude a certain amount of the value of land subject to a qualified conservation easement for estate tax purposes. To qualify for the exclusion, the decedent or a family member must have owned the land for at least three years prior to the decedent's death. They also must have made a qualified conservation contribution, such as a perpetual restriction or easement on the use of real property for conservation purposes, to a charity or other qualifying organization.

In addition, numerous counties are authorized to provide a property tax credit against the county property tax imposed on real property that is subject to a perpetual conservation easement. This credit is in addition to the special property tax assessment of farm property.

Background: MALPF, which was established by the General Assembly in 1977 and is part of the Maryland Department of Agriculture, purchases agricultural preservation easements that restrict development on prime farmland and woodland in perpetuity. In addition to funding from the State transfer tax, MALPF is funded with agricultural land transfer taxes, local matching funds, and the U.S. Department of Agriculture's Farmland Protection Program. MALPF settled on its first purchased easement in October 1980. As of the end of fiscal 2012, MALPF had cumulatively purchased 2,102 farms covering 285,902 acres.

The Rural Legacy program, established in 1997 and administered by DNR, supplements State land preservation programs in order to preserve key areas before escalating land values render protection impossible or before the land is lost to development.

State Revenues: The bill alters the existing preservation and conservation easement tax credit by shifting the program from a traditional tax credit program to a tax credit program subject to an aggregate limitation administered by MET. The bill also (1) allows the credit to be transferable and for certain taxpayers to claim a maximum credit of $10,000 and (2) allows the estate of a decedent who had any unused amount of the credit to claim the unused amount against the decedent's Maryland estate tax liability.

The impact of the income tax provisions will depend on the number of eligible conservation easements conveyed each year. In recent years, the number of easement conveyances has decreased. In fiscal 2003, MALPF acquired easements from 143 farms totaling $33.3 million; in fiscal 2013, MALPF acquired easements from 13 farms totaling $7.9 million. Although the total credit may be substantial, the amount claimed in each tax year under current law is limited to the lesser of $5,000 or the tax liability in the year. In tax year 2012, 312 taxpayers claimed a total of $961,400 in credits. Within the last five years, taxpayers have claimed an average credit of $3,062 in each tax year.

Current law provides that a maximum of $75,000 in credits can be claimed over 15 years. ($150,000 if claimed by certain taxpayers under the bill). The bill provides that any unclaimed amount of the credit can be claimed against the estate tax. To the extent that credits are claimed against the estate tax, estate tax revenues may decrease significantly beginning in fiscal 2015.

Additional Information

Prior Introductions: None.

Cross File: HB 789 (Delegate Stein, *et al.*) - Ways and Means and Environmental Matters.

Information Source(s): Comptroller's Office, Department of Legislative Services

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