SB 345

Department of Legislative Services
Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE

Senate Bill 345 (Senators Middleton and King)
Budget and Taxation Ways and Means

Income Tax - Subtraction Modification - Enhanced Agricultural Management Equipment

This bill expands the existing conservation tillage equipment income tax subtraction modification to include qualified purchases of specified (1) poultry or livestock manure loading or hauling equipment used to transport animal manure from a farm; and (2) commercial fertilizer application equipment used by a farm operator that previously used manure exclusively as a fertilizer source.

The bill takes effect July 1, 2015, and applies beginning in tax year 2015 to qualified equipment purchases made after December 31, 2014.

Fiscal Summary

State Effect: General fund revenues may decrease beginning in FY 2016 due to additional subtraction modifications being claimed. The amount of the revenue loss depends on the amount of qualifying equipment purchased in each year, as discussed below. Potential minimal decrease in Transportation Trust Fund (TTF) and Higher Education Investment Fund (HEIF) revenues. Expenditures are not affected.

Local Effect: Local income tax revenues and local highway user revenues may decrease beginning in FY 2016 due to subtraction modifications claimed against the personal and corporate income tax. Expenditures are not affected.

Small Business Effect: Minimal. Small businesses that purchase qualifying equipment will benefit from the subtraction modification.

Analysis

Bill Summary: The bill expands the existing conservation tillage equipment income tax subtraction modification to include qualified purchases of (1) poultry or livestock manure loading or hauling equipment used to transport animal manure from a farm if the equipment is nonself-propelled wheeled equipment or nonpowered trailed units capable of self-unloading and (2) commercial fertilizer application equipment used by a farm operator that previously used manure exclusively as a fertilizer source. Taxpayers who purchase this equipment after December 31, 2014, may claim a subtraction modification for 100% of the costs of the equipment if the equipment has a useful life of at least four years and the taxpayer (1) owns the equipment for at least three years after the taxable year in which the subtraction modification is claimed; (2) uses the equipment to transport animal manure from a farm; and (3) files a statement from the Maryland Department of Agriculture (MDA) certifying compliance.

The bill also alters the qualifications for claiming the existing subtraction modification for poultry or livestock manure spreading equipment. Under current law, taxpayers can claim a subtraction modification for this equipment used by a farm owner or tenant on farmland in accordance with a nutrient management plan prepared by an individual licensed by the Secretary of Agriculture. The bill will allow the subtraction modification to be claimed if individuals are certified, instead of licensed, by the Secretary of Agriculture.

Current Law: Maryland income tax law provides a subtraction modification equal to the specified expenses incurred by a taxpayer for the purchase and installation of qualified conservation tillage equipment. Taxpayers must meet certain requirements and receive certification from MDA in order to claim the subtraction modification.

Except as noted, taxpayers who meet certain qualifications can claim a subtraction modification for 100% of the qualified expenses of enhanced agricultural equipment including (1) a "notill" planter or drill; (2) liquid manure soil injection equipment; (3) a deep no-till ripper; (4) poultry or livestock manure spreading equipment; (5) vertical tillage equipment (50% subtraction modification); (6) a global positioning system device used for management of agricultural nutrient applications; and (7) certain integrated optical sensing and nutrient application systems. Any unused amount of the subtraction modification can be carried forward for five tax years.

In addition to the State subtraction modification, farm operators can typically expense or depreciate the cost of farm equipment acquired in the tax year, which typically lowers federal and State income tax liability.

Background: Poultry manure is a waste product from the poultry industry and a fertilizer for the domestic grain industry – inexpensive poultry manure is now being used on the

Eastern Shore in place of inorganic fertilizers. However, poultry manure has a 1.0 to 1.5 ratio of nitrogen to phosphorus, which is a lower ratio than the 3.0 to 1.0 ratio of nitrogen to phosphorus needed in a corn crop. As a result, the poultry manure creates an imbalance in the phosphorus balance in the soil.

The objective of the Phosphorous Management Tool (PMT), developed by the University of Maryland, is to identify critical areas where there is high potential for phosphorus loss due to high potential for transport to nearby surface waters and a large source of phosphorus, and also to encourage the use of management practices in those critical source areas that protect water quality. Adopting the PMT is an element of Maryland's Phase II Watershed Implementation Plan (WIP), the federally mandated document that outlines specific steps the State will take to protect and restore the Chesapeake Bay under the Total Maximum Daily Load (TMDL). TMDL sets forth specific pollution reduction requirements for Maryland and other jurisdictions within the bay watershed. All reduction measures must be in place by 2025, with at least 60% of the actions completed by 2017. The U.S. Environmental Protection Agency (EPA) required each bay jurisdiction to develop WIPs detailing the strategies and specific actions that will be implemented to reduce pollution. Phase I WIPs were completed in 2010, and more detailed Phase II WIPs were completed in early 2012. A Phase III WIP, which must be submitted to EPA in 2018, will ensure that all practices are in place by the 2025 deadline.

Regulations implementing the PMT have been proposed over the past two years, and MDA submitted regulations for the phosphorus management tool on November 14, 2014. Due to concerns about the impact of the implementation of the PMT on agricultural operations, the General Assembly adopted budget bill language in the 2014 session restricting MDA funding, except for funds relating to the cost of an economic impact analysis, for final development and submission of phosphorus management tool regulations until MDA submitted a full economic analysis of the impact of the proposed regulations on the State's Chesapeake Bay restoration efforts and on a person who is required to have a nutrient and management plan for nitrogen and phosphorus.

MDA submitted on November 7, 2014, an analysis conducted by the Business Economic and Community Outreach Network (BEACON) at Salisbury University. The report estimated the potential costs and benefits of PMT implementation under three different scenarios and included policy options for the State to provide financial assistance to impacted farmers. One of the options included providing a subtraction modification for manure hauling equipment, as proposed by the bill. The proposed PMT regulations were published for public notice and comment in the December 1, 2014 issue of the *Maryland Register*. The regulations were adopted by MDA in January 2015, but the adoption letter was subsequently withdrawn. The proposed regulations have not been published for final adoption as of February 23, 2015. In its most recent evaluation of Maryland's progress in implementing the milestones associated with the bay TMDL, EPA noted that the failure to adopt PMT regulations was a "shortfall" in the State's otherwise sufficient progress to date.

State Revenues: Additional subtraction modifications may be claimed beginning in tax year 2015. As a result, general fund revenues may decrease beginning in fiscal 2016 due to subtractions claimed against the personal and corporate income tax. TTF and HEIF revenues may decrease beginning in fiscal 2016 due to subtraction modification claims against the corporate income tax. The amount of the revenue loss depends on the amount of qualifying equipment purchased in each year.

The BEACON report estimated the cost of providing a State income tax subtraction modification for manure hauling equipment under a six-year phased implementation of PMT regulations. Based on these assumptions, general fund revenues may decrease by $46,300 in fiscal 2017, $138,800 in fiscal 2018, $185,100 in fiscal 2019, and $97,500 in fiscal 2020. This estimate is based on the following assumptions over the four-year period:

- a total of 30 manure hauling trucks and 10 conveyors will be purchased;
- 177 farms will purchase eligible commercial fertilizer equipment;
- average cost of the equipment – trucks ($85,000), conveyor ($40,000), and fertilizer equipment ($15,000); and
- all subtraction modifications are claimed against the personal income tax.

Revenue losses will be higher to the extent additional farms that are not impacted by PMT regulations purchase eligible equipment and claim the subtraction modification.

Local Revenues: Local income tax revenues and local highway user revenues may decrease beginning in fiscal 2016 due to subtraction modifications claimed against the personal and corporate income tax. Under the BEACON report assumptions above, local revenues will decrease by $17,400 in fiscal 2017, $52,200 in fiscal 2018, $69,500 in fiscal 2019, and $34,800 in fiscal 2020.

Additional Information

Prior Introductions: None.

Cross File: HB 536 (Delegate McIntosh, *et al.*) - Ways and Means.

Information Source(s): Salisbury University, Department of Legislative Services

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