Department of Legislative Services

Maryland General Assembly
2023 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 418 (Senator Elfreth, *et al.*)
Budget and Taxation

Property Tax - Agricultural Land and Improvements - Assessment

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This emergency bill requires that an improvement located on an actively used farm that supports value-added agricultural activities must be assessed at the agricultural use rate. In addition, land that is used for value-added agricultural activities must be valued on the basis of that use and may not be valued as if subdivided. The State Department of Assessments and Taxation (SDAT) must reassess, by July 1, 2023, any improvement described as a value-added agricultural activity on an actively used farm that was assessed as nonagricultural property on or after January 1, 2021, but before the enactment of the legislation.

Fiscal Summary

State Effect: Annuity Bond Fund (ABF) revenues decrease by a significant amount beginning in FY 2024. Under one set of assumptions, revenues decrease by approximately $35 million annually beginning in FY 2024. This decrease may require either (1) an increase in the State property tax rate, or (2) a general fund appropriation to cover debt service on the State's general obligation bonds. General fund expenditures for mileage reimbursements increase by $84,000 in FY 2023. In addition, SDAT will be required to reassign a large portion of existing staff to handle the additional workload required by the bill. As a result, existing departmental responsibilities will be adversely affected or delayed.

Local Effect: Local property tax revenues decrease by a significant amount beginning in FY 2024. Under one set of assumptions, revenues decrease by approximately $300 million beginning in FY 2024. Expenditures are not affected.

Small Business Effect: Potential meaningful. Small businesses that own specified types of buildings located on agricultural land will benefit from reduced real property tax assessments for these buildings and therefore benefit from reduced State and local real property taxes. However, similar businesses that are not located on agricultural property may be at a competitive disadvantage.

Analysis

Bill Summary: Value-added agricultural activity is defined as activity on an actively used farm that is related to (1) specified agricultural alcohol production; (2) specified agritourism; (3) specified equine activities; (4) increasing the value of an agricultural product by processing, manufacturing, packaging, storing, selling, or promoting the agricultural product, if the agricultural product is derived from ingredients produced on the farm or any associated farmland; (5) roadside stands; (6) other agricultural uses that are permissible under local zoning; and (7) any other activities that the Secretary of Agriculture determines by regulation are value-added agricultural activities.

Value-added agricultural activity does not include (1) renting a facility for private events if the facility has a seating capacity of 200 or more individuals or (2) any activity that the local zoning authority has not approved for agricultural use.

Current Law: The Tax-Property Article (§ 8-209) states that it is the intention of the General Assembly that the assessment of farmland (1) be maintained at levels compatible with the continued use of the land for farming and (2) not be affected adversely by neighboring land uses of a more intensive nature.

Land that is actively used for farm or agricultural use must be valued on the basis of that use and may not be valued as if subdivided. Land that is valued as agricultural use must be assessed on the basis of its use value. SDAT must establish in regulations criteria to determine if land that appears to be actively used for farm or agricultural purposes (1) is actually used for farm or agricultural purposes and (2) qualifies for an agricultural use assessment. The criteria must include (1) the zoning of the land; (2) the present and past use of the land including land under the Soil Bank Program of the United States; (3) the productivity of the land, including timberlands and reforested lands; and (4) the gross income that is derived from the agricultural activity.

Generally, land qualifying for an agricultural use assessment is valued between $187.50 to $500 per acre.

Chapter 643 of 2022

Chapter 643 of 2022 required the Maryland Department of Agriculture and SDAT to jointly conduct a study of the assessment of agricultural accessory use improvements. The departments were required to submit a joint report of their findings and recommendations to the Senate Budget and Taxation Committee and the House Ways and Means Committee by December 1, 2022.

In conducting the study, the departments were required to consult with (1) local governments; (2) nonprofit associations that represent agricultural interests, alcohol manufacturers, and equine interests; and (3) other relevant stakeholders.

The study was required to examine (1) whether agricultural accessory use improvements should be assessed using a different methodology from improvements located on nonagricultural land; (2) if a different methodology for assessing agricultural accessory use improvements is recommended, the proper method for assessing agricultural accessory use improvements; and (3) how other states assess agricultural accessory use improvements.

The report was submitted on December 1, 2022, and included the following recommendations:

- Agricultural accessory use improvements should not be assessed using a different methodology from improvements located on nonagricultural land. Based on a report from the University of Maryland, the current assessment methodology used by SDAT is similar to the approach used in most other states.

- Property tax exemptions are largely controlled at the local level, given that the county and local governments receive the largest apportionment of that revenue. To remain consistent across property types, property tax exemptions should remain a local self-determination topic for local governments. For example, Frederick County currently grants a property tax credit to offset the assessment of agricultural use improvements for agricultural property that has been placed in a conservation easement. A jurisdiction that desires to provide tax relief for agricultural accessory use improvements should choose to do so based on their own self-determination and governance.

State Revenues: SDAT advises that the department currently values parcels of land based on the actual use occurring on the land and has done so since 1974. A parcel may have a portion of the land that is actively used for an approved agricultural use that qualifies that portion of the land to receive an agricultural use assessment. The same parcel may have other land not used for an approved agricultural use with that portion of the land being valued at the full cash value of the land. Typically, these portions of land include any homesite located on the parcel. All buildings on a parcel of land are valued at their full cash value based upon the actual type, features, and quality of building construction. In general, land qualifying for an agricultural use assessment is valued at approximately 5% to 10% of the actual market value.

Under the bill, buildings or structures erected on a parcel of land whereby a portion qualifies for an agricultural use assessment would require the building or structure to be assessed as agricultural property, if the building or structure contributes to a value-added agricultural activity. For example, a manufacturing building used to brew beer or distill spirits would no longer be valued based upon the actual type, features, and quality of building construction but rather like an agricultural type of property. According to SDAT, this change in assessment practices would extend to buildings with bars, tasting rooms, banquet facilities, restaurants, retail sales, and similar buildings with commercial kitchens and restroom facilities.

As a point of reference, the Alcohol and Tobacco Tax Commission's annual report for fiscal 2022 indicates the number of agricultural related alcohol manufacturing licenses issued for fiscal 2022:

- Rectifying License – 24;
- Winery License – 7;
- Limited Winery License – 100;
- Farm Brewery License – 35; and
- Limited Distillery License – 5.

As a result of this change in assessment practices, ABF revenues will decrease by a significant amount beginning in fiscal 2024. Under the following set of assumptions, revenues may decrease by approximately $35 million annually beginning in fiscal 2024. The estimate is based on the following:

- there are approximately 359,000 real property tax accounts with an agricultural use assessment, of which approximately 234,000 have a building or structure that could be used for value-added agricultural activities;
- altering the assessment of improvements on this land may result in an assessable base decrease of approximately $31.4 billion in fiscal 2024; and
- the State real property tax rate is $0.112 per $100 of assessment.

SDAT notes that there may be additional revenue impacts once it is determined if facilities such as grain mills, food processing plants, cannabis processing plants, etc., qualify for agricultural use assessments under the bill.

Impact on Debt Service Payments

Debt service payments on the State's general obligation bonds are paid from the ABF. Revenue sources for the fund include State property taxes, premium from bond sales, and repayments from certain State agencies, subdivisions, and private organizations. General funds may be appropriated directly to the ABF to make up any differences between the debt service payments and funds available from property taxes and other sources. The fiscal 2024 State budget includes $1.5 billion for general obligation debt service costs, including $433.8 million in general funds, $1.0 billion in special funds from the ABF, $7.0 million in transfer tax revenues, and $7.5 million in federal funds.

To offset the reduction in State property tax revenues, general fund expenditures could increase in an amount equal to the decrease in the ABF revenues, or the State property tax rate would have to be increased to meet debt service payments. This assumes that the ABF does not have an adequate fund balance to cover the reduction in State property tax revenues.

State Expenditures: The bill alters the assessment of certain types of buildings located on agricultural land by having them assessed comparably to other types of agricultural buildings. SDAT advises that the department would have to reassess approximately 234,000 properties to meet the specifications outlined in the bill. These reassessments will require approximately 58,500 hours to inspect the property and an additional 58,500 hours to make any necessary changes to the SDAT records. SDAT advises that these reassessments will take approximately two to three months to complete, but the additional workload will have to be absorbed with existing budgeted resources as there will not be time to hire and train additional assessors.

Due to the July 1, 2023 deadline to complete the reassessments, other departmental tasks and assessment responsibilities scheduled in calendar 2023 will be adversely affected or delayed. The department will have to reassign a large portion of their existing staff to complete the reassessments required by the bill. On an annualized basis, the additional workload required by the legislation would represent approximately 65 staff positions. However, since the reassessments must be completed within two to three months, a much larger contingent of assessors would be needed to handle the bill's requirements.

The department also advises that there will be increased mileage expenditures of approximately $84,000 in fiscal 2023 as a result of the additional reassessments.

Finally, SDAT will need to mail new agricultural use assessment applications to all agricultural property owners. The application will need to include a description of each building located on the property and the use of each building.

Local Fiscal Effect: Local property tax revenues decrease by a significant amount beginning in fiscal 2024. Based on the assumptions used for the State revenue effect, local property tax revenues may decrease by approximately $300 million beginning in fiscal 2024, based on current county and municipal property tax rates.

Additional Information

Prior Introductions: Similar legislation has been introduced within the last three years. See HB 1282 and SB 567 of 2022.

Designated Cross File: HB 592 (Delegate Watson) - Ways and Means.

Information Source(s): State Department of Assessments and Taxation; Department of Legislative Services

Fiscal Note History: First Reader - February 20, 2023
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