

Department of Legislative Services  
2010 Session

FISCAL AND POLICY NOTE  
Revised

Senate Bill 396

(Senator Middleton, *et al.*)

Budget and Taxation

Ways and Means

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Maryland Estate Tax - Pilot Program for Payment Deferral for Qualified  
Agricultural Property

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This bill requires the Comptroller to allow a payment deferral for up to three years for the Maryland estate tax imposed on qualified agricultural property that passes from a decedent to or for the use of a qualified recipient. The bill specifies that any deferred tax is due immediately if the qualified agricultural property ceases to be used for farming purposes. The Comptroller is required to submit a specified report to the General Assembly by October 1, 2013 on the deferral payment pilot program.

The bill takes effect July 1, 2010, and applies to decedents dying after December 31, 2010. The bill terminates June 30, 2014.

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Fiscal Summary

**State Effect:** Potential reduction in general fund revenues in FY 2011 through 2014. The amount of the revenue decrease depends on several factors including the amount of Maryland estate tax that is owed and the number of qualified recipients who opt to defer estate tax payments. The potential revenue loss is expected to be relatively minor compared to overall revenue collections. General fund revenues will increase beginning in FY 2014 upon repayment

**Local Effect:** None.

**Small Business Effect:** Potential meaningful. Small businesses which are farms may benefit from deferring State estate taxes.

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## Analysis

**Bill Summary:** Qualified agricultural property is real or personal property that is used primarily for farming purposes. A qualified recipient is an individual who enters into an agreement to use qualified agricultural property for farming purposes after the decedent's death.

The amount of tax eligible for deferral is the amount equal to the Maryland estate tax owed multiplied by the percentage resulting from dividing the value of the qualified agricultural property that passes from the decedent to or for the use of a qualified recipient by the value of the gross estate of the decedent. The amount of tax that may be deferred for any one decedent may not exceed \$375,000.

In order to be eligible for a payment deferral, a qualified recipient must file an application and enter into an agreement in a form specified by the Comptroller to use the qualified agricultural property for farming purposes after the decedent's death and file periodic reports or allow periodic inspections as required by the Comptroller.

The Comptroller must submit a report to the General Assembly by October 1, 2013 on: (1) the number of approved applications for Maryland estate tax payment deferral; (2) the number of agricultural acres in which a Maryland estate tax payment deferral was approved under the payment deferral pilot program; (3) the number of qualified agricultural properties approved for Maryland estate tax payment deferral that apply to preserve agricultural land under MALPF; (4) the aggregate value of Maryland estate tax payment deferrals approved under the payment deferral pilot program; (5) the aggregate amount of Maryland estate taxes paid due to exceeding the maximum amount eligible for payment deferral under the payment deferral pilot program; and (6) recommendations for implementing a Maryland estate tax payment deferral program in the State.

**Current Law/Background:** The federal Economic Growth and Tax Reconciliation Act of 2001 provided for the reduction and ultimate repeal of the credit allowed under the federal estate tax for state death taxes paid (federal credit). Maryland, like most states, had an estate tax that was linked directly to the federal credit. Without statutory changes by the General Assembly, the repeal of the federal credit under the 2001 federal tax Act would have automatically repealed the State estate tax because of the link between the State tax and federal credit.

As part of the Budget Reconciliation and Financing Act (BRFA) of 2002, the Maryland estate tax was partially decoupled from the federal estate tax, thereby continuing the State tax notwithstanding the phase out and repeal of the federal credit.

### *Unified Credit*

The Maryland estate tax is calculated as the lesser of the federal estate tax after deducting the unified credit or the federal credit, reduced by any inheritance tax paid. The unified credit used to calculate the State estate tax, which effectively sets the threshold for taxability of an estate, is the unified credit in effect as of the decedent's death as set forth in federal law. Under the federal Act, the amount effectively exempted under the unified credit was increased from \$700,000 to \$1.0 million in 2002, and then phased up over a period of years to \$3.5 million in 2009.

The 2002 BRFA did not, however, decouple the Maryland estate tax from the gradual increases in the unified credit allowed against the federal estate tax. As the unified credit increases, the amount of the Maryland estate tax will decline.

The 2004 BRFA had the effect of freezing the amount of the unified credit at \$345,800 so as to exclude \$1.0 million from the federal estate tax for purposes of the Maryland estate tax calculation. The 2004 BRFA affected the estate tax returns filed for decedents dying after December 31, 2003.

### *2006 Legislation*

Chapter 225 of 2006 limited the amount of the federal credit used to calculate the Maryland estate tax to 16% of the amount by which the decedent's taxable estate exceeds \$1.0 million. Chapter 225 also clarified Maryland estate tax law to reflect the partial decoupling of the Maryland estate tax from the federal estate tax by (1) clarifying that the person responsible for filing a federal estate tax return is also responsible for filing a Maryland estate tax return; (2) providing for the filing of an amended Maryland estate tax return under specified conditions and the timeframe within which this must be accomplished; (3) establishing criteria under which an individual may receive an extension on the deadline to file a Maryland estate tax return; (4) allowing a Maryland estate to elect to treat property as marital deduction qualified terminable interest property in calculating the Maryland estate tax; and (5) providing that such an election on a timely filed Maryland estate tax return must be recognized for the purposes of calculating the Maryland estate tax even if an inconsistent election is made for the same decedent for federal estate tax purposes.

### *Federal Estate Tax*

Federal law allows estates to value farms (and other closely held businesses) at their current use value rather than their highest and best use value if the heirs agree to keep the property in its current use for at least 10 years; however, however, the current use valuation may only reduce the value of the estate by up to \$1.0 million (for decedents

dying in 2009). The law provides for the recapture or payment of estate taxes if these conditions are not met. However, under the federal Economic Growth and Tax Reconciliation Act of 2001 the federal estate tax is repealed for decedents dying in 2010.

Federal law also allows farmers, under certain conditions, to exclude the value of a qualified conservation easement from a taxable estate and to pay estate taxes in installments.

**State Fiscal Effect:** In fiscal 2011, the State is projected to collect \$106.9 million in estate taxes.

General fund revenues may decrease in fiscal 2011 through 2014 from the tax deferral created by the bill. However, the amount of any annual decrease cannot be reliably estimated and depends on the number of farm owners with qualified agricultural property and when they die; the value of the qualifying agricultural property; the value of other assets held by the decedent; the amount Maryland any estates taxes owed; and the number of qualified recipients who opt to participate in a tax deferral program. The potential revenue loss is expected to be relatively minor compared to overall estate tax revenue collections.

Revenues will increase in the years that any deferred payments are paid back, which will presumably begin in fiscal 2014.

Two factors serve to potentially mitigate the effect of the bill on estate tax revenues. While not specifically exempted from the calculation of gross estate value, land subject to an agricultural preservation easement would not be subject to the estate tax if the value of the total estate is less than \$1.0 million. In addition, to the extent that all the property in an estate is passed directly to the surviving spouse of the decedent, the “marital deduction” allowed under the federal estate tax would reduce the taxable estate to zero, so there would be no federal estate tax and therefore no Maryland estate tax.

**Small Business Effect:** According to the U.S. Department of Agriculture, there are approximately 12,830 farm operations in Maryland covering approximately 2.05 million acres. Recent data from the Maryland Agricultural Land Preservation Foundation indicates that fair market value for farmland in the State ranges from \$3,900 to \$14,000 per acre, depending on the county.

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## Additional Information

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Comptroller of Maryland, State Department of Assessments and Taxation, Maryland Department of Agriculture, Department of Legislative Services

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