DEPARTMENT OF TAXATION
2012 Fiscal Impact Statement

1. Patron J. Randall Minchew

2. Bill Number HB 908

House of Origin:
X **Introduced**
_____ **Substitute**
_____ **Engrossed**

Second House:
_____ **In Committee**
_____ **Substitute**
_____ **Enrolled**

3. Committee House Finance

4. Title Land Preservation Tax Credit; application for credits prior to any donation

5. Summary/Purpose:

This bill would remove the requirement that the taxpayer complete the conveyance of a donation in land or land interest prior to applying for Land Preservation Tax Credits. Rather, taxpayers would be permitted to apply for conditional issuance of Land Preservation Tax Credits prior to the donation of land or an interest in land. This bill would provide that the Tax Commissioner may provide written notice to the taxpayer within 30 days after such application is filed that he has determined that a second qualified appraisal is warranted for purposes of determining the fair market value of the donation. If such notice is not provided, this bill would require that the Tax Commissioner conditionally issue any tax credits within 120 days of a complete application for tax credits. If a second qualified appraisal is prepared, the Tax Commissioner would be required to conditionally issue any tax credits within 180 days of notifying the donor, unless the donor has filed an appeal. The application would not be deemed complete until the fair market value of the donation is finally determined by the Tax Commissioner.

The Tax Commissioner's final determination would be required to conditionally issue the tax credits requested in whole or in part or deny the application for tax credits. If the Tax Commissioner denies any portion of the tax credits requested by the taxpayer, he would be required to include in the determination a finding of facts and the specific reasons for the denial.

Upon receipt of a final written determination from the Tax Commissioner, the taxpayer would be permitted to complete the conveyance of the proposed donation. After completion of the conveyance, the taxpayer would be required to provide the Department with certified copies from the appropriate circuit court of the recorded deeds and instruments conveying the donation described in the taxpayer's application. The Department would be required to provide the taxpayer with written certification issuing the tax credits that were conditionally issued within 20 days of receipt of such copies.

If the conveyance of land or interest in land does not conform to the donation included in the taxpayer's application for tax credits, the Department would not be required to issue tax credits. The taxpayer would be deemed to have forfeited any tax credits conditionally issued by the Tax Commissioner if the conveyance of the proposed donation has not been completed within the 120 days immediately following the Department's final written determination to the taxpayer. Such forfeiture would not preclude the taxpayer from applying for tax credits relating to the same proposed donation at a later date. The annual credit cap would then be increased by the amount of conditionally issued credits that are subsequently disallowed or invalidated by the Department or forfeited by the taxpayer.

This bill would change the rule for real property that was partitioned from or part of another parcel of land, any portion of which was previously allowed a Land Preservation Tax Credit. Under this bill, DCR certification would be required if the other parcel was allowed a Land Preservation Tax Credit within three years of the application for tax credits for the current donation, rather than within three years of the donation.

This bill would provide that the fair market value of any donation for which the Department has issued tax credits would not be subject to dispute except upon a showing of fraud or the misrepresentation of a material fact.

This bill would be effective for completed applications made on or after January 1, 2013.

6. **Budget amendment necessary:** No.

7. **Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

7a. Expenditure Impact:

Fiscal Year	*Dollars*	*Positions*	*Fund*
2011-12	$0	0	GF
2012-13	$501,100	1	NGF
2012-13	($501,100)	0	VLCF
2013-14	$500,008	1	NGF
2013-14	($500,008)	0	VLCF
2014-15	$501,664	1	NGF
2014-15	($501,664)	0	VLCF
2015-16	$503,370	1	NGF
2015-16	($503,370)	0	VLCF
2016-17	$505,127	1	NGF
2016-17	($505,127)	0	VLCF
2017-18	$506,937	1	NGF
2017-18	($506,937)	0	VLCF

8. **Fiscal implications:**

<u>Administrative Costs</u>

This bill would have an annual cost of approximately $500,000 in non-General Fund revenues. Because the Department would essentially be prohibited from auditing the fair market value of tax credits that are conditionally issued, the Department would be required to pay professional appraisers to review all applications for conditional issuances. The Department would also be required to request second appraisals for a higher percentage of applications than currently requested.

This estimate is based on the assumption that approximately 40 percent of applicants would take advantage of the conditional issuance process. If the number of conditional applications is higher, then the costs would be greater. This estimate would also vary depending on the complexity of the particular conveyance subject to review or appraisal. For purposes of this estimate, the Department assumed an average review cost of $2,400 and an average appraisal cost of $10,000. However, some appraisals would likely be more time-consuming and, therefore, more costly.

This bill would require the Department to process Land Preservation Tax Credit applications twice – once when an initial application is filed and again when a taxpayer submits evidence that the conveyance has been made. Accordingly, the expenditure impact estimate in Line 7 includes the cost of hiring one full-time employee to review, verify, and process credit applications. The addition of one employee would be particularly important during high volume times, when the majority of taxpayers submit Land Preservation Tax Credit applications.

The costs of this bill would be funded from the portion of the two percent Land Preservation Tax Credit transfer fee that may be used to cover the costs of administering the Land Preservation Tax Credit. Although this would not have a General Fund revenue impact, increasing the amount of the fee that is used for administration costs could potentially decrease the amount of funds transferred to the Virginia Land Conservation Fund. As a result, less funding may be available for the conservation agencies and organizations that currently receive distributions from the fund.

<u>Revenue Impact</u>

This bill would have no revenue impact.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: Yes.

To ensure that DCR reviews all credit applications that exceed $1 million or that are subject to the rules for partitioned land, the Department recommends the following technical amendments:

Line 113, after issued
Insert: or conditionally issued

Line 134, after issued
Insert: or conditionally issued

To ensure that the Department is able to provide the taxpayer with a written certification within the statutory deadline, the Department proposes the following technical amendment:

Line 186, after within
Delete: 20
Insert: 60

11. Other comments:

Current Law

The Land Preservation Tax Credit is equal to forty percent of the fair market value of land or interest in land located in Virginia which is conveyed for the purpose of agricultural and forestal use, open space, natural resource, and/or biodiversity conservation, or land, agricultural, watershed and/or historic preservation, as an unconditional donation by the taxpayer to a public or private conservation agency.

Beginning in calendar year 2007, the aggregate amount of Land Preservation Tax Credits that may be issued in any one year is subject to a cap. For 2007, the cap amount was $100 million. Since calendar year 2008, the $100 million cap has been increased annually. For 2012, the cap is $111,054,000.

Pursuant to legislation passed during the 2012 General Assembly session, this credit cap must be increased by the amount of any credits previously issued but subsequently disallowed or invalidated by the Department. Such invalidated or disallowed credits must then be reissued in a subsequent calendar year.

The fair market value of qualified donations must be determined and substantiated by a qualified appraisal prepared by a qualified appraiser who is licensed in Virginia. Each appraisal must employ proper methodology and be appropriately supported by market evidence. As required by law, the Department has published guidelines for qualified appraisals that incorporate requirements under IRC § 170(h) and the Uniform Standards of Professional Appraisal Practice (USPAP). Among other requirements, USPAP and proposed federal regulations require that the appraisal be made within 60 days before the date of contribution.

To qualify for a tax credit, the qualified appraisal must be signed by the qualified appraiser and a copy of the appraisal must be submitted to the Department. Any appraisal that, upon audit by the Department, is determined to be false or fraudulent, may be disregarded by the Department in determining the fair market value of the property.

If the real property that is the subject of the donation was partitioned from or part of another parcel of land and any other portion of such parcel, or any land partitioned from such parcel of land, has been allowed a Land Preservation Tax Credit, or an application is pending for a Land Preservation Tax Credit, within three years of such donation and the tax credit that would otherwise be allowed to the donor is at least $250,000, the conservation value must be verified by the Director of the Department of Conservation and Recreation (“DCR”). The Director must act on applications within 90 days of receipt of a complete application and must notify the taxpayer and the Department of Taxation of his action.

To receive a Land Preservation Tax Credits, taxpayers must apply after completing the donation by submitting forms prescribed by the Department in consultation with DCR. Credits must be issued in the order that each complete application is received. If more than one application is received at the same time, the credits with respect to those applications must be issued in the order that the conveyances were recorded in the appropriate Virginia circuit court. If a credit requires verification of the conservation value by DCR and such verification has not been received at the time the aggregate cap is reached for the calendar year, the credit shall be issued in the calendar year that the conservation value of the credit is verified.

During the 2012 session, the General Assembly passed legislation that clarifies that, if within 30 days after an application for tax credits has been filed the Tax Commissioner provides written notice to the donor that the preparation of a second qualified appraisal is warranted, the application is not be deemed complete until the fair market value of the donation has been finally determined by the Tax Commissioner. The Tax Commissioner is required to make a final determination within 180 days of notifying the donor, unless the donor files an appeal. The donor has the right to appeal any decision in accordance with the Department's standard appeal process. Although the Department does occasionally request a second appraisal before issuing credits, in most cases the additional appraisal is requested in the course of an audit, administrative appeal, or litigation after the credit has been issued.

Proposal

This bill would remove the requirement that the taxpayer complete the conveyance of a donation in land or land interest prior to applying for Land Preservation Tax Credits. Rather, taxpayers would be permitted to apply for conditional issuance of Land Preservation Tax Credits prior to the donation of land or an interest in land.

This bill would provide that, for each application for which the taxpayer has elected to apply before conveying the donation, the Tax Commissioner may determine if the requirements have been met and review the reasonableness of the fair market value ascribed to the donation. Within 30 days after an application has been filed, this bill would provide that the Tax Commissioner may provide written notice to the taxpayer that he has determined that the preparation of a second qualified appraisal is warranted for purposes of determining the fair market value of the donation. If such notice is not provided, this bill would require that the Tax Commissioner conditionally issue any tax credits within 120 days of a complete application for tax credits. If a second qualified appraisal is prepared, the Tax Commissioner would be required to conditionally issue any tax credits within 180 days of notifying the donor, unless the donor has filed an appeal. The application would not be deemed complete until the fair market value of the donation is finally determined by the Tax Commissioner.

The Tax Commissioner's final determination would be required to conditionally issue the tax credits requested in whole or in part or deny the application for tax credits. If the Tax Commissioner conditionally issues the tax credits requested, in whole or in part, the Tax Commissioner would be required to include in the determination the total dollar amount of tax credits conditionally issued. If the Tax Commissioner denies any portion of the tax credits requested by the taxpayer, he would be required to include in the determination a finding of facts and the specific reasons for the denial.

Upon receipt of a final written determination from the Tax Commissioner, the taxpayer may complete the conveyance of the proposed donation. After completion of the conveyance, the taxpayer would be required to provide the Department with certified copies from the appropriate circuit court of the recorded deeds and instruments conveying the donation described in the taxpayer's application. The Department would be required to provide the taxpayer with written certification issuing the tax credits that were conditionally issued within 20 days of receipt of such copies.

If the conveyance of land or interest in land does not conform to the donation included in the taxpayer's application for tax credits, the Department would not be required to issue tax credits. The taxpayer would be deemed to have forfeited any tax credits conditionally issued by the Tax Commissioner if the conveyance of the proposed donation has not been completed within the 120 days immediately following the Department's final written determination to the taxpayer. Such forfeiture would not preclude the taxpayer from applying for tax credits relating to the same proposed donation at a later date.

This bill would increase the annual credit cap by the amount of conditionally issued credits that are subsequently disallowed or invalidated by the Department or forfeited by the taxpayer, in addition to the amount of credits previously issued but subsequently disallowed or invalidated.

Allowing 120 days from the date of determination to convey the land or interest in land could present problems for taxpayers. Because qualified appraisals must comply with USPAP, the provisions of IRC § 170(h), and the applicable federal regulations, appraisals must be completed within 60 days before a conveyance is made. Accordingly, a taxpayer that applies for a conditional issuance would be required to convey the property within 60 days of the date of appraisal, which is significantly less than the time period for approval of conditional issuance applications and the 120-day period for making a conveyance. In effect, this bill would require that the taxpayer make a conveyance within 60 days or less of the date of application, even if the taxpayer has not received approval from the Tax Commissioner and even if the 120-day period for making a conveyance has not yet passed. A taxpayer may need to obtain a second appraisal after the Department's conditional approval in order to comply with federal requirements for a charitable donation.

This bill would change the rule for real property that was partitioned from or part of another parcel of land, any portion of which was previously allowed a Land Preservation Tax Credit. Under this bill, DCR certification would be required if the other parcel was allowed a Land Preservation Tax Credit within three years of the application for tax credits for the current donation, rather than within three years of the donation.

This bill would provide that the fair market value of any donation for which the Department has issued tax credits would not be subject to dispute except upon a showing of fraud or the misrepresentation of a material fact. This provision would severely limit the Department's ability to audit Land Preservation Tax Credits, which could lead to potential abuse. Because appraisals are based on the opinion of the appraisers as to the value of the property, rather than concrete facts, it is extremely difficult to prove fraud or misrepresentation. Although this bill would allow the Department an opportunity to review appraisals prior to approving credits, the 120-day time period set forth in this bill is not sufficient to undergo an in-depth appraisal process, especially if the Department must scrutinize each application up front.

This bill would be effective for completed applications made on or after January 1, 2013.

Similar Legislation

House Bill 336 would exclude federal government entities from the list of donees entitled to receive a portion of the Land Preservation Tax Credit transfer fee.

House Bill 1268 would extend the $50,000 limitation on the amount of land Preservation Tax Credits that may be claimed annually through Taxable Year 2012.

Senate Bill 352 would allow the executor or administrator of an estate or the trustee of a revocable living trust to transfer Land Preservation Tax Credits on behalf of a deceased taxpayer.

Senate Bill 355 would require the Department to annually publish certain information about Land Preservation Tax Credits.

Senate Bill 403 would increase the amount of the Land Preservation Tax Credit for working farmers.

cc : Secretary of Finance

Date: 1/26/2012 KLC
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