

DEPARTMENT OF TAXATION

2016 Fiscal Impact Statement

1. **Patron** Michael J. Weibert

3. **Committee** House Finance

4. **Title** Income Tax; Application for Land
Preservation Tax Credits Prior to the
Completion of a Conveyance

2. **Bill Number** HB 1385

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would eliminate the requirement that a taxpayer complete the conveyance of a donation of land or an interest in land prior to applying for Land Preservation Tax Credits. Rather, this bill would permit taxpayers to apply for a reserved amount of credits for subsequent issuance prior to the donation of land or an interest in land. Once an application is filed, the Department of Taxation ("the Department") would have 30 days to determine whether a second qualified appraisal is necessary. If a second qualified appraisal is not required, any credits would be required to be issued, or reserved, within 120 days of receiving a complete application for credits. If a second qualified appraisal is required, the Department would have 180 days to complete an appraisal and notify the taxpayer of the amount of credits reserved.

Once an amount of credits is reserved, the taxpayer would have 120 days to convey the donated land or interest in land. Upon conveyance of the proposed donation, the taxpayer would have an unspecified amount of time to provide the Department with documentation of transfer. Within 60 days of receiving such copies, the Department would be required to provide the taxpayer with written certification issuing the reserved amount of credits. 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, the taxpayer would be deemed to have forfeited any credits that were reserved. However, such forfeiture would not preclude the taxpayer from applying for credits relating to the same proposed donation at a later date. This bill would then increase the annual credit cap by the amount of reserved credits that are subsequently disallowed or invalidated by the Department or forfeited by the taxpayer.

This bill would provide that the fair market value of any donation for which the Department has issued 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 for Land Preservation Tax Credits made on or after January 1, 2017.

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

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

7a. Expenditure Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2015-16	\$0	0	GF
2016-17	\$0	0	GF
2017-18	\$459,500	1	NGF
2017-18	(\$459,500)	0	VLCF
2018-19	\$456,800	1	NGF
2018-19	(\$456,800)	0	VLCF
2019-20	\$456,800	1	NGF
2019-20	(\$456,800)	0	VLCF
2020-21	\$456,800	1	NGF
2020-21	(\$456,800)	0	VLCF
2021-22	\$456,800	1	NGF
2021-22	(\$456,800)	0	VLCF

8. Fiscal implications:

Administrative Costs

This bill would result in the expenditure of non-General Fund revenues of \$459,500 for Fiscal Year 2018, and \$456,800 annually for Fiscal Year 2019 and thereafter. Because the Department would essentially be prohibited from auditing the fair market value of credits that are reserved, the Department would be required to pay professional appraisers to review all applications for reserved credits. 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 process for reserving credits. If the number of applications for reserved credits 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:

- 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 such fund.

Revenue Impact

Because this bill would make procedural modifications to the Land Preservation Tax Credit and would not modify the credit qualification requirements, the annual credit cap, or the limit on the amount of credits a taxpayer may claim each year, this bill would have no General Fund revenue impact.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

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 landowner or taxpayer to a public or private conservation agency eligible to hold such land or interest for conservation purposes. The annual cap amount on the credit is \$75 million. For Taxable Years 2015 and 2016, taxpayers may claim credits of up to \$20,000 per year. For Taxable Years 2017 and thereafter, such limit will increase to \$50,000 per 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 certain requirements used for purposes of the federal charitable deduction, and regulations thereunder, the Uniform Standards of Professional Appraisal Practice ("USPAP"), and the regulations of the Virginia Real Estate Appraisal Board. Among other requirements, federal law and the USPAP require that the appraisal be made within 60 days before the date of the contribution.

To qualify for a credit, the qualified appraisal is required to 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 credit that would otherwise be allowed to the donor is at least \$250,000, the credit may not be issued unless conservation value is verified by the Director of the Department of Conservation and Recreation ("DCR"). The Director is required to act on applications within 90 days of receipt of a complete application and must notify the taxpayer and the Department of his action.

To receive a Land Preservation Tax Credits, taxpayers are required apply for the credit after completing the donation by submitting forms prescribed by the Department in consultation with DCR. Credits are required to 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 is required to be issued in the calendar year that the conservation value of the credit is verified by DCR.

During the 2012 session, the General Assembly passed legislation that clarifies that, if within 30 days after an application for 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 may 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.

Proposed Legislation

This bill would eliminate the requirement that a taxpayer complete the conveyance of a donation of land or an interest in land prior to applying for Land Preservation Tax Credits. Rather, this bill would permit taxpayers to apply for a reserved amount of credits for subsequent issuance prior to the donation of land or an interest in land.

For each application received for credits, regardless of whether the conveyance of a donation has been completed prior to the submission of the application, the Tax Commissioner would be authorized to:

- Determine if the requirements for the credit have been met; and
- Review the reasonableness of the fair market value ascribed to the donation.

Unless the Tax Commissioner provides written notice to the taxpayer that a second qualified appraisal is warranted, any credits would be required to be issued, or reserved, within 120 days of receiving a complete application for credits. Within 30 days after an

application for credits has been filed, the Tax Commissioner would be authorized to 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. No application would be deemed complete until the fair market value of the donation has been finally determined by the Tax Commissioner. If a second qualified appraisal is prepared, any credits would be required to be issued or reserved for subsequent issuance within 180 days of notifying the donor, unless the donor has filed an appeal.

The Tax Commissioner's final determination regarding credits requested by a taxpayer that has not completed the conveyance of a donation, would be required to reserve such credits in whole or in part or deny the application for credits. If the Tax Commissioner reserves the requested credits, in whole or in part, the Tax Commissioner would be required to include in the determination the total dollar amount of the credits reserved for subsequent issuance. If the Tax Commissioner denies any portion of the credits requested, 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 the completion of the conveyance, in order to claim any credits, the taxpayer would be required to provide the Department with certified copies from the appropriate circuit court of Virginia of the recorded deeds and instruments conveying the donation described in the taxpayer's application. Within 60 days of receiving such copies, the Department would be required to provide the taxpayer with written certification issuing the reserved amount of credits

If the conveyance of land or interest in land does not conform to the donation included in the taxpayer's application for credits, the Department would not be required to issue credits to such taxpayer. The taxpayer would be deemed to have forfeited any credits reserved 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. However, such forfeiture would not preclude the taxpayer from applying for credits relating to the same proposed donation at a later date.

This bill would increase the annual credit cap by the amount of reserved 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 the requirements for the federal charitable deduction, and the applicable federal regulations, USPAP, and regulations issued by the Virginia Real Estate Appraisal Board, appraisals must be completed within 60 days before a conveyance is made. Accordingly, a taxpayer that applies for a reserved amount of credits 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 applications for reserved credits 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 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 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 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 would be required to scrutinize each application up front.

This bill would be effective for completed applications for Land Preservation Tax Credits made on or after January 1, 2017.

Similar Bills

Senate Bill 486 would allow the conveyance of a fee interest in real property to a private not-for-profit charitable corporation to qualify for the Land Preservation Tax Credit, even if such organization is not organized and operated for natural resource, land conservation, or historic preservation purposes.

cc : Secretary of Finance

Date: 2/4/2016 MTH
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