

Department of Legislative Services
Maryland General Assembly
2016 Session

FISCAL AND POLICY NOTE
Third Reader

Senate Bill 306

(Senators Madaleno and Middleton)

Budget and Taxation

Ways and Means

Agricultural Land Transfer Tax - Calculation

This bill alters the definition of the agricultural land transfer tax by indicating that the tax does not include the 25% surcharge. In addition, the bill specifies that the “total rate of tax” includes the rate of tax imposed for the agricultural land transfer tax plus the county transfer tax rate, but it does not include a 25% surcharge.

The bill takes effect June 1, 2016.

Fiscal Summary

State Effect: None.

Local Effect: Beginning in FY 2017, local jurisdictions will not have to include the 25% surcharge when calculating the county transfer tax rate limit. As a result, local agricultural land transfer tax revenues will increase by a potentially significant amount. County expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Current Law: Agricultural land transfer taxes are paid by any person or business conveying title to agricultural land that is subject to the tax. Either the buyer or the seller, as determined by the contract of sale, may pay the tax. The tax base is the amount of consideration paid for the property, including the amount of any mortgage or deed of trust assumed by the grantee, less the value of any improvements or any land not subject to the tax. The tax rates assessed are: (1) 5% for transfers of 20 acres or more of agricultural land; (2) 4% for transfers of less than 20 acres assessed for agricultural use or as

unimproved agricultural land; or (3) 3% for transfers of less than 20 acres assessed as improved agricultural land or agricultural land with certain site improvements.

The transfer tax is reduced by 25% for each consecutive full taxable year before the transfer was made if the assessment was based on other than farm or agricultural use. A 25% surcharge is imposed on an instrument of writing transferring title of certain agricultural land. The surcharge does not apply to transfers of agricultural land to a child or grandchild of the owner.

All subdivisions have the authority to impose the agricultural land transfer tax under the rates and limitations set by State law. Unless a greater rate of tax was imposed before July 1, 1979, a county may not impose a county transfer tax on a transfer subject to the agricultural land transfer tax at a rate greater than the county rate applicable to the transfer of improved residential property in that county. If a county has imposed a county transfer tax at a rate that exceeds the rate applicable to the transfer of improved residential property, the total rate of tax that applies to a transfer subject to the agricultural land transfer tax may not exceed 5% plus the rate that applies to improved residential property under the county transfer tax. If the total rate of tax that applies to a transfer subject to the agricultural land transfer tax exceeds the maximum rate allowed the tax that applies to the transfer is payable at the rate specified for the agricultural land transfer tax; and the rate of the county transfer tax must be reduced as necessary to comply with the 5% limit.

Background: In preparation to construct an elementary school, the Montgomery County Board of Education condemned the Phillips' farm and paid the family an agreed amount of \$4,142,500 in compensation. From this amount, the county board deducted \$289,760 in taxes, including \$165,528 for the State agricultural land transfer tax plus 25%, or \$41,382, in the State surcharge, and \$82,850 for the county farmland transfer tax. The taxes reduced the Phillips' net from the sale to \$3,852,740. In March 2013, the Phillips sued to recover the \$41,382 surcharge from the county, contending that the surcharge must be included in county farmland transfer tax and not in addition to that assessment. The Maryland Tax Court affirmed the county's denial of the plaintiffs' request for the refund, holding the surcharge was collected in addition to the transfer tax. The plaintiffs appealed the decision to the Montgomery County Circuit Court, which reversed the tax court and awarded the plaintiffs the surcharge payment plus interest from the date of payment by the plaintiffs to the date of return. In turn, the county sought review by the Court of Special Appeals, which certified the case to the Court of Appeals to determine whether the State surcharge is part of the total rate of tax that applies to the agricultural land transfer tax.

The county maintained that the State surcharge was a component of the State tax that was not included in the State agricultural land transfer tax rate, and, accordingly, the county farmland transfer tax was not reduced or otherwise affected by the amount of the State surcharge. The plaintiffs meanwhile argued that the plain language of §13-407(a)(2) and (3) of the Tax-Property Article and the relevant county ordinance provided that a 6% tax

ceiling applied to the total rate of tax, including the State surcharge, which was, by definition, a part of the State agricultural land transfer tax. Therefore, according to the plaintiffs, the county was required to reduce its farmland transfer tax in light of the State agricultural land transfer tax, including the State surcharge, so that the total transfer tax did not exceed the cap.

The Court of Appeals held that, as used under § 13-407(a)(2) and (3), the phrase “total rate of tax that applies to a transfer subject to the agricultural land transfer tax” includes the State surcharge imposed under § 13-303(d). The court found that, by the plain language of § 13- 407(a)(2) and (3), the county farmland transfer tax is subject to and limited by the tax ceiling set forth in § 13- 407(a)(3), which clearly states that if the “total rate of tax that applies to a transfer exceeds” the tax ceiling set forth in § 13-407(a)(2) – which, for Montgomery County, is 6% (5% plus the rate that applies to improved residential property in the County, or 1%) – the county must reduce its farmland transfer tax “as necessary to comply with the” tax ceiling. As specifically provided in § 13-407(a)(2) and (3), the tax ceiling includes “the total rate of tax that applies to a transfer[.]” The total rate of tax is easily determined through a simple mathematical calculation, *i.e.* dividing the total agricultural land transfer tax by the value of the agricultural portion of the land. Nothing in § 13-407 provides, explicitly or implicitly, that the tax ceiling is limited to the portion of agricultural land transfer taxes that is determined by base tax rates.

Continuing, the court found that the total rate of tax that applied to a transfer subject to the agricultural land transfer tax, as set forth in § 13-407(a)(2) and (3), includes the State surcharge imposed by § 13-303(d). The court opined that the plain language of § 13-301(c)(2) was an expression of the General Assembly’s intent to ensure that the State surcharge is a part of the agricultural land transfer tax and, thus, a part of the tax ceiling set forth in § 13-407(a)(2). The court noted that to adopt the county’s interpretation that the State surcharge is not included in the State agricultural land transfer tax would render nugatory the definition of “agricultural land transfer tax” in § 13-301(c)(2).

Moreover, the court observed that when amending the agricultural land transfer tax statutes in 2008, the General Assembly added the State surcharge as part of the State agricultural land transfer tax but did not modify the tax ceiling. In fact, the court opined that its interpretation of the statute is clearly supported by the legislative history of that 2008 amendment. The court stated that the legislative history demonstrates that the State surcharge is to be collected and distributed directly to the State and makes no mention whatsoever that the State surcharge is somehow exempt from the tax ceiling on the “total rate of tax” under § 13-407(a)(2). The court noted that the General Assembly declined to modify or otherwise raise the tax ceiling on the combined State agricultural land transfer tax and county agricultural land transfer tax that may be imposed. Absent any indication in the statutory language or the legislative history that the General Assembly did not intend the State surcharge to be a part of the State agricultural land transfer tax, the court rejected such a strained interpretation of the relevant statutes.

Concluding, the court held that the State surcharge is, by definition, a part of the State agricultural land transfer tax and must be calculated into, and treated as a part of, the tax ceiling limiting a county's agricultural land transfer tax. Consequently, the plaintiffs were entitled to a refund in the amount of \$41,468 (the overcharge of the county farmland transfer tax) plus interest. Accordingly, the Court of Appeals remanded the case to the Court of Special Appeals with instructions to affirm the judgment of the circuit court.

Judge Harrell, with whom Judge Green joined, dissented. The dissent maintained that the statutory scheme in question was ambiguous and resort to legislative history was both necessary and dispositive. The dissent noted that absent from the legislative history was any indication that the imposition of the surcharge, even with the tax ceiling, was intended to be a part of the tax rate. Consequently, the dissent argued that the majority's construction improperly resulted in a refund due to the Phillips from the county. The dissent opined the judgment of the circuit court should have been reversed and the case remanded to the circuit court for entry of a judgment affirming the Tax Court's decision.

Local Fiscal Effect: This bill will have the effect of reversing the recent ruling of the Court of Special Appeals and codifying the agricultural land transfer tax collection process of Montgomery County. Beginning in fiscal 2017, local jurisdictions will not have to include the 25% surcharge when calculating the county transfer tax rate limit. As a result, local agricultural land transfer tax revenues will increase by a potentially significant amount.

Additional Information

Prior Introductions: None.

Cross File: HB 833 (Delegate Ebersole, *et al.*) – Ways and Means.

Information Source(s): Maryland Association of Counties, Judiciary (Administrative Office of the Courts), Maryland Department of Agriculture, State Department of Assessments and Taxation, Department of Legislative Services

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