



MARYLAND
AGRICULTURAL
LAND PRESERVATION
FOUNDATION



MARYLAND AGRICULTURAL LAND PRESERVATION FOUNDATION
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Installment
Purchase
Agreements

2008

*Purchase
of Easements
Using
Installment
Purchase
Agreements*

Overview

The Maryland Agricultural Land Preservation Foundation (MALPF) was established by the Maryland General Assembly in 1977 and is part of the Maryland Department of Agriculture. The Foundation purchases agricultural land preservation easements that forever restrict development on prime farmland and woodland. MALPF settled on its first purchased easement in 1980.

By the end of the 2007 fiscal year, MALPF had helped landowners permanently protect from development 265,691 acres on 1,933 farms. The Foundation has preserved farmland in all of Maryland's 23 counties.

MALPF's program is one of the most successful of its kind in the country. The State of Maryland, with the work of the Foundation and its state and local partners, has preserved in perpetuity more agricultural land (approaching 500,000 acres) than any other state.

The Maryland Agricultural and Resource-Based Industry Development Corporation (MARBIDCO) was created by the State in 2004 to help finance rural business development activities and lend support to farmland conservation programs. MALPF and MARBIDCO are working cooperatively to develop and offer the installment purchase agreement program (IPA).

Easement Purchase Program

MALPF offers sellers of easements three payment options:

- A lump-sum payment at closing
- Equal installment payments from two to 10 years, or
- An installment purchase agreement.

Installment Purchase Agreements

A Maryland Agricultural Land Preservation Foundation IPA is a contract between MARBIDCO (MALPF's conduit partner) and the seller of an easement. The IPA is comprised of two parts. First, the easement seller will receive the payment of the principal (the amount of the offer or the unpaid balance left at settlement) at the end of the period of the agreement. Second, the easement seller will receive tax-exempt semi-annual interest payments during the period of the agreement.

MALPF, through MARBIDCO, will offer IPAs in \$100,000+ denominations as desired by the easement seller at increments of five years from 10 to 30 years. In other words, each \$100,000+ IPA could be for a period of 10, 15, 20, 25 or 30 years.



Maryland
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Interest Payments on IPA

The interest rate will be set at closing for each IPA, and will remain the same for the term of the IPA. The rate will be based on market rates at closing. See <http://www.marbid-co.org/land/ipas.html> for a calculation of interest at today's rates. MARBIDCO will make payments directly to easement sellers through a paying agent.

Timing of Purchases

MALPF accepts applications for sale of easements no later than July 1 of each year. Applications are ranked by each county using a formula that emphasizes the quality of the property. Appraisals are conducted on properties approved by each county. Sellers have 30 days to accept MALPF's offers. Closing will occur as soon as possible after acceptance.

Closing on Purchases

At closing, a landowner signs and gives to MALPF a deed of easement. This easement binds the seller and anyone else who owns or uses the land from ever developing it for anything but agricultural use. The easement is binding at closing and the easement is owned by MALPF in perpetuity.

Cost of an IPA

All program costs, aside from the cost to sell an IPA and any survey that may be required, are borne by MALPF and MARBIDCO. MALPF strongly urges each seller to hire and consult with an accountant, tax attorney or financial advisor who can assist in assessing how an IPA affects his/her financial situation.

Selling an IPA

Each IPA contains a restriction on transfers of the IPA, except to settle an estate. However, after one year, an IPA can be freely transferred to heirs or sold to investors. In the past, sellers of IPAs in the secondary market have assigned the right to receive IPA payments to a trustee bank, which issued certificates of participation that are sold to investors. Sellers must make all arrangements and pay all costs connected with such a sale.

Selling the Land

The IPA has no effect on property ownership. The deed-restricted property can be sold at any time, subject to the terms of the deed of the easement. If the property is sold, the seller will continue to receive interest on and principal of the IPA until the purchase price is paid.

Benefits to Sellers of IPAs

Capital Gains Tax Deferral: IPAs are structured under Section 453 of the Internal Revenue Code to defer capital gains, and capital gains taxes, until the principal payment is made at the end of the IPA term, up to 30 years later.

Tax-Exempt Interest Payments: In the opinion of bond counsel, the semi-annual interest payments received under an IPA will be exempt from federal income taxes. These payments can provide sellers with tax-exempt income over the term of the IPA on the full value of the easement, not just the portion remaining after paying capital gains taxes.

Charitable Contributions: If a "qualified farmer," one who derives more than 50 percent of his/her income from farming, sells an easement for less than appraised value, he/she may be able to deduct the discount up to 100 percent of income in the year of sale, and use any remaining deduction over the following 15 years.

Flexibility for Estate Planning: IPAs can provide an attractive financial instrument to help in estate planning. If the IPAs pass through an estate, the estate taxes can reduce the ultimate capital gains. Farmers with multiple heirs can divide the sale price of the easement into as many IPAs (greater than \$100,000) as desired.

Questions to Consider

A landowner considering selling an easement through an IPA should consider the following questions:

- In what name (personal, joint, trust, partnership, corporation) is the property held?
- What was paid for the land, or what was it worth when it was inherited?
- How much debt does the land secure, and will the lender subordinate its mortgage to the deed of easement?
- How much of the basis in the land should be allocated to the easement?
- In what tax bracket are you, and will you be when you receive payments for the easement?
- If you are selling your easement for less than its fair market value and you are a qualified farmer, what is the value of the charitable contribution over the next 15 years?
- What will the estate tax liability of your heirs be, and how will they pay it?

Applying to a County Program

The landowner who receives an offer from MALPF may choose to go to settlement using the county IPA program where the property is located, if the county has a program and agrees, under legislative authority provided by HB 625 (2004). MALPF will provide a grant to the county of the State's share of the easement offer, and the county will be responsible for the principal of and interest on its IPA. The acquired easement will have MALPF as the primary co-holder with the county as the secondary co-holder of the easement.

Additional Information

Applications and additional information regarding MALPF's acquisitions of easements using installment purchase agreements may be obtained from your county's farmland preservation program administrator. See: <http://www.malpf.info/PAcontact.html>

Each person considering selling development rights under this program must rely on advice from his/her own tax or financial advisor to evaluate the possible financial benefits of this transaction in light of individual circumstances, and to advise on IRS treatment of IPAs.

