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Guiding Growth: A Survey of Tax Incentives

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GUIDING GROWTH: A SURVEY OF TAX INCENTIVES

New England Environmental Finance Center
January 2003

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EXECUTIVE SUMMARY

This report was prepared during the summer and fall of 2002 under the terms of an agreement with the Maine State Planning Office, and in accordance with a cooperative agreement between the Muskie School of Public Service in Portland, Maine, and EPA Region 1 Headquarters in Boston, Massachusetts. The agreement calls for an inventory of current taxation systems or fees employed by other states to help direct growth away from sensitive natural resources and rural areas towards designated or traditional growth areas[1]. This report surveys various, proposed and implemented statewide taxation systems and fees. Finally, a number alternative taxation systems and fees that might be appropriate for the State of Maine are presented.

Currently the State of Maine has implemented a few tax provisions to encourage conservation of farmland, open spaces, and forestland. These mechanisms provide property tax reduction to property owners in exchange for providing a benefit to the public (e.g., conservation of scenic views, enhancement of public recreational opportunities, and the preservation of natural resources and wildlife).

Despite these current tax provisions however, Maine is experiencing accelerated development of rural and natural sensitive areas. The growth mostly consists of large residential homes along or near shorelines or homes in secluded wooded areas. In the short-term, these developments increase a municipality's taxable base, on which it is highly dependent in order to continue its public services. However, in the long run, the municipality faces an increased burden on its budget due to its obligation to extend some of its public services (e.g., fire, police, and school transportation) to all residences, regardless of their location. Allowing development in rural areas and in or near natural sensitive areas may not only permanently harm Maine's natural resources, but also threaten the financial viability of municipalities. In addition, protecting natural resources from further development is also crucial for communities that are highly dependent upon them (e.g., fishing, forestry and tourism industries).

This report reviews tax mechanisms and fee structures that are employed or have been proposed in other states. These systems and fees may assist Maine in the search for an equitable and efficient tax system to protect its natural resources while supporting sustainable development efforts of local communities. However, the effectiveness of the recommended tax systems is very dependent on the rate of the tax and the economic conditions of the region or municipality.

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[1] Terms of agreement;

- identify current taxation and systems or fees employed by other states to help direct growth away from sensitive natural resources and rural areas toward designated or traditional growth areas;
- explore and formulate a number of alternative taxation systems and fees that might be appropriate for Maine.

INTRODUCTION

Current development patterns and increased tax pressures in local municipalities combine to harm both Maine's natural resources and its quality of life. Previous initiatives such as the implementation of zoning laws did not fully result in the desired outcomes. Zoning laws were often too flexible and often did not resist market and political pressures to change zoning regulations to allow development with possible economic growth. A sound taxation system or fee structure may be the solution to slow down development in natural areas and direct it towards areas appropriate for growth.

To protect Maine's natural resources more successfully from future development, more cooperation from current and future landowners as well as developers is needed. In today's society, there is the desire among many to own a home surrounded by natural beauty and away from urbanization. This life-style causes many valuable acres to be consumed for low-density development. Despite the visible harm to the environment, the demand for low-density development in natural areas continues and shows no signs of slowing, partly due to flexible development regulations at the local level. Besides environmental harm, new development, especially in rural areas, creates externalities for the community at large. Externalities such as increased demand on public services have often been overlooked or ignored in the planning process. This causes the actual costs of the development to be considerably higher than municipalities initially assumed. To recover the actual costs of new development, economic incentives or disincentives may be applied, which either recover the true costs or simply discourage development in rural areas.

This report will present taxation systems employed or proposed in other states that focus on discouragement of development in natural and rural areas. By adjusting prices of development through the tax code, government has the ability to cause its citizens to reconsider decisions which in general are hard to regulate for local authorities. The presented taxation system or fee structures have the ability to influence the decision-making process, and might be suitable for the effort to conserve Maine's rural landscapes and natural resources.

It is important to recognize that the selected taxation system or fee structure should be considered a part of a comprehensive approach that, besides development patterns and environmental issues, addresses economic and social conditions of the various regions in the State of Maine. A long-term multidisciplinary approach integrating environmental, economical and social interest should, in order to optimize results, be developed to fit the needs and concerns of communities, businesses, and government.

I. SURVEY OF TAXES AND FEES IN USE

1.1 Current use tax

Among the first widely implemented land tax programs was the current use tax. This property tax relief program was initiated to protect farmers from rising land values in urbanized areas. Today, all states provide property tax relief for owners of agricultural land (Dempsey, 2001). Over time this property tax relief program, also called differential or deferred taxation, has included other parcels of land a community wishes to protect e.g. open spaces, wetlands, and forestlands. To qualify for the program parcels must meet specific requirements. For example, in Maine, parcels on which farming or agricultural activities have produced a gross income of at least $2,000 per year in 1 of the 2, or 3 of the 5 years preceding the date of application to the tax program would qualify. In New Hampshire, the parcels must be at least 10 acres. In Vermont, agricultural and forestland must be at least 25 acres, the forestland must be managed under a 10-year forest management plan...etc. Most states have built-in safety nets to recapture lost property tax revenue when land within the current use program is sold or developed. In these instances, a significant tax penalty is imposed for the back taxes that are owed. The penalty is based on the fair market value of the land while under current use status. Depending on the state, taxes may be owed as far back as 10 years.

A direct short-term advantage of providing a property tax relief to property owners is that many acres of farmland, open spaces, and other sensitive natural areas will remain undeveloped. However, the program does not eliminate the chance for land speculation. For example, the tax relief lowers the costs of holding land for speculators, who may qualify for the program by arranging for their land to be farmed by leasing it to local farmers. When the time is right these landowners, the speculators, will sell the land for development and pay the tax penalty, “which is not significant to a major development” (Stokes, Watson, 1994). Also, municipalities are losing property tax revenue because of the number of parcels that qualify for the property tax relief. “Realistically, not all parcels are threatened by development, especially those located far from large cities and in very rural areas” (Bauman, Durning, 1998). Therefore, adjustment of current use tax rates in rural areas, which are unlikely to be threatened by development, might be appropriate to provide more tax revenue to municipalities. Those in remote areas who feel threatened and/or wish to preserve the land may reduce their tax burden with conservation easements.[2]

1.2 Land Value Taxation

The Land Value Taxation (LVT) approach, also called the split-rate tax, views property tax as two distinct taxes: one on land and one on buildings. Land Value Taxation levies a lower rate on the value of buildings and improvements, and a higher rate on land. As a result, the value created by labor and capital improvements are kept in the private sector.

[2] Conservation easement: a deed restriction landowners voluntarily place on their property to protect resources such as agricultural land, wildlife habitat, wetlands. The landowner authorizes a qualified conservation organization or agency to monitor and enforce restrictions enclosed in the contract.

Also, by taxing land at a correspondingly higher rate, government urges owners who had been speculatively withholding or under-utilizing their land to develop or offer their parcels for development. Hence the land newly available for development spawns from previously used (“recycled”) sites (Nelson, Smith, 1998) - and not from open space. This approach encourages good land use and discourages land speculation.

Generally, the LVT system raises the tax burden on low-intensity users of land and in highly valued land areas (e.g., urbanized areas, and land rich in natural resources). Land-rich, money-poor private property owners suffer with the implementation of the LVT. For those individuals, the policy may include deferments of tax payments. Another option for those property owners is to preserve the land or a part of the land through a conservation easement.

There are countries outside the Unites States (e.g., Estonia, South Africa, New Zealand) and 15 Pennsylvania cities[3], which have implemented the LVT system. All have shown that collecting more of the community-created land value (through taxing the value of the land while lowering the tax on home improvements) is a constructive process for encouraging more efficient land use. As a result of the increased land value and tax pressure, idle lots, under-used buildings, and neighborhoods are turned into productive use. In sum, the LVT encourages more dense development and reduces the pressures of urban sprawl.

In those 15 Pennsylvania cities, 85% of homeowners pay less under the LVT system than they do with the traditional flat-rate approach. For those who pay more it is not significantly more. These people also tend to be wealthier homeowners who can better afford to pay more (Saidel, 2001). In those cities there is a considerable spread between the taxes on the value of land and those on the value of buildings (Appendix A). For example, the small city of Aliquippa taxes the value of land 16 times more heavily than the value of buildings in its property tax calculations. Pittsburgh's tax rate on land is nearly six times the rate of buildings. The Titusville ratio is nearly 9 to 1, while Harrisburg's ratio, which has been 3:1, will soon change to 4:1.

A key strategy for the Pennsylvania cities was to move gradually to the LVT. The guideline was to not shift more than 20% of the taxes from buildings onto land each year for a period of five years, or 10% each year for a period of ten years (Saidel, 2001). This gradual transition, combined with community education, allowed citizens to make the required adjustments.

Owners paying higher land taxes often feel pressured to develop or sell all or a part of their land in order to pay their taxes. In Pennsylvania, there was initial fear that LVT may force premature or excessive development of higher valued lands, including environmentally sensitive areas. However, many came to understand that some development is needed in order to save more precious land.

[3] Pennsylvania cities and their effective split tax rates may be viewed in Appendix A.

The overall intent of the LVT is to promote prosperity, equity, and sustainability (Saidel, 2001). By putting a site to "best use," several benefits are brought to the greater community, e.g., less sprawl and commuter traffic, and an improved quality of life. Because the LVT system is progressive, owners of valuable parcels, i.e. land suitable for development or rich in natural resources, are footing the majority of the bill. They will pay more tax scaled according to the value of the land that they "take" from society.

1.3 Capital Gains Tax on Speculative Land Sales

In 1973 the state of Vermont introduced a tax on capital gain realized on the sales of land held less than six years. The tax is aimed at 1) protecting rural land from short-term land speculations, 2) controlling land prices, and 3) promoting a more efficient use of land (Daniels, Lapping, 1986). The tax ranges from 5% to 80% of the gain and is dependent on the number of years the land has been owned prior to the sale and the increase in land value over time.

The tax only applies to land, not buildings. When buildings are present on the property, an allocation of the sale price between the land and the building(s) must be made. This can be based on an appraisal, or by using allocation guidelines from the Vermont Department of Taxes. The sale of up to ten acres of land that was originally occupied by the seller as a principle residence qualifies for the seller's principal residence exemption. However, the sales of seasonal and or vacation homes held less than six years and sold for a gain create land-gains tax liability on the land's increase in value.

Years Land Held by Transferee	Gain as Percentage of Basis		
	0-99%	100-199%	200% or more
Less than 4 months	60%	70%	80%
4 months, but less than 8	35%	52.5%	70%
8 months, but less than 1 year	30%	45%	60%
1 year, but less than 2	25%	37.5%	50%
2 years, but less than 3	20%	30%	40%
3 years, but less than 4	15%	22.5%	30%
4 years, but less than 5	10%	15%	20%
5 years, but less than 6	5%	7.5%	10%

Source: Vermont Department of Revenue, Property Transfer Booklet. http://www.state.vt.us/tax/PVR%20Booklet.htm - July, 2002.

The primary goal of the tax was to reduce short-term land speculation and subdivision activity, which was mostly created by out-of-state interest. Vermont viewed land speculation as the major cause of subdivision and rural development activities that threatened their natural resources and environmental quality. In addition, land speculations led land prices to increase beyond the ability to pay for many year-around Vermont residents. The capital gains tax on speculative land sales was introduced to collect funds for a property tax relief program for owners of primary residences in Vermont. Daniels and Lapping conducted a study eleven years after the program was initiated and focusing on the impacts of the capital gains tax program. They concluded that the annual number of bare parcels sold had decreased, as well as the average parcel size. The price per acre, however, had increased, indicating a more intense land use. The study also recognized that the tax does not penalize subdividers who hold ownership of the land for longer than six years.

The capital gains tax on speculative land sales generated the following revenues for the State of Vermont.

Year	Tax Revenue (in dollars)
2001	$ 2,010,081
2000	$ 1,729,923
1999	$ 928,743
1998	$ 749,821
1997	$ 1,264,693
1996	$ 826,376

Source: Vermont Department of Revenue,
Division of Property Valuation and Review – November, 2002.

1.4 Live Near Your Work Program

In 1997 the state of Maryland introduced the Live Near Your Work program (LNYW), a partnership between the Department of Housing, the Department of Community Development, local government, and businesses. The program provides a minimum $3,000 grant to employees who purchase an existing home near their place of employment. The grant may be used for closing costs or a down payment on the home, which has to be within the employer's targeted neighborhoods. The direct benefits of the program are geared towards strengthening neighborhoods through increased homeownership and linkage between employers and nearby communities. However, indirect benefits include environmental ones such as slowing down sprawl and reduced commuter traffic.

The grant awards consist of contributions from the employer from the local jurisdiction, and from the State of Maryland. Every citizen of Maryland employed by a participating employer is eligible for the grant. However, the employer may set additional eligibility requirements for their employees. Also, the homebuyer is required to provide matching funds of $1,000 towards the grant awarded. Officially there are no income limits for participation in the program. But state agencies do have the requirement that 51% of participating homebuyers must be families of limited income (annual household income of less than $73,000). Other restrictions include: (1) the LNYW program is only in effect in participating local jurisdictions, (2) the property purchased must become the primary residence of the employee, and (3) the property must be either a single-family dwelling (including a townhouse or condominium), or a two- to four-unit property with the eligible employee occupying one of the units. By accepting the grant, the employee commits to the three-year requirement of living in the property and continues employment with the same company/government agency. Should the employee move or voluntarily terminate employment prior to the three-year requirement**,** the State portion of the grant will be recovered on a pro-rata basis.

While the LNYW program encourages employees to live closer to their work, households with two working adults might find themselves unable to participate in the program, due to employment in different jurisdictions. However, they might decide to move to a participating jurisdiction to enjoy the LNYW benefits while creating a longer commute for the other working household member.

The Department of Housing and Community Development conducted a survey in 2001 among participants of the LNYW program. A total of 427 homebuyers responded, and;

- Roughly 75% (322 homebuyers) were first-time homebuyers;
- 33.5% (143 homebuyers) indicated that they would not have bought their new home without the LNYW incentive;
- 15% (64 homebuyers) switched their means of transportation from driving to walking, cycling or carpooling, and reducing their average commute from 13.5 miles to 1.5 miles;
- Overall, the commuting miles dropped from 10 to 3.4 miles and the commuting time dropped from 25 to 14 minutes.

1.5 Impact Fees

Impact fees are imposed by municipalities or counties on new development, to generate additional revenue to offset expenditures related to the new development. Impact fees are a common tool used to pay for new schools, sewers, roads, parks and other public improvements and amenities. Some view impact fees as a direct form of taxation while others see them as growth deterrents. Impact fees raise funds for expansion while keeping a lid on property taxes. Coupled with zoning restrictions, impact fees have become a tool to dampen growth (Davies, 1997).

Impact fees may put upward pressure on housing costs, possibly causing municipalities that impose the impact fee to become less competitive compared to surrounding municipalities. Therefore, as a growth management tool, an impact fee fails to control sprawl as it pushes development out to municipalities where the fee is not collected (Davies, 1997).

For an impact fee to reflect true costs of development it should include, besides the increased expenses of public services, the economic and environmental costs of increased traffic, storm water run-off, environmental degradation…etc. The calculation of the true costs of development is a complex problem, especially the assessment of environmental costs.

1.6 Job Creation Tax Credit

As a part of Maryland's Smart Growth and Neighborhood Conservation program, the Department of Business and Economic Development initiated the Job Creation Tax Credit program (JCTC) in 1996. The program's goal is to use the state's existing infrastructure more efficiently and minimize the development of rural undeveloped lands for business purposes. To accomplish this, the program encourages mid-sized and smaller businesses to invest in smart growth areas around the state. Small business development and enhanced job growth is especially encouraged in areas easily accessible to available labor pools. There are, however, no specific requirements regarding where employees reside.

The JCTC program provides income tax credits to business owners who create full-time, permanent jobs, and pay at least 150 percent of the minimum federal wage. In order to receive the job creation tax credit, the business entity must create 60 new jobs at the expanding or new facility in a 24-month period. In designated priority funding areas[4], the minimum number of jobs is 25. Outside priority funding areas, the minimum of 60 jobs may be reduced to 30 new jobs if the aggregate payroll for the qualified positions is greater than a threshold amount equal to the product of 60 times the state's average annual salary (currently $2.2 million). The new jobs must be the result of business efforts to establish or expand a business facility, and not through a change in ownership. Also, the positions must be created at one company location in the state.

The credit will be the lesser of $1,000 or $2^{1/2}$% of a year's wages for each new, full-time job calculated on an aggregate basis. If the new or expanded facility is located in a state enterprise zone, a federal empowerment zone or designated neighborhood, then the credit is increased to the lesser of $1,500 or 5% of a year's wages for each new, full-time job. The maximum credit allowed during any credit year for a single facility is $1 million.

However, if during 3 years succeeding the credit years, the average number of qualified positions falls below the applicable threshold number, the state will recapture the credits. If the number of qualified positions falls more than 5%, but not below the applicable threshold number, then the credit is recaptured in proportion to the decline in certified employees. Unused credits may be carried forward for up to five tax years following the year in which the credit could first be used to reduce tax liability. The credit may not be used to reduce taxes owed for earlier years.

In 2000, the program changed into a two-step certification procedure. First, business had to receive precertification – an approval that the business qualifies for the tax credit. Second, final-certification was granted after confirmation that the business met all the requirements to claim the JCTC on their tax return. A company must have created and

[4] Priority funding areas: state enterprise zones, federal empowerment zone, state Department of Housing and Community Development (DHCD) designated neighborhoods, municipalities, areas inside the I-495 and I-695 beltways, or a single growth area designated by each county for the purpose of this credit.

filed for at least one year the threshold number of jobs. The purpose of the two-step procedure is to obtain more information on how long it takes businesses to meet the hiring requirements, and the likelihood that the business will earn the credit and use the credit on their tax return. The JCTC program will terminate by the end of year 2006. This means that jobs created January 1, 2006 will not receive the credit, since a position must be filled for 12 months before the credit may be taken.

From July 2000 until June 2001 the administering Department of Business and Economic Development (DBED) received 34 applications from facilities that were eligible for precertification. These 34 applications represented 6,981 new jobs during the next five years, of which most were scheduled to be created within the next two years. The average annual wage of the new jobs was $53,550. Additionally, DBED received 69 letters from facilities intending to use the credit upon approval of their final-certification requirements. DBED indicated that this was an increase of 21% from the preceding year.

1.7 Tax Shift

Tax shifting moves taxes away from productive activities - e.g., labor and income - and onto activities that should be discouraged - e.g., pollution and resource depletion. It is important to recognize that tax shifting is not about higher or lower taxes. The goal of a tax shift is about using fiscal incentives to promote a change in human behavior. Experiences of tax shifts, mainly in Europe, have demonstrated that tax shifting can be an effective tool to clean up and protect the environment, create jobs, and increase business competitiveness, while maintaining government revenues. In the United States, environmentally sound tax shifts are slowly being implemented on a small scale in various states. For example Minnesota increased its tax on solid waste, Iowa and Vermont removed the tax-exempt status of pesticides and fertilizers. In addition, Vermont introduced a solid and hazardous waste tax. Designing and implementing a tax shift model is not an easy process. It is important that the tax shift occurs slowly and incrementally to provide a smooth transition for those involved: businesses, communities and individuals.

1.8 Regional Tax Sharing

Tax sharing reduces the competitive struggle between municipalities to increase their tax base to fund public services. Regional tax sharing attempts to close the gap between services that citizens expect to receive and local government’s ability to finance those services. If designed favorably, this tax mechanism may support regional planning efforts, e.g., preservation of open spaces and natural resources, and use of existing infrastructure. Although tax sharing does not stop sprawl directly, it creates equity in the provision of public services and can contribute to a reduction in the growth of the overall municipal tax burden.

In 1971, the Minnesota legislature enacted a significant tax-base sharing program. The program pooled 40 percent of the increase in commercial-industrial property valuation of 188 municipalities within the seven counties surrounding the Twin Cities area. The money collected and shared – in 1995 $241 million; 40 % of the region's $603 million increase in property assessment – is distributed to all 188 municipalities, based on their estimated populations and per capita market value of property, compared to the area's average. Those municipalities with a high per capita market value of property receive less money in the tax-sharing program and those with a low market value receive more money. In the early stages of the program, the difference in property valuation between the richest and the poorest towns was 17 to 1; in 1995 this difference has been reduced to 4 to 1. The incremental decrease in the ratio reduced the pressure of sprawl due to the reduced fiscal disparities among towns.

The shortcoming of the Minnesota model is that it uses the increase in property value as the tax base (Huck, 2000). Ideally, tax base sharing should use total property values. Also, the model only shares the growth in commercial and industrial property values. This causes communities with high residential property values and little commercial and industrial base to benefit disproportionately under the Minnesota model. In 1995 there was an attempt to eliminate this shortcoming by adding the sharing of growth-in-value of residential homes worth over $200,000. The Legislature approved the plan but the Minnesota Governor vetoed it.

Minnesota estimates its tax-sharing plan has reduced the economic disparities between its richest and poorest communities from 50-to one to 12-to-one. In addition, it also increased the choices of desirable communities in which to live. Many local municipalities depended so heavily on their property taxes for revenue that they ended competing for development they really did not want. Through tax sharing surrounding municipalities received more revenues to spend as they wished, and reduced the need to accept inappropriate and/or undesired development (NJF, 2000).

In Maine, tax sharing is permitted as well; however, only a few communities have taken advantage of this system that is restricted to industrial or research parks. First Park, a business and technology super-park located in the Kennebec Valley, is a recent example of collaboration between participating surrounding municipalities regarding the sharing of the start-up costs of that park and the tax revenue generated by businesses within the super park.

A similar local example is the Lewiston and Auburn Economic Growth Council, a nonprofit agency, that through partnerships attempts to attract and retain businesses in the Lewiston-Auburn area. The Council seeks to increase the regions tax base and job opportunities by providing companies technical assistance, commercial financing, site searches and marketing services. Increased efficiency and cost savings for both municipalities are among the immediate results of the Council.

1.9 State Income Tax Credit Incentive

Various states - Virginia, Colorado, Connecticut, Delaware, California, South Carolina, Georgia, Maryland, New Jersey and North Carolina - have enacted an income tax credit to provide private landowners with incentives to conserve land and maintain public access. State tax credits apply to land or easement donations to a conservation agency or qualified non-profit organization to help protect the state's prime coastal areas, agricultural and forest lands, wildlife habitat, watersheds, etc. In addition to the direct benefits to the environment and the surrounding community, the program helps private landowners which are rich in land but poor in cash.

Income tax credits are usually capped at a percentage of the fair market value of the land or conservation easement donated. An additional credit may be added if the landowner allows public access. For example, North Carolina enacted its law in 1983; since then, 33,000 acres of land worth $80 million have been protected at a cost of only $3.5 million to the state in the form of tax credits, making the program very cost effective. Many states allow program participants to carry credits from one year to another for a specified number of years. Landowners with restricted incomes who are unable to apply the tax credits against their state income tax liability are allowed to transfer the credit to another taxpayer participating in the program.

The state income tax credit program has proven effective in states that have implemented the policy. There has been an increase in land conservation with minimal administrative costs to the state. Appendix B shows an overview of the tax credit guidelines and computation per state.

II. SURVEY OF SOME PROPOSED TAXES AND FEES

2.1 Maine Toilet Tax

By Maine State Representative David G. Lemoine – 2001

The bill An Act to Create a Sprawl Offset Tax was introduced in an effort to reduce sprawl in Maine. Every toilet connected to septic systems and installed after a specified date would be taxed. The tax rate would be $750 for a toilet connected to a private home and $1,000 in a non-residential property. Toilets connected to septic systems in designated growth areas would be exempt from the tax. The bill was intended to offset the cost to the state of building new septic systems while encouraging growth in towns and cities, where septic systems are already present. Local authorities were allowed to retain 10% of the toilet tax collected revenue to apply towards the cost of collecting the tax, while the remainder would be used for infrastructure improvements and efforts to make housing more affordable for the poor.

2.2 Tax Reform That Agrees With Vermont

By Vermont Fair Tax Coalition

Despite strong conservation efforts, development pressures continue to be high in Vermont, and sprawl is threatening to change Vermont's rural landscape and the vitality of its downtowns. To maintain and attract business back to the traditional downtown areas, the Vermont Fair Tax Coalition (VFTC) proposed to exempt downtowns from Vermont's sales tax to preserve the economic activity in "historic" downtowns.

In its 1999 report the VFTC also highlighted the land value taxation system. The coalition recommends state legislation[5] that would enable cities and towns in Vermont to use land value taxation (based on the Pennsylvania model) in their downtown centers if they choose. Within this system the proportion of the property tax that will be raised from land values and the proportion raised from buildings and improvements should be determined by the cities and towns themselves.

2.3 Review of Oregon's Tax System – Task Force Recommendation to the Tax Code

By Oregon Office of Economic Analysis

In 1999, a report was prepared and presented by a task force comprised of citizens appointed by Governor John Kitzhaber. Their task was to "consider how to increase the stability of Oregon's tax system; how to use it to help people move from dependence on government support to independence; how to encourage workforce training and development; and how to encourage meeting Oregonians' environmental goals." Among the recommendations presented by the task force were environmental provisions including: (1) the modification of pollution control tax credit, which was implemented in 1967 and has not been adjusted to account for significant changes in environmentally friendly development, (2) the establishment of an excise tax on pesticides and fertilizers, and (3) the incorporation of environmental goals into Oregon's revenue system.

The report presents two objectives related to Oregon's environmental goals: 1) effective growth management and 2) creation and maintenance of a sustainable natural environment. The report was critical of the state's current tax policies that did not align with its land use and growth goals. Tax policies that were recommended for review include: 1) current use assessments within designated urban growth areas: the task force believed that this policy inhibits development in areas suitable for high-density development. 2) non-transit oriented development: the task force found that there is little encouragement through the current tax system for (re)development in areas already serviced by public transportation, or extending transportation services to new neighborhoods, including the creation of bike paths and walkways.

The report also included recommendations provided by the Department of Land Conservation and Development, and the Oregon Department of Environmental Quality. One suggestion was that cities should be encouraged to use a property tax differential to support infill and redevelopment within city limits. Secondly, the value of land should be taxed, not the value of improvements. Thirdly, the state should discourage car use within specific urban areas.

[5] In June of 2002 Vermont past legislation to form a study group this Fall that will explore the feasibility of a land value taxation system for Vermont.

2.4 Rhode Island Statewide Planning Program

By State Planning Council Property Tax Subcommittee

In 2001, a property tax subcommittee was formed by Rhode Island Growth Planning Council, appointed by Governor Almond, to develop recommendations to the Growth Planning Council regarding the linkage between property taxes and land use patterns. Efforts of the committee were focussed on issues that could play a role in the relationship between property tax and land use decisions. The following items were discussed:

(1) School funding reform – over-reliance on the property tax to fund schools may be related to urban dis-investment and sprawl issues;
(2) In-depth survey to examine housing and location choices – gather information that could be useful in understanding the role of property taxes in residential housing choices and developing growth management public policies;
(3) Analysis of regional property tax sharing methods – explore methods to reduce property tax bases that currently make municipalities compete for new development, thereby harming rural landscapes and natural resources.
(4) Assist municipalities in revitalizing under-used land and buildings – transfer ownership of vacant and abandoned lots to state or local agencies for affordable housing and/or commercial uses;
(5) Analysis of a uniform assessment practice – identify how the state could develop more uniform assessment and property tax exemption system.

2.5 Minnesota – "Smart Signals – Property Tax Reform for Smart Growth"

Minnesota Planning Environmental Quality Board[6] – MPEQ

In March 2000 the MPEQ Board presented a report that evaluated the influence and impact of fiscal and tax policies on long-term economic, environmental and social interests of the state. In this report the Board proposed Site Value Taxation based on the land value taxation approach, a decrease of tax rates on building values and increase in tax rates on land values. This taxation recognizes that government investments in infrastructure and community services create private wealth in the form of higher land values. The site value taxation recovers this increase in land value from current property owners. The main benefits identified with the use of this taxation program would be increased use of land already serviced by public infrastructure, and improved support for urban redevelopment - including the potential reduction of government subsidies, and public financing for urban renewal projects.

MPEQ recognized that the Site Value Taxation system may not be appropriate for rural areas due to the diversity of land uses, e.g., agriculture, forestry, etc. To accommodate this different implementation strategies could be developed. For example: local (rural) municipalities could continue the current-use taxation approaches for land and buildings that suit unique conditions in their area; and the state could require cities of a certain size

[6] The Minnesota Environmental Quality Board develops policy, long-term plans and reviews proposed projects that influence Minnesota's environment significantly.

or at a particular growth rate to apply site value taxation, due to the state's interest in increased land value capture at the local level.

2.6 New Jersey Future – Smart Growth Credit Plan (SGCP)

New Jersey Future (NJF) and Natural Resource Defense Council (NRDC)

Following a recession in the early nineteen eighties, New Jersey began to enjoy a period of tremendous economic growth and development. Along with the benefits came urban sprawl consuming the New Jersey countryside and shorelines. This unplanned and uncoordinated development caused growth in areas where it did not seem to make sense, for instance in areas without schools, existing sewer systems, or other public services (New Jersey Future, 2001).

To respond to the sprawl pattern, NJF and NRDC designed the Smart Growth Credit Plan for developers and homebuilders. The purpose of the credit plan is encourage more environmentally and economically sustainable development patterns and practices. Developers are encouraged to invest in appropriate or designated growth areas with efficient residential and mixed-use construction projects that minimize land and water impacts. The SGCP is intended to create long-term changes through a short-term incentive program. Therefore, the program is designed to expire after five years of implementation, but to attract a large number of applicants within that time period.

Currently NJF and NRDC are drafting legislation for this plan and are seeking a sponsor to include the proposed legislation in a bill this fall. A detailed outline of the proposed credit plan is available for review and individual use upon request at the NRDC. The outline includes information regarding:

(1) a tax credit of 4% of allowable development costs; including the costs of land for development that meet the criteria provided in the detailed outline;
(2) an additional tax credit of 6% that can be earned by meeting the optional -
    (a) Smart Growth Criteria - which specify the smart growth aspects[7] of what would be required to qualify a development for a tax credit, and/or
    (b) The Green Building Criteria, which specify the green building aspects[8] required to qualify a development for a tax credit.

The above tax credits are purely incentives; they do not prohibit or mandate specific development.

Further, NJF identified a correlation between how municipalities tax their properties and how development occurs. As a result, NJF drafted a bill to amend state legislation to

[7] Smart Growth Criteria include the locations where development would be eligible, and the neighborhood design features that will be required in order to ensure that developments are safer, easier to use for pedestrians and bicyclists, and better served by public transportation.
[8] Green Building Criteria include building design and landscaping techniques that will help minimize the development impacts on human health and the environment, in the short and long term.

address the state's current property taxation system by means of a constitutional convention. Through a statewide election, citizens will be able to select representatives to participate in the convention. During the convention, solutions to fix the state's property tax issues will be created. Once when solutions are created the citizens of NJ will vote again for the most favorable solution. Through voting, legislature puts the power back in the hand of the citizens of New Jersey, who suffered through eight special appointed tax commissions in the last 20 years and failed recommendations.

III. SOME CURRENT PROPOSALS FOR MAINE

This section provides comments and recommendations regarding the taxation systems and incentives programs presented in Part I. The information comments and recommendations are provided by Maine professionals[9] in the field of economics, planning, policy and taxation. Then information was collected through personal interviews and then formatted for this report.

3.1 Current Use Taxation

The current use taxation program in Maine consists of two parts, (1) tree growth, and (2) farmland and open space, it appears from the discussions that tree growth program is the more effective, as it experiences more participation than the farm land and open space, despite the reduced penalties for early withdrawals from the latter.

The current use taxation program is considered a good method for temporary relief. However, when development is very near, people will sell off their land if the price is right, despite the penalty. The penalty revenues could, however, be used to create open-space with a greater long-term conservation benefit. Many recommendations were made to extend the current use taxation program to include working waterfronts.

3.2 Land Value Taxation

Moving the weight of the property taxes off buildings and onto land values will slow down the creep of suburbs into the countryside and along pristine shorelines. Land value taxation encourages efficient use of the land and reduces the tax burden in moderate to high-populated areas, because the municipality's financial burden is distributed across a greater number of property owners.

This taxation method has been proposed in Maine, but without success. Although, it is philosophically strong it is hard to enact politically. The tax should be limited to assigned urban areas, so the use of already-serviced land will increase. Also, limiting the tax to urbanized areas would not require a "circuit-breaker" for those people in rural areas that are rich in land but money poor.

3.3 Capital Gains Tax on Speculative Land Sales

The capital gains tax on speculative land sales is aimed at protecting rural land from short-term land speculations, and promotes a more efficient use of land. The tax range is dependent on the capital gains and the number of years the land has been owned prior to the sale. The tax may include the sale of land and non-primary residences (e.g. seasonal,

[9] See References – Interviews

vacation homes). The tax should be applied to keep rural open space out of development. Open space in urban areas suitable for development should be exempt from the capital gains tax, so increased use of existing infrastructure and services will occur. When implementing this tax, it is crucial to identify traditional growth areas, which may be done through a comprehensive plan.

3.4 Live Near Your Work Program and the Job Creation Tax Credit

A grant to employees who purchase an existing home near their place of employment, located in a targeted neighborhoods, strengthens neighborhoods and communities and increases the use of existing public services. The tax credit's goal is to use the state's existing infrastructure more efficiently and minimize the development of rural undeveloped lands for business purposes; to accomplish this, the program encourages mid-sized and smaller businesses to invest in smart growth areas around the state.

Both programs are interesting ideas, but when implementing such programs the "free rider" problem should be kept in mind, e.g. people who want to move closer to work despite the program. Further, the creation of the designated growth areas and determination of program eligibility requires some serious thought. Also, the tax credit and grant must be of significant levels to make them financially attractive for people and worth their while to "deal with the paper-work".

3.5 Impact Fees

Impact fees are imposed by municipalities or counties on new development. They aim to generate additional revenue to offset expenditures related to new development. Impact fees are a tool to recover capital cost only, and may not be used punitively. When impact fees are implemented, the costs of development are no longer externalized. To be able to charge an impact fee there must be a direct link between increase in capital expenses and the new development (e.g. schools services, sewer, roads….).

However, charging a significant impact fee might destroy the idea of affordable housing. While, impact fees recover capital expenses, they do not stop development. The difficulty Maine is facing right now is that towns want large lots, which provide higher tax income and reduce the increased burden on public services. Large (expensive) lots will not attract mid-income families with school children, since it will be too expensive for them.

3.6 Tax Shift

The goal of a tax shift is to encourage changes in human behavior that will benefit environmental sustainability. For example, the daily commute for individuals living in the rural areas to their work place could be taxed in the form of a carbon tax. In order to be effective, however, the tax must be so significant that it makes people think about their actions, and possibly change their behavior. A tax shift will provide people the flexibility to pay the tax or look for alternatives, e.g. public transportation versus the car. In order for a tax shift to discourage development in rural areas not suited for development, activities with negative environmental impact must be taxed, e.g. car use, placement of septic system, storm water runoff (penalty based on the square footage of the dwelling)…etc.

3.7 Regional Tax Sharing

Tax sharing reduces the competitive struggle between municipalities to increase their tax base. If designed well, this tax mechanism may support regional planning efforts preservation of open spaces and natural resources, and better utilization of existing infrastructure. Difficulties surrounding regional tax sharing include the design of such a project, and the administration of the shared costs and revenues. Lastly, the idea was presented to extend the regional tax sharing program to include residential housing projects.

3.8 State Income Tax Credit Incentive

This income tax credit program would provide private landowners a dollar-for-dollar tax incentive for the conservation of land, possibly with public access. The credit is dependent on the land value and is often subject to a maximum amount which may only be carried forward for a number of years. This program could be beneficial as long as only land that really needs protection qualifies, e.g. land recognized by the state or local government and community as unique land in need of preservation.

A question raised was whether or not large parcels of land owned by businesses would be eligible for tax incentives. Currently, many businesses in Maine already allow public access. If they would be able to get a credit for a service they are already providing they would be considered “free-riders”.

Another concern raised was whether the state would receive sufficient return from this incentive program. While the state provides a significant tax credit to the property owner, it does not gain ownership of the land. Therefore, the public value of preserving a particular parcel of land will have to outweigh the direct costs for the state.

CONCLUSIONS

For many, Maine’s natural resources are a part of their livelihood. For that reason, preserving natural areas will be to the benefit of Maine’s economic vitality, the well-being of its current and future residents. Currently, the sprawl development pattern of single-family homes on large lots is a threat to Maine’s natural resources. Modifying the state’s taxation systems could induce changes in public behavior and influence land use decisions. The state could improve the conservation aspects of the tax code by adjusting or enlarging existing legislation, performing a major restructuring of the taxation system, or by introducing taxes on the development of natural areas.

The various techniques employed and proposed by other states may be limited in a way that the next generation of elected officials could dismantle them (Stokes, Watson, 1994). For example, urban communities fighting to retain their tax base, and growing suburbs faced with increased public expenditures are likely to bend on existing zoning and preservation policies if potential tax revenues seem attractive. Nevertheless, it is important for the state and municipalities to explore the possibility and feasibility of implementing innovative tax techniques to address current development pressures on sensitive natural areas. Reducing the level of urban sprawl will save acres of undeveloped land and benefit taxpayers in the form of reduced municipal capital expenses such as the construction and maintenance of streets, sewers, waterlines and new schools.

Maine should extend the scope of this research to include a thorough evaluation of the underlying causes of the development pressures. For example, how do state policies such as the school funding formula and infrastructure investments influence sprawl? Maine's state school formula is based on population or school enrollment. As a result, the fastest growing towns in the state receive the larger amounts of state aid (Carney, 1999). Secondly, state and local infrastructure investments enable people to move away from urbanized areas to more remote, but affordable areas that have lower taxes. Consequently, commuter traffic increases and road infrastructure needs are increased.

Further, the lack of good ordinances at the town level currently allows development to happen in natural areas. Many towns have adopted minimum zoning laws to allow themselves flexibility, and the ability to consider development that may provide additional tax revenue. Therefore, town reliance on property taxes needs to be included in a more thorough evaluation. When property taxes are the sole source of local tax revenue, excessive tax burdens often result. While most municipalities are interested in and in favor of preserving their surrounding natural resources, they are not capable of withstanding reduced property tax revenue. Differences in economic conditions are largely driving development and zoning decisions. Hence designing and implementing a uniform taxation system to regulate local land use will create different results in different areas and municipalities. To optimize the effectiveness of a taxation system, the most effective tax rate will need to be determined. This may be done by use of economic and statistical forecasting models.

Implementation of the desired tax or fee structure for Maine should be part of a long-term environmental management strategy – with the ultimate goal of achieving environmental and economic sustainability and a high quality of life (RRI, 2002).
A multidisciplinary approach is essential to solve Maine's current challenges of development patterns and property taxation. In a multidisciplinary approach: (1) true environmental costs should be incorporated into pricing systems through the use of economic instruments, and (2) policies and planning mechanisms should encourage and support positive environmental behavior. Critical to the success of a potential environmental tax or fee structure in Maine, is cooperation among communities, businesses, and state and local governments. Moreover, there must be the will to work together towards a shared vision of an environmentally and economically healthy Maine. A shared vision could be defined in a long-term statewide environmental protection plan, which will function as a guide for efficient use and smart investment of natural resources to ensure healthy and sustainable growth.

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Institutions Contacted

Northwest Environmental Watch
1402 Third Avenue, Suite 500
Seattle, WA 98191-2130
Phone 206-447-1880
http://www.northwestwatch.org

American Farmland Trust
1200 18th Street, NW, Suite 800
Washington, DC 20036
Phone 202-331-7300
http://www.farmland.org

The Live Near Your Work Program
Maryland Department of Housing and Community Development
Mitra Basu – program director
1201 W. Pratt Street, Suite D
Baltimore MD 21223
Phone: 410-209-5801 Fax: 410-685-8270
http://www.dhcd.state.md.us/lnyw/lnyw.cfm

The Job Creation Tax Credit
Division of Business Development
Maryland Department of Business and Economic Development
Stacy Kubafcik – program assistant
217 E. Redwood Street, 12th Floor, Baltimore, MD 21202
Phone: 1-888-CHOOSE-MD or (410) 767-4980
http://www.choosemaryland.org/datacenter/taxesincentives/incentives/creation.asp

Vermont Department of Taxes
109 State Street
Montpelier, Vermont 05609-1401
Tel: 802 828 2515
http://www.state.vt.us/tax.htm

Land Trust Alliance
1331 H Street, NW Suite 400
Washington, DC 20005-4711
http://www.lta.org
Publication: Land Use Planning: Role for Land Trusts, October 1994

Office of Economic Analysis
155 Cottage Street NE U20
Salem, OR 97301-3966
Tel: 503 378 3405

http://www.oea.das.state.or.us/

New Jersey Future
Erik Wilkinson – Policy agent
114 West State Street
Trenton, NJ 08608
Tel: 609 393 0008 ext. 105
http://www.njfuture.org

Additional Websites
University of Maine - http://www.ume.maine.edu/~woodlot/farmtax.htm
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Personal Conversations
University of Southern Maine – Portland, Maine: Prof. R. Barringer, Prof. C. Colgan, Dr. S. Merrill, Prof. J. Kartez, Prof. J. LaPlante, Prof. M. Lapping.

Maine
Peter Mills – State Representative
Chris Hamilton – Maine Coast Heritage Trust

The Nature Conservancy
Maine Chapter – Bruce Kidman
Regional Office, Boston, Ma - Philip Tabas

Vermont
Steve Holmes – Vermont Natural Resources Council
Janet Milne – Vermont Law School

Rhode Island
Chris Modisette – Southern New England Forest Consortium

Minnesota
John Wells - Minnesota State Planning Department

New Jersey
Robert Wilkonson – New Jersey Future
Dale Rick – Senior Attorney, Natural Resource and Defense Council

Oregon
Robert Halliberg – Oregon Department of Land Conservation and Development

Interviews:

Ted Koffman - Executive Director of the Eco-Eco Civic Forum
College of the Atlantic
105 Eden St., Bar Harbor, Maine, 04609
e-mail: Koffman@ecology.coa.edu
Tel: 207 288 5015 ext 239

Lachanche, Laurie – Maine State Economist
Augusta, Maine
e-mail: laurie.lachanche@state.me.us
Tel: 1 800 662 4545

Janet E. Milne - Associate Professor
Director, Environmental Tax Policy Institute
Vermont Law School
South Royalton, Vermont 05068 USA
e-mail: jmilne@vermontlaw.edu
Tel: 802 763 8303 ext. 2266

Record, Larry
MaineTax Assessor's Office
Augusta, Maine
Tel: 207 287 4790

Richert, Evan - Associate Research Professor
Muskie School of Public Service and Management
49 Exeter Street
Portland, Maine 04104
e-mail: erichert@usm.maine.edu
Tel: 207 780 4824

Appendix A

Land to Building Tax Ratios in Pennsylvania

Cities Using Land Value Taxation

Cities	Land-to-Buildings Tax Ratio (1996)
Pittsburgh	5.61 to 1
Scranton	3.90 to 1
Harrisburg	4.00 to 1
McKeesport	4.00 to 1
New Castle	1.75 to 1
Washington	4.35 to 1
Duquesne	5.61 to 1
Aliquippa	16.20 to 1
Clairton	4.76 to 1
Oil City	1.23 to 1
Titusville	8.68 to 1

In the above Pennsylvania cities show a considerable spread between the taxes on the value of land and those on the value of buildings. For example, the land-to-buildings ratio for the city of Pittsburgh is 5.61 to 1. This means that in the calculation of property taxes land value is taxed 5.61 times higher than the value of buildings.

Appendix B

Sample of State Income Tax Credit Incentives

Virginia

- state income tax credit applies to Virginia landowners who donate an easement on or after January 1, 2000.
- easement donors may claim a credit against their Virginia State income tax liability of 50% of the value of the donated easement.
- the amount of the credit may not exceed $100,000.
- the amount of the credit used may not exceed the amount of state income tax otherwise due.
- any portion of the credit that is not used up in the year the easement is donated can be carried over for an additional 5 years.

This state income tax credit is *in addition* to the federal income tax benefits that an easement donor would receive.

South Carolina:

- The total amount of the credit cannot exceed 25% of the Federal tax deduction that the donor claims for the gift.
- The credit is limited to $250 per acre of land.
- The donor cannot use more than $52,500 of the tax credit in any one year
- The remaining credit can be used in future years.
- The donor may sell or transfer the state income tax credit to any other taxpayer, with the same restrictions.

Maryland:

- Owners of farms and other open spaces a state income tax credit for the donation of land for preservation easements.
- The credits are capped at $5,000 per year and are available for the next 15 years, with a total limit of $75,000 and are available to owners of agricultural land and other open spaces.
- This tax credit is not specifically designed to protect wildlife habitat. The tax credits were first recommended last year by the state Agricultural Land Preservation Task Force. The new law is intended to curb sprawl, protect the environment, and maintain open space.

Colorado

- A taxpayer donating a conservation easement is permitted to claim a Colorado income tax credit not to exceed $100,000 per easement.

- In those years where there is a state revenue surplus, the donor of a conservation easement may claim a cash refund from the state up to $20,000 in any one year in lieu of a credit. For example, if an easement donor has a $4,000 Colorado income tax obligation, they may offset that obligation with a $4,000 tax credit, and also claim a refund of $16,000 in the first year. The cumulative total amount that may be used cannot exceed $100,000 per easement.

- An easement donor may transfer all or a part of their tax credit to another taxpayer or taxpayers (transferees) so that the transferees may apply the credit against their Colorado income tax obligation. As of this writing, the administration of these provisions is unclear. Efforts are underway to define the process by which this secondary market in tax credits can work smoothly.
- any portion of the credit that is not used up in the year the easement is donated can be carried over for an additional 21 years.

Delaware

- A taxpayer donating a conservation easement is permitted to claim an income tax credit of forty percent of the fair market value of a donation of fee or easement to the state or qualifying conservation organization qualifies towards the tax credit.
- the tax credit may not exceed $50,000

North Carolina

- An income tax credit for the donation of an easement or fee simple title on land useful for fish or wildlife conservation or other similar land by private landowners and corporations.
- The amount of the tax credit is limited to $250,000 for individuals, and $500,000 for corporations.
- The credit allowed by this section may not exceed the amount of tax imposed by this Part for the taxable year reduced by the sum of all credits allowed, except payments of tax made by or on behalf of the taxpayer.
- Any unused portion of this credit may be carried forward for the next succeeding five years.

Sample of State Income Tax Credit

state	maximum credit % of fair market value	 $	carry over
California	*	*	*
Colorado	100	$100,0000/total	21 years
Connecticut	50	not identified	indefinitly
Delaware	40	$50,000/total	
Maryland	*	$5,000/yr	15 years
New Jersey	*	*	*
New York	25	$250,000/total	*
North Carolina	*	$250,000/total	*
South Carolina	$250/acre	$52,500/total	indefinitly
Virginia	50	$100,000/total	5 years

* = no data available