



Anne Arundel County Agricultural Land And Woodland Preservation Program

Frequently Asked Questions (FAQ) about IPAs

What is an installment purchase agreement?

An installment purchase agreement (IPA) is a contract between the County and the property owner selling his/her development rights. In the IPA, the County promises to pay the purchase price for an easement on specified dates in the future. The IPA also commits the County to pay interest on the outstanding purchase

price between the time that the easement is given to the County (at closing) and the date that the purchase price is paid to the seller. IPAs pay \$1,000 each year for as long as 30 years, when the balance of the purchase price is paid.

Can a seller receive cash for development rights?

Only under limited circumstances. The County's first priority will be to purchase easements from sellers who will accept IPAs. Any seller, however, may receive cash at closing equal to the lesser of \$100,000 or 10% of the purchase price when the purchase price exceeds \$100,000. Any seller desiring more cash will be encouraged to apply to the state program, which still makes all-cash purchases.

Why is the County trying to buy easements on an installment basis?

The County believes that, unless it acts quickly to conserve a significant amount of its remaining farmland, this land and the rural character of the County will be lost forever. Deferral of the County's payment of the purchase price should allow the County to make many more purchases than it could otherwise. It accomplishes this by leveraging \$3 million in annual tax revenue that will be devoted to the program.

Why is payment being deferred for up to 30 years?

The County currently issues long-term bonds to fund its long-lived capital improvements such as schools and sewers. IPAs, like the County's bonds, are general obligations of the County whose principal and interest is payable from taxes. Because the County will own the easements forever, spreading the payments over the longest time possible means that taxpayers will pay for the benefits from farmland preservation as they enjoy them.

How would the sale of my easement change with an IPA?

As in a cash transaction, once the County and the owner are ready to conclude the sale the owner would sign and give to the County a deed of easement. By this deed, the owner agrees to use or maintain the property for agricultural purposes. If the County has agreed to pay a portion of the purchase price at closing, a check would be given to the seller or would be applied to claims against the property such as mortgages. The rest of the purchase price would be paid to the seller through the IPA.

When will I be paid?

The IPA would provide for the payment of interest on a semi-annual basis (two times a year) for as long as 30 years, the date +specified in the IPA for payment of the balance of

the purchase price. The interest and principal will be paid to the seller by check mailed directly by the County's Department of Finance.

How does an IPA benefit me?

The primary benefit to you from selling your development rights through an IPA is that you will receive more for your easement than you would if you were paid in cash at closing. The increase in the amount you are paid comes from the semi-annual interest payments made until the time that the principal amount is paid.

The second benefit to you is that the interest paid to you over the life of the IPA is not subject to federal or Maryland state income taxation. You will receive an opinion from bond counsel at closing to this effect.

The third potential benefit to you is that you may be able to elect an installment method for the reporting of capital gain from the sale of the easement. Section 453 of the Internal Revenue Code provides that capital gain may, under the installment method, be deferred until the receipt of the purchase price.

The final benefit accrues to farmers who derive more than 50% of their income from farming. If such a "qualified farmer" sells his development rights in 2007 for less than their appraised value, he can deduct the discount up to 100% of his income in the year of sale, and use any remaining deduction over

the following 15 years. An IPA may allow a farmer to remain qualified for the 100% deduction by deferring capital gains out of the year of sale.

If you are interested in investigating installment reporting of gain or use of the charitable deduction, you should consult with an attorney and an accountant who are experienced with installment real estate sales transactions and knowledgeable about the specific federal laws and regulations that apply to this method of sale. Because individual circumstances vary, the County cannot guarantee that the IRS will approve this method of reporting gain from sale of any particular seller's development rights.

Why would I want to defer payment for as long as 30 years?

Many easement sellers have owned their property, through purchase or inheritance, for a decade or more. These owners could pay capital gains taxes of over 20% of the sale price of the development rights. Deferring receipt of the sale price may allow such sellers to defer capital gains tax for as long as 30 years, meaning that they may not pay most of the capital gains tax in their lifetimes. During that lifetime, they receive tax-exempt interest every six months on the outstanding balance of the easement sale price.

What is the interest rate that I will earn under the IPA?

The tax-exempt interest rate will be set just prior to closing for each IPA, and will remain the same for up to 30 years. The rate will be based on market yields; rates since 2000 have ranged from 4.8% to 6.0%. The County's Finance Department will make interest payments twice a year and principal payments once a year directly to sellers

Is the easement in effect before I receive the entire purchase price?

Yes. The easement and the restrictions on the use of your property go into effect immediately. Instead of being paid cash for your development rights, however, you are essentially being paid with the County's promise to pay you over up to 30 years (along with the County's promise to pay you interest between the closing and then). The County will have the same right to enforce the restrictions on the property's use as it would have if it paid cash to purchase the development rights.

What happens if the County fails to make a payment to me?

The IPA is a binding contract between the seller and the County. The County would lose all creditworthiness in the bond market if it failed to comply with its bargain with sellers, and it would have difficulty in selling bonds to fund its ongoing capital budget. The County

will pledge its full faith and credit, as well as its power to tax, to make payments to you pursuant to the IPA. This pledge is binding on all future County governments.

What happens if I sell the property before the IPA is paid off?

The IPA has no effect on ownership of your property. You are free to sell your property at any time, subject to the terms and conditions of the deed of easement. If you sold the property, you would continue to receive the interest payments due under the IPA as well as the \$1,000 principal payments every year and the balance of the principal after as long as 30 years.

Can I sell the IPA?

The County's standard form IPA prohibits the sale or transfer of the IPA for one year, except to settle an estate. After that time, you are allowed to sell it or give it away, but its sale or a gift of it may have tax ramifications. Any transfer or sale of the IPA must be of the whole document and all of your rights in it. You cannot have some payments sent to you and others sent to another person. If you sell or otherwise transfer the IPA, you must follow the procedures set out in the IPA for notifying the County so that it knows who is entitled to receive payments. You can continue to use the property even if someone else is entitled to payments under the IPA.

Can I leave the IPA to a beneficiary in my will?

Yes. You should consult with your attorney and financial advisor to discuss what role the IPA can play in planning your estate.

Can I change my mind after closing and buy back the development rights?

No. Once the easement is signed, the restrictions on your property are perpetual. The County will neither return the development rights to you nor buy back the IPA.

If my property increases in value after I sell the easement, will the County pay me more?

No. The purchase price of your easement is established at the time that you sign the deed of easement. After that point, no additional compensation will be paid by the County (other than for payments specified in the IPA).

How can I find out more about IPAs?

For further information, contact Barbara Polito, Department of Recreation and Parks, 1 Harry S. Truman Parkway, Annapolis 21401, telephone (410) 222-7317, e-mail bpolito@aacounty.org.