

Reducing Pennsylvania Inheritance Tax



In Pennsylvania, death triggers a state inheritance tax on the distribution of the deceased person’s assets (the “estate”) to the beneficiaries of the estate. Conservation restrictions in support of agriculture on land included in the estate can reduce the inheritance tax owed.

Summary.....	1
Inheritance Tax Rates	1
Reduction in Land Value From Easements Generally ...	1
Land Under Agricultural Conservation Easement.....	1
Agricultural Reserve, Agricultural Use Property, and Forest Reserve	3
Exemption for Intra-family Transfers.....	3

Summary

In Pennsylvania, land that is perpetually restricted by a conservation easement is valued at its restricted value for state inheritance tax purposes.

The value of land restricted by an agricultural conservation easement meeting the statutory definition can be reduced by 50% for state inheritance tax purposes.

Exemption from inheritance tax is available for certain heirs to land restricted by agricultural conservation easements meeting the statutory definition.

The value of land enrolled in the Clean and Green preferential taxation program is its agricultural use value for state inheritance tax purposes.

Inheritance Tax Rates

The [rates](#) used to calculate Pennsylvania inheritance tax vary depending upon the relationship of the beneficiary to

the decedent. The rate for a surviving spouse is 0%; lineal relationships (up to parents or down to children) —4.5%; siblings—12%; others—15%. These rates are applied to the value of the property of the estate passing to each class of beneficiaries.

Reduction in Land Value From Easements Generally

For inheritance tax purposes, property is valued as of the date of the decedent’s death. When land subject to a [conservation easement](#) is valued for Pennsylvania inheritance tax purposes, the restrictions on subdivision, construction of improvements, and activities and uses imposed by the [conservation easement](#) are taken into consideration. The reduction in appraised value resulting from conservation restrictions can result in significant savings in the tax that family members or other beneficiaries would otherwise pay upon inheriting land located in Pennsylvania.

Land Under Agricultural Conservation Easement

Reduction in Value

Section 2122 of the [Inheritance and Estate Tax Act](#)¹ provides for a 50% reduction in valuation for inheritance tax

¹ Article XXI of the Tax Reform Code of 1971, Act of March 4, 1971, P.L.6, No.2, added by Act of August 4, 1991, P.L.97, No. 22, as amended.

purposes of land subject to an agricultural conservation easement meeting the statutory definition. This reduction applies to the value otherwise determined under the Inheritance and Estate Tax Act, which may be the “use value” described in the “Clean and Green” section below.

Exempt Transfers

Section 2111 of the Inheritance and Estate Tax Act lists transfers not subject to the tax. Subsection “s.1” exempts a “transfer of...[land subject to an] agricultural conservation easement” to or for the benefit of lineal descendants (normally taxed at 4.5%) and siblings (12%).² The bracketed phrase does not appear in the Act, but presumably the exemption was targeted at the transfer of land subject to the easement, not the transfer of the easement itself. Conservation easements are not assets owned by individuals and, thus, not the subject of inheritance.

Agricultural Conservation Easements

The special inheritance tax benefits described above are reserved for land encumbered by “agricultural conservation easements,” which is defined by reference to the [Agricultural Area Security Law](#). Which easements will be deemed to meet that definition?

Easements Established Under State Program

Agricultural conservation easements established under the Pennsylvania Department of Agriculture’s [Agricultural Conservation Easement Purchase Program](#) instituted per the [Agricultural Area Security Law](#) seem obviously intended for eligibility for the 50% value reduction under Section 2122, and exemption under Section 2111.

Other Conservation Easements

Other conservation easements may also qualify if they are consistent with the definition provided in §903 of the [law](#):

“AGRICULTURAL CONSERVATION EASEMENT.” An interest in land, less than fee

simple, which interest represents the right to prevent the development or improvement of a parcel for any purpose other than agricultural production. The easement may be granted by the owner of the fee simple to any third party or to the Commonwealth, to a county governing body or to a unit of local government. It shall be granted in perpetuity as the equivalent of covenants running with the land. The exercise or failure to exercise any right granted by the easement shall not be deemed to be management or control of activities at the site for purposes of enforcement of the act of October 18, 1988 (P.L. 756, No. 108), known as the “Hazardous Sites Cleanup Act.

(The reference to “third party” in the definition is commonly understood to mean an entity qualified to hold a conservation easement that is not a government entity, i.e., a land trust.)

The granting documents used to establish agricultural conservation easements may take many forms. Empirical data regarding the acceptability of one form or another regarding inheritance tax appears scarce or non-existent; the authors confine themselves to offering some general observations regarding one form, the *Model Grant of Conservation Easement and Declaration of Covenants*.

Conservation easements based on [the model](#) provide the easement holder the right to prevent essentially all development or improvement of areas identified in the grant as “Highest Protection Area” and the right to prevent the development or improvement of areas identified as “Standard Protection Area” for any purpose other than sustainable agriculture, sustainable forestry, outdoor recreation, and a few other highly constrained activities.

Note that the Agricultural Area Security Law defines “agricultural commodities” to include timber, wood and other wood products derived from trees. Also, because the definition of “agricultural conservation easement” derives

² This exemption was added to the Inheritance and Estate Tax Act by Act 85 of 2012, with minor amendments included in Act of July 13, 2016, P.L. 526, No. 84.

from the Agricultural Area Security Law, it may be presumed to include agricultural conservation easements purchased under the Pennsylvania Department of Agriculture's [Agricultural Conservation Easement Purchase Program](#), established under the same law. The result may be a somewhat more inclusive definition. For example, while the definition does not reference natural gas infrastructure, easements purchased under the Program permit certain non-agricultural improvements including gas development.

If concern arises that the possibility of minor improvements for recreational and other activities (in other words, non-agricultural use) within the Standard Protection Area would disqualify an otherwise conforming conservation easement for the inheritance tax reduction or exemption, then that possibility can be removed when drafting the grant of conservation easement.

Likewise, while the Agricultural Area Security Law definition of agriculture does not specifically describe residential improvements, easements purchased under the Agricultural Conservation Easement Purchase Program provide for a residential area on the eased property. Accordingly, designation of a "Minimal Protection Area" under [the model](#) for the purpose of accommodating *limited* residential use seems consistent with its qualification as an agricultural conservation easement for purposes of the Inheritance and Estate Tax Act.

Agricultural Reserve, Agricultural Use Property, and Forest Reserve

Exempt Transfers

Section 2111(s.1) of the [Inheritance and Estate Tax Act](#) exempts transfers to lineal descendants (normally taxed at 4.5%) and siblings (12%) of agricultural reserve, agriculture use property or forest reserve as those terms are defined in [§2122\(a\)](#) of the Inheritance and Estate Tax Act. The defined terms correlate to use categories qualifying

for the [Clean and Green](#) program instituted under [Act 319 of 1974](#), but the inheritance tax exemption is available for qualifying land whether or not it is enrolled in the program.

Reduction in Value of Land Enrolled in Clean and Green

If the land has been enrolled in the [Clean and Green](#) program instituted under [Act 319 of 1974](#), [§2122\(b\)](#) of the [Inheritance and Estate Tax Act](#) affords an opportunity to reduce taxes otherwise due upon inheritance of land. The land is valued at its "use value," set annually by the Pennsylvania Department of Agriculture, rather than its appraised value for inheritance tax purposes. The use value is typically much lower than fair market value.

Exemption for Intra-family Transfers

Section 2111(s) of the [Inheritance and Estate Tax Act](#) exempts a transfer of real estate devoted to the business of agriculture between members of the same family under certain conditions.

The exemption for "members of the same family" includes ancestors and lineal descendants (normally taxed at 4.5%), siblings (12%) and a variety of aunts, uncles, cousins, nephews, nieces, and spouses of any of them, all of whom would otherwise pay at the 15% rate.

The exemption applies immediately but may be lost if, within seven years from the transferor's death, the land is no longer devoted to the business agriculture.

The "business of agriculture" is defined only by what is specifically included (leasing of property directly and principally used for agricultural purposes) and what is specifically excluded (recreational activities, raising animals for recreational or sporting activities, fur farming, stockyard and slaughterhouse operations, and manufacturing or processing operations of any kind). At least

\$2,000 a year must be derived from the exempted land to continue to qualify for the exemption.

The exemption requires continuation of the business of agriculture, not the continuation of intra-family ownership, during the seven-year period. Purchasers of land transferred out of an estate within the past seven years will want assurance that the inheritance tax exemption was not taken or, if it was, that the owners have complied with applicable conditions for continuation of the exemption; otherwise, the land may be subject to a lien for, and the new owner liable for payment of, the unpaid inheritance tax, with interest.



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