

SOME ALTERNATIVES FOR FARMLAND ASSESSMENT

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Tax rates and sources of revenue continue to be high on the list of concerns of state and local officials and citizens. Even though taxes have been with us for thousands of years, the topic has by no means receded in interest.

Property taxes have been coming under heavy public criticism in Ohio and in many other states. In 1971, property taxes in the amount of \$1 billion, 884.9 million were levied upon Ohio taxpayers. From 1961 to 1971, total property taxes increased by approximately 95 percent. (Property tax per capita in 1971 was \$177.) While Ohio taxes have been rising we should note that approximately 26 states have higher per capita property taxes than Ohio.

Nationwide, the property tax provides about ^{84% in 1971} ~~72~~ percent of all locally collected tax dollars. And in schools approximately 3/4 of the cost is paid through property taxes.

in Ohio, in 1971, approximately 72% of property tax revenues went to schools.

Many states are questioning this use of property as the tax base for education. Basically the debate is centered around the statement that using property as the tax base does not provide for equal funds for educating students in different communities, that it makes the quality of a child's education a function of the wealth of his parents and neighbors, thereby violating the equal protection clause of the 14th Amendment. A New Jersey state superior court judge ruled that property tax usage for schools is discriminatory against low and middle income families. Nationwide approximately 50 other suits are pending, including one in Ohio, all awaiting the U.S. Supreme Court decision on a case in Texas. As of this writing, all arguments have been presented in

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the Texas case and when the Supreme Court writes its decision, anticipated within the next two months, the future reliance on the property tax will be better known.

Property Tax Revenue Variables

The property tax bill can be affected by changes in any one of the following: "true" value, assessment level, or tax rate. True value is synonymous with market value and thus if a property would sell for \$30,000 that would be the true value. The level of assessment has varied by types of property and between counties. In 1971 the average level of assessment in the state was 30.6 percent varying from 24 percent in Pike County to 30.2 in Jefferson County. (The average level of assessment or sales ratio data are determined by dividing the assessed value of property sold by the sales price or consideration. And therefore this represents a calculated figure influenced by the number of properties actually being sold within a specified period of time.) The variation within counties between different types of property has been even greater. The Ohio/^{Tax}Appeals Board, by law, has the duty to define taxable value not to exceed 50 percent of true value. By the end of 1977, when reappraisal is completed, all counties will use a standard property tax assessment rate of 35 percent of the true value of property as it is best determined.

Effective January 1, 1973, after the reappraisal process has been completed within each county, changes in the value of property will be determined annually. Procedures for updating annually so that values are adjusted to 100 percent of market value are presently under consideration by the Ohio Board of Tax Appeals. It is anticipated that the yearly adjustment could be made by applying a flat percentage, either by class (Industrial, Commercial, Residential, Agricultural) or on property in the county considered altogether. For example, if values in the county have increased seven percent then the property value on record would be increased by seven percent. The decision on how much values change will

involve three levels: the county auditor, the local Board of Revision and the Board of Tax Appeals.

The third variable affecting tax revenues from property is the tax rate which is determined by the voter. In 1971 the average tax rate ^{by county} was 47.95 mills. As seen in the following example these variables determine the amount of taxes paid by an individual:

Market Value.....	\$30,000	
Level of Assessment	x .35	
Tax Value.....	\$10,000	#10,500
Tax Rate (Millage)	x.045	.045
Annual Tax Payment	\$ 420	#472.50

Current Use versus "Highest and Best Use"

One current concern in Ohio centers on whether the true value of property should be determined on the basis of its current use rather than its potential probable use. Generally farmers with land near urban areas feel that land being used for agricultural purposes should be valued accordingly and not appraised in terms of its future potential use as a housing development site, a shopping center or a possible industrial site.

The practice of assessing all classes of real estate at the same percentage (35) is referred to as the "uniform rule." In 1964 the concern for uniformity was emphasized in the Park Investment Case when an order was issued to bring about uniformity in assessment of different kinds of property. Since 1964 several actions have been taken regarding the Park Investment Case with the most recent being the November 15, 1972, decision of the Ohio Supreme Court which held constitutional the 6-year adjustment to a standard 35 percent property tax assessment rate in all 88 counties as provided in legislation passed in 1972. At the same time the Ohio Supreme Court held unconstitutional a provision in the new assessment law that required auditors to determine a parcel's true value on the basis of its current use rather than its potential probable use. In essence, the decision orders uniform assessment and property values to be based on the

fair market value that the assessed real property should bring if sold on the open market or "highest and best use."

Agricultural Land Dilemma

At present farmers with farmland near or within the influence of cities are faced with the problem that the property tax levied against their farms may be at a level higher than the farm operation can support. As urbanization occurs, the land becomes more valuable and when property taxes are determined in part by the future potential use of the land the opportunities to continue farming at the same location are diminished. The farmer caught in this situation cannot easily move. Other farming land may not be available in his area and thus moving may entail the loss of his livelihood, his established position in the community and his way of life. At the same time it is necessary to recognize that the same sequence may result in an improved standard of living for some individuals. Each situation has its own set of variables which determine if the net result is a plus or minus. For example, if the farmer is about ready to retire, then selling the land may be ~~most desirable~~ ^{acceptable}. However, a middle-aged farmer may find himself "locked-in", possibly too young to retire but too old to move and start over in agriculture and also too old and perhaps lacking the specific skills needed to ~~be in demand~~ ^{find nonfarm} for a different kind of employment.

A number of states have taken action to cope with urban pressures on farm real estate taxes through the use of differential assessment of farmland. The following discussion summarizes most of these efforts and delineates a number of alternatives which may be considered within the property tax.

Criteria for Judging a Tax

Whether evaluating a particular type of tax or whether examining the merit of modification within a tax, certain criteria are frequently suggested as being

helpful. These criteria include: fairness, economic effects, ease of administration, compliance by the taxpayer, and constitutional compliance.

- a. Fairness--In considering changes within the property tax, will relief be received by those for whom it is intended and if payments by some are reduced who will be expected to make up the difference?
- b. Economic effects--What effect will the change in tax have upon the community? In considering a deferred taxation system how many years back payment is both fair and economically desirable?
- c. Administration--Is the system one where the costs of determining and collecting tax payment are high in relation to the amount of revenue received?
- d. Compliance--Will the administrative office be able to determine who should receive property tax relief and then be able to ensure that the intent of the law is not violated?
- e. Constitutional compliance--Does the tax comply with the existing Constitution and should or can an amendment to the Constitution be made.

Some Alternatives for Farmland Taxation

In determining the value to be used as a base in taxing property and in considering the amount of property taxes that should be paid, many states are considering and using a number of alternatives. The following represents a list of the alternatives most frequently discussed:

(1) Base property value on highest and best use.

This is Ohio's present system and the Ohio Constitution requires a method of valuation based on the fair market value that the assessed real property should bring if sold on the open market.' This alternative has been discussed in detail above.

(2) Differential assessment laws are of three general types: preferential assessment, deferred taxation, and restrictive contracts and agreements.^{/1}

a.) Preferential assessment means that land devoted to agricultural use shall be assessed on the basis of its value in agriculture and that market values reflecting potential uses, such as commercial buildings or subdivisions, shall be ignored. Approximately eleven states direct the tax assessor to value farmland, and in some states also forest and open-space land, on the basis of its current use instead of its current value. States with laws of this nature include: Arkansas, Colorado, Delaware, Florida, Idaho, Indiana, Iowa, Massachusetts, Nebraska, New Mexico and South Dakota. The preferential treatment of farmland includes problems such as: identifying bona fide farm use of all farms to remain as farmland even though some of the land may be in areas that the

^{/1} Dr. Thomas F. Hady, Chief Community Facilities Branch, "Rural Property Taxes-- Where Are We Headed?", Economic Research Service, United States Department of Agriculture, November 30, 1971.

citizenry has decided should go into urban use in the near future.

b.) Deferred taxation laws allow the urban fringe farmer to postpone part of his tax payment until he sells or develops the land. Where deferred taxation laws are used the local assessor determines two values for each parcel of farmland: (A) its value in agricultural use, which serves as the basis for current taxation, and (B) its market value. When the land is sold or converted to nonfarm use, the owner is liable for the difference between taxes based on agricultural value and what they would have been on the basis of market value. The retroactive collection of taxes is generally limited to the most recent three or five years. In some states interest is charged on the additional taxes. States having deferred taxation laws include: Alaska, Kentucky, Maine, Maryland, New York, Minnesota, New Jersey, Oregon, Rhode Island, Texas, Utah and Virginia. A deferred taxation law is now being considered by the Nevada State Legislature.

The state of Connecticut has a deferred taxation law which differs from the above in that the landowner makes application to have the property taxed according to agricultural use. The agreement is for a period of ten years. If the land is sold for other than agricultural purposes within one year, the seller pays the state ten percent of the sales price; if the land is sold within the second year then the seller pays nine percent of the sale price. The percent paid declines until after the end of the tenth year when there is no penalty for selling regardless of the use for which the land is sold.

c.) Restrictive agreements or in essence the acquisition of development rights represent the third way of easing farm property tax burdens. This approach could involve ^{1,} the landowner selling to the government his right to develop his land for a period of, for example, ten years, ^{2,} or ¹ the government buying the farmer's land and leas^{ing} it back ~~to him~~. The former approach is used more than the government actually buying the land. In 1961 Hawaii passed a law providing for a landowner to petition the state to have his land declared as dedicated to specific agricultural uses. If approved, the owner forfeits the right

to change the use of his land for ten years, and the land is assessed on the basis of permitted uses.

California law provides for many varied types of legally binding voluntary contracts and agreements between the landowner and the local government, some running for an initial term of ten years. The assessor is then required to assess on the basis of the legally permitted uses. By early 1968 nearly two million acres had been contracted in this program.

(3) *Percentage Variation in Differing Classes*
A variation of the preferential assessment alternative would be to value all property at market value but set different percentages for different classes of property. In this method different classes must be clearly defined so that there is no question whether the property is industrial, commercial or agricultural. Clearly defining what is agricultural and what is not, presents a number of problems, such as determining the measure to use in determining if the land use is primarily agriculture and when the type of measurement is determined, then where is the line to be drawn in terms of income, cultivated acres, etc. This problem must also be dealt with in some of the other alternatives considered.

In Alabama, in 1972, a special session of the legislature passed a bill that established three classes and provides for different levels of assessment as follows:

Class I--all property of utilities used in the business of such utilities;

Class II--all property not otherwise classified;

Class III--all agricultural, forest and residential property.

The level of assess-to-market value for each class of property is 30 percent, 25 percent and 15 percent, respectively.

(4) *Tax Credit Based on Income*
Still another alternative within the property tax would be to appraise all property at market value and to use a uniform level of assessment but to permit tax credits which would prevent property taxes from being ~~more~~ ^{in excess of} a certain percent of net income.

Bills have recently been introduced which would place a ceiling on the ^{proportion} ~~amount~~ of income that an Ohioan could be required to pay in property taxes. Under these proposed bills a taxpayer whose property taxes exceeded a stated percent of his income would be classified as an overburdened taxpayer. For example, if the limit for property taxes as set at four percent then the taxpayers property tax would not exceed four percent of his annual income. In the August 1972 issue of the Ohio State University Bulletin of Business Research, Dr. Frederick D. Stocker made the following statement:

"Among the more interesting recent developments in state and local finance is the increasing use by states of what is known as a "circuit breaker," to prevent property tax "overloads." In simplest terms, a circuit breaker provision sets by law a ceiling on property taxes in terms of some stated percentage of taxpayer income. When property taxes exceed that ceiling, the taxpayer is entitled to a partial or total rebate of the excess, either as a credit against state income tax liability or as a direct cash refund. Since 1963 almost a dozen states have enacted this form of property tax relief, in every case applying it only to residential property taxes and limiting it to the elderly."

Implications

The foregoing dicussion of some alternative for farmland assessment obviously does not exhaust the possibilities nor ^{does it} make any attempt to judge which of the alternatives represents the best choice. That decision needs to be made by the taxpayer at the voting place or through legislative representatives at the Statehouse.

The challenge is clear--ensuring the principle of uniformity and yet considering property tax relief for farmers on the rural-urban fringe.