

PROPERTY TAX ASSESSMENT OF AGRICULTURAL LAND - BACKGROUND MEMORANDUM

House Concurrent Resolution No. 3047 (attached as Appendix A) directs the Legislative Council to study the property tax assessment and valuation of agricultural property. The resolution states that validity of agricultural property assessments under the productivity formula is increasingly being questioned by farmers whose property market values have declined while property tax valuations have increased and that fluctuations in agricultural property assessments have not been uniform across the state. Assessment of agricultural land has been one of the most common study topics for interim committee review, having been the topic of specific study directives or as part of another study directive during each interim from 1989 through 1998.

PRODUCTIVITY VALUATION OF AGRICULTURAL PROPERTY

The 1981 Legislative Assembly restructured property tax assessments in the state and changed the basis for valuation of agricultural property to a formula to determine its productivity value. True and full value of agricultural property for property tax purposes is based on productivity, as established through computation of the capitalized average annual gross return of the land as made by the North Dakota State University Department of Agricultural Economics as required by North Dakota Century Code Section 57-02-27.2 (attached as Appendix B).

The Department of Agricultural Economics determines annual gross return for property based on the best statistical information it can obtain. For minor production crops, such as lentils and field peas, production statistics are not available so values based on known crops are substituted. Canola was in this category until 2000, when the National Agricultural Statistics Service recognized the growth in canola production and began gathering production data. It is not believed that lack of data on minor crops has a substantial impact on countywide valuations.

Annual gross return for rented land is determined from crop share or cash rent data, and for other land, annual gross return is 30 percent of annual gross income for cropland used for growing crops other than sugar beets or potatoes, 20 percent of annual gross income for cropland used for growing sugar beets or potatoes, and 25 percent of gross income potential based on animal unit carrying capacity of the land for land used for grazing animals. Average annual gross return for each county is determined by using annual gross returns for the county for the 10 most recent years, discarding the highest and lowest annual gross

returns from those years, and averaging the returns for the remaining eight years. Average annual gross return is indexed for inflation to reflect changes in prices paid by farmers. This cost of production factor is determined by the Agricultural Economics Department by comparing National Agricultural Statistics Service indexes of prices paid by farmers over a period of 10 years, discarding the highest and lowest years' indexes, and averaging the remaining eight years' indexes. This amount is divided by the base year index of prices paid by farmers during the seven-year period ending in 1995.

Average annual gross return for agricultural property is capitalized using a 10-year average of the most recent 12-year period for the gross farm credit services mortgage rate of interest.

An average agricultural value per acre is established for cropland and noncropland on a statewide and countywide basis. The Department of Agricultural Economics provides this information to the Tax Commissioner by December 1 of each year, and the Tax Commissioner provides the information to each county director of tax equalization. The county director of tax equalization uses the countywide average received from the Tax Commissioner as the basis for determining and providing each assessor in the county with an estimate of the average agricultural value of agricultural lands within the assessor's district. The assessor uses the average valuation received from the county director of tax equalization to determine the value of each assessment parcel within that district. Within each county and assessment district, the average of values assigned to agricultural property must approximate the averages determined under the formula for the county or assigned to the district by the county director of tax equalization. In determining relative values of parcels of property, local assessment officials are to use soil type and soil classification data whenever possible.

Inundated agricultural land is an exception to the valuation formula. Inundated agricultural land is defined as agricultural property containing a minimum of 10 contiguous acres, if the value of the inundated land exceeds 10 percent of the average agricultural value of noncropland for the county, which is inundated to an extent making it unsuitable for growing crops or grazing farm animals for two consecutive growing seasons or more and which produced revenue from any source in the most recent prior year which is less than the county average revenue per acre for noncropland. Application for classification as inundated agricultural land must be made in writing to the township assessor or county director of tax

equalization by March 31 of each year, except for the year 2001, in which the written application must be made by June 14, 2001. Before all or part of a parcel of property may be classified as inundated agricultural land, the board of county commissioners must approve that classification for that property for the taxable year. The agricultural value of inundated agricultural lands must be determined by the Agricultural Economics Department to be 10 percent of the average agricultural value of noncropland for the county as determined under the formula and valuation of individual parcels of inundated agricultural land may recognize the probability that the property will be suitable for agricultural production as cropland or for grazing farm animals in the future.

2001 LEGISLATION

Senate Bill No. 2068 made changes to the inundated agricultural land definition and added the requirement of written applications for classification as inundated land. The bill was introduced by the Tax Commissioner after study by the Tax Commissioner and local tax officials and others during the 1999-2000 interim.

House Bill No. 1246 would have locked the capitalization rate used in the agricultural property valuation formula within a range of not less than 9.25 percent and not more than 10.5 percent. The bill failed in the House by a vote of 45 to 52.

House Bill No. 1362 would have imposed a cap on the value of any parcel of agricultural property for taxable years 2001 and 2002 of not more than the valuation of that property for taxable year 1999. The bill failed in the House by a vote of 46 to 52.

SUGGESTED STUDY APPROACH

There is continuing misunderstanding or dissatisfaction with agricultural property valuations as generated by the agricultural property valuation formula. This is evidenced by frequent Legislative Council committee studies of this topic and introduction of numerous bills in recent years designed to hold down values of agricultural property.

Much of the criticism of the valuation formula has come from the northeastern part of the state where excess moisture has been a problem for farmers. Standing committee minutes for House Concurrent Resolution No. 3047 contain statements that some believe the problem may relate to use of harvested acres and planted acres data in valuations. However, computations use production from harvested acres and divide that by planted acres, which would produce a lower figure for production per acre if some acreage is planted but not harvested. Review of application of the formula appears to be the objective of the study directive.

It is difficult to recommend a course of action for study of valuation of agricultural property. It appears the logical first step would be to receive a review by a representative of the Department of Agricultural Economics at North Dakota State University on application of the agricultural property valuation formula and a forecast of whether valuation increases are likely in the future. Testimony should also be sought from local officials. After that information is received, it should be decided if change is necessary, and whether it would be more appropriate to make adjustments to the formula or substitute an entirely different method for assessment of agricultural property.

ATTACH:2

**Fifty-seventh Legislative Assembly of North Dakota
In Regular Session Commencing Tuesday, January 9, 2001**

HOUSE CONCURRENT RESOLUTION NO. 3047
(Representatives Herbel, Kingsbury)

A concurrent resolution directing the Legislative Council to study the property tax assessment and valuation of agricultural property.

WHEREAS, since 1981 agricultural property in the state has been assessed for property tax purposes pursuant to a statutory formula intended to determine its agricultural productivity; and

WHEREAS, the valuation method for agricultural property was intended to be based in large part upon detailed soils surveys, which have not been completed; and

WHEREAS, the validity of agricultural property assessments under the productivity formula is increasingly being questioned by farmers whose incomes and property market values have declined while property tax valuations have increased; and

WHEREAS, fluctuations in agricultural property assessments have not been uniform across the state and thorough examination is needed to determine whether the productivity formula results in appropriate valuations of agricultural property for property tax purposes;

NOW, THEREFORE, BE IT RESOLVED BY THE HOUSE OF REPRESENTATIVES OF NORTH DAKOTA, THE SENATE CONCURRING THEREIN:

That the Legislative Council study the property tax assessment and valuation of agricultural property; and

BE IT FURTHER RESOLVED, that the Legislative Council report its findings and recommendations, together with any legislation required to implement the recommendations, to the Fifty-eighth Legislative Assembly.

57-02-27.2. Valuation and assessment of agricultural lands.

1. "True and full value" of agricultural lands must be their agricultural value for the purposes of sections 57-02-27, 57-02-27.1, 57-02-27.2, and 57-55-04. Agricultural value is defined as the "capitalized average annual gross return", except for inundated agricultural land. The "annual gross return" must be determined from crop share rent, cash rent, or a combination thereof reduced by estimated property taxes and crop marketing expenses incurred by farmland owners renting their lands on a cash or crop share basis.
2. For purposes of this section, "annual gross return" for cropland used for growing crops other than sugar beets and potatoes means thirty percent of annual gross income produced, "annual gross return" for cropland used for growing sugar beets and potatoes means twenty percent of annual gross income produced, and "annual gross return" for land used for grazing farm animals means twenty-five percent of an amount determined by the agricultural economics department of North Dakota state university to represent the annual gross income potential of the land based upon the animal unit carrying capacity of the land.
3. The "average annual gross return" for each county must be determined as follows:
 - a. For taxable year 1999, total the annual gross returns for the nine years immediately preceding the current year for which data is available and discard the highest and lowest annual gross returns of the nine. For taxable year 2000 and thereafter, total the annual gross returns for the ten years immediately preceding the current year for which data is available and discard the highest and lowest annual gross returns of the ten.
 - b. The agricultural economics department of North Dakota state university shall establish a base year index of prices paid by farmers using annual statistics on that topic compiled by the national agricultural statistics service for the seven-year period ending in 1995, discarding the highest and lowest years' indexes, and averaging the remaining five years' indexes. For taxable year 1999, the agricultural economics department shall gather the national agricultural statistics service annual index of prices paid by farmers for the nine years ending with the most recent year used under subdivision a, discard the highest and lowest years' indexes, average the remaining seven years' indexes, and divide the resulting amount by the base year index of prices paid by farmers. For taxable year 2000 and thereafter, the agricultural economics department shall gather the national agricultural statistics service annual index of prices paid by farmers for the ten years ending with the most recent year used under subdivision a, discard the highest and lowest years' indexes, average the remaining eight years' indexes, and divide the resulting amount by the base year index of prices paid by farmers. This amount must be divided into the amount determined under subdivision a.
 - c. For taxable year 1998, divide the figure arrived at in subdivision b by six. For taxable year 1999, divide the figure arrived at in subdivision b by seven. For taxable year 2000 and thereafter, divide the figure arrived at in subdivision b by eight.
4. To find the "capitalized average annual gross return", the average annual gross return must be capitalized by a rate that is a ten-year average of the gross federal land bank mortgage rate of interest for North Dakota. The ten-year average must be computed from the twelve years ending with the most recent year used under subdivision a of subsection 3, discarding the highest and lowest years, and the gross federal land bank mortgage rate of interest for each year must be determined in the manner provided in section 20.2032A-4(e)(1) of the United States treasury department regulations for valuing farm real property for federal estate tax purposes, except that the interest rate may not be adjusted as provided in paragraph (e)(2) of section 20.2032A-4.
5. The agricultural economics department of North Dakota state university shall compute annually an estimate of the average agricultural value per acre [.40 hectare] of agricultural lands on a statewide and on a countywide basis; shall compute the average agricultural value per acre [.40 hectare] for cropland, noncropland, and inundated agricultural land for

each county; and shall provide the tax commissioner with this information by December first of each year. Fifty percent of the annual gross income from irrigated cropland must be considered additional expense of production and may not be included in computation of the average agricultural value per acre [.40 hectare] for cropland for the county as determined by the agricultural economics department. Before January first of each year, the tax commissioner shall provide to each county director of tax equalization these estimates of agricultural value for each county.

6. For purposes of this section, "inundated agricultural land" means property classified as agricultural property containing a minimum of ten contiguous acres if the value of the inundated land exceeds ten percent of the average agricultural value of noncropland for the county, which is inundated to an extent making it unsuitable for growing crops or grazing farm animals for two consecutive growing seasons or more, and which produced revenue from any source in the most recent prior year which is less than the county average revenue per acre for noncropland calculated by the agricultural economics department of the North Dakota state university. Application for classification as inundated agricultural land must be made in writing to the township assessor or county director of tax equalization by March thirty-first of each year, except that for the year 2001, the written application must be made within ninety days from March 16, 2001. Before all or part of a parcel of property may be classified as inundated agricultural land, the board of county commissioners must approve that classification for that property for the taxable year. The agricultural value of inundated agricultural lands for purposes of this section must be determined by the agricultural economics department of North Dakota state university to be ten percent of the average agricultural value of noncropland for the county as determined under this section. Valuation of individual parcels of inundated agricultural land may recognize the probability that the property will be suitable for agricultural production as cropland or for grazing farm animals in the future.
7. Before February first of each year, the county director of tax equalization in each county shall provide to all assessors within the county an estimate of the average agricultural value of agricultural lands within each assessment district. The estimate must be based upon the average agricultural value for the county adjusted by the relative values of lands within each assessment district compared to the county average. In determining the relative value of lands for each assessment district compared to the county average, the county director of tax equalization, whenever possible, shall use soil type and soil classification data from detailed and general soil surveys. When such data cannot be used, the county director of tax equalization shall use whatever previous assessment data is best suited to the purpose.
8. Each local assessor shall determine the relative value of each assessment parcel within the assessor's jurisdiction and shall determine the agricultural value of each assessment parcel by adjusting the agricultural value estimate for the assessment district by the relative value of the parcel. Each parcel must then be assessed according to section 57-02-27. If either a local assessor or a township board of equalization develops an agricultural value for the lands in its assessment district differing substantially from the estimate provided by the county director of tax equalization, written evidence to support the change must be provided to the county director of tax equalization.