NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: H.B. 54

SHORT TITLE: Make Farmland Use Value Accurate

SPONSOR(S): Rep. Neely

FISCAL IMPACT

Yes (X) **No ( )** **No Estimate Available (X)**

	FY 1999-00	FY 2000-01	FY 2001-02	FY 2002-03	FY 2003-04
REVENUES					
General Fund	**No General Fund Impact**				
Local Governments	**Potential Local Revenue Increase**				

PRINCIPAL DEPARTMENT (S) &
PROGRAM (S) AFFECTED: County Governments, N.C. Department of Revenue, Ad Valorem Tax Division.

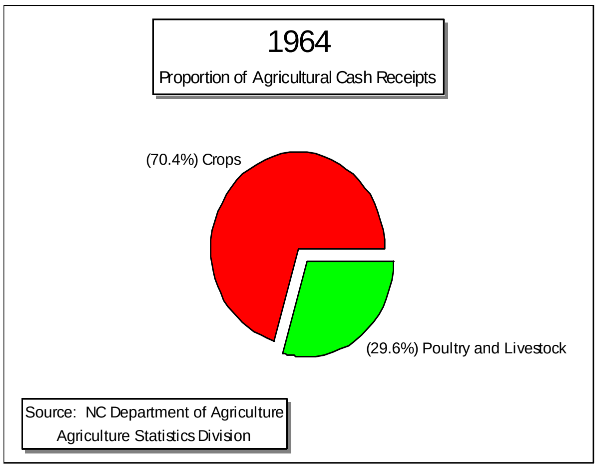
EFFECTIVE DATE: July 1, 2001, and applies to schedules of values adopted for tax years beginning on or after that date.

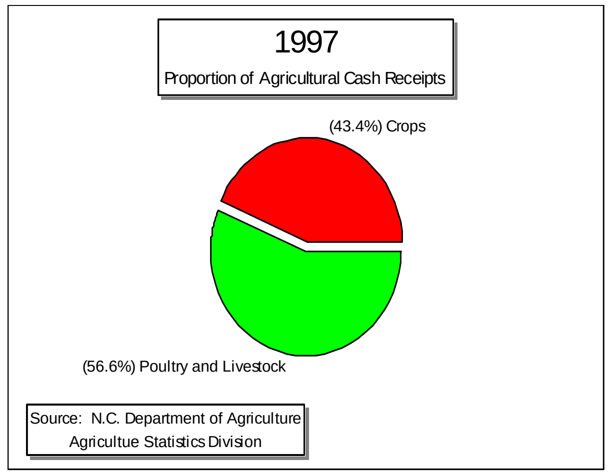
BILL SUMMARY: Under current law farmers are charged property taxes based on the land value for agricultural and horticultural purposes, rather than the full market price. In general, this value is lower than market because it does not reflect any potential alternative uses for the property (i.e. new homes, commercial development, or industrial facilities). Under the current system the adjusted value for agriculture is based on the market price for corn and soybeans, as well as the cost of producing corn and soybeans. A Use Value Advisory Committee is charged with determining the basis for horticultural land. This bill changes the tax basis for both types of land to cash rents, and provides a capitalization rate of 5%. No changes are made to the use value system for forestland. The Revenue Laws Study Committee recommended this proposal.

ASSUMPTIONS AND METHODOLOGY:

Under G.S. 105-289(a) 5 the Department of Revenue and the Use Value Advisory Committee are instructed to develop a manual to assist county assessors in determining the use-value of agricultural, horticultural, and forest land. The law states that the use-value should be based on expected net income from the property. The expected net income for agricultural land shall be based on actual yields, the price of corn and soybeans for the last five years, and the actual cost of growing corn and soybeans during the same period. The law allows the committee to set a method for determining the income potential of horticultural land.

In 1996 and 1997 the Revenue Laws Study Committee was informed that corn and soybean prices may no longer be the most appropriate method for determining the expected income for farmland, as crops are no longer the primary agricultural products of the state. As noted in the charts below, the proportion of agricultural cash receipts that come from crops has declined from 70.4% in 1964 to 43.4% in 1997.





In 1985, the year in which the current use valuation methodology was implemented, crops accounted for 52.8% of agricultural cash receipts.

The Revenue Laws Study Committee was also informed that good cost of production data was no longer available. As a result, Revenue Laws directed the Present Use Advisory Committee to study the issue and return to the Revenue Laws Study Committee with their recommendation for a new system.

In May 1998 researchers from the North Carolina Cooperative Extension Service conducted a statewide survey to determine the appropriateness of cash rent as a new basis for the use value system. The survey asked Extension Directors, Tax Assessors, Farm Credit Service Appraisers, and farmers to provide estimates of agricultural land values (when sold as agricultural land) and agricultural cash rents. Estimates were given for low, medium, and high productivity land. The data was sorted by region (referred to as a Major Land Resource Area or MLRA). Allowances were also made for quota crops. The Extension Service reports receiving survey responses from 98 County Extension Directors and 98 County Tax Assessors. Estimates were also given by Farm Credit for all 100 counties. They received at least one farmer response from 75 counties.

When the Use Value Advisory Board compared the sale price of farmland sold as farmland to the cash rent derived from that land, it found the average rent to value ratio to be 2% in most of the MLRAs. The notable exception is the Tidewater region where the average rent to value ratio is 4.5%. This ratio most closely reflects the true rent to value ratio because the agricultural use of the property in that region is often its highest and best use since there are not many competing pressures to increase the value of the property. For this reason, the Use Value Advisory Board recommends using a 5% capitalization rate. Also, 5% is the nationwide average capitalization rate for farmland.

Department of Revenue officials estimate that approximately 50% of counties no longer use the Use Value manual to determine agricultural use value. Even under the new system, county assessors will be given a significant amount of latitude in determining the use value of a particular piece of land. As such, no specific, statewide fiscal impact is possible. Department of Revenue and Extension professionals believe that, on average, agricultural property tax values will rise as a result of the new system. Some areas will see a small increase, while other areas could see the tax values for agricultural land increase 250%, assuming the assessors in those areas were still using the use value manual. The county assessor will determine the actual increase.

FISCAL RESEARCH DIVISION 733-4910
PREPARED BY: Linda Struyk Millsaps

APPROVED BY: Tom Covington

DATE: **May 10, 1999**

Official Fiscal Research Division Publication

Signed Copy Located in the NCGA Principal Clerk's Offices