

Assessing Farmland According to Use

(Editor's Note: The following report was prepared by Donald J. Epp, an associate professor of agricultural economics at Penn State. In many instances, farm real estate taxes have climbed to a point where farmers feel compelled to sell out because they can't make a profit from farm operations. Taxing farmland according to its use rather than its market value is one method that's been proposed to remedy this situation. Epp takes a look at the impact of use-value assessment on farms throughout the Commonwealth. In Lancaster County, Epp found that use-value assessment would probably increase most farmers' tax bills.)

The prominence given to discussions of real estate taxes has brought to light a long-standing concern among many groups with the way we tax agricultural land, particularly that which is adjacent to growing urban areas. As cities begin to grow out into the surrounding rural areas, some of the best agricultural land is removed from agricultural production.

As land-use shifts from agricultural to urban, surrounding properties also increase in value. This increase in value, resulting from potential use of land for urban development, results in an increased property assessment and an increased bill.

Some farmers have complained that these increased taxes based on potential use cannot be paid with the income received from farming the land. This often "forces" an individual to sell his property in order to get out from under the burden of paying excessive taxes.

Many people have voiced concern with this premature sale agricultural land which often results in "idle" land adjacent to our growing metropolitan centers. The consequent dislocation of people interested in active farming is also a source of concern.

A second source of concern resulting from the shift in use of farmland near cities relates to a sense of aesthetics. Many people believe that open space has a place in an attractive landscape near our cities, and they feel that agriculture could very logically fit into this open space.

A third source of concern with the shift in land-use from farm to urban is that much of Pennsylvania's best farmland is

located very near growing metropolitan areas. These farmlands have not only supported a thriving agricultural industry, but have also contributed to a very substantial service and processing industry related to agriculture.

As farms disappear, the support for these agriculturally related industries is also diminished. Many of them will find it difficult or impossible to continue their operations and additional unemployment problems could result.

There are substantial numbers of people who feel that we should take step to preserve the agricultural industry on the most productive land in Pennsylvania to maintain a strong economic base for such communities.

These groups argue that the diversity provided by agriculture and its related service industries in a growing metropolitan manufacturing center provides opportunities for people with all types of skills to find profitable employment.

Many solutions have been proposed for solving these problems. This article focuses primarily on proposals for altering the methods of taxing farm real estate.

Various suggestions have been made to reduce the farmer's tax bill to allow farmland to be kept in active production, thus achieving the benefits of a diversified economic base and an aesthetic landscape near our metropolitan centers.

The most prominent of these

proposals has been to base agricultural real estate taxes on the value of the land used for agricultural production as contrasted to the value which would result from residential or commercial use. Several bills have been presented to the current session of the Pennsylvania General Assembly to provide for the taxation of agricultural land and other open-space land on basis of its current use rather than on its potential value. These bills have been actively considered by various committees of the legislature and some type of action may be likely in the near future.

Determining the value of real estate

One of the first questions that must be answered is how to determine the agricultural value of farmland that has some alternative use affecting its market price. In other words, if a farm could be used for residential development and is, therefore, worth \$2,000 an acre in such development, and currently has a market price of \$2,000 an acre, how do you determine its agricultural value?

There are three ways generally used to determine the value of a piece of real estate. The most reliable and frequently used method is to compare the sale prices of other pieces of land that are similar to the one in question and have been sold recently. This sale comparison method gives a good indication of what people in the market believe land is worth at the present time.

A second technique that is frequently used for buildings and other improvements is to determine what their replacement cost would be, deducting depreciation based on the age of the buildings.

The third generally used method of appraising real estate is to determine the income that can be generated from the use of that property and capitalize this income into a land value.

These three methods all have problems, when we try to use them to determine the agricultural value of a piece of property near our growing cities.

The first method is difficult to use because no land is used strictly for agricultural purposes. Every comparable sale includes the possibility that the land may be used for residential or commercial development. A replacement cost technique is used for buildings and does not help us to determine the agricultural value of the land. The third method, income capitalization, holds promise because farmland is being used to generate income and this income could be capitalized into a land value.

A problem arises, however, because it's difficult to sort out effect of the farmer's management ability on the productivity of the land. For instance, a poor farmer with good

land may have a low income, but this doesn't mean that his land is not worth much. Likewise, a good farmer with poor soil may have a fairly high income because of his superior management, but that does not mean that the farmland is more valuable. Some method must be devised to determine the value of the farmland separate from the value of the farmer's management ability.

Use-value assessment

A study currently underway at The Pennsylvania State University is investigating the

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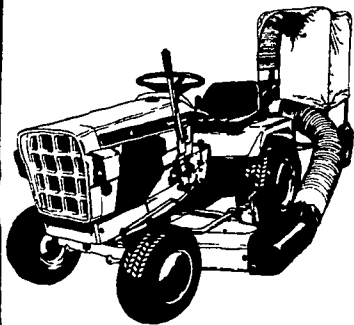
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