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OPEN SPACE EASEMENT FOR FARMLAND

House Bill 5808 (Substitute H-1)
First Analysis (4-17-02)

Sponsor: Rep. Judson Gilbert II
Committee: Land Use and Environment

THE APPARENT PROBLEM:

Policymakers who are concerned about both the loss of farmland in Michigan and the lack of profitability of farming say that one contributing factor is the way in which the land is taxed. Michigan is said to be the only state that does not tax farmland based on its agricultural value. Instead, farmland is taxed at market value, which includes the value the land has for potential developers. Farm property taxes in Michigan are about twice the national average per acre, say representatives of farming interests. (The state does, however, have a farmland preservation program, known as PA 116, which offers farmers lower taxes in exchange for a promise not to develop their land. This has been a beneficial program for farmers, but its impact has been reduced with the passage of Proposal A, which lowered property taxes for farmers as part of the new school financing system. Further, not all farmers are eligible for the program's benefits.)

While there might be no difference between the agricultural use value and the market value of farmland in areas of the state that are heavily agricultural, the difference can be substantial in areas where residential and commercial development are nearby. This leads to higher taxes for farmers on the fringe of development. These higher operating costs increase the pressure to sell for farmers operating in the midst of rapid residential and/or commercial development. Taxing farmland based on its agricultural use value, say proponents, could help keep farmers on the land by reducing their costs and helping to make their operations more profitable. Keeping farmers on the land also reduces urban sprawl, say preservationists, and preserves the rural character of the countryside. Farms, moreover, typically use fewer local services than residential or commercial property.

A number of proposals have been made to establish a form of use value taxation for farmland (See *Background Information*). Yet another approach has been proposed; this one would allow owners of working farmland to seek an open space development rights easement under Part 361 of the Natural

Resources and Environmental Protection Act. The open space provisions are a companion to the farmland preservation program, known as PA 116, found in the same part of NREPA. When an open space development easement is granted, the right to develop the property is surrendered for some period of time (from 10 to 90 years), and the surrendered development rights are no longer subject to ad valorem taxation. This means that farmland would then essentially be taxed based on its value as working farmland and without regard to its value for development if sold.

THE CONTENT OF THE BILL:

The bill would allow an owner of farmland to apply for an open space development rights easement. If granted, the development rights would be exempt from ad valorem taxation; only the value of the farmland minus the development rights would be subject to tax. [This would produce a form of "agricultural use value" taxation for farmland.]

The bill would accomplish this by amending Part 361 of the Natural Resources and Environmental Protection Act (NREPA) to change the definition of "open space land" to include farmland. Specifically, the definition would be amended to include an area approved by the local governing body and the preservation of which in its present condition would conserve farmland.

The bill would require the state to reimburse intermediate school districts, local school districts, community college districts, and the School Aid Fund for revenues lost as a result of the exemption of open space development rights held by a local government.

The section being amended in Part 361 allows an owner of open space land to apply to the local governing body for an open space development rights easement. An approved application contains a statement specifying the current fair market value of the land and the current fair market value of the

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development rights. The development rights are exempt from ad valorem taxation. The local governing body approves or rejects an application based on rules promulgated at the state level after considering the comments and recommendations of various reviewing entities (which would include the county planning commission, regional planning commission, and soil conservation district). An application that is rejected can be appealed to the Department of Agriculture. However, House Bill 5808 would not permit an applicant to appeal if the land in question was farmland.

An open space development rights easement can have a duration of from 10 to 90 years and can be renewed automatically at the request of the landowner. If a landowner terminates early, he or she has to pay the taxes not paid on the development rights plus interest on that amount at six per cent per year compounded. Upon the natural termination of an easement, the landowner must pay the taxes on the development rights for the previous seven years. The act allows for the relinquishment of an open space development rights easement 1) at any time the local governing body determines that the development of land is in the public interest, with the agreement of the landowner; or 2) upon the application of the landowner.

Land for which an open space development rights easement has been approved cannot have structures built on it or have an improvement made to it without approval of the local governing body. House Bill 5808, however, would make an exception for farmland by permitting a structure to be built without approval if its use was consistent with farm operations, including a residence for an individual essential to the operation of the farm and for lines for utility transmission or distribution purposes. The bill would also permit improvements to be made without local approval for a use consistent with farm operations.

Farmland would not be eligible for an open space development rights easement if it was subject to a farmland development rights agreement or an agricultural conservation agreement or the purchase of development rights, and farmland subject to an open space development rights easement would not be eligible for a farmland development rights agreement or an agricultural conservation agreement or for purchase of development rights.

MCL 324.36101 and 324.36106

BACKGROUND INFORMATION:

Earlier in this legislative session, the House passed House Bill 4456, which would create the Alternative Agricultural Production Tax Act, under which farmland could be exempted from the general property tax and instead be subject to an alternative tax based on agricultural use value. The alternative tax would only apply when an exemption certificate had been approved by the local unit of government and the State Tax Commission. For a fuller description of this bill, see the analysis by the House Legislative Analysis Section dated 6-13-01. During the 1999-2000 legislative session, the House debated House Joint Resolution R and House Bill 5779, which would have put the concept of agricultural use value into the state constitution and into the General Property Tax Act, respectively. House Joint Resolution R was unable to garner the necessary two-thirds vote. For a description of that legislation, see the analysis of House Joint Resolution R dated 5-23-00 by House Legislative Analysis Section.

FISCAL IMPLICATIONS:

Fiscal information is not available.

ARGUMENTS:

For:

Proponents say this bill represents a step in the right direction toward taxing farmland on its agricultural use value rather than on its development potential. The bill would use the existing open space preservation program, which requires local unit approval of a tax exemption for surrendered development rights. It allows farmers to choose whether to participate in the farmland preservation program or the open space program. Moreover, it allows some farmers not eligible for the farmland preservation program (due to income guidelines) to put land into the open space preservation program. It will provide some tax relief and some protection from the pressure to develop farmland. It will offer local communities an additional tool to use in combating so-called urban sprawl and in protecting their rural quality. While it is not a large-scale solution to the problem of farmland taxation, it does offer some farmers an opportunity for tax relief and offers some protection against development pressures.

Response:

A typical concern with preservation programs is that they not serve simply as a means for landowners to reduce costs temporarily (through reduced taxes) and

then later develop the property when it is advantageous. The way to discourage this is by assessing significant penalties for leaving the program. Legislators will have to determine whether the penalties under this bill are sufficient to encourage long-term preservation of farmland.

Against:

Critics of similar proposals in the past have expressed concern about their fiscal impact. This bill would hold schools and community colleges harmless by requiring that the state reimburse them for lost revenue. But this will mean lost general fund revenues to the state for other programs.

Response:

Supporters of the bill say the impact should be minimal. Earlier proposals would have assessed all farmland based on agricultural use value or would have created special zones in which farmland was so assessed at the farmer's request. This bill requires farmers to seek an open space easement from local officials on a case-by-case basis, and is likely to have lower participation than earlier proposals.

POSITIONS:

The Michigan Farm Bureau supports the bill. (4-16-02)

A representative of the Michigan Townships Association testified in support of the bill. (4-16-02)

A representative of the Department of Agriculture testified that the department has no position on the bill at present and is working with the Department of Treasury to determine the bill's impact. (4-16-02)

Analyst: C. Couch

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.