

**DEV'T RIGHTS AGREEMENT OR
EASEMENTS ON FARMLAND**

House Bill 4083 as enrolled
Public Act 36 of 2003
Second Analysis (7-14-03)

Sponsor: Rep. Dale Sheltrown
House Committee: Agriculture and
Resource Management
Senate Committee: Natural Resources
and Environmental Affairs

THE APPARENT PROBLEM:

Under the Farmland and Open Space Preservation Act - formerly Public Act 116 of 1974 and recodified as Part 361 of the Natural Resources and Environmental Protection Act - a farm owner may enter into a contract (a development rights agreement) that provides the farm owner with a tax credit and exemptions from several special assessments that generally do not benefit the farmland, in exchange for a promise to retain the land for agricultural use or as undeveloped open space land. The purpose of the agreement is to ensure that the land remains in agricultural use for at least 10 years and that the land not be developed for a non-agricultural use. According to committee testimony, there are approximately 50,000 of these agreements, lasting an average of 25 years, and covering 4.3 million acres of farmland in the state.

The act states that a development rights agreement or easement does not supercede any prior lien, lease, or interest in the property that is subject to the agreement or easement, and any lien recorded under Part 361 is subordinate to a lien of a mortgage that is recorded before a lien under the act is recorded - meaning that a development rights agreement or easement has priority over any subsequently recorded lien, lease, or interest. Reportedly, several landowners enrolled in the PA 116 program have experienced problems when they attempted to refinance a portion of their property, due to the existence of the developments rights agreement on their property. As such, legislation has been introduced to help alleviate the problem.

THE CONTENT OF THE BILL:

The bill would amend Part 361 of the Natural Resources and Environmental Protection Act (NREPA) to require the state to subordinate its interest in a recorded farmland development rights

agreement or an open space development rights easement to a subsequently recorded mortgage lien, lease, or interest if the parcel of land meets certain requirements. In essence, the state would grant priority to mortgage liens or interests in property that is also subject to a development rights agreement or easement.

For the state to subordinate its interest, the property would have to meet certain conditions set forth in sections 36111(2) (a) of the act. For purposes of the bill, the mortgage would have to be for a parcel of land on which (a) the structures were present prior to the recording of the development rights agreement (generally up to two acres, but up to five acres in some instances); or (b) a new residence will be constructed (up to two acres).

In addition, the landowner requesting the subordination would have to be an "individual essential to the operation of the farm", defined in section 36110 to mean an individual who cultivates, operates, or manages farmland and (1) who has a financial interest greater than or equal to half of the cost of producing crops, livestock, or products, and inspects, advises, and consults with the owner on production activities; or (2) who works at least 1,040 hours annually in activities connected with the production of the farming operation.

MCL 324.36103

BACKGROUND INFORMATION:

Eligibility for the PA 116 program is determined by the size of the farm and, in certain instances, the income of the farm. To be enrolled in the program, the land must be 40 acres or more with at least 51 percent in active agricultural use; between 5 acres and 40 acres with more than 51 percent in active

agricultural use, and producing a gross annual income in excess of \$200 per tillable acre; or the farm must be designated as a specialty farm by the Department of Agriculture, be at least 15 acres in size, and have a gross annual income in excess of \$2,000 per year.

Farmland must be enrolled in the PA 116 program for a minimum of 10 years, and may be extended in at least 7-year increments with the maximum length of the enrollment being 90 years. When the agreement expires, the landowner is responsible for repaying the tax credits received during the previous 7 years. If that money is not paid within 30 days, a lien is placed against the property.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill would have no fiscal impact on the state or on local units of government. (HFA fiscal analysis dated 3-27-03)

ARGUMENTS:

For:

Under Part 361, a lien of a mortgage that is recorded with the office of the register of deeds is subordinate to a previously recorded lien created under Part 361 in favor of the state or a local unit of government. As such, if a landowner wants to refinance an existing mortgage or execute a new mortgage, that mortgage would be subordinate to a previously recorded development rights agreement under Part 361. As a result, some financial institutions have refused to refinance a mortgage or execute a new mortgage, or have provided the mortgage at a higher interest rate, because of the development rights agreement on the property. In some instances, this has proven to be a financial burden on landowners as they have been unable to refinance mortgages and take advantage of lower interest rates or else have not been able to obtain a new mortgage, possibly preventing them from building new structures.

A landowner could withdraw from (or not renew an agreement for) the PA 116 program in order to refinance an existing mortgage or obtain a new mortgage. However, getting out of the program creates several problems. First, the landowner would be required to repay any tax credits received during the previous seven years. Second, the process for doing getting out of the program could take a long time, causing the landowner to miss the opportunity to refinance at a lower rate. Finally, once the landowner is released from the PA 116 program, he

or she may choose to not re-enroll once the mortgage is obtained. This, clearly, goes against the entire purpose of the program in the first place. As such, the bill is seen by some as an incentive to the landowner to remain enrolled in the program, thereby furthering the push to preserve farmland.

The bill would address this problem regarding the priority of liens by requiring the state to subordinate its interest in a development rights agreement or easement. This would provide an affected landowner with the opportunity to refinance an existing mortgage or seek a new mortgage without the interference of the state's interest in the property.

It should be noted that the bill does not create any substantial risk to the state, as it often enters into a development rights agreement notwithstanding an existing mortgage on the property. Again, if a person has a mortgage that predates the recording of the agreement, that mortgage has priority over the agreement. The bill would simply permit the landowner to refinance the mortgage and still have priority over the agreement.

Against:

As originally drafted, the bill would permit - rather than require - the state to subordinate its interest in a recorded agreement or easement. In its final form, the bill forces the state to subordinate its interest even when doing so is not in the state's best interest.

Response:

Some believe that financial institutions would still be hesitant to refinance an existing mortgage, would deny an applicant a new mortgage, or would offer a mortgage at a higher interest rate, without an explicit requirement that the state subordinate its interest. If this happened, the bill would fail to achieve its purpose.

Analyst: M. Wolf

■ 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.