



Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536



BILL ANALYSIS

Telephone: (517) 373-5383
Fax: (517) 373-1986
TDD: (517) 373-0543

House Bill 4702 (Substitute S-1 as reported)
Sponsor: Representative Bruce Caswell
House Committee: Tax Policy
Senate Committee: Finance

Date Completed: 2-23-04

RATIONALE

Local assessors and county equalization departments use "sales ratio studies" in making appraisals and equalizations for particular classifications of real property. By comparing the assessed value and the sale price for each parcel of property sold, assessors are able to determine whether overall assessments need to be adjusted, in order to meet the constitutional requirement that a parcel's assessment equal 50% of its true cash value. (The equalization process compares similar parcels within a county or around the State in order to "equalize" their assessed values.) If the sale price for a parcel is considerably higher or lower than the prices of similar parcels, the area's sales ratio study may be affected.

When farmland is sold for nonagricultural purposes, the sale price typically is much greater than it would be if the property were purchased for farming. Since it is not uncommon for developers to buy farmland, there is concern that these sales are skewing sales ratio studies, and indirectly raising the assessment of remaining farmland. It is been suggested that assessors and equalization departments should disregard the sale of farmland sold for nonagricultural use, when making appraising property and making sales study ratios.

CONTENT

The bill would amend the General Property Tax Act to require assessors, in making sales ratio studies and appraisals, to exclude from the sales data all sales of agricultural real property that was not sold for agricultural use.

Specifically, before using sales data on real property purchases, including land contract purchases, in making sales ratio studies and appraisals to assess real property classified as agricultural real property, a city or township assessor, a county equalization department, and the State Tax Commission would have to exclude from the sales data all sales of agricultural real property for which an affidavit had not been filed under Section 27a(7)(n) of the Act. Sales data excluded under this provision could be included in a sales study or appraisal, however, if both the local assessor and the county equalization director agreed to include the sales data. (Under Section 27a(7)(n), a transfer of ownership, for the purpose of assessing property at 50% of true cash value, does not include a transfer of qualified agricultural property, if the person to whom it is transferred files an affidavit with the local assessor and register of deeds, attesting that the property will remain qualified agricultural property.)

MCL 211.8 & 211.27

BACKGROUND

Under Article IX, Section 3 of the State Constitution, the assessed value (or State equalized valuation) of a parcel of property must be based on 50% of its true cash value. A parcel's assessed value is not usually the same at its *taxable* value, which determines the amount of taxes the owner must pay. Article IX, Section 3 provides that a parcel's taxable value (adjusted for additions and losses) may not increase from one year to the next by more than 5% or the increase in the consumer price index, whichever is lower, until there is a transfer of ownership. At that

time, the assessment is “uncapped” and the parcel again is taxed at 50% of its true cash value.

When the property values in an area consistently rise faster than the rate of inflation or 5% per year, there may be a growing disparity between a parcel’s assessed value and its taxable value. As a result, the new owner of a parcel may pay taxes significantly higher than those paid by the seller. Several years ago, it was pointed out that these so-called pop-up taxes could be particularly burdensome to people purchasing farmland, because such sales usually involve substantial tracts of valuable acreage; it was feared that the higher taxes would discourage people from buying farmland in order to keep it in agricultural use.

To address this concern, Public Act 260 of 2000 amended the General Property Tax Act to specify that a transfer of ownership does *not* include the sale of qualified agricultural property, if the transferee files an affidavit with the local assessor and register of deeds attesting that the property will remain qualified agricultural property. In that case, the taxes remain “capped” for the buyer. (“Qualified agricultural property” means unoccupied property and related buildings classified as agricultural, or other unoccupied property and related buildings located on property devoted primarily to agricultural use.)

The Agricultural Property Recapture Tax Act, created by Public Act 261 of 2000, imposes a

recapture tax on transferred agricultural property that ceases to be used for agricultural purposes. The recapture tax essentially represents the difference between the amount of taxes paid on the property while the taxes were capped, and the amount that would have been imposed if the assessment had reverted to 50% of true cash value upon the transfer, for a period of up to seven years before the property’s use was changed. Revenue from the recapture tax is deposited in the Agricultural Preservation Fund.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Agricultural property is unique because of the extent to which it is sold for a different purpose. When a person buys residential property, he or she nearly always intends to keep it in residential use. The same is true when commercial and industrial property is sold. Farmland, on the other hand, is commonly purchased by developers, who plan to convert the property to residential or commercial use, or build an industrial facility on it. Developers also are willing and able to pay a considerably higher price than an individual would pay to keep the land in farming. As a result, this type of sale is far more likely than others to distort sales ratio studies. The bill’s sponsor offered the following example of a sales study:

Farmland Sold for Ag & Non-Ag Use

		Taxable	Assessed	Sale Price	Ratio
Parcel 1	stays in ag	\$55,000	\$75,000	\$160,000	47%
Parcel 2	developed	\$50,000	\$70,000	\$250,000	28%
Parcel 3	developed	\$70,000	\$100,000	\$400,000	25%
Parcel 4	stays in ag	\$70,000	\$100,000	\$210,000	48%
TOTAL		\$245,000	\$345,000	\$1,020,000	34%

Farmland Sold for Ag Use Only

		Taxable	Assessed	Sale Price	Ratio
Parcel 1	stays in ag	\$55,000	\$75,000	\$160,000	47%
Parcel 4	stays in ag	\$70,000	\$100,000	\$210,000	48%
TOTAL		\$125,000	\$175,000	\$370,000	47%

Since 50% is the optimum ratio at which no adjustment in assessments is needed, anything under that threshold should be raised to reach that mark. Thus, according to the 34% ratio produced by including all sales in the study, assessments should be increased by 16%. If the study looked solely at the parcels kept in agricultural use, however, assessments would need to be increased only by 3%.

As a result of the current system, in which all sales are included in sales ratio studies, farmland is being overassessed. Although increased assessments do not affect the amount of taxes paid by current owners of farmland, the assessments will boost the "pop up" taxes that purchasers must pay (unless they file an affidavit under Section 27a). Excluding sales of farmland for nonagricultural use from sales ratio studies would produce more realistic studies and assessments, and promote the use of agricultural property for farming.

Response: Since property taxes on farmland are uncapped only when the land is sold for nonagricultural use, it not clear how this proposal would benefit current and future farmers, since increased assessments affect the taxes paid only by those who buy farmland for nonagricultural use. The bill actually could produce more speculation and sprawl by reducing the amount of the recapture tax that would have to be paid by someone who bought farmland and then decided to develop it after, say, five years.

Opposing Argument

The bill would violate Article IX, Section 3 of the State Constitution. According to the Convention Comment, "The important constitutional objective is *uniformity of assessment...*" (emphasis added). This section requires the Legislature to provide for the uniform taxation of property; the determination of true cash value of property; the proportion of true cash value at which

property must be assessed (which may not exceed 50%); and a system of equalization of assessments. The bill, however, would treat agricultural property differently from all other classifications, as well as provide for separate treatment of different parcels of farmland.

The bill also would undermine the State Tax Commission's discretionary authority and its ability to review decisions of local assessors and county equalization departments. Under the bill, the Tax Commission, as well as assessors and equalization departments, would have to exclude from sales ratio studies sales of farmland for nonagricultural use. At the same time, only local assessors and equalization departments could agree to include sales data that otherwise would have to be omitted. This would leave an unwarranted amount of discretion at the local level, and create the opportunity for assessing officials in different local units to make disparate decisions. The officials in one county could agree to keep data on all of the sales in their sales ratio study, while another county's officials could exclude the data on similar property sold for nonagricultural use.

Under the General Property Tax Act, the State Tax Commission has general supervisory authority over the assessing officers of the State. The Commission is required to review and investigate all complaints that property is improperly assessed, and correct irregularities that are found to exist. In essence, the Commission is responsible for ensuring that property is assessed as required by Article IX, Section 3. Under the bill, however, the Commission could not fulfill that responsibility.

Opposing Argument

The bill would be unfair to owners and purchasers of nonagricultural property, who also may be affected when one parcel sells for far more than other property in an area. This may occur with any classification of property, even if there is no change in use. In a

residential area, for example, one home might sell for an amount that is twice the price paid for any other similar house in the area. Nevertheless, that sale will be included in the sales ratio study, and could inflate the assessment of all other residential property. Although the current homeowners' taxable values would not be affected, the increased assessment could make it more difficult for them to sell their homes in the future.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would have an indeterminate impact on State and local revenues. Changes in taxable values would be affected in an indeterminate direction, if at all, depending on what properties were excluded from sales studies. Without knowing both the value of the properties that would be excluded from a study and the value of properties included in the study, it would be impossible to estimate the impact of the bill. Depending on a wide variety of factors, the bill could result in taxable values for most properties rising at a higher or lower rate or the same rate as under current law. In recent years, the binding constraint on changes in taxable values has been the change in the consumer price index under Article IX, Section 3 of the Michigan Constitution. In years in which the change in the consumer price index is below the rate determined by the sales study, the bill would have no impact. Similarly, in years when the 5% cap on increases in taxable values, contained in the same section of the Michigan Constitution, is effective, the bill would have no effect. The biggest potential effect of the bill, although also indeterminate, would be on property sold during a year because such property is not bound by either the consumer price index or 5% constitutional limitation on its taxable value change in the year it is sold.

Fiscal Analyst: David Zin

H0304\s4702a

This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.