

LR 566 was introduced in 2014 by Senator Hadley, Revenue Committee chair, regarding valuation of agricultural and horticultural land in Nebraska. The purpose of this resolution was to study valuation methods used in other states for comparison to Nebraska's current method and to model a reduction from 75 to 65 percent of market value for assessment of agricultural and horticultural land. A report was issued on December 9, 2014, by committee staff. This document is an executive summary of that report.

I. History and Current Policy.

Nebraska's property tax is rooted in the state constitution. There have been many constitutional challenges and changes over the years. Specifically, the Uniformity Clause has been the primary driver of these issues, particularly as it applies to valuation of agricultural and horticultural land ("Agland.") Three major changes have shaped the application of the Uniformity Clause to Agland valuation.

Prior to the mid-1980's, Agland was valued using a statutory income or earnings method. A constitutional amendment had also been passed which allowed Agland to be treated as a separate class of property. However, the amendment made no change to the Uniformity Clause, which left open the question of whether Agland still had to be valued uniformly with all other classes of property.

A lawsuit was filed by taxpayers who believed their Agland had been overvalued. The Nebraska Supreme Court ruled for the taxpayers finding:

- Since there had been no change to the Uniformity Clause as part of the constitutional amendment, Agland could be classified separately but must still be valued uniformly with all other real and personal property;² and
- The earnings capacity formula specified in the assessors' manual would have been allowable had the resulting values been "correlated to be proportionate with all other real and tangible personal property."

In 1990, another constitutional amendment did create an exception to the Uniformity Clause for Agland, providing that it could be valued differently from all other classes of property but adding language that the results must be "uniform and proportionate upon all property within the class of agricultural land and horticultural land."

Finally, in 2007, the ratio of assessed value to market value for Agland was reduced from 80 percent to the current 75 percent standard. State policy now provides for assessments to be made based on a market or sales comparison approach to determine the actual value for each class and subclass of

¹ Bill Lock, Revenue Committee Staff

² *Banner County v. State Bd. of Equal.*, 226 Neb. 236, 411 N.W.2d 35 (1987).

agricultural and horticultural land.³ The income approach to valuation may be used to determine the actual value for each class and subclass of agricultural and horticultural land but the market or sales comparison approach is preferred in the valuation of agricultural land.⁴

II. Comparison with Other States.

Nebraska's Agland valuation policy is different from our neighboring states for various reasons. Few if any states have a uniformity provision as strictly construed as Nebraska. All of our neighboring states⁵ use an income valuation approach which includes a comparable sales factor, but sales carry less weight in the determination of value than in Nebraska. The ratio of assessed value to market value is also much lower in these states, ranging from eight to 85 percent of market value. Whereas Nebraska uses a three-year average for assessment, these states range from five to eight to 10 year averages for their assessment methods. This would appear to make their assessment methods less accurate in terms of the impact of commodity prices, input costs and comparable sales. It creates a larger lag effect than in Nebraska. As a result, these states saw double-digit increases in values begin later than in Nebraska. These increases will likely continue for a longer period of time too, assuming Agland sales prices decline for a period of time. It should be noted of course that some of our neighboring states, such as Colorado, have a much lower percentage of Agland acres than Nebraska, which allows them to utilize different tax policies.

It is worth noting that many of our neighboring states have also reduced the ratio of assessed value to market value for residential real property. This has the effect of shifting more of the property tax burden to commercial and industrial (business) property. Other mechanisms must then be used to address requests for equal treatment from business property owners. Kansas, for example, has used property tax abatements at the local level and Iowa budgeted \$100 million last fiscal year for business property tax relief.

As a result, Nebraska's property tax base is much broader and much stronger than our neighboring states. While Nebraska continues to rely heavily on the property tax as a source for school finance, other states have weakened their property tax base requiring a shift to income and sales taxes which are not as broad or as resilient as the property tax. Faltering tax receipts in these categories and/or significant cuts to these taxes have led to litigation and other significant issues relative to school finance (e.g. Kansas).

The tax expenditure (foregone taxes) cost of the current Agland policy was \$415 million in 2013.

³ REG-14-006 VALUATION OF AGRICULTURAL AND HORTICULTURAL LAND 006.01.

⁴REG-14-006 VALUATION OF AGRICULTURAL AND HORTICULTURAL LAND 006.03.

⁵Colorado, Kansas, Iowa, Missouri, South Dakota and Wyoming.

III. Impact of a 75-65 Reduction in Agland Assessment

The primary effect of “75-65” at the state level would be an increase in TEEOSA aid⁶ in the \$29-\$30 million range. Other local taxing districts will likely increase their tax rates as valuation for other classes of real property will not increase sufficiently to offset the reduction in taxes paid by Agland owners and to cover annual budget increases.

The reduction in Agland value and tax amount will vary across the state. One of the driving factors is how much of the taxing district’s total property value is comprised of Agland. The higher the percentage of Agland property to total property, the lower the amount of the reduction in value and tax amount will be. Put another way, Agland owners in taxing districts with very little Agland in the district would see the greatest amount of relief in terms of value and tax amount. In these districts the reduction will create a shift to residential and commercial property. If the majority of value in the district is Agland, the reduction in assessed value cannot be shifted to other property and will require an increase in rate to the point where the value reduction loses much of its dollar impact for Agland owners. [See Table 4, page 15 of original report.]

IV. Policy Options

The final section of the report simply lists various policy options that might be considered by the Legislature to address both Agland property taxes as well as property taxes in general. These include:

- 75-65 for Agland;
- Property tax credit for Agland only;
- Residential credit programs;
- Circuit breakers; and
- Reductions in personal property tax.

Any policy change regarding Agland taxes or property taxes in general will necessarily require close scrutiny to determine whether the proposed change meets the strict requirements of Nebraska’s Uniformity Clause.

To read the original report, go to:

http://nebraskalegislature.gov/pdf/reports/committee/revenue/2014_lr566.pdf

⁶ TEEOSA aid does not include special education, property tax credit, homestead or temporary school fund distributions received by each school.