

First Year in the Field: Special Agricultural Homestead Provisions in Retrospect

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Although I have 20-plus years of broad-ranged fee appraisal experience, a rural landscape has always been part of my milieu. When the opportunity came up last year to switch my focus into ad valorem taxation valuation, I hesitated no longer than a nanosecond to accept this challenge. I soon realized that many, if not most, of the valuation principals apply equally as well to assessors as they do to fee appraisers. In that respect, you probably can “make a silk purse (assessor) out of a sow’s ear (fee appraiser). At the basic level, the primary differences in the two professions are in the documentation and reporting of the value conclusions as referenced in “Standard 2: Real Property Appraisal, Reporting” and “Standard 6: Mass Appraisal, Development and Reporting” of the Uniform Standards of Professional Appraisal Practice (USPAP).

If the assessment field in Minnesota had remained primarily as a valuation process rather than a classification process, fee appraisers such as myself could easily be transformed into assessors. After all, they have highly developed mathematical and analytical skills, they have taken the requisite appraisal courses to obtain and maintain their licenses, and they have gained valuable valuation experience in the market in which they specialize. Unfortunately, that is 180° away from the direction the Minnesota assessment system has gone. Article X of the Constitution of the State of Minnesota states that property taxes will be uniform upon the same class of subjects and will be levied for public purposes. To remain true to this “uniformity clause” mandate while striving for still loftier socio-economic goals, modern day legislatures have systematically expanded the property classes, tiers, homestead classifications, education credits, limited market values, and exemptions to incomprehensible levels. We may have uniform and equitable valuation in the Minnesota property tax system, but the net tax burdens within and among the broad property classes are a far cry from being uniform and equitable.

Because of public pressure in the last decade, there have been incremental steps taken by the legislative branch to soften these inequities by making the economically desirable classes more inclusive or expanding the benefits or exemptions within certain classes. We have seen the three residential homestead tiers reduced to two, all of the class rates periodically reduced, the benefit limits raised for most classes, and large scale expansion of the education homestead and education agricultural credits.

We have also seen the creation of the 4d Property Tax Classification, the “This Old House” program, and the Special Agricultural Homestead or “Active Farmer” program. Although each of the programs was designed for a different class of property, they were all intended to soften the tax burden for qualifying property owners in each class who choose to jump through a series of hoops. There is no question that the benefits are substantial for those individuals who qualify, although none of the programs require means testing. Only the recipients would be brash enough to presume that they are more “worthy” of a tax break than those that don’t receive it. Don’t the benefit recipients owe a huge dept of gratitude to the

non-beneficiaries who have to “pay the freight” for financing the others’ tax cuts?. This article will specifically concentrate on the “Active Farmer” program from a county perspective, how it was implemented the first year, and how the program participants benefited.

The 1999 Minnesota Legislature passed legislation for the Special Agricultural and made it retroactive to January 2, 1999 assessment year. Minnesota Statute Subd. 14, Par. (b), the core of the “Active statute, is not lengthy, but it did leave the of certain terminology up to the Property of the Department of Revenue. (See panying box.) The authors of the probably had no idea that the terms farming” or “farther than four townships were ambiguous.

Identification

Even before we knew the full implication of the Active Farmer legislation, we needed to identify those farm owners who might qualify for the program. By definition, they needed to be owners of class 2a, 1b, 2b, or 4b property and who were not yet receiving an agricultural homestead. The initial list included a total of 1,495 parcels. From that list of owners of all non-homestead farms, a unique screen was done to eliminate duplicate names, as were all of the property owners with addresses beyond the seven counties adjoining Steele County. With that, we now had a mailing list of 264 unique names of individuals who owned farms in Steele County that were non-homestead and were potentially eligible to receive the “Special Agricultural Homestead” classification.

To these names, we mailed Form 5-DORHST-8/99 “Application for Special Agricultural Homestead” which requested the owner’s name, social security number, and marital status, the Parcel Identification Numbers of those parcels for which homestead was being claimed, whether the owner or spouse was receiving or claiming another agricultural homestead, whether the owner was listed as an owner/operator by the Farm Service Agency, and whether the owner filed a Schedule F with his tax return for the most recent tax year. The cover letter from our office that went out with the mailing, also requested the number of acres actively farmed for each parcel ID, the owner’s extent of involvement in the day-to-day farming decisions, labor, administration, and management, the owner’s exposure to financial risk and participation in the profits and losses, and to return their completed questionnaires with a copy of their 1998 Schedule F.

Actively Engaged

As the letters were going out, the Department of Revenue Property Tax Division was busy determining the minimum qualifications for an “active farmer.” To be “actively farming”, a person must:

- 1) participate in making day to day farm decisions,
- 2) participate in the day to day labor, administration, and management of the farm,
- 3) assume all or a portion of the financial risks of the farming operation,
- 4) participate in any profits or losses of the farming operation.

Minn. Stat. 273.124, Subd. 14:
(b) Agricultural property consisting of at least 40 acres shall be classified homestead, to the same extent as other agricultural homestead property, if all of the following criteria are met:
(1) the owner is actively farming the agricultural property;
(2) the owner of the agricultural property is a Minnesota resident;
(3) neither the owner nor the spouse of the agricultural property claims another agricultural homestead in Minnesota; and
(4) the owner does not live farther than four townships or cities, or a combination of four townships or cities, from the agricultural property.

the enabling Homestead for the 1999 273.124, Farmer” interpretation Tax Division accom- legislation “actively or cities”

These requirements seem straightforward enough until you realize that there are many different ways to hold title to farmland, many different types of lease agreements, and many different explicit and implicit management arrangements. Besides family farm corporations, farm partnerships, and life estates, there are an indeterminate number of father/son, mother/son, brother/brother, brother/sister, uncle/nephew, grandfather/grandson ownership arrangements in Steele County and even more unstructured management arrangements. The principals in the corporations and partnerships that were set up to avoid paying social security taxes were understandably upset when they didn't qualify. Corporations and partnerships are the entities assuming the risk and sharing in the profits and losses, not the individuals. (Note: The 2000 Minnesota Legislature extended the Special Agricultural Homestead provisions to family farm corporations, joint farm ventures, limited liability companies, and partnerships, with requirements similar to individual ownership.) Likewise, the farmer who "retires" and moves to town, but still helps his son out on a daily basis at the farm, is not at all uncommon. He does not file a Schedule F because his earnings would exceed the minimum he could earn and still draw full social security retirement benefits. He has some type of lease arrangement or contract for deed sale with his son to provide him with an income, but in either event he would not qualify as an "active farmer" because he is not sharing in any of the financial risks and he is not participating in any of the profits and losses of the farming operation. (Note: The 2000 Minnesota Legislature extended the Special Agricultural Homestead provisions to owners whose son or daughter is actively farming the property, providing all of the other requirements are met.) There seems to be no situation in which an individual can qualify for a Special Agricultural Homestead if that person has not filed a Schedule F for the previous year. Even a beginning farmer will not qualify until the following January 2, after which he will have filed his first Schedule F.

Applications Received

From the time of the mailing in November, 1999 until the filing was closed in April, 2000, a total of 43 applications were received. Considering that a number of applications were picked up at the counter and a number were passed out at inspections for other reasons, approximately one application was received for every six letters mailed.

Rather than elucidate all of the different situations that might arise, it might be more enlightening to recite a couple of real-life case studies.

Case Study A

The Albers family (not real name) has had one of the premier dairy herds in Steele County for many years. It has been a tradition for four generations to name the first-born son John. The string was broken in the fifth generation nearly 30 years ago when the family named their first son Ray. The current patriarch, John F. Albers III, is known as John Sr. and owns a residence at the head of the driveway to the main farmstead with an address of 3149 Aggie Road. His son, John R. Albers IV, is known as John Jr. and has lived in the 2-story home on the farmstead at 3209 Aggie Road for his whole life. In June, 1999 John Jr. and his wife purchased a home in a rural subdivision three-fourths mile up the road at 2752 Aggie Road. Ray J. Albers had lived in a mobile home on the same farmstead at 3207 Aggie Road, but moved into his parents 2-story home following his marriage in the summer of 1999. Besides always having lived within a mile of each other, this close-knit family has always worked together in the dairy operation.

All of this background information was unbeknownst to the appraiser when he stopped at 3149 Aggie Road for a follow-up inspection on a building permit. The address was wrong on the building permit,

but John Sr. thought the work was probably done at the farm homestead. Ray said that building permit was actually for interior remodeling on his parents recently purchased home, but they also had a permit to put up a 123,500 bushel grain bin. At the inspection of the interior remodeling at 2752 Aggie Road, most of this information came to light. John Jr. had always lived on the farm that he operated and of course wouldn't have received the mailing about the Special Agricultural Homestead provisions. He normally would have lost the homestead benefits on the 813 acres of farmland that he owned by moving off the farm and into a residential-class homestead. There was no question that he would qualify for and benefit from a Special Agricultural Homestead for the 2000 assessment. On the other hand, Ray had qualified John Junior's mobile home for a relative homestead classification, but the 155 acres of farmland that he bought from John Sr. had always been classified as non-homestead. Ray now qualified for and benefited from a Special Agricultural Homestead for the 1999 assessment, as well as the 2000 assessment and beyond when the relative homestead was switched from the mobile home at 3207 Aggie Road to the 2-story home at 3209 Aggie Road.

This case study illustrates the benefits of the Special Agricultural Homestead to both a semi-retiring farmer moving off the farm and a young beginning farmer who is doesn't own his own home. Their situation sounds like a postman's and assessor's nightmare, but it turned out to be a winning situation for everyone involve.

Case Study B

The Stewart family (not real name) consists of the father, Roger F. Stewart, Sr., and his sons, Roger A. Stewart, Jr. and Michael J. Stewart. Roger Sr. lives in a home in the county seat of an adjoining county, owns 80 acres of farmland in Steele County, and owns a 566-acre of farm in the southwest part of the adjoining county which Roger Jr. lives on, farms, and qualified for a relative homestead. Besides leasing his dad's farm and others, Roger Jr. also owns about 1,200 acres in his home county, cropland in another adjoining county, and 426 acres in Steele County, plus an additional 160 acres in Steele County which he purchased in March, 1999. Michael built a new home on his brother's land in the east-central part of the first adjoining county, owns 65 acres in his home county and 100 acres in Steele County, plus an additional 160 acres in Steele County which he purchased in March, 1999.

Both Roger Jr. and Michael had applied for the Special Agricultural Homestead in Steele County as a result of our mailing, but only Roger Jr. had applied in his home county. The decision regarding both Special Agricultural Homestead applications obviously rested with their home county. Roger Jr. had qualified Roger Senior's farm for a relative homestead, but a person can not receive two agricultural homesteads under different MP numbers. The Stewarts needed to decide, first of all, if they wanted Roger Sr. to continue receiving a special relative agricultural homestead on his farm or if Roger Jr. would receive a Special Agricultural Homestead on his farms in his home county, Steele County, and the other adjoining county. Michael seemingly qualified for a Special Agricultural Homestead on his farms in his home county and Steele County, depending on how the house he built on his brother's land was classified.

This case study illustrates the complexities involved in working across county lines and making sure the left hand knows what the right is doing. There were numerous phone calls, faxes, and e-mails between the three counties involved before the situation was resolved. Both brothers ended up qualifying for the Special Agricultural Homestead, although only Michael realized its benefits. Likewise, the computer tax system needs to know the specifics for the parcel(s) that qualify the taxpayer for the Special Agricultural Homestead, but which are not full agricultural homestead properties in Steele County. Cross-

county information on qualifying taxpayers from each of the six adjoining counties, as well as fractional homestead information, is dumped in a non-calculating carryover file.

Determinations Made

As the applications were coming in, a great deal of time was spent verifying the information. What is the classification was for all the parcels? Where did the owners live on January 2? Do they own or rent a residence? If they rent, are they related to the owner? Do they own agricultural land in another county? How far are the parcels located from the home? Oftentimes a relative of the applicant was discovered who qualified for the Special Agricultural Homestead, even though the original applicant was denied that benefit. The results of the selection process were as follows:

REJECTED APPLICATIONS

	APPLICATIONS		PARCELS		ACRES	
	COUNT	%	COUNT	%	COUNT	%
Already Ag Hmstd	7	47%	42	68%	2,428	61%
Keeping Rel Hmstd	1	7%	2	3%	352	9%
> 4 Twps Away	1	7%	3	5%	160	4%
Not Active/No Sch F	5	33%	14	23%	1,007	25%
Not Classified Ag	1	7%	1	2%	14	0%
TOTALS ----->	15	100%	62	100%	3,960	100%

The most common reason for the rejection of an application was that the farm owner was qualified for or already receiving an agricultural homestead on at least part of his ownership interests. Some individuals thought that they could get a homestead on their mother’s or brother’s land that they farmed and some thought they could reset their \$600,000 benefit limitation and start over at the 0.35% class rate with the new program. Those persons who indicated that they rented their land out or did not include their Schedule F with their application were denied a homestead because they were not actively engaged in farming. A few individuals needed to do a cost/benefit analysis and decide between keeping a relative homestead where they lived or receiving a Special Agricultural Homestead on the agricultural land that they owned.

Approximately two-thirds of the applications received were accepted. The final picture looked as follows:

ALL APPLICATIONS RECEIVED

	APPLICATIONS		PARCELS		ACRES	
	COUNT	%	COUNT	%	COUNT	%
Rejected Applications	15	35%	62	38%	3,960	38%
Accepted Applications	28	65%	103	62%	6,469	62%
TOTAL RECEIVED ---->	43	100%	165	100%	10,429	100%

Conclusion

The fact that the Minnesota property tax system is extremely complex and confusing is not lost on serious observers of the system. Bring in the 4d Property Tax Classification, the “This Old House” program, and the Special Agricultural Homestead provisions with their burdensome time requirements for verification, interpretation, programming, and ongoing recordkeeping and you have an administrative nightmare. We have gotten so far away from the “uniformity clause” and “fairness doctrine” of ad valorem taxation, that the only solution is a new tax code based on strict interpretation of the original constitutional principals. The shoulders of the Minnesota income tax system should be broad enough to carry all of the “social engineering” that our legislators and we would care to formulate.

Having stated the obvious, most of us can also probably agree that the chances for meaningful simplification of the property tax system are probably between “slim” and “nil.” As we’re holding our breath, we can only do our best with an imperfect system. To that end, I’ve designed an application form for collecting the information needed for making a decision on Special Agricultural Homestead petitioners. In some small way, maybe we can create more time for our primary calling: **VALUATION**.

Anyone who would like the original Special Agricultural Homestead application form in MS Word can send a request to wendell.engelstad@co.steele.mn.us.

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