



## MEMORANDUM

TO: County and City Assessors of the State of Iowa

FROM: J.J. Severson, Tax Attorney, Policy and Communications Division

RE: Agricultural Classification

DATE: April 26, 2017

### ISSUE PRESENTED

Recently, the Department has learned of several handbooks or manuals that various assessors are using to determine whether property should be classified as agricultural for property tax purposes. The Department notes that some aspects of the handbooks or manuals stray from the law in many places. This memo attempts to correct common errors and misconceptions the Department found. Assessors who continue to classify property in an erroneous manner could be found to have committed misconduct, as that term is defined in House File 478, 87<sup>th</sup> G.A., 1st Sess. §5 (Iowa 2017).

### APPLICABLE LAW

Agricultural real estate shall include all tracts of land and the improvements and structures located on them which are in good faith used primarily for agricultural purposes except buildings which are primarily used or intended for human habitation as defined in subrule 71.1(4). Land and the nonresidential improvements and structures located on it shall be considered to be used primarily for agricultural purposes if its principal use is devoted to the raising and harvesting of crops or forest or fruit trees, the rearing, feeding, and management of livestock, or horticulture, all for intended profit. Agricultural real estate shall also include woodland, wasteland, and pastureland, but only if that land is held or operated in conjunction with agricultural real estate as defined in paragraph “a” or “b” of this subrule.

Iowa Admin. Code r. 701—71.1(3)“a”(405,427A,428,441,499B) (2017).

As with all real estate, “the assessor shall classify property according to its **present use and not according to its highest and best use.**” Rule 71.1(1).

## DISCUSSION

The Department recognizes that determining classification for property tax purposes is a fact-intensive process that requires the judgment of the assessor. Drafting an office manual for assessing staff to reference is useful in order to maintain consistency in classifications. However, the manuals must conform to Iowa law, and must not be used in a manner that results in a finding contrary to the rule setting forth the criteria for classification. The following errors, if found in your jurisdiction's manual, should be corrected immediately:

### 1. The Assessor Classifies Property

Rule 701—71.1(1) states that it is the responsibility of the assessor to determine the proper classification of real estate. The assessor may not shift this duty or burden to the taxpayer by requiring that the taxpayer apply for, submit evidence, or provide documentation of profitability in order for the property to be classified as agricultural. The assessor must make the classification using his or her best judgment based on the facts available. The assessor should be able to make this determination without the use of proprietary information, such as financial statements or federal or state tax returns. Forms that request the production of such proprietary information to support the owner's contention that the property should be classified as agricultural must state clearly that any information given to the assessor becomes public and will not be kept confidential. Finally, Iowa Code section 441.18 does not permit the assessor to require the taxpayer provide proprietary or extraneous information in order to receive the agricultural classification. It is improper for the assessor to classify property as residential or commercial as a default position, and then demand proprietary information from the taxpayer in order to receive the agricultural classification.

### 2. Iowa Code section 441.21 and Iowa Administrative Code rule 701—71.1 Controls

Definitions of terms used in rule 701—71.1 are found within the rule itself, or within the Code sections to which the rule pertains. Definitions pertaining to other parts of the Code do not pertain to terms used for property tax classification purposes. Furthermore, classification is not an exemption and it is improper to apply the same criteria used to determine exemptions when evaluating property for property tax classification. The standard for reviewing the facts for an exemption is different from the standard used to review facts for classification. Classification is never based on the disparate assessed values that exist between agricultural real estate and the other classes of real estate. Also, several manuals seem to take the position that different classification standards apply based on the size of the tract. There is no legal authority for evaluating parcels of more than ten acres differently from parcels of less than ten acres for classification purposes. Moreover, there is no authority to require a property owner to show an actual profit every three out of five years or over a similar time period. These requirements stem from IRS regulations regarding hobby loss income tax cases and are not part of the agricultural classification standards. For land to be considered to be used primarily for agricultural purposes, it must be used for an **intended profit**, not an actual profit. IRS guidelines

pertaining to farm hobby loss situations may be useful to help determine whether the farming activity is being run with a profit motive, but should only be used in an advisory way.

### **3. Present Use Is the Standard**

Highest and best use is not the standard for determining property tax classification in Iowa. Property shall not be classified based on how one might market the land for sale. Property may only be classified based on its present use. It appears several manuals suggest denying an agricultural classification if the property has been recently rezoned, is being held for possible future development, would be marketed as something other than agricultural property or does not conform with the use of other surrounding properties. While the answer to these factors may be a relevant part of any inquiry, to the extent that they pertain to the highest and best use of the property is not a proper criteria for denying an agricultural classification. If it can be shown that the agricultural activity is being run with the intent to make a profit, whether or not actual profits exist, it will generally qualify as agricultural irrespective of the highest and best use of that property.

### **CONCLUSION**

Assessors shall evaluate any internal guidelines, manuals or directives used to classify agricultural property to ensure that the guides do not misapply or violate Iowa law.