

The FSZ: Preserving California's Prime Agricultural Farmland

I. Introduction

Everybody would like a 35 percent discount on their property tax bill. Under recently enacted legislation, by agreeing to restrict the use of their land to agricultural and compatible uses, California farmers can enjoy just such a discount. In order to understand why farmers should enjoy this discount, it is first necessary to understand California's policies regarding the preservation of its agricultural lands.

In 1965, the California State Legislature enacted the California Land Conservation Act of 1965, commonly referred to as the Williamson Act. The express purpose of the Williamson Act is to preserve a maximum amount of the State's agricultural land, which is necessary to the maintenance of California's agricultural economy, and to assure an "[a]dequate, healthful and nutritious food for future residents of this State and nation." Changed conditions since 1965 make traditional Williamson Act contracts much less attractive to owners of California's best agricultural ground, and consequently, enrollment into Williamson Act contracts is destined to steadily decline.

In August of 1998, the Legislature breathed new life into the Williamson Act by amending it to provide for the establishment of "Farmland Security Zones." This article discusses the Farmland Security Zone legislation, and how this legislation will help in the fight to preserve California's agricultural land.

II. Overview of the Williamson Act

Under the Williamson Act, an owner of agricultural land may enter into a contract with the county whereby the landowner agrees to restrict the use of the land to the production of commercial food or fiber for a term of not less than 10 years. The term of the contract is automatically extended each year unless notice of cancellation or nonrenewal is given. Certain compatible uses are also allowed on the property. In return, the landowner is taxed on the capitalization of the income from the land, and not on the fair market value.

A. How property is valued under a williamson act contract

Land subject to a Williamson Act contract is valued on a yearly basis according to its income-producing ability. In general terms, the assessor values the land by taking the fair rental value based on typical rentals received in the area for similar land, as well as the actual rent being paid (if any) on the subject land. Then, the fair rental value is divided by a capitalization rate specified by law. The capitalized value, which will serve as the land's value under the Williamson Act, is the quotient developed by this calculation.

B. Changed conditions

Since the passage of the Williamson Act, it became apparent that owners of prime farmland and land used for high value crops may not realize the property tax reductions under traditional Williamson Act contracts sufficient to justify restricting their land to agricultural purposes. This is due to two primary reasons: (1) the method of calculating value under the Williamson Act; and (2) the passage of Proposition 13. In many areas, the rental value of agricultural land actually meets or exceeds the unrestricted factored base year value of the land. In such cases, the landowner will not derive much benefit, if any, from entering into a traditional Williamson Act contract. As discussed below, Proposition 13 exacerbated this problem. In 1978, California voters passed Proposition 13, which made property taxes dependent on acquisition value rather than its fair market value. As a result, owners of farmland that had not changed hands for many years already enjoy a low factored base-year value, which in many cases is lower than the Williamson Act value. This is particularly true when dealing with prime row-crop lands with high rental values. The reduced incentives to place this land into the Williamson Act undercuts California's policy of preserving a maximum amount of its agricultural land. This is where the Farmland Security Zone legislation (Chapter 353, Statutes of 1998) attempts to cure the problem by correcting the incentives.

III. Overview of the farmland security zone legislation

A. Rescission of Williamson Act contracts

The Farmland Security Zone legislation authorizes landowners to petition the county board of supervisors ("Board") to rescind their existing Williamson Act contract in favor of a new Farmland Security Zone Contract ("FSZ Contract"). The landowner must have an existing Williamson Act contract before the Board can approve a FSZ Contract. For land not currently in a Williamson Act contract, the Board may allow enrollment of the land into a Williamson Act contract, then authorize the immediate rescission of those contracts in favor of FSZ Contracts.

B. Resultant property tax savings

Land subject to a FSZ Contract is valued for assessment purposes at 65 percent of the value of its Williamson Act value, or its Proposition 13 value, whichever is lower. This is the tax incentive that legislators hope will encourage owners of agricultural land to put their property into Farmland Security Zones.

C. Additional tax savings

In addition to the 65 percent assessment value, the Farmland Security Zone legislation requires that new special taxes for urban-related services be levied at an unspecified reduced rate on land enrolled in a FSZ Contract, unless the tax directly benefits the land or the living improvements on the land. Whether this will provide any real benefit is difficult to predict because the rate of reduction is not specified, and because of the uniqueness of each parcel placed into a FSZ Contract.

D. Prohibits annexation of land

The Farmland Security Zone legislation prohibits the annexation of land enrolled in a FSZ Contract to a city, or a special district that provides non-agricultural services, or for use as a public school site. In addition, the Farmland Security Zone legislation prohibits a local agency

formation commission (LAFCO) from annexing or otherwise obtaining control of land subject to a FSZ Contract, except under very limited circumstances.

E. Extends the contract period to 20 years

Williamson Act contracts must be for at least a 10-year period. The new Farmland Security Zone legislation provides that the FSZ Contracts be for at least a 20-year period.

F. No cancellation provisions

Williamson Act contracts may be immediately terminated (as opposed to nonrenewed) under extraordinary circumstances and when cancellation is consistent with the Williamson Act or it is in the public interest. There does not appear to be such authority in the Farmland Security Zone legislation, which makes it unclear as to whether the land enrolled in a FSZ Contract may be cancelled. Both author and the sponsors of the legislation, Senator Jim Costa and the California Farm Bureau Federation, respectively, do not believe that cancellation should be allowed.

IV. Land that qualifies to be enrolled in FSZ contracts

The following requirements must be met to place land into FSZ Contracts:

1. Land must be currently in a Williamson Act contract

As discussed above, before land may be placed into a FSZ Contract, it must first be subject to a Williamson Act contract.

2. Landowner request

No land may be placed into a FSZ Contract unless expressly requested by the landowner.

3. Grade of land

To qualify, land must be designated on the Important Farmland Series maps as predominately on or more of the following: (1) prime farmland; (2) farmland of statewide significance; (3) unique farmland; or (4) farmland of local importance.

4. Sphere of influence

Any land located within a city's sphere of influence may not be included in a Farmland Security Zone, unless expressly approved by resolution by the city with jurisdiction within the sphere.

V. Implementation

Because the Farmland Security Zone legislation passed in late 1998, there has not been much time for counties to implement any structure for processing landowner requests to establish Farmland Security Zones, or to prepare the FSZ Contracts. In fact, many counties may not even be aware that these FSZ Contracts are even available. Below is a suggestion on how any requests may be handled.

A. Timing of applications

1. Land not yet in Williamson Act contracts

If the land is not already in a Williamson Act contract, the landowner will have to apply with the county on or before the date the county requires the landowner to apply for a Williamson Act contract. Then, the application to have land be put into a Williamson Act contract, and recommend that the Board authorize the immediate rescission of the Williamson Act contract in favor of a FSZ Contract. This request can be reviewed through the same mechanism by which the county reviews the Williamson Act contract. Assuming the parcels in question qualify, the Board would then approve the placement of the parcel into FSZ Contracts.

2. Land already in Williamson Act contracts

If the property is already in Williamson Act contracts, no time is set in the legislation as to when those can be changed into FSZ Contracts. However, it appears logical to have any applications to put land into a FSZ Contract to be processed with any other Williamson Act contract applications.

B. Effect of nonrenewal

As with Williamson Act contracts, either the county or the landowner may provide the other with a notice of non-renewal, which then triggers a gradual ratcheting up of the assessed value over a period of years to its Proposition 13 value. The valuation of the land following the service of a non-renewal notice is treated as follows:

- **Step 1:** Determine the Proposition 13 Base Year Value (BYV);
- **Step 2:** Determine the Williamson Act Value (WAV);
- **Step 3:** Subtract the WAV from the BYV;
- **Step 4:** Establish the present net worth value of the based on the number of years remaining on the Contract, and the yield rate established by the Board of Equalization;
- **Step 5:** Multiply the present net worth value by the difference between WAV and BYV as established in Step 3.
- **Step 6:** Add the WAV with the number produced in Step 5 to get your taxable role value for that particular year.

The present worth value becomes greater as the years remaining under the Contract become fewer, so the amount to be added to the WAV increases every year until the expiration of the Contract, when the assessed value will equal the BYV.

In situations where the owner serves the notice of nonrenewal, or the owner fails to protest a notice of non-renewal provided by a county, city or nonprofit organization, this valuation formula applies immediately upon the service of the non-renewal notice. If the county, city or nonprofit organization provides the notice of non-renewal, and the owner objects, then the above formula applies when less than six years remain until the termination of the period for which the land is enforceably restricted.

C. Questions raised regarding the farmland security zone legislation

As with any new legislation, there will be questions regarding its validity and implementation. For instance, an argument could be made that Revenue and Taxation Code section 423.4 is unconstitutional because it allows an escape of a just and equal assessment, favor or reward. On

March 10, 1999, the Attorney General's Office concluded that Revenue and Taxation Code section 423.4 is constitutional because farmland under a Farmland Security Zone Contract is under more use restrictions than land that is subject to a Williamson Act contract. In fact, the Attorney General found that ". . . [t]he former must be valued less for property tax purposes than the latter" because the Constitution prohibits the same valuation for lands subject to different restrictions.

VI. Analysis of the revenue impact on the county general funds

The Williamson Act is a permissive program that established a three-way partnership between the state and the participating local government and landowners. Each partner receives the benefits of agricultural land conservation and the certainty provided by agricultural preserve zoning in return for a modest monetary sacrifice. Landowners give up their development rights and some speculative value in the property; local governments give up a portion of their property tax base; and the state, for its part, provides open-space subventions to participating counties to replace foregone property tax revenue. The current subvention rate is five dollars per acre for prime farmland and one dollar per acre for nonprime land. At the current enrollment of 15.8 million acres, the state contributes nearly \$37 million annually to support the program. It is a little known fact that with the creation of the Educational Revenue Augmentation Fund (ERAF) in 1993, and its compounding effect on the property tax allocation formula imposed by A.B. 8 in 1979, county governments actually may money off of Williamson Act contracts.

Even with the additional property tax benefits provided landowners to encourage their longer term commitments under the FSZ Contracts, most counties will still obtain more general fund revenue from the FSZ Contract valuations, plus the state's subventions, than from their ERAF-reduced share of the Proposition 13 value. A fiscal analysis for Monterey County illustrates this point.

VII. Conclusion

The new Farmland Security Zone legislation provides the owners of agricultural ground a 35 percent reduction in the valuation of their land by enrolling it into FSZ Contracts. The authors predict that this will provide the much-needed incentives to put prime agricultural land into Farmland Security Zones which, in turn, will help to promote California's long-standing policy to preserve its agricultural lands.