

December 2018 Newsletter

President`s Message



PMKCA President Joe Clarkson

Aloha PMKCA Neighbors

Real Property Tax and Agricultural Land – Part 3, Minimizing Taxes Owed

Very few people want to pay more taxes than they need to, but many people pay far more property taxes than necessary, probably because they become confused by the myriad combinations of tax rates and property valuation assessments. Records of property tax assessments and taxes paid for any parcel in Hawai'i County are public information freely available on line, so it easy to find examples of probable confusion.

After looking at the public record, I found that one friend of mine in Pa'auilo Mauka had been paying taxes under the Homeowner classification (and rate) for many years and decided to apply for agricultural classification and assessment. His taxes due went up by 50%. Another friend on Kaapahu Road had been in the agricultural assessment for many years and converted to homeowner status. Her taxes paid went up 500%. These two examples show that there is no way to use classification status alone as a reliable

indicator of how much property tax will be due.

Disclaimer: The following discussion is based on my understanding of property tax issues from reading Chapter 19 of the County Code and from interviews with management staff at the Tax Office. I am not a tax accountant or a lawyer. I urge everyone who wishes to clarify their tax options to consult with their attorney or officials with the Tax Office. I present the following information as my best interpretation of property tax issues only to illustrate the complexity of the issue and prompt everyone to seek consultation with appropriate authorities.

Many of us who live in the PMKCA areas of Kalopa and Pa'auilo Mauka live in our own home and live on a small parcel of land that is zoned Agriculture. All of the following information is relevant only to people in that situation.

Many of us have also been given agricultural classification and land assessment as a matter of course for many years, if not decades. These assessments greatly reduce the assessed value of the land surrounding our homes, but do not affect the assessment of the homes themselves, which are always assessed at market value while it is in agricultural classification. Because of the Tax Office audit (discussed in Part 1), this past practice of an automatic and routine assessment of our land at agricultural values will not continue.

Many of us have received letters from the Tax Office notifying us that we need to re-apply for agricultural classification by December 31st of this year if we want to continue to have our land receive agricultural assessment values. **DO NOT IGNORE THIS LETTER.** If landowners do not submit the required application by the end of the year, all their land will be assessed at market value.

A typical market value for 5 acres in the PMKCA area ranges from \$200,000 to \$250,000, but under agricultural assessment the land is taxed as if its value is typically much less, often as little as \$2,500 for 5 acres. Since the tax rate for agricultural land is \$9.35 per \$1,000 of assessed valuation, if the assessed value of five acres of land rises from \$2,500 to more than

\$200,000, it would immediately add \$1,800 or more to your tax bill. Typically, every acre of land in the PMKCA area which is taken out of agricultural use assessment will cost about \$360 in additional taxes.

Even if we have agricultural classification, our homes are always assessed at market value. If we have applied for and received homeowner exemptions, these exemptions are deducted from the total value of land and home, but are usually shown as being deducted from the home on the assessment notices we receive every year. These exemptions vary by age, disability status and as a percentage of the value of the home (20% of the assessed value of the home, not to exceed \$80,000). Add up the relatively low assessment for the agricultural land, the assessed value of the home and deduct all the homeowner exemptions and you get the taxable assessed value of the property. Multiply that value by the agriculture tax rate of \$9.35 per \$1000 of assessed value and you get the amount of taxes owed for the year.

But there is another option available to all of us who live in our own home, even if it is located on agriculturally zoned land. We can apply to be taxed at the homeowner rate, which, at \$6.15 per \$1000, is considerably less than the agricultural rate of \$9.35 per \$1000. However, to get the lower rate as a homeowner, we must forgo the lower agricultural assessment on our land and accept having it assessed at market value.

Whether the homeowner status will result in a lower tax bill depends on the relative values of the home and the land. If the home, after all exemptions are deducted from its value, has a considerably higher assessment than the market value assessment of the land, having both land and home taxed at the lower rate of \$6.15 per \$1,000 may produce a lower tax bill than by staying in agricultural status.

Here is how to compare the two options. Every assessment notice has several values listed for both the land and the home (including other buildings on the property). They can be found either on the assessment notice you are sent every March 15th, in the public records at the Tax Office or on the Tax Office web site. They are:

Land Market Value;
Land Assessed Value;
Building Market Value;
Building Assessed Value;
Exemption;
Net Taxable Value.

To see what your taxes should be under an agricultural land classification, add the Land Assessed Value and the Building Assessed Value and subtract the Exemption. This will result in the Net Taxable Value shown if you are already in Agricultural classification status. Multiply that Net Taxable Value by 0.00935 and you will get your tax owed for the year.

If you want to see what you would pay under the Homeowner land classification, add the Land Market Value and the Building Assessed Value and subtract the Exemption. Multiply the result by 0.00615 and you will get the tax owed as if under the Homeowner classification.

Since the agricultural rate is just about 1.5 times more than the homeowner rate, if the net assessed value of the home (after exemptions are subtracted) is at least 1.5 times higher than the Land Market Value, then homeowner classification status will result in lower taxes.

There are other advantages to being in the homeowner classification. If real estate values decline, the market value assessment of your property will decline. This is true for either homeowner status or agricultural status, but if real estate values increase again, homeowner assessed values can only increase by 3% per year, whereas agricultural assessed values for the home go up as fast as market prices go up. Agricultural land assessed values are always determined by the values associated with a particular agricultural use.

A disadvantage of switching from homeowner classification to agricultural classification is that Building Assessed Value will immediately become equal to Building Market Value even if the Building Assessed Value under

equal to Building Market Value even if the Building Assessed Value under the homeowner classification is still much lower than the market value due to the 3% increase limitation history.

But there are other advantages to being in the agricultural classification that might be important to a land owner. A second farm dwelling permit is available only to owners of property that is being used as a farm and an agricultural classification would be important evidence in securing any second farm dwelling permit. It is important to note that no additional dwelling on a farm property can be rented without losing the ability to have an agricultural classification. To retain the agricultural classification, it must be used rent-free by people who work on the farm. In fact, rental of any home on a property prevents the landowner from getting any of the rate or assessment benefits of either the agricultural classification or the homeowner classification except for the homeowner exemption.

The current program by the Tax Office to audit all agricultural land for actual use in agriculture complicates matters even more. If a landowner has been told that they must re-apply for agricultural status for their land, there is no certainty that the application will be granted in full. Those acres that are not deemed to be in agriculture will have their assessed value jump to market value. Since that is a much higher value and since the agricultural tax rate is 150% higher than the homeowner rate (at the present time), then staying in agricultural status might result in much higher taxes than expected.

Tax Office appraisers will begin evaluating Non-Dedicated applications in late December and early January. Each applicant will be sent a letter disclosing the results of the appraiser's evaluation and will have a chance to discuss the possibility of further adjustments with the appraiser and the Tax Office. Once an applicant knows what their agricultural use assessment is likely to be, it will be possible to evaluate the tax consequences and decide on the best option for choosing a classification.

It is therefore VERY IMPORTANT TO STAY IN CONTACT WITH THE TAX OFFICE and their appraisers to find out how much land will stay in agricultural status. Even after the first of the year, it is possible to revert to

homeowner classification rather than stay in agricultural classification, but the request to do so must be made before assessment notices are mailed on March 15th. Preferably, any decision to revert to homeowner classification would be done well before then, but the decision should only be made with a clear understanding of your latest assessed property values and after consultation with the Tax Office.

If you are not already receiving a homeowner exemption, you cannot revert to homeowner classification and the lower rate that goes with it. You can always apply for the homeowner exemption if you live in your home, but applications for homeowner exemptions must be made before December 31st in order to be applied to the following year's assessment.

The Tax Office will not optimize your classification status for the lowest possible tax. They will only assess your property under the status you have applied for. However, they will assist you in determining how much tax you would owe under different classifications, but you have to ask them to do so. It is also important to remember that once the annual assessment notices are mailed out on March 15th, the only option available for the year is to appeal the assessment under the classification you last applied for; it is then far too late to change classifications for that year. Good luck!

Best Regards,

Joe Clarkson
President, PMKCA