

AGRICULTURE TAXES IN TEXAS

Rebekka M. Dudensing¹ and Lonnie L. Jones²

Texas agriculture and agribusiness firms pay state and local taxes, and like other businesses and individuals, they enjoy certain tax exemptions and special provisions. These exemptions and provisions are important to farmers and ranchers, but they are a relatively small percentage of the overall exemptions and exclusions granted by state and local governments.

Farmers, ranchers, and agribusiness managers—as well as governmental officials—need to understand these tax exemptions and how revisions to them might affect agriculture. Agribusinesses also need to know which state or local agencies they should contact to secure the tax benefits provided by Texas law. Texas residents can also use this information in determining how the overall tax burden should be divided among various groups.

TAX PROVISIONS FOR AGRICULTURE

Texas farmers, ranchers, and agribusiness firms, can use the following tax benefits:

- ▶ Agriculture and open space land is appraised at a lower rate than for other types of property.
- ▶ Agriculture is exempt from these taxes:
 - ▶ State and local sales and use taxes on farm inputs and products (such as feed, seed, equipment, and chemicals).
 - ▶ Motor vehicle sales and use taxes for vehicles specialized for agricultural production.
 - ▶ Sales and excise taxes on fuel used on farms and ranches.
 - ▶ Some state franchise taxes.

The most significant tax savings for farmers, ranchers, and agribusinesses are the reduced valuation of land used for agriculture, timber, conservation, or wildlife and the exemptions from state and local sales and use taxes.

¹Assistant Professor and Extension Economist

²Professor Emeritus, Department of Agricultural Economics

PRODUCTIVITY VALUATION OF OPEN SPACE LAND

Property taxes are a large portion of the taxes that farmers and ranchers pay. However, every state has some form of preferential treatment for agricultural, conservation, or open space land that is intended to preserve those spaces and endeavors.

In Texas, value is assigned to certain properties based on their agricultural or timber productivity value rather than on market value. To receive this special valuation, the land must be used for conservation or wildlife management, or for producing crops, livestock or exotic animals, timber, or nursery crops and related products.

Productivity value is an estimate of the value of the land if it is used for agriculture, timber or wildlife only; it excludes other market forces such as speculation or commercial development, which add value to the land. The landowner, therefore, pays taxes on a valuation that may be significantly below market value, which is used for assessing most other properties.

Productivity valuation is applied only to such property as the land, fences, stock watering tanks, and irrigation wells. Houses, barns, milking parlors, and other improvements are assessed at the prevailing market value.

The taxation of certain open space land is addressed by Article VII, Section 1-d-1 of the Texas Constitution and Subchapter D (Sections 23.51 through 23.60) of the Texas Tax Code. The two provisions for productivity valuation are Section 1-d agricultural valuation, and Section 1-d-1 open space valuation. Though the terms *agricultural valuation* or *ag exemption* are often used, *open space land* is the appropriate term for much of the land that receives a productivity valuation.

Open-space valuation depends how the land is used, not on any characteristics of the landowner. To qualify for the open-space designation, the land must have been in agricultural production, including land for

timber, conservation, and wildlife management, for 5 of the past 7 years. In the current year, the land must be devoted principally to agricultural use at the intensity of use generally accepted in the area. These intensity standards vary among counties and are set by the local appraisal district.

Open space land receives a reduced tax burden. However, all Texans are exempt from property taxes on investments such as bank accounts and vehicles.

To receive the special appraisal for wildlife management, the owner must use the land for the purposes stated in the tax code. People who acquire land that was previously qualified as open space must apply in their own name by April 30 to avoid losing the special valuation. The valuation status then remains in force until the qualifications change or the appraiser requests a new application.

The open space provision is not an absolute exemption; if the land changes to a nonagricultural use, the owner must pay a rollback tax equal to the tax savings for the 5 most recent years (plus 7 percent interest accrued from the dates that the taxes were due). The provision saves taxes only for people who maintain their land's open space status for more than 5 years. Nevertheless, this special treatment saves landowners more money in yearly tax savings than any other state or local agricultural tax exemption or provision.

Few landowners qualify for the original 1966 1-d agricultural valuation. This designation is tied to both the land and the landowner and must be applied for each year it is claimed. Section 23.42 of the Texas Tax Code stipulates:

- ▶ The land must have been exclusively devoted to or developed for agriculture for the past 3 years.

- ▶ The landowner must use the land for agriculture as his/her occupation or as a business venture for profit in the current year.
- ▶ Agriculture must be the landowner's primary occupation and source of income.

This section defines agriculture as "the raising of livestock or growing of crops, fruit, flowers, and other products of the soil under natural conditions as a business venture for profit." Wildlife and timber uses do not qualify for Section 1-d valuation.

If the land use changes and no longer qualifies for an agricultural appraisal, the landowner must pay the difference between its tax based on productivity value and the tax based on market value for the present year and the preceding 3 years plus interest at the rate published for delinquent taxes.

The agricultural or open-space valuation is a major benefit to farmers, ranchers, and owners of qualified land. Texas landowners enjoy significant property tax savings from the open space valuation provisions (Table 1).

In 2011, open space valuations saved Texas landowners an estimated \$2.70 billion in school property taxes alone. By 2015, this savings is projected to increase to \$2.95 billion because the market value of land is expected to increase faster than the productivity use values.

School property taxes account for more than half of the total property taxes levied in Texas. Landowners also benefit from lower county and city property taxes under the open space provision.

This provision accounted 35 percent of school property tax savings (or public revenue loss) in 2001 and for 45 percent in 2011. A partial list of tax savings is available

TABLE 1. PROJECTED VALUE OF THE OPEN SPACE PRODUCTIVITY VALUATION FOR AGRICULTURE ON SCHOOL PROPERTY TAX SAVINGS.

EXEMPTION AND SPECIAL VALUATION	2011 (MILLIONS OF DOLLARS)	2013 (MILLIONS OF DOLLARS)	2015 (MILLIONS OF DOLLARS)
<i>Special appraisal for agriculture and timber land¹</i>	2,702.8	2,792.6	2,947.0
All Residence Homestead Exemptions	1,750.7	1,844.9	1,947.2
All Other Exemptions	1,545.5	1,632.1	1,738.0
Total exemptions and special valuations	5,999.0	6,269.6	6,632.2
Agricultural exemptions as a % of total exemptions	45.1%	44.5%	44.4%

¹The special appraisal includes both agriculture and open space valuations.
Source: Texas Comptroller of Public Accounts, Tax Exemptions & Tax Incidence, 2011.

from the Texas Comptroller of Public Accounts on the web at: <http://www.window.state.tx.us/taxinfo/incidence/96-463TaxIncidence02-11.pdf>.

The open space provision of the Texas Tax Code is often criticized because it decreases property tax revenue to local jurisdictions. Since 2007, more tax revenue has been lost to open space valuation than to homestead exemptions. This change occurred because the number of building permits plummeted in 2007 and residential homestead exemptions stay about the same, while the open-space valuation changes when the value of real property increases.

However, the open space exemption is assumed to remove less tax revenues than do the exemptions for properties such as religious and charitable organizations, educational institutions, personal property (vehicles, jewelry) or intangible property (bank deposits, stocks, bonds, etc.). The Texas Comptroller (Combs 2011) reports that the value of these exemptions cannot be estimated. Similarly, the value of exemptions to farm produce and implements cannot be estimated.

For information on the open space provision of the Texas property tax law, including how to apply for an exemption, contact the local county Central Appraisal District office.

SALES AND USE TAX EXEMPTIONS

Farmers and ranchers are exempt from state and local sales taxes for most agricultural inputs they buy and for the products they sell. The exemption covers:

- ▶ Virtually all inputs used exclusively to produce agricultural goods.
- ▶ Products sold by farms and ranches such as grain, milk, livestock, and raw cotton for further processing.
- ▶ Raw food products such as vegetables and meats sold directly to consumers.

Without these exemptions, farmers and ranchers would pay a 6.25 percent state tax plus a local sales tax of up to 2 percent for their inputs and sales. This benefit is not unique to agriculture; the exemption is used across other industries to avoid taxing products multiple times as they move through production and distribution channels. Texas does not charge sales tax on non-prepared food products, regardless of whether they are purchased from farmers or from grocery retailers.

In 2011, the total sales tax exemptions granted on agricultural inputs amounted to \$414 million (Table 2). Most of this exemption was for the purchase of feed, seed, and supplies, machinery, and equipment used for producing agricultural products.

Farms and ranches receive tax breaks similar to those enjoyed by other businesses—for example, exemptions on manufacturing inputs.

Although these tax savings are important to farmers and ranchers, exemptions for inputs amounted to only 1.7 percent of the value of all sales tax exemptions in Texas in 2011 and only 1.4 percent of the value of all sales tax exemptions plus exclusions on services.

In comparison, exemptions for food products for home consumption totaled \$1.47 billion. Exemptions on manufacturing materials, equipment, and supplies totaled \$10.41 billion. The value of sales tax exemptions on agricultural inputs also trailed that of other exempted categories such as health care supplies (\$689.6 million) and residential gas and electricity (\$881.5 million). The largest exclusion was \$879.2 million for physician services.

Agriculture's share of sales tax exemptions has declined since 2001, and the state comptroller projects that the trend will continue through 2013 (Table 2). This likely reflects the fact that, although agricultural receipts continue to increase, agriculture makes up a smaller share of the state's economy.

As of January 1, 2012, agricultural businesses must obtain a Texas Agriculture and Timber Exemption Registration Number ("Ag/Timber Number") from the state comptroller. They may apply online at the comptroller's website (URL: www.GetReadyTexas.org) or request a paper copy from the comptroller's office to register the business name and address, agricultural products produced, and applicant's Social Security Number. The Ag/Timber Number is available immediately. Permits obtained in 2011 through 2014 are valid through December 2015. The sales tax exemption for most items purchased for farm or ranch use is obtained by completing a sales tax exemption form when buying the items. Note that the exemption forms have changed to include the Ag/Timber number. Buyers without a number and certificate may pay the sales tax and apply for a refund.

MOTOR VEHICLE SALES AND USE TAXES

Texas tax law does not provide a blanket exemption for motor vehicles used in agriculture. Trailers and self-propelled farm machines such as tractors and combines used exclusively in farm production are exempt from the 6.25 percent motor vehicle sales and use tax. Some vehicles that have been modified to distribute feed or fertilizer may also be exempt from motor vehicle taxes.

Exemptions are not based on vehicle registration status; a truck's farm registration does not exempt it from the motor vehicle tax.

TABLE 2. PROJECTED VALUE OF SALES AND USE TAX EXEMPTIONS FOR AGRICULTURE.

EXEMPTION	2011 (MILLIONS OF DOLLARS)	2013 (MILLIONS OF DOLLARS)	2015 (MILLIONS OF DOLLARS)
Agricultural feed, seed, chemicals, and supplies	263.5	277.2	293.8
Livestock for food	16.1	16.9	17.9
Agricultural machinery and equipment	78.4	82.5	87.4
Horses, mules, and work animals	8.7	9.2	9.8
Commercial fishing ice	0.2	0.2	0.2
Total \$151.316 agricultural exemptions	366.9	386.0	409.1
Timber operations	22.3	24.6	27.1
Electricity for agricultural use	24.5	27.0	29.2
Agribusiness items	0.5	0.5	0.5
Total agricultural exemptions by other codes	47.3	52.1	56.8
Total agricultural input exemptions	414.2	438.1	465.9
Food for home consumption	1,466.0	1,579.8	1,713.8
School lunches and certain food sales	43.3	46.9	50.8
Exemptions in all other sectors*	22,840.8	25,210.3	28,470.2
Total exemptions	24,764.3	27,275.1	30,700.7
Exclusions on services	5,810.8	6,500.3	7,331.1
Agricultural input exemptions as a % of total exemptions	1.7%	1.6%	1.5%
Agricultural input exemptions as a % of total exemptions and exclusions	1.4%	1.3%	1.2%

*Includes items taxed by other law (\$8.6 billion in 2011).

Source: Texas Comptroller of Public Accounts, Tax Exemptions & Tax Incidence, 2011.

Farmers and ranchers were projected to save about \$24.4 million in 2011 under this exemption (Table 3). These savings apply to specially adapted motor vehicles used exclusively for producing crops and livestock. In 2011 agricultural producers accounted for about 19.5 percent of the statewide total motor vehicles sales and use exemptions of \$125.3 million. Although the value of agricultural exemptions is projected to increase through 2015, the share is expected to decline as spending and exemptions grow faster in other sectors than in agriculture. The law also provides exemptions for nonagricultural businesses, such as child care facilities.

Farm vehicles as defined above may also be exempt from the Texas Emissions Reduction Plan (TERP) surcharge. The TERP surcharge on the sale or lease price of diesel-powered vehicles of at least 14,000 pounds is issued to help the state improve air quality and meet federal pollution emissions standards. The surcharge is 2.5 percent for 1996 model vehicles or earlier, and 1 percent for vehicles that are of 1997 models or

later. Farm equipment is also exempt from the state's 2 percent Off-Road, Heavy-Duty Diesel Equipment surcharge.

Representatives of agricultural businesses should contact the comptroller's office to see if they qualify for an exemption from motor vehicle taxes.

FUEL TAX EXEMPTION

Much of the gasoline and diesel that farmers and ranchers buy is used for agricultural production; the fuel that is not used on public highways is exempt from the motor fuel tax. In 2011 this exemption saved farmers and ranchers \$10.8 million and amounted to about 9.6 percent of the value of all exemptions under this law (Table 4). In 2015, the value is projected to remain at just under 10 percent of the total fuel exemptions.

TABLE 3. PROJECTED VALUE OF MOTOR VEHICLE SALES AND USE TAX EXEMPTIONS FOR AGRICULTURE.

EXEMPTION	2011 (MILLIONS OF DOLLARS)	2013 (MILLIONS OF DOLLARS)	2015 (MILLIONS OF DOLLARS)
Farm or timber use exemption	24.4	25.1	26.4
Exemptions in all other sectors, including public sector and private households	100.9	106.7	114.5
Total exemptions	125.3	131.8	140.9
Agricultural exemptions as a % of total exemptions	19.5%	19.0%	18.7%

Note: The above figures reflect exemptions from the motor vehicle sales and use tax and not exemptions from the TERP surcharge.
Source: Texas Comptroller of Public Accounts, Tax Exemptions & Tax Incidence, 2011.

Fuel for off-road use, such as plowing and harvesting crops, is exempted from fuel taxes.

To obtain an exemption from the motor fuels tax, an end user number must be obtained from the Texas State Comptroller of Public Accounts (Form AP-197) and an end user signed statement (Form 06-710—agricultural use only—or Form 06-352—some nonagricultural use) must be submitted to the distributor.

FRANCHISE TAX EXEMPTIONS

Texas’ business tax is called the “franchise tax,” and farms organized as corporations are subject to it. However, farms, like other businesses, with a tax liability of less than \$1,000 and gross sales less than \$1,030,000 do not pay the tax, although they must still report their income.

Many non-profits are also exempt from the franchise tax. Agricultural marketing associations and agricultural cooperatives, including farm credit cooperatives and insurance mutuals, are exempt from the franchise tax. Producer members of cooperatives benefit from this exemption because they result in lower prices and increased patronage (dividend) payments.

SUMMARY

Agriculture enjoys several tax exemptions and favorable provisions at the state and local level. The total tax savings documented from all agriculture exemptions totaled \$3.15 billion of \$38.2 billion in exemptions in 2011. By 2015, it is projected to be \$3.45 billion (Table 5). The projected tax savings suggest:

- ▶ Tax exemptions and special provisions are significant to farmers and ranchers. The tax savings to agriculture and agribusinesses in 2009 amounted to almost three-quarters of the average annual net farm income in Texas from 2007 to 2009 (Economic Research Service, USDA). The tax savings actually exceeded the state’s net farm income of \$2.2 billion in 2009, a record low year for farm incomes.
- ▶ The school property tax savings derived from the open-space land valuation accounted for 85.7 percent of all agriculture’s special provisions in 2011. The actual benefit is even higher because of city and county exemptions.
- ▶ Though exemptions and special provisions give farmers and ranchers significant tax savings, they are a relatively small part of the total exemptions and exclusions that state and local governments grant to taxpayers. For 2011, agriculture’s provisions were about 8.3 percent of the state’s \$38.2 billion in reported exemptions.

TABLE 4. PROJECTED VALUE OF FUEL TAX EXEMPTIONS FOR AGRICULTURE.

EXEMPTION	2011 (MILLIONS OF DOLLARS)	2013 (MILLIONS OF DOLLARS)	2015 (MILLIONS OF DOLLARS)
Agricultural use exemption	10.8	11.1	11.4
Exemptions in all other sectors	102.1	105.0	107.6
Total exemptions	112.9	116.1	119.0
Agricultural exemptions as a % of total exemptions	9.6%	9.6%	9.6%

Source: Texas Comptroller of Public Accounts, Tax Exemptions & Tax Incidence, 2011.

TABLE 5. PROJECTED VALUE OF TAX EXEMPTIONS FOR AGRICULTURE.

EXEMPTION OR PROVISION	2011 (MILLIONS OF DOLLARS)	2013 (MILLIONS OF DOLLARS)	2015 (MILLIONS OF DOLLARS)
Open space land valuation	2,702.8	2,792.6	2,947.0
Sales and use tax exemption on agricultural inputs	414.2	438.1	465.9
Motor vehicle sales and use tax exemption	24.4	25.1	26.4
Fuels tax exemption	10.8	11.1	11.4
Total	3,152.2	3,266.9	3,450.7

Source: Texas Comptroller of Public Accounts, Tax Exemptions & Tax Incidence, 2011.

FOR MORE INFORMATION

Combs, Susan. Window on State Government Website. Office of the Texas Comptroller of Public Accounts. Austin, Texas. 2011. <http://www.window.state.tx.us>.

Combs, Susan. *Tax Exemptions & Tax Incidence*. Office of the Texas Comptroller of Public Accounts. Austin, Texas. 2011. <http://www.window.state.tx.us/taxinfo/incidence/96-463TaxIncidence02-11.pdf>.

Dudensing, Rebekka M., & Lonnie L. Jones. *Understanding Texas Taxes*, E-584. Texas A&M AgriLife Extension Service, The Texas A&M System. 2011. http://communities.tamu.edu/community_resources_and_economic_development_programs/cred_publications.php.

Dudensing, Rebekka M. *Texas Property Taxes*, E-256. Texas AgriLife Extension Service, The Texas A&M System. 2010. http://communities.tamu.edu/community_resources_and_economic_development_programs/cred_publications.php.

Economic Research Service. (2011). Farm Income Data Files: Texas. U.S. Department of Agriculture. <http://www.ers.usda.gov>.

Fambrough, Judon. *Ag-use Exemption: Fact or Fiction?*, Publication 1361. Real Estate Center, Texas A&M University, College Station, Texas, January. 2010. <http://recenter.tamu.edu/pdf/1361.pdf>.

Malme, Jane. *Preferential Property Tax Treatment of Land*. Working Paper WP93JM1. Lincoln Institute of Land Policy, Cambridge, Massachusetts. 1993.

McCorkle, Dean A., Rebekka Dudensing, David P. Anderson, Dan Hanselka, James LeBas, Doug Freer, & Gary Preuss. 2011. *The Food and Fiber System and Production Agriculture's Contribution to the Texas Economy*, MKT 3579-B, Texas A&M AgriLife Extension Service, The Texas A&M System. February. <http://agecoext.tamu.edu/resources/library/publications.html>.

Polyakov, Maksym, & Daowei Zhang. Property Tax Policy and Land-Use Change. *Land Economics* 2008. 84(3):396-408.

Real Estate Center. Building Permits Database. Texas A&M University. 2010. <http://recenter.tamu.edu/data/bp/bps/st48.asp>.

Wunderlinch, Gene. "Land Taxes in Agriculture: Preferential rate and Assessment Effects." *American Journal of Economics and Sociology* 1997. 56(2):215-228.