

LIMITED-SCOPE AUDIT PROPOSAL

Property Valuation: Evaluating the Potential Impact of Changing How Agricultural Land is Valued in the State

SOURCE

This audit proposal was requested by Representative Adam Smith.

BACKGROUND

Depending on its use, real property (i.e., land and buildings) can be classified as residential, commercial, or agricultural. State law requires all real property in the state be valued annually for tax purposes. In most cases, one of several property valuation methods can be used to estimate the market value of the property. However, K.S.A. 79-1476 requires all agricultural land be valued at its use value—a measure of the land's net returns—rather than its market value. In 2016, the total of all agricultural land in the state was valued at \$2.3 billion, which accounted for about 7% of the value of all real property in the state.

The Division of Property Valuation within the Department of Revenue oversees the valuation of all real property. In determining the use value of agricultural property, K.S.A. 79-1476 requires the division to use an eight-year average of net returns. Using an eight-year average minimizes the year-to-year effects that drought, natural disasters, and other factors can have on agricultural land values. The division and the Department of Agricultural Economics at Kansas State University have developed a methodology to calculate this eight-year average. The method uses historic cost factors (e.g. herbicides prices and equipment repairs) and historic income factors (e.g. crop mix and crop yield) to determine the average net return of agricultural land over the eight-year period. Legislators are interested in knowing how increasing the number of years in this calculation would affect the value and taxation of agricultural property in the state.

AUDIT OBJECTIVES AND TENTATIVE METHODOLOGY

The audit objective listed below represents the question that we would answer through our audit work. The proposed steps for the objective are intended to convey the type of work we would do, but are subject to change as we learn more about the audit issues and are able to refine our methodology.

Objective 1: How would increasing the number of years used to calculate the average value of agricultural land affect the property's value and taxation? Our tentative methodology would include the following:

- Work with officials from the Division of Property Valuation and Kansas State University to understand the rationale for an eight-year average.
- Have officials from the Division of Property Valuation and Kansas State University estimate the effect increasing the eight-year average to other windows of time would have on the value and taxation of agricultural land in a small sample of Kansas counties.

- Work with officials from the Division of Property Valuation, Kansas State University, and other appropriate stakeholders to identify any other effects or consequences from increasing the eight-year average.

ESTIMATED RESOURCES

We estimate this audit would require **100 staff hours** to complete.