

Office of the Attorney General
State of North Dakota

Opinion No. 84-35

Date Issued: November 14, 1984
Requested by: Kent Conrad
State Tax Commissioner

--QUESTIONS PRESENTED--

I.

Whether, for the purpose of the ad valorem tax exemption for a farm residency, net income from farming activities includes cash rents received by the owner of rented farm land.

II.

Whether, for the purpose of the ad valorem tax exemption for a farm residence, net income from farming activities includes crop shares received by the owner of rented farm land.

--ATTORNEY GENERAL'S OPINION--

I.

It is my opinion that, for the purpose of the ad valorem tax exemption for a farm residence, net income from farming activities does not include cash rents received by the owner of rented farm land.

II.

It is my further opinion that, for the purpose of the ad valorem tax exemption for a farm residence, net income from farming activities includes crop shares received by the owner of rented farm land.

--ANALYSES--

I.

Section 57-02-08(15) of the North Dakota Century Code, in part, exempts from ad valorem taxation '. . . a residence which is situated on a farm and which is occupied or used by a person who is a farmer.' For the purpose of the exemption, the statute defines 'farm' and 'farmer.'

The exemption for a farm residence must be strictly construed. Section 57-02-08(15)(b), N.D.C.C.; *Mills v. Board of County Commissioners*, 305 N.W.2d 832 (N.D. 1981).

Section 57-02-08(15)(b)(2), N.D.C.C., defines a farmer as follows:

(2) 'Farmer' means an individual who normally devotes the major portion of his time to the activities of producing products of the soil, poultry, livestock, or dairy farming in such products' unmanufactured state and who normally receives not less than fifty percent of his annual net income from any one or more of the foregoing activities; and the term also includes an individual who is retired because of illness or age and who at the time of retirement owned and occupied as a farmer as defined above the residence in which he lives and for which the exemption is claimed.

Section 57-02-08(15)(b)(3), N.D.C.C., defines net income from farming activities as follows:

(3) 'Net income from farming activities' described in paragraph 2 means taxable income from those activities as computed for income tax purposes pursuant to chapter 57-38 adjusted to include the following:

(3) The difference between gross sales price less expenses of sale and the amount reported for sales of agricultural products for which the farmer reported a capital gain.

(b) Interest expenses from farming activities which have been deducted in computing taxable income.

Chapter 57-38, N.D.C.C., provides that federal taxable income is the starting point for the calculation of an individual's North Dakota income tax liability and only those adjustments expressly provided by statute may be made to increase or decrease federal taxable income. Sections 57-38-01(8), 57-38-01.1, and 57-38-01.2, N.D.C.C.; *Erdle v. Dorgan*, 300 N.W.2d 834 (N.D. 1981).

A taxpayer owning farm land and who receives a fixed rental for it without reference to production is not engaged in the business of farming for federal income tax purposes. IRS Reg. Sections 1.61-4(d) and 1.175-3. This income is not reported on the federal income tax schedule for farm income (Form F), but is reported on the schedule for rents and royalties. 1984 Fed. Taxes (P-H) ¶ 7161 at 7109 and ¶7165 at 7113. This is consistent with the North Dakota Supreme Court's decision which denied the farm residence exemption. *Mills v. Board of County Commissioners*, 305 N.W.2d 832 (N.D. 1981).

The North Dakota Supreme Court has held that the federal self-employment tax is a tax separate from the federal income tax. *Messner v. Dorgan*, 228 N.W.2d 311 (N.D. 1974), cert. denied, 421 U.S. 949. Nevertheless, it is significant to note that income derived from the rental of farm land is not included for the calculation of the tax on self-employment income unless there shall be material participation by the owner in the production or the management of the agricultural pursuit. IRS Reg. Section 1.1402(a)-4(b).

Therefore, it is my opinion that, for the purpose of the ad valorem tax exemption for a farm residence, net income from farming activities does not include cash rents received by the owner of rented farm land.

II.

The analysis to Question I also applies to Question II with respect to the applicability of federal law.

A taxpayer owning farm land and who receives rental for it that is based upon farm production is engaged in the business of farming for federal income tax purposes. IRS Regs., Sections 1.61-4(d) and 1.175-3. In this case, the landowner has assumed some of the risk of the farming operation.

Therefore, it is my opinion that, for the purpose of the ad valorem tax exemption for a farm residence, net income from farming activities does include crop shares based upon production that are received by the owner of rented farm land.

EFFECT

This opinion is issued pursuant to Section 54-12-01, N.D.C.C. It governs the actions of public officials until such time as the questions presented are decided by the courts.

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