

Understanding the Homestead and Farmstead Exclusions



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In November of 1997, Pennsylvania voters approved a change in the Commonwealth constitution to allow a method of real property tax relief, called a homestead exclusion, to be implemented in Pennsylvania. A homestead exclusion provides real property (also known as “real estate” or “property”) tax relief to homeowners. It allows certain properties, such as homes, to receive preferential treatment under the real property tax, reducing the owner’s taxes. The November vote changed the constitution to permit the General Assembly to pass legislation implementing the homestead exclusion.

Passage of the Homestead Property Exclusion Program Act in May, 1998 (Act 50 of 1998), provided implementing language and rules for how the homestead exclusion can be used in your school district, county, and municipality (township, borough, or city). Homestead exclusions and a similar exclusion for farm properties, called the farmstead exclusion, now can be made by school districts, counties, townships, boroughs, and cities.

Under Act 50 of 1998, a taxing jurisdiction (school district, county, or municipality) can implement homestead and farmstead exclusions without any change to the existing local tax structure, as long as the jurisdiction can pay for them without increasing real property taxes. The law also provides a mechanism for school districts to change their local tax structure by relying more upon an earned income tax, and in exchange reducing the real property tax and eliminating several nuisance taxes (the per capita, occupation, and occupational privilege taxes). School districts making this change are required to use the homestead and farmstead exclusions to make these real property tax reductions.

This bulletin was developed to help you understand the homestead and farmstead exclusions, what they do, how they can be implemented in your community, and how you would apply to receive the exclusions for your own property. Because the homestead and farmstead exclusions are not necessarily tied directly to the school tax changes in Act 50 of 1998, this leaflet does not attempt to address local tax reform issues, except where they may relate to the exclusions.

What are homestead and farmstead exclusions?

What is the homestead exclusion?

The homestead exclusion is a way to target real property tax relief to homeowners who have their permanent residence in the taxing jurisdiction (school district, county, or municipality). The homestead exclusion reduces the assessed values of homestead properties, reducing the property tax on these homes. The homestead exclusion provides the same dollar tax reduction to all eligible properties in the taxing jurisdiction, including houses on farms, condominiums, single family homes, and other places of permanent residence owned by the occupant.

The homestead exclusion allows homeowners real property tax relief of *up to one half of the median assessed value of homesteads in the taxing jurisdiction (county, school district, city, borough, or township)*.^{*} If the median assessed value of homesteads in a school district is \$40,000, for example, the school district may provide for each homestead property an exclusion in tax assessment of up to one-half of that median, or \$20,000. The actual exclusion allowed will be set by the school district. All homestead properties in the school district will receive the same size exclusion, which will reduce each taxpayer's school real property tax bill. A homestead property formerly valued for tax purposes at \$50,000 would be taxed as if its value were only \$30,000 (\$50,000 minus the \$20,000 exclusion), effectively reducing its school real property tax bill by 40 percent.

What is a "homestead" property?

A homestead property is a dwelling primarily used by an owner as his or her permanent home. The owner may be living temporarily at another location, but he or she must have the intention of returning to that home. No one can have more than one permanent home at any one time. Homestead properties do not include rental units, vacation homes, camps, or other homes in which the owner does not live on a permanent basis. In general, it is the address where the owner registered to vote and has registered his or her driver's license.

The homestead property includes the land under the dwelling, as long as it is owned by the same person who owns the dwelling. The formal definition of property is the same as that used for determining residence status for the earned income tax.

^{*} The median value is the middle value of all homestead properties in the jurisdiction, when the values are arranged from smallest to largest. The median value of 10, 25, 28, 50, and 100, for example, is 28.

Why do some people want the homestead exclusion?

The recently passed school tax reform bill (Act 50 of 1998) allows school districts to shift the school tax burden from the real property tax to the earned income tax. Under Act 50, school districts can choose to levy a higher earned income tax rate, and in exchange must use these additional revenues to eliminate nuisance (per capita, occupation, and occupational privilege) taxes and reduce the real property tax. More of the school tax revenue required locally will come from the earned income tax, and less will come from the real property tax. The homestead exclusion is intended to target real property tax relief to homeowners, to ensure that the real property tax reductions go first to those who own their own dwellings.

What is the farmstead exclusion?

The farmstead exclusion is a similar method of targeting real property tax relief to farmers. It lowers the taxes farmers pay on farm buildings (other than the farm house, which receives tax breaks through the homestead exclusion), as long as at least one farm owner lives on the farm. This reduction is in addition to other existing real property tax relief programs aimed at farms, such as Act 319 (often referred to as "Clean and Green"), which reduces the assessed value of farmland.

The farmstead exclusion allows farmers real property tax relief similar to that provided to homeowners by the homestead exclusion. By law, if a homestead exclusion is offered in a taxing jurisdiction (county, school district, city, borough, or township), the farmstead exclusion also must be offered. The farmstead exclusion is set by the governing body and cannot exceed the amount of the homestead exclusion.

What is a "farmstead" property?

A farmstead property includes all buildings and structures that are used primarily for agricultural purposes (such as housing animals or storing supplies, production, or machinery) on a farm of ten contiguous acres or more in size. The farmstead must be the permanent residence of at least one owner, as defined under the homestead definition. The farmstead exclusion would be applied to buildings and structures that are not already exempt from real property taxation under other laws. The requirement that an owner live on the farm means that farms owned and operated by absentee owners will not be eligible for the farmstead exclusion.

Why do some people want the farmstead exclusion?

The farmstead exclusion is intended to target some additional real property tax relief to farmers, who also argue that the real property tax is particularly unfair to them. Compared to other local businesses, some argue, farmers pay an unfair amount of local taxes. Unlike other local businesses, the majority of a farm's productive assets (land and buildings) are subject to local taxation through the real property tax. This isn't true for most nonfarm businesses, whose productive assets are nontaxable items such as machinery, inventory, and office equipment. Compared to businesses of the same size in their own communities, farmers thus can owe much more in real property tax.

In addition, as for other taxpayers, the amount farmers owe in real property tax is not directly related to their ability to pay those taxes. The taxes are based on the value of the land, including its speculative value for development, and not on the value of what farmers can make from farming that land. The "Clean and Green" program helps reduce taxes on farm *land* to what can be made from farming, but it does not apply to the *buildings* on a farm.

How do homestead and farmstead exclusions work?

How do homestead and farmstead exclusions reduce real property taxes?

The amount of real property tax owed by any taxpayer is the tax rate (measured in mills) multiplied by the assessed value of his or her property (see Example 1). If the assessed value of the property is made smaller, the amount of the tax owed will be smaller. With a homestead exclusion of \$20,000, for instance (see Example 2), the taxpayer in Example 1 would owe only \$600 in taxes. Notice that under the homestead exclusion the percent reduction in assessed value (\$20,000 reduction in value ÷ \$50,000 original value = 40%) is the same as the reduction in taxes (\$400 saved ÷ \$1000 owed before = 40%).

Example 1:

A taxpayer in Sample School District with a property assessed at \$50,000 will owe \$1,000 in property tax if the tax rate is 20 mills (2 percent).

Assessed value X tax rate = Tax owed

or

\$50,000 X 20 mills (2 percent) = Tax owed

or

\$50,000 X 20 mills (2 percent) = \$1,000

Example 2:

The same taxpayer in Sample School District receives a \$20,000 homestead exclusion on his or her property, and now will owe only \$600 in property tax. The homestead exclusion provides a \$400 tax savings to the taxpayer.

(Assessed value – homestead exclusion) X tax rate = Tax owed

or

(\$50,000 – \$20,000) X 20 mills (2 percent) = Tax owed

or

\$30,000 X 20 mills (2 percent) = \$600

The homestead exclusion will be based on and will change *assessed* values, not *market* values. Market values are the price at which a property would sell with both a willing buyer and seller. Assessed values are the values used in calculating real property taxes, and always are calculated as a percentage of market value. The percentage used on all properties in a county to calculate assessed values is set by the County Board of Assessment Appeals during reassessment, and is called the assessment ratio. Unless the property itself is changed in some way that affects its market value, through either physical improvements or demolition, this assessed value will not be changed or recalculated until the next reassessment occurs.

How can homestead and farmstead exclusions be implemented in my community?

In general, the homestead and farmstead exclusions are implemented in a taxing jurisdiction by action of the local elected officials. Initially, they must decide to implement the exclusions and (most importantly) decide how to pay for them. The Homestead Property Exclusion Program Act specifically prohibits raising real property tax rates to pay for the homestead or farmstead exclusions, so another source of revenue must be found. For most jurisdictions, this will be possible only through tax reform, because they will need substantial new revenues to pay for the exclusions. Some jurisdictions with a major budget surplus may be able to implement the exclusions as well.

School districts also can implement the homestead and farmstead exclusions by adopting the new local tax structure under Act 50 of 1998, which shifts the local tax burden from the real property tax to the earned income tax. Real property tax reductions resulting from school tax reform in Act 50 of 1998 must be accomplished through the homestead and farmstead exclusions. Depending upon how much additional revenue a school district receives from changing its earned income tax, the school district also may have to reduce real property tax millage rates if its new homestead and farmstead exemptions would exceed the constitutional limit of 50 percent of the median assessed value of homestead properties in its jurisdiction. This new tax structure (and thus the exclusions) are

implemented locally through a voter referendum initiated by the school board or local voters.

Property owners enroll their properties for the homestead and farmstead exclusions through an application to their county tax assessment office. This office then will use these applications to calculate the median value in each taxing jurisdiction and the total value of properties receiving the exclusions. County tax assessment offices are required to update and provide this information annually to local officials for their use in setting the size of the exclusions. Although the application handling and reporting responsibilities will create additional work for county offices, Act 50 of 1998 includes a one-time \$6 million grant to help defray startup costs.

When local officials get the information from their county tax assessment office, they then must set the size of the homestead and farmstead exclusions they will provide in their jurisdiction. The maximum size of the homestead exclusion is half of the median assessed value of homestead property in the jurisdiction, as determined by the county assessor. The size of the farmstead exclusion cannot be larger than that of the homestead exclusion. Local officials will have to ensure that the exclusions are not set too high or they won't be able to afford to pay for them.

If the jurisdiction crosses county lines (as school districts sometimes do), the exclusions in both parts of the jurisdiction across the county line must be the same after adjusting for the common level ratios. The homestead and farmstead exclusions also must be adjusted after reassessment.

Will the homestead and/or farmstead exclusion be the same on my school, county, and municipal taxes?

No. Each homestead property will be subject to three different homestead exclusions: 1) the homestead exclusion for your school district taxes, which will be set by the school district and based on the median value of homesteads in your school district; 2) the exclusion for your county taxes, which will be set by the county and based on the median value of homesteads in your county; and 3) the exclusion for your city, borough, or township taxes, which will be set by your municipality and based on the value of homesteads in your municipality. These values likely will be different because assessed values vary across and within jurisdictions. Farmstead properties similarly will be subject to three different farmstead exclusions.

What are the effects of homestead and farmstead exclusions?

Do the homestead and farmstead exclusions provide real tax savings?

Yes and no. The homestead and farmstead exclusions forbid school districts, counties, and municipalities from raising real property tax rates to make up for tax revenue lost due to the homestead or farmstead exclusion. On the other hand, it is important to remember that these tax reductions are not free; they must be paid for with increases in other local taxes. If *school districts* implement the exclusions under Act 50 of 1998, the exclusions will be paid for through the earned income tax. *Counties and municipalities* must find another way to pay for the exclusions because these jurisdictions are not included in Act 50. Someone must pay more so others can pay less.

Not all taxpayers will end up saving more in local taxes once the exclusions have been paid for. An individual home owner may receive a smaller real property tax bill due to the homestead exclusion, but also may end up paying more in other taxes as a result. Some people with relatively high job incomes may end up paying more in the earned income tax than they save, while homeowners with low incomes or not much earned income (such as retirees) may pay less overall.

Is this the end of the real property tax?

No. Because the homestead exclusion exempts only a maximum of one-half of the median assessed value of properties, most properties still will owe some real property tax. It may mean the end of real property taxes for owners of properties worth less than half of the median value of homesteads, and it will provide reductions in real property taxes to other owners of eligible property.

In addition, the homestead and farmstead exclusions by themselves only forbid raising real property tax rates to make up for tax revenue lost due to the homestead exclusion. Jurisdictions still will be able to raise real property tax rates in the future as they need more tax revenue. If school districts implement the exclusions as part of tax reform under Act 50, however, they will be able to make only limited increases in the future without getting voter approval, as one condition to their accepting the new tax system.

Will my taxes go down or up if the homestead exclusion is implemented?

If your own property is eligible to receive the homestead and/or the farmstead exclusion, the amount of real property tax reduction your property receives depends upon: 1) whether the exclusion is set at the maximum amount or at some smaller level; 2) the overall value of homestead property in your community; and 3) how the value of your own property compares to the median value of homesteads in your community.

The homestead exclusion can be a maximum of one-half of the median value of homestead properties in the jurisdiction. Some jurisdictions may choose or be able to afford only a smaller exclusion (such as one-quarter of the median value). A larger exclusion should provide you with a larger real property tax reduction. The farmstead exclusion cannot be larger than the homestead exclusion.

The overall value of homestead property in the community affects the size of the homestead exclusion; if properties in general are worth a lot, the dollar value of the homestead exclusion will be high because the median value of homestead properties likely will be high. If the median value of homestead properties is \$50,000, the maximum exclusion for all eligible properties will be \$25,000 (half of the median value of \$50,000); in contrast, if the median value is \$70,000, the homestead exclusion in the jurisdiction will be a maximum of \$35,000 (half of the median value of \$70,000). A larger median value in the jurisdiction means that larger homestead and farmstead exclusions are possible in that jurisdiction.

The *percentage* reduction in your real property tax bill will be influenced by how the value of your own property compares to the median value of homesteads (see Table 1). If your property is worth less than the median value of homestead properties in your community (and your jurisdiction uses the maximum homestead exclusion of one-half the median value), you may experience a more than 50 percent reduction in property taxes. Conversely, if your property is worth more than the median homestead, you may experience a decrease of less than 50 percent in your real property taxes.

In the example shown in Table 1, notice that all properties receive a \$30,000 reduction in value due to the homestead exclusion. The properties with the lowest values receive the largest percentage reductions in their taxes, while the more highly valued properties receive smaller percentage reductions. Everyone's taxes are reduced by \$600, but this has a bigger relative impact on properties with smaller values than on those with larger values. An owner of a property with an initial value of \$40,000 in this sample community would enjoy a 75 percent reduction in property taxes, while this same \$600 would represent only a 30 percent reduction in real property taxes to the owner of a property valued at \$100,000.

In general, who benefits and who loses from the homestead exclusion?

How the homestead exclusion is paid for in a jurisdiction will have a big effect on who benefits and who loses from it. Jurisdictions considering implementing the homestead exclusion should make a thorough and objective analysis

Table 1. Effect of homestead exclusion on properties in a sample jurisdiction.

- Median value of homesteads: \$60,000
- Homestead exclusion: half of median value, or \$30,000
- Tax rate: 20 mills

Without the Homestead Exclusion		With the Homestead Exclusion of \$30,000		Percent Decrease in Real Property Taxes
Property Value	Tax Owed	Property Value	Tax Owed	
\$30,000	\$600	\$0	\$0	100%
\$40,000	\$800	\$10,000	\$200	75%
\$50,000	\$1,000	\$20,000	\$400	60%
\$60,000	\$1,200	\$30,000	\$600	50%
\$70,000	\$1,400	\$40,000	\$800	43%
\$80,000	\$1,600	\$50,000	\$1,000	38%
\$90,000	\$1,800	\$60,000	\$1,200	33%
\$100,000	\$2,000	\$70,000	\$1,400	30%

of the potential effects on their own community. In general, however, the homestead exclusion should benefit permanent residents who own their own home in the taxing jurisdiction. All eligible property owners in the jurisdiction will receive the same dollar savings, but as Table 1 illustrates, this will make a bigger difference for owners of properties with lower values than for those who own properties with higher values.

Depending upon how the exclusions are paid for, renters generally will lose under a homestead and farmstead exclusion. Rental properties are not considered homestead properties, so they will be ineligible for the exclusion. Renters, however, at least indirectly pay the real property tax; rent usually is set by landlords to cover all expenses, including the real property taxes on the property. If taxes are high, rent will be higher than if taxes are low. Renters will be hurt by the exclusion because they likely will be paying more in local income taxes (to pay for the exclusion) but will not receive any reduction in the amount they indirectly pay in real property tax.

Local businesses will not benefit from the homestead exclusion, which is designed to ensure that property tax reductions go to home and farm owners. On the other hand, they will not pay more in real property or other local taxes because of the homestead exclusion if it is implemented under tax reform. If the exclusions are implemented by using budget surpluses and are followed by real property tax increases in the future, they may end up paying more real property tax in the future because of the exclusion.

In general, who benefits and who loses from the farmstead exclusion?

How the farmstead exclusion is paid for in any one jurisdiction similarly will have a big effect on who benefits and who loses from it. Jurisdictions considering implementing the farmstead exclusion should make a thorough and objective analysis of its potential effects on their own community. In general, however, the farmstead exclusion should benefit family farmers who live on their farm. All eligible farm owners in the jurisdiction will receive the same dollar savings, but as Table 1 indicates, this will make a bigger difference for owners of properties with lower values than for those who own properties with higher values.

If the farmstead exclusion is paid for through local income taxes, local residents who pay that tax will bear the costs of the exclusion. Resident farmers will be paying higher income taxes to pay for the exclusions, just like other residents, but they also will be receiving the homestead exclusion on their home in addition to the farmstead exclusion. The farmstead exclusion is received in addition to the homestead exclusion on any eligible farm.

How can I get a homestead or farmstead exclusion on my property?

How do I apply for a homestead or farmstead exclusion?

To receive a homestead or farmstead exclusion on your property, file an application form with your county assessor. If the assessor determines that your property is eligible, you will receive the exclusion(s) if they have been implemented by your county, school district, and/or municipality (township, borough, or city).

The deadline for applying will be set by each county, but can be no later than March 1 of each year. The county commissioners can adopt a schedule for reapplications or for reviewing previously approved properties. The assessor must provide public notice at least 75 days before the filing deadline so people will have enough time to apply.

If your application for a homestead or farmstead exclusion is denied, the assessor must provide you with a written notice by first-class mail no later than 120 days after the filing deadline. Failure to provide such notice is deemed an approval of the application.

If my application is denied, how can I appeal?

If your application is denied, you can appeal the assessor's decision to your county's board of assessment appeals. The exact name of this board varies depending upon the class of county. Appeals generally are limited to whether the parcel under question meets the definition of "farmstead property" or "homestead property."

What are my responsibilities under the homestead and farmstead exclusions?

If your property receives the homestead or farmstead exclusion, you must notify the county assessor if your use of the property changes to a nonqualifying use (if, for instance, you move out of your home and rent it to others, or convert the farm buildings to a nonfarm use). You have 45 days after such a property change to notify the assessor. If you fail to notify the assessor within the time deadline, you could be found guilty of a misdemeanor of the third degree and be sentenced to pay a fine not exceeding \$2,500, plus any taxes you should have paid but did not due to the exclusions (with interest), plus an additional penalty of 10 percent of the unpaid taxes.

References

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This publication is intended strictly to help you understand more about the homestead and farmstead exclusions. The material is general and educational, and is not intended to be legal advice, nor to replace the need for legal advice. If you need legal counsel, you should seek the aid of a competent professional in your area.

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