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PROPERTY TAX INCENTIVES TO
PRESERVE FARMING IN AREAS OF
URBAN PRESSURE

by

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Property Tax Incentives to Preserve Farming in Areas of Urban Pressure

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A concern with the "preservation" of farming is widespread in the United States, especially in areas that have experienced rapid urban growth in recent years. One of the most popular devices for modifying the impact of urban influences upon farming is provision for the levy of real estate taxes on the basis of the farm value of farmland rather than on the basis of the prices for which farmland is sold when it is being transferred to a nonfarm use.¹

I shall argue that farm-value assessments can be instituted in a way that materially affects the farming decisions of many farmers under one very important set of circumstances, although not under many other circumstances. I shall argue that traditional economic thinking, by its assumptions, denies the existence of the circumstances under which farm-value assessments can promote the continuance of farming and focuses instead only upon those in which it cannot.

First, I shall outline in general terms the two kinds of circumstances to which I refer above and discuss the factors that perpetuate these circumstances and make them important. Following that, I shall discuss as examples Orange and Suffolk counties in the New York metropolitan area.

CLASSIFICATION OF THE RURAL-URBAN GRADIENT

Bryant in a recent paper has subdivided the rural-urban continuum into five classes: rural, semirural, semisuburban, suburban, and urban.² Bryant defines his classes as follows:

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¹ Thomas F. Hady and Ann Gordon Sibold, *State Programs for the Differential Assessment of Farm and Open Space Land*, United States Department of Agriculture, Economic Research Service, Agricultural Economics Report no. 256 (Washington, D.C., April 1974); Robert J. Gloudemans, *Use-Value Farmland Assessments: Theory, Practice, and Impact* (Chicago: International Association of Assessing Officers, 1974).

² William R. Bryant, *Farmland Preservation Alternatives in Semi-suburban Areas*, Agricultural Economics Extension 75-5 (Ithaca, N.Y.: Cornell University, April 1975).

1. *Rural*.—Few urban pressures are present in rural areas, although some nonfarm people live in the countryside. Farming and other extensive activities are the primary uses of land. Farmland seldom sells for more than its farm value. Owners of farmland have very low expectations about the possibility of selling their land for more intensive uses.

2. *Semirural*.—Urban pressures are an important part of the physical setting in semirural areas. The nonfarm population in semirural areas outnumber the farm population by more than 10 to 1. Farmland sells for up to three times its farm value when transferring to a nonfarm use, with much land speculation present. Many landowners hope to sell their farmland for nonfarm uses, but most will be unable to do so within the next five years.

3. *Semisuburban*.—There is hardly a landscape in a semisuburban area that does not include many nonfarm residences. The nonfarm population in semisuburban areas outnumber the farm population by more than 30 to 1. Farmland sells for five times or more its farm value, and landowners have high expectations about the possibility of selling farmland for nonfarm uses. Unlike semirural areas, there is a good possibility that nearly all the farmland in semisuburban areas could sell for at least twice its farm value within five years.

4. *Suburban*.—These areas are mostly residential, with some commercial and industrial uses present. A few estate-type farms may be found, but there are no full-time commercial farms. Prices of land in suburban areas may be ten or more times its farm value.

5. *Urban*.—City parks are the only type of open space found in urban areas. Intensive land uses, whether they be residential, industrial, or commercial, occupy nearly all the land in urban areas.

One might argue with the precise points at which Bryant has located his class boundaries, but his definitions do highlight the diffuse nature of the urban-rural interface and the dimensions in terms of which an "urban gradient" might be defined. The dynamic nature of events in the belts that surround our cities is emphasized, and landowner expectations under conditions of uncertainty are identified as at least a critical element.

ADAPTABILITY OF FARM-VALUE ASSESSMENTS TO GRADIENT CLASSES

If we take Bryant's gradient classes as he has defined them, there is only one class in which it appears likely that farm-value assessments can be fully effective in sustaining continued farming. This is the semirural class. Farming is not being inhibited by urban influences in rural areas, while in suburban and urban areas very little or no farming remains, and the nonfarm demand for land sustains prices so high that no real estate tax adjustments could induce the few farmland owners who are still there to refrain from selling to nonfarmers or from converting the land to a nonfarm use themselves.

Farming frequently has been declining quite rapidly in semisuburban areas, and, as Bryant has defined this class, most landowners who are still farming there find possibilities for a nonfarm sale too great to make a permanent

commitment to farming attractive, regardless of any tax incentives that may be offered. Farming in most areas requires continuous repair and updating of real estate improvements. It is not enough simply not to sell to a nonfarmer. Farming can be preserved only when it is attractive enough to call forth the commitments implied in a continuous stream of capital investments. Other factors also are necessary for the preservation of farming. There must be a continuous supply of highly skilled and strongly motivated farm operators. Rates of return in farming are not high enough to make it clearly preferable to the economic alternatives that are close by in semisuburban areas. Farming also is highly dependent upon the supplies and services that can be provided only by specialized agribusiness firms. There is a critical minimum mass of farming that is needed to support these specialized activities, and farming in most semisuburban areas is slipping below this level.³

But if tax adjustment can contribute so little in so many of Bryant's classes, why can it make a critical difference in the semirural areas? And are there, indeed, such areas?

TRADITIONAL ECONOMIC THOUGHT ABOUT THE RURAL-URBAN INTERFACE

It is at this point that the unrealistic nature of traditional economic thinking becomes evident. That thinking assumes that all actors in economic processes have full knowledge of all relevant matters. In the case at hand, this means a knowledge of the rate of future urban growth and of the housing preferences of the people involved. Theoretical discussions usually assume also that land conditions, combined with local preferences, are such that urban growth advances in a solid wall across the countryside, consuming all in its path. This theory contains no basis for predicting long fingers of urban penetration into rural areas or the diffuse scatteration of urban uses across the countryside.

This theory denies the existence of speculation, because it denies the uncertainty that underlies speculation. It fails to address itself to situations in which some land is selling for prices much above what farmers could pay out of farm income, while adjacent, and in all discernible respects equivalent, land fails for years to sell or, if forced onto the market, sells for a much lower price.

The nationwide rise in land prices has helped to obscure the true nature of the semirural land market. Deviations of the real market from the ideal could be explained as very transitory aberrations. Indeed, in many areas semirural quickly passed to semisuburban and then to suburban. Now we are beginning to face the prospect in many parts of the country that semirural areas may remain in that condition for many years. Points supporting this expectation include the following:

1. A declining rate of population increase.
2. Rapid rises in the costs of commuting relative to other costs, especially escalating auto and gasoline prices.

³ Pritman S. Dhillon and Donn A. Derr, "Critical Mass of Agriculture and the Maintenance of Productive Open Space," *Journal of the Northeast Agricultural Economics Council*, vol. 111, no. 1 (May 1974).

3. The very high costs of constructing single-family dwellings of the kind associated with suburbanization.
4. The consequent shift to apartment and mobile home living with the associated popularization of a "confinement" life-style.
5. A tax "crunch" in areas of scattered settlement that makes them less attractive. This is the result of inflationary amplifications of the high costs of supplying urban-type public services to scattered settlers.

The current depressed economic conditions are aggravating the effects of some of the above factors, but these effects will surely long outlive the current recession.

It is now becoming obvious that urban people have located themselves in fingers, spotted subdivisions, and isolated houses throughout large areas that cannot possibly become wall-to-wall city. Some additional land will sell for nonfarm purposes—the processes of urban scatteration will not close down quickly—but there is no chance that a majority of the land can be sold for urban prices in these areas.

At this point it is useful to consider another respect in which traditional economic thinking is unrealistic. It neglects to include in its assumptions an allowance for the difficulties associated with land-use transfers. The difficulties of reestablishing farming in an area, for example, are often such that, once farming is gone, land well adapted to it lies idle for years, even though it has become obvious that it is not needed for urban purposes. The critical-mass problem mentioned above is a factor in this. So too is the problem of attracting skilled operators and adequate capital. The suitability of land for farming often is not obvious after it has laid idle some years. Even when a skilled operator has recognized its potential, he usually still must convince a banker of its promise. Moreover, farm improvements by this time usually are decadent or obsolete, so the banker must make funds available not only for purchasing the land but for new buildings as well. The standard rules of banking make it more difficult to finance a farm when the land and barns must be bought separately than when they come together.

Transfers out of farming also usually involve difficulties. If a landowner wishes to continue farming, it usually is unwise for him to sell individual house lots, especially frontage strips. Such sales bring residents who are not sympathetic with the noises, odors, pesticide applications, and other activities of farming. Such sales often invite vandalism. And in most semirural areas today, once the frontage is sold, there is little opportunity to sell the "backage." Generally, farmers are unwise to sell house lots for less than two or three times what they could pay for the land out of farm income. Even when these farmers consider the sale of their entire farm there are problems—the costs of moving, the risks associated with selecting a new unit in an unknown area, and the problems of reestablishing business contacts. In this case, too, farmers are often unwise to sell at prices less than two or three times what they could pay for the land from farm income.

Some farmers who sell land, of course, are ready to retire. Theoretically, all transfers out of farming could come at the close of active farm generations. Potential urban users, and even speculators, however, usually are not willing to wait the lengths of time this would imply. And the fact that they can afford to pay the prices needed to pull land out of active farming reflects some income disparities between farm and nonfarm occupations as well as some "real" difference in productivity between land used for urban purposes and that used for farming.

THE REAL ESTATE ROULETTE GAME

The uncertainties about which lands will appeal to urban users and how fast urban demand will grow invites gambling quite as much as any horse race. There simply are no known ways to predict accurately which lands will sell for \$500, \$1,000, \$5,000, or \$10,000 per acre a year or five years hence.

The land market in the semirural areas becomes a gambling game—real estate roulette. Everyone knows there is no chance that the area can become wall-to-wall urban uses within many years (Bryant sets a five-year minimum limit on this time period for semirural areas; I would prefer a longer one—say, ten years). But everyone is certain that some owners will be able to sell for quite attractive capital gains.

There is a temptation for everyone to gamble. Many "investors" buy land purely in the hope of capital gains. Even the farmers who have held the land for many years become tempted not to invest further in new barns and other farm improvements that would not increase either salability or price for nonfarm purpose. They can be well aware that, if they are not lucky enough to make a nonfarm sale, they will end up with a "junk" farm which they cannot sell even at a good farm price. Occasionally a wealthy person may be willing to buy even a run-down farm for a country estate, but there are not enough wealthy people to ensure this for every farm. Some run-down farms are held by families in unsettled estates for three or four generations. They hold in continuous hope of a high-priced sale, although they have abandoned hope of a good rate of return on their investment over the whole period of waiting. Commonly members of the second and succeeding generations have become urban workers, and, while often they are not rich, they still are not forced to sell.

The farmland itself sometimes is used for farming under these circumstances, but at best the use usually is inefficient. If farming has lost its critical mass, no skilled operators remain who want to expand. If the land is well suited to crop production for cash sale without capital improvements for lime, stone removal, drainage, or storage facilities, farmers may travel several miles to use it. But if it occurs in a dairy area, where expensive buildings and materials handling facilities are needed, it is likely not to be used at all. Brush starts to encroach rapidly in many parts of the country, and soon there is no hope ever of returning the land to farming.

Unfortunately, farmers often feel that they have to gamble this way. They

see enough scattering urbanites moving in around them to substantially raise the costs of public services and to assume control of local government. Restrictive ordinances and sharply rising taxes begin to become realities. Soon the nonfarmers, aware of what they paid for land and what the remaining farms are assessed at, press for the "highest and best use" assessment of the farms. This means that farmers are to be taxed as though all of their land really could be sold for house lots within the near future. Farmers set these prices, of course, by refusing to sell lots for less. Now the prices are being used against them.

As long as the cities were moving ever outward, farmers (and speculators too) who gambled and lost did not lose large amounts. And for the public it did not matter that farming, once destroyed, rarely returns. The land eventually became urbanized anyway.

After thirty years of urban growth it is difficult to remember that the real estate market can change. It is especially difficult, too, to visualize the possibility that quite satisfactory communities could be created in which urban and rural uses are more or less permanently intermingled. But, if we are to make the best of the legacy we have inherited from the last thirty years of sprawl, we surely must learn precisely this.

IMPORTANCE OF SEMIRURAL AREAS

The semirural areas cover very large parts of some regions in the United States. In the megalopolis, from Portland, Maine, to Richmond, Virginia, any lands that are not urban, suburban, or semisuburban are semirural. This may include as much as a quarter of the total megalopolis. Semirural areas are common on the piedmont from Richmond to Birmingham. (There should be a way to define semirural areas in terms of the lights one can see from an airplane on a clear night. A flight from Portland to Birmingham reveals a most intriguing variety of light patterns.) There is much that is semirural in upstate New York and Pennsylvania, southwestward around the Great Lakes to Milwaukee, and in the states that border the Pacific.

A study of an area adjacent to Syracuse, New York, revealed strong urban influences out to some 15 miles, with no chance for wall-to-wall city to expand more than an average of 2-3 miles in many years.⁴ A study of purchasers of rural land east of Rochester, New York, revealed similar conditions there.⁵

EXAMPLES OF SEMIRURAL AND SEMISUBURBAN AREAS

Studies are in progress in Orange and Suffolk counties, New York, that are revealing the contrasts between semirural and semisuburban conditions and documenting: (a) the way in which farming can be destroyed without enough

⁴ Howard E. Conklin and Richard G. Dymsha, *Maintaining Viable Agriculture in Areas of Urban Expansion* (Albany: New York State Office of Planning Services, June 1972).

⁵ William R. Bryant, *The Rural Land Market in Wayne County, New York*, Agricultural Economics Research 74-8 (Ithaca, N.Y.: Cornell University, August 1974).

urban alternatives to occupy more than a small part of the land, (b) the response of farmers in those areas to an opportunity to "get off the roulette wheel," (c) the reluctance of farmers in semisuburban conditions to reduce their chances for a nonfarm sale even in return for a greater assurance of being able to continue farming, and (d) preliminary indications of farmers' responses to a program for purchasing development rights as a means for preserving farming in semisuburban areas.⁶

THE ORANGE COUNTY SEMIRURAL AREA

Orange County is a semirural area. It is in the lower Hudson Valley, but above the highlands of the Hudson that cross the valley at West Point. The center of the county is about 50 miles from New York City. Suffolk is on the eastern end of Long Island and farther from New York City than Orange. The island is heavily urbanized, however, partly at least because of its recreational features and its historically good transportation facilities. The value of farm products produced in Suffolk County exceeds that for Orange, but much of Suffolk agriculture is almost a type of biological manufacturing. Nonfarm demand for land is such that all farmers could sell out on short notice at prices far above the farm value of their land. Suffolk thus qualifies as a semisuburban area.

The total population in Orange County increased 21 percent during the decade of the 1960s but still remains at an average of only 266 persons per square mile, although there are two small cities and many villages within the county. The *1969 Census of Agriculture* counted 925 commercial farms as compared with 1,757 for 1959, a decrease of 47 percent compared with a state-wide decrease of 39 percent. The value of farm production increased 42 percent in this decade, in contrast to an increase of 28 percent in the state. Field examinations indicate that, in spite of the large increase in farm output in the 1960s, farm improvements are not being maintained or replaced at levels that will permit long-run farm survival.

In the fall of 1974 a new set of assessed values was put into use throughout Orange County that roughly would have doubled taxes on farmland had there not been provisions for farm-value assessments. After the reappraisal almost none of the farmland was assessed at less than \$1,000 per acre, even though the State Board of Equalization and Assessment, acting under the Agricultural District Law, has placed a farm value of \$300-\$400 per acre on most farmland in the county. The stated policy was to assess on a "highest and best use" basis, and since at least some farmland had sold recently for house lots in all towns of the county, this use was considered highest and best. The new tax bills came out at an average of about \$50 per acre of farmland. In New York, to obtain a farm-value assessment, it is necessary for most practical purposes

⁶ Unpublished research data from New York Hatch Research Project 429, being conducted under the supervision of the author.

for the land under consideration to be within an agricultural district.⁷ The New York State agricultural district enabling legislation is designed to encourage and facilitate the continuance of farming on good farmland until it really is needed for nonfarm purposes. It accomplishes this by applying a package of provisions within districts that increase farmers' chances for continuing while at the same time discouraging nonfarm development.⁸

The law provides that districts may be formed through either landowner or state initiative, but the state has not yet used its initiating authority. A somewhat complex series of steps is needed to form a district by landowner initiative, with action occurring at both county and state levels.

Once districts have been formed, the following provisions hold within districts:

1. *Permit agricultural value assessments.*—Farmers may have the value of their land in excess of its value for farming exempt from taxation if they produce an annual average of \$10,000 in farm products and file an annual application. Land which has received this exemption is subject to a maximum five-year rollback if converted to a nonfarm use.

2. *Limit ordinances affecting agriculture.*—Local governments may not enact ordinances that would restrict or regulate farm structures or farm practices beyond the requirements of health and safety.

3. *Instruct state agencies to encourage farming.*—State agencies must modify administrative regulations and procedures to encourage the maintenance of commercial agriculture to the extent compatible with health, safety, and any applicable federal regulations.

4. *Modify eminent domain proceedings.*—The right of public agencies to acquire farmland by eminent domain is modified although not removed. These agencies are required to give serious consideration to alternative areas before good farmland can be taken for public uses.

5. *Restrict public funds for nonfarm development.*—The right of public agencies to advance funds for sewer, water, and other facilities that would encourage nonfarm development is modified.

6. *Limit special service tax assessments on farmland.*—The power of special districts to impose benefit assessments or special ad valorem levies on farmland for sewer, water, lights, sanitary land fills, and nonfarm drainage is limited.

About 3 million acres have been placed in districts in the nearly four years

⁷ Farmers outside districts who produce more than \$10,000 in farm products per year may obtain farm-value assessments by signing commitments for eight years. They must sign a new commitment each year and are subject to severe penalties if they convert the land to a nonfarm use while a commitment is in force. Very few farmers have signed commitments.

⁸ William R. Bryant and Howard E. Conklin, *Legislation to Permit Agricultural Districts in New York*, Agricultural Economics Extension 74-17 (Ithaca, N.Y.: Cornell University, August 1974); Howard E. Conklin and William R. Bryant, "Agricultural Districts: A Compromise Approach to Farmland Preservation," *American Journal of Agricultural Economics*, vol. 56, no. 3 (August 1974).

since the enabling law was passed, and district formation continues at a relatively high rate.

Nearly all full-time farms in Orange County have been placed in agricultural districts, and nearly all farmers who qualify have asked for a farm-value assessment. Few farmers in districts elsewhere in the state have asked for such assessments, although some other districts have been formed in anticipation of reappraisals that are not yet completed.

Very little farmland is being sold at the present time in Orange County, and several foreclosure actions are pending against those who bought acreages prior to the reappraisal program and the current building slump. Farmers, however, began asking for districts while land prices were still strong, even though inclusion in a district reduces a farmer's chances for a nonfarm sale at the same time that it improves his chances for remaining in farming. Many farmers interviewed recently have stated a long-standing feeling that many years would elapse before all of them could sell more than frontage, or an occasional lot, at the revaluation prices.

Farm-value assessments have reduced the taxes for which farmers in Orange County have been billed in the past year by \$1.5 million.⁹ This is a reduction of over 50 percent of what otherwise would have been their bill—an amount in dollar terms that is \$27 per acre, or \$3,000 per farm. Most farmers interviewed have indicated that they will be able financially to remain in farming at this level of taxation and will do so until they get an adequately financed offer for their whole farm at a value that will justify movement to another area. Most do not expect such an offer for many years. At the reduced level, taxes on these farms are roughly four times higher than on comparable farms in upstate areas.

At the full reappraisal level of taxes, some farmers would have been forced into bankruptcy and some others would have needed to borrow against the value of their land to pay the levies. A few who asked not to be included in a district because they thought they had sold their farms now find that the options were not picked up and therefore are paying taxes at the full reappraised level.

Taxes on other rural lands in Orange County were increased along with farmlands as a result of the reappraisal, but apparently urban-type property taxes on the average were little changed.

Traditional economic thinking would claim that, without farm-value assessments in Orange County, the price of farmland would decline to reflect the capitalized value of the tax increases. The economically optimum use of farmland still would remain farming, and use therefore would not change, although farmland owners would suffer diminutions in their estates.

This analysis ignores the capital structure of farm businesses, the continuous need for large new capital investments, the scarcity of the skills needed for

⁹ Personal correspondence from Robert Bosman, formerly attorney for the New York State Board of Equalization and Assessment.

successful farming, and the psychological effect on farmers of what appears to be an attempt by new scatteration residents, through their control of local government, to avoid paying the high public service costs they are creating, by transferring them to farmers. Young farmers normally borrow heavily to get started in farming. They operate with narrow margins. An increase in taxes of \$3,000 per farm could make it very difficult to meet their debt payments. And the scarcity of farm skills, combined with the scarcity of capital, would make it difficult for others to pick up the farms of the bankrupt operators.

As noted above, many of the farms in Orange County now are much in need of new, modern barns. Farmers in the recent past have hesitated to invest new capital. Surely to have found their taxes doubled would not have stimulated renewed confidence in the future of farming. The dominance of the point of view of the newly arrived nonfarmers in local government is underlined by the fact that the reassessments were, in the farmers' words, "rammed down their throats."

Agricultural districts not only provide an opportunity for farmers to obtain farm-value assessments but give farmers some assurances that the newly dominant urban point of view will be less able to harass them in other ways. Farmers in the county still do not speak with high levels of confidence about their future. Some are hoping to move elsewhere in the state, and others are urging their sons to move or choose another occupation. Many, however, are beginning to become cautiously optimistic. Clearly their confidence is absolutely prerequisite to the "preservation" of farming in Orange County.

THE SUFFOLK COUNTY SEMISUBURBAN AREA

The agriculture of Suffolk County differs sharply from that in Orange. While the value of farm products is a third greater, the area of land in commercial farms is only 40 percent as much. In fact, only 10 percent of the total land area of Suffolk County is used by farmers, in contrast to 30 percent in Orange.

The market prices of open-land acreage appear to be some three to five times higher in Suffolk than in Orange. The value of the farmland for farming is on the order of twice that in Orange, but clearly it is nonfarm factors that sustain the high market prices. All farmland in the county could be sold quickly at prices well above farm value. Not all of it would be "housed up" quickly. Some would go into estate-type developments, some would be used for recreation, and some, of course, would be held speculatively for some time.

With an assurance of a nonfarm market for their land, farmers in Suffolk County have not initiated formation of agricultural districts. For them an increase in their chances to stay in farming, including reduced real estate taxes, would not be adequate compensation for a reduction in their chances for a nonfarm sale.

It is true that Suffolk County has not yet undertaken a countywide reassessment effort, and farmland still is assessed well below its market price for

nonfarm uses. On the other hand, farmers there are well aware that such an effort is very likely in the future and that approvals for agricultural districts can be obtained more easily before reassessment than after.

There is a strong interest in Suffolk County, however, in preserving some of the farming, and the county has become a pioneer in developing a practical program for public acquisition of development rights.¹⁰ County funds have been budgeted for this purpose, and offers to sell these rights have been solicited from landowners. Appraisals and negotiations are now in progress.

Public purchase of development rights would leave farmers with only the right to use their land for farming. A market-value assessment then would be a farm-value assessment. Even levies of inheritance taxes would henceforth be based on farm value and therefore less likely to disturb farm operations.

SUMMARY

Economic thinking traditionally has dismissed farm-value assessments of farm real estate as an ineffective means for securing the continuance of farming in the face of urban growth. In the traditional model such assessments do not change the use that is optimum, although it is recognized that they may modify income distributions and thus raise equity questions.

I have argued that the traditional model does not adequately reflect institutional and psychological reality. Given the vast uncertainties associated with urban growth, the almost random nature of some events in urban growth areas, the heavy demands of at least some types of farming for continuous infusions of new capital, the rules that govern capital availability, the scarcity of farming skills, critical-mass requirements for the continuance of farming, and the impact of some political acts upon the confidence of farmers in the future of their industry within given areas, I have argued that assessment policies can have a direct affect upon farming in semirural conditions.

I have argued at the same time, however, that if farm-value assessments are combined with other provisions for protecting farmers from the impact of scattering urbanites, as in New York's agricultural districts, the total effect will be increased more than proportionately.

But I have pointed out that chances for a high-priced nonfarm sale can be so high that farmers are not willing to trade any reductions therein for increased assurances that they can continue farming. This is the condition in semisuburban areas as represented by Suffolk County. Suffolk's unique experiment in the public acquisition of development rights on farmlands certainly will reveal some important new insights.

¹⁰ John V. N. Klein (County Executive), *Farmland Preservation Program: Report to the Suffolk County Legislature* (Hauppauge, N.Y., September 1973).