

More property tax due after selling farmland (2/2/19)

The obligation to pay real estate tax (RET) falls on a person that is recognised as RET payer at the beginning of the year. The RET Act also imposes a 1.5% surcharge on any farmland that is left unfarmed. Who stands to pay the surcharge if such land is sold early in the year and the Rural Support Service (RSS) finds at the year end it has not been farmed properly?

The root of the problem

This question arose in a dispute heard by the administrative court. A person had sold farmland early in the year and paid the full RET charge due for the period left until the year end. The RSS later notified the municipality that the land had been surveyed and recognised as unfarmed. So the municipality required the former owner to pay the surcharge, too. The person objected in the belief he was no longer responsible for farming the land or paying the surcharge.

A surcharge liability falling on the former owner

The RET Act provides that both the standard rate and the surcharge are payable by the person that is recognised as RET payer at the beginning of the year, and the payment obligation stands until the next tax year after ownership or possession expires. Only a lot of up to one hectare or subject to statutory farming restrictions escapes the surcharge. So if the new owner, who is not yet recognised as RET payer in the year of sale, neglects to farm the land, the former owner will face the adverse financial consequences. Why?

Firstly, the surcharge encourages the owner to farm the land or take at least minimum steps necessary to keep the land in good farming condition and prevent its environmental degradation. The RSS procedure for recognising land as unfarmed implies that unfarmed is land that has not been farmed in a long time. So the former owner is allowed enough time to take steps to avoid the surcharge.

Secondly, the procedure for imposing the surcharge allows the landowner to estimate how much RET will be due if he neglects to farm the land as required by law.

Thirdly, efficient collection is crucial in tax law. Farmland may change hands several times a year, and finding the person held liable for neglecting the land creates an extra financial and administrative burden, putting at risk RET collection and achieving the statutory purpose. And the Constitutional Court of Latvia has found that the procedure for imposing the surcharge meets the principle of proportionality.

PwC recommendation

When it comes to drafting a contract for the sale of farmland, it is advisable to insert a clause that provides for compensating the former owner if he is liable to pay the surcharge.