

# Real e-State

An electronic newsletter for real estate professionals

From the desk of:

## The Real e-ditor



Actress and comedienne Lily Tomlin once said "The road to success is always under construction." We are all on the road to success. Some of us travel it a little faster, others a little slower. Some of us will arrive invigorated and refreshed. Others may be detoured and sidetracked along the way. Some may never make it all the way there. But, ultimately, we're all looking for pretty much the same basic rewards in life: personal health; happiness; money; power; and perhaps respect. As the new year begins, this is as good a time as any to check the map and compass on each of our respective roads to success.

I do that by first reflecting on the year that was. What goals did I set? Did I achieve them? Were my goals honest goals? Or were they too easy, or too difficult? What have I learned from last year's successes and shortcomings that can shape my ambitions for this year? Who helped me along the way, and how can I show them my appreciation for their help?

After taking stock, I sit down with pencil and paper (or at my computer), and start writing random thoughts about things I would like to accomplish over the next twelve months. I think about all kinds of goals, both personal and professional. This process is scary and inspiring at the same time. If you are not a goal-setter, and I wasn't until just a few years ago, the hardest part about goal-setting is getting started.

Get over that natural self-consciousness you feel when examining your deepest desires and ambitions. Goal setting is not selfish, it is self-reflective. Getting to better know and understand what *will* make you happy (not what makes you happy) is a great motivating force. If you have never set personal goals before, why not give it a go? You have nothing to lose. And who knows? You might just find that the road to success will take some unexpected and exciting turns for the better!

**A problem is a chance for you to do your best.**

~ Duke Ellington

## EYE ON THE COURTS

BY: DAVID M. SAPERSTEIN

### Arbitration

In a closely-watched case involving whether a real estate agent is an appropriate party in arbitrations between buyers and sellers, the Michigan Court of Appeals ruled against the agents. In an unpublished opinion issued 2/1/05, *Real Estate One, Inc. v. American Arbitration Assn.*, Real Estate One ("REO") sued the American Arbitration Association ("AAA") in an attempt to extricate itself from buyer-seller arbitrations. Consistent with an arbitration program of the Michigan Association of Realtors, REO included an arbitration provision in its standard purchase agreements. Although REO is not a party to the purchase agreements, it had found itself named as a party in disputes between buyers and sellers. Accordingly, REO filed a lawsuit requesting the Court to order AAA not to list REO as a party in all future claims filed with AAA under the arbitration provision.

REO argued that it was not itself a party to the purchase agreements, and therefore had not agreed to arbitration. It argued further that requiring REO to address the issue of whether it was a proper party in each arbitration was costly and unnecessary. The Court ruled that whether REO was a proper party to a particular dispute depends upon the individual facts of the case. Accordingly, although not deciding the issue of whether REO was a proper party to any individual arbitration, the Court refused to issue an injunction against AAA that would be applicable to all future disputes.

**"Real Estate One ("REO") sued the American Arbitration Association ("AAA") in an attempt to extricate itself from buyer-seller arbitrations."**

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## EYE ON THE LEGISLATURE

BY: DANIELLE M. SPEHAR

In a prior issue of Real e-State we evaluated the U.S. Supreme Court's decision in *Kelo v. New London* (04-108) in which the power of local government to condemn private property for economic development, even by a private developer was reaffirmed. The Kelo Court held that the U.S. Constitution does not prohibit such takings, although states are free to prohibit them. In analyzing *Kelo*, we noted that the Michigan Supreme Court ruled in *Wayne County v. Hathcock* that seizing private property for economic development purposes violates the Michigan Constitution, even though the development contributes to the health of the general economy. In July 2005, we questioned whether Michigan would ultimately acquiesce to the reasoning of the U.S. Supreme Court

in *Kelo*.

On August 31, 2005, Michigan State Senator Tony Stamas introduced a resolution to place before voters in the next general election a constitutional amendment to prohibit the taking of private property by state or local governments and transferring it to a private entity for the primary benefit of that private entity, rather than for "the use or benefit" of the public. If passed by the voters, the proposed resolution would place in the Constitution a standard similar to the Michigan Supreme Court's 2005 ruling in *Hathcock*, which reversed its 1981 "Poletown" ruling, and held that a government taking is not justified just because a different use of the property might increase government tax revenues.

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# PROPOSED REFORMS STREAMLINE CURRENT TAX CODE AT THE EXPENSE OF DELETING CHERISHED DEDUCTIONS

BY: KASTURI BAGCHI

Tick tock! Tick tock! The time to prepare and file those dreaded tax returns is less than three months away. For most of us, this yearly ritual is cumbersome and complicated at best because of the detailed record-keeping, confusing instructions and complex forms. The good news is that the members of the President's Advisory Panel on Federal Tax Reform (the "Panel") "feel your pain." The Panel's November 2005 report recommends two different tax schemes, both of which are designed to make the tax code "simpler, fairer and more conducive to economic growth" as required by the President.

After twelve public meetings, the Panel has proposed two alternatives to the current tax code to satisfy the President's criteria, namely the Simplified Income Tax Plan (the "SIT Plan") and the Growth and Investment Tax Plan (the "GIT Plan"). While the two plans vary in the taxation of business and capital income, the SIT Plan and GIT Plan do share the following common traits:

- Both plans strive to simplify the tax filing procedure by "allowing every taxpayer to use a simple tax form which is less than half the length of the current Form 1040...[and] eliminating a complicated set of phase-outs that leave taxpayers wondering whether they are eligible to benefit from numerous provisions."

- Both plans purport to increase the fairness of the present tax code by "shifting some tax preferences from de-

ductions, which tend to benefit high income households, to tax credits, which benefit all taxpayers equally,...[by] reducing marriage penalties by ensuring that the rate brackets, the Family Credit, and the taxation of Social Security benefits for married couples are twice the amounts for singles,"

and by eliminating the Alternative Minimum Tax which has become an additional tax burden on many unsuspecting middle income households.

- Both plans encourage economic growth by "reducing the double-tax on

corporate profits earned in the United States ...[and] lowering the top marginal rates on individuals and businesses." By way of example, the current tax code contains the following six tax brackets: 10%; 15%; 25%; 28%; 33%; and 35%. Under the SIT Plan, the tax brackets have been identified as 15%, 25% 30% and 33% while the GIT Plan tax brackets are 15%, 25% and 30%. With respect to large businesses, the current tax code implements eight tax brackets, while both the SIT Plan and GIT Plan have only one tax bracket. In terms of the double tax on corporate profits, the current scheme taxes dividends at 15% or less which will increase to ordinary tax rates after 2008. The SIT plan, however, excludes 100% of dividends generated by domestic companies while the GIT Plan maintains a tax on such dividends at the 15% rate.

The goal of the Panel to provide a simpler, fairer and pro-growth tax code is laudable. But, in the 200 plus page report prepared by the Panel lurks recommendations by the Panel under both the SIT Plan and GIT Plan which may endanger two of Americans' most cherished deductions.

**The Free Press reported that this proposal has caused a huge uproar because of "worries that ... [it] will cause people to hold off on buying or selling houses and depress values for more expensive homes."**

The first target is home mortgage interest. Presently, home mortgage interest may be deducted by itemizers for interest up to \$1.1 million of mortgage debt. The Panel has proposed to convert this deduction into a tax credit available to all taxpayers equal to

15% of the mortgage interest paid on debt ranging from \$227,000 to \$412,000 based on the average regional price. The Detroit Free Press reported on October 16, 2005

that this proposal has caused a huge uproar from the developer and realtor com-

munities because of "worries that ...[it] will cause people to hold off on buying or selling houses and depress values for more expensive homes." The Detroit Free Press also disclosed that recently the "Congressional Budget Office said capping the deduction at \$500,000 could increase tax revenue by nearly \$50 billion from 2006 to 2015."

It is beyond the scope of this article to determine if (possibly) bursting the real estate bubble is a lesser evil than increasing the tax revenue to lower the ever expanding national deficit. However, trying to assess the impact of the Panel's proposal with respect to home mortgage interest on the average taxpayer is an equally difficult task. By converting the

home mortgage deduction into a tax credit for all tax payers on a lower mortgage amount could mean an increase in the adjusted taxable income for many Americans. But this could be offset by the lower tax brackets and the reduction of the marriage tax penalty. In other words, a case by case analysis is required.

The second deduction that the Panel seeks to eliminate altogether is state and local taxes. Currently, itemizers can deduct state and local taxes. But under the SIT Plan and GIT Plan, no deduction or credit is given to any taxpayer for such taxes. As in the case of the mortgage interest deduction, the impact of this elimination must be analyzed on a case by case basis because there are other mitigating factors to consider.

With the President's recent low approval ratings, debating the pros and cons of the Panel's reforms may be a bit premature. The White House may seek to avoid additional controversy so soon after the President's failed campaign to privatize Social Security. Perhaps next year at this time we will have a better understanding of the fate of the Panel's tax reforms.

## Courts (Continued from Page 1)

Does this mean that real estate agents should not include arbitration provisions in their purchase agreements? Not necessarily. The arbitration clause does not create the conflict between the buyers and sellers; it merely establishes the forum for the litigation. If the buyers were willing to file an arbitration claim against the real estate agent, they would probably be just as likely to sue the agent in Court. Accordingly, the question is whether the agent would prefer any such claims (hopefully rare) to be litigated in Court or in arbitration.

### Release of real estate agent

In a recent, published opinion, *Hall v Small*, the Michigan Court of Appeals reviewed and upheld the enforceability of a provision in a closing document that held the agents harmless for conditions in certain systems. Following the closing, the buyers discovered mold problems and sued both the sellers and real estate agents for alleged misrepresentations.

The sellers argued that the hold harmless provision was not enforceable because only the buyers and sellers had signed it, not the real estate agents. The buyers argued fur-

ther that there was no consideration for the contract because the agents did not agree to perform any act or pay any money. The Court disagreed and dismissed the real estate agents. The Court held that there was no ambiguity in the contract and no misunderstanding of the contract terms. The Court held further that the hold harmless provision was properly considered part of a larger contract, consisting of numerous documents signed at closing. Because the buyers and sellers each agreed to perform certain obligations in the overall contract, the contract was supported by consideration and enforceable.

Unlike the other two cases cited in this article, the Court's opinion in *Hall* is published. This is significant because it means that future cases are required to follow its reasoning. Real estate agents who want some protection against being named in a dispute between buyers and sellers, may want to consider incorporating a release into their standard closing documents.

### Renewals

Another unpublished case highlights the importance of following exactly the procedures for renewal specified in a lease. In

*Beckett Properties, Inc. v. Warrant Radio Company*, issued 8/18/05, the plaintiff's commercial lease with the defendant granted the plaintiff/tenant two successive renewals upon ninety days' written notice. Notices were to be in writing and sent by registered or certified mail to the defendant/landlord. Unfortunately for the plaintiff, it sent the renewal notice by email. Although the defendant received the email, it decided to lease the property to a third party. The Court unanimously held that the plaintiff had not validly exercised the option to renew because the exercise was not in strict compliance with the contractual language.

**Every man should be born again on the first day of January. Start with a fresh page. Take up one hole more in the buckle if necessary, or let down one, according to circumstances; but on the first of January let every man gird himself once more, with his face to the front, and take no interest in the things that were and are past.**

~Henry Ward Beecher

## Legislation (Continued from Page 1)

After several committee amendments, the revised Joint Resolution passed in the House (106 to 0) and the Senate (31 to 6) on December 13, 2005. The Resolution places before voters in the next general election a constitutional amendment which restricts but does not eliminate the use of eminent domain by state or local governments to take private property from one person and transfer it to another. While the Joint Resolution does not permit takings for purposes of "economic development" or for increasing tax revenues, if the objective is to eradicate urban "blight," then the burden of proof would be on the condemning authority to demonstrate "by clear and convincing evidence" that the particular property is being taken for a public use, i.e. that the particular property is blighted. In other cases the condemning authority would only have to meet the less stringent "preponderance of the evidence" standard. If a taking is of an individual's principal residence the person would have to be paid at least 125 percent of the fair market value.

The matter now lies in the hands of Michigan voters to determine whether the use of eminent domain to take private property will be restricted in Michigan.

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**An optimist stays up until midnight  
to see the new year in. A pessimist  
stays up to make sure the old year  
leaves.**

**~Bill Vaughan**

## EPA ISSUES FINAL RULE ON STANDARDS FOR ENVIRON- MENTAL INQUIRY

BY: MARTIN B. MADDIN

Anyone who deals with the transfer of commercial real estate understands the significance of conducting environmental due diligence. On November 1, 2005, this was highlighted once again as the Environmental Protection Agency ("EPA") published its final rule regarding the federal standards and practices for conducting an "All Appropriate Inquiry" ("AAI" and/or the "Rule") into a property's environmental condition (40 CFR Part 312). The AAI standards and practices "are intended to result in the identification of conditions indicative of releases and threatened releases of hazardous substances on, at, in or to the subject property."

The new Rule is significant because compliance with the Rule is a prerequisite to qualifying for certain landowner liability protections under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"). Examples of such landowner liability protections include defenses for "innocent landowners," "bona fide prospective purchasers," and "contiguous property owners." In addition to the foregoing landowner liability protections, parties receiving grants to conduct characterizations or assessments of brownfield properties under EPA programs must conduct them in compliance with the new AAI standards.

According to the Rule, an AAI report is valid for one year prior to the date of acquisition of the property, but any interviews, lien searches, review of federal, state, tribal and local government records, visual inspections, and the declaration by the environmental professional cannot be more than 180 days old. If the AAI report is more than one year old, an entire new AAI report must be prepared.

Additionally, in an attempt to ensure the quality of the AAI, the Rule requires that environmental professionals meet certain experiential and educational standards. Specifically, the Rule defines an environmental professional as "a person who possesses sufficient specific education, training, and experience necessary to exercise professional judgment to develop opinions and conclusions regarding conditions indicative of releases or threatened releases on, at, in, or to a property, sufficient to meet the objectives and performance factors" of the Rule, and has: (1) a current Professional Engineer's or Geologist's license or registration from a state, tribe or U.S. territory and three years of relevant full-time work experience; or 2) a federal, state or tribal issued certification or license and

three years of relevant full-time work experience; or (3) a Baccalaureate degree or higher in science or engineering and five years of relevant full-time work experience; or (4) ten years of relevant full-time work experience (the "Professional").

Furthermore, the Rule requires that certain inquiries and analyses be made by the Professional, while other inquiries must be made by or for the prospective landowner. The Professional must: 1) interview past and present owners, operators and occupants (owners of nearby properties must also be interviewed if the property has been

"abandoned"); 2) review historical sources of information as far back "as it can be shown that the property contained structures or from the time the property was first used for residential, agricultural, commercial, industrial, or governmental purposes";

3) review federal, state, tribal and local government records; 4) make visual inspections of the facility and adjoining properties; 5) obtain commonly known or reasonably ascertainable information; and 6) evaluate the degree of obviousness of the presence or likely presence of contamination at the property and the ability to detect the contamination by appropriate investigation.

The prospective landowner, or the Professional if such obligations are delegated to the Professional, must: 1) search for environmental cleanup liens; 2) make an assessment of any specialized knowledge or experience the prospective landowner may have; 3) make an assessment of the relationship of the purchase price to the fair market value of the property, if the property was not contaminated; and 4) obtain commonly known or reasonably ascertainable information.

Finally, after making such inquiries and analyses, the Professional must prepare a written report that includes: 1) a declaration by the Professional that he or she meets the qualifications for environmental professionals under the Rules; 2) a declaration that the AAI was performed in accordance with the requirements of the Rule; 3) an opinion on whether conditions indicative of a release or threatened release of hazardous substances at the property have been identified; and 4) whether any data gaps exist and the significance of such gaps.

Ultimately, the Rule should result in a more comprehensive environmental picture of the property. However, this will likely result in increased costs and a longer waiting period for the completion of environmental due diligence.