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An electronic newsletter for real estate professionals

From the Desk of

The Real e-ditor
Steven D. Sallen

Tax, Tax and More Tax! Vendor Payments, Assessed Value, Business and Classification!

They say only two things are certain in this world: *death* and *taxes.* With government budget deficits dominating the domestic news these days, the basic tax burden for you and me is not likely to ease! So, to that extent, we do have some certainty. The problem is, tax *policy* in America is far from certain! We know the ox will be gored; the question is, whose ox will be gored? Understanding tax policy, and how it impacts virtually every fabric of our lives, is critically important. Just ask a life insurance agent or estate planning expert whether tax policy affects their business and the businesses of their clients! Every time a client inquires about the possibility of foreclosure of real property, the discussion inevitably turns from the damage caused by the obvious loss of investment, to the less obvious tax implications of giving a property back. Often injury follows insult, where seven figure losses, can result in similar sized tax implications!

In some countries, the "long view" may mean twenty, fifty or even one hundred years. In modern America, the long view is measured in weeks or months, certainly not years! Proper planning becomes challenging, and often more a matter of political tea leaf reading, than real strategizing. Perhaps that is why the cable news channels spend so much time hyping the next election cycle, even before the dust settles on the previous campaign.

Of the five articles in this issue of *Real e-State*, four are tax-related, and demonstrate how tax policy is influenced by the politics of every branch of government. In our bipolar political landscape, federal, state and local fiscal policies and taxing priorities seem to lurch first to the left, then to the right, and back again. The result of all this uncertainty is felt in boardrooms and living rooms all across the country.

The following pages demonstrate these rapidly shifting political sands, at every level (federal, state and local) and branch (executive, legislative and judicial) of government. With every city, county, state and the federal government drowning in red ink, you can be sure that the left-right-left debate over how much of your money you get to keep will continue hot and heavy for years! Protecting your hard earned money will require frontline intelligence and constant vigilance.

Steve Sallen

Rollback of Onerous IRS Form 1099 Reporting Requirements

By: William E. Sigler

The Health Care Reform Bill, passed last year, contained a provision that would, starting in 2012, require businesses that make a payment to a vendor for goods or services of over $600 annually to report that amount to the IRS on a Form 1099. This much-criticized requirement has now been repealed by the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011. It might have been repealed sooner if they could have come up with a shorter name for the statute.

The reporting requirement was repealed largely because of the concern voiced by many small business owners, that the new reporting requirements would be very burdensome. Repeal of the requirement means that the law reverts to the rules that were in effect prior to passage of the Health Care Reform Bill. Thus, businesses must continue to issue Form 1099s for payments of $600 or more to service providers. Likewise, the exception for reporting payments made to corporations remains in effect.

The new law also repeals a provision in the 2010 Small Business Jobs Act that, after December 31, 2011, would have required landlords to issue Form 1099s for payments of rental property expenses if those payments exceed $600 annually, even if the rental

"The reporting requirement was repealed largely because of the concern voiced by many small business owners …"

operations of those landlords did not arise to the level of a trade or business. This means that landlords do not need to report specific rental property expenses unless they are otherwise required to be reported under the tax laws. For example, landlords whose rental operations amount to a trade or business must continue to issue Form 1099s if their payments to service providers are over $600 annually.

If you have any questions regarding this or any other tax issues involving your business or rental properties, please do not hesitate to contact us.

Transfers That May Unexpectedly Upcap Taxable Value

by: Mark H. Fink

In 1994, Michigan voters passed Proposal A, amending the Michigan Constitution to limit annual increases in property tax assessments. The purpose of Proposal A was to limit tax increases on property, as long as it remains owned by the same party, even though the actual market value of the property may have risen at a greater rate. Subsequent amendments of the General Property Tax Act (GPTA) "capped" annual assessment increases at the lesser of 5% of the assessed value of the property for the previous year, or the increase in the rate of inflation from the previous year. After certain "transfer[s] of ownership" occur, however, the "taxable value" becomes uncapped and thus subject to reassessment based on actual property value.

> ***"… a surviving spouse who remarries and quit claims to himself and his new spouse, jointly ... is a "transfer" of ownership for purposes of the GPTA …"***

The Michigan Supreme Court recently resolved two questions relating to the effect of transfers of ownership involving joint tenancies, including ownership by husband and wife as a tenancy by the entirety. The first question involved the transfer of ownership by right of survivorship; *i.e.* the death of one of the joint tenants. In that situation, the Court held that because the change in ownership occurred by operation of law, it does not constitute a "conveyance" and, therefore, is not a "transfer" of ownership for purposes of the GPTA. Consequently, the death of one joint tenant does not uncap the taxable value of real property.

On the other hand, the Court ruled that, where the surviving joint tenant (now the sole owner) conveys title to himself and another (as, for example, a surviving spouse who remarries and quit claims to himself and his new spouse, jointly), there is a "transfer" of ownership for purposes of the GPTA, and in that situation, the taxable value is uncapped. Thus, a series of seemingly permitted transfers without uncapping, can have the cumulative effect of uncapping the property assessment for purposes of the GPTA.

For more information, see *Kloosterman v City of Charlevoix,* or contact Maddin Hauser.

The Coming And Going Of A Michigan Business Tax

by: Geoffrey N. Taylor

On January 27, 2011, Michigan Governor Rick Snyder introduced a draft of the Michigan Corporate Income Tax Act ("Act"). If enacted, this tax would replace the current Michigan Business Tax beginning January 1, 2012. However, certain aspects of the Michigan Business Tax, including the nexus, apportionment, and unitary provisions, are continued in the new Act. According to Governor Snyder, replacing the Michigan Business Tax with a simple, fair and efficient corporate income tax will even the playing field and enable all businesses and industries, large and small, to grow and create jobs.

Unlike the Michigan Business Tax, only C corporations would be subject to tax under the Act. So called "pass-through" entities, such as S corporations, partnerships, limited liability companies and sole proprietorships, would be exempt from tax under the Act. Owners of those entities would continue to pay tax on business profits under Michigan's individual income tax scheme.

The proposed income tax rate is a flat 6%. The proposed tax base is federal taxable income subject to certain adjustments before allocation or apportionment (*e.g.*, for non-Michigan revenues). A major criticism of the Michigan Business Tax is that it imposes tax liability even if a business is losing money; this would be rectified under the new Act.

The Act would also eliminate the existing system of tax credits and deductions, retaining from the Michigan Business Tax only the Small Business Alternative Credit, which allows smaller businesses to pay an alternative 1.8% tax on adjusted business income.

It is estimated that replacing the Michigan Business Tax and the Corporate Income Tax with the Act will result in revenue loss to the state treasury of approximately $1.8 billion, on a full-year basis. The Act also contains a restructuring of the Income Tax Act applicable to individuals, which is intended to offset this loss and make the shift to the Corporate Income Tax revenue neutral, beginning in fiscal year 2013.

Look for future updates concerning the Michigan Corporate Income Tax Act in future issues of *Real e-State*, or contact your Maddin Hauser attorney.

State Tax Commission Withdraws Classification Appeals

by: Kasturi Bagchi

Last summer, *Real e-State* readers were made aware of the campaign launched by the State Tax Commission (STC) to reclassify real property and/or personal property from "industrial" to "commercial" status for property tax purposes, by filing 10,331 classification appeals with the Michigan Tax Tribunal (MTT) pursuant to MCL 211.34c(7).[1] The STC publicly announced that its goal was to prevent certain tax benefits from being awarded to owners of personal property improperly classified as "industrial" by the tax assessor.[2] The MTT began hearing these appeals in November 2010 and it has been rumored that, at least in the early cases, the Department of Treasury, acting on behalf of the STC, failed to meet its burden of proof.[3] Without much fanfare, the STC held a meeting on December 7, 2010 in which they resolved to *withdraw* all 10,331 classification appeals.[4]

Does this signal an about-face by the STC? The December 7 Memo and Bulletin 22 of 2010 issued simultaneously by the Department of Treasury (the "Bulletin")[5] would suggest otherwise. In the Bulletin, the Department of Treasury reaffirms the STC's position as follows: (i) the legislature intended to provide certain tax breaks only to manufacturing and processing businesses in Michigan; (ii) "because of erroneous interpretations of [MCL] 211.34c, businesses that clearly do not qualify have been receiving the exemption"; and (iii) "industrial parcels used to define industrial personal property as defined in MCL 211.34c(3)(c) means parcels on which manufacturing and processing is taking place."[6] The December 7 Memo confirms that the STC approved the Bulletin and then "directed staff to prepare orders to change the classification for properties believed to be inappropriately classified for the 2009 and 2010 years."[7] This clearly suggests that the reclassification campaign is not over and that the STC will be taking a different approach rather than resorting to the MTT.

> ***"… the STC held a meeting ... in which they resolved to withdraw all 10,331 classification appeals."***

The STC may be waiting to unveil its new approach until a decision is rendered in *Iron Mountain v. Naftaly, docket number 140817,* where the Michigan Supreme Court is examining the constitutionality of a provision of MCL 211.34c(6) which provides that there is no appeal available from STC classification decisions. This case will have a significant impact on the reclassification process, so stay tuned in future *Real e-State* issues for updates.

Endnotes:

[1]See *Reclassification of Property By the State Tax Commission Threatens Loss of Tax Incentives*, by Kasturi Bagchi and Michael K. Hauser, *Real e-State*, July 2010, Volume 7, Issue 3, available at www.maddinhauser.com.

[2]For a greater discussion of these benefits and the motivation behind the campaign, see *id*.

[3]The author spoke with a representative of the STC on April 14, 2011 who did not want to be identified in this article. The representative confirmed that the MTT made it very clear to the STC in these early cases that it would not rule in the favor of the STC. So rather than wait for a ruling to be issued and reported, the STC withdrew the appeals prior to a final determination by the MTT.

[4]*See* Memorandum dated December 7, 2010 from Kelli Sobel, Executive Director, State Tax Commission to Assessors and Equalization Directors available at www.michigan.gov/treasury.

[5]Also available at www.michigan.gov/treasury.

[6]The Department of Treasury also noted the following within the Bulletin: (i) "only warehousing directly associated with manufacturing and processing can be considered industrial"; and (ii) a property that qualifies for the industrial facility tax exemption or is zoned industrial is not automatically deemed industrial property.

[7]Whether the STC has authority to re-classify property in such a manner is questionable. The plain language of MCL 211.34c(1) would suggest that only the assessor has the right to classify property while MCL 209.104 authorizes the STC "to give advice and counsel to assessing officers."

New Law Grants Special Lease Termination Rights To Residential Tenants

by: Michelle C. Harrell

Michigan legislators have given a powerful remedy to victims of stalking, sexual assault or domestic violence, but perhaps at the expense of uninvolved residential landlords. M.C.L. 554.601b (the "Act") took effect as of October 5, 2010, and amends the Landlord and Tenant Relationships Act to provide residential tenants who have been subjected to stalking, rape or domestic violence with special lease termination rights. The policy behind the Act is that persons who are being victimized should be able to relocate for their personal safety without being subjected to rent liability. The Act does not differentiate between stalking, sexual assault or domestic violence and provides qualifying tenants with the same lease termination rights.

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New Law Grants Special Lease Termination Rights

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The Act applies to all residential leases even if the lease does not refer to the Act. The Act provides that a lease may contain a reference to the Act and give notice to the tenant of his or her rights. However, if the lease does not contain the suggested provision stated in the Act, the landlord is required to post written notice of the Act's provisions that is visible to a reasonable person in the landlord's property management office or deliver written notice to the tenant when the lease agreement is signed.

Specifically, the Act is applicable to any tenant who (1) has a reasonable apprehension of present danger to the tenant or his or her child from domestic violence, sexual assault or stalking while that person is a tenant, and (2) is subject to a residential lease that was entered into, renewed or renegotiated after October 5, 2010. Even if a tenant qualifies under the Act and meets the notice and documentation requirements described below, any co-tenant that does not also meet those same requirements remains fully liable upon the lease. The Act does not apply to, or change any requirements relating to security deposits and prepaid items (such as first and last months rent), and those amounts continue to be subject to applicable statutory requirements other than the Act.

To be released from his or her rental obligation, the tenant must meet specific notice and supporting documentation requirements under the Act, including: (a) a valid personal protection order (PPO), or an order removing an abusive person from a home issued by a court that remains in effect as of the date that it is submitted to the landlord; (b) a valid probation order, conditional release order or parole order that is still in effect upon submission to the landlord that indicates that the person subject to the order is subject to conditions necessary to protect the tenant or child of the tenant, such as a no-contact provision; (c) a written police report that has resulted in the filing of charges by the prosecuting attorney if the charges were filed not more than 14 days before submittal of the notice to the landlord; (d) a written police report that resulted in the filing of charges by the prosecuting attorney if the charges were filed more than 14 days before submittal of the notice to the landlord if the tenant demonstrates a verifiable threat of present danger from domestic violence, sexual assault or stalking, which can be shown by the submission of the report described in (e); or (e) a report in substantially the form set forth in the Act that is verified by a licensed health or mental health professional, a clergy member or a crisis center counselor.

> *"… the landlord is required to post written notice of the Act's provisions that is visible to a reasonable person in the landlord's property management office …"*

If the tenant meets the notice and supporting documentation requirements, the tenant is released as a matter of law from any obligation to pay rent, no later than then first day of the second month that rent is due after the notice is given. The tenant's release from his or her rental payment obligation does not take effect until after the tenant vacates the leased premises. In other words, the tenant is not entitled to remain in possession of the leased premises without paying rent.

After the tenant vacates, the landlord is prohibited from intentionally releasing forwarding address information or documentation submitted by the tenant to the person that was identified as the source of the tenant's reasonable apprehension of domestic violence, sexual assault or stalking. The landlord is allowed to reveal forwarding address information only as reasonably necessary to accomplish a landlord's regular and ordinary business purpose.

If a tenant submits a notice and supporting documentation under the Act, and you are not certain if you are required to release a tenant from his or her rent payment obligations, please contact us and we will be pleased to review your situation.

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