

32nd Annual
Tax Symposium

**PULLING THE CAP OFF OF
UNCAPPING EVENTS**

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PRESENTATION OVERVIEW

A BRIEF OVERVIEW OF PROPOSAL A TAX LAW IN MICHIGAN.

- HOW TO IDENTIFY “UNCAPPING EVENTS” UNDER PROPOSAL A WITH SPECIAL EMPHASIS ON RECENT TRENDS
- WHAT IS THE DIFFERENCE BETWEEN AN “ADDITION” AND AN “UNCAPPING” EVENT?
- HOW TO AVOID COMMON “UNCAPPING EVENTS”



AN OVERVIEW OF PROPOSAL A

- In March 1994, Michigan voters approved a constitutional amendment (Proposal A) meant to address (a) school funding inequities and (b) high property taxes.
- Proposal A included two key provisions affecting Michigan property tax law:
 - Growth on taxable value of individual parcels of property is limited to the LESSER of inflation or 5%; and
 - When property is SOLD or TRANSFERED, its resets to the State Equalized Value (“SEV”).

AN OVERVIEW OF PROPOSAL A

- **SEV Definition:** One half of your property's fair market value. If a property is worth \$500,000 according to the taxing authority, the SEV is \$250,000. So, if total mills on a property are 50 mills (1 mill for every \$1K of value), property taxes are \$12,500.
- **Taxable Value:** The value of real property taking into account the protections of Proposal A.
- **Example:** In 2022, Dan Campbell purchases a property worth \$1,000,000. For the 2023 year, the SEV and TV will be the same. With a 50 mill tax rate, taxes owed for 2023 will be \$25,000. In 2023, the value of the property goes up 10% to \$1,100,000. The SEV is now \$550,000, which would trigger taxes of \$27,500, but Proposal A (barring a transfer or addition) requires taxation at the taxable value. Let's say inflation was 3%, then the TV is \$500,000 X 1.03 or \$515,000 eliciting taxes of \$25,750 (a savings of \$1,250). As the years go by, the benefits of Proposal A continue to grow.

AN OVERVIEW OF PROPOSAL A

- Proposal A codified, “The property’s taxable value in the immediately preceding year minus any losses, multiplied by the lesser of 1.05 or the inflation rate, plus all additions. MCL 211.27a(2)(a).
- What is an “addition” under Michigan Property Tax law?
- An “addition” is an increase in value caused by new construction...a physical addition of equipment or furnishings...” Article 9, Section 3 of Michigan’s Constitution.
- As an example, let’s say Coach Campbell’s home undergoes a small renovation increasing the value by \$20,000 in 2023. Then, the TV is not the aforementioned \$515,000. It is \$515,000 (TV) + the addition (\$20,000)=\$535,000.

HOW TO IDENTIFY AN UNCAPPING EVENT?

- Upon a transfer of ownership of property after 1994, the property's TV for the calendar year following the year of the transfer is the property's SEV for the calendar year following the transfer. MCL 211.27a(3).
- Transfer of ownership means the conveyance of title to or a present interest in property, including the beneficial use of the property, the value of which is substantially equal to the value of the fee interest. MCL 211.27a(6)



COMMONLY OVERLOOKED UNCAPPING EVENTS

- A CONVEYANCE TO A TRUST IS AN UNCAPPING EVENT
- Exception, when the sole beneficiary of the trust is the transferor or the transferor's spouse.
- Exception, when the beneficiary is the settlor/transferor's (or settlor/transferor's spouse's) mother, father, brother, sister, son, daughter, adopted son/daughter, grandson/granddaughter and the property is not used for a commercial purpose.

COMMONLY OVERLOOKED UNCAPPING EVENTS

- DISTRIBUTION FROM A TRUST IS AN UNCAPPING EVENT
- Exception, when the distributee of the trust is the transferor or the transferor's spouse.
- Exception, when the real property distribution is made to the settlor/transferor's (or settlor/transferor's spouse's) mother, father, brother, sister, son, daughter, adopted son/daughter, grandson/granddaughter and the property is not used for a commercial purpose.

COMMONLY OVERLOOKED UNCAPPING EVENTS

- CHANGE IN TRUST BENEFICIARY IS AN UNCAPPING EVENT
- Exception, when the change adds or substitutes the spouse of the sole present beneficiary.
- Exception, when the change is made which adds the settlor/transferor (or settlor/transferor's spouse's) mother, father, brother, sister, son, daughter, adopted son/daughter, grandson/granddaughter and the property is not used for a commercial purpose.

COMMONLY OVERLOOKED UNCAPPING EVENTS

A conveyance of an ownership interest in a corporation, partnership, sole proprietorship, limited liability company, limited liability partnership or other legal entity if the ownership interest conveyed is **more than 50%** of the corporation, partnership, sole proprietorship, limited liability company or limited partnership.



COMMON UNINTENTIONAL UNCAPPING EVENTS

- A simple transfer from Dan Campbell into Gritty, LLC is an uncapping event regardless of ownership interest in the company.
- A transfer from one business to another.
- A transfer to a Trust without meeting one of the previously discussed exceptions.

TRANSFERS WHICH ARE NOT “UNCAPPING” EVENTS

- Transfers from one spouse to another or from a decedent spouse to a surviving spouse.
- Since December 31, 2014, a transfer of residential property if the transferee is the transferor’s or the transferor’s spouse’s mother, father, brother, sister, son, daughter, adopted son, adopted daughter, grandson, or granddaughter and the property is not used for a commercial purpose.
- A transfer of real property or other ownership interests among members of an “affiliated group,” 1 or more corporations connected by stock ownership to a common parent corporation.

TRANSFERS WHICH ARE NOT “UNCAPPING” EVENTS

- A transfer of real property or other ownership interests among corporations, partnerships, limited liability companies, limited liability partnerships or other legal entities if the entities involved are **commonly controlled**.
- **Common Control:** *TRJ & E Properties v City of Lansing (2018)*: “...we decline to adopt any specific percentage as the definition of common control.”

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THANK YOU

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Overview

- We know what an “uncapping event” is within the context of Michigan property taxes.
- We know the difference between an “addition” and an “uncapping event”
- We know the pitfalls and of common uncapping events and how to reduce the chance our clients make these mistakes which can cause significant and unexpected tax increases.