

An electronic newsletter for real estate professionals

From the desk of:
The Real e-ditor



When our leaders (and news media) fail us, we all lose. Lately, examples of leadership failure abound. Detroit Mayor, Kwame Kilpatrick's widely reported personal indiscretions may have cost the City millions of taxpayer dollars to settle a whistleblower lawsuit for, what now appears to have been, a personal cover up. New York Governor Elliott Spitzer's sudden crash-fall from power likely ruined his career (to the delight of *Wall Street*), with who knows what lasting consequences for our nation's third most populace state. Idaho Senator Larry Craig resigned in disgrace last year after being nabbed in a sex-sting in an airport men's room. The Monica Lewinsky scandal dominated the news media and distracted our entire nation for much of President Clinton's second term in office.

The common theme in these, and countless other scandals involving political leaders in our country is, of course, sex. The news media simply cannot give enough coverage to the lurid and tawdry. But when it comes to covering substance, and the many weighty issues of the day that affect us all, we get only sound bytes and talking-head commentary, with precious little informed analysis. Apparently, sex sells more than just cars or lipstick.

What galls me most, however, but what got infinitesimal press coverage, was the recent release of a national study that ranked Detroit's Public Schools dead last of the 50 major school districts ranked for graduation rate of its students – just 24.9% of Detroit's public school students graduate! Just in case you missed it, I'll rephrase that. More than 75% of Detroit Public School students fail, leave or dropout of school! By comparison, the highest graduation rate among the country's 50 largest urban areas was 71.8% (Mesa Arizona), and the average graduation rate was 51.8%. Frankly, I think that even the "best" rate is terrible! And when asked by the Detroit News to comment, a Detroit Public Schools spokesman *declined* to do so. The Detroit School Board President said she doesn't believe the results. Perhaps she believes an MSU study that puts the dropout rate at 31.9%, as if that is any better.

Are you outraged? If you live in Michigan, heck – if you have a pulse, you cannot afford not to be outraged. As the economic engine of our state, Detroit runs on two fuels: 1) the money of businesses and investors who believe in our area and are willing to risk their capital to prove it, and 2) the brainpower, sweat and toil of its workforce. But if 75% of the workforce does not even graduate from high school, what businesses or investors will risk their capital here to create the good and high paying jobs we so desperately need? Even traditional Big-3 manufacturing jobs require a high school diploma or GED! How can we possibly attract new high paying, high technology jobs to a region whose major urban core does not graduate three fourths of its children from high school?

And yet in the midst of what is most assuredly an education crisis, where is the outrage? The Mayor is bogged down in his own mess, pretending it's business-as-usual. The Governor issued a bland statement through her press secretary that "[w]e must provide a quality education for every child and provide them with the tools they need to be successful ..." Inspiring, huh? Where is the call for an emergency task force? Where is the call for reorganization? Where is the call for accountability? Where is the call for some action (any action!) to demonstrate an understanding of the gravity of the situation? Who will step up and save the future for the school children of Detroit?

Steven D. Sallen
 Editor-in-Chief

**ATTORNEY GENERAL OPINION
 CLARIFIES TRANSFER TAX
 EXEMPTION PROVIDING RELIEF IN
 CERTAIN RESIDENTIAL
 TRANSACTIONS**

BY: DANIELLE M. SPEHAR

Many of our readers are already familiar with certain exemptions from transfer tax under the Michigan Transfer Tax Act, such as written instruments in which the value of the consideration for the property is less than \$100.00, or written instruments to confirm title already vested in a grantee, such as a quit claim deed to correct a flaw in title. However, there are actually 23 written instruments and types of property transfers that are exempt from Michigan Transfer Tax. [Michigan Transfer Tax = \$3.75/\$500.00 of consideration paid.]



A recent Attorney General Opinion (Opinion No. 7214), issued in response to Michigan's current housing slump, clarifies exemption "t" which applies to residential sales at prices lower than the price paid for the home when it was originally purchased by the Seller. According to the Attorney General Opinion, the criteria that must be satisfied for exemption "t" to apply are:

- 1) The property must have been occupied as a principal residence, and classified as homestead property;
- 2) The property's State Equalized Value ("SEV") for the calendar year in which the transfer is made must be less than or equal to the property's SEV for the calendar year in which the transferor acquired the property; and
- 3) The property cannot be transferred for consideration exceeding its true cash value for the year of the transfer (*i.e.*, 2 times SEV).

The Attorney General Opinion offers examples to demonstrate how the exemption may or may not apply. One example is based on a

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**MORE ON THE JOINT TENANCY
 EXCEPTION TO UNCAPPING**

BY: MICHAEL K. HAUSER

In our last issue, Lindsay Jerabek discussed the December, 2007 Michigan Court of Appeals case of Moshier v. Whitewater Twp., which endorsed a new exception to the property tax uncapping rules. In short, no uncapping was caused when "Parents" conveyed property to themselves and "Son" as joint tenants with rights of survivorship, and then "Mother" quitclaimed her interest to "Son" after "Father's" death. Homeowners who intend to pass their properties to their children may desire to engage in similar transactions to prevent property taxes from uncapping. This article is intended to provide a brief news update on the subject, and to mention some related federal tax issues.

First, it is notable that Michigan's State Tax Commission, by notice dated February 5, 2008, instructed the local assessors handling property taxes in Michigan to follow the Moshier holding. However, the notice gave a "caution" that the Moshier case "should be read with a narrow interpretation, given the specific facts" of that case. The notice also stated that the State Tax Commission "is working with the Legislature to provide clarification in the statute regarding this issue." Thus, if the Legislature agrees with the State Tax Commission's apparent conclusion that Moshier is an unintended loophole, this method to avoid an uncapping may not last long.

Second, homeowners should realize that transfers of property to themselves and a child as joint tenants are potentially taxable gifts for federal tax purposes. The amount of the gift is generally equal to the proportionate interest in

**Giftg a joint tenancy
 interest during a Parent's life
 might cause unintended current
 gift tax or have the side effect of
 increasing estate taxes after death.**

the property gifted. For example, if Parents (as 50/50 joint tenants) convey to themselves and Son (as 33/33/33 joint tenants), then Parents have made a combined gift of 33% of the house. Each Parent is allowed to make a total of \$1 million of gifts during his or her lifetime, without gift tax – and if less than \$1 million is gifted, any unused exemption amount can be used against estate tax after death. Thus, depending on the situation,

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FIFTEENTH ANNUAL REAL ESTATE SYMPOSIUM FOCUSES ON RISK MANAGEMENT

BY: KASTURI BAGCHI

If you were unable to join us at this year's Real Estate Symposium Entitled "Myth Busting - Separating Fact from Fiction in Real Estate Management" held on March 12, 2008, here are the highlights of the program:

Managing shareholder (and our very own Editor in Chief) Steven D. Sallen opened this year's symposium by noting the firm's diverse practice areas and some of the opportunities we have had over the past year to assist our clients in their successes.

Misconceptions of Insurance Coverage

Our insurance experts, Dianne Kennedy of Oswald Companies, Kenneth Korotkin of Korotkin, Insurance Group, and Harry Colburn of the Colburn Group, engaged in a lively panel discussion lead by moderator and Maddin Hauser shareholder John E. Jacobs. They examined the role of the insurance agent in the real estate due diligence process. Attendees learned that by involving their insurance professional early in the due diligence process, agents can more effectively advise them on the appropriate types and levels of coverage. Furthermore, by requiring sellers to provide loss history reports, the agent can also help you determine if the property is right for you. In the leasing and borrowing contexts, agents can also review your contracts from a risk shifting perspective to identify uninsured events (i.e., how would you pay for an indemnification). The panelists also examined some of the important basics such as the difference between an insurance certificate and a binder. The panel discussion concluded by focusing on the unintended consequences faced by a landlord under a triple net lease scenario which requires the tenant to procure hazard, liability and loss of rents insurance. The primary goal of a triple net lease is to pass on all operating costs. Our attendees learned that it does not mean that the tenant should actually purchase the insurance as the named insured. As the named insured, such an insurance policy is really designed to protect the tenant and not a third party such as a landlord. The panelists discussed some of the unintended consequences of the tenant obtaining their insurance including the following:

- i) When the tenant purchases a property hazard insurance policy including coverage for loss of rents, would the insurer pay out on a loss of rents claim? Typically, loss of rents coverage applies when the lease is terminated or cancelled; but if the lease is cancelled or terminated, no loss of rents coverage would apply because the insurable interest of the named

insured (that of the tenant) has vanished. The other problem is that loss of rents coverage applies to those insured *receiving* rental income and not *paying* rent.

- ii) When the tenant obtains the insurance, then the tenant and not the landlord will control the claims and adjustment process.
- iii) The tenant is not likely to procure as many forms of coverage as a landlord would unless the lease specifically requires the tenant to do so. The most overlooked forms of coverage include building ordinance, boiler and machinery, flood and wind.

- iv) When the tenant buys the insurance, what happens if the tenant moves out and there is a vacancy? There may be a gap in time before the next tenant moves in and meanwhile your asset may be uninsured, as vacant buildings can be difficult if not impossible to insure.

Tax Foreclosure Process and Its Impact on Credit Reports

Following the insurance panel, our next two presentations explored the property tax foreclosure process and its ramifications on your credit report. Shareholder David Hart guided our audience through a hypothetical situation related to the consequences of failing to pay real property taxes due and owing in 2006:

- i) on March 1st of 2007, unpaid taxes are reported to the county treasurer;
- ii) on June 1st, 2007, county treasurer sends out first delinquent tax notice;
- iii) on September 1st, 2007, county treasurer sends out second delinquent tax notice with notice of \$15.00 fee;
- iv) on October 1st, 2007, the additional fee of \$15.00 shall be added to the unpaid taxes;
- v) on February 1st, 2008, the county treasurer sends out third delinquent tax notice with information of additional penalties and interest;
- vi) on March 1st, 2008, the property is forfeited if the taxes remain unpaid. Once the property is deemed forfeited, a judgment of foreclosure can be sought by the applicable governmental authority. However, title to the property itself has not passed to such governmental authority. A certificate of forfeiture must be filed within 45 days;

vii) By June 15, 2008, the applicable governing authority must file a petition to foreclose; but the real property is not actually foreclosed upon so that the title passes until effectively in March 2009.

While it takes almost 3 years for you to finally lose your interest in your property due to failure to pay taxes, Courtney D. Roschek warned our audience of the negative consequences on your credit score of not acting quickly. Information concerning non-payment of taxes and tax foreclosures are commonly collected by the big three credit bureaus. This topic was also recently explored in our November 2007 issue.

To Buy or To Lease: That is the Question

Our symposium concluded with a role play between shareholder Richard F. Roth and associate James M. Reid IV discussing the pros and cons of purchasing vs. leasing real property. A few of the important factors to consider in making such a decision include:

- i) Is the client looking to make an investment and receive a return on capital;
- ii) How much control/responsibility does the client want over the real property in terms of occupancy and improvements;
- iii) Does the client want to remain flexible in terms of location; and
- iv) How well can the client absorb unanticipated expenses.

If you are interested in finding out more about the topics covered at our symposium, please log onto our website at www.maddinhauser.com for a copy of the materials.

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scenario in which a husband and wife purchased real property in 2006, occupied the property as their principal residence, and sold the home to a third party in 2008. The property's SEV when acquired in 2006 was \$74,000.00 and the SEV when sold in 2008 was \$72,000.00. Consequently, the first and second criteria are satisfied. The true cash value, which is calculated by doubling the SEV at the time of transfer, was \$144,000.00 in this case. Assuming a sales price in 2008 of \$140,000.00 then the sale does not exceed its true cash value, thus satisfying the third criteria and exemption "1" would apply. The tax savings to the selling homeowner in this case would be \$1,050.00.

Sellers must be cautioned, however, that a request to apply exemption "1" that fails to meet all three criteria could result in imposition of a penalty equal to 20% of the tax assessed in addition to the tax due. Also, no similar exemption exists for County Real Estate Transfer Taxes.

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*If opportunity doesn't knock,
build a door.*

*~Milton Berle,
actor*

Recent Construction Lien Act Amendments Benefit Homeowners and Contractors

By: Stuart M. Dorf

Are you or one of your clients thinking about building a dream house? How about renovating an existing one? Do you represent contractors, subcontractors, suppliers or laborers? If so, this short bulletin is for you.

The Michigan legislature passed a series of amendments effective January 3, 2007 ("Amendments") to the Michigan Construction Lien Act ("Act") in an effort to increase protections to homeowners as well as subcontractors, suppliers and laborers. For homeowners, the Amendments to the Act increase both obligations and consumer protections in rather significant ways. In terms of obligations, owners are now required, upon receipt of the a sworn statement, to give notice that the sworn statement was received, to each subcontractor, supplier or laborer that provided a notice of furnishing or those named in the sworn statement if notice of furnishing was excused. Further, an owner now may not accept a full or partial waiver of lien from a person other than the lien claimant named in the waiver of lien, without verifying its authenticity.

Offsetting the new obligations are several new protections. First, the Michigan Department of Labor and Economic Growth (the "DLEG") is now mandated to maintain a website of contractors whose failure to renew licenses or pay subcontractors, suppliers and/or laborers causes the Homeowner Construction Lien Recovery Fund¹ to make a payment. Secondly, homeowners can search the database to avoid doing business with those contractors who are unreliable, and bring an action to discharge a lien previously recorded by a person who rendered services, but *was not licensed* as required by law. If the homeowner prevails in such a suit, the unlicensed person will be liable for damages, including costs and attorney fees that resulted from the recording and attempts to enforce the improper lien.

Subcontractors, suppliers and laborers have also experienced new burdens and benefits from the Amendments. The Amendments require a supplier to have documentary proof that he has obtained a credit application from the contractor or subcontractor before providing the material or equipment and obtain a credit report to determine the financial stability of the subcontractor or contractor. No recovery from the Fund will be permitted if: (i) the credit report

discloses insolvency at the time of application or within 2 years of the application; (ii) receivership; or (iii) total delinquent judgments of more than \$1,000.00. The Amendments also limit payments to suppliers who continue to supply material or equipment in an amount greater than the credit limit established by the supplier or if the contractor or subcontractor



was delinquent in paying a debt to the supplier in excess of a certain timeframe at the time the material or equipment was supplied. One of the benefits of the Amendments is an increase in the maximum recovery of a subcontractor, supplier and/or laborer under the Fund from \$75,000.00 per residential structure to \$100,000.00. Moreover, the legislature took additional steps to insure the Fund continues to remain solvent. Rather than providing

for one-time assessments and fees *and* potential surprise assessments, the Amendments now require the payment of ongoing renewal fees until the Fund's balance reaches \$6.0 million; once the \$6.0 million dollar threshold is met, renewal fees are to be suspended. However, the Amendments also provide for reinstatement of renewal fees when the Fund's balance falls back below \$4.0 million. The revisions of the fee structure are intended to create a more stable source of revenue for the fund.

So the next time your clients decide to work with contractors, subcontractors, suppliers or laborers, make sure they are aware of the new burdens and protections afforded to them by these Amendments.

¹ The Homeowner Construction Lien Recovery Fund (the "Fund") was established by the State of Michigan to provide a means of economic redress in the event that all debts owed on a home building or remodeling project were not paid by the licensed contractor. Unpaid subcontractors or suppliers of goods or services can be protected from loss by presenting their claims to the Fund after following all required procedures.

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the joint tenancy interest gifted to Son. To prevent double taxation, Parent's estate would effectively get a credit for gift tax already paid.

While it is difficult to generalize about what steps would be advantageous for estate and gift tax purposes, it is clear that estate and gift tax issues should be considered before beginning to convey joint tenancy interests which are more geared at preventing property taxes from uncapping.

Although a current conveyance of a joint tenancy interest may be a taxable gift, if Parent in the above example remains a joint tenant at the time of his/her death, the Parent's estate will likely include