

An electronic newsletter for real estate professionals

From the desk of:

The Real e-ditor



The real estate market now seems to be in a "holding pattern" here in Southeast Michigan. Not that there is no activity. On the contrary, most people I speak with seem busy this Summer; myself included. However, many new deals seem designed to limit losses, rather than to make profits. This fact was reinforced to me recently when a client sent me a letter of intent and asked me to prepare a new lease for one of his buildings. When I analyzed the proposed terms, I was shocked to learn that landlord's cost of building out the tenant improvements was roughly equal to the value of three years of base rent. And the lease term was only three years!

When I pressed my client to explain his logic in doing the deal, he said: "I need a tenant in the building. There is no mortgage on the property, and the tenant will cover a portion of the tax, insurance and common area maintenance charges. With luck, they will renew in three years and then I can make some money." His point was that even though it was a lousy deal, it was better than no deal. And of course, there is always the upside that three years from now the tenant may prefer to renew at a rental rate more favorable to the owner.

As I wrestled with this cold new reality, it struck me that a lot of our clients are in this predicament. Tenants are demanding (and getting) buildouts, periods of free rent, shorter terms, and lower rental rates. The mindset of some building owners has to be, if we can shorten sail and batten down the hatches, we should weather this storm all right. The only questions are, how long will this storm blow, and do we have enough sea-room? Sea-room in the case of real estate ownership can be translated as capital or, at least, positive cash flow. My client's lack of a mortgage on the building gave him the "sea room" to make that lease deal.

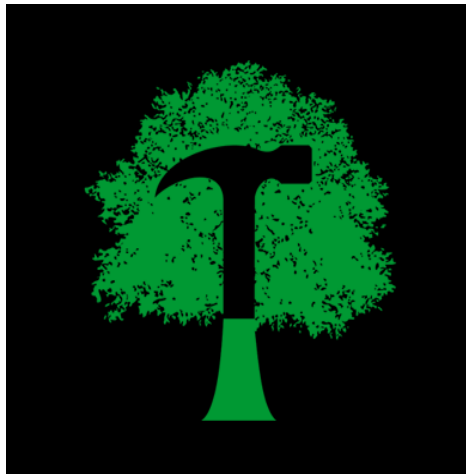
So, if our region's foul winds have you battering down your hatches, take heart . . . you're in good company. Let's just hope this "storm" blows itself out soon.

Steven D. Sallen
Editor-in-Chief

THE "GREENING" OF REAL ESTATE: DEMAND COMPELS ACTION

BY: LINDSAY A. JERABEK

We are rethinking what cars we drive (goodbye gas guzzling SUV's), what we eat (goodbye trans fats), how we light our homes (hello compact fluorescent bulbs) . . . and more recently, the quality of our living and working spaces. Like it or not, the environmental movement is permeating and redefining the real estate market with force and speed.



This article is intended to give a brief look at what is to come from Maddin Hauser in the upcoming year, as we follow and respond to the growing industry of sustainable or "green" development.

It goes without saying that the state of commercial and residential real estate leaves a lot to be desired during this nationwide economic decline, especially in Michigan. Refreshingly, studies are emerging which indicate that investment in green building yields promising economic returns, such as increases in real estate values.

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DEADLINE LOOMS FOR MORE STRINGENT REQUIREMENTS FOR ABOVEGROUND STORAGE TANK SYSTEMS

BY: DANIELLE M. SPEHAR

Effective August 13, 2008, state rules require that all above-ground storage tanks (ASTs) used to store flammable and combustible liquids must have spill protection, overfill protection and corrosion protection. The new rules enacted by the Michigan Department of Environmental Quality ("MDEQ") Waste and Hazardous Material Division in 2003 had a five-year grace period, which expires August 12, 2008. These new rules apply to ASTs of any size, regardless of their date of installation. Previous rules had excluded coverage for tanks installed prior to 1992, however, no such exclusion exists under the new rules. Under the new requirements, storage tanks installed after August 13, 2003 are referred to as "new" and storage tanks installed before August 13, 2003 are referred to as "existing."

Owners and operators of ASTs must choose one of the following actions for an existing AST: (1) add spill, overfill protection, and corrosion protection; (2) replace existing ASTs with new ASTs that conform to all requirements of the rules; or (3) close the existing ASTs by August 12, 2008.

"Failure to meet the impending deadline may result in the issuance of citations, fines or "red tag" status"

If you elect to replace or close an existing AST, 30 days ad-

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MICHIGAN SUPREME COURT SLAMS THE DOOR ON TRANSFER TAX LOOPHOLE CREATED BY COURT OF APPEALS

BY: KASTURI BAGCHI

In February 2008, the Michigan Supreme Court issued an order based on its underlying decision reported in *Lake Forest Partners 2, Inc. v. Michigan Dep't of Treasury*, 2007 WL 2887220 (Mich 2007), which ultimately reversed and remanded an earlier ruling of the Michigan Court of Appeals which had allowed developers, builders and purchasers of newly constructed buildings to reduce transfer tax liabilities arising under the State Real Estate Transfer Tax Act, MCL 207.521, *et seq.* ("SRETTA").

The facts in *Lake Forest* are straightforward. The developer entered into 45 purchase agreements, each containing a promise to sell vacant land *and* to construct a home on such land. Separate prices were recited for the lot and for construction of the home. The purchase agreements were not recorded and title was transferred by recording warranty deeds after construction was completed. At the time the deeds were recorded, the developer paid state and county transfer taxes based on the value of the unimproved lots. The state subsequently ordered the developer to pay penalties and satisfy a tax deficiency equal to the difference between transfer taxes based on the value of the unimproved lots and the value of the improved lots.

With respect to assessing transfer taxes under SRETTA, the Court of Appeals found that Section 522(e) requires the value of the real property to be determined "at the time of transfer", but that Section 523(1) does not require payment of the transfer tax until the instrument

evidencing the transfer is recorded. 271 Mich. App. 244, 248-253 (Mich. App. 2006). Because an equitable interest in each lot was transferred to each purchaser at the time the purchase agreements were entered into, the Court of Appeals concluded that the developers rightfully paid state transfer taxes based solely on the value of the unimproved lot.

On appeal, the Michigan Supreme Court held that the findings of the Court of Appeals contradicted the unambiguous language of SRETTA and that the developer should have paid state transfer taxes on the basis of the value of the improved lots, not the unimproved lots. Specifically, the Supreme Court found that SRETTA "imposes a tax on the value of the transfer effectuated by the instrument that is being recorded." 2007 WL 2887220 at 4, *quoting* 271 Mich.App. at 253.

This finding is substantiated by Section 523(1) of SRETTA, which only imposes a tax on certain *recorded* instruments evidencing a transfer. Even though an equitable interest may have transferred to the purchasers when the purchase agreements were executed, these instruments were not recorded. The plain language of SRETTA requires the transfer tax to be imposed on the recorded instrument that evidences the transfer, which in *Lake Forest* are the deeds as opposed to the purchase agreements. Because the statute requires the transfer tax to be assessed at the time the transfer is evidenced by a recorded instrument, it would only make sense to determine



the value of the property at the time such instrument is recorded. Since the consideration paid for the deeds in *Lake Forest* included the cost of the lot and the home, the aggregate value was the appropriate basis for measuring the transfer taxes due and owing.

When a single purchase agreement governs both the sale of unimproved land and the construction of improvements, state transfer tax liabilities increase by postponing the valuation of the property from the time the purchase agreement is executed until the time the deed is recorded. However, methods already being used to prevent the uncapping of taxes could also mitigate transfer tax liabilities so that you pay transfer taxes on the unimproved lot only. For example, notably in *Lake Forest*, with respect to the county transfer tax deficiency arising under the County Real Estate Transfer Tax Act, MCL 207.501, *et seq.*, the parties entered into a consent order in which it was agreed that the county transfer tax would only be assessed on the value of the unimproved lot, provided that the developer used two separate contracts, one for the sale of the lot and one for the construction of the building. 747 N.W.2d at 246. Similar arrangements should also reduce state transfer tax liabilities.

"Since the consideration paid for the deeds in Lake Forest included the cost of the lot and the home, the aggregate value was the appropriate basis for measuring the transfer taxes due and owing."

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"The world has a habit of making room for the person whose words and actions show that they know where they're going."

~Napoleon Hill

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vance written notice to the MDEQ is required. The new rules also require owners and operators to: (1) complete an assessment to confirm any release to the environment and, in the event there is visible, olfactory, or analytical evidence of a release, corrective action will be required; (2) properly empty liquid contents or sludge; and (3) safeguard the AST against future potential trespassers.



Failure to meet the impending deadline may result in the issuance of citations, fines or "red tag" status requiring the cessation of operations until compliance is achieved. With the impending expiration of the grace period, it is imperative that owners and operators of ASTs containing flammable or combustible liquids promptly review the requirements and their options under the State's Storage and Handling of Flammable and Combustible Liquids Rules.

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Environmental proactivity in the real estate market is no longer a "feel-good" endeavor. Consumer demand is on the rise for sustainable development and consumers are actively looking for investment opportunities. In a survey by BOMA, USGBC, and Real Estate Media, 82% of property professionals said greening their portfolios was a priority. According to the same study, 2/3 of the respondents have allocated funds to green initiatives. Whether motivated by greater corporate accountability for environmental impact or for other reasons, such as mere economics, the writing is on the wall.

According to RREEF Real Estate, buildings account for 39% of the nation's primary energy use, 70% of its electricity consumption, 30% of raw materials use, and 30% of greenhouse gas emissions. As more and more researchers are quantifying and qualifying the "carbon footprint" of buildings and other improvements, professionals in the real estate industry are taking a second look at their business models.

A quick Google search uncovers the many "green" real estate brokerage firms popping up all over the United States, and Michigan is no exception. Brokers are updating their antiquated portfolios of inefficient buildings in response to owner, tenant,

and employee expectations for high-performance commercial and residential buildings that offer low operating costs due to energy conservative appliances and systems and green rooftop gardens. For landlords, this means an edge on competition. For developers, this means a much welcomed reprieve from the ever-increasing pressure of high energy and water costs. Consumers are also looking for buildings that promote better health through the use of low toxic materials that implement energy management principles.

While nothing in life is free, it appears it may no longer cost a pretty penny for a green building. According to Turner Construction's 2005 Green Building Market Barometer, it costs a mere 0.8% more for basic LEED (Leadership in Energy and Environmental Design) certification, which may be easily recouped through lower operating costs.

As you embrace sustainable development and its impact on your personal and professional endeavors, the real estate practice group at Maddin Hauser will do our part to keep you apprised of opportunities to make your transactions a little "greener".

*You can't wait for inspiration. You have to go after it with a club.
~ Jack London*