

# REAL ESTATE TAX PRORATION

## House Bill 4929 as introduced First Analysis (10-7-97)

**Sponsor: Rep. Lynn Owen**  
**Committee: Tax Policy**

### ***THE APPARENT PROBLEM:***

One of the matters that is typically addressed at a real estate closing when property changes hands is the payment of property taxes. Property taxes that have recently been paid or are due to be paid are usually prorated so as to divide them between the buyer and the seller. This can be a vexing issue. Parties to a sale are free to agree to any kind of tax proration, but it appears that there are local customs that determine how prorations are handled in most transactions. One legal commentator has said real estate tax proration is the bane of many real estate lawyers "principally because the methods of proration used in Michigan vary so much from locality to locality that the methodology becomes almost incomprehensible." Proration is made more complicated in those cases when it involves separately prorating the taxes levied by different local tax collecting units -- the city or township, the school district, the county, etc. -- using each unit's different fiscal year. (The author goes on to say, however, that "it can become very understandable if a few basic points are grasped." Michigan Real Property Law: Principles and Commentary by John G. Cameron, Jr.)

The issue is often framed as being a matter of whether property taxes are treated as if they are paid in advance (for future public services), in arrears (for past services), or concurrently (for ongoing services). Apparently, in Michigan, there are differing views on this, and it is a matter of local custom how property taxes are prorated. (It should be noted that each tax statement and receipt for taxes is required to contain the dates of the fiscal year of each taxing unit of government during which taxes on the statement or receipt will defray the costs of governmental services.) Obviously, some methods of proration benefit the seller and other methods benefit the buyer.

Some real estate professionals in southeasternmost Michigan have complained that people there have been given conflicting information about the fiscal year for which taxes were being collected and about how taxes should be prorated. This has led to confusion and frustration among parties to real estate transactions, and sometimes to parties to a transaction feeling they have been misled or cheated. There is also the problem that if a person moves from a part of the state where one

proration method is used to a part where another method is used, he or she could end up paying double property taxes by following local practices in each case.

Some real estate professionals and others would very much like for there to be a standard statewide method of prorating taxes at closings. Legislation has been introduced to accomplish this.

### ***THE CONTENT OF THE BILL:***

The bill would amend the General Property Tax Act to specify that taxes levied by this state or by a city, county, village, township, or other taxing unit are considered to be for the calendar year in which the taxes are levied, regardless of when the taxes are collected.

(Note: It is anticipated that a floor substitute will be offered that will contain language specifying that this provision is for purposes of the proration of taxes in a private real estate transaction only.)

MCL 211.40

### ***BACKGROUND INFORMATION:***

The conclusion of the section on real estate tax proration in Michigan Real Property Law: Principles and Commentary, 2nd Edition, by John G. Cameron, includes the following.

"Thus, there are many variations in tax proration. Either the buyer or the seller may realize a substantial and often unanticipated gain, depending upon which method of proration is used. In nearly all cases the choice of method is purely artificial, having nothing to do with the reality of whether governmental services are purchased in advance, in arrears, or concurrently.

Even though the Michigan attorney general has opined that real estate taxes in Michigan are collected for the calendar year in which they are levied . . . , by statute, where the parties to a private transaction do not agree

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otherwise, real estate taxes must be prorated between them as if paid in advance on a due date basis."

buyer and seller, potentially creating a new set of "winners" and "losers."

Section 2(4) of the General Property Tax Act says: In a real estate transaction between private parties in the absence of an agreement to the contrary, the seller is responsible for that portion of the annual taxes levied during the 12 months immediately preceding, but not including, the day title passes, from the levy date or dates to, but not including, the day title passes and the buyer is responsible for the remainder of the annual taxes. As used in this subsection, "levy date" means the day on which a general property tax becomes due and payable.

### ***FISCAL IMPLICATIONS:***

The House Fiscal Agency reports that the bill would have no fiscal impact. (Fiscal Note dated 9-24-97)

### ***ARGUMENTS:***

#### ***For:***

The aim of the bill is to bring some clarity to the issue of prorating property taxes when property is sold. The bill would specify in statute that property taxes are considered to be for the calendar year in which they are levied. Taxes levied, for example, on December 1, 1997, are to be considered for the 1997 calendar year. (There is already a 1980 attorney general's opinion to that effect.) The bill is not intended to make any changes to how taxes are collected or disbursed, or when, nor will it affect how units of government determine their fiscal years. Its purpose is simply to make a clear statement about who is responsible for taxes when real estate changes hands so that tax proration will be simpler and standardized across the state. (Advocates say it will not affect parties to a transaction from making whatever arrangements they want in their sales agreement.)

#### ***Response:***

The General Property Tax Act already contains provisions regarding the proration of taxes in Section 2. This bill would amend Section 40. Is the bill amending the right section? Do the two provisions create the potential for conflict between two different sections of the act? That would be particularly unfortunate, since avoiding conflict and confusion are among the main purposes of the bill.

#### ***Against:***

While it is understandable that some people prefer a standard method of prorating property taxes in real estate transactions, is it really wise to overturn longstanding local practices? The bill will in some areas change how taxes are routinely apportioned between

**POSITIONS:**

The Michigan Association of Realtors strongly supports the bill. (10-6-97)

The Michigan Townships Association supports the concept of the bill, but is concerned that it amends the wrong section of the act. (10-6-97)

The Michigan Municipal League is neutral on the bill if it is amended to specify that the calendar year language is for the purpose of prorating property taxes only, and is opposed to the bill if that amendment is not added. (10-6-97)

Analyst: C. Couch

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