



Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536

BILL ANALYSIS



Telephone: (517) 373-5383
Fax: (517) 373-1986

House Bill 4173 (as enacted)
Sponsor: Representative David C. Maturen
House Committee: Tax Policy
Senate Committee: Finance

PUBLIC ACT 217 of 2015

Date Completed: 1-21-16

RATIONALE

The State Real Estate Transfer Tax imposes a tax on the seller of property in Michigan, subject to a number of exemptions. One of the exemptions applies to the sale of a principal residence that has not increased in value since its purchase; that is, if the property's State equalized valuation (SEV) is less than or equal to its SEV on the date it was purchased by the seller, the seller may claim an exemption. Previously, however, the Act imposed a penalty if the exemption was claimed and the State Treasurer found that the property had been sold "at a value *other than* the true cash value" (emphasis added). The Act does not define true cash value, and did not specify that a sale was exempt from the tax if property sold for *less* than the true cash value. Reportedly, in practice, the Department of Treasury did not charge the tax to a seller if the property's SEV for the year of the sale was less than or equal to its SEV for the year in which it had been purchased, and the sales price was not more than two times the property's SEV, which is considered a proxy for true cash value for purposes of property taxation. This interpretation was consistent with a 2008 Opinion of the Attorney General (No. 7214), "If the SEV for the property at the time of transfer by the owner is less than or equal to that property's SEV on the date the owner purchased or acquired the property, the seller may claim an exemption...provided that the property is sold for *not more than* its true cash value" (emphasis added). Despite the existing practice, some people were concerned about how future Treasury Department officials might construe the law.

In addition, the exemption for a principal residence became the subject of litigation when the Department denied refunds to homeowners who paid the tax after selling their homes for less than what they had paid to buy them. In each case, although the SEV at the time of the sale was lower than the SEV when the homes were purchased, the sales price was more than twice the SEV at the time of the sale. The Tax Tribunal allowed the exemption but the Court of Appeals reversed based on its interpretation of the term "true cash value" in the penalty provision. The Court essentially held that the homeowners must have sold their property for exactly double the SEV at the time of the sale in order to claim the exemption. In July 2015, the Supreme Court reversed the Court of Appeals (*Gardner v. Department of Treasury*, 498 Mich 1). The Supreme Court stated, "It is very unlikely...that the Legislature impliedly intended the property's 'true cash value' to mean precisely twice its SEV. Rather...the exemption requires an arm's length transaction, which, by definition, gives the property its true cash value."

Due to these developments and the varying interpretations of the statutory language, it was suggested that the language of the Act should be revised.

In a related issue, there was a period of time in recent years when the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) were claiming an exemption from the real estate transfer tax for the sale of foreclosed homes they sold directly, although several county treasurers were attempting to collect the tax. In those cases, Fannie Mae and Freddie Mac evidently had buyers sign agreements to pay the tax on their behalf. In May 2013, the U.S. Court of Appeals for the Sixth Circuit ruled that, under Federal law, the two corporations were exempt from the tax (*County of Oakland, et al. v. Federal Housing Finance Authority, et al.*, Nos. 12-2135 and 12-2136). The Act, however, did not provide a method for a

buyer who paid the tax on behalf of a seller to request a refund, and Fannie Mae and Freddie Mac reportedly were slow to request refunds for the buyers who did so. The Department of Treasury has a form and process for sellers to request a refund, and online instructions indicate that a property owner who purchased from Fannie Mae or Freddie Mac may use the form. It was suggested that the Act itself should allow a seller, or a buyer who paid the tax on behalf of a seller, to request a refund if the person believes that the property was eligible for an exemption at the time of the transfer.

CONTENT

The bill amended the Real Estate Transfer Tax Act to do the following:

- Allow an exemption from the transfer tax for a principal residence if its SEV is equal to or less than the SEV on the date of purchase and the transaction was for a price at which a willing buyer and a willing seller would arrive through an arms-length negotiation.**
- Delete the requirement that a penalty be assessed if, after the exemption was claimed, the State Treasurer determined that the sale was at a value other than the true cash value.**
- Allow a seller, or a buyer who paid the tax on behalf of the seller, to request a refund of the tax paid if he or she believes that the property was eligible for an exemption at the time of the transfer.**

The bill took effect on December 15, 2015.

Section 6 of the Act provides for exemptions to the real estate transfer tax for various types of transfers or instruments. As amended by the bill, Section 6(u) allows an exemption to the tax if all of the following apply:

- The property qualifies for the principal residence exemption.
- The SEV of the property is less than or equal to the SEV on the date of purchase or on the date of acquisition by the seller or transferor.
- The transaction was for a price at which a willing buyer and a willing seller would arrive through an arms-length negotiation.

The bill added the third condition listed above.

Previously, if the State Treasurer found, after the exemption was claimed, that the sale or transfer was at a value other than the true cash value, then a penalty of 20% of the tax had to be assessed in addition to the tax due. The bill deleted this requirement.

The bill also provides, in Section 6(u), that if the seller or the buyer who has paid the tax on behalf of the seller believes that the property was eligible for an exemption under this subdivision at the time of the transfer, the seller or the buyer may request a refund from the Department of Treasury in a form and manner determined by the Department. The bill states that this subdivision is retroactive and applies to a sale, exchange, assignment, or transfer on or after June 24, 2011.

The bill also amended Section 3, which imposes the real estate transfer tax on specified instruments, provides that the person who is the seller or grantor of the property is liable for the tax, and generally requires the tax to be paid to the county treasurer within 15 days after delivery of the instrument making the conveyance.

The bill added Section 3(4) to provide that, after the tax is paid, if the seller or the buyer who has paid the tax on behalf of the seller believes that the property was eligible for an exemption under Section 6 at the time of the transfer, the seller or the buyer may request a refund from the Department of Treasury in a form and manner determined by the Department. The bill requires the Department to pay the refund if it determines that the property was eligible for the exemption under Section 6 at the time of the transfer. The bill specifies that this subsection is intended to be

retroactive and applies to a sale, exchange, assignment, or transfer beginning four years immediately preceding the bill's effective date.

MCL 207.523 & 207.526

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill clarifies the qualification for an exemption to the real estate transfer tax. As previously written, the Act allowed an exemption for a principal residence whose SEV was equal to or less than the SEV on the date of purchase by the seller, but required the Department to penalize the same homeowner if he or she sold the property for an amount that was not exactly the true cash value. Evidently, the Department did not charge the tax to a homeowner or impose the penalty in such a situation, as long as the sales price was not more than twice the SEV. Although this practice was consistent with a 2008 Attorney General's opinion, there were concerns that future Treasury Department officials could apply the law differently.

At the same time, however, because the Department interpreted "true cash value" as twice the SEV, the Department denied refunds to individuals who sold their homes for less than what they paid, because the sales price was more than double the property's SEV. In *Gardner v. Department of Treasury*, the Michigan Supreme Court held that these homeowners were entitled to an exemption from the real estate transfer tax. The Court concluded, "To be entitled to the transfer tax exemption under... [Section 6u)], the petitioning taxpayer need only demonstrate that the property at issue is the principal residence of the seller or transferor, that it has an SEV at the time of conveyance that is less than or equal to the SEV at the time of acquisition, and that it was sold or transferred for a price at which a willing buyer and a willing seller would arrive through arm's-length negotiation."

By codifying the Court's conclusion in the statute, and deleting the penalty provision, the bill clarifies the exemption for individuals who sell their homes for a diminished value.

Supporting Argument

If the real estate transfer tax is paid on the transfer of property that is later found to be exempt from the tax, an option to request a refund should be available whether the seller paid the tax or it was paid by the buyer on behalf of the seller. Previously, the Act did not directly address the refund of taxes already paid. The bill therefore allows a request for refund to be initiated either by the seller or by the buyer who paid the tax on the seller's behalf, and requires the Treasury Department to pay a refund it determines that the property was eligible for an exemption at the time of the sale. While the Fannie Mae and Freddie Mac situation was the impetus for this change, the refund process is available to any seller or buyer who paid the real estate transfer tax and believes that the property was eligible for an exemption.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill will reduce State School Aid Fund revenue by an unknown amount depending upon the number of properties affected and their specific characteristics. The average number of transfers in which a buyer or seller pays the tax, although the transfer is exempt, also is unknown. Similarly, it is not known how many transactions involving a principal residence have been subject to the 20% penalty that the bill eliminated. The tax generated \$233.4 million during FY 2013-14.

Because of the retroactive provisions of the bill, revenue will likely be reduced more during the first year the bill is effective than in later years. Although Section 6 generally indicates the characteristics of transfers and instruments that are exempt from the tax, the amendments to that section authorize refunds under Section 6(u) (for a principal residence, as described above) and

the changes are retroactive to June 24, 2011. However, the amendments to Section 3(4) (regarding refunds) are retroactive only to four years before the bill became effective but will affect refunds associated with any of the exemptions in Section 6, not just those in Section 6(u).

Fiscal Analyst: David Zin

H1516\s4173ea

This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.