SECREST WARDLE

community watch

MONITORING LEGAL ISSUES THAT AFFECT MICHIGAN MUNICIPALITIES

04.11.11

The *Klooster* Conundrum: When Does Taxable Value Uncap and What to Tell Property Owners

By Stephanie Simon Morita

Last month's Michigan Supreme Court decision in *Klooster v City of Charlevoix* (decided March 10, 2011) has raised several issues pertaining to the duties of assessors and when an assessor should uncap a property's taxable value. The Court's determination that a written document is not necessary for a transfer of ownership to occur, which transfer could trigger uncapping of taxable value, has provided clarity, while at the same time possibly requiring a greater examination of a property's ownership history. In light of the decision in *Klooster*, an assessor should be concerned with: 1) Whether to uncap taxable value after receiving a deed creating a joint tenancy; 2) To what extent does an assessor need to investigate the ownership history of a piece of property; and 3) What to tell a property owner who asks whether the creation of a joint tenancy will decrease future tax liability.

SECREST WARDLE NOTES

By way of its decision in *Klooster*, the Supreme Court explained a document is not necessary for a transfer of ownership of real property triggering uncapping of taxable value to occur under the State's tax statutes. In situations with successive joint tenancies, assessors should look at whether the conveying party is an "original owner" to determine whether a tax statute transfer has occurred and an uncapping should occur. As a result of *Klooster*, an assessor's ability to uncap taxable value has been strengthened in certain situations where no specific conveyance document exists.

In *Klooster*, the Court was faced with determining whether one of three transactions was a transfer of ownership under the General Property Tax Act (GPTA), and whether the transactions were excepted from uncapping taxable value under the MCL 211.27a(7)(h) joint tenancy exception. The three transactions were: 1) The conveyance by an original owner into a joint tenancy with his son; 2) The termination of the joint tenancy due to the death of the original owner; and 3) The conveyance by the son into a joint tenancy with his brother. The Court held that: 1) The conveyance into the joint tenancy by the original owner is not a transfer of ownership; 2) The termination of the joint tenancy by the death of the original owner is a transfer of ownership – but this transfer is excepted under the statute from uncapping; and 3) The son's transfer into the joint tenancy with his brother is a transfer of ownership which triggers uncapping because the son is not an original owner.

The key to understanding the Court's reasoning is its explanation of who is considered an "original owner." The Court explained that for purposes of the joint tenancy exception to uncapping, the following are considered to be "original owners": 1) A sole owner at the time of the last uncapping; 2) A joint owner at the time of the last uncapping; and 3) A spouse of either a sole or joint owner at the time of the last uncapping. In *Klooster*, because the father obtained his interest in the property prior to enactment of the 1995 taxable value and uncapping statutes, the Court examined his interest *as if* it had occurred after the statutes had been enacted. Because the father's acquisition of the property would have resulted in an uncapping under today's statutes, the Court found him to be an "original owner."

Accordingly, whether an assessor should uncap taxable value after receiving a deed creating a joint tenancy will depend on the facts of each case. If the facts show that the deed creating a joint tenancy is from a party who does not qualify as an original owner, then taxable value should be uncapped. Conceivably, this could result in having to review decades of ownership history. While many assessors rely on the

transfer information contained within their own files, it should be expected that in some cases such information will be incomplete. As an example, an assessor may not be notified of the death of the last remaining original owner joint tenant, even though under *Klooster* such an event constitutes a conveyance to the non-original owner joint tenant – and presumably would trigger the statutory requirement of filing a property transfer affidavit with the assessor.

So, the issue becomes how far should an assessor go to investigate ownership history, and more importantly for many, how much time and money should an assessor spend looking into the matter? Ideally, every deed creating a joint tenancy should result in a review which enables the assessor to clearly determine whether or not the grantor of the deed is an original owner. In reality, how much time and money is spent, especially in the case of a search which cannot be done through a Register of Deeds website and requires a physical visit, may have to be a case-by-case business decision. It is possible, however, that the instances where a physical visit is required could result in large percentage increases in taxable value, because the last deed which would trigger an uncapping is most likely dated before 1995 and too far back to be included in the on-line records.

Also, inquiries at local assessing offices can be expected as to the possible property tax advantages afforded to the non-original owner joint tenant survivor (in the *Klooster* case, it was the son before he deeded the property to himself and his brother). Care should be taken to not answer the question of whether transferring the property via deed into a joint tenancy will lessen potential tax liability because "tax liability" may encompass more than just property taxes. As an example, under federal statute, the *Klooster* son may have to pay capital gains income taxes based upon the increase in value from the price his father (the original owner) paid and what the son sells the property for at a later date. Had the son received the property as the result of a will instead of the joint tenancy deed, capital gains tax would most likely be calculated based upon the difference in value on the date of the father's death versus the value on the date the son sells the property – potentially a much smaller tax. A prudent course of action is to recommend all inquiring parties to consult with a tax professional to make a determination as to whether there truly would be a "tax liability" advantage.

The *Klooster* decision, while providing some much needed clarity as to when an uncapping of taxable value should occur in a joint tenancy situation, may have created more work for assessors. What should certainly be clear from the opinion is that under the GPTA a written document is not required for a transfer of ownership triggering an uncapping of taxable value to occur. In this regard, the decision strengthens the ability of assessors to uncap taxable value in certain situations where a document evidencing a transfer of ownership does not exist.

CONTACT US

Farmington Hills
30903 Northwestern Highway, P.O. Box 3040
Farmington Hills, MI 48333-3040
Tel: 248-851-9500 Fax: 248-851-2158

Mt. Clemens
94 Macomb Place, Mt. Clemens, MI 48043-5651
Tel: 586-465-7180 Fax: 586-465-0673

Lansing
6639 Centurion Drive, Ste. 130, Lansing, MI 48917
Tel: 517-886-1224 Fax: 517-886-9284

Grand Rapids
2025 East Beltline SE, Ste. 209, Grand Rapids, MI 49546
Tel: 616-285-0143 Fax: 616-285-0145

www.secrestwardle.com

SECREST SW WARDLE

CONTRIBUTORS

Municipal Practice Group Chair
William P. Hampton

Senior Editor
Steven P. Joppich

Editor
Bonny Craft

We welcome your questions and comments.

OTHER MATERIALS

If you would like to be on the distribution list for Community Watch, or for newsletters pertaining to any of our other practice groups, please contact Secrest Wardle Marketing at **swsubscriptions@secrestwardle.com** or **248-539-2850**.

Other newsletters include:

Benchmarks – Navigating the hazards of legal malpractice
Blueprints – Mapping legal solutions for the construction industry
Boundaries – A guide for property owners and insurers in a litigious society
Contingencies – A guide for dealing with catastrophic property loss
Fair Use – Protecting ideas in a competitive world
In the Margin – Charting legal trends affecting businesses
Industry Line – Managing the hazards of environmental toxic tort litigation
Landowner's Alert – Defense strategies for property owners and managers
No-Fault Newsline – A road map for motor vehicle insurers and owners
On the Beat – Responding to litigation affecting law enforcement
On the Job – Tracking developments in employment law
Safeguards – Helping insurers protect their clients
Standards – A guide to avoiding risks for professionals
State of the Art – Exploring the changing face of product liability
Structures – A framework for defending architects and engineers
Vital Signs – Diagnosing the changing state of medical malpractice and nursing home liability