

## New Exemption for Uncapping of Residential Property Tax Takes Effect December 31

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December 6, 2013

Owners of residential property in Michigan, including cottages, wanting to transfer the property to a relative without uncapping the value for property tax purposes, may be in luck. The Michigan Legislature has adopted a new exemption to Michigan's PA 415 of 1994, MCL211.27a ("Act 415") to allow transfers of real property between certain relatives without uncapping the property tax.

Under Act 415, a property's taxable value is capped and allowed to increase only at the lesser of 5% or the inflation rate. (MCL §211.27a(2)(a)). However, in the calendar year following a "transfer of ownership," a property's taxable value will be changed to equal the property's state equalized value for the year following the transfer. (MCL §211.27a(3)). This increase of the taxable value to the state equalized value is commonly referred to as "uncapping", and it could result in significant increase in property tax liability for the new owner after a transfer.

A "transfer of ownership" under Act 415 is broadly defined and includes most commonly understood transfers, including most transfers between relatives. The statute also exempts certain transactions from the definition of a "transfer of ownership". (MCL 211.27a(7)). Recently, the Michigan Legislature adopted the following new exemption for some transfers between family members, which is effective beginning December 31, 2013:

*[A] transfer of residential real property if the transferee is related to the transferor by blood or affinity to the first degree and the use of the residential real property does not change following the transfer. As used in this subdivision, "residential real property" means real property classified as residential real property under section 34c.*

(MCL 211.27a(7)(s)).

The first key element to this exemption is that the transferee must be related to the transferor "by blood or affinity to the first degree". This is a phrase which is not in common usage, but the Michigan Department of Treasury has issued Bulletin 5 of 2013 which states:

*Affinity to the first degree includes the following relationships: spouse, father or mother, father or mother of the spouse, son or daughter, including adopted children and son or daughter of the spouse.*

This definition would have been clearer if they had used the term "blood or affinity" but the use of simply "affinity" probably still means the same thing: transfers can be made from a parent to a child or vice versa, or to a spouse or the parents of a spouse. Transfers between siblings would not be covered in that those are considered to be a second degree relationship. Any other transfer such as from grandparents to grandchildren would not be covered by the exemption. It is not clear, however, if the Bulletin's definition is dispositive, or if it is supported by Michigan law. Also, a Treasury Bulletin is not binding precedent on a court. But it does provide a conservative interpretation for use by transferors.

The second key element is that it must be residential real property before and after the transfer. Residential real property is defined as real property classified as residential real property under MCL 211.34c: (i) vacant parcels, land with buildings, and condominium apartments which are used for, or probably will be used for, residential purposes; (ii)

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parcels used for, or probably will be used for, recreational purposes, such as lake lots and hunting lands located in an area used predominately for recreational purposes; and (iii) a home, cottage or cabin on leased land and mobile homes that would be assessed as real property except that the land on which it is located is exempt. In short, this definition covers not only what is normally considered to be residential, but also recreational lands and residences on leased land.

With proper planning, this new exemption may provide a useful exemption to transfer residential property (including recreational lands) from one generation to the next without uncapping the property tax. As with any new legal development, unexpected issues will arise when it is put into effect, such as a transfer by a trust or the effect of the state and county transfer tax. For more information, regarding this exemption or for assistance with transferring property, please contact: