Legislative Analysis

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MORATORIUM ON POP-UP

House Bill 4440 (Substitute H-1)
Sponsor: Rep. Andy Meisner
Committee: Commerce

First Analysis (3-14-07)

BRIEF SUMMARY: The bill would leave the property taxes capped when a principal residence (an owner-occupied residence) was transferred during the period beginning March 1, 2007 through September 1, 2008. This would apply only in cases where the residence was to continue to be a principal residence for the new owner. This means a principal residence would be exempt from the "pop-up" in taxable value.

FISCAL IMPACT: By eliminating the increase in taxable value that would normally occur when a residential property is sold, the bill would reduce state and local revenue by an unknown amount. (For additional information, see Fiscal Information.)

THE APPARENT PROBLEM:

Generally speaking, the increase in the assessment of a parcel of real property cannot increase from one year to the next by more than the rate of inflation or five percent, whichever is less. However, when property is sold or transferred, its valuation returns (or “pops up”) to 50 percent of market value. The assessment is uncapped and from that point, the assessment cap once again begins to apply, this time to the readjusted assessment.

The assessment cap provisions were part of Proposal A, the new school financing system adopted by voters in 1994. Prior to Proposal A, property taxes were based on state equalized valuation or SEV, which was defined as 50 percent of true cash value. Since then, taxes have been based on "taxable value," which essentially is the SEV adjusted downward by the cap on assessment increases. One result is that owners of similar neighboring homes pay different amounts in property taxes based on the length of occupancy. The assessment cap and pop-up together mean, obviously, that when a home is sold, the new buyer is likely to face a significantly larger property tax bill than the old owner. A recent report by the Michigan Citizens Research Council, using 2003 data, put the gap between taxable value and state equalized value at about 78 percent.

Some people say that the "pop-up" results in "sticker shock" for new owners caught unawares and for people shopping for a first home or new home. It also may discourage some homebuyers from acquiring previously owned homes rather than newly built houses (often in jurisdictions with lower tax rates). Critics of the "pop-up" also allege that older homeowners get locked into homes they otherwise might leave because of the tax consequences of moving. This, in turn, is said to have an effect on such things as the school age population.

The General Property Tax Act contains a definition of what constitutes a "transfer" for the purpose of the "pop-up" and contains a list of transactions that do not count as transfers. Legislation has been proposed that would amend the definition of a "transfer" in such a way as to put an 18-month "freeze" on pop-ups.

THE CONTENT OF THE BILL:

House Bill 4440 would amend the General Property Tax Act to exempt from the "pop-up" the transfer of a principal residence (an owner-occupied residence) for the period beginning March 1, 2007 through September 1, 2008. This would apply only in cases where the residence was to continue to be a principal residence for the new owner.

House Bill 4440 is tie-barred to House Bill 4441, which would amend the State Real Estate Transfer Tax Act. That bill would increase the transfer tax on property being sold from $3.75 to $4.25 for each $500 (or fraction of $500) of the property being transferred. This would apply to principal residences transferred beginning May 1, 2007 through December 31, 2008. The additional 50 cents would be credited to the general fund of the local tax collecting unit to be used for public safety (police, firefighters, other first responders, school safety officers, and school resource officers). House Bill 4441 is tie-barred to House Bill 4440. This means neither bill could take effect unless both were enacted.

MCL 211.27a and 34d

FISCAL INFORMATION:

House Bill 4440: By eliminating the increase in taxable value that would normally occur when a residential property is sold, the bill would reduce state and local revenue by an unknown amount. The statewide average millage rate for homestead property is approximately 34 mills. Of this, the state imposes the six-mill State Education Tax (SET), which accrues to the School Aid Fund. The remainder, about 28 mills, remains at the local level.

House Bill 4441: Increasing the Real Estate Transfer Tax by 0.10% ($0.50 per $500) for the 20-month period from May 2007 through December 2008 would generate about $42 million, based on existing activity. To the extent that HB 4440 (which would temporarily remove the "popup") increases both sales activity and residential housing prices, the estimate would also increase.

ARGUMENTS:

For:

This bill is part of a package of bills that House Democrats have said is "designed to jumpstart Michigan's economy by increasing home sales," with the "added benefit of creating stronger communities by empowering more . . . residents to buy homes of their own."

The current system, whereby property assessments rise significantly when homes are sold, is a disincentive to homebuying in several ways. People say that it "locks in" longtime homeowners who enjoy a large tax advantage they are loathe to give up by moving, even if they otherwise would prefer to leave a family home for a smaller home or a home that better fits their current lifestyles. (The argument is that where once we were concerned about taxing people *out of* their homes, now we are tax-capping people *into* their homes.) It can also keep first homebuyers out of the market. Together, this in turn keeps new young families out of some communities, affecting school populations.

Stimulating the housing market, at a time when it is struggling, will have related beneficial economic impact since when people buy homes they spend money on other goods and services as well. Supporters say, "Consumers who spend less on their homes have more money to spend on big-ticket items, such as furniture and appliances, which pumps more money into the local economy."

Companion legislation would provide offsetting additional revenue over the short-term to local units of government for vital public safety services, such as police and fire protection.

Against:

Critics of the bill, while appreciating its short-term goal, and agreeing that the current assessment cap/pop-up system needs addressing, have raised objections to this approach. A comprehensive approach to the problem is required. Some say that the moratorium will distort the real estate market in several ways. It will hurt homebuilders by giving a tax advantage to the purchase of an existing (capped) home over a newly built home. (Plus, companion legislation would raise transfer taxes on new and existing homes to offset the tax break provided only existing homes.) Also, for existing homeowners trying to sell, it will lock in the current inequities, with homes for sale side by side possibly carrying widely different tax burdens based on how long the current occupants have lived there.

Other critics point out that there will be revenue losses to local units, and not just in the short run. People buying homes during the 18-month moratorium will have their taxes capped for as long as they own the home; revenue will be lost to schools and local units year after year. Constitutional questions have also been raised, since the constitution anticipates taxes being uncapped when property is transferred. While statute can define what constitutes a "transfer," it is illogical for the law to say selling a home is not a transfer for one 18-month period but is at all other times.

The "cliff" nature of the proposal also has been criticized. What happens in 2009? Will all home sales be pushed into the 18-month period? Will the moratorium be extended? Will the legislature need to address numerous tales of property sales just missing the moratorium (just before or just after)?

POSITIONS:

The Michigan Association of Realtors indicated a position of "qualified support" in testimony before the House Commerce Committee. (3-13-07)

A representative of the Grosse Pointe municipalities indicated support for the bills. (3-13-07)

The Michigan Association of Homebuilders testified in opposition to the bill as written. (3-13-07)

The Michigan Municipal League indicated opposition to the bill as a stand-alone bill (without legislation to address other negative effects of the cap/pop-up on municipal finances). (3-13-07)

The Michigan Townships Association testified in opposition to the bill. (3-13-07)

The Michigan Association of Counties indicated opposition to the bill. (3-13-07)

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