UNDERSTANDING PROPOSAL A IN A DECLINING MARKET

Important Information

Please read the enclosed information. If you still have questions, you can contact your

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"Helping both Before and After the Sale"

Proposal A

On March 15, 1994, Michigan voters approved the constitutional amendment known as Proposal A.

Proposal A was designed to limit the growth in property taxes by the Consumer Price Index (CPI) until ownership in the property was transferred.

How It Works

Prior to Proposal A, property taxes were based upon State Equalized Value (SEV). With the implementation of Proposal A, property taxes are now based upon Taxable Value.

Each year, the Assessing Office must calculate the SEV for every property based upon the time frame as outlined by the State Tax Commission. A property's taxable status is determined as of December 31, which is called Tax Day.

Additionally, each property has a Capped Value. Capped Value is calculated by multiplying the prior year's Taxable Value, with adjustments for additions and losses, by the CPI as calculated by the State of Michigan and cannot increase by more than 5%. **For 2007, the CPI has been calculated at 3.7%.**

Taxable Value (TV), which property taxes are based on, is defined as the **<u>lower</u>** of State Equalized Value or Capped Value.

Generally speaking, this means that unless the current year SEV is less than the previous year Taxable Value multiplied by the CPI, the current years Taxable Value will increase by the CPI.

SEV = 50% of True Cash Value

Capped Value =

(Prior TV-Losses) x (1+ CPI*) + Additions

* Percent of change in the rate of inflation or 5%, whichever is less, expressed as a multiplier

Taxable Value =

The <u>lesser</u> of State Equalized Value or Capped Value unless there is a transfer of ownership.

The Equalization Timetable

The State Tax Commission rules establish that a local Assessing officer must utilize a 24 month sales study to calculate assessments each year. The 24 month time period begins April 1 two years prior to tax day and ends March 31 in the year preceding tax day.

For 2007 Assessments, the 24 month sales study begins April 1, 2004 and ends March 31, 2006.

Sales that occur in the current calendar year after March 31st will not be considered in the sales study until the following year.

In a normally inclining market, this process generally helps taxpayers since current sale prices are higher than those analyzed in the sales study and assessments will tend to lag current market conditions. However, **if sale prices are declining, it will take time for the assessment cycle to recognize the falling prices** as well, to the detriment of taxpayers under Proposal A.

Actual Sale Price is <u>not</u> True Cash Value

The law defines True Cash Value as the **usual** selling price of a property. The Legislature and the Courts have very clearly stated that **the actual selling price of a property is not a controlling factor in the True Cash Value or State Equalized Value** as calculated by the Assessor. For this reason, when analyzing sales for the purpose of determining assessment changes, the Assessing Office will review sales and exclude non-representative sales from the assessment analysis.

Inherent in the definition on usual selling price is the assumption that the sale does not involve any element of distress from either party.

For this reason, all distressed sales, such as sales involving **mortgage foreclosure** or sales involving transfers to or from relocation companies are not considered as typical sales in the valuation of property for assessment purposes.

Transfers of Ownerships and Uncapping of Assessments

According to Proposal A, when a property (or interest in a property) is transferred, the following year's SEV becomes that year's Taxable Value. In other words, if you purchased a property in 2006, the Taxable Value for 2007 will be the same as the 2007 SEV. The Taxable Value will then be "capped" again in the second year following the transfer of ownership.

It is the responsibility of the buyer in a transfer to file a Property Transfer Affidavit with the Assessors Office within 45 days of the transfer. Failure to file a Property Transfer Affidavit will result in a penalty of $5 per day for each day after the 45 day period with a maximum penalty of $200. Property Transfer Affidavit forms are available at the Local Assessors Office.

Again, it is important to note that a property does not uncap to the selling price but to the SEV in the year following the transfer of ownership.

Principal Residence Exemption

If you **own and occupy** your home as your principal residence, it may be exempt from a portion of local school operating taxes. You may check your percentage of principal residence exemption on your "Notice of Assessment".

If the percentage exempt as "Principal Residence" is 0% on your assessment notice and you wish to claim an exemption for the current year, a Principal Residence Exemption Affidavit must be completed and filed with the Assessors Office prior to May 1.

Furthermore, if you currently have a Principal Residence Exemption on your property and you no longer own and occupy the property as your primary residence, you must rescind the Principal Residence Exemption with the Assessors Office.

Forms to claim a new exemption or to rescind a current exemption are available at the Local Tax Assessors Office during normal business hrs.

So What Does it all Mean?

How can my assessment go up with the current market conditions?

As stated in the Equalization Timetable, for 2007, the time period of the sales study for assessment review is April 1, 2004 through March 31, 2006. Sales occurring after March 31, 2006 will not be reviewed until the 2008 assessment cycle.

In determining assessment adjustments for a neighborhood, the sale prices of homes are compared to existing assessed values to determine the level of assessment. State law requires this level to be at an average of 50% of value for the time period under review. Individual market areas within the City tend to appreciate (or decline) at different rates. Generally speaking, assessments tend to increase or decrease at a more stable pace. As such, it is quite possible that, even with current market conditions, assessment reviews of sales indicate levels of assessment in certain areas of the City at levels less than 50% and increases in 2007 assessments are necessary.

How can my Taxable Value go up when my SEV goes down? (or stays the same as last year)

Remember that the definition of Taxable Value is the lesser of SEV or last year's Taxable Value (adjusted for physical changes) times the CPI. (3.7 % for 2007).

Since the beginning of Proposal A in 1994, overall increases in SEV have generally been greater than the increase in Taxable Value capped at the CPI. The longer a property has been owned and capped, the greater the gap between SEV and Taxable Value. Even with no change in SEV for 2007, or with a decrease in SEV for 2007, if there is still a gap between SEV and Taxable Value, and the 2007 SEV is greater than the Taxable Value in the previous year the Taxable Value will increase to the limit of the CPI cap.

If, however, the 2007 SEV is lower than the calculation of last year's Taxable Value multiplied by the CPI, then the 2007 Taxable Value will be the same as the 2007 SEV.

Example of Declining State Equalized Value and Increasing Taxable Value

This example illustrates a property, purchased in 1995 and uncapped in 1996. In 1996 the SEV becomes the new Taxable Value and then the property is recapped at the CPI. The SEV will increase or decrease based on market conditions. The Capped Value is adjusted by the CPI in the following year. Taxable Value is determined by using the SEV or Capped Value, whichever is less.

In this example, the property experiences a loss in the SEV from 2005 to 2007. Although the loss was due to market conditions, the Taxable Value continues to increase by the CPI during 2005-2007. The Taxable Value will continue to increase at the CPI until the SEV falls below Capped Value.

	SEV	Capped	Taxable	CPI
1995	$ 100,000	$ 97,000	$ 97,000	2.60%
1996	$ 104,000	$ 104,000	$ 104,000	2.80%
1997	$ 110,000	$ 106,910	$ 106,910	2.80%
1998	$ 116,650	$ 109,790	$ 109,790	2.70%
1999	$ 126,500	$ 111,540	$ 111,540	1.60%
2000	$ 137,500	$ 113,650	$ 113,650	1.90%
2001	$ 145,250	$ 117,280	$ 117,280	3.20%
2002	$ 154,750	$ 121,030	$ 121,030	3.20%
2003	$ 160,000	$ 122,840	$ 122,840	1.50%
2004	$ 165,000	$ 125,660	$ 125,660	2.30%
2005	$ 175,000	$ 128,550	$ 128,550	2.30%
2006	$ 169,800	$ 132,790	$ 132,790	3.30%
2007	$ 165,110	$ 137,700	$ 137,700	3.70%