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BACK TO THE FUTURE?

CONSTITUTIONAL CHALLENGES TO MICHIGAN'S PROPERTY TAX SYSTEM:

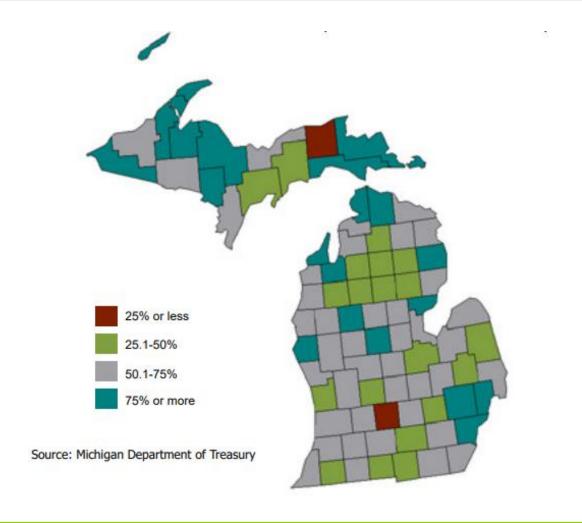
Where We Have Been, Where We Are, and Where We May Be Going

Michigan Association of Counties - Legislative Conference – 2023

Presented by Ted Seitz April 25, 2023

Back to The future: Michigan's Property Tax System

Michigan—like many other states has historically placed a heavy burden on property taxes to fund local governments and their services.





Back to The future: Where We Have Been

- Over the past 40 years, Michigan voters adopted property tax limitations (in 1978) and 1994) "in response to the unpredictable variations and unconstrained growth of assessed values that were affecting tax bills." Citizens Research Council of Michigan, Memorandum 1169 (July 2022), Local Governments Respond to Property Tax Limitations By Raising Tax Rates.
- For much of this same time period, Michigan's delinquent property tax collection process was not working well.



Back to the future: Where We Have Been (cont.)

- Michigan's tax lien delinquent tax collection process took "about six years to complete" and, as a result of this delay, many homes and businesses lingered in the tax revision process—left abandoned and hazardous.
- The longer the delinquent properties were left unaddressed, the more costly and burdensome the rehabilitation. Abandoned also properties contributed to crime, blight, and decay.
- The burden of these consequences fell on local governments, adjoining property owners, and taxpayers.



Back to the future: Where We Have Been (cont.)

As the Michigan Legislature at that time recognized, the system posed "several "public policy" problems, including:

- (1) It was "unfair to those who pay their taxes on time";
- (2) The lack of tax revenue that was owed and budgeted "thwart[ed] local government operations";
- (3) The tax collection process was "labor intensive and time-consuming";
- (4) The back-taxed, often abandoned properties "cause[d] urban blight"; and
- (5) The system "hamstr[ung] land acquisition and redevelopment projects."

House Analysis of General Property Tax Act Amendment Bills Package, July 23, 1999.



Back to the future: 1999 Public Act 123—Change For The Better

- In 1999, the Michigan Legislature revised the process for collecting delinquent property taxes—Public Act 123—moving away from the tax lien system. Counties now had the option to opt-in and the elected County Treasurer could now act as the "Foreclosing Governmental Unit."
- The new process, set forth largely in MCL 211.78 et seq., included new safeguards to assist property owners and prevent foreclosure.
- Numerous property tax exemptions apply to those are impoverished, disabled, or mentally incapacitated.
- Multiple notices—both of delinquency and potential foreclosure—must be provided to those with an interest in the tax delinquent property.



Back to the future: 1999 Public Act 123—Change For The Better (cont.)

The PA123 tax foreclosure process also allows for those potentially subject to foreclosure to offer objections to the foreclosure, which are to be addressed by the Circuit Court at a public hearing.

If property is ultimately foreclosed and not redeemed (by March 31) the property transfers to the FGU and then dispersed in several possible ways, including:

- (1) Right of First Refusal;
- (2) Public Auction; or
- (3) State or County Land Bank Authority.



Back to the future: 1999 Public Act 123—Change For The Better (cont.)

Under PA 123, the FGU was statutorily obligated to keep all amounts received from tax foreclosure auctions and deposit the collected funds above the taxes owed into a Delinquent Tax Revolving Fund (DTRF), via a statutory waterfall.

If the FGU declared a surplus in the DTRF, the surplus could be transferred into a County's General Fund.





Back to the future: PA 123—A Resounding Success

- Significantly benefitted property owners, who were delinquent in their property taxes.
- Also, reduced blight and improved notice to taxpayers.
- Other benefits...





Back to the future: Michigan Becomes The Model

Other states amended their tax foreclosure statues—using Michigan as the model—to streamline their tax foreclosure process, combat blight, and return properties to the market.





Back to the future: Constitutional Challenges To Michigan's Tax Foreclosure Statute

- Notwithstanding these improvements, and the FGUs' strict compliance with Act 123's requirements, beginning in 2014 delinquent taxpayers alleged that the requirement directing FGUs to retain all sale proceeds—and use the proceeds to pay unpaid taxes, maintain tax-foreclosed property that cannot be sold, and for costs associated with the foreclosure process—violates the Takings Clause.
- For years, these cases ran on parallel tracks in state and federal courts. The courts initially rejected these challenges, both on jurisdictional and constitutional grounds. See Rafaeli, LLC v. Oakland Cty., (Mich. Ct. App. Oct. 24, 2017); see also Wayside Church v. Van Buren Cty.
- Takings claims had also been rejected under similar statutes codified in other states. See Automatic Art, L.L.C. v. Maricopa Cty. (D. Ariz. Mar. 18, 2010); Reinmiller v. Marion Cty. (D. Or. Oct. 16, 2006).



Back to the future: Rafaeli v. Oakland County - The Michigan Supreme Court Steps In

That changed when, in *Rafaeli*, the Michigan Supreme Court held that Michigan's Takings Clause is violated when FGUs sell tax-foreclosed property at auction and retain more than the taxes owed—as the GPTA required. *Rafaeli* held as a matter of Michigan property law that those with property interests in foreclosed property have a "right to collect the surplus proceeds that are realized from the tax-foreclosure sale," and that a county's "retention of those surplus proceeds under the GPTA amounts to a taking of a vested property right requiring just compensation" **under Michigan's Constitution**. The Court also relied

upon rights dating from the Magna Carta.





Back to the future: The Michigan Supreme Court Steps In (cont.)

The Michigan Supreme Court reasoned that, "when a property is taken to satisfy an unpaid tax debt, just compensation requires the [FGU] to return any proceeds from the tax-foreclosure sale in excess of the delinquent taxes, interest, penalties, and fees reasonably related to the foreclosure and sale of the property—*no more, no less.*" *Rafaeli* (emphasis added).

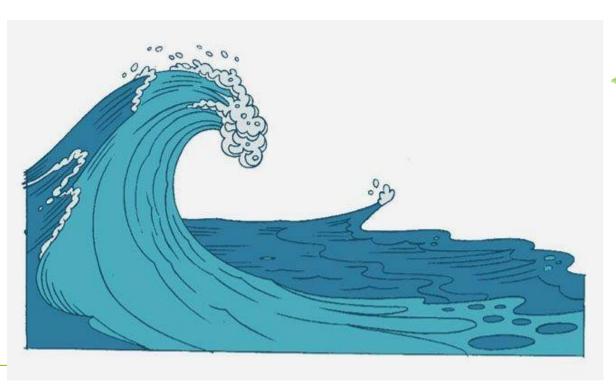
The Court further clarified a number of issues with surplus proceeds claims under the GPTA, and rejected fair market value as a measure of compensation for claimants.





Back to the future: Wave Of State And Federal Court Lawsuits

The United States Sixth Circuit Court of Appeals notes "deluge of litigation" in Michigan state and federal courts regarding Michigan's tax foreclosure system – based upon *Rafaeli*.







The Michigan Supreme Court in Rafaeli stated that:

"[n]othing in [its] holding . . . prevents the Legislature from enacting legislation that would require former property owners to avail themselves of certain procedural avenues to recover the surplus proceeds." *Id.* at 460 n.108.

So, during the depths of COVID restrictions and a little over a month after the 2020 elections...





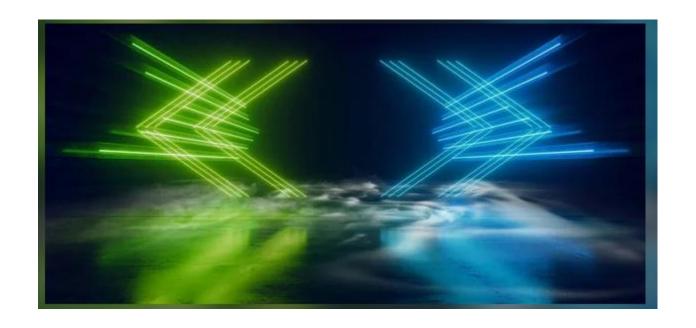
The Legislature responded to *Rafaeli* by amending the GPTA and creating a mechanism for former interest holders in tax foreclosed property to recover the surplus proceeds.

In December 2020, the Legislature unanimously adopted 2020 Public Acts 255 and 256, which provide a process for former interest holders in tax foreclosed to claim an interest in sale proceeds in excess of the minimum bid and other foreclosurerelated fees.





The new process applies to foreclosures occurring after *Rafaeli*. Like *Rafaeli*, Acts 255 and 256 allow former interest holders of foreclosed property to recover excess sale proceeds, but not fair market value. Mich. Comp. Laws § 211.78t.





Under Michigan law, any person with a "legal interest in property immediately before the effectiveness of a judgment of foreclosure of the property," may submit a claim for excess sales proceeds, including but not limited to former lienholders, mortgagors, heirs, along with the person listed on the deed for the tax foreclosed property. Mich. Comp. Laws § 211.78t(12).



Since *Rafaeli*, Michigan courts have applied its holding and further refined the relief available to surplus proceeds for claimants not subject to the Act 256 claims procedure. In *Proctor v. Saginaw Cty. Bd. of Comm'rs*, 340 Mich. App. 1; __ N.W.2d __ (Mich. Ct. App. 2022), *application pending*, the Michigan Court of Appeals rebuffed attempts to gain additional relief beyond that allowed under *Rafaeli* by adding federal claims. The court "disagree[d] with plaintiffs' contention that they are entitled to any recovery beyond the surplus proceeds from the tax foreclosure sale," but "agree[d] that plaintiffs are entitled to post-tax sale interest on such surplus proceeds." *Id.* at 27. The court observed that state law establishes the extent of a property interest, and the Fifth Amendment merely protects that interest, if any. *Id.* at 29.

On September 22, 2022, the Michigan Court of Appeals held that "Rafaeli did not announce a new rule of law but returned the law to that which was recognized at common law and by the ratifiers of the Michigan Constitution of 1963, see Rafaeli 505 Mich at 472, and should be given full retroactive effect." Schafer v. Kent Cty., 2022 Mich. App. LEXIS 5692, at *9 (Mich. Ct. App. Sept. 22, 2022), application pending.



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Back to the future: Back In the "Time-Machine" - Hall v. Oakland

On October 13, 2022, the Sixth Circuit issued its decision in Hall v. Meisner, 51 F.4th 185 (6th Cir. 2022) (cert. petition filed Mar. 10, 2023). Hall recognized the predominance of state law issues that permeate these matters, and ordered the district court to abstain from ruling on the plaintiff's takings claim under the Michigan Constitution. The court "vacate[d] the district court's dismissal of [plaintiffs'] takings claim under the Michigan Constitution . . . , and remand[ed] that claim with instructions for the district court to abstain from adjudicating it" because "[w]hether the facts alleged here violate the Michigan Constitution's Takings Clause is an issue for the Michigan courts to decide."





Back to the future: Back In the "Time-Machine" - Hall v. Oakland (cont.)

Nevertheless, *Hall* concluded that Oakland County had taken Ms. Hall's "equitable title" to her home at the time the property was foreclosed upon and title transferred to the FGU—which stated a claim for violation of the *federal* Takings Clause. 51 F.4th 196-97. The Sixth Circuit also relied upon property rights purportedly set forth in the *Magna Carta*.



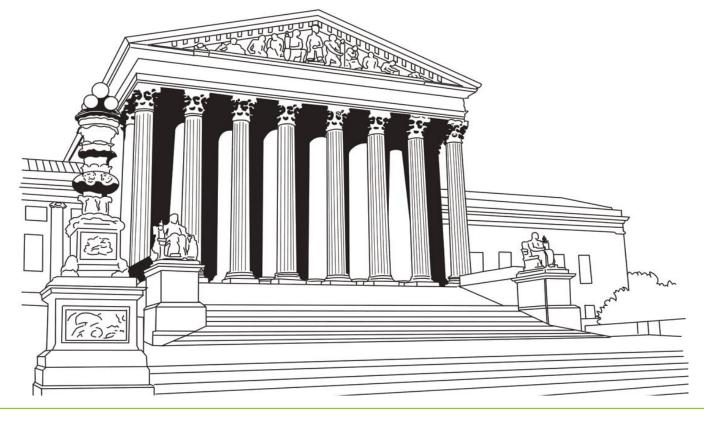
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Back to the future: Michigan Is Not Alone –The U.S. Supreme Court and Tyler v.

Hennepin County

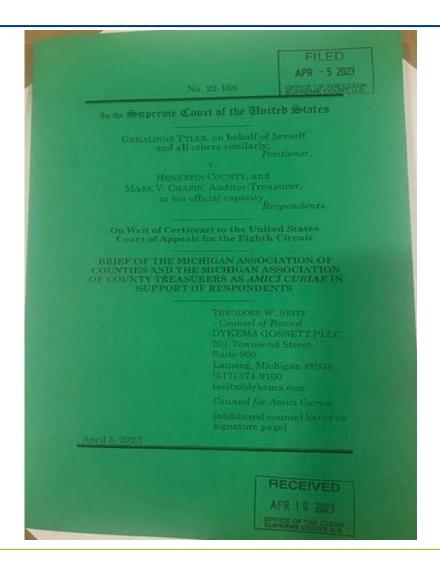
In January, the United States Supreme Court granted cert in case challenging Minnesota's tax foreclosure system under the federal Fifth (Takings) and Eighth

Amendments (Excessive Fines).



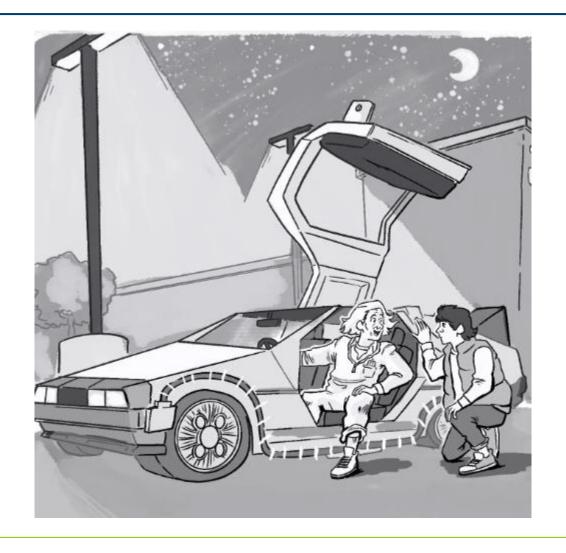


Back to the Future: MAC Offers Michigan's Unique Perspective





Back to the future: Who's/Whose "Right" and Where Do We Go From Here?





Questions?



- Email: <u>tseitz@dykema.com</u>
- Call after presentation:
 - Ted Seitz (517) 374-9149