MICHIGAN REAL PROPERTY REVIEW

Vol. 24, No. 3 **Fall, 1997**

THE "SPECULATIVE BUILDING" DESIGNATION IN ACT 198

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In 1974, the Michigan legislature enacted Act 198, the "Plant Rehabilitation and Industrial Development Districts Act" (the "Act"), to stimulate economic development and promote a favorable business climate in Michigan for manufacturers. The Act provides substantial property tax incentives for new manufacturing facilities located in Michigan.

Industrial operations are among the projects eligible for tax abatement under the Act. The kind of industrial property eligible for tax abatement includes real property improvements, buildings, structures and personal property, e.g., machinery, equipment, furniture and fixtures. This eligibility for abatement applies whether the industrial property is owned or leased.

If the qualified industrial user is a lessee of the real and/or personal property for which tax abatement is sought, the lessee must be the one responsible for paying the ad valorem real property taxes under the terms of the lease. When a tenant is sought for personal property, the qualified lessee must also be the owner or lessee of the personal property. If a non-qualified entity is responsible for the payment of the real property taxes, neither the landlord nor the manufacturer can receive tax abatement on real or personal property taxes, even though the facility may be leased to a manufacturer.

Generally, to obtain tax abatement under the Act, the area in which the facility is located must be first designated by the local governmental unit as an Industrial Development District (IDD). The IDD must be established before an application for tax abatement can be approved. The request for an IDD must be filed with the clerk of the municipality before construction or acquisition of the facility occurs. An application for tax abatement must be submitted to the local governmental unit within six months of the date the physical work commences on the project for which the abatement is sought.

The local government unit can approve tax abatement for any period from one to twelve years. If the application for tax abatement is approved, the local governmental unit forwards the application and the resolution approving the application to the State Tax Commission. The State Tax Commission reviews all of the documentation submitted. If the Act's requirements are satisfied, the State Tax Commission issues an Industrial Facilities Exemption Certificate ("IFEC") exempting the qualifying facility from ad valorem real and personal property taxes. The qualifying entity is then removed from the regular ad valorem tax rolls of the local governmental unit for the period for which tax abatement is granted and, instead of the normal ad valorem tax, it pays a specific tax called the "Industrial Facility Tax" ("IFT"). The IFT is 50% of the normal ad valorem property tax.

In all cases but one, an application for tax abatement must be made within six months of the date physical work commences on the project. The Act provides for the tolling of the "six-month" rule only in the case of "speculative buildings." A "speculative building" is defined in the Act as:

> ...a new building that meets all of the following criteria and the machinery, equipment, furniture and fixtures located in the new building:
>
> (a) The building is owned by, or approved as a speculative building by resolution of, a local governmental unit in which the building is located or the building is owned by a development organization and located in the district of the development organization.
>
> (b) The building is constructed for the purpose of providing a manufacturing facility before the identification of a specific user of that building.
>
> (c) The building does not qualify as a replacement facility. MCLA 207.553(8).

A qualified user who later takes occupancy of a building which has received a "speculative building" designation may obtain both real and personal property tax abatement under the Act. MCLA 207.560. The Act further provides that when tax abatement is granted to a qualified user, the effective date of the abatement is the December 31 next following the date that the speculative building or any portion of the speculative building is used as a manufacturing facility. MCLA 207.557(1).

Two kinds of "new" facilities are available to industrial users, the speculative building and what is commonly referred to as the "design/build" facility. In the design/build facility, the user consults with a builder/developer regarding the user's particular needs. After negotiations, the user and builder/developer enter into a contract to construct a facility tailored to the user's specifications. Work then commences on the construction of the facility. In the case of small manufacturing facilities, the time lapse from the execution of the contract to occupancy of the facility is generally less than one year.

The generic speculative building is a facility constructed by a builder/developer for sale or lease to a user or users who have yet to be identified. The size of the facility, the building and site layout, and the building's finishes are all determined by the builder/developer. The builder/developer makes these decisions based upon its experience and its prescience in anticipating future demands in the marketplace. Developers constructing generic speculative buildings design these facilities to be easily adaptable to the needs of a variety of industrial users.

A speculative building virtually eliminates the lag-time between the user's identification of its need for an industrial facility and its ability to take possession of that facility. A speculative building is ready for immediate occupancy. Speculative buildings are particularly attractive to industrial users who (a) do not have extraordinary operational requirements and so do not require facilities tailored for an unusual use, (b) do not have an opportunity to plan well in advance for their increased space needs and/or (c) who are temperamentally disinclined to assume the risks, delays or uncertainties that may be associated with a design/build process.

The Act's "speculative building" designation is only available for a "new" building constructed for or adaptable to use as a manufacturing facility. Rehabilitated or replacement buildings do not qualify as speculative buildings. The "speculative building" designation can be sought at any time from the date that the work on the improvement physically commences provided that the building has not yet been occupied. Once the building has been partially or completely occupied, it is no longer a "new" facility and can no longer receive the "speculative building" designation.

The Act does not specifically require that an IDD be created before a project can receive the speculative building designation. The language of the Act supports the interpretation that a project can receive a "speculative building" designation before creating an industrial development district. MCLA 207.553(8)(a). To date there are no published cases to guide counsel for the applicant or counsel for the local unit, nor has the State Tax Commission adopted any rules, regulations or policy statements on this issue. This interpretation, however, is consistent with the legislative intent and would, if adopted, encourage local governmental units to utilize the speculative building designation. Because the local governmental unit may be resistant to a request to create an IDD for a speculative building, the elimination of the requirement to create an IDD as a prerequisite to granting the designation should reassure the local governmental unit that it will retain all of its options vis-a-vis the later review of the request for the creation of an IDD and the actual application for tax abatement when a qualified user is ultimately identified.

The first step to obtain a "speculative building" designation under the Act is to apply by letter to the local governmental unit in which the facility is to be built. When the letter request for the designation and all accompanying documentation have been submitted, the request is scheduled for a public hearing before the governing body of the local unit. At the close of the public hearing, the local governmental unit may adopt a resolution designating the facility as a "speculative building" thereby tolling the six-month rule and saving the opportunity for tax abatement for a subsequently identified and qualified user.

Each local governmental unit has its own requirements for the kind, nature and extent of the information required to be included with the written request. Some local units have existing tax abatement policies which set forth, inter alia, the criteria that the facility must meet in order to obtain the "speculative building" designation. Some local governmental units have no comprehensive tax abatement policies or have policies which do not include criteria for the "speculative building" designation. There is a general resistance to the concept of speculative buildings receiving "tax abatement." This bias usually proceeds from a lack of familiarity with the concept and reflects the community's mistaken belief that a "speculator" is seeking favorable tax treatment at the expense of the community and other taxpayers. In these cases, the familiarization of the local governmental unit with the concept of the speculative building designation and its advantages to the community is necessary.

Facilities designated as "speculative buildings" under the Act are exempt from the general requirement that the application for tax abatement to be filed within six months of the date that the physical work on the project is commenced. The application for tax abatement by a qualified user can be filed after the expiration of the six-month period. The "speculative building" designation is intended to preserve for

a qualified end-user the opportunity to apply for tax abatement after the expiration of the normal six-month period. The designation itself does not grant tax abatement for the facility to the builder/developer. It does not even commit the city to grant tax abatement to a qualified user except under such terms and conditions as may be acceptable to the city when the application is actually made.

A developer who constructs a speculative building and requests a "speculative building" designation under the Act should consider including in its application a statement that the facility may be leased out by portions or units. The written request should describe the number of units into which the facility may be divided, the square footage of each unit, and a statement that the developer reserves the right to later assemble some or all of the units into a larger unit or units. A sketch of each unit's location within the facility should also be provided. Care should be taken that each unit is configured in such a way that it can be easily assembled into a larger unit to suit the particular needs of a qualified user.

A builder/developer who gives a local governmental unit notice that the facility may be divided into units, describes the units by square footage, and provides a visual depiction of those units should anticipate that the local governmental unit will be disinclined to allow it to reduce the size of the several units at a later date. The recommended practice is that the builder/developer create individual "building block" units of such square footage and in such a configuration that each can be easily assembled into a larger unit to accommodate the qualified manufacturer.

The reason for including in the application the statement that the facility may be divided into units is to preserve the opportunity for tax abatement for a qualified user of less than the entire facility. Should a non-qualified user take possession of a portion of the facility before a qualified user and the application for the designation fails to include a statement that the facility may be divided into portions or units, the State Tax Commission has indicated that it will take the position that the entire facility loses its character as a "new" facility and that such an event forecloses the opportunity for tax abatement for a later qualified user.

Industrial areas which are eligible for tax abatement will tend to develop faster than similar property where abatement is not available. The "speculative building" designation can be effectively used by a local governmental unit to direct and accelerate industrial growth in targeted areas. These areas can be used as tools to realize a local governmental unit's specific goals, e.g., diversification of its tax base, diversification of its industrial base, increasing the tax base for special municipal projects, and diversion of new development traffic from already congested areas, etc. The "speculative building" designation and the development of objective criteria for the consideration of the application for that designation should be an integral part of a community's tax abatement policy.

Buildings which receive a "speculative building" designation can be warehoused in a municipality's inventory of industrial sites which are immediately available to qualified users seeking tax abatement. Unoccupied speculative buildings, or those ultimately occupied by users who do not qualify for tax abatement, remain on the municipality's tax rolls at the normal non-homestead tax rates. Even when a facility is designated as a "speculative building," the local governmental unit has the discretion to accept or reject the application of an otherwise qualified user, the authority to determine the number of years for which it will grant tax abatement (if it does approve an application) and the ability to impose upon a qualified user in a tax abatement agreement such conditions as the local governmental unit deems appropriate in connection with the grant of tax abatement.

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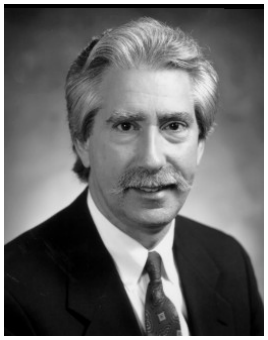

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