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Ax Your Taxes

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February 9, 2010

Property tax bills comprise as much as half of a property's operating costs. Overassessments imposed by municipalities saddle property owners with an unfair share of the tax burden. These unjustified assessments directly and materially impact the property's net operating income and consequently the taxpayer's bottom line. Each year, however, another opportunity is presented to take action to plug this significant revenue drain.

A real property tax appeal, particularly amid a distressed real estate market, presents a ready way to reset the municipality's assessment consistent with the property's true fair market value. Where the market value of property plunges, the taxes associated with that property should naturally follow suit.

That concept certainly has gained traction, as astute property owners filed an unprecedented number of appeals in 2009. Due to budgetary constraints, most municipalities do not conduct formal property revaluations more than every 10 years. This does not mean, however, that local governments are unaware of the economic climate and its impact upon property values. As a result, taxpayers that file an appeal will likely benefit, either through consensual negotiated settlements or by virtue of judicial decisions.

Cole Schotz, for example, recently represented the owner of a 138,000-square-foot distressed office building in Lyndhurst. By impressing upon the town that the property was plagued with an 86% vacancy rate and was in need of significant capital investment to improve marketability, the town agreed to settle the matter by reducing the assessment from a value indicating $126 per square foot to $108 per foot. This multi-year resolution resulted in over $149,000 in tax savings for the proactive property owner.

In January of each year, taxpayers receive a Property Tax Assessment Notice that identifies the assessments assigned to properties for the current tax year. Making the assumption that this figure reflects the property's true value, however, can prove an expensive mistake. In years when a town has conducted a town-wide revaluation--again, about every 10 years--the numbers should match. As property values adjust each year thereafter, however, tax administrators will apply an equalization ratio, which takes into account the previous year's average sale prices when compared to the average of these properties' assessments on the books. Only by applying this equalization ratio is a taxpayer able to understand the true value dictated by the assessment number.

In New Jersey, for example, the county tax administrator determines equalization ratios by comparing arms' length sales transactions during the past tax year. If the average assessment value on single-family homes is $1 million, for instance, and last year's average sale price was $2 million, the equalization ratio is 50%. In reality, this process is more nuanced, as commercial, industrial and residential properties and vacant land are evaluated separately and a weighted average is utilized depending on the property type's relative relationship to the town property makeup. The administrator ultimately arrives at one equalization ratio for the entire town regardless of the property at issue.

It is therefore the assessed value, as equalized by the applicable ratio (that is, divided by the ratio), that taxpayers should compare to fair market value when determining whether to file an appeal. If this equalized value does not reflect a particular property's fair market value, the taxpayer will be stuck paying higher taxes than are warranted. This overage, if left unchecked, will compound annually as municipalities' tax rates continue to trend upward. Because the filing of an appeal also creates a risk that towns may seek a tax increase, through a cross-appeal, a preliminary assessment of value, conducted with the assistance of your attorney and appraisal expert, is critical before filing.

As soon as the property's current assessment is confirmed, by reviewing the Property Tax Assessment Notice, the owner--or a tenant that bears the majority of the property tax obligation--should schedule an appointment with an attorney who is experienced in commercial property taxation and who has relationships with professional appraisers. The attorney will then be able to perform, at no cost, the necessary preliminary analysis and determine whether an appeal has merit. If the appeal is warranted, attorneys usually handle these matters on a contingency-fee basis--so there is no attorney fee unless tax savings are realized.

The appeal process itself is fairly straightforward. Filing deadlines are critical, as they are jurisdictional in nature and typically fall in or around the first quarter of the year--e.g., Mar. 1 in New York and Apr. 1 in New Jersey. The necessary filing will include basic information like address, block and lot and the current assessment. A simple declaration that the property is being overassessed usually suffices, as the appraisal report/testimony will ultimately form the crux of the case.

Towns will typically settle if made to understand that significant exposure exists or if the amount in controversy resembles the cost to defend. The municipality will also be motivated to resolve the discrepancy in order to avoid budget problems in the future and to avoid the possible expense of floating bonds in order to fund sizeable refunds. Municipalities will usually negotiate resolutions that favor awarding taxpayers credits against future tax obligations so as to avoid this very situation. If an appeal is not settled, the current backlog of cases means that a formal adjudication on the merits will not occur for at least a year.

For commercial properties, appraisal fees range from $3,500 to $10,000, plus hourly rates for appearances at settlement conferences or trial. Taxpayers can often manage these costs by having the appraiser prepare a less expensive summary-limited report for negotiation purposes, as the vast majority of cases settle. Taxpayers can also expect an attorney contingency fee ranging between 25% and 33% of any tax savings actually realized.

Ultimately, pursuing a meritorious tax appeal means that owners and/or tenants can ensure that they are paying only their fair share of the municipality's tax burden and no more. A tax reduction also improves the owner's net operating income and bottom line. It additionally makes the property more marketable, as a critical component of any prospective buyer's due diligence involves a review of a property's income and expenses and tenants will consider the amount of taxes their prospective leases would obligate them to pay.

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