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TAX CERTIORARI AND CONDEMNATION



Performing Due Diligence On Taxes and Condemnation

All too often as tax certiorari and condemnation attorneys we have been called upon to remedy or at least alleviate the failure of purchasers and their attorneys to fully perform due diligence or carefully draft contractual clauses relating to real property tax and condemnation.

Real Property Taxes

Real property taxes – especially in high tax areas such as Nassau County and New York City – are often a property's single highest expense. Since both Nassau County and New York City now undertake annual reassessments the possibility of future tax shock is readily apparent.

Taxpayers in Nassau County and New York City should now be aware of the possibility of a reassessment on sale during the annual revaluation process. However, the county's 2003 revaluation coming after decades without any revaluation lulled many property owners into complacency. For instance, a client contracted to purchase an apartment house in August 2002 just five months before the county revaluation became effective, but during the period in which tax impact notices showing its effect were being sent out. The purchaser valued the property on the bases of the 2001-02 property taxes of \$65,000, plus an estimated 2002-03 increase. The 2003 revaluation increased the taxes to \$125,000, effectively reducing the value of the property by over \$600,000.

Checking out the then available information about the revaluation would have enabled the client to either renegotiate

the sale price or delay the purchase until definitive assessment and tax information were obtainable. Information on pending revaluation is available by calling the local assessor or the County Director of Real Property Tax Services. Most attorneys specializing in the review of real property tax assessments will also know of pending revaluations in their areas.

A purchase of those assessing units which annually reassess, i.e. Nassau County and New York City, will not necessarily trigger an increase in assessment based solely on the purchase price. Most assessment officials and property tax attorneys agree that the new sale prices are significant but not the only factor in establishing a new assessment. Both Nassau County and New York City want to keep the assessment of similar properties roughly comparable. Thus, the effect of a high sale price will often be limited.

Relatively low sale prices will not always result in lower assessments. Purchasing a property with a long term lease is often more akin to purchasing the lease rather than the property. Such a lease, i.e. for an anchor or supermarket in a shopping center, or a freestanding commercial or retail building, may be below market. In such a case, the purchase is for the landlord's leasehold value and does not include the value of the tenant's leasehold rights. The assessor may quite properly ignore the purchase price in favor of a capitalization of current rental values.

The more difficult question is "what happens after a sale in assessing jurisdictions which a.) do not annually reassess or b.) are not planning a revaluation?" The simple answer is that nothing should happen.. Reassessment solely on sale or in the absence of a comprehensive plan of reassessment is not allowed. "The respondents' practice of selective reassessment of only those properties in the village which were sold during the prior year contravenes statutory and constitutional mandates. *Krugman v Board of Accessors*. 141 A.D.2d 175,183,533 N.Y.2d 495, 501 (2d Dept. 1988). (The author was counsel for amici curiae in this case) See also *Stern v Assessor, City of Rye*, 268 A.D.2d 482, 483, 702 N.Y.S2d 100, 102 (2d Dept. 2000), where the city's program to selectively reassess properties which were both recently improved by adding the value of the improvements to the recent purchase prices, was invalidated.

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Reassessment on sale has been allowed when all properties are reviewed and a sale is one of several circumstances that may result in reassessment. *Nash v. Assessor, Town of Southampton*, 168 A.D. 2d 102, 108, 571, N.Y.S 2d 951, 955 (2d Dept. 1991), (The author was counsel for the property owners in this case).

Condemnation

Most major highways have planned widenings or improvements which may not occur for many years, if not decades. The seller does not always have notice of such future road improvements. Moreover, even when the owner has notice, such improvements may not physically take place for many years and are, thus invisible to the naked eye.

Seemingly minor road widenings can have a drastic effect on value. Consider a six acre shopping center with 120,000 square feet of store area and 350 parking spaces. Condemnation of a 10-foot-wide strip along the highway could eliminate up to 70 parking spaces, drastically reducing the operating effectiveness and value of the center. The loss of curb cuts could result in the inability of trucks to conveniently access the property.

There is little relevant applicable statutory law. If the contract is silent on the issue of condemnation, the Uniform Vendor and Purchaser Risk Act (General Obligations Law, §5-1311) applies. If “all or a material part” of the property “is taken by eminent domain, the vendor can not enforce the contract, and the purchaser is thereby deprived of the right to enforce the contract; but there shall be, to the extent of the ...taking, an abatement of the purchase price.”

What to do about these problems? Suggested responses include:

1. The purchaser should check out whether a condemnation is in the works. Although any unit of government – as well as utilities and public authorities—may acquire property, the vast majority of takings are partial acquisitions for road improvements by governments which own and control the road. It is a relatively simple matter for a purchaser’s attorney to make an inquiry to the New York State Department of Transportation, or a county, town or village department of public works, to check out actual and future highway plans.

2. The contract of sale should contain a specific provision dealing with the rights and obligations of the parties in the event of both full and partial takings. Partial takings present the most problems.

If a taking occurs between contract and closing – in the absence of a provision to the contrary – the seller who is still in title is the owner of the claim. However, the purchaser, although having no claim, ultimately suffers the consequences of the taking. The simplest solution is to provide that, in such circumstances, the purchaser has the option to close and the sole right to make a claim. At a minimum, the purchaser would have a remedy to offset economic losses by filing a claim for just compensation.

There are many permutations on this theme. The contract could also provide for a specific reduction in the purchase price based on a specific formula. It is not the scope of this article to discuss the many formulas and considerations which go into determining the economic effect of a partial taking and how counsel should deal with them. The basic advice is that there should be some provision so that it does not result in messy litigation.

3. A purchaser should demand a representation of no notice of taking. Frequently, one party or the other is aware of a planned condemnation. What happens when the seller is aware of the pendency of a condemnation, but the purchaser is not? Can the seller not disclose this knowledge to the purchaser?

If so, what are the consequences? Is this fraud? Can the contract be rescinded? Can the purchaser sue for damages? The cases are mixed on these questions. Some hold that, even if the seller is fully aware of the pendency of a condemnation, non-disclosure is not grounds for rescission or damages. The court’s reasoning is essentially that this knowledge is generally available to the purchaser had it exercised due diligence. Other cases have gone the opposite way, imputing to the seller an obligation of good faith to disclose and allowing the purchaser to pursue a remedy.

The real answer is no real estate practitioner should allow this situation to occur. The purchaser should always demand a representation from the seller that it is not aware of any pending condemnation. Here, too, there are various shades of obligation and disclosure. A demand that the seller disclose knowledge of any “threatened condemnation” is too all encompassing and impractical. A more practical demand is for the seller to represent that it has not received “written” notification of a condemnation. This is reasonable since a condemnation under the Eminent Domain Procedure Law must be preceded by some notice even if the condemnation is actually some years away. This is a concrete item which the seller can disclose and upon which the purchaser can make a reasonable business determination.

One further proviso. It would also be prudent for the purchaser’s attorney to consult with someone familiar with condemnation law and procedures so that he or she can frame an appropriate provision to address the problem. Variations in contractual provisions and the allocation of damages are virtually endless and deserve some close attention. However, a condemnation provision drafted without the guidance of a lawyer familiar with condemnation may fail to take into account the practicalities of how the condemnation process occurs and the way that damages can be paid.

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