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New Appeal

-- Seeking Reassessment? Act Now, Tax Attorneys Warn --

By Suzann D. Silverman as published by ***Commercial Property Executive***, June 2010

With the Federal Reserve repeatedly calling attention to commercial real estate assets' decline in market value and reduced access to financing, taxing jurisdictions have shown greater openness of late to appeals for reduced property taxes. That trend has offered many owners some badly needed breathing room. But as municipalities themselves become more strapped for cash, winning tax appeals looks likely to become much more challenging.

The commercial property sector is a natural place for municipalities to look for revenue, noted Elliott Pollack, chairman of the property valuation department of Pullman & Comley L.L.C. and a director of the American Property Tax Counsel. After all, commercial properties already make up a large proportion of communities' tax bases, and most legislators would much rather hike taxes on a local office building than on their constituents.

Some states have enacted tax caps, according to Stephen Paul, a partner at Baker & Daniels L.L.P. and vice president of the Tax Counsel.

But those limits can be deceiving. In Indiana, where he practices, residents' taxes are limited to 1 percent of value, while apartments are capped at 2 percent and commercial property at 3 percent. The risk, Paul said, is that the greatest pressure to raise assessments will be on commercial properties, which have the highest ceiling by percentage.

And when property values do inevitably begin to climb, the raw tax liability will naturally rise with them.

Paul expects a surge in tax litigation to result, with local appeals becoming harder to win and a greater number reaching the state level.

Eventually, these cases will get a fair hearing, he believes, but that outcome may require a time-consuming, expensive effort by owners.

The steady erosion of municipal finances across the country presents an additional reason for concern, according to John Garippa, senior partner of Garippa Lotz & Giannuario and president of the Tax Counsel.

While bonding capacity should yield enough cash for municipalities to cover refunds, at least in theory, Garippa forsees potential for reductions in many municipalities' ability to bond. Legislation may also cause delays by extending the deadlines for municipalities to distribute tax refunds.

The predicted rise in interest rates is also likely to have an impact, he noted, driving cap rates up and asset values down. "That's why it's important for clients to be on top of this," he cautioned.

When it comes to property tax disputes, being on top of it means preparing in advance to appeal to ensure that deadlines are met, and then gathering the details necessary to persuade the court. While many property owners file appeals every year (most settle rather than try their luck in the backlogged courts), there are still a good number that do not, Garippa said. But with assessments based on the previous year's data, current assessments may not fully reflect the market downturn. That offers an opportunity to argue for an assessment decrease.

In New York City, for instance, the Real Property Income & Expense filings that the finance department required in 2009 were based on 2008 data, which did not reflect the full extent of the commercial real estate market crash that occurred at year-end 2008, explained Joseph Giminaro, special counselor & co-manager of the tax certiorari department for Stroock & Stroock & Lavan L.L.P. It is too soon to evaluate how the tax commission will view updated data, but Glenn Newman, president of the commission, has indicated that he wants to see all data that shows the difficulties property owners are enduring. "I think it's very favorable that the tax commission is openly saying it wants to hear these stories," Giminaro observed.

That positive attitude seems common nationally. Tax certiorari attorneys, who specialize in tax appeals, are achieving some significant reductions.

In the hospitality arena, for example, "it is not unusual to see total assessments drop by more than a third," said Garippa, who represents some of the nation's largest hotel operators. Big-box stores saw a similar drop in the past year, he noted. Pollack, too, has seen significant decreases; he reports that appeals for hotel properties are typically garnering tax reductions of 20 to 40 percent. And while hotel and retail properties have been subject to the largest overassessments, owners of other property types can also mount successful appeals. Older industrial properties are another big area.

Taxing jurisdictions typically have based value largely on income capitalization and replacement value, not comparable sales, but one area that offers growing potential to strengthen appeals is brand value, since so-called intangible benefits are not taxable. Retail and hospitality properties are the categories whose brand value is most readily recognized by tax courts, according to Paul. Part of hotels' income is derived from the flag, and shopping centers typically count on big-name stores to attract customers.

Mall owners have brought branding to a new level in recent years with efforts for company name recognition among consumers. Office property owners are newer to this strategy and have had less success. However, that will come with time, Paul predicted.

In the meantime, with data now available on the softer market and municipal difficulties looming, "now's the time to take a tax appeal," Paul said.

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