

Practice Update

Challenging New York City Real Property Taxes

January 15, 2018

New York City faces a continuing decline in state and federal funding and increased property taxes continue to be a reliable revenue stream to fund local services. Every January 15th, the NYC Department of Finance (DOF) sends to each owner of NYC commercial real property a Tentative Assessment setting forth (i) the market value of the lot (including improvements), (ii) the actual assessed value of the lot, and, most importantly, (iii) the value upon which the lot will be taxed for the upcoming tax year. The property owner has until March 1st to challenge the Tentative Assessment determining the amount of tax to be paid on the property. If this tax appeal, often referred to as Tax Certiorari or Tax Cert, is not filed by March 1st, the owner loses any right to challenge the assessment for the upcoming tax year.

An overview of the key dates, approaches for valuation, and process for challenging findings are outlined below.

Important Dates

The NYC real property tax assessment and Tax Cert procedure is calendar driven. Please consider the following dates:

- The upcoming NYC tax year begins on July 1, 2018 and runs through June 30, 2019 (the 2018/2019

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tax year).

- The January 15, 2018 Tentative Assessment for the 2018/2019 tax year is based on the property's condition as of January 5, 2018 (referred to as the "Tax Status Date").
- **The absolute deadline for filing a Tax Cert challenge to a property's assessment is March 1, 2018**, as property owners that do not file Tax Cert applications by March 1st lose any right to contest assessments for the ensuing July 1, 2018 through June 30, 2019 tax year.

Permitted Valuation Approach

Most NYC commercial property is comprised of Tax Class 2 properties (i.e., buildings with greater than three residential units, such as cooperatives and condominiums) and Tax Class 4 properties (i.e., non-residential commercial property other than utility buildings). For tax assessment purposes, the market value of each commercial property is determined using the income capitalization approach. Neither the cost approach (sometimes called the replacement approach) nor the comparable sales approach is used by NYC to value Class 2 or Class 4 property for tax assessment purposes.

For income-producing commercial properties, the actual income and expenses reported by the property owner are used to determine the property's net operating income. *For mixed-use property*, each category of income must be separately stated; for example, gross residential income must be separated from gross office income. All income derived from the property must be disclosed; including parking receipts, laundry income, and utility and tax escalations paid by tenants. Similarly, in determining net revenue expenses directly related to the operation of the property that are to be deducted from the gross revenue must be separately stated.

Non-operational expenses, such as mortgage interest, depreciation, and corporate income tax, are not considered. Although the entire cost of a capital

improvement cannot be deducted in the year of expenditure, a reasonable reserve may be treated as a deduction for one or more years.

For owner-occupied commercial property, the income from comparable (i.e., comparable in terms of location, use, size, age, and condition) income-producing property is imputed on a per square foot basis to the owner-occupied property. For example, the rental income reported by the owner of a comparable factory is imputed to an owner-occupied factory. Similarly, the income reported by the owner of a comparable rental apartment building is imputed to a cooperative or condominium residential building.

For properties that are partially owner-occupied, comparable rent is imputed to the owner-occupied portions of the property and actual rent is considered for the non-owner-occupied portions.

Expenses for owner-occupied properties are calculated as a percentage of gross imputed income based upon the nature, condition, and use of the property.

After determining net operating income, a capitalization rate (often called the cap rate) is applied. In simple terms, the cap rate is the annual rate of return expected by an investor in the property. The cap rate varies based on the use, condition, and location of a particular commercial property. Arithmetically, the cap rate is the net operating income divided by the market value of a property expressed as a percentage. In many cases, the success of a Tax Cert appeal hinges on the cap rate applicable to the property.

NYC Tax Commission Hearings

Between March and October, the NYC Tax Commission conducts hearings with property owners who have timely challenged their Tentative Assessments or their representatives to consider whether an assessment should be reduced. At such

hearings, information and documentation supporting a property owner's appeal may be presented. Hearing Officers typically render decisions within weeks of a hearing.

If the property owner accepts a NYC Tax Commission offer to reduce the assessment, the Tax Cert process is concluded, the reduction is effective as of July 1st, and the property owner may apply for a refund of any tax overpayment. If the NYC Tax Commission does not extend an offer to reduce the assessment, or if the property owner does not accept the offer (e.g., the property owner believes that a greater reduction is warranted), the Tax Cert appeal for the current year may be continued by filing a Petition in New York Supreme Court on or before October 24th. It is noteworthy that Tax Cert cases very rarely proceed to trial because the appeals for which Petitions are filed are considered in the next year by the NYC Tax Commission, which has jurisdiction over two years of Tax Cert cases (i.e., those initiated in the current year and those continued from the previous year).

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