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How a purchase price may affect your property taxes: Answering common questions

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The volume of commercial real estate transactions continues to increase and is predicted to reach a ten-year high in 2016. This has led many owners to inquire as to how their purchase price will impact their property tax burden. Prospective purchasers contact our office with increasing frequency during the diligence stage, requesting an analysis of their tax burden in light of a potential sale. There are a variety of factors that should be taken into account when reviewing a purchase and its property tax situation. Below are some common questions highlighting misconceptions about purchase prices and assessments.

Will my property taxes go up as a result of my purchase price?

Some of our clients have expressed concern that their assessed value and corresponding property taxes will be increased as a result of the purchase price. Each jurisdiction is different in the way a purchase price is considered.

Practitioners in the field are typically aware of a jurisdiction's intention to perform a revaluation and re-assess properties for an upcoming assessment roll. For example, Nassau County is no longer performing annual revaluations, but has plans to perform a revaluation for the 2018 assessment roll. If a property is located in a jurisdiction that performs revaluations, the sales price will be taken into consideration during that process. The assessment should not be raised to the purchase price without first considering all factors surrounding the sale. It is of critical importance that counsel explain these factors to the assessor and provide evidence as to why they should be reviewed in conjunction with purchase price.

Many jurisdictions have not performed revaluations in decades. In these jurisdictions, the assessor cannot raise the assessment as a result of a sale. Even if a sale shows a property to be significantly underassessed, the assessor may not change the assessment. Any increase of the assessment in these jurisdictions as a result of sale would result in "selective reassessment." The highest court in the state has determined that if a property is reassessed based upon sale in these jurisdictions, such a change is illegal and the assessment should be returned to the previous value.

Will my property taxes be decreased if my purchase price is below the assessment?

If the purchase price is below the market value of the current assessment, a grievance should be filed for the assessor to review the property and its claimed assessment. The assessor will need the relevant documentation and an explanation of the factors impacting the sale in order to make a determination that the sale was arm's length and legitimately indicated market value. Upon such a determination, a buyer of over-assessed property may achieve significant tax savings.

What other information will influence the assessor's opinion of value?

The assessor will want to review the contract of sale and closing documents in order to confirm the buyer and seller are not related in any fashion. Counsel should also explain to the assessor any additional factors that may have influenced the transaction. For example, a 1031 exchange allows property owners to defer capital gains or losses due upon sale, so long as the property is received within 180 days. Buyers approaching the expiration of 1031 benefits may pay a purchase price premium for a property rather than let the 1031 period expire. An assessor unaware of this crucial information will not be able to properly factor it into their determination.

Similarly, property purchased with the intent to occupy can influence the price paid. This is an even more significant factor if the purchaser occupied the property prior to the purchase. In that scenario, the cost of moving, the potential loss of workers because of a relocation, and the intangible value of a known location to customers and colleagues may persuade a current occupant to pay above market value. This will need to be presented to the assessor as key factors in the purchase price.

The assessor will also want to make sure the property was sufficiently exposed to the market and the sale was not distressed. While bank sales are often distressed, the recession has changed the way some banks shed assets. Many banks now have strong relationships with the real estate community, relationships that allow banks to market assets more efficiently. However, a bank sale can still raise the suspicion of a distressed situation. Property owners should be prepared to demonstrate to the assessor that the property's price is representative of market value.

All of the factors outlined above need to be considered in conjunction with the jurisdiction in which they are located. This will enable the property owner to accurately budget their tax burden as well as avail themselves of the opportunity to achieve significant tax savings.

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