City assessor's approach could exacerbate damage to negatively impacted properties post-pandemic - by Peter Blond

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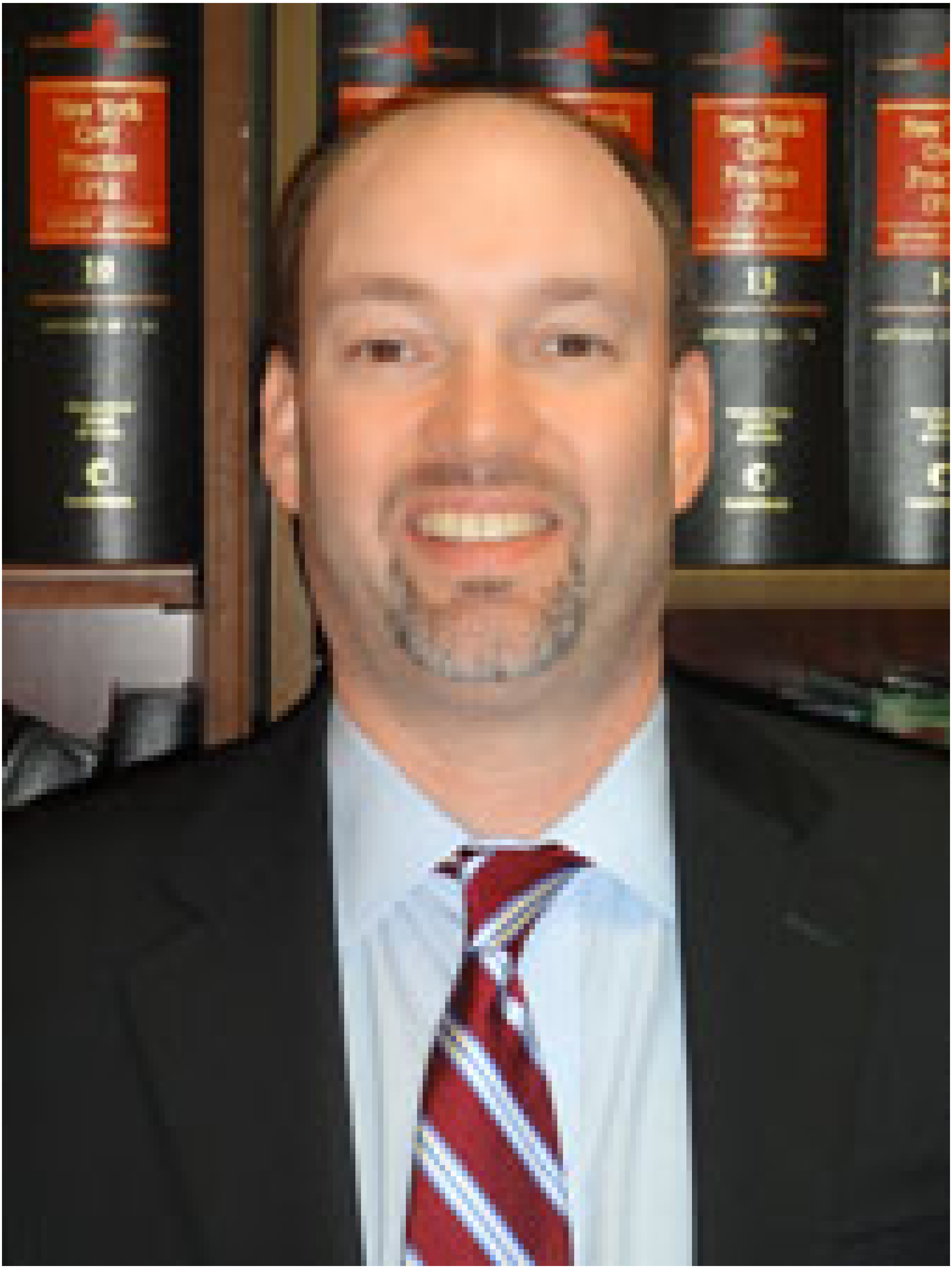

With the return of Broadway and seemingly "life" in Midtown Manhattan, the New York City Department of Finance may feel more emboldened to raise assessments aggressively in January. Any assessment increases in January will impact real estate tax bills commencing in July of 2022. While incremental improvements certainly have been appearing in all boroughs for most occupancy types, the local economic recovery is still in its infancy. Without politicizing the discussion, Federal financial assistance to state and local governments was enormous in 2020 & 2021 for mostly obvious and necessary reasons. Yet, unless you believe money trees grow in The White House garden, an equal or greater Federal bailout is highly unlikely in 2022.

It is critical to keep in mind that the City Department of Finance slashed assessments in January of 2021 (presumably in response to the anticipated economic damage inflicted by the pandemic). As is frequently the case, however, in moments of blind panic we often grasp for whatever is in reach. There are many that would describe the city's actions as a lesser of evils approach in light of the damage caused to so many properties by the pandemic. While there is no doubting the city's goal to do the right thing, the approach may ironically exacerbate the damage for the properties most negatively impacted.

Similar to the method utilized by the Department of Finance following Hurricane Sandy, 2021/22 assessments were generally slashed by certain percentages based on building classification and location. In response to Sandy, finance granted certain zip codes 10% reductions to their actual assessment that also typically held for the following tax year as well. This included many properties that were wholly unaffected by Sandy's wrath but got to enjoy the ride.

Contrast that with 2021's pandemic policy that led to reductions in excess of 30% for some property types, such as retail. While a blind reduction of 10% is unlikely to shift the rental marketplace's balance of power (because each property presents its own pros and cons to determine the appropriate level of rent per s/f), 30% is massive. For example, two physically identical contiguous properties both received a 30% reduction from the Department of Finance on the 2021/22 actual assessment roll. Let's assume for discussion purposes that both properties had identical actual assessments for 2020/21 & 2021/22. Let's also assume that both properties received nearly identical gross income per annum prior to the pandemic. Both properties have three stories with ground floor retail and upper floor office space.

Property X was deeply impacted by the pandemic insofar as their "Mom and Pop" retail tenants all vacated and have not been replaced. The office tenants remain in place, but several have been granted rent concessions and several still owe rent for periods of 2020. The property's potential annual rent roll has decreased from $400,000 per year to $200,000. To be clear, this is a property suffering from a 50% drop in the potential GI while the city has blindly granted a 30% reduction to the assessed value.

Property Y was fortunate enough to largely have institutional retail tenants that mostly paid in 2020 and mostly remain in place with previous lease arrangements as is. One small store at Property Y is vacant. The office tenants remain in place with some minor arrears/concessions granted. The property's potential annual rent roll has decreased from $400,000 per year to $360,000. To be clear, this is a property suffering from a 10% drop in the potential GI while the city blindly granted the same 30% reduction to the assessed value.

As landlords desperately search for tenants, the rental prospects for Property X’s vacant retail will be negatively impacted by competitor buildings’ ability to offer equal taxes per s/f but in a tenanted building with a more stable landlord. Needless to say Property Y’s landlord can also be more aggressive in base rent offerings to attract the tenant whereas the building in much greater distress would likely be in a weakened position to accept such a level of income if the building is simultaneously servicing debt.

While it was never the city’s intention to create or exacerbate the winners and losers in post-pandemic real estate, the question as to how they will treat the greatly disparate real estate tax outcomes moving forward remains to be seen. Based purely on economics, many properties may receive enormous increases in January whether called for or not. It is accordingly critical to consult with your tax certiorari counsel to determine if your 2021 income and expenses and January 5th, 2021 rent roll support your 2022/23 assessed value, which should be released on or about January 15th, 2022.

Peter Blond, Esq. is a partner at Brandt, Steinberg, Lewis & Blond LLP and the immediate past chair of the NYC Bar committee on condemnation & tax certiorari, New York, N.Y.