# Rising inflation should reduce property taxes, not increase them - by Brad Cronin and Sean Cronin

December 14, 2021 - Long Island

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Among the many fears that come with rising inflation is a concern that inflation will be another factor that will increase property taxes. However, if analyzed properly, inflation is actually a factor that should suppress property taxes, not increase them. This is due to the fact that most property sectors are experiencing stagnant or declining rents, yet inflation has increased virtually every line item in the expense category for owners. The resulting decrease in net operating income directly affects the property value for assessment purposes and, therefore, should result in a lower property tax amount.

Owners have been finding ways to manage higher expenses for almost two years now. Many property owners have only recently stabilized their new expense budgets in response to COVID and its variants. Now, after navigating historically difficult circumstances, property owners are being wacked with rapidly increasing inflation.

Inflation decreased owner's net operating income in just a short period of time and shows no sign of ceasing any time soon. Labor shortages have increased the cost of almost every service required to maintain and repair commercial properties. Supply chain issues have then further multiplied the impact of wage inflation. Even when the more expensive labor is available, the cost of raw materials has gone up exponentially. After laying out money for greater cleaning costs, lay out reconfigurations and countless dollars on PPE equipment, owners must now account for paying even more for management costs, maintenance costs, and skyrocketing amounts for capital expenditures.

Just as property expense budgets are rising, so are municipal budgets. Increases to budgets have been tempered in the past by New York's two-percent tax cap. The tax cap limits increases in the levy to two-percent or the rate of inflation, whichever is less. For years, low inflation was assisting owners by keeping the increases in budgets well below two-percent. Thus, the corresponding tax rate increases were much lower than if budgets were increasing at the full two-percent cited in the law. Now, we embark on a new period of time when inflation will be beyond two-percent, thus maximizing the amount budgets can increase. In addition, municipalities still retain the right to pierce the two-percent cap with a majority vote.

A simple analysis would indicate that while budgets go up, so must property taxes. This is only true if all other factors remain equal. If COVID has taught us anything, it is that all property sectors were affected differently. Retail, office and hospitality were shut down, reopened and reinvented in the way many of these operations now run their businesses. These sectors bore the brunt of the COVID changes to property ownership and saw that reflected in their bottom line. The assessor's formula, which determines the appropriate value for tax purposes, requires all these factors to be taken into consideration. When collections decline or remain the same, but inflation causes expenses to increase, this yields a lower value at which a property should be taxed.

The other component that must be altered when analyzing a property in the new world is the risk associated with that investment. We are seeing investors flee for more consistent opportunities rather than navigate the ever-changing terrain of commercial real estate. Even those that stay in the real estate market, there is no doubt that an industrial building with high ceilings is currently a more straightforward investment than a retail strip center. This volatility in both the uncertainty in net income, as well as the market sector at large, must be captured in the form of a higher capitalization rate. This higher cap rate will then yield a lower assessment for tax purposes.

Most experts are predicting that inflation is here at least for the immediate future. For some property owners, if inflation can be counteracted by correspondingly rising revenue, the impact can be combatted to a degree. However, for property sectors that have seen a decline in the desirability of their investment due to decreased net income, inflation is a devastating blow. Under these circumstances, a property owner cannot just grin and bear the higher tax rates. Owners must be ready to provide evidence to show that inflation does not impact all properties evenly. This proof will show that for their property, inflation has adversely impacted their bottom line. This negative impact can then be turned around to display that the inflation phenomenon compels a decrease in their assessment and tax burden under the assessor's formula.

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