Tax Planning Identifies Options, Outlines Strategies

When buying commercial property, prospective owners typically focus their attention on tenancy, operational costs, and long-term income growth potential. While those are important factors, buyers should also consider the potential savings from thoroughly analyzing the real estate tax bill.

Taxes are sometimes viewed as a necessary evil that can be ignored until after the closing. While ignorance may be bliss for a short time, this approach can have significant financial implications. Buyers might be missing important grounds for appeal that would affect the tax assessment and the corresponding tax bill. At the same time, they could be overlooking changes in the assessed value that resulted in short-lived tax reductions.

This is particularly true in retail properties that have experienced changes in vacancy or income in recent years. By reviewing an assessment before the purchase, buyers can ensure they are not swayed by misleading tax bills or not missing opportunities for appeals.

As the prospective buyer, you'll want to determine if the owner obtained assessment relief prior to the purchase. If so, the tax bill on which your tax prorations are based could grossly understate what you'll pay in the first year of ownership. For example, if the assessment were reduced in one year based on vacancy, the assessment will be returned to full value in the following year. Once a vacant building has changed hands, obtaining vacancy relief becomes problematic particularly when the purchase price exceeds the Assessor's estimate of market value as vacant. This is just one regular example of buyer oversight that winds up causing problems after the purchase. It is important to have these discussions in advance of the closing so you are fully informed about the tax bill on which you base your tax and purchase price assumptions.

At the same time, new owners regularly assume that appeals are only available every three years or four years, depending on the property's location. Although the assessment cycle may have already commenced, property owners can appeal their assessments each year assuming there is a basis for an appeal.

For example, if a building has a significant drop in occupancy or income, is being renovated, or has structural damage, or other changes that would affect its value, those factors can be part of an appeal any year, so long as it is filed by the deadline. Ownership should never assume that an appeal is not warranted without first discussing it with their tax advisors.

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As investors and business owners consider buying a property, they should review the assessment and consider whether it accurately reflects the market value. They should also determine what calculations were used in estimating market value.

While no one likes to pay taxes, it is important to approach with as much lead time and attention as one would apply to other building financial issues. Real estate taxes can account for more than 50 percent of a building's expenses, making it an important area of focus for any prospective buyer.

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