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Court of Appeals
STATE OF NEW YORK

TAX EQUITY NOW NY LLC,

Plaintiff-Respondent-Appellant,

– against –

CITY OF NEW YORK, NEW YORK CITY DEPARTMENT OF FINANCE,

Defendants-Appellants,

STATE OF NEW YORK, NEW YORK OFFICE OF REAL PROPERTY TAX SERVICES,

Defendants-Appellants-Respondents.

AMICUS BRIEF FOR CITIZENS BUDGET COMMISSION

Date Completed: October 27, 2022

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 500.1(f) of the Rules of Practice of the Court of Appeals of the State of New York, the Citizens Budget Commission states that it has no parent corporation and issues no stock; therefore, no publicly held corporation owns 10% or more of the Citizens Budget Commission.

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STATEMENT OF INTEREST OF *AMICUS CURIAE* CITIZENS BUDGET COMMISSION

Citizens Budget Commission ("CBC") is a nonpartisan, nonprofit civic organization whose mission is to achieve constructive change in the finances and services of New York City and New York State governments. CBC was founded in 1932 as a research organization to analyze the City's finances and evaluate the management of its government, to report on these matters to CBC's trustees, and to make recommendations for improvements to municipal officials. CBC expanded its scope of research in 1984 to include the State government.

As a respected watchdog, research organization, and nonpartisan resource dedicated to improving the financial management of the City and the State for the benefit of all New Yorkers, CBC has investigated, researched, and documented the flaws in the City's property tax system. Overseen by its trustees, who are highly accredited individuals with professional experiences in government and the private sector, CBC has written a number of reports that address the inequities created by the property tax system. These reports generally utilize publicly available data and information generated by other research organizations, such as the Independent Budget Office of New York City and the Furman Center at New York University. Staff members of CBC have given testimony before both

City and State legislative hearings concerning these matters.[1] CBC has consistently reached the same conclusion over many years: New York City's real property tax system is inherently unfair.[2] CBC submits this brief as *amicus curiae* to present the CBC's position on this important issue, and to provide the Court with information about the unfairness of New York City's real property tax system.

SUMMARY OF ARGUMENT

A fundamental principle of tax policy prescribes that similarly situated properties should be taxed at the same rate. New York City's current tax system in many ways fails to adhere to this core principle of horizontal equity. Specifically, residential homes with the same value are taxed at materially different amounts. Importantly, the tax system disadvantages homeowners in areas experiencing slow market appreciation or depreciation. These issues demand a determination that the

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[1] *See, e.g.*, Ana Champeny, *Testimony on Preliminary Report on New York City Property Tax Reform, Submitted to the New York City Advisory Commission on Property Tax Reform,* Citizens Budget Comm'n (June 16, 2021), https://cbcny.org/advocacy/testimony-preliminary-report-new-york-city-property-tax-reform; Ana Champeny, *New York City Property Tax Reform: Testimony Submitted to the New York City Advisory Commission on Property Tax Reform*, Citizens Budget Comm'n (Nov. 27, 2018), https://cbcny.org/advocacy/new-york-city-property-tax-reform; Carol Kellerman, *Testimony on Flaws in New York City's Real Property Taxation System Submitted to the NYS Assembly Committee on Real Property Taxation*, Citizen Budget Comm'n (Jan. 22, 2016), https://cbcny.org/advocacy/testimony-flaws-new-york-citys-real-property-taxation-system.

[2] *See id.*; *see also* Ana Champeny, *Comments on New York City Property Tax Reform*, Citizens Budget Comm'n (Dec. 4, 2019), https://cbcny.org/advocacy/comments-new-york-city-property-tax-reform; Andrew Hayashi, *Options for Property Tax Reform: Equitable Revenue Raising Reforms for New York City's Property Tax* (Dec. 6, 2013), https://cbcny.org/sites/default/-files/media/files/Options%20for%20Property%20Tax%20Reform.pdf [hereinafter Options for Prop. Tax Reform].

current system must be overhauled to comport with constitutional and established legal precepts requiring fairness and non-discrimination. As *amicus curiae*, CBC respectfully submits this brief in support of the positions advocated by Plaintiff-Appellant Tax Equity Now NY LLC ("TENNY").

NEW YORK CITY'S PROPERTY TAX SYSTEM
<u>IS CRITICAL TO NEW YORK CITY'S FISCAL STABILITY</u>

New York City faces daunting and unique issues with regard to establishing the taxable value of property. Fairness in New York's property tax system is essential given the extraordinary importance of the property tax to the City's economy and fiscal stability.[3] The City's property tax revenue is a function of the value of all private taxable real estate—commercial, residential and utility—in New York City, and has grown rapidly, increasing about four times, from $327 billion in fiscal year 2000 to $1.39 trillion in fiscal year 2023.[4] The property tax is expected to generate $31.2 billion in revenue in fiscal year 2023, which amounts to nearly 31 percent of the City's revenue, or nearly $1 out of every $3 that the City

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[3] References to the "City" are to Defendants-Respondents City of New York and New York City Department of Finance, and references to the "State" are to Defendants-Respondents State of New York and New York Office of Real Property Tax Services.

[4] *See* N.Y.C. Dep't of Fin., *Annual Report of the New York City Property Tax, Fiscal Year 2019* (Aug. 2019), https://www1.nyc.gov/assets/finance/downloads/pdf/reports/reports-property-tax/nyc_property_fy19.pdf; N.Y.C. Dep't of Fin., *2022/23 Final Assessment Roll* (May 25, 2022), https://www1.nyc.gov/assets/finance/downloads/pdf/22pdf/fy23_final_roll_summary.pdf.

spends.[5] The property tax has been a stable source of income for the City—property tax revenue has grown an average of 6.0 percent per year since 1999.[6] As the most significant and stable source of tax revenue in New York City, the property tax system is crucial to enabling the City's successful, efficient, and just operation.

NEW YORK CITY'S PROPERTY TAX SYSTEM CREATES UNJUSTIFIED INEQUITIES AMONG RESIDENTS

Notwithstanding the importance of tax revenue to the City, the property tax system is wildly unfair and inequitable. In New York City, a property's tax bill—the amount of property taxes owed in a given year—involves a complex, multistep calculation that lacks the transparency and equity necessary for a fair tax system, particularly when, as is the case in New York City, the property tax system is such an important source of tax revenue.[7] The laws governing the property tax system in New York City permit for the imposition of different assessment rules and tax rates on the four different property classes, and the City assesses and taxes different properties within each class at significantly different percentages of market value. Intra- and inter-class disparities manifest themselves when two properties

[5] N.Y. Office of Mgmt. & Budget, NYC Mayor, *Adopted 2023 Financial Plan (2022)*, https://www1.nyc.gov/assets/omb/downloads/pdf/fp6-22.pdf; Champeny, *Comments on New York City Property Tax Reform*, *supra* note 2.

[6] Champeny, *Comments on New York City Property Tax Reform*, *supra* note 2.

[7] *See generally* Options for Prop. Tax Reform, *supra* note 2.

have the same market value but substantially different property tax bills. Indeed, disparities among individual properties can be far greater than the average intra- or inter-class imbalances suggest. As addressed below, the laws of the State and practices of the City lead to disparities in taxation among and within classes, resulting in conspicuous inequities.

A. The City's Class Share System Inequitably Distributes Tax Burdens.

New York City's property tax system unfairly distributes the tax burden among the City's residents and property owners. Following a legal challenge to the property tax assessment practices of the town of Islip, in 1981 the New York State Legislature passed S7000A, which created a new property classification system for Nassau County and New York City. S7000A established a class share system, whereby each class of property was to continue to pay roughly the same share of the levy as in 1981, subject to modest annual adjustments. The share of market value each class represents, however, is not constrained. While nearly half of all property value in the City derives from Class One properties (one-, two-, and three-family homes, and condominiums in small buildings), only 14.2 percent of the levy is collected from that class.[8] The favorable treatment of Class One properties is

[8] *See* N.Y. City Council, Res. No. 1365-2020 (Council Member Daniel Dromm).

reflected in the tax burdens on the other classes[9] (including other rental buildings and commercial properties), all of which bear a much larger share of the property tax levy than their share of market value.

When comparing property tax burdens, the appropriate measure is the effective tax rate ("ETR"), which is the tax liability divided by the market value. The discrepancy between the class shares of the levy and of market values causes average ETRs in different classes to diverge starkly. The result is that the average Class One ETR is lower than the average ETR for other classes. While some divergence in ETRs among different property types can be justified by policy rationales, the class share system results in homeowners generally facing a lower property tax burden than renters, despite the former group tending to be wealthier than the latter group, on average.

Real Property Tax Law ("RPTL") Section 1803-a seeks to address this issue by requiring the City Council to reset the class shares each year to account for changes due to market forces and physical changes (such as new construction), with the formula for these calculations detailed in the law.[10] State law limits the increase

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[9] Class Two properties include all other residential property, including rentals, condos, and co-operative properties. Class Three properties are utility properties. Class Four properties are commercial properties. N.Y. Real. Prop. Tax Law § 1802; *see also* Options for Prop. Tax Reform, *supra* note 2, at 2.

[10] N.Y. Real Prop. Tax Law § 1803-a.

in each class's share to five percent each year; increases in excess of the cap are distributed to the other classes at the sole discretion of the City Council. The City and State have avoided or limited the impact of this obligation to redistribute class levy shares in response to physical and market forces by enacting annual legislation to reduce this cap on the increase in class shares.[11] By 2010, the cumulative effect of the lower caps on class shares was an average tax reduction of $832 per Class One parcel.[12] As a result, Classes Three and Four subsidize Class One, notwithstanding the fact that Class One holds nearly half of all of the property value in the City.

B. City and State Assessment Rules and Methodologies Lead to Inequities Between Properties of the Same Value in Different Tax Classes.

The current property tax scheme levies disparate tax burdens on properties of the same value in different classes. For example, CBC reviewed and analyzed the property tax bills for a two-family brick home (Class One) in Park Slope/Carroll Gardens and an office building (Class Four) in East New York/Starrett City.[13] For each property, the market value in fiscal year 2013 was $483,000. Under

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[11] *See* N.Y.C. Dep't of Fin., *Annual Report of the New York City Property Tax, Fiscal Year 2019*, *supra* note 4.

[12] Letter from Ronnie Lowenstein, Dir., Indep. Budget Office, to Steven Spinola, President, Real Estate Board of N.Y. (June 15, 2010), https://ibo.nyc.ny.us/iboreports/-classharejune-152010.pdf.

[13] *See* Options for Prop. Tax Reform, *supra* note 2, at 4.

a "pure" property tax system in which assessment was based solely on market value, both properties would be assessed and taxed at the same rate. However, the home in Brooklyn has an assessment ratio (the ratio of the assessed value to the market value) of only 1.21 percent, while the commercial property is assessed at 45 percent of its full market value. Although the target assessment ratio for Class One is six percent, the Park Slope/Carroll Gardens home in this example has an even lower assessment ratio because of caps that limit assessment increases over one- and five-year periods.

When considered along with the nominal tax rates set for each class, the inequity in tax burden between the two properties is easy to see. The ETR, the property tax as a share of market value, is 0.22 percent for the two-family home and 4.63 percent for the office building. While there are policy reasons for a municipality to place a higher tax burden on certain types of properties, this example highlights the extreme differences in New York City, with the owner of the commercial property paying a tax bill *21 times greater* than the owner of the two-family home, despite their properties having the same market value. The high tax burden on the commercial property creates an unappealing climate that deters commercial activity in areas that need it, and the disparity is unfair to the taxpayer whose asset is taxed at a much higher rate than other similarly valued properties.

Similar discrepancies in assessment ratios and ETRs arise between one-to-three family homes and large rental properties, resulting in a higher tax burden generally on renters compared to homeowners, despite the latter group tending to be wealthier than the former on average.[14]

C. Assessment Rules Also Lead to Inequities Between Similarly Valued Properties in the Same Class.

Similarly situated properties within the same class are not treated uniformly. Caps on assessment increases and phase-ins result in properties with the same market value being assessed and taxed differently, depending on market trends in their neighborhoods. The result is completely counterintuitive: the practice of imposing caps results in lower ETRs for properties in appreciating neighborhoods.

Among one-, two-, and three-family homes, the ETR ranged from well below 0.25 percent to a maximum of 1.31 percent in fiscal year 2019.[15] In 2019, just 42 of 188 neighborhoods had ETRs above 1.0 percent, including 17 of 18 neighborhoods in Staten Island, 16 of 37 neighborhoods in the Bronx, seven of 57 neighborhoods in Queens, just two of 49 neighborhoods in Brooklyn, and none of

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[14] N.Y.C. Indep. Budget Office, *Twenty-Five Years After S7000A: How Property Tax Burdens Have Shifted in New York City* (Dec. 5, 2006), https://ibo.nyc.ny.us/iboreports/propertytax120506.pdf.

[15] Jenna Davis & Ana Champeny, *New York City Homeowners: Who's Got the Unfairest Tax Burden of Them All*, Citizens Budget Comm'n (Sept. 12, 2018), https://cbcny.org/research/new-york-city-homeowners.

Manhattan's 27 neighborhoods. A higher ETR is directly related to the assessment ratios found in those neighborhoods; neighborhoods with median ETRs above 1.0 percent all have median assessment ratios above 4.8 percent (compared to a target of six percent). Conversely, the 34 neighborhoods with median ETRs below 0.5 percent all had median assessment ratios below 2.2 percent.

Furthermore, although commercial buildings and residential buildings with more than ten units are not protected by the assessment caps described above, the phase-in rules applicable to these properties generate intra-class inequities in a similar manner; properties in fast-appreciating neighborhoods end up with lower ETRs than identically valued properties in neighborhoods with more stable prices. To illustrate the intra-class inequity caused by phase-ins, CBC analyzed two residential properties with more than six units and no commercial space, one in Bay Ridge/Dyker Heights, Brooklyn and the other in Kingsbridge Heights/Bedford, the Bronx.[16] Although the first property was worth $19,000 more than the second property in fiscal year 2013, as determined by the income-producing standard for Class Two buildings, its assessment ratio was 26.19 percent, while the ratio for the second property was 45 percent. The reason for this disparity was that the first property had been appreciating, while the second property had been depreciating. In this case, the result was that the ETR for the Kingsbridge Heights property was 72

[16] Options for Prop. Tax Reform, *supra* note 2, at 6–7.

percent higher than the ETR for the property in Bay Ridge: 4.99 percent versus 2.90 percent.

D. The Undervaluation of Co-ops and Condos Causes Both Inter- and Intra-Class Inequity.

The valuation methodology for Class Two, all residential properties not included in Class One, is another source of inter- and intra-class inequity, both among Class Two co-ops and condos themselves, as well as between co-ops and condos and large rental buildings. A significant number of Class Two buildings are owner-occupied condos and co-ops, rather than income-generating rental properties. Nonetheless, RPTL Section 581 requires the City to value condos and co-op buildings as if they were rental properties.[17] The Department of Finance ("DOF") therefore looks to the income and expenses from comparable rental buildings to estimate the income that owner-occupied condos and co-ops would generate if rented. This approach significantly understates the market value of co-op and condo units, compared to the price at which these units would sell in the private market—the benchmark used to determine market value for Class One homes. This process especially undervalues condo or co-op buildings constructed before 1974.[18] For

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[17] N.Y. Real Prop. Tax Law § 581.

[18] Furman Ctr. for Real Estate & Urban Policy, *Shifting the Burden: Examining the Undertaxation of Some of the Most Valuable Properties in New York City* (July 2013), https://furmancenter.org/-files/FurmanCenter_ShiftingtheBurden.pdf.

these properties, the comparable rental buildings chosen by the DOF often contain units subject to rent regulation, which typically generate less income than unregulated buildings and serve as a poor basis for estimating potential income for pre-war co-ops.

Furthermore, the valuation method leads to inequities between owner-occupied co-ops and condos and rental buildings. Because condos and co-op buildings are typically undervalued, they have lower assessed values and, consequently, lower tax bills and ETRs than they would if they were assessed on the basis of more accurate valuations, *i.e.*, based upon current sales.[19] In addition, many Class Two condos and co-ops receive significant tax abatements, reducing their bills by at least 17.5 percent.[20] The combined effect of undervaluation and the abatement is enormous. The average ETR for Class Two condos and co-ops in fiscal year 2013 was 4.08 percent based on the DOF's determinations of market value, and only 0.78 percent when an alternative, sales-based valuation methodology is used and the abatement is taken into account (the latter rate is comparable to the average ETR for Class One residential property in FY 2013).[21] By contrast, the average ETR for large

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[19] *See* Options for Prop. Tax Reform, *supra* note 2, at 7–8.

[20] *See* N.Y.C. Dep't Of Fin., *Cooperative & Condominium Tax Abatement*, (last updated 2022), https://www1.nyc.gov/site/finance/benefits/landlords-coop-condo.page.

[21] *See* Options for Prop. Tax Reform, *supra* note 2, at 7.

Class Two rental buildings is 4.60 percent.[22] Owners of rental buildings pass on at least part of the property tax liability to tenants, meaning that renters with lower average incomes face a higher tax burden than co-op and condo owners with higher average incomes.

E. Comprehensive Property Tax Reform Is Needed to Address Inequities in the New York City Property Tax.

The preceding examples demonstrate that similarly valued properties are not uniformly treated by the City. Though the target assessment ratio is six percent of market value for Class One properties and 45 percent of market value for the other classes, the reality is that the assessment ratio is oftentimes vastly different from the target assessment ratio due, in large part, to the effects of the State-imposed caps and phase-ins. Therefore, owners of properties with the same market values have their properties assessed at substantially different amounts and pay substantially different taxes, an unfair result that should be corrected.

For these reasons, for several years, CBC has advocated for substantial reform to the New York City property tax system. CBC has advocated for the State to require a multiyear, phased-in narrowing of differences in effective tax rates among types of property by overhauling the provisions for caps and phase-ins so

[22] *Id.*

they become more equitable.[23] Specifically, CBC recommended the elimination of the existing share system, elimination of assessment caps, and implementation of a valuation system that reflects actual real estate market value, using more transparent methods that take advantage of the data available to the Department of Finance.[24] CBC has also supported the repeal of Section 581 and the reclassification of cooperative buildings and residential condominium units within Class One, where the valuation would be based on comparable sales prices.[25] Additionally, CBC has supported a property tax relief program to provide a rebate of owner-occupied residential property tax bills when those tax bills exceed a set share of income, commonly referred to as "circuit breakers."[26]

CONCLUSION

For the foregoing reasons, CBC supports TENNY's brief in support of its appeal from the February 7, 2020 decision and order of the Supreme Court, Appellate Division, First Department. While the ostensible purpose of property classification is to help reduce the tax bill for certain properties and to support certain of the City's policy goals, wide disparity in tax treatment persists among and within

[23] Kellerman, *Testimony on Flaws in New York City's Real Property Taxation System Submitted to the NYS Assembly Committee on Real Property Taxation*, *supra* note 1.

[24] Champeny, *New York City Property Tax Reform: Testimony Submitted to the New York City Advisory Commission on Property Tax Reform*, *supra* note 1.

[25] *Id.*

[26] *Id.*

the classes, arising from flaws in the market value and assessment process.[27] The City's tax system should be fair, economically efficient, inexpensive to administer, transparent to taxpayers, and susceptible to few unintended consequences. The present property tax system lacks all of these characteristics. Thus, CBC respectfully submits that these issues warrant this Court's attention and, ultimately, a determination by the trial court that the current system must be changed.

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[27] *Id.*

CERTIFICATE OF COMPLIANCE

I hereby certify pursuant to 22 NYCR § 500.13 that the foregoing brief was prepared on a computer. A proportionally spaced typeface was used as follows:

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