

10 Commonly Overlooked Ways To Reduce California Real Property Taxes

As property tax practitioners, we at Ad Valorem Solutions (AVS) often assumed that all owners of commercial property in California recognize that they can reduce their taxes to a minimum – they just occasionally needed our assistance in getting there. We have found that assumption to be misplaced, however. While most owners are quick to challenge a valuation that they believe is too high, many have only a vague notion of the numerous other avenues available to lessen their property tax burden. The following are 10 ways to lower taxes that are frequently overlooked by even the most sophisticated California commercial property owner; there are a myriad of others.

1. Failure To File Proposition 8 Appeal By September 15 Of Each Tax Year

The easiest but most commonly overlooked action is the filing of a Prop. 8 appeal by 9/15 of each tax year. A Prop. 8 appeal, unlike a base year value appeal, contests the value for a particular tax year only; the resulting value can be increased by the Assessor in any subsequent year to the “trended base year value.” Since it applies only to a single year, you must make a timely filing or you cannot obtain a tax refund for that year. You snooze, you lose – even though you may successfully lower your assessment for a specific tax year, you won’t get a refund if you haven’t made a timely appeal filing. We strongly urge our clients: when in doubt, FILE. The only downside is that once you proceed with an appeal, the Assessment Appeals Board can raise your assessed value as well as lower it; however, since you can always withdraw your appeal without penalty before hearing, this risk can readily be managed.

The form of appeal supposedly is standardized throughout California. It isn’t. You therefore should ensure that you have the most current form for all counties in which you own property. Each year, you should determine which properties are candidates for appeal, whether by reason of over-valuation, erroneous base year valuation or erroneous change of ownership determination (the latter two are discussed below). Carefully fill out the form. In your opinion of value, don’t state a value in excess of what you might be able to prove at hearing. Check ALL conceivable bases for your appeal, and except in rare cases, check the box indicating that you desire your appeal also to serve as a claim for refund. This will enable you to collect some interest if you’re successful. Remember: you can win your appeal, but if you have failed to make a timely filing or to indicate that you desire your appeal to serve as a claim for refund, you won’t recover all the money to which you are entitled.

2. Failure To File Appeal Of Supplemental Or Escape Assessment Within 60 Days Of Mailing

Whenever you receive any correspondence from the Assessor or the Tax Collector, read it carefully IMMEDIATELY. The issuance of certain notices (not your receipt or review) starts that clock on immutable appeal deadlines. You probably are familiar with supplemental assessments; they’re typically issued when a property has been sold or ownership otherwise changes or when new construction has been completed. Escape assessments are less common, but you may see more of them in the coming years. They are issued when the Assessor discovers that he’s missed something – a change of ownership, new construction or even an erroneous exemption. They can show up at any time. Don’t ignore these notices.

Appeals must be filed within 60 days after the date the supplemental/escape notice was issued or you won’t be entitled to a refund of taxes. In certain circumstances that date is extended to 60 days after your receipt of a tax bill for the assessment, but why chance it – file an appeal within 60 days after the date appearing on the notice. Again, you have to use the form provided by the Assessor for the county in which the property is located so be sure to request those forms immediately. State your basis for appeal clearly and when in doubt, check more boxes rather than fewer. You won’t be entitled to a refund if you don’t file a timely appeal, even if you are found to be right in contesting the new value.

3. **Failure To Seek Correction of Erroneous Change of Ownership Determination/Base Year Value.**

This one requires a careful review of historical records. If the Assessor has reassessed your property in the past on the basis of an alleged change of ownership, e.g., a transfer of more than a majority interest in a partnership, but you determine that a change of ownership did not occur, you may appeal that reassessment at any time. But even if you're successful, you may not be entitled to a refund of taxes paid. You can obtain a refund only if you have made a timely filing of an appeal. Remember too that the Assessor can seek to reassess your property – many years after the fact – if he “discovers” a missed change of ownership. Recently we were successful in overturning an escape assessment that was issued some fourteen years after the alleged change of ownership! The moral is that you should examine any potential or alleged changes of ownership that may have occurred during your occupancy of a property and determine the appropriate course of action. The sooner you act, the more you'll save in property taxes.

A property's base year value can be changed only upon a change of ownership or after new construction. Irrespective of its genesis, the new base year value must be appealed within four (4) years after the tax year in which it is determined (except as to an erroneous change of ownership determination, which can be appealed at any time). Unlike a Prop. 8 value, once a base year value has been reduced, you gain the benefit of that reduction in all succeeding tax years, so the tax saving impact is substantial. Again, however, you are not entitled to a refund – even if you successfully lower the base year value – for any tax year in which you failed to file an appeal. This is a prime motivation for filing an appeal if there is ANY possible basis for a reduction. You can always dismiss the appeal if you later determine that it is without merit.

4. **Failure to give timely notice of change of partners/shareholders/members to the Secretary of State –even if the transaction does not trigger a Change of Control (More than 50%)**

Being aware of the rules can help to save tax dollars by avoiding penalties. The law requires any person or legal entity acquiring ownership in any corporation, partnership, limited liability company or other legal entity owning real estate in California subject to local property taxation to complete a change of ownership statement with the State Board of Equalization within 45 days of the transaction. Failure to do so can result in 10% penalty of the taxes assessed on the new base year value or, in the event that the transaction does not represent a change in control, the penalty is based on 10% of the current assessed value. So, if you are involved in partnerships that own real estate, learn the rules and save tax dollars.

5. **Failure To Ascertain If Ownership Entity Subject To “Original Co-Owner” Rules**

When a partnership, corporation or limited liability company holds title to real property, the property usually will not be subject to change of ownership reassessment unless there has been a transfer of at least a controlling interest, e.g., a new party has obtained more than a 50% interest, or an existing minority owner has obtained a majority interest, in the entity owning the property. Smart owners structure any significant change in the ownership of corporate shares or partnership/limited liability company interests in a way which avoids a change in ownership and resulting reassessment. But even the most diligent owner often overlooks the “original co-owner” rules and finds out – too late – that what appears to be a transfer of less than a majority interest is actually a change of ownership for property tax purposes.

Under the original co-owner rules, parties holding title to property in one form, for example, three (3) co-tenants each owning a one-third interest, can transfer title to another entity, for example a limited liability company, in which they hold interests in the exact same proportion, i.e., one-third each, without triggering a reassessment. This exclusion has its price. If after the transfer, the original co-owners transfer – cumulatively over time - more than 50% of the ownership interests in the new entity, there is a change of ownership, and resulting reassessment, when the threshold has been crossed, even if no owner has obtained more than 50% of the ownership interests. Most owners subject to the original co-owner rules fail to realize that the triggering event has occurred until it's too late.

6. Failure to file the 571L Business Property Statement by the last Friday in May, or as directed by the Assessor.

Anyone doing business in California who has in excess of \$100,000 of business property MUST file a Business Property Statement (571L). Many small business owners are unaware of this requirement and can be surprised when they receive a four year escape assessment with a large “failure to file” penalty. Business property includes all the usual things such as machinery and equipment, office furniture, computers and related equipment, communications systems, tenant improvements and art objects. It does not take much to add up to the \$100,000 minimum. Check out our asset base and contact the assessor to get the filing requirements and forms.

The statutory deadline for filing the 571L is the last Friday in May. DON'T put it off, as failure to file timely can cost you 10% of assessed value. FILE, FILE, FILE, as failure to not filing at all could result in a 25% penalty. Remember, you are in control, learn the rules and apply them to your situation and save tax dollars.

7. Failure To Seek Cancellation Of Penalties, Interest and Redemption Fees On Delinquent Taxes

Believe it or not, there are situations where you can obtain a cancellation of the penalties, interest and redemption fees on delinquent taxes – which accrue at the rate of 10% for the first year and 18% for each year thereafter. We've been successful in eliminating penalties and interest going back 5 years, but it required an exhaustive search of tax bills and Assessor's records to establish grounds for the cancellation. Some owners who get behind in their tax payments seek an installment plan, but we find that such plans often limit your ability to negotiate future reductions in penalties and interest. Since each situation is different, if you haven't made the first installment by December 10 or the final installment by April 10, don't just assume that you owe the penalty and interest. There are a number recognized grounds for avoiding this extra expense.

In certain situations, if your cash flow is tight and you feel confident that your timely filed appeal will result in a reduction in your assessment, you may determine not to pay your taxes on time. Contrary to popular belief, in many (but not all) counties in California, timely payment of contested property taxes is not a requirement for pursuing an assessment appeal. In fact, in those counties, so long as you are successful in obtaining any reduction in the assessment for which the taxes owed, you may pay the full amount of the reduced taxes – without interest or penalty – within thirty (30) days after the date of mailing of a corrected tax bill. Even in those counties which have adopted an ordinance to require payment of taxes as a condition of your appeal, you don't have to pay the full amount of the contested taxes so long as you obtain a reduction in the challenged assessment. Not a tactic for the faint of heart but a very effective way to deal with cash flow difficulties in the right situation.

8. Failure to segregate costs for new construction and to reconcile building costs reported the Business Property Statement (571L).

Here is another chance to create your own tax savings. To save the money though, you must learn the rules and make sure they are applied to your project. With NEW construction projects it is common to incur costs that may not be assessable. These types of costs would include expenditures that do not add value to the project such as demolition, excessive ground preparation costs and change orders. These costs are normally captured by category in project accounting records. The idea is that if IT'S NOT THERE, IT DOES NOT ADD VALUE. When these COSTS ARE REMOVED from the cost records that are reported to the assessor, the costs are not included in the assessed value. It is REALY that simple, but it is rarely done.

In a situation where tenants have lots of improvements, it can also be prudent to check to make sure the owner and tenant ARE NOT REPORTING THE SAME COSTS. It common for double assessments of tenant improvement costs to occur. Remember that the real estate division in the assessor's office rarely discusses account information with the business property division. So, duplications can and do

happen. Look for the opportunity and if you find it, file an appeal to get your value reduced and your money back.

9. Failure to file for property tax exclusion of Seismic, ADA and Fire Suppression construction costs within 30 days of project completion.

Here is an opportunity to be creative and save tax dollars at the same time. Like other overlooked opportunities to save property tax dollars –YOU MUST ACT TIMELY. This exclusion from property tax was enacted to encourage building owners to upgrade certain safety-related items in their buildings. The exclusion is for costs that are incurred in the remodel or upgrading of an existing building which include seismic or earthquake retrofitting, fire suppression or improvements that would make a building more assessable to disabled persons. The costs can include overlooked items such as demolition, and costs necessary to accommodate the retrofitted item. The development of these costs to be excluded from your assessment is a GREAT opportunity to save tax dollars.

To cash in on this opportunity, visit the assessor's office before your project begins, and inform them that you want to take advantage of the applicable exclusion. FILE the exclusion forms as soon as your excluded costs have been identified, but in no case LATER THAN 30 DAYS PAST PROJECT COMPLETION. Remember, if you don't file, you lose.

10. Failure To Seek Refund Of Documentary Transfer Tax Erroneously Paid

This one always raises eyebrows. Most sellers of commercial property (since the seller typically pays transfer taxes) assume that if the Recorder demands payment of the tax as a condition to recording the grant deed or other transfer document, the tax must be owed. Not necessarily so. We recently recovered \$170,000 for a seller who had no idea that no tax was owed, but the Recorder, once we provided the legal basis, quickly refunded all taxes paid. The documentary transfer tax statutes are ancient and ambiguous, and counties have resisted every effort to clarify those statutes at the state level. Couple that with the fact that most sellers are only giving up a small portion of their gains (the tax ranges from a low of \$1.10 to a high of 16.10 per \$1,000 of taxable value), and you have the perfect setting for a "painless" tax.

There have been a number of recent California appellate court decisions that give a taxpayer various legal bases for seeking a refund of documentary taxes paid, even in those cases where it would appear that the transfer tax is owed. And in the murky area of change of control of corporations, limited liability companies and partnerships, the law is less than clear as to when a tax is owed and when it isn't. In fact, our recent calls to a number of Recorder's offices have revealed significant variations in their "interpretation" of applicable statutes and ordinances. Fortunately, the period for filing a claim for refund is much longer than that applicable to real property taxes so you may be able to recover payments many months after payment. Again, however, you must file to recover any monies.

These are just the more common examples of non-value ways to reduce taxes related to commercial real estate in California. Since each requires timely action on the part of taxpayers, many of these opportunities are lost simply because an owner is unaware of that the procedure exists or despite knowing about it, fails to appreciate the consequences of procrastination. AVS can help get you off the dime; contact us at 415-956-8090 or tbayer@advaloremsolutions.net.

All you have to lose is your money.