2012 NEWSLETTER

Law Report

BACK TO NORMAL?

by Michael J. Elliott

The recession of the last four years was born in the real estate markets. Property values plummeted forcing many properties under water and causing unprecedented numbers of short sales and foreclosures. Distressed properties have plagued the market and threaten to do so into the future.

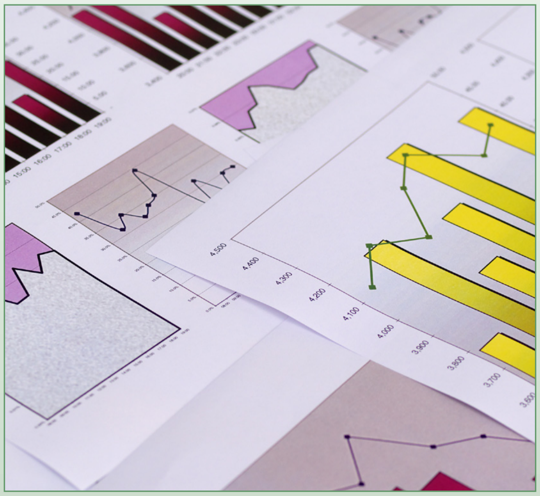
The tax assessment world has been greatly affected by these events. Over the past few years, local Assessors have reduced many (but not all) assessments to reflect declining market values; however, these reductions have mostly been too little, too late. As a result, taxpayers have filed record numbers of tax appeals seeking to reduce their assessments so they properly reflect the diminished value of their properties. Aggressive property owners have contested their assessments year after year – rather than once each triennial or quadrennial reassessment year – trying to force assessments down to catch up with falling property values.

In general, it appears property values may be leveling off; however, some markets continue to see downward (but less pronounced) pricing movement. As property values stabilize, will the tax assessment world go back to normal? And, what will normal look like? Here are our views.

Commercial Property In Cook County

Rent demand for all types of commercial real estate fell dramatically as the economy contracted. Layoffs and reduced spending by businesses and consumers resulted in greatly reduced demand for rental space of all types. This supply-demand imbalance caused vacancy rates to rise and rental rates to fall. It has become common practice for tenants to re-negotiate lease rates at renewal (or earlier) with discounts of 20% to 30%. The combination of increased vacancy and reduced rents has caused cash flows to fall dramatically. Meanwhile, capitalization rates have risen, as investors require a greater return on their real estate investments given the elevated risks of owning real estate. The combination of these factors has forced commercial property values to fall substantially.

As cash flows have plummeted, many commercial property owners have been unable to make their loan payments and commercial foreclosures have risen. We are now seeing record numbers of bank-owned properties being offered



to the market at greatly reduced prices (30% to 70% off market peak) forcing property values down across the board.

In general, the Assessor has not reduced commercial property assessments to reflect declines in market values. Until recently, there has been a shortage of current sales comparables that enable the Assessor to determine current commercial property values. This has forced taxpayers

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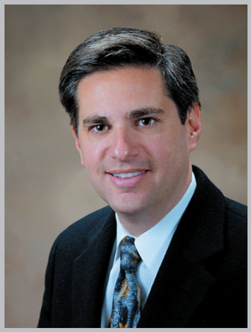

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"All taxpayers should review their assessments every year or two to see whether current conditions ... warrant filing of a new assessment appeal. This will be the new normal"

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to file appeals and prove to the assessing officials what is happening with their property and what their property is worth.

Fortunately, the Cook County Assessor and Board of Review are listening and granting substantial reductions to commercial property owners who prove their cases. If a property suffers from high vacancy or low cash flow, the assessment reduction can be substantial but often granted for one-year only (the presumption being that this condition is not permanent). As a result, taxpayers may be forced to contest each year, but the results are worth the effort. Persistence pays off.

Commercial Property In The Collar Counties

Commercial properties in the collar counties have suffered from the same negative economic forces that have impacted commercial properties in Cook. And, in many cases, collar county properties have fared worse when they are located furthest from job and transportation centers. The phrase "location, location, location" never had greater meaning than today.

In general, assessments in the collar counties have either remained constant or declined slightly from market peaks despite substantial declines in property values. As is the case in Cook, this has forced taxpayers to file appeals to pursue reductions they are entitled to.

Some Boards of Review have been open minded in understanding the plight of the commercial property owner and have awarded substantial assessment reductions when adequate evidence is provided. Lake and McHenry Counties have been particularly open-minded. Other Counties have been less co-operative forcing the taxpayer to file additional appeals to the Property Tax Appeal Board (PTAB) or the Circuit Court.

Residential Property In Cook County

Residential property values have fallen everywhere. Declines of 30% to 40% from market highs are typical. It is not unusual for a property today to be worth what it was seven to ten years ago. Short sales and foreclosures dominate the market forcing prices lower and preventing meaningful appreciation from occurring.

Some markets appear to be faring better (or worse) than others. Unique homes in the best locations where owners have been less impacted by the financial crisis (through job loss, investment losses, etc.) and where foreclosures are less common have fared better. Conversely, commodity properties in areas dominated by families with limited savings have experienced high levels of foreclosures. Properties in these areas have been among the hardest hit.

In 2009, the Cook County Assessor took the unprecedented step of reducing assessments of nearly all residential properties in the county to reflect declining property values. Subsequently, many residential properties that were triennially reassessed in 2010 (north suburbs) and 2011 (south suburbs) saw further reductions. Nevertheless, record numbers of tax appeals were filed in 2009, 2010 and 2011 as property owners fought for additional relief because property values fell faster than assessments. Taxpayers who filed appeals and proved their home was worth less than the Assessor's valuation overwhelmingly won their appeals. And, in many cases, taxpayers filed winning appeals year after year.

Residential Property In The Collar Counties

Collar county residential properties have suffered price deflation just as in Cook; however, the areas furthest from Chicago have tended to experience greater declines.

Historically, homebuyers have been attracted to the collar counties because they provided a lower-cost alternative to living in Chicago and its ring suburbs. People were willing to drive further to reduce their housing costs. But, as home prices in Chicago and its suburbs have fallen, the collar counties have lost much of their price advantage. Demand for housing in peripheral areas of the collar counties has fallen greatly. Furthermore, foreclosure rates there are high as working-class families cannot afford to keep their homes when facing a protracted job loss. This is a bad combination of events. As a result, price declines in some collar county areas have ranged from 40% to 60%.

Residential assessments in the collar counties have generally declined each of the last three years because the collar county Assessors are required to value property by evaluating sales over the past three years. This valuation method, however, tends to overvalue property in a declining market because sales two and three years ago reflect higher valuations.

Assessors and Boards of Review in some collar counties (Lake and McHenry, in particular) have been willing to reduce assessments based on current appraisals and evidence of current sales. Some have even been willing to consider short sales and foreclosures if the properties were in livable condition at time of sale. Other counties have been inflexible, insisting they are required to consider sales over the past three years, thereby forcing taxpayers to file appeals to PTAB.

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2012 ASSESSMENT SEASON HAS STARTED

The 2012 assessment season has begun. This year, all property in the City of Chicago will be re-assessed.

There are eight townships in the City of Chicago (Rogers Park, Lakeview, Lake, Hyde Park, West, Jefferson, North, and South townships). Property owners in each of these townships will receive a notice of reassessment in the mail during 2012. This notice will set forth the proposed 2012 assessment (referred to as the re-assessment). Taxpayers will have thirty days to file an assessment appeal with the Assessor's office to seek a reduction in the proposed re-assessment.

Property owners in each of the other 30 townships in Cook County will also have an opportunity to contest their assessments in 2012. If the Assessor increases the assessment of a property in a non-reassessment township, the taxpayer will receive a mailed notice of reassessment and be given thirty days to file an appeal. Taxpayers are generally re-assessed in a non-assessment year if they received a one-year assessment reduction in the prior year. One-year reductions are often granted if the property experienced above-normal vacancy or below-normal operating income. All taxpayers will have the right to appeal during the 30-day filing period for their township regardless whether their assessment has been increased or not.

The Assessor has released a schedule of anticipated filing deadlines for each of the 38 townships in Cook County. This schedule can be found on the Assessor's web-site (www.cookcountyassesor.com – click on "Appeal filing and closing dates"). The Assessor plans on releasing assessments and accepting appeals for three to four townships each month. The first filing deadlines will occur at the end of February (Riverside, River Forest and Norwood Park townships). The last filing deadlines are scheduled to occur in early November.

It will take the Assessor's office about 60 days to resolve all appeals in a given township.

After the Assessor completes his work in a given township, he will certify his books. The Cook County Board of Review will then establish its own 30-day appeal deadline for the Township. The taxpayer will then have a second opportunity to appeal its assessment with the Board of Review. The Board will decide its cases within about 60 days following its filing deadline. If the Assessor and Board maintain this schedule, the Board should complete all of its work by June 1, 2013.

The Assessor is starting this assessment season about six months earlier than in past years. He is doing this so that all appeals will be completed by late spring. This will enable the 2012 2nd installment tax bills to be mailed in late summer and be payable in early fall. This will be a great improvement over prior years when tax bills were mailed as late as November and due in December.

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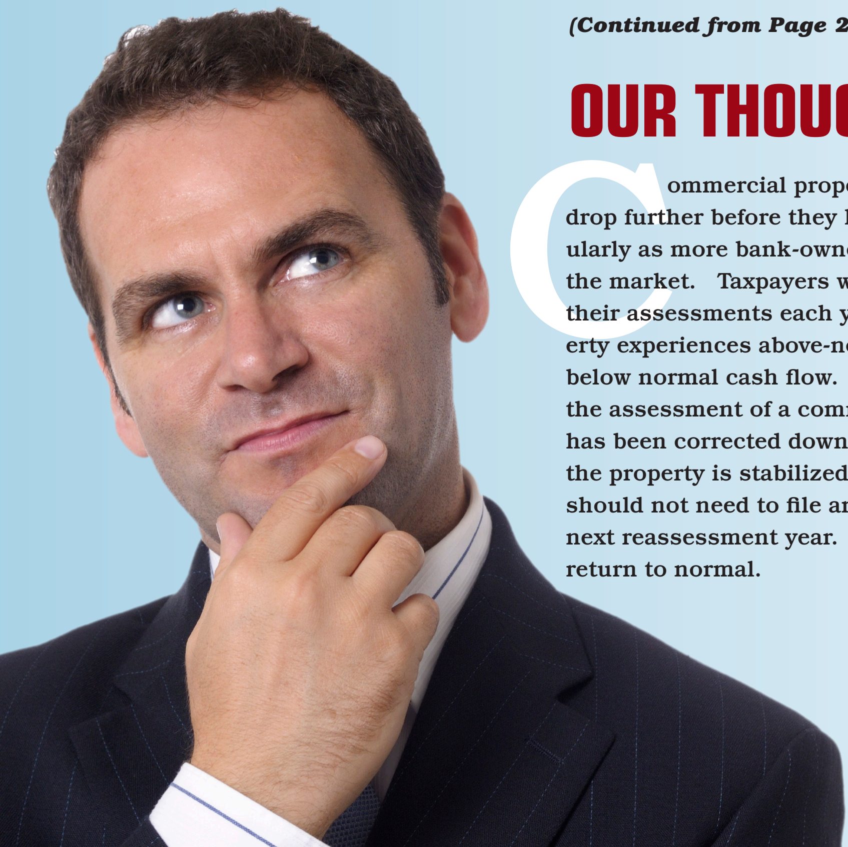

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OUR THOUGHTS

Commercial property values may drop further before they hit bottom, particularly as more bank-owned properties hit the market. Taxpayers will need to appeal their assessments each year if their property experiences above-normal vacancy or below normal cash flow. Otherwise, once the assessment of a commercial property has been corrected down to market, and the property is stabilized, the taxpayer should not need to file an appeal until the next reassessment year. This will be a return to normal.

Residential property values may be stabilizing in many areas. If the assessment of a home has been corrected down to market, an appeal should not need to be filed until the next reassessment year. This too will be a return to normal.

All taxpayers should review their assessments every year or two to see whether current conditions (high vacancy and/or reduced rents in the subject property, evidence of price declines of comparable properties, etc.) warrant filing of a new assessment appeal. This will be the new normal.