DON'T JUST ACCEPT YOUR TAX ASSESSMENT

Ensure tax bills reflect continuing value reductions for office assets caused by COVID's long-term effects.

By Cecilia Hyun

Since early 2020, the COVID-19 pandemic has upended lives and disrupted the normal course of businesses, including those in the commercial real estate market. As in many other sectors, however, this public health crisis has not affected all commercial properties equally.

Real estate occupied by essential businesses such as grocery stores, sellers of household goods and warehouse clubs, for example, have weathered the pandemic well. A few have even increased their market share. By contrast, many office buildings, hospitality and non-essential retail properties have suffered severely.

Taxing jurisdictions and assessors have responded to the crisis with varying degrees of success. The Ohio Legislature passed special legislation (spearheaded by Siegel Jennings Managing Partner Kieran Jennings) to allow a onetime, 2020 tax year valuation complaint for a valuation date of Oct. 1, 2020, since the usual tax lien date of Jan. 1 would not have shown the effects of COVID.

Other assessors applied limited reduction factors to account for the sudden pandemic-induced decrease in property values.

As values recover, it is important for taxpayers to monitor still-unfolding consequences as they review their property tax assessments.

Initially, hotels and experiential property uses suffered the steepest losses as travel declined or completely halted. While the long-term effects of COVID-19 are still emerging as the pandemic progresses, office properties may be the real estate type changed the most, and perhaps permanently so. Central business districts (CBDs) and suburban campuses or headquarters have been particularly hard hit.

Cecilia Hyun
Siegel Jennings Co.

In the last six to 12 months, many people have returned to working in an office at least part of the time, especially since vaccinations have become widely available. However, the emergence of virus variants has stalled the full return to the office that looked imminent earlier this year.

Some firms, including Twitter, Zillow, Spotify and Dropbox, decided that they will not require workers to return to the office at all, making remote working a permanent option. Other companies, including Google, Nationwide, Microsoft and Intuit, will continue with a hybrid model that requires workers to be in the office some of the time.

Many of those employers are using an office hoteling model. Hybrid arrangements require less physical office space per employee, although employers will need to balance having fewer employees onsite against the desire for low-density occupancy.

With more employees working remotely, many office tenants have subleased space they no longer need, adding to available office supply. For example, toward the end of 2020, the Chicago metro region's office market reached a record high in available sublease space, with two-thirds of it in the CBD. For employees who work in CBDs, there is an added concern of commuting via public transit.

In the initial stages of non-essential business closures and governmental stay-at-home orders across the country, many tenants sought rent abatements and concessions. Tenant defaults and increased unemployment exacerbated office vacancy levels.

Some of the workforce in more densely populated markets may have relocated away from central business districts, at least at the beginning of the pandemic, also influencing office space demand.

As acceptance of remote work increased, both employers and workers not tied to a physical office location gained employment and talent-search opportunities beyond their local markets. This, too, has influenced the demand for office space.

The Columbus area's overall office vacancy rate was more than 23 percent in the third quarter of 2021, according to Cushman & Wakefield. That vacancy figure includes more than 1 million square feet of sublease space but does not include offices leased but underutilized — or not used at all — because of employees working from home.

As these vacancy rates and overabundant sublease inventory demonstrate, there is a disconnect between the space that office tenants are currently leasing and their actual real estate needs. As leases expire, it will not be surprising to see tenants renegotiate for smaller footprints and shorter durations as they adjust to their changing requirements.

The shrinking need for office space is not limited to markets with dense populations and public transit commuters. In fact, these trends reverberate in suburban markets. Multiple large suburban office buildings in the Cleveland area, together totaling almost 2 million square feet, were 75 percent empty in the fall of 2021 because of employees working remotely.

This suggests that property tax assessments may be based on outdated lease information. Accurate valuation of office properties for taxation will require proper consideration of lease renewals and related activity. In reviewing assessments, it will be critical to scrutinize any older sale transactions assessors used for comparison that were based on pre-pandemic leases.

Positive signs are emerging for the commercial real estate market overall. *Bloomberg* recently reported that domestic U.S. travel for the year-end holidays is expected to be near pre-pandemic levels. Downtown foot traffic, hotel stays and visitor counts have been climbing back from the lows seen early in the pandemic.

Despite this good news, office properties face persistent challenges. Recently, Marcus & Millichap reported that the office sector was one of the only property types lagging in 2021 commercial real estate transaction volume compared with the same time in 2019. (The other was medical office.)

Flexibility on the part of both tenants and owners will be key in riding out the continuing waves of lease maturities and renewals in this changing market.

Since assessors are often using lagging data in their assessments, attention to the continued effects of COVID on office properties will be vital to ensuring that property tax valuations reflect a property's fair market value.

Remember, too, that various assessors are treating COVID effects differently, so as always, it is wise for property owners to consult with experts familiar with assessment law and appraisal practice in their local jurisdictions.

With careful observation of market changes, strategic planning and review with trusted tax experts, taxpayers can help ensure that their real estate tax burden is fair. ■

Cecilia Hyun is a partner with Siegel Jennings Co. LPA. The firm is the Ohio, Illinois and Western Pennsylvania member of American Property Tax Counsel (APTC), the national affiliation of property tax attorneys. Hyun is also a member of CREW Network.

Reading Precast Inc.
Manufacturer of Precast Concrete Products

Redi-Dock® Provides Instant Drive-In Access to Your Facility

- Modular
- Minimal site prep
- Low maintenance
- Delivered & set
- Easily relocated
- Lengths to 50'
- Infinite widths
- Heavy duty rating
- No future demolition
- ADA ramps available

Call: 800-724-4881
www.ReadingPrecast.com
anthony@readingprecast.com