REVERSAL OF FORTUNE – THE CITY'S HOTEL ASSESSMENTS SKYROCKET

In an apparent reversal of fortune, the Department of Finance has made an abrupt about face from the generally lower assessments of last year by dramatically ratcheting up the new 2007/08 assessments this year. This is one of the largest assessment jumps that hotels have ever seen.

The Finance Department raised the tentative assessments Citywide by an overall 35%. However the increases were even more pronounced for some of the City's premier hotels. For example, the Marriott Marquis saw an increase from $162,540,000 to $227,205,000 (an 80% change), the Grand Hyatt, from $75,105,000 to $135,405,000 and over 40% jumps at The Pierre, Sheraton Manhattan, Le Parker Meridian, Waldorf, and Roosevelt Hotels.

The outer boroughs were not spared either Brooklyn hotels saw assessments increase by 74%, Queens by 34%, Staten Island by 19% and the Bronx by only 6%.

This big tax hike is more surprising because last year hotels did not see much of a change in taxable assessed value and some hotels decreased slightly. There was speculation in some city papers that some industry leaders and consultants met with the City last year and convinced them to change the method of arriving at the assessed value for hotels. This method may have contributed to the modest assessments for the 2006/07 tax year because the Finance Department was using older 2004 calendar year income and expense figures but the changed valuation methodology that was adopted was the basis for this year's big rise.

The City's changing methodology of assessing hotels

For over 75 years hotel assessments took into consideration the fact that a hotel was both a piece of real estate and an operating business. Numerous court cases pointed out that using unallocated income and expenses for assessing hotel buildings was incorrect. The courts reminded assessors that business income could not be used to assess real estate but some method of allocation or extraction had to be employed to remove the income related to furniture fixtures and equipment, franchise and business enterprise value.

In New York City, assessors accepted this premise but chose different approaches over the years to accomplish the job. In some years they would deduct a factor for business value when using sales to value hotels. In recent years sales are not used to assess most commercial properties and income capitalization is the primary method. Hotels were assessed in various ways over the years sometimes by applying higher capitalization rates or deducting business income, or applying an expense ratio of 75% to room revenues before capitalization. All these approaches are now abandoned and a new formula is being employed.

Under the new method assessments are based on a unique valuation formula where room revenues are converted into market value. This formula, I caution, is one that is not used anywhere in the country.

The new formula

The first step is to estimate room revenue by taking the latest income and expense statement and adjusting it upwards to account for normal occupancy, alterations etc. added to this number is a percentage of food and beverage and conference and exhibit income. The total income thus derived is divided by 365 and then multiplied by 960 for luxury hotels (and a multiplier of 900 for class 3 and 4 hotels.) According to the Finance Department, this calculation provides you with the fair market value of the hotel's real estate. If there are also apartments retail, office, garage, signage /billboard, telephone or other income, the net income from these categories is then capitalized and added to the prior calculation. The entire product is multiplied by 45% to reach the assessment value.

The end result for a hotel with a room income range of $295 to $371 is that it would have a guidelines income of $475 and an estimated market value per room of $456,000 per room, an assessment of $205,200 per room, and taxes of $22,572 per room.

Nowhere in these calculations is there given any effect to the age and condition of the property, its franchise, advertising budgets or whether it is a union or nonunion operation.

If you do not think this is a fair or accurate way to value hotels in the most important hotel market in the country you are in good company. In fact the assessors union has already spoken out decrying this methodology and claiming it was a contrived deal made by a consultant and the industry leaders. The Chief reported in its May 2006 article that the assessor's union leader, David Moog, claimed the formula violated good assessing practices and was not a proper way to determine fair market value

Instead of providing tax relief to hotels it has taken an ugly turn against the hospitality industry, just gaining a foothold after the 9/11 impacts.