Condo closings aren't simple

So, You Want to Do Condominium Closings?

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You are asked to represent a purchaser of a condominium unit in a building that was recently converted into a condominium. The building was a commercial building before the sponsor purchased it for the purpose of converting it into residential use.

The building, a ministorage facility, was purchased by the sponsor on or about June 10, 1998. The sponsor rehabilitated the building for residential use and filed an offering plan with the attorney general to sell condominium units in the building. This offering plan was accepted for filing by the attorney general on Jan. 31, 2000. The closings for sales of the units did not start until sometime after May 11, 2001. Your client closed on the purchase of her unit in August 2001.

So far, nothing unusual. You agree to a standard fee of between $1,500 and $2,000 for your services. As part of your due diligence, you read the offering plan that was approved by the attorney general a year before, and a title report that you carefully scrutinized.

Everything appears in order and your client closes on the purchase of her unit. One year after the August 2001 closing, your client calls you and, in a distressed (perhaps hostile) tone, tells you that she has just been received a tax bill from the city of New York (the July 1, 2002 tax bill for 2002-'03) for her share of $338,339 in "deferred taxes." The title report made no mention of "deferred taxes." Nothing in the offering plan indicated or even hinted at such a potential liability.

'7 Vestry LLC v. N.Y.C. Dept. of Finance'

According to a recent decision of the Appellate Division, First Department, you did not do your job. *7 Vestry LLC v. New York City Dept. of Finance*, 22 AD3d 174, 800 N.Y.S.2d 398 (1st Dept. 2005), appeal denied, 2006 N.Y.App. LEXIS 596 (Ist Dept. Jan. 19, 2006).

You should have examined the July 1, 2000 bill rendered to sponsor, and have seen a notation on that bill indicating that $6,046 of that bill was noted as being for "ICIP DEFERRED." From this, you should have realized that your client would be liable for paying taxes that otherwise would have been paid by an owner of the building that was sold to the sponsor and converted from commercial to residential use. The court said that:

> The individual unit owners had constructive notice [of their future tax liability] because a prudent purchaser would have scrutinized the tax bills for the current year and years prior to the purchase date and would have seen the ICIP deferral notation in 2000 and investigated further. Each purchaser who purchased his/her unit after the July 1, 2000 tax bill took title subject to the tax lien created by the ICIP tax deferral repayment requirement, which lien is enforceable against that purchaser. Id. at 184.

You never thought, as part of your due diligence, to ask for the July 1, 2000 tax bill since the offering plan contained the total taxes for 1999-'00 and 2000-'01, and made no mention that a portion of the 2000-'01 bill was for "deferred ICIP taxes."

Further, at the closing, your title company provided a statement regarding taxes paid or owing and there was no mention of a deferred tax liability. A closing adjustment was made between the sponsor and your client that covered payment of all outstanding taxes for the current tax year.

To:

'ICIP DEFERRED'?

Even if you had examined the July 1, 2000 tax bill for the tax year 2000-'01, and seen the "notation" that $6,046 of that year's tax bill was for "ICIP DEFERRED," you would have had no idea what this meant.

Not only did the Appellate Division hold that you should have known what this meant, you should also have been alerted to the fact that the city was not just seeking $6,046 in deferred taxes from the property, but $338,339, since this was only the first of 10 installments. You should have known that your client would subsequently be responsible for her pro-rata share of these taxes (based upon her percentage of the residential common interests in the building).[1]

ICIP, as you should have known, stands for the Industrial and Commercial Incentive Program. This program is designed to encourage improvements or expansions of property being used for industrial or commercial purposes in a de-signaged "deferral area."

Under this program, an owner submits a proposal for making improvements (the proposed construction). The Department of Finance issues a preliminary certificate of eligibility for the program. After completion of the work and the filing of a "certificate of completion" the project is granted final approval for the tax benefits by the Department of Finance.

Those benefits may be tax abatements or deferrals. In the *7 Vestry* case, the benefits were that no taxes would be paid for the value of the improvements (that is, the portion of taxes for the property attributable to the increased valuation due to the improvements) for a period of seven years. For a period of three years thereafter, the owner pays the "normal taxes on the property." Id. at 176. Then, from the 11th to the 20th year after approval, the deferred (incremental) taxes are paid without interest. Id. Thus, there is no abatement of taxes, but a deferral of taxes for no less than 10 years and for as many as 20 years. This deferral is dependent upon the property remaining, throughout this 20-year deferral period, a commercial or industrial property.

The prior owner of the subject property received ICIP tax deferral benefits from 1990-'01 through 1997-'98 "based on physical improvements and a conversion of the property to a mini-storage facility." Id. at 177.

Certificate of Eligibility

The prior owner had submitted an application for a final certificate of eligibility for the tax benefits (which he received) in 1990 but it was incomplete, because it "did not include a certificate of completion or the requisite certification of the minimum required project expenditures to show that the approved physical improvement had been made." Id., at 177.

The Real Property Taxation Law (RPTL) and the Administrative Code both require that a "copy of the certificate of eligibility" be recorded by the issuing agency in the same manner as a mortgage. RPTL §489-eeee(4); Administrative Code §11-260[e].

Had this been done, it would have shown up on your title report. It seems self-evident that this recordation requirement is just for this purpose--to inform future purchasers of property that it comes with an otherwise hidden tax liability.

The city Department of Finance had developed the practice "as far back as 1987" of issuing preliminary certificates of eligibility to be followed by a final certificate "once the proposed construction project has been completed and after submission and review of an application fo a final certificate of eligibility documenting completion of the project (see 19 RCNY §14-41 [i])." Id. at 184. As indicated by the Appellate Division's citation, this practice was embodied in the Department of Finance's regulations.[2] And, based upon this practice, the Finance Department deferred taxes after the temporary certificate of eligibility was issued, as occurred in this case. RPTL 489-eeee(4) and Administrative Code §11-260[e] refer only to a "certificate of eligibility" not a preliminary or final certificate of eligibility.[3]

This practice was followed in this case even though the project had been completed in 1990, as was evident from the owner's application for a final certificate of eligibility that year. Id. at 177.[4]

In addition to the notation "ICIP DEFERRED" on the July 1, 2000 tax bill, the Appellate Division also pointed to a letter dated Feb. 5, 1999, in which the Finance Department notified the sponsor that if it did not cure its failure to file an annual ICIP certificate of continuing commercial use, it would forfeit ICIP benefits for the 1999-'00 tax year. It was given

60 days to cure. A second such notice was sent in February 2000 regarding the 2000-'01 tax year. The Appellate Division raised the possibility that the sponsor did not understand the significance of these notices for future tax liability, by stating: "Instead of responding, 7 Vestry ignored these notices, given its plan to convert the property to residential condominiums, a use incompatible with the ICIP program." Id. at 181.

In addition to these letters, the Appellate Division pointed to the fact that: "The revocation of ICIP benefits for the property was noted in the Department of Finance's public tax and assessment roles and on the various print and computer records, which are made available to the public at large." Id. at 178.

Court's Holding

Based upon these facts, the court concluded: "Thus, as the record shows, 7 Vestry proceeded with its residential condominium conversion fully alerted to the fact that the property was receiving ICIP benefits." Id. at 181.

As for the unit owners, who all purchased their units after May 2000, they, as stated above, received actual notice of their liability for deferred taxes in July 2002, when they received their bills for the 2002-'03 tax year.

The court could have limited its holding regarding your client to the principle that she was a successor in interest to the sponsor as owner of the property and, therefore, liable for the taxes imposed on the property. It noted that the unit owners, who all purchased their units after sales commenced in May 2000, received tax bills for the 2002-'03 year seeking their apportioned share of the deferred tax liability for that year. Id. at 178-79.

However, the court did not stop there, as you wish it had. It stated that, notwithstanding the fact that the offering plan and subsequent amendments made no mention of deferred tax liability, and the first taxes billed to the individual unit owners referencing the ICIP deferral reinstatement appeared in the July 1, 2002 tax bill for the 2002-'03 year: "the individual plaintiff unit owners are nonetheless chargeable with knowledge of the reinstated deferred ICIP tax benefits." Id. at 181-82.

'Chargeable With Notice'

The court cited the principle that: "A 'purchaser of land is chargeable with notice, by implication, of every fact affecting the title, which would be discovered by an examination of the deeds or other muniment of title of his vendor, and of every fact, as to which the purchaser, with reasonable prudence or diligence, ought to become acquainted.'" *Matter of Delafield 246 Corp. v. City of New York*, 11 AD3d 268, 273 (1st Dept. 2004), lv denied, 4 NY3d 703 (lst Dept. 2004), quoting *Cambridge Vall. Bank v. Delano,* 48 NY 326, 336 (1872).

What, you asked, about the fact that the title report you received at the time your client purchased her apartment in August 2001 contained no indication that there was an unrecorded tax lien upon your client's property? The Appellate Division was unsympathetc, noting that "Real property tax liens arise automatically, by operation of law, when the tax is levied against the property." *7 Vestry, 22* AD3d at 183. It added that "By law, all deferred taxes constitute tax liens against the property as of the date they are due and payable. (Administrative Code §11-264[b])." Further, "tax liens are never recorded because the tax rolls themselves are public records, accessible to all and furnishing notice to all (citation omitted)." Id.

You should also have known that your title company, for this reason, excepts tax liens from its policy.

You advise your client to join with other unit owners and the sponsor in challenging the imposition of these deferred taxes on the ground that the city should have recorded a certificate of eligibility for ICIP benefits in "the same manner as a mortgage (see RPTL 489-eee [4] § 489)." Id. at 179.5

The argument is that had the city done so, it would "have given 7 Vestry and the condominium owners notice of the ICIP deferral prior to their purchase." Id. Presumably, the sponsor (and unit owners) would have been able to get a better deal (one that offset these hidden costs).

Justice Louis York of the Supreme Court agrees with you and grants your motion for summary judgment, with one caveat. He finds that your challenge to a governmental action is properly an Article 78 Proceeding, and holds that the four-month statute of limitations for such proceedings bars your challenge to the first installment of $6,046--concluding that the July 1, 2000 tax bill for 2000-'01 put the sponsor on notice that this sum was being sought by the city. He did not address the fact that the unit owners had no notice of what was contained in this bill.

The Appellate Division reversed. It disagreed with Justice York's holding that the Department of Finance had failed to comply with the law requiring that it file a certificate of eligibility for deferred tax benefits under the ICIP program in the same manner as a mortgage.

The Appellate Division held that RPTL §489-eeee[4] and Administrative Code §11-260[e] only require recordation of a final certificate of eligibility even though this statute and regulation only refer to a "certificate of eligibility." The court, however, was not satisfied with leaving it at that, adding: "In any event, plaintiffs' knowledge of the property's ICIP benefits would render any recording requirement irrelevant." Id. at 184. 6

No Private Cause of Action

You think about telling your client to sue the sponsor for its failure to notify her of these deferred taxes in the offering plan. You then recall that there is no private cause of action under the Martin Act (General Business Law §352, et seq.), which governs disclosure requirements for condominium offerings. *The Vermeer Owners, Inc. v. Gerald Guterman et al.,* 78 N.Y.2d 1114 (1991).[7]

You will, no doubt, think twice in future about charging between $1,500 and $2,000 for a condominium closing.

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Endnotes:

1. Once an Offering Plan is declared effective (based upon purchase agreements being entered into for 15 percent or more of the offered units), the Sponsor obtains new tax lots from the City Surveyor that are allocated to each unit of the Condominium. This must be done before the Declaration is filed containing the tax lots for each unit. Only after the Declaration is filed can the sale of individual units be "closed" and title transferred. The Appellate Division decision states that the Sponsor "began to sell the individual condominium units in May 2001 [and] parent lot 21 was thereafter apportioned into individual condominium lots, effective in December 2001, in time for the new lots to appear on the 2002-'03 tax rolls. Accordingly, the next payment of reinstated deferred taxes for tax year 2002-'03 was apportioned among the individual condominium lots and billed to the unit owners." Id. at 178-79.

2. See decision of Justice York dated Oct. 3, 2003 (Index No. 121786/02) ("The Finance Department's procedure embodied in its regulations, is to issue a temporary certificate of eligibility followed by a permanent certificate of eligibility at the successful conclusion of the project").

3. The issue arises whether this practice was ultra vires, even if contained in a regulation, since this practice avoided the recording requirement of RPTL 489-eeee(4), thereby nullifying its purpose of providing notice to potential purchasers.

4. Apparently, the owner did not complete the necessary paperwork to obtain a final certificate of eligibility. As noted by the Appellate Division: "Since the prior owner submitted an application in 1990 for a final certificate of eligibility that did not include a certificate of completion or the requisite certification of the minimum required project expenditures to show that the approved physical improvement had been made, a final certificate of eligibility was not issued (see RPTL 489-ffff [4])." Id. at 177.

5. Elsewhere, the court noted that the Administrative Code (§11-260[e]) contains the same requirement. Id. at 184.

6. The Appellate Division also held that the city had a complete statute of limitations defense. [You wish that the court had limited its decision to this complete defense, instead of broadly indicting you for your lack of "reasonable" due diligence.] The Appellate Division held that the four-month statute of limitations period for an Article 78 action against the city [CPLR §217] for all of the deferred taxes ran from the July 1, 2000 tax bill. As Justice York had, the Appellate Division ignored the fact that your client had no notice of this bill, or how it caused an injury to her, since it was rendered over one year before she purchased her apartment. The same Appellate Division had said, in another decision regarding the four-month statute of limitations for an Article 78 Proceeding set forth in CPLR §217[1]), that:

> "A determination becomes 'final and binding' when the aggrieved party receives notice of the determination (Court of Appeals citations omitted)." *90-92 Wadsworth Avenue Tenants Assoc. v. City of New York Department of Housing and Community Development,* 227 A.D.2d 331, 656 N.Y.S.2d 8, 9 (1st Dept. 1997). See also, *In re Biondo v. New York State Board of Parole,* 60 N.Y.2d 832, 834 (l983)["Indeed, 'fundamental fairness would seem to compel the conclusion that a petitioner should not be held to have been dilatory in challenging a determination of which he was not aware (citation omitted).'"].

7. A distinction exists between Martin Act claims, which deal with the disclosure requirements for offerings of condominium units, and claims for breach of contract, which deal with promises made in the offering plan for future action that are not kept. See *511 West 232nd Owners Corp. v. Jennifer Realty Co.,* 98 N.Y.2d 144 (2002). Your claim fits within the disclosure requirements of the Martin Act. See *Whitehall Tenants Corp. v. Estate of Robert S. Olnick et al.,* 213 AD2d 200 (1st Dept. 1995).