Can Clean-up Costs Provide a Tax Break?
An Update on New Jersey Legal Developments

This is a copy of an article written by Archer Real Estate Tax Appeal attorneys Jeff Gordon and Alex Paul Genato, which appeared in the February 2017 issue of Chemuniqué, the newsletter for the Chemistry Council of New Jersey. Click here to learn more about Archer's Real Estate Tax Appeal Group.

A property tax assessment represents a percentage of the property's fair market value. A tax appeal, which in most circumstances must be filed by April 1 in New Jersey, represents a claim that the property is overvalued. So, when can anticipated environmental clean-up costs be used as a basis to reduce assessed value and the corresponding taxes?

At one time, taxing districts argued that environmental contamination should not be considered to reduce value because that would reward an owner for undesirable behavior. Such arguments gave no consideration to whether a current or prior owner contaminated the property or the circumstances of the event. The New Jersey Supreme Court ultimately rejected such arguments as violative of the requirement that all property be treated uniformly based on its market value. It ruled that any diminution in market value caused by environmental contamination must be considered. Inmar Assocs., Inc. v. Carlstadt, 112 N.J. 593 (1988). The Court left the method of calculating any value reduction to the Tax Court.

For years, the Tax Court provided no such method. Spurred by a Bankruptcy Court decision, the Tax Court began issuing decisions in 2004 that set forth acceptable methods. Typically, the Tax Court spreads the estimated remediation costs equally over an extended timeframe, and permits a deduction for the present value of those costs. That method may not be perfect, but it provides some reasonable relief to owners laden with significant clean-up costs. Using similar logic, the Tax Court has recognized taxing districts may raise assessed value as property is cleaned up in recognition of the improvement. Metuchen I, LLC v. Metuchen Bor., 21 N.J. Tax 283 (Tax 2004).

More recently, the Appellate Division affirmed a "flexible and pragmatic approach." It rejected the taxing district's position that a property must be valued as clean, with any deduction for remediation costs permitted only if amortized over a period of years. Rather, it found that the purchase price of a contaminated property is the best indication of its value, due to the unique issues raised by environmental conditions that would not be reflected in other, purportedly comparable properties. Orient Way Corp. v. Lyndhurst Tp., 28 N.J. Tax 272 (App. Div. 2014).

Taxing districts also periodically argue that contamination costs cannot be considered where the owner is not the primary responsible party or is indemnified by others. In such instances, they argue, the current owner can sell the property at a price reflecting its "clean" condition and should be assessed as such. The taxing districts' position appears to again plainly violate uniformity and other legal requirements. New Jersey law requires that all interests in the real estate be assessed, resulting in a fee simple valuation that ignores separate interests. "The entire bundle of rights inherent in real property is subject to assessment. Leasehold interests, life tenant and remainder

interests, co-tenant interests, mortgagor and mortgagee interests, grantor and grantee interests (where less than a full fee is conveyed), and environmental remediation obligations are not separately assessed. Instead, the full value of the fee is assessed as though there were no separate interests." J. Gordon, New Jersey Tax Handbook (2017 Ed.) at 140; see also Orient Way, supra at 8 (rejecting an approach that would ignore the effect of contamination on the property's value). Thus, any separate interests of current owners verses prior owners (or other responsible parties), the latter of which may have a negative value, should be united, so that the property is valued hypothetically as if all rights and responsibilities are with one party.

Finally, property owners should welcome more recent decisions that appear to limit the Appellate Division's decision in Pan Chemical Corporation v. Hawthorne, 404 N.J. Super. 401 (App. Div. 2009). Pan Chemical denied a deduction for contamination while the property was "in use" when a taxpayer continued a skeleton operation to intentionally avoid triggering remediation obligations. The Court seemed bothered by Pan's attempt to skirt environmental obligations while using those same obligations for tax relief. However, in a case litigated by the authors, the Tax Court rejected similar arguments by the City of Elizabeth where, while a property remained in use, the owner reported known environmental contamination and complied with clean-up obligations. Elizabethtown Gaslight Co. v. Elizabeth City, Docket No. 001115-2011 (Tax 2011). Similar results were reached more recently in ACP Partnership v. Garwood Borough, 29 N.J. Tax 102 (Tax 2016).