CRE PERSPECTIVE

Fore Thought

by Franklin Hannoch, Jr., CRE

In December 1994, the Appellate Division of the Superior Court of New Jersey affirmed an earlier opinion and judgment of the Tax Court of New Jersey regarding the value of a private member-owned country club for tax assessment purposes. The complaint was filed by the taxpayer following a municipal-wide revaluation, in which the club's real estate tax burden was increased threefold. The judgment of the Tax Court that was affirmed on appeal reduced the new assessment by approximately 45 percent, but its finding of facts sets a troubling precedent. The affirmation was based largely on case law that holds: "Findings by a trial court are ordinarily sustained on appeal when supported by adequate, substantial and credible evidence." The Appellate Court also recognized that the Tax Court is "accorded special expertise," and if dissatisfied with the proofs, can arrive at "its own opinion of true value"..."Providing it is based upon evidence in the record."

Highest And Best Use

What is troubling about this case is the finding in regard to highest and best use. Typically, for tax assessment purposes, property is valued as it is used by the owner. Here, the court held that the highest and best use was for residential subdivision into 79 one-acre lots. The judge opined that country club use was not maximally productive, and cited the text book criteria of physically possible, legally permissible, financially feasible and, as mentioned above, maximally productive.

The witness for the country club found that the highest and best use was as a public golf course, but conceded that the acreage could be divided into 79 one-acre lots at a much lower per lot value than the defendant's $500,000 to $725,000. On appeal the parties agreed that the land could accommodate 79 lots and the Appellate Court in its opinion said, "The trial judge found the highest and best use of the property was for conversion to single-family residential development, and this determination is not challenged on appeal. The parties stipulated that 79 one-acre housing sites could be developed on the property."

What country club can meet this test and retain its recreational use? To carry this view to an illogical conclusion, all country clubs should be valued for tax purposes as residential subdivisions thereby making it totally uneconomic for them to survive. The defendant's expert concluded that the land alone was worth $18,450,000, or $233,500 per raw lot. Even though the trial court found less, this is equal to an annual tax of $516,600. Assuming a 250 person membership, the annual land tax per member alone is nearly $2,100.

Open Space Benefit

The Court's view is far too short-sighted. If the subject, in existence for over 80 years, had been developed as a residential subdivision, it would diminish the value of the surrounding property that not only enjoys the open space amenity but also the opportunity to affiliate. This concept is not unlike the transference of value from anchor department stores to mall tenants in a super regional shopping center. Not only does the elimination of the club impact negatively on surrounding property, but the proposed use would tax the municipal budget for additional services and possible capital expenditures such as a new school.

Rather than tax country clubs out of existence, municipalities should zone them to preclude other than recreational use or in some other fashion acquire the development rights in order to prevent alternate use. Open space is desirable. Governments go to great expense to acquire it. Country clubs provide it free of charge.

There is another aspect to this issue that appears not to have been addressed by highly competent valuation witnesses, learned counsel, the Tax Court judge in his bench opinion or the Appellate Court in its review and affirmation. The

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country club in question covers some 184-acres, the bulk of which, including 16-1/2 holes of the course, are located in one municipality. The remaining acres are situated in an adjacent community and contain the prestigious club house, pro shop, lockers, tennis courts, swimming pool and utility buildings for course maintenance. Only the assessment on the golf course portion was challenged, because it was there that tax lightning struck due to revaluation.

If the highest and best use of the 158-acres devoted to golf course was for residential subdivision, the value or equalized assessment value of the golf course improvements in the adjoining taxing district should have been deducted from the value of the land in the so-called higher use. In other words, the parties to this litigation did not recognize that they had made a "fractional appraisal."* ("An appraisal of a unit in itself without regard to the effect of its separation from the whole," said the late Byrl N. Boyce, CRE, in *Real Estate Appraisal Terminology*.) It must be assumed that the club house, etc., are of no value if the golf course becomes a residential subdivision. For example, a one-family house on the most valuable commercial property in town is worthless when the land is put to its potential.

In the country club situation, when the land is subdivided into residential home sites, the specialized improvements have no value because the golf course they served is no longer there for the serving. You can't have it both ways, even on a hypothetical change of use. The appraiser has the option of giving no value to the improvements or deducting their worth from the land value and adding them in. In either case, the value is the same—only the allocation is different. The judge in this case, at the very least, should have deducted the full value of the improvements, even if located in another community, from his land value estimate as a subdivision, otherwise he has valued them twice.

In conclusion, it appears that when evaluating the highest and best use of a country club from the standpoint of maximal productivity, for tax assessment purposes, consideration should be given to the negative impact on surrounding property and municipal budgets in hypothetically changing the use. In this case the taxpayer had the opportunity to "take a mulligan" in an appeal to the higher court but, unfortunately, was unable to improve its lie.

**Author's Note:* The existing use of improved property ceases to become the highest and best use when the value of the land alone exceeds the value of the land and improvements combined. At this point, it becomes economic to demolish the improvements and redevelop in a higher, better and more productive legal use.

POST SCRIPT: Since this article was written, an appeal was taken to the New Jersey Supreme Court, but certification was denied. Only the 1992 case was decided and appealed without success—but, according to New Jersey law, the original reduction in assessment was binding on the municipality for two additional years based upon the Freeze Act. The community challenged the applicability of the Freeze, left the original assessment intact, and that appeal is still pending. Meanwhile, the taxpayer has appeals pending in the Tax Court for subsequent years, so there still are opportunities to get on the right course.