# Selling Mechanics

Tools for Becoming a Successful Salesperson
In the New York City Residential Market

BY NEIL J. BINDER

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ISBN 0-9679249-5-2
1. Real Estate 2. New York City 3. Business

Front cover illustration by Devis Grebu; back cover photograph by Jordan Rosenberg.

Nice Idea Publishing
352 Park Avenue South
New York, NY 10010

# Dedication

This book is dedicated to the managers of Bellmarc. They have each made a career in serving the salespeople in their respective offices, and, even more important, they have continued to search for a better way to serve our customers and clients.

Dan Berman — Midtown
Stacey Max — Downtown
Veronica Raehse — West Side
Janice Silver — East Side
Lisa Strobing — Broadway

# Acknowledgments

This book is the accumulation of the efforts of many people. Those most important are as follows:

Marc Broxmeyer, my partner at Bellmarc
Jon Felice, Esq., attorney
Alan Feldman, C.P.A., chief financial officer of Bellmarc
Janice Silver, manager of Bellmarc's East Side office
Lisa Strobing, manager of Bellmarc's Broadway office
Veronica Raehse, manager of Bellmarc's West Side office
Stacey Max, manager of Bellmarc's Downtown office

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# Introduction

Being a successful salesperson requires that you become an authority on your subject matter. You must be committed to being a professional and intimately learn the ins and outs of the business. You must make a significant investment in your future.

A substantial portion of my professional life has been dedicated to figuring out how to sell apartments in New York City. And yet I find that as the years progress, there is ever more that I don't know. I'm more confused today than I was when I began. How is this possible? I teach. I write books and articles. And then I'll go to a class and learn something that will alter my entire impression of how this business works. I'll teach a class and a student will pose a question that puts me in a new world of uncertainty. I'll read a book and say to myself, "My God, how could I be so stupid?" It is this confusion that continues to plague me.

I remember participating in a workshop years ago. I went somewhat against my will with the encouragement of my partner, Marc. There were maybe 20 people in the class and the chairs were arranged in a circle. When the teacher began I was immediately turned off to his esoteric mental gymnastics. I remember folding my arms in front of me and sighing from time to time as he spoke. Suddenly the teacher came up to me and said, "I suppose that everything is very clear to you, isn't it, Mr. Binder?" I nodded: "Yes. It is very clear. Everything is black or white. There is no gray." The teacher nodded: "Yes, and there must always be an objective." I nodded: "Yes." Then he looked at me intensely and said, "Mr. Binder, what would you do if your objective was to be confused?" I paused. I didn't have an answer. I started to lose control.



It felt as if a boulder had knocked me down. My emotional wall and my sense of logic fell apart. "What the hell is going on?" I thought.

The teacher saw that I was having a meltdown and said: "Ah, I see. Yes. Now you understand. I'm pleased that you are so clear." I wasn't clear at all. I was an emotional mess, and I didn't have a clue why. The teacher turned away to speak to others in the room, and I found myself yearning to hear every word he said. Suddenly I needed him. I wanted to learn all I could from him to understand the nature of my problem.

Many years have passed since. I have never been the same. Now I'm not clear about anything. Now I am constantly confused and searching. When I teach a class, I tell my students that my objective is to make them all confused and that the more confused they are the more satisfied I will be. They laugh, but I'm serious. I know that the more confused they are, the more they'll learn and the harder they'll search for real answers.

The odd quality about this confusion is that I am confident that it is a step forward. I know that you are wondering what I mean and that you want me to teach you only about selling and real estate. But I can't, because I don't know how. All I can do is show you how confused I am at the present time.

CHAPTER 1

# Forms of Ownership

*Understanding the product you are selling is fundamental to adequately explaining choices to the customer.*

## COOPERATIVE APARTMENTS

Cooperative apartments became popular before the turn of the 20th century. Initially, they were used by clubs and societies to create a measure of camaraderie. These clubs acquired buildings and created residences. Members would pay rent on the units they occupied; if they left the society or club, they would have to move out.

This form of cooperative ownership continued until around the Depression, when a lot of these buildings went bankrupt. Then, during and after World War II, when rent-control laws restricted the ability of landlords to obtain sufficient income from their property, cooperatives were created as a means to circumvent these laws. But coops didn't really catch on because people preferred single-family houses and moved out to suburban areas, where they were affordable.

In the 1970s, as a result of high inflation coupled with the Arab oil embargo and an economic recession, interest in coops bloomed again. Landlords, prevented from adequately increasing rents because of the city rent laws, became desperate, and cooperative conversions were a solution to their predicament.

The story behind this conversion process is an interesting one. During the 1970s and 80s, New York State permitted a landlord to convert to cooperative ownership using one of two alternatives: an eviction plan, which required that 35 percent of the tenants in occupancy subscribe to purchase their apartments, and a noneviction plan, which required that only 15 percent of the apartments be sold. Most landlords chose the eviction plan because it allowed them to evict tenants who didn't buy. Obviously these were the poorest tenants. Thus a great irony unfolded — in the city's attempt to protect poor tenants by restricting rent increases, the city stimulated the conversion to cooperative ownership, which resulted in these same tenants being forced from their homes. I am reminded of a saying by Thoreau: "There is no odor so bad as that which arises from goodness tainted.... If I knew for a certainty that a man was coming to my house with the conscious design of doing me good, I should run for my life."





A cooperative is a corporation just like any other corporation. It must seek authorization from the State of New York to do business and obtain a certificate of incorporation. Thereafter, this corporation acquires title to the apartment building from the landlord and becomes the owner. The corporation has stockholders, and they are entitled, solely as a result of their ownership of the stock, to lease a designated apartment in the building. Thus, the stock in the corporation is the homeowner's evidence of ownership, and the lease, known as a *proprietary lease*, affirms and prescribes the homeowner's right to reside in a specific apartment.

The transaction process is therefore rather simple: The landlord sets up a corporation and sells the building to the corporation at a designated price. The corporation issues shares of stock to subscribing tenants and outsiders who invest money in the corporation. The corporation transfers this money to the landlord in payment against the purchase price. To the extent that the corporation doesn't sell shares to all the apartments, the landlord takes unto himself the unsold shares as compensation for the remaining balance due under the terms of the

property purchase. In this way, all shares relating to all apartments are "issued" — some to outsiders, some to tenants and the remainder to the landlord.

Under the terms of the coop plan, an owner of shares is entitled to reside in a designated apartment and receive a proprietary lease and is thus effectively paying rent. However, given the proprietary nature of this lease, a special name has been designated for the payment, *maintenance charge*, and since the unit owner is also a tenant, he/she is often referred to as a *tenant-shareholder*. Maintenance covers the cost of operating the building as well as the allocable portion of the building's real estate tax and the debt payment associated with a mortgage placed on the building, referred to as the *underlying mortgage*.

Let me talk a little about the underlying mortgage. Since the coop corporation owns its building, it can obtain a loan secured by that building. This mortgage is recorded against the entire property, and the monthly cost of carrying this loan is shared by all the homeowners through their monthly maintenance payments. Therefore, in acquiring a cooperative apartment, the purchaser essentially pays for two loans: the loan on the purchase of the shares of stock and the loan associated with a portion of the underlying building mortgage.

In most localities outside of New York, when a cooperative apartment is being sold, the broker will recite the price by first stating the share price and then the underlying-mortgage allocation. In cases in which a cooperative apartment owner is entitled to take depreciation because the apartment is used for business, she is entitled to use this full price for determining the depreciation deduction. Interest on both loans is normally tax deductible.

Let me give an example: Say a building has an underlying mortgage of $1 million and there are 100 apartments, each having an equal share allocation. The underlying mortgage associated with each apartment would be $10,000. If an apartment is sold for $250,000, this is the price for the transfer of the shares and lease. But the full price of the





apartment, including the underlying-mortgage allocation, is $260,000.

The real estate tax on a coop follows the same form as the interest deduction on the underlying mortgage. The taxes are paid in full by the cooperative corporation, with each owner paying his allocable share through his monthly maintenance payment.

Since a buyer is purchasing shares of stock in a corporation, he is not really buying real estate, and there is no deed associated with the transfer. Thus, the owner is not technically obtaining a mortgage but what is known as a *financing*. This is done by filing a *U.C.C.-1* form in the New York County Clerk's office against the name of the owner for the amount of the claim, which has as collateral the shares of stock in the cooperative corporation and the proprietary lease. The buyer gives an assignment of his shares of stock and his proprietary lease to the bank, and then the bank gives the buyer the money. (Brokers in the ordinary course of business are somewhat casual with this terminology and regularly refer to a coop loan as a mortgage even though it isn't one.)

Section 216 of the Internal Revenue Code permits deductibility of interest and real estate taxes on a cooperative apartment as if it were a single-family home. New York State also allows this deduction. However, there are federal and state laws that the cooperative corporation must also conform to so its shareholders can take this tax deduction. First, there can be only one class of stock. This means that all shareholders have the same rights. No apartment owner can have preferences or privileges not available to other owners except for the right to occupy a distinct apartment and vote his allocated shares. Second, the apartments must be for dwelling purposes only, though the regulations have created certain exceptions, such as professional apartments that qualify because they are dwellable. Third, the cooperative cannot distribute money out of its earnings and profits to shareholders. And fourth, no more than 20 percent of the income from the building can come from sources other than the tenant-shareholders, such as commercial rents, health-club charges and interest income.

Obviously, this last limitation can create problems for a cooperative, particularly if there is a lot of rent from ground-floor stores. As a result, the concept of a *condop* was born. A condop is a building that has been partitioned into condominium units in which one unit is owned by a cooperative corporation. For example, a landlord owns a building with considerable retail rent. He decides to convert his building to unit ownership and does so by creating a condominium consisting of two unit deeds. One deed relates to the ground-floor stores, and the second deed relates to the apartments on the upper floors. He then creates a cooperative corporation and transfers the condominium deed relating to the apartments into that entity. The cooperative corporation accordingly owns the unit deed to a portion of the building rather than to the entire building. Each year, the tenant-shareholders receive two financial reports: one relating to the economic affairs of the cooperative corporation and the other relating to the economic affairs of the condominium. (There is another definition frequently provided by real estate brokers for the term condop: when a cooperative corporation has no board-approval requirement, brokers have labeled this type of building a condop, the theory being that it is a hybrid since it is owned as a cooperative but has no board approval on a transfer of ownership like a condominium.)

There are, of course, advantages and disadvantages to ownership of a cooperative apartment. One advantage is tax deductibility of the interest and real estate taxes associated with owning a primary residence. A second advantage is derived from the approval process on the purchase of an apartment, which is performed by an elected group of shareholders who form the board of directors of the coop. The board normally meets on a monthly basis to go over building affairs, among them approving sales of apartments. The board will usually request an array of information, including financial data, tax returns, personal reference letters and documents supporting the financial position of the buyer. Generally, the buyer will also be required to submit to an interview. If the documentation is acceptable and the interview is favorable, the board will approve the purchase. Only upon this approval can the seller transfer ownership.





Let me explain why the approval process is a favorable aspect of ownership. I used to live in a cooperative building consisting of 45 apartments. I had two young children, and we pretty much knew everyone in our building — it was a little community. The people who lived there looked at their apartments as their homes. When I grew up, I lived in a house. My friends were pretty much the same from the time I was young until I left to go to college. I've spoken to many other people who recall a similar experience — the sense of constancy in their environment when they grew up. A coop seeks to create this same sense of continuity and community. If a rock star known for living a rather unconventional lifestyle wanted to purchase in the building, chances are high that he wouldn't get in. He isn't the type of person my building wanted living there. If someone wanted to purchase the apartment as an investment and to rent it, he also wouldn't have been approved. The building wanted permanence, not transience. The approval process aims to provide a sense of security and to encourage a sense of community in a building.

Another positive feature of cooperatives is the vast selection of them. In Manhattan, coops constitute approximately 75 percent of the owned housing stock. In some areas, like the West Side and Greenwich Village, this figure is much higher, while in other areas, like the East Side and Midtown, it's lower. Most prewar buildings are coops, while most newly constructed buildings are condos. In order to explore the largest number of choices, a buyer would be well advised to include coops because of their prevalence — the greater the choices, the greater the opportunity.

Let me talk about the disadvantages of coop ownership. The board-approval process can be undesirable to some buyers, particularly those with limited financial resources, since most coops have more rigorous

financial requirements than condominiums do. In most instances, a condominium buyer can obtain a mortgage without any limitation on the amount, and the buyer doesn't have to prove any income beyond that required by the bank to get the loan. It is rare to be able to purchase a cooperative with a loan exceeding 75 percent of the purchase price, and many premier buildings set a limit as low as 50 percent. Indeed, some coops prohibit loans secured by the apartment entirely, so the buyer must use all cash.

In addition, investors would find coops unappealing because they normally do not permit, or severely restrict, the right to rent.

Another disadvantage is the cost of borrowing money for the purchase. Interest rates for coop loans are generally about one-half percent higher than those charged for condos.

## CONDOMINIUMS

Condominiums were developed later than coops, stimulated by an act of Congress that permitted this form of ownership to receive tax benefits and mortgage financing. The trend was born in Florida and California in the 1970s and later spread to New York City. During the 1980s, interest rates were volatile, and banks, in an effort to protect themselves from rate fluctuations, were hesitant to offer long-term mortgages to coops. When developers sought construction loans for new residential properties, they were unable to get financing from banks. By building condominiums, the developer would have to finance only the construction period and then this loan would then be paid off as individual buyers obtained mortgages to purchase their units. In addition, banks were happy to grant condominium mortgages because the mortgages could be readily sold on Wall Street and were thus viewed as short-term investments. Furthermore, because condominium apartments could be bought without board approval and weren't prohibited from being rented out, investor activity expanded the market.





Real estate is defined as land and anything permanently affixed thereto. The ownership of land pertains not merely to the ground surface. It also includes a theoretical slice of the earth running down to its core and the air space rising above; thus, a unit deed can be issued to an apartment occupying that air space. In addition to the condominium-unit deed there is a master deed, which covers the entire building and sets forth the rights and obligations of each unit owner as well as the association's rules. In a cooperative, these rights of occupancy and the building rules are found in the apartment's propriety lease and the corporation's bylaws. A mortgage on a condominium apartment is similar to a mortgage for a house. In both cases, it is a claim on the property associated with a *unit deed*, which is recorded against the property in the County Clerk's office.

Since a condominium apartment is real estate, the real estate taxes are not paid by a cooperative corporation but are paid directly by the unit owner to the city. There is also a monthly *common charge*, to cover the cost of building operations, but normally none of this charge is tax deductible because it isn't applied to interest expense or real estate tax. This monthly charge is spelled out in the master deed and unit deed and consists of a percentage unit interest of the whole. Therefore, assuming all apartments are identical, if there are 100, the unit interest for each would be 1 percent, and each owner would have a monthly common charge covering 1 percent of the cost of running the building.

In a condominium there is a *housing association*. This association also elects an association board of trustees, which has officers who are responsible for overseeing the affairs of the condominium. Those portions of the building not within the confines of a specific apartment are referred to as the *common elements*, and the housing association oversees them on behalf of all the owners.

A condominium costs more than a similar cooperative because the common charge, which doesn't include a debt payment on an underlying mortgage, is lower. In order to evaluate a similar coop and condo,

an upward adjustment must be made to the condo to reflect this difference. In addition, because the interest rate on a condominium mortgage is usually lower by about one-half percent, a buyer of a condominium can borrow more to purchase an apartment and have the same monthly debt payment as he would have if he purchased a cooperative apartment. Because there are no real estate taxes in the condominium common charge, brokers normally describe the monthly cost of owning a condo as consisting of two components — the monthly common charge and the monthly real estate taxes — while a cooperative apartment entails only the monthly maintenance.

In addition to these two factors, there are also two intangible elements that affect condominium price. The first is the perceived ease of sale. Buyers generally believe that there is no or only a minimal approval process. While this is often true, more and more condominiums are demanding extensive information about the buyer, including her financial condition, as a prerequisite for getting the condominium to sign a waiver of the condominium's *right of first refusal*. This right of first refusal, which is stipulated in the master deed and unit deed, allows the association to refuse a buyer under the proviso that if it does so the condominium association will buy the unit under the same terms and conditions expressed in the buyer's contract. In practice, the right of first refusal has become a powerful tool for stonewalling transactions with undesirable purchasers. The common strategy used by condominium associations is to make repeated demands on the buyer for more and more information as a condition to signing the waiver. The buyer becomes more and more frustrated and eventually recognizes what's going on — the transaction falls by the weight of the association's intransigence and its refusal to sign the waiver. With the right of first refusal as their negotiating device, many condominiums now require purchasers to present documentation similar to that required by a cooperative. Nevertheless, a substantial portion of condominium buildings, particularly newly constructed ones, have no restrictions,





and the general perception that a condominium transaction is much easier is still valid.

The other element that augments the value of condos is investors. Their participation adds to demand and thus stimulates higher prices.

The result of all these distinctions is that condominium apartments under $1.5 million tend to have a price premium of about one-third when compared with a cooperative. Thus, a cooperative apartment fairly priced at $1 million would compare to a condominium priced at $1.3 million. This premium drops to about 15 percent for higher-priced apartments because they are less attractive to investors. In addition, the value of the interest-rate discount on a mortgage becomes less meaningful since buyers of higher-priced apartments do not generally ask for mortgages over $1.1 million, which is the maximum amount that is tax deductible.

Another important feature of a condominium is its higher transaction costs. At the end of the first chapter in my book *The Ultimate Guide to Buying and Selling Coops and Condos*, I list the closing costs for the buyer and seller for both a cooperative and a condominium apartment. In reviewing these figures, you will notice that the cost of recording a mortgage and deed in a condominium as well as the title insurance is considerable. None of these costs exist for a cooperative.

Let me discuss the concept of *lien risk*, which can best be understood by an example of two similar situations with two very different outcomes. In the early 1990s, a builder put up two buildings of similar size with 350 units each — one was called the CitySpire, located on 56th Street in Midtown Manhattan, and the other was called the Boulevard, located at 86th Street and Broadway on Manhattan's West Side. CitySpire was built as a condominium, the Boulevard as a cooperative. The developer had financial difficulties, and two banks took over the unsold apartments. For CitySpire, the bank was the Bank of Nova Scotia; for the Boulevard, the bank was Citibank. Immediately after taking control of the apartments in CitySpire, the Bank of Nova Sco-

tia ceased paying the common charges. Citibank, however, continued to make the monthly maintenance payments to the Boulevard. Each bank had control of approximately 100 apartments. The litigation generated by these buildings continued for approximately two years. During this time, desperate for the money necessary to operate the building, CitySpire's condominium association levied a special assessment against the remaining 250 condominium-unit owners equal to about 50 percent of their monthly common charges. No special assessment was ever levied in the Boulevard. After approximately two years, the final foreclosure of the condominium units in CitySpire occurred. An auction was held, and the Bank of Nova Scotia pocketed all the resulting money. No money was ever paid back to the condominium association so it could reimburse homeowners for the special assessment, let alone for the unpaid common charges on the foreclosed units. In the case of the Boulevard, once the foreclosure was finalized, Citibank sold all the cooperative units to an investor free and clear of any claims for unpaid maintenance.

In the case of CitySpire, the bank held a lien on each of the condominium units. This lien had legal priority over the claim of the condominium association. Therefore, the Bank of Nova Scotia was entitled to any moneys forthcoming and had a right to be fully satisfied before the condominium was.

In the case of the Boulevard, Citibank had a claim to the stock. The proprietary lease for each cooperative apartment was merely associated with the stock. If Citibank failed to make the monthly maintenance payments, the cooperative corporation had a right, under the proprietary lease, to institute eviction proceedings for nonpayment of rent. Thus, to protect its position, Citibank was required to continue to remain in good standing with its monthly obligation.

Governmental authorities were aghast. The fact that condominium owners were placed at such a terrible disadvantage when there was a delinquency in receiving monthly common charges from one or more





unit owners was considered an injustice that needed to be rectified by legislation. The proposed legislation gave condominiums a priority over lending institutions for six months of common charges. The banks' response was that if this change in the law were made, they would incur greater "lien risk" and would charge every condominium purchaser a higher interest rate to compensate for that risk. The proposed legislation was tabled and never discussed again.

In summary, a bank charges less for a condominium loan than for a cooperative loan because there is less risk of losing its money.

## STRATEGIES FOR DEALING WITH COOPERATIVES AND CONDOMINIUMS

The best selling strategy for a salesperson is to present a buyer with the broadest array of ownership choices. However, there are times when a condominium is the best option. This would be the case given the following circumstances:

- The buyer has limited cash and cannot afford to put 25 percent down and have what the board deems a comfortable level of liquidity after the closing.
- The buyer is an investor seeking property to rent.
- The buyer absolutely refuses to disclose any financial information whatsoever. (But many condominiums do require this information under their right of first refusal.)
- The buyer has a high level of debt from other sources.
- The buyer's yearly income is unstable because of commissions or job changes.
- The buyer has a bad credit history or criminal record.
- The buyer does not intend to use the apartment as a primary residence.

Difficulties often arise with buyers who have significant income and wealth from foreign sources but limited resources in the United States

and are thus unable to adequately prove their net worth to the cooperative. It is recommended that a certified public accountant provide a financial report to the cooperative certifying the financial condition of the purchaser. In addition, it is preferable for the buyer to maintain bank balances with a bank that has a reputation in this country. But regardless of how closely the foreign buyer adheres to these stipulations, some coops will still recognize only U.S. assets and income.

Another challenge is the purchaser who doesn't meet the cooperative's stringent financial requirements. In some instances, the cooperative will permit another party to guarantee the obligation of the purchaser. This is common in the case of parents guaranteeing the obligation of a child. However, in many buildings a guarantee is unacceptable, and the only way this situation can be resolved is for the party giving the guarantee to jointly purchase the apartment with the proposed occupant.

There are cases in which a hesitant board is satisfied when the buyer deposits an additional sum of money into a cooperative's bank account for a defined length of time as additional security. The amount can be as much as two years' maintenance and the period of time as long as five years. If the buyer proves responsible in making monthly payments for the designated period, he can then request the return of these funds, and the board can elect to either return the money or hold it for an additional length of time. While this solution is often proposed by the coop board, sometimes an alert salesperson can make a deal by suggesting it to the parties.

## TENANCY IN COMMON

Tenancy in common is not a common form of ownership in New York City. It exists when a group of people acquire a property and agree to share all the benefits and obligations of ownership. Toward this purpose, they sign a tenancy-in-common agreement allocating a specific





area or apartment to each participant as well as a portion of the ongoing costs. It is usually very informal and normally requires broad participation of all the owners in the care of the property. This leads to one disadvantage of a tenancy in common, which is that everyone must be involved. There is also a tendency not to have professional management. There is very limited marketability for these kinds of property, and often when one owner wants to sell, the entire property must be sold to achieve maximum value. It is also impossible to get a mortgage on one unit through a tenancy in common — only a mortgage on the entire building is normally obtainable, which all the tenants in common must individually sign.

## TOWNHOUSES (SINGLE-FAMILY HOUSES)

Obviously one advantage of a townhouse is the amount of space and control the owner has over the property. There is also greater privacy. Many people consider townhouses to be the ultimate prestige property, and they frequently sell at considerable premiums. The disadvantages are security and the owner's direct responsibility for the maintenance and repair of the property. And townhouses don't offer grand city views.

Obtaining a mortgage on a townhouse is based on equity percentage down and monthly housing cost. Monthly housing cost is determined by the real estate tax and insurance. A good rule of thumb for insurance is to use 1 percent of the selling price. So insurance on a $3 million property should be about $3,000 per year.

In considering real estate taxes, the City of New York identifies four classes of property. Class 1 includes one-, two- and three-family homes and condominiums in small buildings that are not more than three stories. The assessed value is determined at 15 percent of the value of the property multiplied by the yearly tax rate for this class. Class 2 consists of all other coops and condominiums. The value of the building as a

whole is multiplied by 45 percent in order to determine the assessed value, and this amount is multiplied by the applicable yearly tax rate. Classes 3 and 4 are basically utilities and commercial properties.

The tax assessment on a Class 1 single-family house is levied at no more than 6 percent of its value. In addition, the assessment cannot increase by more than 6 percent a year and no more than 20 percent in any five-year period.

Let me offer an example to describe how this works. Mr. Jones owns a townhouse that he bought 30 years ago. His taxes are $24,000 per year. He sells the property for $5 million. Under city law, the assessment is 15 percent of $5 million, which is $750,000. When the assessed value is multiplied by the tax rate of 15 percent, it computes to $112,500. (The rate changes year to year, and this is an approximation.) However, since this is an increase that exceeds 6 percent per annum, the new tax is limited to $25,440, which is 6 percent more than the previous year's. Each succeeding year, the rate can increase by 6 percent, but in the fourth and fifth years the rate cannot go up more than 2 percent because the accumulated increase in the prior three years was 18 percent and the law restricts the increase to no more than 20 percent in any five-year period.

In a condominium and cooperative, the real estate tax is determined for the entire building by reference to the tax assessment in comparable multiple-dwelling properties. Accordingly, the price of each apartment sale is not relevant in determining the tax paid by the owner. The assessor applies the Class 2 levy, which provides that the assessment value is 45 percent of the full value.

Here's an example of how this works. Mr. Smith lives in a 2,000-square-foot condominium. He sells it for $2 million, which is $1,000 per square foot. Each year the city assessor evaluates building sales in the area and determines that for the current year the market rate is $500 per square foot. The building Mr. Smith lives in has 300,000 square feet, so the value is $150 million, and the assessment value is





45 percent of this, or $67.5 million. The tax rate for Class 2 property is 12 percent (this is approximate), which means that the yearly tax for the entire building is $8.1 million. Mr. Smith's unit interest is 1 percent, so his yearly tax charge is $8,100. The assessment can go up based on comparable building sales, and the buyer of Mr. Smith's condo will have a yearly change in his tax charge to reflect the change in value.

In new construction, the general method for determining the tax assessment is 45 percent of the qualifying construction costs of the building. This has resulted in enormous tax burdens for new buildings when compared with older properties, whose assessment is a function of comparable sales of similar multiple-dwelling properties. The city has sought to ameliorate this enormous cost somewhat through certain tax-abatement programs that phase in the tax burden over a period of years, but after that limited period the taxes can be especially heavy when determined on a square-foot basis.

## RENTALS

Obviously, since there is no ownership in a rental, there are no tax advantages or future profit advantages. However, there is also no requirement for equity beyond the investment in a security deposit. This offers the tenant considerable flexibility in moving and greater liquidity. Generally in a rental apartment, a landlord's responsibility is more pervasive. In a cooperative or condominium, if the refrigerator breaks, the apartment owner is responsible for fixing or replacing it. In a rental, the landlord is responsible. The landlord also has to paint the apartment and maintain the interior in good condition. A tenant is less inclined to invest in remodeling a rental and even if he does, many landlords won't permit it.

In recent years, apartment rentals have become more abundant in Manhattan and are now an important aspect of the selling strategy for many customers. When evaluating rental properties, a salesperson

should generally use a multiple of 40 times the monthly rent as the qualifying income for a prospective tenant. It is customary for commissions to be paid by the tenant, though in many newly constructed buildings the landlord will offer compensation to brokers.

## QUESTIONS AND ANSWERS

***Mr. Velasquez is a foreigner. He is interested in purchasing property in New York City to be used as a home for his family, and he will also conduct business in the apartment when he is in this country. You are his broker. What are Mr. Velasquez's choices, and which choice do you recommend?***

The fact that Mr. Velasquez is a foreigner means that he may have a problem getting a mortgage. It also means that he may have more trouble being approved by a coop board, assuming that he has limited U.S. income. The broker should seek to ascertain whether Velasquez will need a loan and should direct him to a mortgage broker to prequalify. To the extent that he has income or verifiable assets that are not based in the United States, he should get an accountant's letter. If he is going to obtain a mortgage from a foreign bank, it should be a known financial institution.

Conducting casual business is not a problem in a cooperative or condominium apartment as long as it is not a violation of zoning laws. The broker should find out what type of business will be run from the apartment. The buyer will have a problem with many coops if the apartment is not intended to be his primary residence.

Assuming that casual business is not an issue, I would recommend a condominium unless the buyer has significant income and assets in the United States. If he does, then I would suggest either a cooperative with less-stringent admission requirements or a condominium.

***You receive a call from a tenant in a building that is converting to cooperative ownership. He is thinking about how he might be able to profit from this situation. What are you going to tell him?***

The tenant can attempt to assign his right to buy. The tenant can do this by either making a deal with an investor who will buy the rights and then subsequently resell the apartment to a third party — a procedure known as *flipping* — or by seeking a buyer-user directly with the assistance of a broker.

An investor is safer because the agreement normally requires that the investor make the assignment payment at the time of signing the contract, which is placed in escrow with the tenant's attorney. However, if a buyer-user can be found who is comfortable entering into an unconventional transaction, the likelihood of profitability is higher since there is no middleman. Obviously, the most ideal strategy for the tenant in occupancy is to acquire the apartment himself, own it for two years and then sell it. This would permit him to enjoy all the gain and considerable tax benefits on the sale.

***You are the exclusive agent for the owner in a coop. He gives you two financial statements for the building. What does this mean?***

The building is a condop. One financial statement relates to the condominium, consisting of a residential unit and commercial unit(s), and the second financial statement is for the cooperative corporation, which owns the unit deed on the residential units. From a practical matter there is very little effect on the homeowner other than that costs of operating the building are shared between the condo units.

***You have a buyer who doesn't understand why there is a mortgage on the building in a coop he is considering. He also notices that there is an item titled "land-lease payment" on the financial statement. He asks, "What's going on — does the coop rent this building or have a mortgage on it?" What do you have to say?***

The building can have a mortgage since it has only one deed in the name

of the cooperative corporation. If there is also a land lease, it means that the lease is subject to a mortgage. This permits the coop to place a mortgage on the building even though the coop doesn't own the land.

***Horace Jones earns $50,000 a year. He has $25,000 in cash and is looking to buy a cooperative apartment. What do you recommend?***
Mr. Jones does not have enough income and cash to comfortably purchase an apartment. He should rent unless he can obtain a significant increase in investment cash and possibly a guarantor.

***What is lien risk?***
In a condominium, the bank has superior claim over the condominium association. If the unit owner fails to pay his common charge, the condominium may find that even though it has a valid claim it will be unable to collect the funds it is owed if the bank has also not been paid. This is because a foreclosure often yields less money than is necessary to pay all secured creditors, and the bank must be paid before the condo's claim is satisfied.