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Tax Certificates

County auctions provide greater reward, greater risk

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Real estate investor Tom Dixon last year bought \$46,000 worth of tax certificates backed by seven townhouses, single-family homes and office condos in Miami-Dade.

Steven Gara plans to invest about \$2,000 this year. He resells the tax certificates on eBay, the online auction site, for returns in the triple digits.

Each year when a property owner fails to pay property tax by an April 1 deadline, they are deemed delinquent. In order for the county to collect on its property tax bills, it auctions the delinquent property taxes in the form of tax certificates.

Bidders — which can be any individual or entity — agree to pay the tax and then competitively bid on the interest that should be attached to the tax amount paid. Bidding starts at 18 percent, and the lowest bidder wins the certificate.

The annual interest rate ranges from 18 percent to zero or to a flat 5 percent rate for the life of the tax certificate, whichever is greater. Certificates are valid for seven years.

At some point, the property owner must pay the investor the full tax amount plus interest accrued.

Or the certificate owner may force a tax deed sale of the property after owning the certificate for two years.

In a tax deed sale, the property is auctioned off and the investor is paid off. Tax liens have seniority over lenders and other creditors. The owner of the property receives whatever is left of the sale proceeds.

High return

This could be the second year in a row of strong returns, likely exceeding certificates of deposit and most stock indexes.

Last year, the average annual interest rate on tax certificates in Miami-Dade County was 6.96 percent, up from 0.31 and 0.30 in 2007 and 2006, respectively.

In Palm Beach County, the annual rate jumped to 7.8 percent in 2008, up from 0.74 in 2007 and 0.84 in 2006.

The interest rate depends on how much it costs an investor to borrow money to buy the certificates and how quickly a property owner redeems a tax certificate, Miami-Dade County Tax Collector Fernando Casamayor said.

“Based on both factors, I would assume the interest rate will probably go up [this year],” he said. “The cost of money has gone up a little bit, and I think [property owners] have decided to take a little bit more time to pay off the certificates.”

Historical return rates for Broward County tax certificates were not available.

With unemployment on the rise, an increasing number of homeowners have defaulted on property taxes.

Tax certificates can be a great investment, but investors are required to do a lot of research and understand the process well to be successful, investors and county officials warn.

Over the last 10 years, institutional investors and their agents have done most of the buying.

“Unless you clearly understand what you are doing, please, do not invest your life savings in these tax certificates,” said Anne Gannon, Palm Beach County’s tax collector.

Her office is advertising 38,162 tax certificates this year, up from almost 28,000 a year ago.

Certificate owners can apply for a tax deed sale between the third and the seventh years. The longer the investor waits to apply for a tax deed sale, the riskier the investment becomes. That’s because the condition of the property might have deteriorated and lost value over the years, said real estate investor Jeannette Verster in Hialeah.

“It is good to start the tax lien sale process as soon as possible,” she said. “If you wait for seven years, and it is a bad property, you lose all your money.”

Before the housing market crashed, investor Gara said he would pay \$150 to \$200 for tax certificates. He’d then sell them on eBay and other online auction sites for between \$1,500 and \$2,000.

Today, he gets about \$600 for similar transactions, said Gara, president of SGBizServices but the market is starting to heat back up again.

“Tax certificates themselves aren’t worth as much because they are tied to the relative value of the house,” said Gara, who also buys certificates from counties in Arizona and Colorado. This picture is brightening though as the economy recovers.

Higher rates, higher risks

The sharply lower value of South Florida real estate is causing some investors to reconsider how much risk they are willing to take.

Politano is one of them. He used to buy certificates for Merrill Lynch and still manages the portfolio now owned by Bank of America, which acquired the giant Wall Street firm in September 2008.

Last year, he bought \$66 million worth of tax certificates in Miami-Dade alone, according to the county tax collector’s office.

Florida law is designed to make it harder for homeowners to lose their primary home.

If a homesteaded property doesn’t sell at auction, the investor has the option to buy it for 50 percent of the assessed value or put it on the county’s list of properties to sell for the value of the delinquent taxes. If the house doesn’t sell in three years, the county takes title to the property, and the investor doesn’t get paid.

“We had properties that we allowed to go to the List of Land for Taxes,” Marks said, referring to the county’s list. “Clearly, they had a lot of equity in them, but not as much as half of the assessed value plus the outstanding taxes,” she said. “It was more than what they were worth. Throwing good money after bad money is not a good business practice.”

Earlier this year, Politano unsuccessfully tried to get legislators to change the law so that homesteaded and non-homesteaded properties are treated the same.

Politano will try to get the law changed again next year, he said, but he may face an uphill battle.

“I don’t see that happening,” said Liggett, with the National Tax Lien Association. “Politically, it won’t be a very popular thing for any legislator to go about making it easier to take someone’s homestead.”