Federal Appellate Court Ruling May Substantially Extend Deadlines For Challenging Local Tax Assessments

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Local governments are dependent for their operating funds on the taxes they collect. In turn, that collection depends on the apportionment of the required lump-sum revenue among the various taxpayers in the taxing jurisdiction. As a practical matter, municipalities—and most taxpayers—generally would seem to prefer that decisions on how to allocate the tax burden be promptly decided and that challenges, if any, be quickly resolved. For one thing, if taxpayers were permitted to defer their challenges for lengthy periods of time, local governments could find their fiscal planning subjected to a significant risk of being retroactively disrupted.

A recent decision by the US Court of Appeals for the Second Circuit, in *Cloverleaf Realty of New York, Inc. v. Town of Wawayanda,*[1] suggests that a prompt and final resolution of local taxing disputes may now be significantly more difficult to accomplish. In the *Cloverleaf* case, the Second Circuit rejected the contention of a county government in upstate New York that the four-month Article 78 statute of limitations barred a taxpayer's federal court challenge to tax assessments that had been approved years earlier. This federal appellate court decision may have the effect of throwing local government budgets into extreme disarray.

THE NEW YORK RULE

The *Cloverleaf* case was decided nearly three decades after a leading ruling on a similar issue was handed down by New York State's highest court, the New York Court of Appeals. The 1980 decision, *Press v. County of Monroe,*[2] involved plaintiffs who were the owners of property improved with garden apartments, known as "Poplar Gardens Apartments," located in Monroe County, New York, within the boundaries of the Gates-Chili-Ogden Sewer District.

The facts underlying the *Press* decision are as follows. Pursuant to the requirements of Section 271 of the New York County Law, on August 16, 1972, the administrative board of the sewer district adopted a proposed amended rate schedule for 1973 that imposed a flat dollar charge per unit on structures containing one, two, or three dwelling units. The proposed amended rate schedule classified apartment, duplex, and townhouse complexes (which included any structure or series of structures located within a single lot or tax account number containing four or more dwelling units) differently. For these types of apartment complexes, the proposed amended rate schedule counted an efficiency apartment (*i.e.*, a studio or one bedroom apartment) as one-half a unit, a two-bedroom apartment as three-quarters of a unit, and a three-bedroom apartment as one unit. The sewer assessments then were computed by taking the number of units assigned to the apartment complexes using this formula and multiplying that unit count by the flat dollar charge. However, any apartment complex that consumed a total of

more than 60,000 gallons of water per unit per fiscal year would be charged on the basis of water actually consumed. In that situation, the number of units would be determined by dividing the actual gallons of water consumed by 60,000, and that number would then be multiplied by the flat dollar rate to get the sewer assessment.

In determining the 1973 sewer assessment for the Poplar Gardens Apartments, the sewer board converted the 135 garden apartments to 113 "units" based on the mix of efficiency, two bedroom and three bedroom apartments located within the complex. That unit number was then multiplied by the flat dollar rate for that year, producing a proposed sewer assessment of $11,092 for 1973. The sewer district assessment roll containing the figure for the complex was filed with the Monroe County Legislature on September 6, 1972. After a public hearing on September 30, 1972, the assessment roll was affirmed and adopted by the Monroe County Legislature on October 11, 1972.

Two years later, in 1974, the sewer district's administrative board, employing the same rate schedule with a revised flat dollar charge, prepared the assessment roll for 1975. For this assessment, the sewer district determined that the water consumption at the Poplar Gardens Apartments complex exceeded the critical 60,000 gallon figure. As a result, the assessment proposed by the sewer district was based on the 9.6 million gallons of water consumed at the complex, rather than on the previously-calculated 113 "unit" formula. Under this scenario, the sewer district assigned 160 "units" to the complex, resulting in a tax levy of $20,001. The 1975 assessment roll with this figure was filed with the Monroe County Legislature on September 12, 1974, and, after a public hearing, was affirmed and adopted by it on October 22, 1974.

In 1975, when the sewer district prepared the assessment roll for 1976, the assessment for the Poplar Gardens Apartments complex again was based on the amount of water actually consumed, this time 8.38 million gallons. This usage was divided by 60,000 to arrive at 140 "units" assigned to the complex and amounted to a tax levy of $17,501. The 1976 assessment roll was filed with the Monroe County Legislature on September 16, 1975, which, after a public hearing on October 4, 1975, affirmed and approved the roll as filed.

On June 28, 1978—nearly six years after the Monroe County Legislature had approved the 1973 assessment roll, nearly four years after it had approved the 1975 assessment roll, and nearly three years after it had approved the 1976 assessment roll—the plaintiffs, the owners of the Poplar Gardens Apartments complex, brought an action in state court seeking a declaration that the 1973, 1975, and 1976 assessment rolls were void by reason of the unconstitutionality of the underlying rate schedule. In particular, the owners argued that the tax schedule impermissibly treated apartment complexes differently from other types of dwelling units located within the sewer district. The defendants moved to dismiss the complaint on the ground that the action was barred by the four-month statute of limitations.

The trial court denied the motion to dismiss and ordered an immediate trial on the issue of whether the rate classification system was unconstitutional. The intermediate appellate court reversed the trial court's ruling and dismissed the action on the ground that it was not commenced within the applicable statute of limitations—four months—after the adoption of the assessment rolls for the three years in question. The case then reached New York's highest court, the Court of Appeals.

In its decision, affirming the decision of the appellate court, the Court of Appeals explained that the appeal turned on identifying the correct statute of limitations applicable to the declaratory judgment action. It decided that the four-month statute of limitations contained in § 217 of the Civil Procedure Laws and Rules, (CPLR), was the governing statute of limitations, and it accordingly concluded that the action had been properly dismissed as time-barred.

As the Court of Appeals explained, the parties' controversy could and should more properly have been resolved in a proceeding known as an "Article 78" proceeding. This is the judicial vehicle typically used to challenge final decisions of local and state governments in New York. The Court of Appeals determined that the owners of the complex could and should have commenced an Article 78 proceeding to challenge the assessment adopted each year by the Monroe County Legislature when it approved the assessment roll of the sewer district for each particular year. In the majority opinion, the Court of Appeals further reasoned that despite the fact that the decision to approve the assessment was done by a county legislature, it was not a "legislative" act.[3] The Court of Appeals explained that a legislative act is an enactment of a local law. The assessments, the Court of Appeals noted, were approved each year via resolution, not by enactment of a local law. The Court of Appeals found that in approving the assessments each year, the Monroe County Legislature enacted no statutory provision and took no action that would have had any carry-over effect beyond

the particular assessment year.[4] The Court of Appeals further decided that whether the action of the county legislature in this situation was viewed as administrative, quasi-administrative or otherwise, judicial review could properly have been sought and obtained via an Article 78 proceeding. That being the case, inasmuch as an Article 78 proceeding, with its four-month statute of limitations, challenging the 1973, 1975 and 1976 assessments was time-barred in June 1978 when the plaintiffs commenced their declaratory judgment action, that declaratory judgment action, too, was time-barred.

THE CLOVERLEAF CASE

For nearly the past 30 years, the law in New York with respect to the timing of challenges to local tax assessments seemed settled by the *Press* case. The Second Circuit's decision in *Cloverleaf*, however, has threatened to upset the rules by which local governments in New York—and New York taxpayers—have operated for all of these decades.

The *Cloverleaf* case was brought by plaintiffs Cloverleaf Realty of New York, Inc., and Sunrise Park Realty (collectively "Cloverleaf"), which owned two parcels of land in the upstate New York town of Wawayanda. In 2005, the town prepared a tentative special assessment roll to fund improvements to the water and sewer district that included the Cloverleaf parcels. Following a public hearing, the town approved the tentative assessment roll. The town then transmitted the assessment roll to Orange County, which levied the taxes against the property owners within the district. As a result, Cloverleaf received tax bills from the county totaling $38,642.01.[5] Cloverleaf timely paid the full amount of the taxes, but did so under protest.

In 2006, Cloverleaf brought a declaratory judgment action against the town and the county in a New York state court. That complaint sought to invalidate the assessments on two grounds. First, Cloverleaf argued that New York law required the assessments to be made on a "benefit basis," where taxes would be based on the proportional share of the benefit each property in the district would receive from the improvements. Cloverleaf contended that the assessment roll was in fact enacted on an *ad valorem* basis, meaning that taxes were based on the assessed value of the properties, a violation of the "benefit basis" requirement. Second, Cloverleaf argued that procedural due process required providing actual notice of the public hearing by mail, and that the town's posting of a notice in a newspaper advertisement was insufficient. The trial court found that the four-month statute of limitations contained in § 217 of the CPLR applied to Cloverleaf's claims, and it dismissed the complaint as untimely.

Cloverleaf subsequently brought a civil rights action in a federal district court in New York pursuant to 42 U.S.C. § 1983, again alleging that the failure to provide notice by mail violated the Fourteenth Amendment's right to due process. Although this claim was essentially identical to one of the claims asserted in the previously dismissed state court action, Cloverleaf sought to take advantage of the longer statute of limitations applied by federal courts to § 1983 actions against New York state officials.[6] The federal district court dismissed the action on the pleadings, concluding that the federal court claim was precluded by the earlier state court dismissal. The district court then granted a motion by Cloverleaf to reconsider the dismissal, but ultimately adhered to its initial order. Cloverleaf appealed.

In its opinion, the federal appellate court reversed the dismissal and reinstated the action. The Second Circuit explained that the "difficulty in this case" arose from the circumstance that Cloverleaf's procedural due process claim was untimely under the law applied by the New York courts, but timely under the law applied by the federal courts. It acknowledged that federal courts "must give to a state-court judgment the same preclusive effect as would be given that judgment under the law of the State in which the judgment was rendered."[7] Moreover, the Second Circuit recognized that the federal district court had based its decision on its conclusion that under New York state law, a dismissal on statute of limitations grounds was treated as a judgment "on the merits," and that the claim, therefore, could not be re-litigated in another forum. However, Cloverleaf argued that the federal district court's analysis was wrong and that a claim that was dismissed solely for lack of timeliness does not bar a subsequent claim brought in another state or jurisdiction. The Second Circuit agreed with Cloverleaf.

The Second Circuit pointed out that the US Supreme Court has recognized that, "the traditional rule is that expiration of the applicable statute of limitations merely bars the remedy and does not extinguish the substantive right, so that dismissal on that ground does not have claim preclusive effect in other jurisdictions with longer, unexpired limitations periods."[8] Stated differently, the federal appellate court continued, unless a state's claim-preclusion law departed from the traditional rule and treated a dismissal on statute of limitations grounds as a ruling on the merits of the

claim, courts in another jurisdiction need not give claim-preclusive effect to that dismissal. It then reasoned that a federal court, exercising its federal question jurisdiction, was plainly a jurisdiction separate from that of the State of New York. Thus, it continued, the remaining question was whether New York's claim-preclusion law departed from the traditional rule, and instead treated a dismissal for lack of timeliness as extinguishing both the right and the remedy.

The Second Circuit concluded that New York law did not depart from the traditional rule. It quoted from the New York Court of Appeals decision in *Tanges v. Heidelberg N. Am., Inc.*,[9] to the effect that, "The expiration of the time period prescribed in a Statute of Limitations does not extinguish the underlying right, but merely bars the remedy."[10] According to the Second Circuit, the dismissal of Cloverleaf's procedural due process claim for lack of timeliness was not on the merits and merely barred its ability to obtain relief in the state courts of New York; the "underlying right" remained intact, and a remedy remained available in the federal courts.

The Second Circuit then referenced a nearly 30-year-old decision by the New York Court of Appeals, *Smith v. Russell Sage College*,[11] where the New York Court of Appeals affirmed the dismissal of an employment discrimination claim on claim-preclusion grounds, observing that a prior dismissal of the same claim on both statute of limitations and statute of frauds grounds was "sufficiently close to the merits for claim preclusion purposes to bar a second action." The Second Circuit conceded that it had in the past read *Russell Sage* as establishing that under New York law, a dismissal for lack of timeliness was a judgment "on the merits" that destroyed both the right and the remedy.[12]

However, the Second Circuit continued, in light of what it stated was the New York Court of Appeals' more recent statement of New York state law in *Tanges*, the Second Circuit's reading of *Russell Sage* was "no longer appropriate given the earlier case's ambiguity." The Second Circuit said that, first, the initial dismissal in *Russell Sage* was not merely on statute of limitations grounds, but also on statute of frauds grounds. The Second Circuit said that the New York Court of Appeals appeared "to have concluded that the two grounds *taken together* lead to a conclusion that the prior dismissal was 'sufficiently close to the merits' to give it claim-preclusive effect." The Second Circuit stated that it did not read this as a statement that a dismissal for lack of timeliness was, standing alone, a judgment "on the merits."

Second, the Second Circuit noted that in *Russell Sage*, "the motion to dismiss the first action was treated as one for summary judgment on which the court considered submissions of the parties" outside the pleadings, making claim preclusion "especially" appropriate in the eyes of the New York Court of Appeals. The Second Circuit stated that that was "not true" in *Cloverleaf*.

Third, the Second Circuit also noted that the court in *Russell Sage* was not confronted by the situation it faced in *Cloverleaf*: a dismissal for lack of timeliness by a court in another jurisdiction with a shorter statute of limitations. Because the *Russell Sage* decision did not confront the question of whether a claim originally dismissed as time-barred should be precluded when later reasserted in another jurisdiction with a longer statute of limitations, it should not be understood as having settled that question, the Second Circuit declared.

Accordingly, the Second Circuit concluded that dismissal of a claim solely for lack of timeliness in a New York state court did not preclude the same claim from being brought in another jurisdiction with a longer statute of limitations, including a federal court exercising its federal question jurisdiction. The Second Circuit then vacated the district court's order dismissing Cloverleaf's suit, and remanded the matter for further proceedings consistent with its opinion. Although this decision did not find that Cloverleaf was correct that the assessments were unconstitutionally enacted, it now has the opportunity to prove that in federal court.

CONCLUSION

The Second Circuit decision in *Cloverleaf* discusses a number of court cases, including opinions by New York State's highest court, and a variety of legal principles in reaching its conclusion. Interestingly, the *Cloverleaf* opinion did not even mention the *Press* decision that directly dealt with tax assessments and applicable statute of limitations. It also chose to ignore the very significant New York State public policy of settling tax assessments quickly—permitting challenges only within four months—for the benefit of both local governments and other taxpayers. That the plaintiffs in *Cloverleaf* brought a federal claim that was "essentially identical" to their state court action that had been dismissed on statute of limitations grounds, only serves to highlight the practical problems with the Second Circuit's ruling.

In several recent cases, the Second Circuit has certified questions to the New York Court of Appeals for its perspective. It is not clear why the Second Circuit chose

not to do so in this case, but rather chose to essentially undermine well-established New York law on the time frames applicable to property tax assessments challenges and challenges to similar types of municipal decisions. The *Cloverleaf* ruling may create significant problems for local and state governments. Decisions of these entities may no longer be protected by the short statute of limitations applicable under state law if they are challengeable under the much longer statute of limitations applicable to federal claims. The ultimate life and impact of this decision remain to be seen.

NOTES

1. 572 F.3d 93 (2d Cir. 2009).
2. 50 N.Y.2d 695 (1980).
3. Had the Court of Appeals found that it was a "legislative" act, an Article 78 proceeding would be an inappropriate vehicle to challenge the assessments.
4. The dissenting opinion, while agreeing with the need for finality in these situations to assure the orderly administration of government, hotly disagreed with the majority's finding that this was not a legislative act. 50 N.Y.2d at 704-706.
5. Cloverleaf Realty of New York, Inc. was billed $28,574.39, and Sunrise Park Realty was billed $10,067.62.
6. *See, e.g., Owens v. Okure*, 488 US 235, 251 (1989) (holding that New York's three-year statute of limitations for general personal injury actions is applicable to § 1983 actions filed in federal courts in New York); *see also Jaghory v. New York State Dep't of Educ.*, 131 F.3d 326, 331 (2d Cir. 1997) (observing that "the statute of limitations for a claim under § 1983 that accrued in New York is three years"); *Meyer v. Frank*, 550 F.2d 726, 728 (2d Cir. 1977) ([T]he three year New York statute of limitations governs [plaintiff's] instant § 1983 claim.); *Romer v. Leary*, 425 F.2d 186, 187 (2d Cir. 1970) (It is now settled...that in a suit seeking declaratory and injunctive relief which is based on [§ 1983], the applicable limitation in a case arising in New York is the three year limitation....).
7. *Migra v. Warren City School Dist. Bd. of Educ.*, 465 U.S. 75, 81 (1983).
8. *Semtek Int'l Inc. v. Lockheed Martin Corp.*, 531 U.S. 497, 504 (2001).
9. 93 N.Y.2d 48 (1999).
10. *Id.* at 55.
11. 54 N.Y.2d 185 (1981).
12. *See EFCO Corp. v. U.W. Marx, Inc.*, 124 F.3d 394, 397 (2d Cir. 1997); *Bray v. N.Y. Life Ins.*, 851 F.2d 60, 64 (2d Cir. 1988).