Commercial Real Estate Tax Escalations

Tenant shall pay its proportionate share of any real estate tax increases over a base year.

The New York City Department of Finance taxes every commercial building annually. The tax bill is paid by the landlord, but in most office leases, the landlord passes through a portion of that bill to the tenants. Specifically, the tenants pay their proportionate share of any tax increase above their base year tax bill.

The following sections break down three key terms: proportionate share, real estate tax increases, and base year, and close with how to project the tax pass-through expense over the lease term.

PROPORTIONATE SHARE

Proportionate share is the tenant's square footage divided by the building's total square footage. A tenant occupying 5,000 SF in a 100,000 SF building has a 5% proportionate share.

EXAMPLE · PROPORTIONATE SHARE

Tenant Rentable Square Footage ÷ Building Rentable Square Footage = Proportionate Share

REAL ESTATE TAX INCREASES

The real estate tax increase is the difference between the building's current-year tax bill and the base year tax bill. If the base year bill is $1,000,000 and the current-year bill is $1,050,000, the increase is $50,000. The tenant pays no portion of the base year amount, only its proportionate share of the increase above the base year bill.

EXAMPLE · TAX INCREASE CALCULATION

Tenant’s tax charge: 5% x $50,000 = $2,500

DETERMINING THE BASE YEAR

The base year sets the benchmark tax amount from which future increases are measured. If the building's real estate taxes rise above that amount, the tenant is responsible for its proportionate share of the increase.

The base year will be defined in the lease as either a fiscal year (FY) or a calendar year (CY).

A FY base year aligns directly with the NYC tax cycle which runs from July 1 through June 30, while a CY base year blends the second half of one fiscal year with the first half of the next.

CY2026, for example, consists of January through June 2026 from FY2026 and July through December 2026 from FY2027.

CY base years often work best for leases commencing in the first half of the year, while FY base years align more cleanly for leases commencing in the second half. A lease commencing in July 2026, for example, would align with FY2027.

EXAMPLE · BASE YEAR BY 2026 COMMENCEMENT WINDOW

January – June	CY2026
July – December	FY2027

PROJECTING FUTURE TAX INCREASES

Tax escalations are based on future tax bills that haven't been issued; precise tax projections over the life of a lease are impossible. To give tenants a sense of how tax increases may accumulate, two common approaches include applying a fixed annual increase — 3% is a common assumption — or calculating the property's compound annual growth rate (CAGR) using actual published tax bills from the NYC Department of Finance.

EXAMPLE · CAGR FORMULA

(FY2026 Bill ÷ FY2016 Bill)^(1/10) – 1 = 10-Year CAGR

The 10-year tax escalation model below provides a sample analysis of a tenant occupying 5,000 rentable square feet in a 100,000-square-foot building, based on a fixed 3% annual tax escalation assumption.

10-YEAR TAX ESCALATION MODEL · ILLUSTRATIVE

TENANT SF	BUILDING SF	PRO-RATA SHARE	BASE YEAR TAX	ESTIMATE
5,000 SF	100,000 SF	5.00%	$1,000,000	3.00%

LEASE YEAR	BUILDING TAX	INCREASE OVER BASE	ANNUAL CHARGE	PER SF
YEAR 1	$1,030,000	$30,000	Abated	Abated
YEAR 2	$1,060,900	$60,900	$3,045	$0.61
YEAR 3	$1,092,727	$92,727	$4,636	$0.93
YEAR 4	$1,125,509	$125,509	$6,275	$1.26
YEAR 5	$1,159,274	$159,274	$7,964	$1.59
YEAR 6	$1,194,052	$194,052	$9,703	$1.94
YEAR 7	$1,229,874	$229,874	$11,494	$2.30
YEAR 8	$1,266,770	$266,770	$13,339	$2.67
YEAR 9	$1,304,773	$304,773	$15,239	$3.05
YEAR 10	$1,343,916	$343,916	$17,196	$3.44
TOTAL · YEARS 2–10			$88,891	$17.78