Pratt Center for Community Development

Testimony on Reform of the 421-a Property Tax Exemption Program
to the New York City Council Housing & Buildings Committee
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Support Comprehensive, Citywide Reform (Intros. 490 & 487)
to Create Affordable Housing and Save Taxpayer Dollars

Chairman Dilan, members of the Housing & Buildings Committee, thank you for the opportunity to testify. I want to begin by thanking the Committee, Speaker Christine Quinn, and the Bloomberg Administration for your hard work on this important topic. We have come to collectively recognize that 421-a property tax exemption program – which made sense when it was created in the 1970s – has become a deeply misguided, tax giveaway of hundreds of millions of dollars primarily for luxury housing. We all agree that profound reform is necessary – but not easy – and I have deep appreciation and respect for the work of the Committee, the Speaker, and the Administration to make this reform happen.

At the same time, I believe that the changes proposed by Speaker Quinn and Mayor Bloomberg – while a substantial improvement on the status-quo – do not go nearly far enough toward comprehensive reform to create affordable housing and make the best use of taxpayer dollars.

The starting point here is simple: Developers and owners of market-rate housing – like the rest of New Yorkers – should pay their taxes. If they want a tax break, they need to provide the public benefit of creating affordable housing.

Intro 490, sponsored by Councilmember Palma (and Intro 487, sponsored by Councilmember Gerson) is built on this basic point. Anywhere in the city, developers seeking a tax break would have to include 30% affordable housing, on-site, and commit to keep it permanently affordable. Otherwise, they are still welcome to build – they would just have to pay taxes like the rest of us.

Still Too Big a Giveaway (approximately $100 million each year)
In 2006, the City gave up more than $400 million of revenue through the 421-a program, for all of the buildings granted exemptions over the past years. Perhaps more significantly, the City authorized $963 million (in lifetime, net present value terms) of tax breaks for newly built buildings that came onto the market in 2006.

Of this nearly $1 billion, much went to buildings containing affordable housing (through the 20-year exemption for 80/20 buildings in Manhattan, or the 25-year benefit for affordable housing elsewhere in the city). But approximately $422 million went for newly-built buildings that contain not one single unit of affordable housing (calculations and assumptions are attached).

The proposal by Speaker Quinn and Mayor Bloomberg would help to correct this problem. However, we estimate that the City would still be giving out approximately $100 million each year (in lifetime, net present value) of tax breaks for market-rate new developments outside the exclusion zone that do not contain any affordable housing.

Councilmember Palma's bill would correct this $100 million annual mistake. Instead of a $100 million tax giveaway for market-rate housing in upper Manhattan and the outer boroughs, we would either get on-site affordable housing, or we would collect the tax revenue (which can then be used to build affordable housing elsewhere).

Still Subsidizing Luxury Development in Every Borough
This $100 annual million mistake is not simply a dollar figure. It is high-end buildings, in every borough, that receive large tax breaks, even though they are priced far out-of-reach of the vast majority of residents in their neighborhoods.

The Pratt Center recently released a report identifying high-end condos in neighborhoods in all five boroughs that would continue to receive generous tax subsidies (of up to $107,000 per unit in lifetime benefits) even under the compromise proposal to reform the 421-a program supported by the Speaker and the Mayor.

This report highlights 54 condo buildings (samples below) that would still be eligible for 421-a tax relief, even if they would have been built after the proposed reforms. These buildings contain more than 6,100 high-priced condominiums, far beyond the reach of the average New Yorker.

Not one unit is priced for less than $350,000, most are above $600,000, and some exceed $2 million. They are located in every borough, in neighborhoods including Riverdale, Flushing, Long Island City, Brighton Beach, East Harlem, Washington Heights, and Roosevelt Island. Even with the new limits proposed on the benefits, the estimated lifetime tax breaks on these buildings – post-reform – would be over $500 million.

Citywide Reform Will Not Significantly Dampen Development
Opponents of citywide reform have argued that eliminating the as-of-right, 15-year benefit for market-rate construction in the outer boroughs will harm development. But I believe this is a mistaken argument for a number of reasons:

- The 421-a benefit is a relatively small factor relative to other much more important factors, like the housing market, the cost of construction, and interest rates.
- HPD projects that having 421-a benefits enables a developer to charge about $30,000 - $40,000 more for a condo. In the vast majority of places around the city, developers would still develop even if they had to sell the unit for $30,000 - $40,000 less.
- NYC is facing an affordable housing shortage, not a market-rate housing shortage. The vacancy rate for low & moderate income units is under 3%. For higher income units, the vacancy rate is nearly 10%.
- Market-rate units do not "trickle down" to make things easier for working families. The housing market overall is so tight that even with the highest rates of market-rate production in years, there is no impact on more moderately-priced units.
- Therefore, even if there are a few units somewhere that need the 421-a benefit to take place, it is not worth the many market-rate units that are receiving large tax breaks.

We need to use tax incentives to create affordable housing, not market-rate housing. We can have both – but since developers will continue to build market-rate housing because it is profitable, we need to use tax breaks for affordable housing only.

If the Council is truly concerned about making room for moderate- and middle-income housing units, there are a range of options. We have in the past explored a "tiered affordability model," which would allow developers to receive 421-a benefits for providing affordable units on a sliding scale – from 30% of the units at or below 50% of the area median income, up to 100% of the units affordable to families earning 120% of the area median income. This model would enable developers to receive tax benefits for creating permanently affordable housing for moderate and middle income families.

More & deeper is reasonable
Especially with the kind of tiered approach outlined above, it is entirely reasonable to seek more and deeper affordable units from this program – especially in strong-market areas.

Councilmember Gerson has an especially good idea in this regard. In those areas where developers are eligible to receive <u>both</u> 421-a tax benefits <u>and</u> an inclusionary zoning density bonus, they should have to do more than just the minimum to get only one of those. This was the general rule in Manhattan prior to the Hudson Yards Rezoning – developers had to include 27% affordable units to get both benefits.

These are very large benefits, especially in Manhattan. The value of the tax break, per affordable unit, of the 20-year exemption in Manhattan is $119, 598 per market-rate unit, or more than $475,000 per affordable unit. And the value of inclusionary zoning is significant as well, allowing a 33% density bonus where land is worth $200 per square foot. With these substantial benefits, it is perfectly feasible for developers to include more affordable housing.

In addition, these requirements could be easily aligned with HDC's Mixed Income Program which provides financing for developments that are 50% market, 30% middle-income, 20% low-income.

Commit More Money to the Affordable Housing Trust Fund
I am pleased that the Speaker and the Mayor have agreed on the wisdom of creating an Affordable Housing Trust Fund, capitalized by anticipated savings from the 421-a reforms being proposed. However, the $400 million figure that has been proposed is far too small.

I concur with the analysis by Housing First!, which found that these reforms would lead to about $1.5 billion (lifetime value, in net present value) from the development of new buildings in the next 10 years – and that at least $1 billion must be committed to affordable housing.

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For all these reasons, I enthusiastically support Intro. 490 by Councilmember Palma (to insure that developers seeking tax breaks citywide include 30% affordable housing, on-site, and permanent), and also Intro. 487 by Councilmember Gerson (to require developers receiving both 421-a and inclusionary zoning benefits include 35% affordable housing).

With these reforms, the City Council can shift the 421-a program from a hundreds-of-millions dollar giveaway for luxury housing to a program that truly creates affordable housing and makes wise use of taxpayer dollars.

Thank you very much for this opportunity to testify, and for your work on this important issue.

<u>**Calculations and Assumptions for 421-a Calculations**</u>

Data on newly-granted 421-a tax exemptions granted in FY2006, based on data from the NYC Department of Finance and the Office of Management and Budget, is as follows:

Tax Expenditure for Newly Granted 421-a Exemptions in FY2006					
		For 1 year only		**Lifetime NPV**	
	Units	**Total**	**Per Unit**	**Total**	**Per Unit**
		(in millions)		**(in millions)**	
10 yr	2,614	$38.1m	$14,578	$273.9 m	$104,709
20 yr	3,957	$43.0 m	$10,854	$473.3 m	$119,598
15 yr	2,015	$8.5 m	$4,234	$80.2 m	$39,810
25 yr	3,007	$11.1 m	$3,698	$135.9 m	$45,107
Total	11,593	$100.7m	$8,687	$963.0 m	$83,071
Source: NYC DOF and OMB					

We have made the following assumptions about how these benefits might be shifted by reform:

- The 20 and 25 year benefits would go exclusively for affordable housing.
- The 10 year benefits would be eliminated.
- Half of the buildings granted a 15-year exemption are likely in areas that would be covered by the newly-revised exclusion zone, so would not get an as-of-right benefit. Half are likely to be outside that area, so they would still get a benefit.
- Of the buildings granted 25 year benefits, half likely included affordable housing, and half were likely in NPP/REMIC areas where they received the 25-year benefit as-of-right.

Comprehensive 421-a Reform
Create Affordable Housing & Save Taxpayer Dollars
Frequently Asked Questions

Councilmember Annabel Palma has introduced legislation that would comprehensively reform the NYC 421-a property tax exemption program to create affordable housing and save taxpayer dollars. Comprehensive reform means:

- Citywide affordability requirements
- 30% of the units affordable to households earning up to 50% of AMI
- On-site affordable units (i.e. no "certificates")
- Permanent affordability

Speaker Quinn (with the support of Bloomberg Administration) has proposed more modest changes:

- Affordability requirements only in Manhattan (below 135th Street on west side, 116th Street on east side); parts downtown, brownstone, and norther Brooklyn, and parts of the Brooklyn/Queens waterfront.
- Market-rate-only developments would continue to receive large tax subsidies in Upper Manhattan, the vast majority of Brooklyn and Queens, and all of the Bronx and Staten Island.
- 20% of the units affordable to households earning up to 80% of AMI
- On-site affordable units (i.e. no "certificates")
- 20-year affordability

Frequently Asked Questions

Don't we need all the housing development we can possibly get? Don't we have a housing shortage? Isn't the city going to grow by 1 million more people? Shouldn't we provide tax subsidies for market-rate housing to make sure we build all we can?

- NYC is facing an affordable housing shortage, not a market-rate housing shortage. The vacancy rate for low & moderate income units is under 3%. For upper income units – the kind of units being produced by market-rate new construction, the vacancy rate is nearly 10%.
- Market-rate units do not "trickle down" to make things easier for working families. The housing market overall is so tight that even with the highest rates of market-rate production in years, there is no impact on more moderately-priced units.
- From 2002 – 2005, with the highest market-rate housing production in years, NYC lost more than 150,000 affordable units. Market-rate construction is not helping to create affordable housing.
- The 1 million new New Yorkers in the decades to come will be working-class immigrants, not yuppies and millionaires.
- We need to use tax incentives to create affordable housing, not market-rate housing. We can have both – but since developers will continue to build market-rate housing because it is profitable, we need to use tax breaks for affordable housing only.

Won't citywide affordability requirements stop development?

- No. Developers in the vast majority of cases will still build without the tax incentives.
- The 421-a benefit is a relatively small factor relative to other much more important factors, like the housing market, the cost of construction, and interest rates.
- HPD projects that having 421-a benefits enables a developer to charge about $30,000 - $40,000 more for a condo. But is the vast majority of places around the city, developers would still develop even if they had to sell the unit for $30,000 - $40,000 less.

Aren't the neighborhoods proposed for coverage in the Mayor's bill the only neighborhoods where market-rate development will cross-subsidize affordable housing?

- No. According to HPD's own financial analysis, there are another 15 neighborhoods (beyond those proposed for coverage in the Mayor's bill) where applying affordability requirements would not prevent development.
- There are many more neighborhoods where the housing market is very strong –Bed-Stuy, Bushwick, Brighton Beach, Astoria, Long Island City, Sunnyside, Woodside, Jackson Heights, Flushing, Forest Hills, East Harlem, Washington Heights/Inwood, Riverdale, etc.

What about neighborhoods where not much market-rate housing is taking place?

- If market-rate housing is not happening already, changes to the 421-a program are not going to make much difference.
- The City could use some of the several billion dollars generated through 421-a reform to subsidize and therefore jump-start mixed-income/affordable development in these areas.
- The vast majority of residents in these neighborhoods are working-class and low-income families. They want to see housing they can afford, not housing that is far beyond their reach.

Doesn't the cap on "assessed value" solve the problem by putting a cap on benefits?

- No. The assessed value cap still allows luxury units to receive very large benefits (without including any affordable units).
- At an "assessed value" cap of $65,000, units outside the exclusion zone, would all still be eligible for a tax price, no matter how high the sales price, worth up to $107,000 lifetime.
- In addition, "assessed value" is not a meaningful predictor of the value of a unit. Data suggests that assess value of new construction is all over the map.

Is 30% affordability too much? Isn't the standard an "80/20?"

- 80/20 has been the standard for many years. In today's hot housing market, market-rate housing development can support more affordable units.
- Councilmember Gerson has proposed a creative solution in Intro. 487, which would require that developers who receive BOTH 421-a benefits and inclusionary zoning have to create at least 35% affordable housing on-site.
- Where necessary, the City could use some of the money generated by 421-a reform to provide subsidies in individual cases where developers were willing to include affordable housing but could demonstrate that the subsidy is necessary for affordable units.

Since the tax break is only for 20 years, doesn't the affordability have to be limited to 20 years?

- No, since this program is voluntary, developers who want a tax break could be required to commit that the affordable units would be affordable in perpetuity.
- With so much affordable housing being lost, we need mechanisms to guarantee that the affordable housing we are subsidizing today stays affordable into the future.
- Most developers only consider the first 20 years of profitability in deciding whether or not to do a deal. Letting affordable units go to market-rate after 20 years creates a windfall for the owners, but not one that is necessary to finance and develop the building.
- We have suggested changes in Albany tha would allow developers to continue to receive an ongoing tax exemption on the affordable units in perpetuity as well, so they could more easily keep these units affordable.

Isn't the "certificates" program an entrepreneurial & efficient way to create affordable units?

- No, the "negotiable certificates" program is one of the most inefficient affordable housing programs every created. Instead of paying $1 in taxes, a market-rate developer can give an affordable housing developer just 15 cents.
- The large majority of all of the certificates have been bought from just one development company (Atlantic Development Group). This is a sign of an inefficient market.

Won't we lose the money that has been going to certificates for affordable housing?

- No, not if the City & State work together to dedicate the new tax revenue that the City will receive for affordable housing to the City's Affordable Housing Trust Fund.

How much of the new revenue should be committed to affordable housing?

- We believe that at least $1 billion should be committed to affordable housing.
- We estimate the "net present value" (in today's dollars) of the new revenue that the City will received as a result reform being proposed is $1.5 billion on development that will take place in the next 10 years.
- We therefore call for a one-time transfer of assets of at least $1 billion (50% of a conservative estimate of the value of the new revenue).

Doesn't the Bronx lose out if certificates are eliminated?

- No, a portion of the Affordable Housing Trust Fund could be targeted to Bronx neighborhoods where developers now use certificates.
- This would enable more developers – not-for-profit, neighborhood-based, and reputable private affordable housing developers – to participate in helping promote affordable housing in Bronx neighborhoods.

Isn't the legislation proposed by Speaker Quinn (and supported by the Bloomberg Administration) a good compromise between affordable housing and the interests of the real estate community?

- No, the Speaker/Mayor proposal will make no difference in the dozens of neighborhoods (outside core Manhattan) where developers are busy building market-rate housing.
- Real estate interests are relatively happy because most of what they see as the "next frontier" neighborhoods would not be affected by the Administration's proposed reforms.
- It is up to the City Council and State Legislature to insure that we use tax incentives to create affordable housing, not to unnecessarily subsidize luxury housing.

More questions? Contact:

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Still Subsidizing Luxury Development:

50 High-End Condo Developments That Would Still Be Eligible for 421-a Tax Breaks Even After Proposed Exclusion Zone Expansion and Reform

The Pratt Center for Community Development recently released research showing that high-end condos in neighborhoods in all five boroughs would continue to receive generous tax subsidies (of up to $107,000 per unit in lifetime benefits) even under the compromise proposal to reform the 421-a program supported by City Council Speaker Christine Quinn and Mayor Michael Bloomberg.

This report highlights **54 condo buildings (samples below)** that would still be eligible for 421-a tax relief, even if they would have been built after the proposed reforms. These buildings contain more than **6,100 high-priced condominiums**, far beyond the reach of the average New Yorker.

<u>Not one unit is priced for less than $350,000, most are above $600,000, and some exceed $2 million</u>. They are located in every borough, in neighborhoods including Riverdale, Flushing, Long Island City, Brighton Beach, East Harlem, Washington Heights, and Roosevelt Island. Even with the new limits proposed on the benefits, <u>the estimated lifetime tax breaks on these buildings – post-reform – would be **over $500 million.**</u>

THE BRONX	
	**Solaria (640 W. 237th Street)** **Riverdale** 65 market-rate condos, 20 stories $720,000 - $2 million Would still be eligible for estimated lifetime tax break of: $6,975,475[1]
BROOKLYN	
	**Oceana Condominium & Club** **Brighton Beach** 850 units (multiple buildings) $620,000 - $2 million Would still be eligible for estimated lifetime tax break of: $87,007,700
MANHATTAN	
	**The Bennett, 736 W. 187th Street** **Washington Heights** 55 market-rate condos, 7 stories $509,000 - $794,000 Would still be eligible for estimated lifetime tax break of: $5,221,288
QUEENS	
	**44-27 Purves Street** **Long Island City** 57 market-rate condos, 15 stories $440,000 - $1.3 million Would still be eligible for estimated lifetime tax break of: $9,405,000
STATEN ISLAND	
Photo not available	**130 Bay Street Landing** **St. George** 101 market-rate condos, 9 stories Avg. sales price: $500,000 Estimated Building Lifetime Tax Break: $8,300,000

[1] NOTE: The method used for estimating the tax break is described in the full report.