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Testimony of Ronnie Lowenstein
To the Committee on Economic Development of the New York City Council
On the Atlantic Yards Project

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Good afternoon Chairman Sanders and members of the committee. Thank you for the invitation to appear before you today regarding the proposed Atlantic Yards development in Brooklyn.

Councilmember James and other elected officials asked IBO to analyze the economic and fiscal impact of the project. Although IBO's study is largely done, new information about the project, including today's announcement that there will be more space devoted to residential use—and less to commercial use—has delayed completion of our analysis. I will draw upon the work we have done to make the following comments and observations about the project.

In short, our analysis of the terms of the memorandum of understanding (MOU) signed by the developer, the city, and the state identified a number of benefits in addition to the public sector's capital contribution of $200 million that would result in savings for Forest City Ratner Companies (FCRC). While the city's share of the capital contribution will have a direct cost to the city budget, in most cases the other benefits would not impose a direct budgetary cost. I expect that when IBO's analysis is complete, we will conclude that on the narrow question as to whether the project generates sufficient new tax revenue to offset the cost of the public investment, we will find that there is a net fiscal surplus. Atlantic Yards could also use a number of economic development and housing incentives which are generally available to any qualifying project in the city.

Before taking a more detailed look at some of the provisions, let me begin by noting that given IBO's fiscal orientation, our analysis has focused on the fiscal issues related to this project. There are many other aspects of this, and any other, economic development project that should also be considered, including the impact on traffic, public transportation capacity, the environment, and the existing neighborhood. There are also important issues to consider regarding the land use and planning processes, and the use of state authority to override local zoning and acquire property through eminent domain. The fact that we don not address these issues in no way means that we think they are unimportant. Instead, it reflects our focus on questions our office is best qualified to tackle, leaving these issues to analysts with greater expertise in such matters.

That said, let me turn to our analysis of the financing and subsidies described in the February 2005 memorandum of understanding between Forest City Ratner Companies, the New York State Empire State Development Corporation (ESDC), and the New York City Economic Development Corporation (EDC). Under the MOU, a variety of benefits and subsidies would be available to FCRC. In examining these benefits and subsidies, it is important to distinguish between those that would be available to any developer meeting specific program criteria at Atlantic Yards or elsewhere in the city—these are known as as-of-right benefits—and the discretionary benefits being made available to Forest City for this specific project.

Benefits from Existing Programs at Atlantic Yards

Because the various as-of-right benefits expected to be used at Atlantic Yards would, by definition, be available to any qualifying project, IBO does not include them in our analysis of the fiscal impact of the project. Two of the most important as-of-right benefits that would be used are existing property tax exemptions. Even though the entire project would technically be exempt from city property tax because all of the land would be owned by ESDC, the MOU calls for Forest City to make payments in lieu of the taxes (PILOTs) equivalent to what would be owed if the property were not fully exempt. The calculation of those PILOTs will take into account the savings that would be available under the two traditional as-of-right tax incentive programs.

Industrial and Commercial Incentive Program. Under the Industrial and Commercial Incentive Program (ICIP) commercial projects in the Atlantic Yards area of Brooklyn qualify for a full exemption of the property tax attributable to the new investment for a period of 16 years, followed by nine years of partial exemption. The partial exemption gradually reduces each year so that after 25 years, the development is fully taxable. In addition, the assessments for the first 13 years are not adjusted for appreciation. The PILOT for the non-arena portion of the project will reflect the ICIP benefits that would be available for the commercial space.

Housing Benefits. The PILOT for the non-arena portion would also reflect benefits available under the 421-a program that fully exempts qualifying residential projects from the property tax attributable to the new investment for a number of years followed by a phase-out period. Projects must include an affordable housing component to qualify for 421-a benefits The length of the exemption period depends on a project's location in the city and the type of affordable housing program offered. At Atlantic Yards, the standard 421-a benefits provide for 21 years of full exemption followed by a four-year phase-in period.

Additional Programs for Housing. The recently announced affordable housing agreement between FCRC and ACORN for Atlantic Yards conforms to the "Mixed Income" program developed recently by the New York City Housing Development Corporation (HDC). Under this program, HDC combines 421-a with three other types of subsidies: low-cost financing of first mortgages funded with proceeds from tax-exempt private activity bonds; low-cost financing of second mortgages funded with HDC reserves; and federal Low Income Housing Tax Credits. To qualify for the Mixed Income program, 30 percent of all units must be affordable to middle-income families and 20 percent must be affordable to low-income families.

There is no direct cost to the city's Expense or Capital Budgets for HDC's Mixed Income program. Two of the four subsidy sources in the program—private activity bonds and HDC reserves—represent limited public resources. The use of these resources to build housing at Atlantic Yards means that they would not be available for development elsewhere. But the competition for these funds would depend on the construction timetables for Atlantic Yards and other projects. There are two types of tax credits available: competitively awarded 9 percent tax credits and as-of-right 4 percent credits. Although the state has a limited supply of 9 percent tax credits, use of the 4 percent credits for Atlantic Yards would not affect availability for other projects.

Special Benefits for the Atlantic Yards Project

Under the MOU, Forest City would receive a number of benefits beyond the as-of-right benefits which yield savings for the development. However, not all of these discretionary benefits would have a cost to the city's current budget baseline. In such cases, IBO does not count the benefit as a cost to the city budget. For example, if property is currently tax exempt, there is no new cost to the city's budget if the exemption is continued in a new form.

Capital Contribution. The city and the state each plan to contribute $100 million to the project for site preparation and infrastructure work on and around the arena site. The city's contribution, but not the state's may also be used for site acquisition costs. In the MOU the arena site consists not only of the arena building and its associated parking lot, but the other building sites on the portion of the project lying west of Sixth Avenue. According to the MOU these sites would be used for commercial towers, although more recent announcements indicate that some or even most of these sites may now be devoted to residential development.

The city's $100 million contribution has already been incorporated in the city's Capital Commitment Plan, with $50 million scheduled for 2006 and another $50 million for 2007. The city will finance this as part of its regular capital program using general fund revenues to service the debt. Based on the interest rate assumptions in the Mayor's Executive Budget, the annual debt service costs for these bonds will be about $7.3 million.

The source of the state contribution has not yet been identified.

Low-Cost Arena Financing. A new local development corporation (LDC), affiliated with the state's ESDC, will be created to finance the arena. The LDC will issue $450 million in tax-exempt bonds to be used towards construction of the arena. There will be a separate PILOT agreement for the arena building and parking garage. Forest City will make PILOT payments to the LDC, equivalent to the property tax on the arena. Until the construction bonds are retired, the PILOT payments will be used for debt service on the bonds. Ten percent of any unused portion will go to arena maintenance, and any remaining portion will go to the ESDC. After the bonds are retired, 10 percent of the PILOT payment will go to arena maintenance and all of the remainder will go to ESDC.

Forest City saves money in two ways under this arrangement. First, because the bonds are tax exempt, the interest costs will be lower. If we assume that in the absence of the tax-exempt financing, FCRC were to issue $450 million of its own taxable bonds, the interest rate on those bonds is likely to be about 1.5 percentage points higher than the interest rate on the LDC bonds. In present value terms, the savings from the tax-exempt bonds over 30 years is $76 million. This subsidy is borne by taxpayers throughout the U.S. There is a cost to the city budget only to the extent that holders of the LDC bonds are also New York City residents who will not pay city income tax on the interest they earn from the LDC bonds. IBO has not estimated this cost, but we believe that it is quite small.

The arena financing arrangement offers Forest City a second source of savings. In a more typical arrangement, a developer's costs would include construction financing and property tax payments net of tax incentives such as ICIP. In the case of Atlantic Yards, the PILOT payments will be used to cover construction financing costs, saving Forest City the cost of property tax payments that would be due after the ICIP exemption period. If we assume that a sports arena has a market value, excluding land, of approximately $100 per square foot, then the savings have a present value of $13 million in 2005 dollars. Since much of the land on which the arena would be built is currently owned by the Metropolitan Transportation Authority (MTA), and therefore tax exempt, the property tax savings for Forest City represents no new cost to the city budget.

It should be noted that the MOU calls for the PILOTs on the arena building to be paid to ESDC for 99 years. The city will get none of this revenue.

Loss of Existing Property Tax. Although much of the arena building will sit on land currently owned by the MTA, a portion will be on land that has been privately owned. Once Forest City acquires this land or it is taken by the state using its eminent domain powers, the ownership will be transferred to the arena LDC and ultimately ESDC. As a result, the city will lose about $100,000 in current tax payments from these properties. Over 30 years the present value of these foregone payments is about $1.8 million. IBO includes these foregone property tax revenues as part of the project's cost to the city.

Sale of City Land and Street Beds. The MOU contemplates the sale of portions of several city streets to Forest City, which will then be de-mapped and the land will become part of the development site. The city will also sell two city-owned parcels to ESDC. The terms of the sales will differ depending on whether they involve land directly under the arena building or land elsewhere in the development site.

The sale prices for the street beds east of Sixth Avenue and the city-owned plot lying outside the arena footprint are supposed to be based on fair market value of the land as part of the development. Therefore, this transaction will result in no subsidy to Forest City. Because the PILOT payments for the non-arena portion are to reflect regular city property tax, taking into account the as-of-right exemptions, there is also no fiscal cost to the city.

Because the city streets and one city-owned lot lying directly under the arena building are to be sold for $1 rather than for their market value, this transaction represents a subsidy for Forest City. IBO estimates that the current value of the affected street beds, based on current use of near-by land, is about $60,000. The Department of Finance's estimate of the market value of the city-owned lot is $93,800. Because the city currently receives no property tax from this land IBO does not include this as a cost to the city budget.

Economic and Fiscal Impact. IBO was asked to estimate the fiscal impact of the project. Because the recent changes in the project plans directly affect our results, we cannot give a precise estimate of the impact today. I can tell you that it is almost certainly positive. Our preliminary results indicate that the arena portion of the project would generate enough city and state tax revenue to cover the public sector's investment and generate a modest surplus for the city and state combined. The state does somewhat better than the city because it can tax the income of non-residents, including the players on visiting teams. The MTA would also receive new tax revenue.

It is worth noting that this result contradicts the accepted wisdom that public investments in sports facilities rarely provide any positive returns. A key explanation for the New York surplus in this case is that the city and state are recapturing economic activity that had been lost to New Jersey. Spending by New York fans of the Nets that had been going to New Jersey will now occur here, as will that of those current New Jersey fans who choose to follow the team to Brooklyn.

Of course, the project is more than an arena. The exact amount of office space that will be developed is uncertain, but if FCRC were to proceed with half the amount contemplated in the MOU, the additional tax revenue would increase the size of the fiscal surplus for the city and the state. (The city gains more than the state because it eventually receives property tax after the as-of-right ICIP exemptions expire.) If one accounted for the fiscal impact of the new housing being created then the net fiscal surpluses are even greater.

Rail Yard Development Rights. The project depends on Forest City acquiring development rights to the area above the MTA's rail yard that form the core of the site. A letter from the MTA to Forest City in February committed the parties to a process that would result in the MTA receiving a market-based price for the rights. Earlier this week, the MTA issued a Request for Proposals laying out a bidding process that will be open to other developers besides Forest City. Given that Forest City already controls much of the adjacent private property which would likely be needed to exploit the development potential of the rail yard air rights, there may be a limited number of bidders.

Our full report on the economic and fiscal impacts of the Atlantic Yards project will be completed shortly. Thank you again for inviting me here today and I would be glad to answer any questions you may have.