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# Testimony of Ronnie Lowenstein Before the City Council Finance Committee On Financing Plans for the New Yankee Stadium, April 10, 2006

Good morning Chairman Weprin and members of the finance committee. My name is Ronnie Lowenstein and I thank you for inviting IBO to testify at today's hearing.

The plan for financing a new stadium for the Yankees includes direct subsidies and exemptions from state and local taxes as well as access to tax-exempt bonds for building the stadium. Over a 30-year period, these subsidies and exemptions would cost the city $170 million (present value) and the state an additional $85 million. For the Yankees, these benefits, including savings that result from the use of tax exempt bond financing, add up to $276 million over 30 years (present value). The value of these subsidies and exemptions are summarized in the table on the last page of this testimony.

The tax-exempt bond financing is the largest of the benefits offered to the Yankees, saving the team $147 million over 30 years. These bonds depend upon an unusual arrangement for repayment and the city is awaiting word on whether it complies with federal tax rules.

I will briefly review each of the benefits and then discuss the tax-exempt financing subsidy in greater detail.

***Capital Investments.*** The city will spend $149 million over the next three years for replacement parks and other improvements around the new stadium, including the demolition of most of the existing stadium structure. The need for these projects is a direct consequence of the new stadium plan, particularly the parks replacement mandated under state law. The state will also contribute $70 million towards the construction of new parking garages.

This spending for parks and infrastructure will be financed by issuing bonds through the city's regular capital program, with the principal and interest payments funded with general city revenues. The projects are already included in the current capital plan, with commitments scheduled for 2007, 2008, and 2009. The 30 year present value of the city's debt service obligations for these projects is $139 million. Assuming the state also uses bond financing for its $70 million contribution, the present value of the state's debt service cost is $66 million.

***Property Tax Exemption.*** The new stadium will be exempt from New York City's property tax because it will sit on public land and will be legally owned by the a subsidiary of the city's Economic Development Corporation, and leased to the Yankees. The Yankees will make a payment in lieu of taxes, or PILOT, but it will be used to pay debt service on the construction financing rather than flow into the city's coffers in place of the foregone property tax. IBO estimates that this exemption generates savings to the Yankees of $84 million (present value) over 30 years. These savings are net of the tax breaks under the Industrial and Commercial Incentive Program that would automatically apply if the stadium were taxable. The property tax exemption does not reduce the city's current revenues because there is no property tax today from the parkland being transferred to the Yankees or from the existing stadium. Because there is no loss of current revenue, IBO does not include the value of the exemption as a cost to the city.

***Sales Tax Exemption.*** The project will be exempt from city, state, and Metropolitan Transportation Authority (MTA) sales tax on purchases of construction material, equipment and fixtures installed in the stadium. This benefit is granted at the discretion of the Industrial Development Agency. IBO estimates the 30-year cost of the exemption for the city will be $10.5 million and $11.4 million for the state and MTA combined. The exemption results in an equal amount of savings for the Yankees.

***Rent Credits.*** Under the current lease between the Yankees and the city, the team has been allowed a rent credit of up to $5 million each year from 2001 through 2005 for costs associated with planning and designing the new stadium. Under the June 15, 2005 memorandum of understanding between the city and Yankees, the team will be entitled to additional $5 million rent credits for 2006, 2007, and 2008 as well, although with construction expected to be underway by then, most of the planning costs for the new stadium will have already been incurred.

***Capital Replacement/Operation Reserves.*** When the new stadium is completed, the city and state will each make one-time $4.7 million payments into reserve funds for the stadium. The state's payment will be used for infrastructure and other purposes "as the parties may agree." The city's contribution will be used to ensure that the stadium "continues to operate as an up-to-date, first-class major league baseball stadium." Thirty years after the stadium opens the city will make an additional $8.5 million payment for the same purpose. The city's contribution to these reserves will total $5.4 million in present value terms.

***Mortgage Recording Tax Exemption.*** Like the sales tax exemption, this benefit is also granted at the discretion of the Industrial Development Agency and it has been made available for the project. However, because this project uses bond financing rather than mortgage financing, the exemption is unlikely to result in significant cost.

***Foregone Rent.*** The Yankees will pay no rent for the use of the new stadium. This is in contrast with the current lease under which the Yankees owe annual rent payments. Unlike the current lease, which allows the team to deduct day-to-day maintenance expenses from the rent, the lease for the new stadium will require the Yankees to pay for maintenance and upkeep. The city will also be spared the expense of making major repairs in the old stadium in the coming decades. Because these future costs and savings are uncertain and to a considerable extent offset each other, IBO has assumed that the net value of these changes in the lease is zero.

***Access to Tax-Exempt Bond Financing.*** The largest benefit for the Yankees comes from the tax-exempt financing. Tax-exempt bonds lower the project financing costs for a developer because investors are willing to accept a lower interest rate since their interest income is not subject to income tax. IBO assumes that the difference in interest rates between taxable and tax exempt bonds is 1.5 percentage points. This means that the Yankees can save about $10.6 million annually. The present value of the savings for the team over the 30-year financing period is $147.4 million.

The cost of this subsidy falls largely on the federal government. IBO estimates that the annual cost in federal tax revenues will be about $3.2 million, or $44.0 million over 30 years (present value). The impacts on the city and state budgets depend on how many of the investors who buy the bonds are New York residents. It is likely that a not-insignificant share would be residents, given the triple tax-free nature of these bonds and the existence of municipal bond mutual funds targeted for New York investors. Assuming that half of the buyers reside in the city, the cost to the city budget is about $2.2 million over 30 years and the cost to the state budget is roughly $4.1 million.

In order to make the savings for the Yankees possible, the proposed financing plan relies on an aggressive interpretation of what investments that largely benefit private entities are eligible for the tax exemption. The Bloomberg Administration has asked the Internal Revenue Service for a letter ruling on the matter. It is not clear whether a ruling will be made before the Council plans to vote on the use of PILOTs later this month.

The tax-exempt status of bonds for federal income tax purposes is governed by the federal internal revenue code (IRC). Exemption from city and state income tax is determined by city and state laws, which closely parallel federal provisions. In general, the IRC limits tax exempt status to projects with a governmental or public purpose, although bonds for some private activities can qualify. In 1986 an amendment sponsored by Senator Daniel Patrick Moynihan—who had long sought to ban the use of tax-exempt bonds for sports facilities—was enacted specifically excluding sports facilities from projects eligible to use tax-exempt private activity bonds. The IRC permits some private projects that are not eligible to use private activity bonds to qualify for government purpose bonds if they satisfy several tests spelled out in the revenue code.

In the case of the Yankee's stadium, the important eligibility test to qualify as public purpose in the IRC is known as the "private payment test." A project is disqualified under this test if more than 10 percent of the revenue used to pay the debt service on the bonds is generated directly from the project itself—by rental payments, for example. (This test is one reason why the project does not include rent paid from the team to the city.) Viewed from the opposite perspective, at least 90 percent of the revenue paying the debt service must come from broader sources such as general taxes or fees that apply to the whole city or other broad geographic area.

Although the Yankees are in fact paying for construction of the stadium rather than the government, their intention is to do so with tax-exempt financing. This makes it necessary to structure the agreement so that the money pledged for debt service on the bonds bears enough resemblance to a regular city tax that the deal can get past the private payment test.

The solution devised by the project's planners is a payment in lieu of taxes, which according to the Industrial Development Agency documents will be calculated in a manner similar to the city's regular property tax. (The stadium will actually be exempt from property tax because it will be publicly owned and leased to the Yankees, rather than being owned outright by the Yankees, in part to help qualify the deal for tax exempt financing.)

Given the large annual payments needed to service the $866 million of tax exempt bonds proposed in the financing plan, it is not clear that a property tax-based PILOT would be sufficient. Assuming an interest rate of 6.5 percent, annual debt service payments for 30 year, level payment bonds would be about $66 million. Based on the $736 million estimated construction cost for the new stadium plus the existing land value, IBO estimates that a regular property tax bill would be about $37 million (before exemptions)—considerably below the annual debt service payments.

***Costs and Benefits.*** In total, the bond financing, direct subsidies, and exemptions will save the Yankees $276 million and cost the city $170 million in foregone revenue and additional expenses; the state's tab is $85 million. However, these costs should not be viewed as the total fiscal impact for the city of the stadium project; such an estimate would also include the impact on city revenues of any additional economic activity associated with the new facility. Because so much of the debate on the stadium proposal has centered on parks and transportation issues, IBO has not invested the resources necessary for a complete fiscal analysis.

But I will conclude with a few observations about the stadium's likely broader economic effects. The incremental job and revenue estimates used by the stadium's planners are relatively modest. This project replaces a facility that has been operating in recent years near its full capacity with a slightly smaller facility, so there is little reason to expect much gain in local economic activity beyond the three year construction period. The Yankees will generate additional revenues as a result of the higher average ticket and concession prices at the new stadium, but because a large share of sports business income flows to a relatively small number of players, and owners—few of whom reside in the city—much of these earnings will be spent elsewhere.

Thank you and I will be glad to answer any questions.

**(Costs)/Savings From Exemptions and Subsidies for New Yankee Stadium**

*Present value over 30 years (millions of dollars)*

| | City Costs | State/MTA Costs | Yankees' Savings |
|---|---|---|---|
| Replacement Parks and Infrastructure | ($138.6) | $0.0 | $0.0 |
| Parking Garages | 0.0 | (66.0) | 0.0 |
| Property Tax Exemption | 0.0 | 0.0 | 83.8 |
| Sales Tax Exemption | (10.5) | (11.4) | 21.9 |
| Tax Exempt Financing | (2.2) | (4.1) | 147.4 |
| Rent Abatement | (13.4) | 0.0 | 13.4 |
| Capital Replacement Reserves | (5.4) | (3.9) | 9.4 |
| **TOTAL** | **(170.1)** | **(85.5)** | **275.8** |

SOURCES: IBO; January 2006 Capital Commitment Plan; New York City Industrial Development Agency