



THE CITY OF NEW YORK
INDEPENDENT BUDGET OFFICE

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June 15, 2010

Steven Spinola
President
Real Estate Board of New York
570 Lexington Avenue
New York, New York 10022

Dear Mr. Spinola:

As you requested, IBO has analyzed the impact of the almost annual changes to the state law that determines the share of the property tax levy paid by each of the four classes of property. These changes to state law, made at the request of the City Council and the Mayor, have been aimed at holding down increases in homeowner tax bills in the face of rising market values, but because of the tight interconnections of the city's property tax system, adjustments to provide relief to one type of taxpayer usually results in adverse effects for others. IBO estimates that as a result of the series of one-year adjustments made since 1992 when the current system for apportioning property tax burdens was put in place, owners of residential property saw savings, while owners of commercial property have generally paid more than they would have if the original law been followed each year.

IBO analyzed the implementation of the adjusted caps from fiscal year 1993 through 2010. On June 9th, 2010, the City Council passed a home rule request to the state legislature requesting passage of state legislation that would once again lower the cap for 2011. Once the final tax rates for 2011 are set we can update our estimates through 2011.

Owners of Class 4 properties—all non-residential property other than utilities—paid \$494 million more in 2010 than they would have had the original law not been amended each year. For the average Class 4 property owner, the levy shift is \$21,039 or \$0.64 per square foot. Utility property owners in Class 3 paid about \$348 million more in 2010. Conversely, the two residential classes saw property tax savings. IBO found that owners of one-, two-, and three-family houses saw savings of \$617 million in 2010, or about \$832 per tax lot. Owners of coops, condominiums and rental buildings saw savings of \$225 million, equal to about \$96 per apartment.

Background

The division of city property into four classes and the process for allocating the levy among the classes dates from the December 1981 enactment of S7000A, which took effect in fiscal year 1983. Class 1 primarily consists of one-, two-, and three-family houses, small condos, and vacant land adjacent to other Class 1 parcels. Class 2 consists of all residential property with more than four units (two or more units in the case of coops). Class 3 is made up of the property of utility companies, and Class 4 includes all other properties.

One of the features of S7000A was to preserve each class' existing share of the levy, with annual adjustments as the relative shares of total market value among the classes shift over time. Because class share adjustments affect only the allocation of tax burden, not the overall size of the tax levy, adjusting one class' share requires compensating adjustments for the other classes.

As originally enacted, S7000A contemplated regular adjustments to the share of the levy paid by each class of property based on market value studies by the New York State tax equalization office, although the adjustments were routinely postponed. The original law also provided the city with authority to make discretionary adjustments of up to 5 percent to each class' levy share in addition to the changes resulting from the market value studies. Although the market value adjustments were not made, the Mayor and the City Council made significant discretionary adjustments each year to lower the levy share for Class 1. Without these adjustments, the share of the levy paid by Class 1 would have risen over time because market values were growing faster in Class 1 than in other classes. In an attempt to remove much of the city's discretionary role in determining the class shares, the system was revised for the 1992 fiscal year. Class shares were re-benchmarked to 1989 and were to be automatically adjusted each year to reflect changes in market value, with annual increases in any class' share capped at 5 percent. The only remaining discretionary power in the class share system comes into play when the growth in aggregate market value for one class would result in a change in its market value share greater than the cap. In that case, the City Council is given the authority to determine the allocation of the excess among the other classes.

In most years since 1992, however, the Mayor and the City Council have requested and received from Albany a series of one-year adjustments lowering the cap on the annual market value adjustment from the statutory 5 percent. These adjustments are done in order to minimize Class 1 tax rate increases driven by the growth in market values. State legislation reduced the cap to 2.5 percent from 1997 to 2000, then 2 percent from 2001 to 2007 (except 5 percent in 2005), and since 2008, the cap has been 0 percent. (See Table 1)

Findings

There were statutory adjustments to the cap in 1993, and then in every year from 1995 through 2010. IBO estimates that the cumulative effect on the class shares from lowering the cap each year compared with class shares that would have resulted from using an annual 5 percent cap each year is a shift in 2010 tax liability of \$842 million from residential taxpayers—\$617 million shifted from Class 1 and \$225 million from Class 2. That burden was shifted onto the commercial properties—about \$494 million onto Class 4 and \$348 million onto Class 3.

Table 2 shows the levy shifted each year from 1993 to 2010 by tax class. The amount shifted in a given year is the difference between the property tax liability under the caps as implemented each year from 1992 through that year and IBO's estimate of property tax liability if the 5 percent cap in the original law had been used each year. Positive values indicate that property tax liability is being shifted onto a class, while negative values show liability being reduced. Class 1 and 2 have benefited from the caps with reduced liability in almost every year. Class 3 also saw a reduction in liability from 1995 to 2001, but has been seeing an increase in liability since 2002, in excess of \$300 million for each of the past two years. Class 4 has generally seen an increase in liability, peaking at over a \$530 million shift in 2009.

These data are also shown in a chart attached at the end of the letter. From the chart, the effect appears to have been lowest in the early part of the decade. The differences appear particularly acute

during the recent real estate boom when market values grew rapidly and the cap was reduced to 2 percent and then 0 percent.

With the recent action by the City Council and the Mayor calling for a 2.5 percent cap in 2011, the shift of liability from Class 1 to Class 3 and Class 4 will continue, although with a higher cap, the shifts will probably be smaller than they were in 2008 through 2010.

What if There Were No Cap? The absence of a cap on annual class share adjustments, whereby each class' levy share would be adjusted simply for the change in market value shares, would have produced different results. The liability shifted off of Class 1 would be even larger with no cap than with a 5 percent cap, especially from 2004 to 2008, showing that even the 5 percent cap would have been protective of Class 1 because growth in the market value share exceeded 5 percent a year. Similarly, the 5 percent cap reduced Class 3 liability compared to no cap from 1995 to 2000. Classes 2 and 4 would have seen a lower liability under a system with no caps than with the original law setting a 5 percent cap, because growth above 5 percent in the other classes would not have been shifted onto them.

Levy Shift for Average Tax Payers. The shift in levy from one class to another affects owners of different types of properties within each tax class differently. Table 3 shows the average levy in 2010 for each tax class, and for selected property types within a tax class, first under the adjusted caps and then if the 5 percent cap had remained in place.

The average one-, two-, or three-, family home owner's tax bill was reduced by \$844 or almost 24 percent as a result of the lower caps. The residential properties in Class 2 also saw a reduction in the average levy, but at just over 3 percent. Overall, the levy per apartment was reduced by \$120, ranging from a \$96 reduction for the average rental apartment to a \$221 reduction for the average condominium.

Conversely, the average levy for utility property in Class 3 and commercial properties in Class 4 increased. For the utility property, the average levy shift was \$1.1 million or a quarter of the average tax bill. (The class 3 average is high because of a few very large tax payers among the utilities; the median increase is \$21,885). Because property taxes are part of the cost base used in setting utility rates, the regulated utilities in Class 3 are able to pass much of their increase along in higher utility rates. The commercial property in Class 4 has, on average, about \$5,800 in levy shifted onto each tax lot, or 7 percent of the current levy. The average Manhattan office building, for example, had \$112,000 in levy shifted onto it, while the average warehouse or factory saw a shift of \$2,300 and the average store, a shift of \$3,500.

IBO also calculated the average commercial property levy on a per square foot basis, to account for variations in size. Overall, commercial properties pay \$6.67 per square foot in property tax levy, and about \$0.46 of that levy has been shifted as a result of class share caps below 5 percent.

If you have any questions, please feel free to contact me at (212)442-0225 or Ana Champeny, anac@ibo.nyc.ny.us or (212) 442-1524) who conducted the study.

Sincerely,

Ronnie Lowenstein

Table 1: Class Share Adjustment Cap, Based on State Legislative Action

Year	Cap
1993	2.00%
1994	5.00%
1995	2.75%
1996	2.75%
1997	2.50%
1998	2.50%
1999	2.50%
2000	2.50%
2001	2.00%
2002	2.00%
2003	2.00%
2004	2.00%
2005	5.00%
2006	2.00%
2007	2.00%
2008	0.00%
2009	0.00%
2010	0.00%

SOURCE: IBO

Table 2: Annual Property Tax Liability Shift, Actual Law Compared to 5 Percent Cap

Dollars in millions

	Class 1	Class 2	Class 3	Class 4
1993	\$5.80	\$(69.30)	\$95.52	\$(32.03)
1994	\$0.10	\$(44.27)	\$0.05	\$44.12
1995	\$(20.47)	\$(99.62)	\$(10.28)	\$130.37
1996	\$(42.18)	\$(160.61)	\$(21.38)	\$224.17
1997	\$(67.66)	\$(64.98)	\$(34.58)	\$167.23
1998	\$(55.75)	\$(17.35)	\$(51.45)	\$124.57
1999	\$(75.76)	\$(18.20)	\$(69.70)	\$163.66
2000	\$(31.27)	\$(5.74)	\$(92.40)	\$129.41
2001	\$(7.95)	\$0.10	\$(30.00)	\$37.86
2002	\$(41.81)	\$(0.08)	\$5.38	\$36.52
2003	\$(94.21)	\$(1.68)	\$22.25	\$73.63
2004	\$(163.77)	\$(16.69)	\$18.07	\$162.39
2005	\$(177.58)	\$(45.23)	\$43.52	\$179.30
2006	\$(260.86)	\$(195.13)	\$98.25	\$357.72
2007	\$(349.63)	\$(154.55)	\$144.13	\$360.07
2008	\$(473.65)	\$(62.82)	\$153.22	\$383.25
2009	\$(665.67)	\$(183.08)	\$318.72	\$530.05
2010	\$(616.94)	\$(225.25)	\$348.05	\$494.12

SOURCE: IBO

NOTES: 5 Percent Cap assumes that excess increases are shifted in proportion to market value among the classes, whereas existing law allows the NYC City Council discretion is distributing excess among the other classes. Positive values indicate that property tax liability is being shifted onto a class, while negative values are liability being reduced.

Table 3: Shift in Average Levy, by Property Type, between Current Shares and Shares under a 5 Percent Cap, 2010

	Average Levy, Actual Caps	Average Levy, 5 Percent Cap	Difference in Average Levy	Percent Change in Average Levy
All Class 1 (per lot)	\$3,513	\$4,345	\$(832)	
1-, 2-, and 3-Family Homes	\$3,571	\$4,415	\$(844)	-23.7%
Other Class 1	\$3,284	\$4,061	\$(777)	
All Class 2 (per unit)	\$3,519	\$3,639	\$(120)	
Rental Buildings	\$2,800	\$2,896	\$(96)	-3.4%
Cooperative Buildings	\$4,940	\$5,109	\$(169)	
Condominiums	\$6,469	\$6,690	\$(221)	
All Class 3 (per tax lot)	\$4,366,359	\$3,225,000	\$1,141,359	26.1%
All Class 4 (per tax lot)	\$83,126	\$77,305	\$5,821	
Manhattan Office Buildings	\$1,603,885	\$1,491,586	\$112,299	7.0%
Other Class 4	\$47,581	\$44,250	\$3,331	
Warehouse/Factory	\$33,150	\$30,829	\$2,321	
Store	\$50,582	\$47,040	\$3,542	
All Class 4 (per square foot)	\$6.67	\$6.21	\$0.46	
Manhattan Office Buildings	\$9.16	\$8.52	\$0.64	6.9%
Other Class 4	\$5.50	\$5.11	\$0.39	
Warehouse/Factory	\$1.89	\$1.76	\$0.13	
Store	\$5.88	\$5.47	\$0.41	

SOURCES: IBO, Department of Finance Recordbook

NOTES: 5 Percent Cap assumes that excess increases are shifted in proportion to market value among the classes. Positive values indicate that property tax liability is being shifted onto a taxpayer, while negative values are liability being reduced.

Impact of Class Share Adjustments, Compared to 5 Percent Cap, 1992-2010

