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**Testimony of George Sweeting
Before the City Council Finance Committee
On the Tax Treatment of Coops and Condos**

February 26, 2004

Good morning Chairman Weprin and members of the committee. My name is George Sweeting and I am a deputy director at the New York City Independent Budget Office. I appreciate the opportunity to appear before you regarding the property tax treatment of residential cooperatives and condominiums and the effectiveness of the coop/condo abatement that was created in 1997.

The abatement was a first step towards giving apartment owners the same tax benefits as private homeowners. Unfortunately, due to the vagaries of New York's property tax laws and the formulation of the original abatements, some coop and condo owners are reaping tax benefits even beyond what private homeowners receive. This is particularly on the Upper East Side and the Upper West Side in Manhattan. More than one-third of the abatement—at a cost of \$88 million to the city—goes to coop and condo owners who have tax rates at or below that of private homeowners. At the same time, even with the abatement, virtually all coop and condo owners in the boroughs other than Manhattan still face tax burdens that are well above those of private homeowners.

The abatement's shortcomings may have been initially tolerated because it was supposed to be only a stop gap measure pending more comprehensive reform. Seven years later, the shortcomings remain and there is still no plan to move to a more comprehensive solution. If the abatement becomes the last word on coop/condo reform, the city needs to consider attending to some of its shortcomings when the program is up for renewal later this year. For example, if additional benefits are being considered as part of the renewal, those benefits could be targeted to the parts of the city where the largest differences between homeowner and coop and condo tax burdens remain.

As the members of this committee know quite well, the New York City Property Tax system is extremely complicated. There are four classes of property. Each class has a different assessment ratio, a different assessment method, a different process to limit assessment increases, and a different tax rate. The average taxpayer has a difficult time comparing the tax burden of two properties in the same tax class and an even greater difficulty comparing properties in different classes. To overcome these difficulties we compare properties based on the effective tax rate, which is computed by dividing the final tax bill by the full market value of each property.

When dealing with coops and condos, there is a further complication in computing the effective tax rate. Under Section 581 of the New York State Real Property Law, these properties are to be

valued as if they are rental properties, and indeed until very recently, the city has tended to value them as if they were rent-regulated properties. As a result the city's official valuations for coops and condos tend to be much lower than if the property were valued using sales price based market values, although the extent of the difference varies across the city. Given that the goal of coop/condo reform is to obtain the same tax treatment as Tax Class 1 homes—where sales prices are the basis for setting market values—it seems reasonable to use sales-based market values when computing the effective tax rate for coops and condos.

Our effective tax rate analysis indicates that there are very wide disparities in the tax burdens not just between Tax Class 1 and Tax Class 2, but within the coop and condo class, as well. (I have included a table at the end of this testimony that summarizes the differences by borough.)

In Manhattan, the typical coop owner faces a tax burden, before accounting for the abatement, which is nearly as low as those enjoyed by Manhattan Tax Class 1 owners. The story is quite different in the other boroughs, where coops and condos bear significantly higher tax burdens than private homes.

Comprehensive coop and condo reform was expected to involve a shift to sales-based valuation and the application of the Tax Class 1 assessment ratio and tax rate to the properties. In the mid-1990s, the Department of Finance asked for time to resolve several knotty methodological and technological issues. Pending development of a plan to achieve comprehensive reform, the current abatement was adopted as a stop-gap to give some immediate relief. Because it operates on top of the existing assessment system, which ignores coop and condo sales prices, the current abatement does not take into account the differences in how much relief is needed to deliver a Tax Class 1 tax burden. As a temporary fix, such “rough justice” was accepted, but with the program now apparently permanent, the inefficiencies in the current abatement stand out.

IBO estimates that of the \$250 million in tax relief that will be paid through the coop/condo abatement in fiscal year 2004, \$88 million (35 percent of the total) is unneeded if the goal is to give coop and condo owners a Tax Class 1 tax burden. More than two-thirds of the unnecessary spending goes to owners with effective tax rates below the Tax Class 1 level *before* the abatement. The balance goes to those with effective tax rates above the Tax Class 1 level, but who do not need all of their abatement benefit to reach the Tax Class 1 effective tax rate. Virtually all of the unnecessary spending occurs in Manhattan, particularly in the prime coop neighborhoods east and west of Central Park.

When the abatement is up for renewal, the city might want to consider ways of reducing the inefficiency, although that is a polite way of saying raise some people's taxes. The value of the abatement might be reduced in some parts of Manhattan, or even eliminated. Alternatively, if the abatement is expanded, then perhaps the greater benefits could be reserved for those parts of the city where the gap between coop/condo effective tax rates and Tax Class 1 effective tax rates are greatest. For example, tripling the benefit for coops and condos outside Manhattan, while leaving the current abatement rules in place in Manhattan, would increase the cost of the program by \$100 million and give most non-Manhattan coop/condo owners the equivalent of class 1 tax treatment.

Nonetheless, no amount of tinkering with the abatement will deliver an equal benefit to all apartment owners. To do this requires changing assessment practices so that coops and condos are valued and taxed like private homes. IBO estimates that such a shift, which implies raising taxes on those apartments currently below Tax Class 1 levels, would cost \$287 million— only \$37 million more than the cost of the current abatement. Although some of the problems in moving to such a solution that were raised by the Department of Finance no doubt remain, the fiscal impact of such a shift would no longer be very great.

Thank you again for the opportunity to testify and I would be happy to answer any of your questions.

Average Effective Tax Rates by Borough

	Class 1	Coops	Condos
Manhattan	0.8038	0.8903	1.0441
Bronx	0.7387	1.5715	1.2080
Brooklyn	0.6468	1.2681	1.1535
Queens	0.7105	1.4595	1.2518
Staten Island	0.7102	1.3306	1.2531

SOURCE: IBO