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Ronnie Lowenstein
DIRECTOR

December 3, 2015

Andrew Reicher
Executive director
Urban Homesteading Assistance Board
120 Wall Street, 20th Floor
New York, NY 10005

Dear Mr. Reicher:

At the request of the Task Force on City-Owned Property, the Independent Budget Office has estimated the cost of the task force's proposal to provide a full tax exemption to Housing Development Fund Corporation coop buildings that got their start under the aegis of the housing department's Division of Alternative Management Program. The full exemption would replace what is currently a partial exemption and would be in effect during a newly proposed 40-year regulatory agreement. If the proposal were approved, the expiration of the current agreement, which ends in 13 years, will be accelerated to 2018, at which point the new agreement would take effect and last through 2057.

IBO estimates that the task force's proposal would cost the city $19.1 million more per year than if the current agreement were to be extended through 2057. Similarly, the task force's proposal would cost the city $11.4 million more per year through 2057 than under an alternative proposal from the housing department, which would provide a partial tax exemption larger than under current law. Finally, if the current regulatory agreement is allowed to expire without further action to extend or replace it, the city would receive $33.5 million per year in property tax payments from the coops from 2029 through 2057.

If you have any questions regarding this analysis, please contact me or IBO's property tax analyst, Geoffrey Propheter, who prepared these estimates. He can be reached at geoffreyp@ibo.nyc.ny.us or 212-341-7363.

Sincerely,

Ronnie Lowenstein

MEMORANDUM

Date: **December 3, 2015**

To: **George Sweeting**

From: **Geoffrey Propheter**

Subject: **Cost Estimates for Alternative Tax Exemptions for Some HDFC Coops**

Introduction

The Task Force on City-Owned Property (TCOP) asked IBO to conduct a cost analysis of its proposal to fully exempt from the property tax coops formed under the supervision of the Department of Housing Preservation and Development's (HPD) Division of Alternative Management Program (DAMP). Through the DAMP program, HPD sells city-owned residential buildings to a Housing Development Finance Corporation (HDFC), a cooperative intended for low- and moderate-income shareholders, for $250 per apartment. In exchange for accepting income restrictions on shareholders for the duration of a regulatory agreement with HPD, the city offers the coop, among other benefits, a partial reduction in property taxes, which we refer to as the "DAMP exemption."

IBO estimates that TCOP's proposal, compared with current policy, would cost taxpayers $19.1 million more a year on average over the next 40 years—and could cost more depending on how the full exemption is administered. Many of the coops formed under the alternative management program currently receive the state School Tax Relief (STAR) exemption, and the city is reimbursed by the state for the forgone revenue. A full exemption would presumably cost the city the reimbursement if these HDFC coops are treated as a classified exemption like property owned by nonprofits. IBO also estimated the cost of TCOP's proposal under various scenarios of buildings opting out of the proposal to avoid restrictions on resales under new regulatory agreements that would be part of the proposal.

TCOP, a group of community-based organizations, also asked IBO to estimate the revenue implications of HPD's alternative proposal, which would further reduce the affected coops' property tax liability but not fully exempt them from the tax. Compared with HPD's proposal, IBO estimates that TCOP's proposal would cost taxpayers $11.4 million more a year on average over the next 40 years.

Finally, TCOP asked the IBO to analyze sales of apartments in these HDFC coops over the last five years. IBO identified 990 coop apartment sales from 2011 through 2015. Adjusting for inflation, the citywide median price (in 2015 dollars) was $270,200, with prices ranging from $82,500 to $2.0 million; 83.6 percent of the apartments sold for $500,000 or less.

TCOP initially submitted a list of research questions to IBO. After subsequent conversations with TCOP, IBO reformulated the questions, which are shown below. Following a discussion of the methodology and assumptions used by IBO in this analysis, we offer our cost estimates following each question.

Methodology and Assumptions

To estimate the property tax revenue implications of TCOP's and HPD's proposals, IBO collected assessment data from the Department of Finance's real property assessment database on coop properties currently receiving the exemption because they were created under DAMP. Based on conversations with TCOP members, IBO modeled the revenue implications of a 40-year regulatory period beginning in 2018 and extending through 2057. (Unless otherwise noted, all years refer to city fiscal years.) Future tax expenditures were calculated using the Class 2 tax rate in 2016 (12.883 percent) and discounted at 4.0 percent.

In order to answer each of the questions posed by TCOP, IBO had to adopt a variety of simplifying assumptions. The following assumptions apply to the entire analysis:

First, as we are comparing TCOP and HPD proposals to the current DAMP regulatory agreement, to create a common baseline, IBO assumed that the current agreement, which expires 13 years from now, would instead be renewed in 2028 and continue in its current form through 2057.

Second, we assumed that the average number of coop apartments participating in the program in the future will equal the current number of 16,058 apartments.

Third, we assumed that assessed values will grow on average by 3.9 percent a year, which is the inflation-adjusted average annual growth in assessed value for the former DAMP properties over the last 30 years.

Fourth, IBO assumes that a newly adopted regulatory agreement does not forgive property taxes that are currently in arrears. If outstanding balances are instead forgiven in the future, the forgone revenue would be an additional cost of the proposals. Neither TCOP's nor HPD's proposals include provisions to forgive outstanding balances.

In addition, IBO made a number of assumptions that are unique to each of TCOP's questions. We provide more information on these assumptions when discussing each question.

Importantly, IBO's analysis does not consider tax expenditures for HDFCs that are not coops—namely, rental housing and one- to four-family homes. These properties may receive the exemption tied to DAMP or a variety of other exemptions. The analysis also does not consider properties that received DAMP at some point in the past but are not currently benefitting from the exemption in 2016. These properties previously lost or voluntarily relinquished their eligibility, and their eligibility status is assumed not to change during the proposed new regulatory period. Hence, the analysis is based on the universe of HDFC coops currently receiving the DAMP exemption rather than the universe of all HDFC housing.

Assessment of Impact on Tax Base

What is the forgone tax revenue from the current DAMP tax exemption each year?

For fiscal year 2016, the tax expenditure for properties receiving a DAMP exemption is $36.4 million. Coop apartments, which make up 82.3 percent of all residential units in the program, are responsible for 76.3 percent of the tax expenditure, or $27.7 million.

Average Tax, Levy, and Tax Expenditure for Properties Receiving the DAMP Exemption, 2016

Property Type	Number of Apartments	Levy Per Apartment	Total Tax Expenditure, *in millions*	Tax Expenditure Per Apartment
1-4 Family	49	$1,512	0.01	$1,537
Coops	16,058	1,221	27.7	1,728
Rental	3,397	1,201	8.5	2,516
Total	**19,504**	**$1,219**	**$36.4**	**$1,865**

SOURCE: Independent Budget Office analysis of Department of Finance data
NOTE: Dollars may not add due to rounding.

What would be the forgone annual tax revenue for DAMP exemption coops based on HPD's proposal?

Under current law, for properties entering the DAMP program after 1990, taxable assessed value is limited to 6.0 percent growth a year or 20 percent growth over five years. For 2016, taxable value for the coop buildings equals $9,787 (the taxable assessed value cap) multiplied by the number of coop apartments in the building. The cap is expected to grow an average of 3.7 percent a year through the current regulatory period. HPD proposes lowering the assessment cap to $6,695 for 2016 for coops with the DAMP exemption, and further proposes to limit the cap growth to 3.0 percent annually.

In present value terms, we estimate that HPD’s proposal would result in an average tax expenditure of $34.9 million, a $7.7 million annual increase over current law through 2057.

What would be the forgone annual tax revenue for DAMP exemption coops under the task force’s proposal granting a full property tax exemption?

TCOP proposes a full property tax exemption for the HDFC coops in formerly city-owned buildings. In addition to the assumptions described in the methodology section, the calculations necessary to estimate the proposal’s cost in terms of forgone property tax revenue required an additional simplifying assumption: these coop owners continue to receive all of the other tax exemptions they currently enjoy. For 2016, property tax records indicate that 9,448 of the 16,058 apartments in the HDFC coops also received STAR exemptions; other awarded exemptions include veterans, senior citizens, disabled homeowner, and J-51. IBO’s analysis of TCOP’s proposal assumes that awarding a full property tax exemption would not affect these other exemptions. As will be discussed shortly, this assumption produces a small underestimate of the proposal’s total cost to city taxpayers.

IBO estimates that were current policy extended through 2057, the DAMP property tax exemptions for coops would cost the city a total of $1,088.9 million in present value terms. HPD's proposal would increase the expenditure to $1,396.2 million, a $307.3 million increase. TCOP's proposal would increase the expenditure to $1,851.9 million, a $763.0 million increase. Thus, TCOP's proposal would cost $455.6 million more than HPD's proposal over the life of the program, or $11.4 million more a year on average.

TCOP's Proposal Would Cost the City $11.4 Million More a Year on Average Than HPD's Proposal

Dollars in millions

Scenarios	Estimated Tax Expenditure
Current DAMP Cap	$1,088.9
HPD-Proposed Cap	$1,396.2
TCOP-Proposed Cap	$1,851.9
Difference Between HPD and Current Policy	$307.3
Annual Average	$7.7
Difference Between TCOP and Current Policy	$763.0
Annual Average	$19.1
Difference Between TCOP and HPD Proposals	$455.6
Annual Average	$11.4

SOURCES: Independent Budget Office, Department of Finance
NOTES: Dollars are discounted at 4.0 percent a year through 2057. The table does not include the estimated cost of losing the state STAR reimbursement, over the proposed regulatory period. Columns may not add due to rounding.

Under state law, the city is currently reimbursed for STAR property tax exemptions on coops with the DAMP exemption as well. If the full exemption proposed under TCOP's option were treated as a classified exemption similar property owned by nonprofits, then the city would forgo the state reimbursement for STAR granted to the residents of coops with the DAMP exemption. Assuming the city forgoes the reimbursement, the above estimates will slightly understate the total cost of a full exemption for these properties. IBO estimates that forgoing the reimbursement would increase the aggregate cost of TCOP's proposal through 2057, bringing the estimated total to $470.1 million relative to HPD's proposal, or $11.7 million more per year. However, it is also possible that the city could structure a full exemption in such a way that this additional cost would not be incurred.

Assessment of the Tax Revenue Generation from Coops That Opt Out

TCOP asked IBO to estimate revenue implications of HDFC coops opting out of a new regulatory agreement. Given the city's robust real estate market, the boards of some coops in neighborhoods where apartments have high potential resale value may find it financially advantageous to opt out of a new regulatory agreement. In such instances, reducing the cost of coop ownership by exempting some or all property taxes may not be sufficient benefit to persuade shareholders to continue accumulating equity in the coop. Thus, in areas of the city with particularly strong market growth, we would expect to find more coops exercising an option to opt out of regulatory agreements. Since DAMP regulatory agreements impose income restrictions on coop shareholders, the effect of opting out is to not only return the coop's actual assessed value to the property tax roll but also to reduce affordable home ownership options for low- and moderate-income households.

In order to answer TCOP's questions regarding opting out, IBO defined housing markets of differing strength across the city. Based on an analysis of nonrental residential median sales prices in 2014 and 2015, IBO divided the city into seven regions and coded their housing market strength as strong, moderate, or weak based on the annual change in real median sales prices. The accompanying table describes the areas identified. As there are no coops with DAMP exemptions in Staten Island, the borough was omitted.

The Strength of the City's Current Residential Market Varies Within and Across the Boroughs

Area	Area Description	Market Strength
Manhattan-Upper	North of E 96th St, North of 110st between Frederick Douglass Blvd. and 5th Ave, and North of West 116th St at Frederick Douglass Blvd.	Moderate
Manhattan–Mid/Lower	The rest of Manhattan not already defined.	Strong
Bronx	The entire borough.	Weak
Brooklyn–Downtown	From the East River east on Congress St./Bergen St. and North on Classon Ave to and including the Navy Yard	Strong
Brooklyn–Williamsburg/Greenpoint	The portion of Williamsburg and Greenpoint west of the Brooklyn-Queens Expressway.	Strong
Brooklyn – Rest	The rest of Brooklyn not already defined.	Moderate
Queens	The entire borough.	Weak

SOURCE: Independent Budget Office analysis of Department of Finance property sales data

Once a coop building opts out of the DAMP regulations, its apartments become eligible for a city abatement if the apartment is the property owner's primary residence. The abatement offsets some of the city's savings from restoring the assessed value of buildings that opt out to the tax roll. The net revenue gain to the city from coops opting out of DAMP regulations is the difference between the baseline DAMP tax expenditure and the abatement some coops would become eligible to receive. IBO's analysis incorporates the offsetting effect of the abatement and assumes that all coop apartments are occupied as primary residences.

If 50 percent of coops with DAMP exemptions in strong markets opted out of the current regulatory agreement, how much tax revenue would these properties generate annually?

If 50 percent of these coops in strong markets opted out, IBO estimates their present value tax liability would be $5.9 million a year on average. This results from an $8.9 million increase in property taxes that are partly offset by $3.0 million in coop abatements.

However, since these properties currently have some tax liability remaining after the DAMP partial exemption, the city already receives a portion of the buildings' expected $8.9 million annual liability. The portion that would represent new revenue to the city is the buildings' tax expenditure under current policy, were current policy extended through 2057. In this case, IBO estimates the new revenue these properties would generate on average is $3.2 million a year—$6.2 million from property taxes less the $3.0 million from the coop abatement.

If 50 percent of coops with DAMP exemptions in strong markets opted out, how much additional tax revenue would these properties generate annually compared with HPD's proposed cap?

Because HPD's proposal lowers the tax liability of the DAMP exemption relative to the current regulatory agreement, if a building opts out of HPD's proposal the city will collect additional revenue beyond what it would collect had they opted out of current policy. If half of the DAMP exemption coops in strong markets opted out of HPD's proposal, IBO estimates the new revenue to the city will average $4.3 million annually in present value terms. About three-quarters, or $3.2 million, of this additional revenue is due to current policy while the balance, $1.1 million, is due to the marginal increase from the more generous exemption under HPD's proposal.

If 50 percent of coops with DAMP exemptions in strong markets and 10 percent of all other DAMP exemption coops opted out of the current regulatory agreement, how much tax revenue would these properties generate annually?

Under these opt-out conditions, IBO estimates that the coops' full tax liability would be $8.1 million a year on average through 2057—$11.7 million from the property tax less $3.7 million from the coop abatement. In terms of new revenue, however, we estimate that the net gain to the city in present value terms is $4.0 million a year on average. The majority of this, $3.2 million as noted above, is from coops in strong markets with the remainder coming from coops in moderate and weak markets.

How much additional tax revenue would coops with DAMP exemptions generate annually in each type of market if they opted out of TCOP's proposal assuming 25 percent, 50 percent, 75 percent, and 100 percent opt-out rates?

TCOP asked IBO to estimate revenue impacts if these coops opted out of the organization's proposed regulatory agreement, which provides a full property tax exemption. The additional revenue to the city is therefore the difference between the coops' tax expenditure under current policy minus the abatement the coops become eligible to receive once they opt out. IBO estimated net gains in property tax revenue for strong, moderate, and weak markets under the four different opt-out rate assumptions. If all coops with DAMP exemptions opt out of TCOP's proposal, the city is poised to gain $14.9 million a year on average through 2057 in present value terms. At the other extreme, if a quarter of all coops in each market opt out, the city's net gain is on average $3.7 million annually over the same period.

Because the annual new revenue to the city reported in this section is 1) measured against a scenario in which the TCOP full exemption is assumed to have been adopted, and 2) offset by the abatement which coops that opt out would be eligible to receive, these estimates differ from other estimates reported earlier in the analysis. For illustration, consider the case of a 100 percent opt out rate. A prior question posed by TCOP asked for the additional cost of offering a full exemption to these coops, which we estimated as $19.1 million a year through 2057. This question asks how much additional revenue the city would gain if coops opted out of a regulatory agreement offering full property tax abatements. In this case, $19.1 million is not new revenue but rather the expected liability under current policy. Instead, the new revenue source comes from eliminating the current tax expenditure that the coops enjoy, worth $27.2 million a year on average. From this amount IBO subtracted $12.3 million to account for the abatement buildings opting out would become eligible to receive. The difference is the net new revenue the city is expected to receive under a 100 percent opt out scenario—$14.9 million a year.

The Amount of New Revenue to the City Increases as the Percentage of Coops Opting Out Increases
Dollars in millions

	Opt-Out Rates			
Market Strength	**25 Percent**	**50 Percent**	**75 Percent**	**100 Percent**
Strong	$1.6	$3.2	$4.7	$6.3
Moderate	1.8	3.5	5.3	7.1
Weak	0.4	0.8	1.2	1.6
Total	**$3.7**	**$7.5**	**$11.2**	**$14.9**

SOURCE: Independent Budget Office

The above analysis assumes the current regulatory period is extended through 2057, which assumes not only that HPD fails to adopt a new regulatory framework but also that the city council approves a straight extension of existing policy after 2029 when the current regulatory period ends. An alternative way to view the tax revenue implications is to assume that the City Council does not approve a straight extender and instead lets the DAMP exemption expire without a new HPD regulatory agreement. In this case, the city would receive the affected coops' full tax liability from 2029 onward.

IBO modeled the total property tax revenue (that is, new revenue plus existing liabilities under the current regulatory agreement) the coops would generate for the city through 2057 if the City Council refused to approve any new DAMP exemptions after 2029. Overall, the city would receive $33.5 million a year in present value terms if no new regulatory agreement is in place after 2029. Nearly half of the revenue, $16.1 million, would be generated by affected coops in moderate markets.

The City Would Receive More Revenue Per Year from Coops with DAMP Exemptions in Moderate Markets if No New Regulatory Agreement Is in Place After 2029
Dollars in millions

Market Strength	Total Revenue
Strong	$11.7
Moderate	16.1
Weak	5.8
Total	**$33.5**

SOURCE: Independent Budget Office
NOTES: Columns may not add due to rounding.

Sale Frequency and Sales Prices

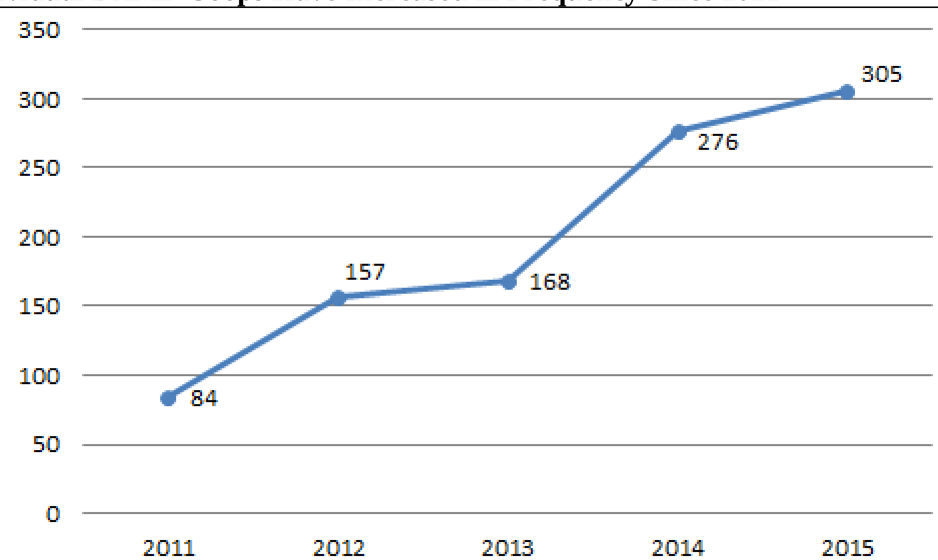
What has been the annual *number of resales in HDFC coops each year over the past five years?*

HPD does not sell DAMP properties to an HDFC at market price but instead at $250 per apartment. As these are not arm's-length transactions (that is, the price a willing buyer and willing seller would pay in a competitive market), including them in a sales analysis would distort our perceptions of the market. To provide a clearer picture of the market for HDFC coop apartments, IBO used a $80,000 price threshold to distinguish arm's-length from non-arm's-length transactions.

IBO identified 990 DAMP coop apartment sales presumed to be arm's-length transactions taking place from 2011 through 2015. Sales have become increasingly more frequent during this period, more than doubling over the five-year period.

Importantly, IBO excluded coop sales with multiple apartments bundled together in a single transaction. Since TCOP's goal is to understand the sales dynamics for individual coop apartments, including bundled transactions—which IBO cannot disaggregate into individual sales prices—would bias the analysis.

Sales of Individual DAMP Coops Have Increased in Frequency Since 2011



SOURCES: Independent Budget Office, Department of Finance

For each year over the past five years, what has been the lowest, highest, and median sales price for HDFC coops overall, and *in each of the following markets: weak, moderate, and strong?*

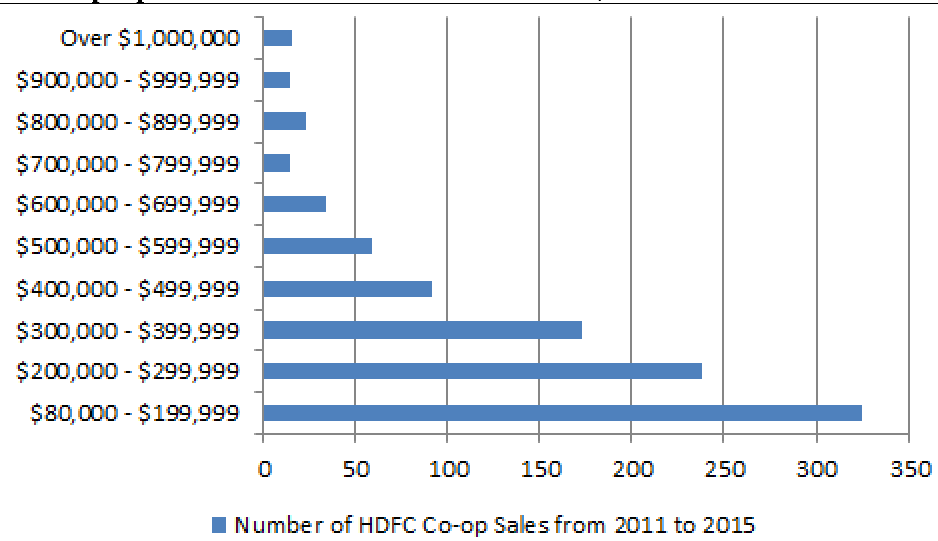
The citywide inflation-adjusted median sales price for the 990 presumed arm's-length coop sales over the last five years (in inflation-adjusted 2015 dollars) was $270,200, with prices ranging from $82,500 to $2.0 million.

Sales Data for Coops in DAMP Exempt Properties, 2011 Through 2015				
		Sales Price		
Real Price	**Number of Sales**	**Minimum**	**Median**	**Maximum**
Strong	**449**	**$90,900**	**$360,000**	**$1,913,800**
Manhattan–Mid/Lower	359	$90,900	$387,500	$1,913,800
Brooklyn–Downtown	14	$148,300	$369,000	$772,400
Brooklyn–Williamsburg/Greenpoint	76	$92,100	$236,900	$604,400
Moderate	**524**	**$82,500**	**$210,000**	**$2,039,700**
Manhattan–Upper	466	$82,500	$213,700	$2,039,700
Brooklyn–Rest	58	$85,600	$197,200	$755,500
Weak	**17**	**$82,900**	**$122,800**	**$271,000**
Bronx	17	$82,900	$122,800	$271,000
Citywide	**990**	**$82,500**	**$270,200**	**$2,039,700**

SOURCE: Independent Budget Office analysis of Department of Finance property sales data
NOTE: Dollars are deflated to 2015 values.

As further illustrated in the bar graph below, a majority of HDFC coops sold for under $300,000. Moreover, 83.6 percent of the coops sold for $500,000 or less.

Half of DAMP Coop Apartments Have Sold for Under $270,200



SOURCES: Independent Budget Office, Department of Finance