Evaluation of Commercial Revitalization and Commercial Expansion Tax Expenditure Programs Prepared for New York City Council Finance Committee Pursuant to Local Law 18

NYC Independent Budget Office
Dec 18, 2017
1995: Commercial Revitalization Program (CRP)
- What:
  - Property Tax Abatement
  - Commercial Rent Tax reduction
- Who:
  - Non-Residential
  - Lower Manhattan (South of Murray)
  - Built before 1975

2000: Commercial Expansion Program (CEP)
- What:
  - Property Tax Abatement
- Who:
  - Non-Residential
  - Manhattan North of 96th & outer boroughs
  - Built before 1999

2005: CRP Expansion
- What:
  - Commercial Rent Tax reduction
- Who:
  - Non-Residential
  - Expanded Lower Manhattan (south of Canal Street)
  - Built any time

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Other Programs and Modifications

- **1995:**
  - The 421-g program for conversion of commercial buildings into multiple dwellings in the CRP region.
  - 14-year abatement of about 80 percent of the real estate taxes paid on the property before conversion.

- **2005:**
  - Commercial Rent Tax (CRT) exemptions for World Trade Center.
  - CRT exemptions for Downtown ground floor retail.
Overview of Findings

• **Cost:** CRP and CEP cost $27.4 Million in 2017

• **Participation rates:** CRP 22% and CEP 1% max.

• **Effects:**
  – Downtown vacancy rates went down after 1995, but not because of CRP.
  – Employment numbers show a similar result.

• **Design:**
  – Participants already invest much more than the “minimum required physical improvements.”
Participation Requirements

Lease Terms & Physical Improvements

Small firms (# Employees < 125)
- 3 years or longer lease for both programs
- $5 Minimum Physical Improvement for CRP and $2.50 for CEP.

Large firms (# Employees > 125)
- 10 years or longer for both programs
- $35 Minimum Physical Improvement for CRP and $25 for CEP
  - (respectively, $10 and $5 for renewal leases)
CRP and CEP Benefits

- Property Tax Abatement
  - Minimum of applicants property tax per sq. ft. and $2.50
  - For 3 or 5 years with 2-year phase-out schedule
    - 10 years for Manufacturing in CEP
CRP and CEP Benefits

- Property Tax Abatement
  - Minimum of property tax per sq. ft. and $2.50
  - For 3 or 5 years with 2-year phase-out schedule
  - For 10 years for Manufacturing in CEP

- Commercial Rent Tax (CRT)
  - Only Part of CRP (Downtown Manhattan)
  - Tax base reduction equal to 100% of gross rent.
    - 1995-2005: 3 or 5 years with a last 2-year phase-out
CRP and CEP Costs in 2017

• Total Cost in 2017: $27.4 Million
  • Equivalent to paying 197 police officers per year

• Property Tax Abatement
  $18.4 million

• Commercial Rent Tax Reduction
  $9 million
EVALUATION
What were the goals?

• Does the law state the goals of these programs? No!

• Based on the testimonies and the design of the program, assumed CRP-CEP goals are:
  – Reduce vacancy rates
    • Short term: through CRP/CEP benefits
    • Long term: through building improvements
  – Increase employment

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To Evaluate

• Program Participation Rates
• Neighborhood Effects
  – Office Vacancy Rates and Rents
  – Employment Level
• Building/Lease Level Effects
  – Investment or Physical Change
  – Owners’ Rental Income
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- Are the programs meeting their goals?
- Are the goals still relevant?
- Are the programs efficient?
Haves and Have nots

DATA
Available Data

• **Neighborhood Office Rents and Vacancy Rates**
  – Cushman and Wakefield (1984-2016)

• **ZIP-Code by Industry Employment**

• **Buildings Sq. Ft., other exemptions, etc.**

• **Owners’ Rental Income**
CRP-CEP Applications Data

• CRP/CEP Applications
  – Haves:
    • 2010-17: Address, Lease term, Program Type, Expenditures, # Employees, Owner’s Name, Tenant's name, Office or Manufacturing
    • 1995-2010: Address, Lease term, Program Type
  – Have Nots:
    • Detailed records are destroyed for applicants prior to 2005.
    • For 2005-10 there are only hardcopies.
Data: Have-Nots

• Building Level Vacancy Rates
  – Source: Currently collected by DOF

• Establishment/Address level employment
  – Source: QCEW matched over time

• Income and Expense For all owners
  – Source: Real Property Income and Expense (RPIE)

• Other Limitations:
  – Commercial Rent Tax data did not record CRP Special Reduction
    • until 2017
    • No building level data
  – No consistent record of past Property Tax Abatements
    • They are only recorded on a rolling basis
ELIGIBILITY AND PARTICIPATION
Eligibility

Gross Sq. Ft. of Downtown Commercial and Mixed-Use Buildings by CRP Eligibility

Independent Budget Office of NYC
Participation Rates

The graph shows the participation rates from 1995 to 2017 for different programs:

- CRP-95 Participation Rate (green stars)
- CRP-05 Participation Rate (red dotted line)
- CEP Participation Rate (black dashed line)

The participation rate for CRP-95 shows a steady increase until around 2005, followed by a decline. CRP-05 has a lower and more stable participation rate throughout the years. The CEP participation rate is consistently lower than the CRP rates.
Participation/Eligibility - Summary

• The majority of downtown buildings are office space that were built before 1975.
  – About 12mn SQ feet were turned residential by 421-g
• The maximum CRP participation rate was 22%.
• Although number of CEP applications has recently grown, the participation rate is very low (1% at its highest).
Treatment and Control

• Basic Question:
  – what would have happened without these programs?

• Solution Concept:
  – Consider an experiment with “treatment” and “control” groups.
  – Compare the outcomes of the two groups.
OFFICE VACANCY RATES
Vacancy Rates vs. CRP Enrollment Rates in Downtown Manhattan

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Deviations from Historical Averages

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Vacancy Rates - Summary

• We do not observe any off-the-trend effects of CRP on vacancy rates.
  – Similar trends in other areas, including Hudson Waterfront in New Jersey.
  – Considering 1984-2001, our regression estimates show a very small negative effect which is statistically insignificant. That is no effect.
  – Similarly, no effects are found for office rents.
EMPLOYMENT
Employment: Downtown

Figure: CRP Region
Employment - Summary

• Again, very similar trends are found in Midtown.

• However, Downtown employment grew slower during 1995-2000.

• Industry composition matters a lot:
  – After controlling for industry composition, post-95 Downtown still grew at a slower rate.

• Similar results found for CEP employment.
  – Highly expected given the low participation rates.
PHYSICAL IMPROVEMENTS
Effect of $5 Minimum Expenditure Requirement (CRP Applications 2010-17)

<table>
<thead>
<tr>
<th>Expenditures Less than ...</th>
<th>Percent of Applicants</th>
</tr>
</thead>
<tbody>
<tr>
<td>$6 Per Sq. Ft.</td>
<td>20%</td>
</tr>
<tr>
<td>$10 Per Sq. Ft.</td>
<td>38%</td>
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<table>
<thead>
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<th>Expenditures Greater than ...</th>
<th>Percent of Applicants</th>
</tr>
</thead>
<tbody>
<tr>
<td>$35 Per Sq. Ft.</td>
<td>32%</td>
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</table>

- Their property tax benefits do not exceed $10 over 5 years.
- They are spending much more than minimum requirements ($5.00) and their benefits.
Effect of $2.50 Minimum Expenditure Requirement (CEP Applications 2010-17)

- They are mostly manufacturing applicants.
- $2.50 minimum expenditures are more significant in CEP areas.

### Percent of Applicants

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<th>Expenditures Less than ...</th>
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<tbody>
<tr>
<td>$3 Per Sq. Ft.</td>
<td>42%</td>
</tr>
<tr>
<td>$6 Per Sq. Ft.</td>
<td>63%</td>
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<th>Expenditures Greater than ...</th>
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<tr>
<td>$25 Per Sq. Ft.</td>
<td>11%</td>
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Physical Improvements in Tax Assessments vs. CRP-CEP Applications Data

Figure: CRP Investment Data vs. Property Tax Assessment Physical Improvements.

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CONCLUSIONS
Summary of Findings

• Downtown vacancy rates went down after 1995, but not because of CRP.
• Employment numbers show a similar result.
• Participation rate in CRP is 22% max.
• CRP and CEP cost $27.4 Million in 2017
Summary of Findings (Cont.)

- CRP $5 Minimum required investments are below the typical for most leases.
  - CEP $2.50 Minimum required investments are significant.

- The property tax assessments do not measure the CRP-CEP physical improvements.
  - We do not get a “return on investments.”
  - The collection effort varies by time and region
  - This limits further analysis of physical improvements
Further Considerations

• In recent years, Downtown office vacancy rates are very similar to midtown.
  – Downtown office space is newer
    • 421-g : Older buildings to residential
    • Market forces: Newer (post 1975) buildings to residential
      • A different industry mix from 1995
  • Participation rates in CRP are NOT countercyclical
    – Doesn’t look like a safety net.
Procedural Recommendations

- Include stated goals in the law
- Measurable Goals:
  - Tracking goals in data e.g. vacancy rates
- Retaining data of tax expenditure programs.
- Upgrading data collection procedures for the policy evaluations.