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**Testimony of George Sweeting**  
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**To the New York City Council Committee on Contracts**  
**On Intro 251-A, Fair Wages for New Yorkers Act**

**November 22, 2011**

Good afternoon Chair Mealy and members of the Contracts Committee. My name is George Sweeting. I am deputy director of the New York City Independent Budget Office. Thank you for the opportunity to testify at this hearing on the "Fair Wages for New Yorkers Act." As many of you know, our office does not take positions on policy matters. Because our role is to provide information and analysis, I am not appearing before you today as a proponent or an opponent of the legislation.

I will be discussing three points. First, despite questions raised in testimony from IBO and others last May, the final version of the Economic Development Corporation (EDC)-commissioned report continues to rely heavily on data from incentive projects that are not covered by the proposed legislation to model the impact of the proposal. Second, there is a need for more detailed language in the bill to make clear how benefits are to be tallied and which projects are covered. Third, I will present our estimates of the number and types of projects likely to be covered under the bill. That analysis suggests that between 42 and 48 of the projects initiated by EDC/IDA (Industrial Development Agency) in the years 2002 through 2008, or about six or seven per year, would have been covered by the legislation.

***Use of ICIP/ICAP in EDC Study***

Shortly before the hearing last May on a previous version of Intro 251, EDC released the executive summary of a study the city commissioned from Charles River Associates (CRA) to evaluate the economic impact of the legislation. At the time, IBO and others noted that the study relied on data from projects receiving benefits under the Industrial Commercial Incentive Program, or ICIP, which was the city's largest single property tax expenditure for economic development. (ICIP had already been replaced by the Industrial Commercial Abatement Program, or ICAP, which curtailed some benefits available under ICIP and also limited the tax effects by transforming it from an exemption to an abatement.)

Even last spring it was clear that ICAP projects would not be subject to the living-wage provision because existing state law would not allow the city to change the eligibility rules for this program. The city's property tax is set in state law and therefore property tax exemptions must

also be established by state law. Unless specifically stated, the city is not authorized to add additional requirements, such as a living-wage provision, beyond those spelled out in the state law establishing the specific exemption program. For this reason, we were surprised to see that the study used ICIP projects to estimate the impact of the living-wage proposal on real estate development.

The full study has now been released and it continues to rely on ICIP projects to model the effect of the proposed legislation on economic development decisions by developers. Given the differences in the types and scale of projects receiving ICIP/ICAP and those more likely to be covered by the living-wage provisions (ICIP projects are smaller, more disbursed outside Manhattan, and more likely to include retail use) it is questionable whether the results of the Charles River analysis are applicable to the living-wage case.

### ***Defining Who is Covered***

As Intro 251 has worked its way through the legislative process, there have been changes intended to narrow the types of projects and tenants that would be subject to the living-wage requirement. The current draft of the bill includes language reflecting these changes, but there are some sections in the bill where further clarification will be needed.

The most important issues concern how the benefits are tallied when applying the \$1 million test for whether the living-wage provision will apply to a project. First, the current draft of the legislation does not specify how the value of tax exempt bond financing assistance will be measured. There are at least three alternatives available:

- the face value of the bonds issued
- the estimated cost to the city budget of providing the tax-exempt financing, which is the benefit reported in the Economic Development Corporation's *Annual Investment Projects Report*—better known as the Local Law 48 report, or
- an estimate of how much the use of tax exempt financing saved the developer.

Using the face value would overstate the assistance, since the developer gets reduced cost financing, not free financing. Presumably the intent is to use something closer to one of the other options, but the draft is silent on this question.

Tax-exempt bonds benefit developers by allowing them to issue bonds at a lower interest rate than if they used taxable financing because investors are willing to accept the lower rate in exchange for exempting the interest income on the bonds from federal, state, and local income tax. IBO has estimated that the taxable bond rate that yields equivalent after tax income is at least 50 percent higher than the tax-exempt rate for investors who are New York City residents. The rate differential depends in part on investors' marginal tax rates, with those in the top bracket receiving the largest benefit from holding tax free bonds. Thus, the higher the marginal rate, the higher the comparable taxable rate would need to be. In contrast to IBO's estimate of a 50 percent differential, EDC assumes that the taxable rate would be 24 percent higher in calculating the cost to the city budget for Local Law 48 report purposes.

When estimating the value of tax exempt financing there are big differences between the cost to the city (the second alternative) and the benefits to the developer (the third alternative). To give a rough sense of the difference in the size of the calculated benefits under the two measures consider the following example. A project receiving \$5 million in tax exempt bonds would be estimated by EDC to cost the city about \$51,000 in foregone tax revenue (an estimate of the value in today's dollars). Based on our calculation, the interest savings to the developer, assuming a tax-exempt interest rate of 6 percent would be \$1.8 million, if a comparable taxable rate were 50 percent higher than the rate on the tax-exempt bonds. Both calculations assume 30-year, fixed-rate bonds.

The legislation does not make it clear which calculation should be used, although the Local Law 48 reports do provide the EDC measure if that is preferred.

A second question with how benefits will be tallied is whether the calculations are to be done using present values or nominal values. Present values take into account the time value of money by applying a discount to future values. The issue is particularly important when bond financing and other long-term assistance is involved. Most economic development analysis is done using present values but the bill does not specify which is to be used.

A third question in tallying the benefits is how the financial assistance in discounted land sales and discounted energy prices are to be estimated. Finally, it is not clear whether the legislation is intended to include state and federal assistance as well as city assistance when tallying the total benefits received, in the case where the city and/or its economic development organization has the authority to confer state and federal benefits.

A different type of definitional question concerns the exclusion of manufacturing firms from the provisions of the bill. There is no formal definition of manufacturing using either descriptive terms or reference to federal industrial classification systems. Moreover, while the bill excludes a project from the living-wage provision when "the primary industry conducted at the project location is manufacturing," that language suggests that in the case of a manufacturing firm that has a city-assisted project where the primary work involves warehousing and shipping those workers would be covered. Were such support functions intended to be exempt if the firm is primarily a manufacturing business?

If the legislation moves forward, it may be desirable to designate a single city agency or official to determine whether individual projects meet the criteria to be covered. Another alternative would be to amend the requirements of Local Law 48 to provide all of the data that would go into such a determination. It should also be noted that the values in the EDC report can change from year to year, particularly as projects are completed and operations begin. But, what happens if a developer's assistance meets the threshold at the start but upon more data being available falls below. Or conversely, if a project's benefit ends up being greater and they cross the threshold a few years after receiving the benefit. Is the determination intended to be made just once at award or reassessed annually?

### ***How Many Projects Could Be Affected***

Large numbers of projects that receive significant financial assistance from the city and its financial- assistance entities would be excluded from the living-wage provisions under the current draft of the bill. These include benefits granted as of right such as ICAP, 421-a, and J-51; small businesses, particularly tenants in new commercial developments, with gross revenues of less than \$5 million; not-for-profit entities receiving assistance to develop their own facilities (although their tenants may be subject to the requirements) and affordable housing developers. Another set of excluded projects are those where state entities such as the Empire State Development Corporation and the Liberty Development Corporation are the leading government economic development entity. Thus, to cite one example, Atlantic Yards would not have been covered. The bulk of covered projects are likely to be projects that are currently included in the Local Law 48 reports exclusive of manufacturing and nonprofits.

IBO estimates that a total of 42 projects started in 2002 through 2008 would have met the threshold of receiving \$1 million in assistance. This estimated is based on the cumulative benefit reported in the Local Law 48 report from 2009—which uses EDC’s method of calculating bond-financing assistance. That’s an average of six projects a year. In 2009 and 2010, with the recession dampening development, no projects met the criteria. Although we could readily exclude manufacturing and nonprofit projects, based on the EDC funding program reported in the Local Law 48 data, we could not readily identify small businesses, and so this may be an overestimate.

Of these projects, 16 were in Manhattan (nearly 40 percent), 10 were in Brooklyn (nearly one-fourth), eight were in Queens (nearly 20 percent), seven were in the Bronx, and one was in Staten Island. There is fluctuation across years. There were just two projects in 2008 and three projects in 2006, but nine projects in 2005 and eight projects in 2002, 2004, and 2007.

Nine of the projects, mainly in the Bronx, Brooklyn, and Queens were wholesale food and drink distributors, while six other projects were not food distributors. There were six projects for companies in financial and business services, all in Manhattan, including assistance to the American Stock Exchange, NASDAQ, Ernest and Young, and the Bank of America. Office building projects totaled five: 7 World Trade Center, the New York Times building, One Bryant Park, and Metrotech in Brooklyn. There were three projects in the information sector (IAC/InterActiveCorp, New York Post, and Hearst Corporation) and three in shipping/cargo (such as FedEx). There were two projects in each of the following: retail developments (the Terminal Market and the Related Hub, both in the Bronx); local airports (American Airlines and Aero at JFK); and sports stadiums (Yankee Stadium and Citifield).

In terms of the value of the assistance in 2009, as reported by EDC, the largest financial assistance recipients were American Airlines (\$77 million), Yankee Stadium (\$59 million), Bank of America (\$50 million), the Hearst Corporation (\$34 million), and Citifield (\$30 million). However, because most the deals were smaller financial assistance packages, the average benefit was \$10 million and the median benefit was less than \$4 million.

Using the alternative definition of bond-financing assistance that estimates the savings to the developer, IBO found that an additional six projects would have been covered by the living-wage bill (exclusive of other benefits that the companies received). These six projects included two retail developments (East River Plaza and East Harlem Automall), two airlines (Continental and Jet Blue), one office building (Bank One Tower in Brooklyn), and the W Hotel in downtown Manhattan.

In summary, IBO found that the final version of the EDC-commissioned study continued to rely on data from projects that will not be covered by the living-wage law to estimate the economic development impacts of the proposal; that the legislation has a number of key provisions that merit clarification and more thorough definitions; and that applying what we understand to be the intent of the legislation, a total of 42 to 48 projects from all those initiated by EDC/IDA between 2002 and 2008 would have been covered by the legislation, with the range depending on how bond-financing assistance is defined.

Thank you again for the opportunity to testify, and I would be happy to take your questions.