

Unintended Consequences: New Absentee Landlord Tax Will Hit Poorer Neighborhoods Hardest

The recently adopted city budget for 2004 includes a new surcharge for absentee landlords who rent out their one- to three-family homes. The Mayor's budget office expects the surcharge to garner \$44 million in 2004. A new analysis by IBO finds that the properties affected by the surcharge are more numerous than estimated by the Mayor's office. Moreover, because absentee landlord properties are not spread evenly across the city, the impact of the tax increase—about \$570 on average—will be felt disproportionately in some neighborhoods. IBO found them to be concentrated in neighborhoods where households have relatively low incomes and African Americans and Latinos are a large share of the residents.

East New York, Bedford-Stuyvesant, and Bensonhurst have the largest number of one- to three-family homes with absentee landlords. Each of these neighborhoods has more than 3,400 properties that may be subject to the surcharge. Because few of the properties facing the surcharge are covered by rent regulations, landlords will be free to try to pass on much of the burden of paying the new tax to their tenants.

Under New York City's property tax system, owners of one- to three-family homes generally pay less tax as compared to the market value of their properties than do owners of apartment, commercial, and other types of buildings. This lower tax burden for one- to three-family homes, which make up the majority of properties in Tax Class 1 of the city's multilevel system, was put into place as a way to encourage homeownership. The new surcharge—an additional payment equaling 25 percent of the regular tax bill—reduces that preferential treatment if instead of living in the house the owner rents it out as an income-producing property.

How Many Homes? The city has not previously documented the number of class 1 properties that are not owner occupied. This means the city's Department of Finance will have to commit considerable time and effort to determine which properties are actually subject to the new tax.

One analysis presented last spring using 1999 Housing and Vacancy Survey data estimated that there are 75,000 class 1 houses owned by absentee landlords. (New data from the 2002 Housing and Vacancy Survey recently became available. Preliminary analysis using the new survey shows approximately 103,000 class 1 houses with absentee landlords.) Although the Housing and Vacancy Survey contained information on owner occupancy, the survey is based on a relatively small sample of households. An alternative approach is to use the 2000 census, which is based on a much larger sample and can therefore yield a more reliable estimate.

Also available...

Understanding
New York City's
Budget: A
Guide

...at www.ibo.nyc.ny.us

**New York City
Independent Budget Office
Ronnie Lowenstein, Director
110 William St., 14th floor
New York, NY 10038
Tel. (212) 442-0632
Fax (212) 442-0350
e-mail: ibo@ibo.nyc.ny.us
<http://www.ibo.nyc.ny.us>**

Although the census does not include an explicit question about owner occupancy, it is possible to estimate the number of properties without owner occupants in each of the city's 2,217 census tracts.

IBO's analysis of the 2000 census data indicates that the number of one- to three-family homes with absentee landlords may be as high as 130,400. For major property types we estimated percentages of the non-owner occupied properties in each census tract and then applied those percentages to similar property types on the city's 2003-2004 tax assessment roll in each tract. Based on IBO's estimate of the number of affected properties, the new surcharge will raise \$76 million in revenue—\$32 million more than the Mayor's budget office expects.

Where Absentee Landlord Homes Are Concentrated

By Number of Class 1 Properties

East New York	3,882
Bedford-Stuyvesant	3,509
Bensonhurst	3,469
Jamaica	3,457
Canarsie	3,389

By Percentage of Class 1 Properties

Williamsburg	49%
Corona	49%
Mott Haven	48%
Concourse	47%
Bushwick-Ridgewood	42%

SOURCES: IBO, 2000 Census.

NOTE: Percentage ranking based on at least 500 one- to three-family homes in the neighborhood.

Tax Class Fix? Part of the rationale behind the new surcharge is to bring the tax burden on absentee landlords with Tax Class 1 properties closer to the burden faced by the owners of four- to six-unit apartment buildings that comprise Tax Class 2A. Based on the finance department's estimated market values on the 2003-2004 assessment roll, the median effective tax rate in class 2A is more than four times higher than in class 1—\$3.02 per \$100 of market value versus \$0.70 per \$100 of market value. While reducing the tax advantage for class 1 absentee landlords may be a reasonable goal, the complexity of the city's property tax system makes it difficult to adjust one inconsistency in isolation of others.

For example, the distinction between three-family and four-family houses is somewhat arbitrary. There are certainly instances of owners residing in one apartment of a four-family house who face much higher tax burdens than do those in three-family houses. Partly because of this higher tax burden, the median sales price of four-family houses has been virtually

identical to the median price of three-family houses in recent years.

Moreover, the difference in tax burdens between class 1 and class 2A may not be as large as some comparisons suggest. The city assesses these two types of properties using different methods: class 1 property is assessed using sales data while the market value of class 2A property is estimated using an approach based on future income streams. When IBO estimated the effective tax rates of four-family homes using 2001 and 2002 sales data, the difference in tax burdens between class 1 and class 2A narrowed substantially—\$0.70 per \$100 of market value for the median three-family home versus \$1.16 per \$100 of market value for four-family buildings.

Some of the properties that are now subject to the surcharge were deliberately moved into class 1 about 10 years ago in order to ease the growth in owners' future bills. These are small, mixed-use buildings with two or three units, often called "moms and pops." With a store on the ground floor and apartments above, these properties are common in the boroughs outside Manhattan. Because they had higher tax burdens when they were shifted from Tax Class 2A and they have not had the benefits of class 1 treatment for as long a time, the mixed-use properties already face much higher tax burdens than do the typical two- or three-family houses. The median effective tax rate on three unit mixed-use buildings is \$0.98 per \$100 of market value compared with \$0.70 for a three-family house. Although mom-and-pop owners start out with higher tax burdens, they will face the same 25 percent surcharge as other absentee owners.

Different Neighborhoods, Different Impacts. IBO's analysis of census data indicates that absentee landlord properties are not spread evenly throughout the city. So the impact of the surcharge will be felt differently in different boroughs and neighborhoods. Properties owned by absentee landlords tend to be found in lower income areas and neighborhoods with high concentrations of households headed by African Americans, Latinos, and other minorities.

Looked at on a boroughwide level, Brooklyn and Queens have an overwhelming share of the properties affected by the surcharge—together they account for 80 percent of the one- to three-family homes that are not owner occupied. Not surprisingly, the neighborhoods with the most class 1 absentee landlord houses are in these two boroughs.

East New York has the most properties affected by the surcharge, with 3,882 class 1 absentee landlord houses. It is

followed closely by Bedford-Stuyvesant with 3,509, Bensonhurst with 3,469, and Jamaica with 3,457. All of the 11 other neighborhoods in the city with 2,000 or more properties subject to the surcharge are located in Brooklyn and Queens.

Census Tracts with the Fewest Absentee Landlords Have Highest Average Incomes

Absentee Landlord Ranges	Average Income	Percent Non-White
Lowest (0-19.5%)	\$72,682	35.3
Second (19.5-29.3%)	61,887	50.7
Third (29.3-44.3%)	50,813	65.0
Highest (44.3-100%)	48,657	70.0

SOURCES: IBO, 2000 Census.

NOTE: Absentee landlord ranges refers to census tracts by percentage of absentee landlords for one- to three-family houses.

Likewise, these two boroughs also have many of the neighborhoods with the highest percentages of class 1 homes that are owned by absentee landlords. In both Williamsburg and Corona, 49 percent of the one- to three-family homes are not owner occupied. Among the neighborhoods with the most properties subject to the surcharge, 31 percent of East New York's class 1 properties have absentee landlords, 35 percent in Bedford-Stuyvesant, and 23 percent in Bensonhurst.

The concentration by income and race and ethnicity can be most specifically seen through an analysis of census tracts, which are smaller geographic areas than neighborhoods. IBO

divided the city's 2,217 census tracts into four groups based on the percentage of class 1 houses owned by absentee landlords. In the quarter of census tracts with the highest percentage of absentee landlords, the average household income was \$48,657. In the quarter with the lowest percentage, the average income was \$72,682. Similarly, the groups of census tracts with the highest percentage of absentee landlords also had the most households headed by nonwhites: 70 percent versus 35 percent in the census tracts with the fewest absentee landlords.

Who Pays? Property owners do not bear the entire tax burden. At least a portion of the surcharge will pass through to the tenants in these properties. How much is ultimately borne by the tenants will depend on market conditions. Very few of the apartments in Tax Class 1 houses are subject to rent regulation, so landlords will have flexibility in determining how much of the surcharge they can try to shift to tenants; how much can be shifted will ultimately depend on local housing markets.

For this year the surcharge equals 25 percent of a property's regular tax bill, or about \$570. The legislation passed in Albany enabling the city to implement the new tax allows the surcharge to rise to 50 percent next year. However, under the local legislation establishing the surcharge it will remain at 25 percent, and the city's current Financial Plan for 2005 does not anticipate that increase will occur.

Written by George Sweeting