New York Tax Uncertainty

By Joel Marcus, Esq.

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The future of New York City's 421-a tax exemption is highly uncertain, particularly in light of the election of Mayor Bill de Blasio, whose initiatives appear to call for sweeping changes to the program.

The 421-a program, which is scheduled to expire on June 14, 2015, provides substantial real estate tax exemption benefits for the developers of new multifamily buildings. Currently, the city determines the level of exemption provided to an eligible building under 421-a; that determination is based on a geographical and functional basis.

That could change under de Blasio's proposed "Five-Borough, 10-Year Plan." The proposal, relating to the creation or preservation of 200,000 units of affordable housing, frequently references the 421-a program, alluding to its future presence in the real estate market.

The city created the 421-a program in 1971 to encourage multifamily construction by granting a partial tax exemption for the property owner. In 2008, changes to the program had a prospective effect on 421-a projects. These modifications included a dramatic expansion of the Geographical Exclusion Areas (GEA), in which properties must meet additional requirements to qualify for an exemption. The amended laws eliminated as-of-right, or automatic, benefits for new multifamily construction throughout Manhattan. In addition, significant sections of the outer boroughs became part of the GEA, effective for buildings that commenced construction after June 30, 2008.

The law created exceptions for projects within the GEA to obtain a tax exemption. To qualify, at least 20 percent of the units must be affordable to families whose income at initial occupancy does not exceed 60 percent of the area median income adjusted for family size. In addition, projects located in a GEA could qualify for benefits via the purchase of negotiable certificates. Under the negotiable certificates program, affordable housing developers can sell negotiable certificates to market-rate developers, who use the certificates to access tax abatements.

Hints of change

Based on Mayor de Blasio's proposal, the percentage of affordable housing required per project may increase to provide for more affordable units.

The proposal highlights the establishment of a new, mandatory Inclusionary Housing Program, which will serve a broader range of New Yorkers with varying income levels. The Inclusionary Housing Program offers an optional floor area bonus to developers of new residential buildings, in exchange for the creation or preservation of affordable housing.

The new residential housing can be onsite or offsite, so long as it is within the same community board jurisdiction or within a half-mile radius of the site receiving the floor area compensation. The program seeks to promote economic integration in areas of the city undergoing significant new residential development. In order to qualify under the current Inclusionary Housing Program, the affordable units must be affordable to households at or below 80 percent of the area median income.

In contrast to the current Inclusionary Housing Program, some observers speculate that the mayor's proposed program would require all developers to put aside at least 20 percent of their units for low-income families. These units would then remain permanently affordable.

Currently, developers are able to layer 421-a benefits on top of inclusionary housing benefits, therefore allowing developers to take advantage of both programs. By allowing this double-dipping of benefits, the city creates a greater incentive for developers to provide onsite affordable housing.

However, de Blasio's plan may change the way developers use multiple subsidy programs together. The proposal states that in situations where a developer pursues multiple subsidies, the city will increase the percentage of affordable units required for eligibility and/or require that the developer provide deeper affordability.

No automatic exemptions?

Some observers have speculated that the mayor's plan may expand the GEAs of the city and reduce, if not completely eliminate, any as-of-right areas for 421-a construction. As Manhattan is already a GEA, this proposal would affect those areas in the outer boroughs that were not classified as GEAs in 2008. Moreover, developers in the expanded GEAs would be required to provide a higher percentage of affordable units (some proposals call for as much as 50 percent affordability) and offer apartments to families at 40 percent to 50 percent of area median income.

Proposed changes to the program also include eliminating some of the strict requirements that developers must meet in order to receive a 421-a Certificate of Eligibility. For example, under the current program, a qualifying property must meet one of the following three conditions:

- All affordable units must have a comparable number of bedrooms to the market rate units, and a unit mix proportional to the market rate units. Or
- At least 50 percent of the affordable units must have two or more bedrooms, and no more than 50 percent of the remaining units can be smaller than one bedroom. Or
- The floor area of affordable units is no less than 20 percent of the total floor area of all dwelling units.

Mayor de Blasio's proposal seeks to modify or eliminate what the administration terms "inefficient regulations," since existing requirements may force developers to build larger units than the market dictates.

Overall, the filing process to receive a Certificate of Eligibility is time consuming, due to regulations such as the unit distribution requirement. Mayor de Blasio's proposal states that it seeks to "streamline the 421-a program, improving its usefulness to developers and its ability to promote affordability, by eliminating outdated and unnecessary programmatic, eligibility, and oversight requirements."

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