Testimony Submitted to the New York State Assembly Standing Committee on Real Property Taxation on New York City's Real Property Taxation System

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I am Carol Kellermann, President of the Citizens Budget Commission (CBC). Established in 1932, CBC is a nonprofit, nonpartisan civic organization dedicated to improving the financial management and service delivery of New York State and New York City.

I appreciate the opportunity to share with you CBC's thoughts on the flaws in the New York City property tax and how to improve it. It is appropriate for a State legislative committee to explore these issues because the City's property tax is structured by State law. State law codifies and perpetuates the basic problems, and State law could go a long way toward fixing them.

My testimony today will focus on the flaws in the treatment of residential properties.

The most significant issues are:

1. ***Among residential properties, rental buildings— occupied by those who typically are less able to afford it— are taxed more heavily than single family homes.*** The effective tax rate for most rental buildings is more than four times that for a single family home.[1] This preferential treatment is also extended to owners of cooperatives and condominiums in larger buildings.[2]

   Some might find this difference in tax burdens appealing because they believe landlords of rental buildings pay the taxes from their profits, but this is a questionable assumption. In the New York City rental market, landlords are often able to pass on the cost of tax increases to their tenants. This does not happen immediately, but tax increases are reflected in rent increases sought when leases are renewed or apartments become vacant. For rent-regulated apartments (about 60 percent of all rental units), property tax levels are one of the major factors considered in determining allowable rent increases.[3] Therefore, much of the higher tax burden on rental properties is borne by renting families. While the amount varies, property taxes are equal to about one-fifth of the rent on average among New York City rental apartments.[4]

Not surprisingly, homeowners are better off economically than renters. The median household income of renters in New York City in 2013 was $41,500; the median for homeowners was nearly double that, $80,000. About 21 percent of renters had income below the federal poverty threshold compared to 8 percent of owners.[5]

Overall the economic position of homeowners is much better than that of renters; taxing renters at higher rates is inappropriate for millions of families.

2. ***Within the two subgroups of residential properties— small homes and large rental buildings— property tax rates vary widely for somewhat arbitrary reasons and with adverse impacts on those least able to pay***. The tax rates that I have used to make the previous point are average rates for the different types of properties. You might reasonably think that all properties within each category are subject to the same effective rate, but this is not the case. For homeowners the effective rate varies from near zero to about $3.10 per $100 of market value; for large rental buildings the rate varies from near zero to about $5.95 per $100 of market value. [6] Why are owners of the same type of property subject to different tax rates?

   The answer lies in the good intentions of state lawmakers gone awry. In order to protect owners and renters from the impact of large and unexpected increases in their tax bills, the state law contains provisions known as "caps" and "phase-ins." Caps limit the percentage increase in a tax bill (technically in the assessed value) each year; phase-ins require that the increase in taxes (again, technically in assessed value) be spread over a multiyear period with the increase in any single year limited to a share of the full increase.

   The practical impact of the caps and phase-ins is that property tax bills for homes and apartments for which market values are growing significantly are less than they would be otherwise. Since many New York City property values increased notably in recent years, these provisions have a significant impact. For fiscal year 2015 the estimated property tax revenue forgone was about $1.5 billion due to caps for homes including cooperatives and condominiums, and more than $2.0 billion due to phase-ins for rental buildings.[7]

   Protecting families from economically troubling, sudden increases in housing costs is a worthy policy goal, but the current caps and phase-ins pursue it in a highly unfair manner. The largest benefit goes to those whose homes are experiencing the most favorable market trends; little or no benefit goes to those whose housing value is not growing rapidly. In New York City this means the bulk of the benefit goes to higher income families living in the most desirable neighborhoods, and little benefit goes to lower income families living in neighborhoods where housing values are stagnant or declining. To illustrate, a study using fiscal year 2013 data found that homeowners on the Upper East Side of Manhattan had a median annual income of $146,500, and the median income of a homeowner in Morrisania in the Bronx was about $40,000; yet the typical one- to three-family home on the Upper East Side received a tax benefit of more than $36,000 from the cap provisions while in Morrisania the tax benefit from the cap provision was merely $1,075. A policy that works in this inequitable fashion needs improvement.[8]

Please note that in identifying the major problems with the New York City property tax, I have **not** argued that the tax is too high. In the aggregate, New York City relies less heavily on property taxes than most large cities, and its tax on homeowners is unusually low. The overall tax burden is high in New York City because of other taxes, notably the personal income tax on residents. Accordingly, the solution to the problems identified is not necessarily lower aggregate property taxes; it is fairer and more economically efficient property taxes.

Change in state law should follow two policy directions in order to promote a better system:

1. ***Require a multiyear, phased-in narrowing of differences in effective tax rates among types of property.*** The rates for rental units and homeowners should be the same; this is likely best accomplished gradually over a period of 10 or more years, but it will happen only if mandated by State law.

2. ***Overhaul the provisions for caps and phase-ins to be more equitable.*** The greatest benefits should go to those least able to adjust to an increase in their tax bill, and not to those with the greatest gain from market trends. Greater reliance on "circuit breaker" type provisions that link property tax credits to household income can help toward this end and can be incorporated in state income tax law.

I hope you find these facts, observations, and recommendations helpful. CBC would be happy to work with the Committee by answering any questions and providing further information. A copy of a 2013 CBC report describing the issues summarized here in greater detail is attached to this testimony.

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[1] Citizens Budget Commission, *5 Year Pocket Summary*, "Table 4: City of New York Real Property Tax" (February 2015).

[2] Citizens Budget Commission, *The Most Important Economic and Fiscal Decisions Facing the Next Mayor*, "Options for Property Tax Reform: Equitable Revenue Raising Reforms for New York City's Property Tax" (prepared by Andrew Hayashi, December 2013), www.cbcny.org/sites/default/files/Interactive/2013_Conference/REPORT_PropertyTaxes_12062013.pdf.

[3] New York City Rent Guidelines Board, *Housing NYC: Rents, Markets & Trends 2015*.

[4] Based on data for rent-stabilized buildings found in New York City Rent Guidelines Board, *Housing NYC: Rents, Markets & Trends 2015*, "Appendix C.1," "Appendix C.2," and "Appendix C.3.")

[5] New York City Rent Guidelines Board, *Housing NYC: Rents, Markets & Trends 2015*, "Appendix C.1," "Appendix C.2," and "Appendix D.2."

[6] Citizens Budget Commission, *The Most Important Economic and Fiscal Decisions Facing the Next Mayor*, "Options for Property Tax Reform: Equitable Revenue Raising Reforms for New York City's Property Tax" (prepared by Andrew Hayashi, December 2013), p. 17, www.cbcny.org/sites/default/files/Interactive/2013_Conference/REPORT_PropertyTaxes_12062013.pdf.

[7] Citizens Budget Commission, *The Most Important Economic and Fiscal Decisions Facing the Next Mayor*, "Options for Property Tax Reform: Equitable Revenue Raising Reforms for New York City's Property Tax" (prepared by Andrew Hayashi, December 2013), p. 17, www.cbcny.org/sites/default/files/Interactive/2013_Conference/REPORT_PropertyTaxes_12062013.pdf.

[8] Citizens Budget Commission, *The Most Important Economic and Fiscal Decisions Facing the Next Mayor*, "Options for Property Tax Reform: Equitable Revenue Raising Reforms for New York City's Property Tax" (prepared by Andrew Hayashi, December 2013), pp. 21-22, www.cbcny.org/sites/default/files/Interactive/2013_Conference/REPORT_PropertyTaxes_12062013.pdf.