

# Real Estate NEW YORK

## Property & the Law

By Michael Bailkin

### New Direction Can Boost Development

It is no secret that New York City's two most important industries, financial services and real estate, have been crippled by the economic downturn and credit freeze. More recently, the New York development industry has been in free fall, with wholesale layoffs of critical personnel. If development is not stimulated, New York will not only lose revenues, but the industry's critical mass will be eroded as well, crippling it for the future.

Ingenuity and new direction can help save the day. Take the state and city's incentive programs, for example. Such programs are too often underutilized. Developers need capital, and through creative financing and the cooperation of local and state government, we can refuel the lifeblood of a core industry.

The existing primary incentive programs are as of right and are discretionary. The primary as-of-right programs are ICAP and REAP. ICAP provides real estate tax abatement on post-development increases for up to 25 years. REAP generates cash rebates and city income tax credits up to \$3,000 per job per year, for up to 12 years.

These programs, while valuable, have their limits. ICAP is available only in the outer boroughs (and in Manhattan for commercial

At the same time, these programs provide cost reductions or offsets, not capital. Even the new federal stimulus program (so-called Renovation Zone Facilities Bonds), which gives the city an allocation of \$121.7 million of tax-exempt authorization, does not provide direct capital or increased loan amounts. It only reduces rates.

The critical need for the industry continues to be capital, particularly subordinated loans. Private lenders are considering first-lien loans, but only at low loan-to-value ratios. If the city/state generated loans for 25% of project costs, developers undoubtedly could obtain the remaining 75%.

The city and state can also use their powers to leverage capital. Given fiscal limits to using direct city/state funds and constitutional prohibitions against the use of city/state credit to guarantee private loans, the best approach is to utilize existing programs in more creative ways. There are a number of possibilities, but the following three potential approaches for capital stand out:

**Tax Increment Financing:** New York can provide a TIF equivalent through NYCIDA, which can issue revenue bonds for private investors based on projected real estate taxes, using PILOT to collect the taxes and pay the bondholders. Assuming taxes of \$20 per square foot, \$300 per square foot in project capital could be raised. Here, the city should get subordinated mortgage payment equal to the taxes.

**HUD 108:** HUD can provide subordinated loans to developers at very low rates. A locality can authorize aggregate loans of five times its annual CDBG allocation. This gives New York capacity for \$1.25 billion of 108 loans that could leverage \$5 billion of projects. The primary impediment is that if a developer defaults, HUD offsets it from these CDBG allocations. A potential cure is a private guarantee fund to backstop a pool of loans.

**Direct Sources:** At least two existing sources, JDA and MERF, could be expanded. While JDA loans are limited to companies, loans to tenants for fit-out work could reduce a developer's capital requirements; in commercial condo projects, JDA loans could also be used for the purchase price. Since MERF funds are provided by the Port Authority of New York and New Jersey, there are fewer fiscal restraints for their expansion.—RENY

*The views expressed here are those of the author and not those of Real Estate New York.*

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renovation). REAP is available in the outer boroughs and in Lower Manhattan if most of the jobs come from outside the city. However, with rentals in Manhattan at a low point, these programs are currently less attractive.

Discretionary programs also have limited impact. The primary vehicle here is the New York City Industrial Development Agency. The "standard" NYCIDA package for private projects provides sales tax abatement on construction materials and initial equipment, as well as a mortgage-recording tax abatement. For most projects, this generates savings in the range of 4% to 6%. NYCIDA is empowered to increase benefits by extending sales tax abatements and providing PILOT for projects not eligible for ICAP. However, NYCIDA uses this option conservatively.