Abating Inequality

Rents, Wages and Renewal of the 421-a Housing Tax Exemption

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This report was produced as an independent assessment of public policy and does not represent the views of anyone except the author.

Summary

Two key city programs designed to address the scarce supply of rental housing and rising rents in New York City -- rent regulation and the 421-a tax exemption program -- expire on June 15, 2015, unless renewed by the New York State Legislature. This report focuses on the 421-a program and its effectiveness in advancing Mayor de Blasio's commitment to fighting income inequality by building affordable housing "on a grand scale."

The de Blasio Administration proposed in early May 2015 to revise the affordable housing requirements for developers who receive 421-a tax breaks and apply affordability requirements citywide. The Administration expects that with its proposed changes, the number of affordable units built under the program would double from 12,400 to more than 25,000 over the coming decade.

This report concludes that the 421-a program could create ten to twenty thousand additional housing units for low-income families over the next decade by including an off-site option for construction of affordable units. An off-site option would allow developers in high-cost Manhattan neighborhoods to build a larger number of affordable units in certain other areas, taking advantage of lower land and construction costs outside of Manhattan. This large expansion in the number of affordable units available to low-income New Yorkers would enhance the program's effectiveness in fighting income inequality. An off-site option would also place the housing closer to where nearly three-quarters of low-income families currently live, and expand the number of families served by the program. An off-site option can readily be structured so that affordable apartments are located in areas that are safe and provide good access to jobs, schools and neighborhood services, important goals of the program.

The report also recommends that a revised 421-a program should be designed to guarantee that developers in high-rent areas such as Manhattan and western Brooklyn and Queens provide affordable apartments for low-income families (those with incomes below 40 percent or 60 percent of the New York area median income, which translates to $31,100 and $46,600, respectively, for a family of three) and foreclose the possibility that developers in high-rent areas opt to serve primarily middle-income families, which would dilute the program's effectiveness in addressing income inequality.

Third, the report concludes that the 421-a program should <u>not</u> require prevailing wages for construction workers, as construction unions have proposed. Doing so would raise costs, reduce the amount of affordable housing produced, and undercut the effectiveness of the program in addressing the effects of income inequality in the city.

Introduction

In a city with notoriously scarce and expensive housing, housing cost and availability is an issue that reaches into nearly every neighborhood. Housing costs and scarcity lead prospective renters and buyers to bring checkbook in hand as they hunt for apartments, ready to make an immediate offer if they find something they like. Similarly, a topic of conversation for any newcomer to New York is where they will live, a conversation that takes as its starting point that the choices will be constrained by the stresses of finding a place and the trade-offs between neighborhood amenities, length of commute and cost. Indeed, public opinion polls consistently find that housing and rents are among the most critical issues to New Yorkers, along with the economy and public safety.[1]

Housing pressures have intensified over the last decade as rents marched steadily upward, even during the financial crisis and ensuing recession, while household incomes of New Yorkers shrank. The aftermath of the financial crisis brought a little-noticed if ignominious milestone: since 2009, the majority of renters in the city have paid more in rent, as a percentage of their incomes, than is generally considered to be affordable. U.S. Census Bureau surveys show that 53% of renters paid more than 30 percent of income in rent in 2013, up from 49% in 2008 and 42% in 2000. Thus, housing affordability is officially a problem for the majority of renters, who comprise two-thirds of all households in the city.

As much as it affects people across the income spectrum, the cost of housing is a much more intensive problem for lower-income families and households. Households with incomes less than 60 percent of the New York area median income[2] pay, on average, 51 percent of their income in rent. By contrast, those with incomes in excess of 130 percent of area median income pay only 15 percent of their income in rent.

Two key city initiatives designed to address the combination of high housing costs and scarce supply expire on June 15, 2015, unless renewed by the New York State Legislature. Best known are the city's rent regulations, which include rent control and rent stabilization, both designed to constrain the increase in rents resulting from inadequate housing supply for the city's growing population. The second program is known as 421-a, which provides tax breaks for new construction in order to spur expansion of the city's housing stock, thus reducing rent pressures. Since the mid-1980s, the 421-a program has also included requirements for affordability of 20 percent

[1] See, for example, the Quinnipiac University poll of New York City residents in which 20% named the economy as the most important issue facing New York City, 13% named housing and 12% naming crime. Quinnipiac University Poll, "Release Detail," Nov. 19, 2014.

[2] Consistent with the 421-a program, incomes are expressed as a percentage of the metropolitan area's median income, adjusted for household size.

of newly constructed units in certain geographic areas, intended to directly address the lack of affordability for lower-income families and households.[1]

As the June 15 expiration date has approached, debate has focused on the 421-a tax exemption program due to the widespread criticism of the program as it stands in current law. This report also focuses on 421-a for this reason, and also due to its pricetag -- $1.1 billion annually in foregone tax revenue -- and its implications for addressing the intersection of income inequality and housing.

It is important to evaluate the 421-a tax exemption program in the context of income inequality for several reasons. Rents are the largest single expense for low-income families, and thus critically affect the economic fortunes of those who have been most affected by rising inequality. Tax exemptions are one of the few city programs that can directly address the effects of income inequality, and as such are a critical topic given Mayor Bill de Blasio's pledge to fight income equality. A well-designed 421-a program thus offers the opportunity to address this difficult problem.

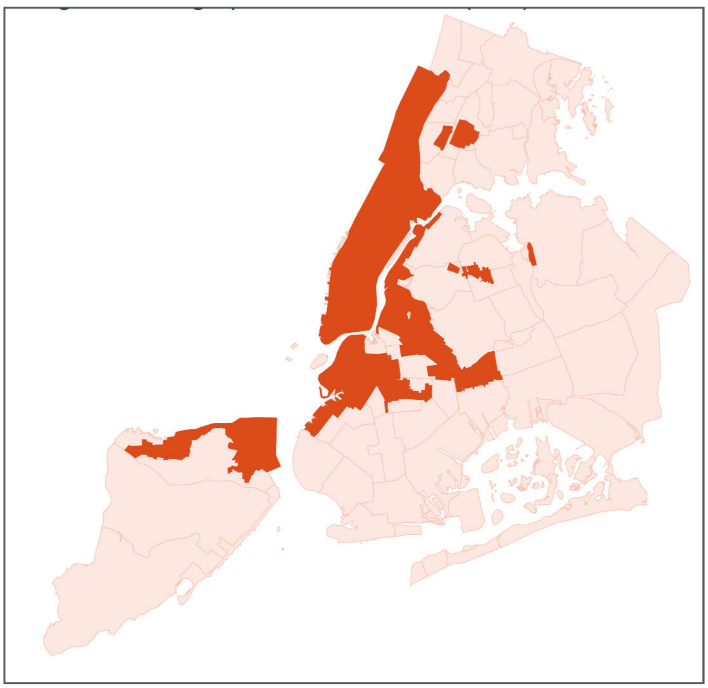
[1] For convenience, the terms "families" and "households" are used interchangeably in this report. Technically, families are composed of related individuals, whereas households include unrelated persons, such as a group of roommates living together.

421-a and the Mayor's Proposed Reforms

The 421-a program was first adopted in the early 1970s during an era when there was a sharp drop in new housing construction. Under the program, building owners are exempt from paying additional real estate taxes due to the increased value of the property resulting from the improvements made. Projects must be new construction of multiple dwelling units. Rental apartments built with 421-a tax exemptions are subject to the provisions of the Rent Stabilization Laws during the exemption period.[1]

By the mid-1980s, there was rising concern that the tax benefits were no longer needed in economically booming neighborhoods in central Manhattan, while concerns mounted about rising rents and long-time residents being forced out of their neighborhoods. The program was amended to require developments in a Geographic Exclusion Area (GEA) to make 20% of the units in each development affordable to low-income households in exchange for the tax benefit. The GEA was expanded several times and now includes all of Manhattan and gentrified areas of western Brooklyn and Queens (see Figure 1). For developments in the rest of the city, the tax benefit is available "as of right," e.g., without affordability requirements.

Figure 1. 421-a program's Geographic Exclusion Area



Source: Association for Neighborhood and Housing Development, Inc., "421-a Developer's Tax Break Expiring June 2015," January 2015

[1] Rent Guidelines Board, "2015 Housing Supply Report," May 28, 2015. Note that apartments with rents above $2,500 are not subject to rent stabilization.

Properties now receive an exemption for 10 to 25 years depending on location and the number of units reserved as affordable to low-income tenants. Affordable units built using the tax benefit must be on-site with the market-rate apartments.

The current program has been criticized as enriching developers, not providing a sufficient number of affordable units, lacking affordability requirements outside the GEA, and fueling gentrification and displacement of low-income families. Eye-popping examples of luxury developments receiving millions in tax exemptions for relatively few affordable units re-enforced perceptions that the program is a boondoggle for the rich.[1]

In early May 2015, Mayor de Blasio proposed a broad set of reforms to the tax benefit program. The Mayor's proposal would increase the share of affordable apartments required in each development from 20 percent to 25 or 30 percent. It eliminates the benefits for condos and prohibits "poor door" separate entrances that have come to symbolize the tale of two cities.

De Blasio's proposal would also make some of the apartments affordable to a tier of low-income families that are not currently served, and would lengthen the benefit term from 20 or 25 years to 35 years, consistent with the length of time apartments must remain affordable,[2] substantially increasing the value of the tax break.[3] The 25 or 30 percent affordability requirement would apply to all developments receiving the tax benefit, not just within the GEA. Developers would choose from a menu of three options with various requirements for affordability and for combining the 421-a tax benefit with direct subsidies and bond financing. (See Table 1 for set-asides under each menu option, and Table 2 for income and rent levels associated with each category of household income.)

For the first time, the program includes set-asides for households earning less than 40 percent of the median incomes in the New York region. These households comprise nearly two-thirds of rent-burdened households in the city, and pay a high percentage of their incomes in rent. (See Table 3.)

The first option requires that 25 percent of unit be affordable, including 10 percent for residents with incomes at 40 percent of AMI. Another 10 percent of units would be reserved for households earning 60 percent of area median incomes, and the final 5 percent for households earning up to 130 percent of area median incomes. City officials expect that developers in Manhattan and close-in Brooklyn and Queens neighborhoods where market rents are high will choose this option. If that is the case, then the first option effectively is the replacement for the affordability requirements in current law, which only apply to these GEA neighborhoods.

[1] For accounts of luxury developments receiving 421-a benefits, see Steven Wishnia, "How Your Tax Dollars Are Wasted To Build Luxury Apartments," Gothamist.com, March 18, 2015.

[2] Ryan Hutchins and Brendan Cheney, "Why De Blasio's 'affordable housing' proposal won over developers," Capital New York, May 7, 2015

[3] Independent Budget Office, "The Mayor's 421-a Proposal: Estimating Tax Revenue Forgone and Affordable Housing Gained," June 2015.

Table 1. Current and proposed requirements for 421-a affordable housing

Income level	Current 421-a program (GEA only)	Administration's proposal		
		First option	Second option	Third option
40% of AMI	n/a	10%	n/a	n/a
60% of AMI	20%	10%	n/a	n/a
70% of AMI	n/a	n/a	n/a	10%
130% of AMI	n/a	5%	30%	20%
Total set-aside	20%	25%	30%	30%

Table 2. Household income and rent levels for low and middle-income affordability programs

	Household income				**Affordable rent** (30% of income)			
HH size	**Very Low Income** (40% of AMI)	**Low Income** (60% of AMI)	**Low Income** (70% of AMI)	**Middle Income** (130% of AMI)	**Very Low Income** (40% of AMI)	**Low Income** (60% of AMI)	**Low Income** (70% of AMI)	**Middle Income** (130% of AMI)
1	$24,200	$36,300	$42,350	$78,650	$605	$908	$1,059	$ 1,966
2	$27,640	$41,460	$48,370	$89,830	$691	$1,037	$1,209	$ 2,246
3	$31,080	$46,620	$54,390	$101,010	$777	$1,166	$1,360	$ 2,525
4	$34,520	$51,780	$60,410	$112,190	$863	$1,295	$1,510	$ 2,805
5	$37,320	$55,980	$65,310	$121,290	$933	$1,400	$1,633	$ 3,032
6	$40,080	$60,120	$70,140	$130,260	$1,002	$1,503	$1,754	$ 3,257
7	$42,840	$64,260	$74,970	$139,230	$1,071	$1,607	$1,874	$ 3,481
8	$45,600	$68,400	$79,800	$148,200	$1,140	$1,710	$1,995	$ 3,705

Table 3. Household incomes and rent burdens in New York City

Source: U.S. Census Bureau, American Community Survey. Data for 2009-13.

	All renter HHs		**Rent-burdened HH**		**Pct of each income group that are rent burdened**
Household income	**# HH**	**Pct.**	**# HH**	**Pct.**	
Below 40% AMI	783,253	40%	658,193	63%	84%
40% to 60% AMI	282,482	14%	190,265	18%	67%
60% to 130% AMI	556,011	28%	168,774	16%	30%
Above 130% AMI	350,273	18%	24,803	2%	7%
Total	**1,972,020**	**100%**	**1,042,036**	**100%**	**53%**

City officials expect that developments in middle markets such as Astoria and parts of Flushing and Jamaica would choose the second menu option, which requires 30 percent of units be affordable to families earning 130 percent of AMI. In "struggling" neighborhoods such as East New York, where City Hall plans to rezone and focus development, city officials expect that developers would combine the tax benefit with other subsidies to create a range of affordable options for households earning 70 percent and 130 percent of AMI.

In announcing his proposal, the Mayor declared, "No more tax breaks without building affordable housing in return. Period." He said that with these changes, the number of affordable units built under the program would double from 12,400 to more than 25,000 over the coming decade, enough to house 65,000 New Yorkers.[1]

The proposal won the immediate support of the Real Estate Board of New York (REBNY), a key stakeholder, while housing advocates criticized it as continuing to be too generous to developers.

[1] Office of the Mayor, "Mayor de Blasio Calls for Sweeping Overhaul of Tax Benefits to Spur More Affordable Housing," press release, May 7, 2015.

421-a and Income Inequality

The 421-a program is quite complex and its renewal raises a number of different issues that are currently subject to intensive discussion in Albany. This report focuses on the program's effectiveness in addressing the effects of income inequality on lower-income New Yorkers who are the intended beneficiary of the program's affordability requirements, and central to the issues being discussed by the Legislature.

Viewed through the lens of income inequality, several aspects of the de Blasio Administration's 421-a proposal stand out. These include:

- "Widening the band" of incomes targeted by the program to include households earning less than 40 percent of area median incomes and households earning 70 percent and 130 percent of AMI, replacing the current program's focus on those earning 60 percent of AMI.

- Providing developers with a menu of options, each targeting a different mix of income groups, that they can choose from on a building-by-building basis.

- Maintaining the requirement that affordable units be constructed on-site with the market-rate units.

- Expanding the number of developments subject to prevailing wage requirements for service workers, while resisting a push by construction unions to include prevailing wage requirements for construction workers.

The first three are integrally inter-related, and their impact on mitigating income inequality must be considered in the context of where they would be used by developers -- whether in high-rent, middle market and economically struggling neighborhoods. The prevailing wage issue is also critical to income inequality effects of 421-a, but can be discussed separately.

Effects in Manhattan and high-rent areas of Brooklyn and Queens

The de Blasio Administration expects that in Manhattan and the high-rent areas of western Brooklyn and Queens (which generally overlap with the current GEA), developers would utilize the first menu option, which includes a 10 percent set-aside for very low-income families (40% of AMI), 10 percent for low-income families (60 percent of AMI) and a new 5 percent set-aside for middle-income families (130 percent of AMI).

To the extent that developers elect the first option, inclusion of the very low-income set-aside strengthens the program's effectiveness in addressing the effects of income inequality, as families at this income level comprise nearly two-thirds of all rent-burdened households in the city and are not targeted in the current program.

Developers in Manhattan and other high-rent areas also have the opportunity to choose the second or third options, which utilize higher income thresholds. This is a critical issue since real estate analyses show that only these markets have the financial capacity to support affordable apartments for low-income families.[1] If developers in these areas selected the second or third options, which allocate most affordable units to middle-income households, the effect would be to greatly dilute the 421-a program's effectiveness in addressing income inequality. The 421-a program should ensure that this does not happen and that affordable units are allocated primarily if not entirely to lower-income New Yorkers.

Importantly, de Blasio's proposal maintains the requirement that affordable housing be built on-site. This requirement had been relaxed in the late 1980s, when developers in the GEA were permitted to purchase "certificates" from developers of low-income units elsewhere in the city. The trading value of the certificates resulted in inefficient use of the tax subsidy, however, and this option was later repealed.

When the idea of offering an off-site option has been raised,[2] the Administration has opposed an off-site option, citing the value of maintaining economic diversity in gentrifying neighborhoods and building affordable housing in neighborhoods with low crime rates and good access to jobs, quality schools and local services.

These are clearly important considerations and should be reflected in the design of any revamped 421-a program. But the on-site requirement as currently constituted appears to be counterproductive for two reasons.

First, the on-site requirement sites these critical affordable units far from where the large majority of potential program beneficiaries currently live. Nearly three-fourths of low-income renters who are paying excessive proportions of their income in rent live outside of these high-rent neighborhoods. Figure 2 shows with a yellow tint the Community Board districts where affordable 421-a apartments have been built, contrasted with where rent-burdened low-income families live. As can be seen, most rent-burdened low-income families live outside Community Board districts where affordable 421-a units have been constructed in recent years:

- 73% of all rent-burdened *low-income* households (incomes below 60% of AMI) live in Community Board districts outside the 421-a benefit area.[3]
- An identical 73% of rent-burdened *very low-income* households (incomes below 40% of AMI) live in Community Board districts outside the 421-a benefit area.

[1] Josiah Madar, "Inclusionary Housing Policy in New York City: Assessing New Opportunities, Constraints, and Trade-offs," NYU Furman Center, New York University, March 26, 2015.

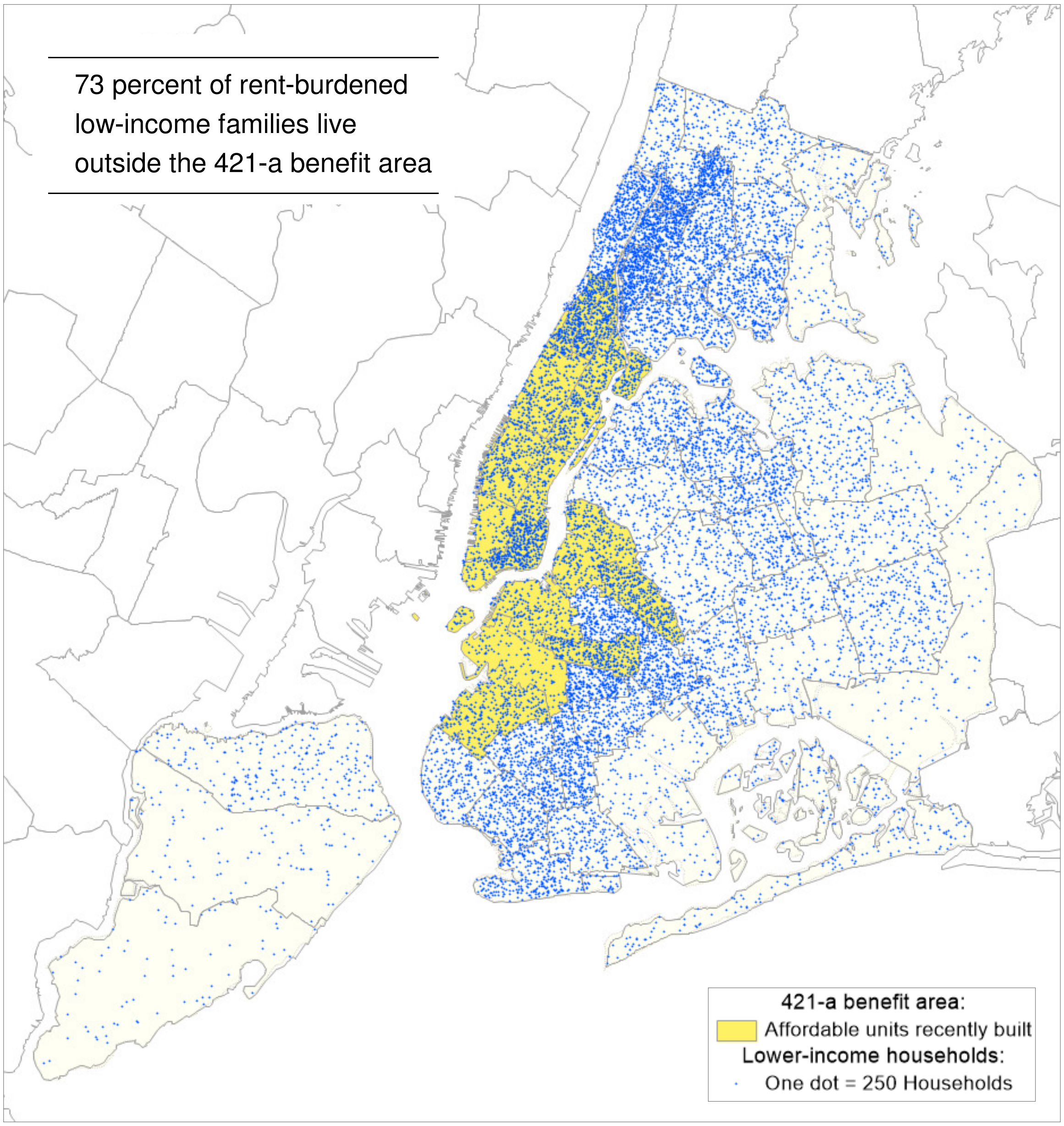
[2] Two recent reports have discussed this issue. Madar, op. cit. and Howard Husock and Alex Armlovich, "Mend It, Don't End it: NYC's 421-a Affordable Housing Tax Exemption," Manhattan Institute for Policy Research Issue Briefs, No. 34, May 2015.

[3] For purposes of this discussion, the "benefit area" under the current 421-a program is defined as Community Board districts where affordable housing has been constructed under the 421-a program. These districts are identified based on the analysis maps published in Association for Neighborhood and Housing Development, Inc., "421a Developer's Tax Break Expiring June 2015," January 2015.

Figure 2. Rent-burdened lower-income households (up to 60% of AMI)

Data are based on household incomes for 2009-13. Includes households that currently pay more than 30% of income in rent and have incomes below 60% of area median income. Note that households are shown as randomly distributed within each Community Board, based on total number of households in each Board.

Source: U.S. Census Bureau, American Community Survey



Low-income families living outside the benefit area would need to move out of their current neighborhoods in order to take advantage of the 421-a program. While some might desire to do so, many people presumably prefer to stay close to family, schools, jobs and services where they currently live. Concentrating lower-income units in far-away neighborhoods places unfair and unnecessary restrictions on low-income households' ability to take advantage of affordable housing options.

Another important consideration concerns program costs and the scale of benefits provided under 421-a. Because many of the new buildings are in areas with high land and development costs, the effect of the on-site requirement is to drive up costs and restrict the number of apartments that can be constructed through the program. This has been justified for reasons of economic diversity and providing families with access to jobs, schools and other neighborhood services.

There is actually no need to choose between more units and attractive neighborhoods, however. Policymakers could restrict off-site units to designated neighborhoods that offer job access, good schools, low crime and neighborhood amenities and still realize substantial cost savings. This point can be seen clearly in Table 4, which shows examples of the current cost, in foregone taxes, of recent 421-a projects that have included affordable units. The table shows foregone tax revenue per affordable housing unit. This metric provides a basis for comparison that includes the tax benefit that may have been needed to spur construction in the first place, almost certainly a bigger sum outside Manhattan than in Manhattan, and the benefit needed to underwrite the affordable units.

The examples in Table 4 show that foregone tax revenues in the Manhattan core are two to three times the foregone tax revenues in Upper Manhattan, Williamsburg and Park Slope. Even if construction of affordable units was limited to these attractive neighborhoods, thousands more affordable units could be constructed.

More broadly, the NYU Furman Center has estimated that, with the same foregone tax revenue, nearly three times as many affordable apartments could be created if they were built in lower-rent neighborhoods instead of in Manhattan and western Brooklyn and Queens.[1] The 421-a program could thus be revised to maintain the goal of building affordable housing in attractive and safe neighborhoods that offer employment and educational opportunities and neighborhood services, but not be limited to the highest-cost areas of the city.

There are other reasons as well to pursue an off-site component to affordable housing. Families outside the 421-a benefit area not only comprise nearly three-quarters of rent-burdened lower-income households, these are also the neighborhoods that have most struggled as a result of rising inequality:

[1] Josiah Madar, "Inclusionary Housing Policy in New York City: Assessing New Opportunities, Constraints, and Trade-offs," NYU Furman Center, New York University, March 26, 2015.

Table 4. Foregone tax revenue in 421-a developments with affordable housing component, tax exemption started in 2011/12 or later.

Source: Municipal Art Society of New York, "421-a Tax Exemption" interactive map on-line at http://www.mas.org/urbanplanning/421a

		Foregone annual tax revenue (000)	**Affordable units**	**Annual foregone taxes per unit**	**Monthly foregone taxes per unit**
Brooklyn/Queens	1310 Jackson Ave, Qn	$189	3	$63,000	$5,250
	1115 Broadway, Qn	$372	16	$23,250	$1,938
	509 Glenmore Ave Bk	$71	2	$35,500	$2,958
	960 Myrtle Ave, Bk	$330	17	$19,412	$1,618
	26 Fayette St, Bk	$32	1	$32,000	$2,667
	80 Metropolitan Ave, Bk	$798	30	$26,600	$2,217
	52 N 1 St, Bk	$544	9	$60,444	$5,037
	287 McGuinness Ave, Bk	$163	7	$23,286	$1,940
	384 Bridge St, Bk	$1,775	76	$23,355	$1,946
	86 Congress, Bk	$247	6	$41,167	$3,431
	152 4 Ave, Bk	$509	19	$26,789	$2,232
	500 4 Ave, Bk	$662	31	$21,355	$1,780
	169 16 St, Bk	$274	6	$45,667	$3,806
	593 6 Ave, Bk	$252	5	$50,400	$4,200
	Total	**$6,218**	**228**	**$27,272**	**$2,273**
Upper Manhattan	620 W 143 St	$606	17	$35,647	$2,971
	1465 5 Ave	$321	11	$29,182	$2,432
	1820 Madison Ave	$238	5	$47,600	$3,967
	Total	**$1,165**	**33**	**$35,303**	**$2,942**
Lower East Side	256 Bowery	$543	5	$ 108,600	$9,050
Chelsea	500 W 23 St	$1,559	22	$70,864	$5,905
	540 W 28 St	$1,324	18	$73,556	$6,130
	431 W 37 St	$529	20	$26,450	$2,204
	534 W 30 St	$5,659	74	$76,473	$6,373
	303 10 Ave	$1,327	18	$73,722	$6,144
	505 W 37 St	$12,170	167	$72,874	$6,073
	320 W 38 St	$10,527	114	$92,342	$7,695
	352 W 37 St	$2,655	41	$64,756	$5,396
	560 10 Ave	$11,835	163	$72,607	$6,051
	770 11 Ave	$12,284	173	$71,006	$5,917
	Total	**$59,869**	**810**	**$73,912**	**$6,159**

- Median household incomes of renters living outside the 421-a benefit area fell by 14 percent between 2000 and 2009-13.
- Over the same period, median rents increased 15 percent in this area.
- As a result, the median rent burden (rent as a percentage of household income) increased from 27 percent to 33 percent among renter households outside the 421-a benefit area.[1]

Mayor de Blasio has emphasized the importance of producing affordable housing "on a grand scale," calling it "a pretty sacred mission, from my point of view."[2] Clearly, any reasonable way to increase the number of affordable apartments built from 421-a tax breaks would strengthen the program's effectiveness in addressing income inequality. Expanding the amount of affordable housing in neighborhoods closer to where families who are the intended beneficiaries currently live would also enhance the equity of the program.

Based on the Administration's estimate that 12,400 affordable units would be constructed over the next decade under the current program (all in the GEA), it can be estimated that an off-site option creates the opportunity for an additional 10,000 to 20,000 affordable units to be built by taking advantage of the lower land and construction costs outside of Manhattan -- but still in highly attractive neighborhoods.[3] The effect on the overall program is substantial, increasing the number of affordable units from the Administration's projection of 25,000 over the next decade to 35,000 or more -- with the entire increment set-aside for low-income families.

An off-site option would need to be carefully structured to ensure that the number of units built was commensurate with the tax subsidy, and that the units were built in areas with adequate access to jobs and educational services and local amenities. It could readily be limited to gentrifying areas of Brooklyn and Queens, and/or combined with the Administration's rezoning of East New York and a number of other neighborhoods where relatively dense housing development is contemplated. It would thus complement important strategies for the city's development and for providing housing options for rent-strapped low-income New Yorkers.

[1] In comparison, within the 421-a benefit area, median household incomes increased by 2 percent among renters and rents increased 29 percent. The median rent burden grew more slowly than outside the 421-a benefit area -- from 25 percent to 28 percent -- and remains below the corresponding figure for outside the 421-a benefit area.

[2] Ryan Hutchins, "De Blasio's 421-a plan boosts prevailing wage for service workers," Capital New York, May 26, 2015.

[3] This estimate assumes that at least one-half of the affordable units built in Manhattan under the Administration's proposal would shift to off-site locations in the other boroughs, and that of the 12,400 affordable units that the Administration projects would be built over the next decade under current law, approximately 10,300 are in Manhattan, similar to the distribution in recent years.

Effects in middle markets and struggling neighborhoods

Developers in middle markets that have not seen affordable 421-a units developed, such as Astoria, Flushing and Jamaica, are expected by city officials to choose the second menu option that requires 30% of units be affordable to families earning 130% of AMI. The resulting rents are generally below or in line with market rents. Figure 3 shows that in these middle-market neighborhoods, over 80% of recent rentals are affordable to families earning 130 percent of AMI. Thus, while the 421-a program would continue to spur much-needed housing construction in these neighborhoods, it would not introduce a new affordability option for families in these areas, since the large majority of existing apartments on the market in these areas are currently affordable to these middle-income households.[1]

The Administration points out that to the extent these areas gentrify and rents escalate rapidly, the 30 percent of units subject to the affordability provisions will protect those tenants from unaffordable rent levels. This is a forward-looking benefit of the Administration's proposal but does not change the current affordability picture.

In struggling neighborhoods such as East New York, the Administration expects that developers would combine the 421-a tax benefit with other subsidies to build apartments that are affordable for households earning 70% and 130% of AMI. As shown in Figure 3, market rents are generally within what is affordable to middle-income families. As shown in Figure 4, approximately one-third to two-thirds of recent rentals in these areas are affordable to low-income families earning 70 percent of AMI. The 10 percent of units set aside for these families may create new affordable options for them. This is an immediate benefit, but constitutes a relatively small portion of the overall program.

Prevailing wages for construction workers

As Albany took up the de Blasio Administration's 421-a proposal, construction unions proposed that developers be required to pay prevailing wages on 421-a projects. The de Blasio Administration had proposed to expand the existing prevailing wage requirement for service workers, but strongly opposed a prevailing wage requirement for construction workers, citing independent studies which found that a prevailing wage requirement would result in 30 percent fewer affordable units would be built.[2]

At first glance, a prevailing wage requirement might seem to help 421-a address income inequality issues, ensuring middle-class wages for those producing the new housing units. However, by reducing the number of affordable units, a prevailing wage requirement would have the opposite effect. Under prevailing wages, tradespeople such

[1] The rents of recent movers reflect rents subject to rent regulation, rents reduced by other public subsidies, and public housing as well as market rents. To account for this, the maps in Figures 3 and 4 show the percentage of recent rentals that are above the cut-off for middle-income (Figure 3) and lower-income (Figure 4) households. If few units are above the threshold, presumably market rents are somewhere below the 130 percent or 70 percent thresholds. The maps thus provide a way of assessing likely market rents relative to government definitions of middle and low-income households.

[2] Will Bredderman, " Deputy Mayor: Prevailing Wages Would Cost City 17,000 Affordable Apartments," New York Observer, June 1, 2015.

Figure 3. Percentage of recent rentals that are affordable to middle-income households (130% of AMI)

Data are shown for Community Board districts that have not had 421-a affordable housing built under the current program. Rents are for households that moved between 2009 and 2013.

Source: U.S. Census Bureau, American Community Survey

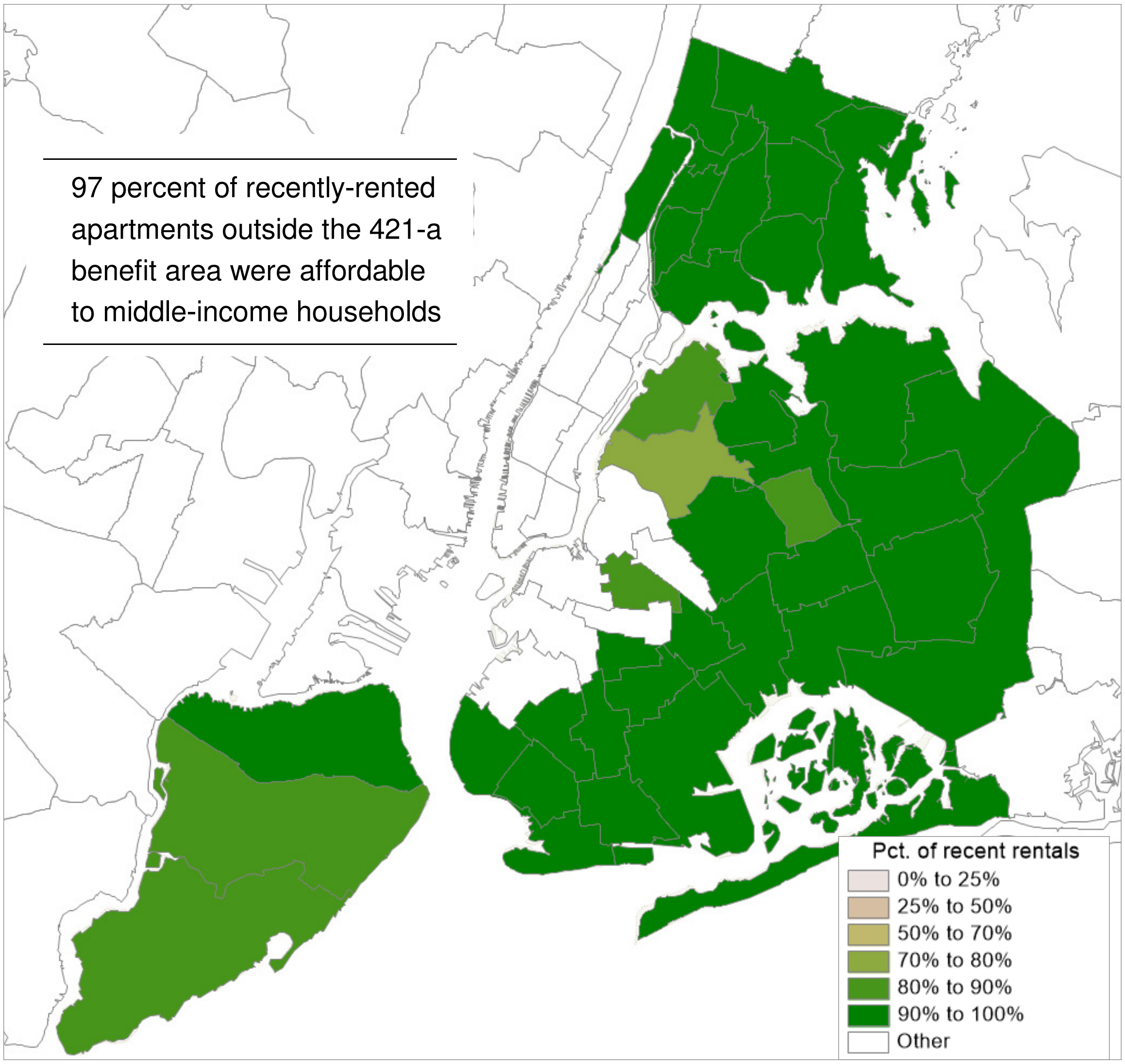
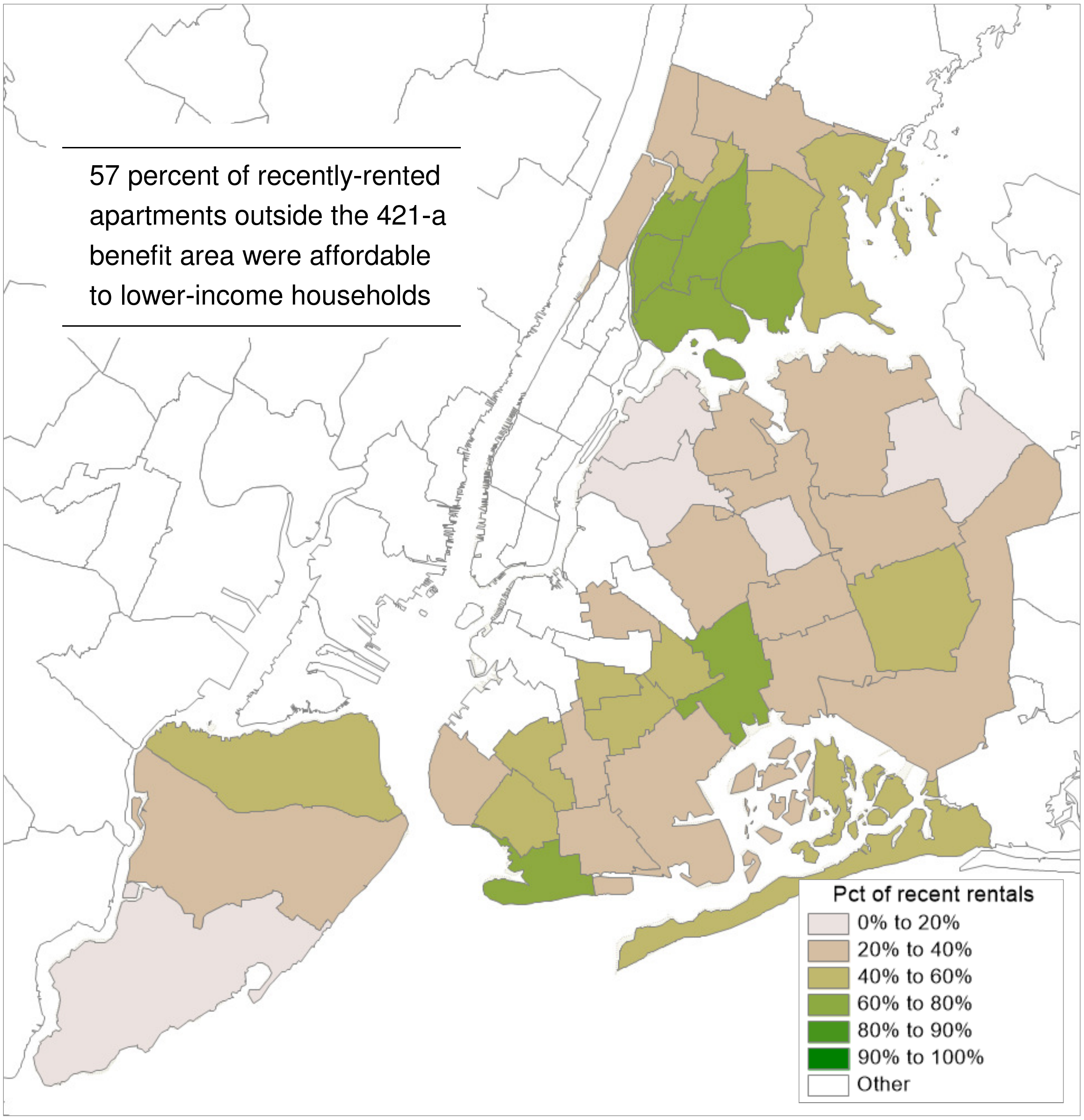


Figure 4. Percentage of recent rentals that are affordable to lower-income households (70% of AMI)

Data are shown for Community Board districts that have not had 421-a affordable housing built under the current program. Rents are for households that moved between 2009 and 2013.

Source: U.S. Census Bureau, American Community Survey



as bricklayers, carpenters, electricians, plumbers, steamfitters and laborers earn $40 to $65 an hour, with higher hourly rates for overtime, plus $20 to $51 per hour in benefits.[1] These wage rates translate into annual incomes well above the cut-offs for low-income families to qualify for affordable 421-a units. The effect of a prevailing wage requirement would thus be to shift benefits from lower-income residents to relatively higher-income tradespeople, a change that would run counter to the equity goals of the 421-a program.

[1] Office of the Comptroller, City of New York, Section 220 Prevailing Wage Schedule, 2014-2015.

Conclusion

The City's *OneNYC* strategic plan, released this spring, calls for equity to be the lens used to "assess who will benefit, who is burdened or needs help" for "all of our planning, policymaking, and governing."[1] In that spirit, this report assesses key aspects of the 421-a tax exemption program for new housing construction, which expires on June 15, 2015 and is currently costing the city $1.1 billion annually in foregone tax revenue.

This analysis leads to three conclusions. First, a revamped 421-a program should be designed to guarantee that developers in high-rent areas such as Manhattan and western Brooklyn and Queens provide affordable apartments for low-income families (e.g., incomes of 40 percent or 60 percent of AMI). The finances of these developments can support low-income units, as proven under the existing program. Elsewhere in the city, this is unlikely to be the case, according to the NYU Furman Center analysis -- the most detailed public analysis available. This result could be assured via geographically defined areas as in current law, or other methods; the specifics require analysis that goes beyond the scope of this report.

Second, a revamped 421-a program should include an off-site option that could create ten to twenty thousand additional housing units for low-income families by taking advantage of lower land and construction costs outside of Manhattan. An off-site option would expand the number of families served by the program, site the housing closer to where the large majority of low-income families currently live, while also readily ensuring that the new apartments are located in areas that are safe and provide good access to jobs, schools and neighborhood services.

Third, the 421-a program should not require prevailing wages for construction workers, as doing so would raise costs, reduce the amount of affordable housing produced, and undercut the effectiveness of the program in addressing the effects of income inequality in the city.

The specifics of an off-site option would need to be developed carefully in order to make best use of the tax subsidy and ensure that new units are built in areas with adequate employment and educational opportunities and neighborhood services. That challenge, however, is worth meeting in order to realize the larger goal of effectively addressing the effect of rising inequality and rents on lower-income New Yorkers.

[1] City of New York, "One New York: The Plan for a Strong and Just City," April 22, 2015, p. 116.