New York City's Ten Year Capital Plan for Housing

How the city of New York added 180,000 housing units and stopped neighborhood blight.

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THE MID-1980S were a turning point in American housing policy. As the federal Section 8 housing production programs ended and federal budgetary constraints grew, the locus of innovation in housing policy shifted from the federal government to states and cities. Any examination of these local innovations must include the experience of New York City. For decades, the city has been the testing ground for new policies that were later emulated by other American cities and by the federal government. During the Ten Year Capital Plan for housing (hereinafter referred to as the Ten Year Plan), announced by Mayor Edward I. Koch in 1985 and now lasting beyond fifteen years, the city has spent more than $5.1 billion to build or rehabilitate more than 180,000 housing units.

THE TEN YEAR CAPITAL PLAN

For New York City, innovation in housing policy is not an isolated or unusual occurrence. Before the New Deal, when the federal government moved to the forefront of housing policy creation and funding, New York City was the unquestioned national leader in that field. At the turn of the last century, the city enacted the nation's first housing code, the Tenement Housing Act of 1905. The first publicly owned housing for low-income families in the United States was built on Manhattan's Lower East Side in 1934, three years before the first federal public housing program. New York's leadership role in housing continued after World War II. In 1957, New York City was the first city to outlaw discrimination based upon race in the sale or rental of privately owned homes. And, in the mid-1960s, together with New York State, the city used interest-rate subsidies and tax exemptions to spur the construction of tens of thousands of apartments for middle-income families under the Mitchell-Lama Program.

Mayor Koch's announcement in the mid-1980s of a multi-billion dollar program for housing was surprising in scale but not focus. The city had just survived near-bankruptcy, and a strong economy allowed it to borrow again in order to refinance its debt on more favorable terms. With housing prices rapidly escalating beyond the means of many of the city's residents, the need for housing was obvious. In addition, the city had just signed consent decrees in which it promised to provide housing to all homeless individuals. The program also fit the political needs of a mayor running for reelection and seeking support from low-income and minority communities.

Despite the revival of New York City's economy in the mid-1980s, many of the neighborhoods north of 96th Street in Manhattan, in the South Bronx, central Brooklyn, and southeastern Queens had yet to recover from the devastation of the 1960s and 1970s. During this period, more than 700,000 people moved out of the city, and more than 300,000 units of housing were either lost to abandonment or destroyed by arsonists. Some neighborhoods resembled bombed cities of postwar Germany. The city administration's response was to accelerate its process for foreclosing properties with real estate tax delinquencies. Seemingly overnight, the city took title to more than 100,000 units of housing and a significant inventory of vacant land through tax-foreclosure proceedings. Most of this housing was severely

deteriorated and much of it was occupied by the poorest households in the city. The city's housing agency, the Department of Housing Preservation and Development (HPD), was unprepared for its new role as the city's second-largest landlord. This lack of preparedness caused further property deterioration.

In the end, the city's vast stock of tax-foreclosed housing and land proved to be both a huge burden as well as the raw material for the Ten Year Plan. Without the ability to provide free or nominally priced buildings and land to the hundreds of nonprofit and private developers, New York City would have been unable to achieve the production rates anticipated by the Ten Year Plan. In 1985, Mayor Koch announced a plan for a "five-year $4.4 billion program to build or rehabilitate around 100,000 housing units for middle-class, working poor, and low-income families and individuals." To fund the program, he proposed using excess financing proceeds to float approximately $1 billion in bonds. Other revenues would come from the city's Housing Development Corporation and the city's capital budget. Over ten years, the financial commitment to the program grew to $5.1 billion.

Although the sources of revenue would change over the course of the Ten Year Plan, the use of the city's capital budget for housing construction and rehabilitation was unprecedented. Historically, the city used capital dollars to fund transportation, public facilities, and other infrastructure improvements. The capital dollars invested in housing beginning in the mid-1980s amounted to a municipal recognition of the importance of housing to the city's economic future.

The main purpose of the Ten Year Plan was to address a shortage of housing; a second focus was neighborhood revitalization. According to Koch, "We intend to undertake a major effort to rebuild entire neighborhoods or, perhaps 15 to 25 square blocks throughout the city ... [i]t is anticipated that such a concentrated revitalization would provide the hub for further development." This emphasis on rebuilding neighborhoods devastated by abandonment was reiterated in 1989: "We're creating more than just apartments—we're re-creating neighborhoods. We're revitalizing parts of the city that over the past two decades had been decimated by disinvestment, abandonment and arson."

Between 1987 and 2000, New York City built or rehabilitated approximately 182,000 housing units, excluding federally subsidized units. The overwhelming majority of the $5.1 billion that was spent came from the city's capital budget; remaining funds were obtained from the federal and state governments. In its peak year—FY 1992—the city spent more than $660 million on housing production and development. Although by FY 2000 this had declined to $269 billion, it still exceeded the amount the city spent on housing prior to the Ten Year Plan by a factor of ten.

Between 1987 and 2000, New York City implemented the largest municipal housing program in the nation's history, spending an estimated three times more than the total housing expenditures of the next several dozen largest cities combined. The Ten Year Plan was marked by innovation in terms of the types of housing, the financing, and the types of public-private partnerships that were created. While it is highly unlikely that any other city will ever mount a housing program of the same scale, the experiences of New York City's Ten Year Plan are instructive.

A MIX OF FLEXIBLE PROGRAMS

Most housing initiatives, at both the federal and local levels, typically involve one program that is replicated for all types of neighborhoods. In contrast, the Ten Year Plan encompassed more than one hundred different programs. While the large number of programs is partially attributable to the tendency of succeeding mayoral administrations to re-name many of the existing programs, HPD funded several dozen different programs simultaneously. This variety enabled the city to be flexible in creating strategies for particular buildings and neighborhoods. At the same time, many programs used similar tools and principles, resulting in programmatic economies of scale and replicability.

Unlike most federal programs, New York City's programs typically used a gap finance approach to subsidize the capital and—indirectly—the operating costs of the housing. Typically, the city determined the cost of a project, the amount of equity the owner could contribute, and the amount of private market debt the owner could service (after operating costs were subtracted from rental income). Estimates were based upon prevailing and expected market conditions and, in the case of occupied rental buildings, the rent-paying ability of current tenants. The difference between the cost of rehabilitation and new construction on the one hand, and the sum of equity and private market debt on the other, was made up by city financing, primarily in the form of nominal interest rate loans.

The largest set of programs involved the moderate rehabilitation of more than 73,000 occupied rental units. Many of the buildings treated under these programs required only upgrading or replacement of major building systems such as boilers, plumbing, roofs, or windows. For buildings with relatively modest needs, 3-percent loans were made available to owners under

the Article 8-A program. For those with larger requirements, HPD used the innovative Participation Loan Program (PLP). Under PLP, owners received loans that combined funds from private market-rate lenders and the city itself, which charged a 1-percent interest rate. The net interest rate charged to the owner depended upon the building's rent roll (or rent-paying capacity) and the work required. Buildings with especially high needs and/or extremely low income tenants received loans in which the city's contribution was proportionately greater and the blended interest rate lower.

Perhaps nowhere was the city's creativity in crafting flexible programs more apparent than in its efforts to deal with the land and buildings to which it took title as a result of tax foreclosure. Nearly 20,000 units of housing were created on vacant, city-owned land. The city's contribution to this housing typically was limited to the sale of land at nominal prices ($500 per unit) and a capital subsidy ranging from $10,000 to $15,000 per housing unit. In addition, more than 41,000 units of vacant tax-foreclosed housing were rehabilitated, together with an additional 28,000 units of occupied tax-foreclosed units. Under some programs, the city owned the properties during rehabilitation; in others, rehabilitation was undertaken after the properties were transferred to a variety of private and nonprofit owners.

The city's flexibility also extended to the ultimate owners of the properties. Rather than a one-size-fits-all approach of public or private ownership, the city created enough program variety to attract private real estate developers as well as nonprofit organizations. For example, local developers were enlisted in the Neighborhood Entrepreneurs Program (NEP) to take title to abandoned buildings, rehabilitate them with city and federal dollars, and operate them. Similarly, nonprofit, community-based organizations, participating in the Neighborhood Redevelopment Program (NRP) and its predecessor, the Community Management Program, rehabilitated more than 5,500 housing units. The city was even able to promote homeownership among thousands of former tenants in its Tenant Interim Lease Program (TIL). Under TIL, the city conveyed rehabilitated multifamily properties to very low income tenants who had proved their ability to manage their buildings. This allowed the city to tap the capacity of the full spectrum of qualified owners and developers in its efforts.

LEVERAGING PRIVATE RESOURCES

If New York City had not taken advantage of the resources and capacity of the private sector, it would not have been able to achieve the levels of production and diversity of programs required under the Ten Year Plan. In terms of financial resources, we have already mentioned the pivotal role of private mortgage capital. Many of the city's leading financial institutions made the construction and permanent loans for the city's gap financing method.

In addition to leveraging private capital, the city leveraged the capacity and expertise of banks. One of the signal achievements of the Ten Year Plan was the remarkably low level of corruption or fraud that accompanied the expenditure of such large sums of public money. HPD did not have the staff or expertise to effectively monitor the use of funds. Instead, under many programs, the banks performed this monitoring function as they disbursed construction loans, much as they would for a market real estate loan. In some instances, the banks acted individually; in others they worked together. For example, many of the banks provided funds to the Community Preservation Corporation (CPC), an intermediary, which in turn underwrote and monitored the loans to developers.

CPC was only one intermediary organization that was enlisted to stretch the capacity of HPD. The day-to-day management of the homeownership initiatives was entrusted to two nonprofit organizations. More than 13,000 units of one-, two-, and three-family homes were built by private developers, working under the supervision of the New York City Housing Partnership, a business group. An additional 4,000 single-family homes were built under the Nehemiah Program by coalitions of churches in East Brooklyn and the South Bronx. These intermediaries supervised development, arranged financing, and marketed the homes.

Community-based nonprofit housing developers also worked with intermediary organizations to rehabilitate city-owned rental buildings. New York City was fortunate to be the only city in the nation in which both major low-income housing intermediaries—the Enterprise Foundation and the Local Initiatives Support Corporation (LISC)—worked with community development corporations. LISC and Enterprise created programs, provided technical assistance, and, perhaps most important, through their joint New York Equity Fund, raised and invested equity through the syndication of the Low Income Housing Tax Credit to private investors, including leading corporations. Because these intermediaries acted as fiduciaries to the entities that invested in the Equity Fund, they provided needed oversight and gave credibility to the hundreds of small community-based developers.

Perhaps nowhere has the city's privatization of functions been more apparent than in its efforts to stem the abandon-

ment of privately owned housing. When Rudolph Giuliani became mayor, the city had stopped vesting title to tax-delinquent properties, due to the high cost of managing the properties and the poor record the city enjoyed as a landlord. Yet without a credible threat that their properties would be taken for failure to pay taxes, property owners often had little incentive to pay taxes. In 1996, the city adopted a two-pronged tax collection and anti-abandonment strategy that made extensive use of the private sector. The city no longer took ownership of tax- delinquent properties. Instead, like other major U.S. jurisdictions, it sold tax liens to a private trust that sought either collection or foreclosure.

Not all buildings were subject to tax lien sales; buildings that met the statutory definition of "distressed" would be removed from the tax lien sale. Instead, for these buildings, a newly enacted program called the Third Party Transfer Program was created. Under Local Law 37 of 1996, the city commenced foreclosure proceedings against these distressed buildings, which were transferred not to the city, but to new responsible third parties, with city financing. In 1999, the city began transfers to a nonprofit intermediary in contemplation of transfers to third parties. This intermediary, the Neighborhood Restore Corporation, held title to the buildings, stabilized them, and managed them until the city designated the ultimate third party. This period of ownership by Neighborhood Restore Corporation allowed the city and the ultimate owners to inspect the properties, develop scopes of work for rehabilitation and arrange the necessary financing.

To date, four rounds of property vestings have been begun, involving more than 342 properties and 4,200 housing units. The city has identified a variety of private, nonprofit, and tenant cooperative owners for the buildings. Although the program has not been free from controversy, it has won recognition for innovation from the Pioneer Foundation.

ACHIEVING INCOME MIX

One of the most contentious issues during the early years of the Ten Year Plan was the appropriate income mix for households. Tenant advocates pressed the city to increase the proportion of units allocated to low-income families. The city, under pressure from consent decrees guaranteeing housing to each homeless family, sometimes sought to house high proportions of homeless families in the buildings. Countervailing pressure came from neighborhood residents, who felt that efforts to rebuild and stabilize their neighborhoods would be jeopardized by large numbers of households who might be prone to crime, substance abuse, or mental illness. In addition to community pressure, in the late 1980s and 1990s evidence was beginning to accumulate that housing programs that concentrated the poor caused more problems than they solved.

In the end, the city generally made significant efforts to promote a balanced mix of incomes. With the exception of housing projects that sought to accommodate formerly homeless tenants with special needs, most of the rental programs limited the proportion of homeless families to approximately 15 percent. In addition, most of the programs sought to house a mixture of low- and moderate-income tenants. This income mixing served two purposes. First, it reduced the concentration of extremely needy people, providing children with role models of working families and reducing the prevalence of social problems. Second, it provided an opportunity for cross-subsidy. This was made possible, in part, because of the city's ability to restructure rents as a result of the tax foreclosure vesting and use of city financing. Apartments that would normally have been subject to stringent rent regulation had their rents increased to achieve economic feasibility. Existing low-income tenants were spared the impact of higher rents. But relatively higher-income and new tenants who could pay higher rents did so, helping to offset the extremely low rents paid by the poor.

REACHING THE MIDDLE CLASS

In many American cities, the private market adequately provides affordable housing for all but the poorest. In New York City, however, this has been less true. Young families, immigrants, and one-wage-earner families are particularly ill-served.

The homeownership programs of the Ten Year Plan were designed to serve the middle class. Under the Partnership's New Homes Program, one-, two-, and three-family homes were sold to families with annual incomes that ranged from $32,000 to $75,000. The Nehemiah Program reached lower-income buyers, selling somewhat more modest homes to households with incomes as low as $27,000 per year. In addition to allowing families the opportunity to accumulate assets, the homeownership programs served other functions. First, in the absence of these programs, many upwardly mobile families might have left the city and moved to the suburbs. Second, the programs drew middle-income residents into the city's distressed neighborhoods, increasing income diversity.

As the city attempted to squeeze more production out of a declining capital budget, it experimented with other middle-income housing initiatives. For example, city-owned land was made available for the development of 3,000 new middle-

income rental apartments through the Cornerstone Program. Some of these projects will be financed by a second new initiative, The New Housing Opportunities Program (New Hop). Under New Hop, the city's Housing Development Corporation blended taxable bond proceeds with its corporate reserves to offer developers below-market interest-rate financing. This program, like Cornerstone, does not entail the expenditure of city capital funds.

NEIGHBORHOOD REVITALIZATION

One of the greatest innovations of the Ten Year Plan was that it married the twin objectives of housing production and neighborhood revitalization. Most housing programs in New York City (and elsewhere), prior to the Ten Year Plan, usually lacked a focus on neighborhood impact. From the beginning, HPD sought to use housing to catalyze economic and community development. This was evident in its choice of sites, as well as its partnerships with community-based organizations and neighborhood entrepreneurs.

Anecdotal evidence of the success of the Ten Year Plan in promoting neighborhood revitalization is obtained from viewing neighborhoods in the South Bronx, Harlem, and central Brooklyn. Where once there was block after block of emptiness, today most vacant buildings have been renovated, are in the process of rehabilitation, or have signs announcing future work. Commercial areas that were once barren are thriving. Streets that used to be deserted are bustling.

Research is beginning to confirm this anecdotal evidence. Several studies have examined the impact of the Ten Year Plan on neighboring property values and found that upon the completion of the development or rehabilitation of housing, the sale prices of adjacent properties increased from 2.3 percent to 7.0 percent. Property values within 500 feet of the new project increased by 1.3 percent to 7.7 percent, relative to the prices of homes located in the same census tract but more than 500 feet from the new housing. This suggests that the new or rehabilitated housing built under the Ten Year Plan has generated spillover benefits that are capitalized in nearby property values. These benefits derive from the elimination of blighted and dangerous conditions, the creation of quality buildings, and the in-migration of additional population.

MISSED OPPORTUNITIES

Although the innovations and achievements of the Ten Year Plan are exceptional, New York City did not fully capitalize on the opportunities offered by such a large expenditure of public money. Although the city used private market actors to expand its capacity and leverage an array of private resources, it did not sufficiently employ market-based incentives in the administration of programs. For example, the selection of developers to participate in programs was typically not based upon considerations of cost-saving. Instead, requests for qualifications were solicited, developers were designated, and the city, together with selected developers, would work out project budgets.

These budgets did not typically include incentives for cost-saving. In the early years of the Ten Year Plan, the Construction Management Program (CMP) demonstrated the consequences of this program flaw. In an attempt to accelerate the pace of rehabilitation, HPD retained large construction companies to rehabilitate more than 1,500 units of housing. The construction managers simply bid out the subcontracts without budget limitations. With no financial incentives to rein in costs, hard costs exceeded $100,000 per unit rather than the $60,000 to $65,000 per unit typical at that time. Other programs also lacked incentives to cut costs. For example, soft costs for NEP and NRP were determined according to a set schedule. Since developers were not rewarded for obtaining lower prices for such expenses as attorneys' and architects' fees, they seldom did so. Similarly, for many other programs, the developer's fee was based on a percentage of the unsubsidized total development cost. Hence, the higher the cost, the greater the return to the builder.

In addition to introducing market-based incentives, the city could have achieved more "bang for its buck" if it had attacked the problem of high construction costs. A recent report for HPD and the New York City Partnership found that the cost of construction in New York City was the highest in the United States. According to one set of estimates, the cost to construct a mid-rise building in New York City was 4 percent higher than in Los Angeles, 10 percent higher than in Chicago, and 22 percent higher than in Dallas. The reasons for the high costs are varied, but high union wages and restrictive work rules add thousands of dollars in useless requirements and lost productivity.

The New York City government is also to blame for much of the high cost of construction. Its zoning resolution is hopelessly complex and outdated; its environmental and land-use procedures are burdensome and invite costly litigation; its building code is full of special-interest provisions; and its building department has long had management problems. The high cost of construction in New York City is not a secret. Previous

studies have documented the problem and made recommendations. Nevertheless, until very recently, the city has failed to act to implement reforms; instead, it has used tax dollars to bandage the problem. The achievements of the Ten Year Plan are impressive, but one can only imagine how much more housing could have been produced if the entire $5.1 billion had been spent on housing rather than on wasteful practices and inefficient procedures.

The current recession, together with the impact of the destruction of the World Trade Center, make it difficult for the current administration to carry on many of the programs of the past fifteen years. Despite Mayor Bloomberg's recent commitment of additional resources to housing, capital for housing is limited. Nevertheless, under any reasonable set of budget estimates, New York will continue to spend more money on housing than any other city in the country. The challenge for the first decade of the twenty-first century will be how to achieve more with less. Mayor Bloomberg has recently begun this process by announcing his commitment to adopt a money-saving model building code and by promoting the rezoning of certain areas for residential development. Of course, more needs to be done in partnership with the development community and labor unions. The city's cumbersome land use and environmental review processes need to be revamped and streamlined. Labor and management need to reform wasteful work-rules and reach agreements to make development in the boroughs outside of Manhattan financially feasible. Significantly, New York has shown in the past that it is able to innovate to meet the needs of changing times. This track record of innovation augurs well for the future.