To the Members of the Public Subsidy Board,

My name is Anthony Tufariello and I am a Co-Founder and Managing Partner of Cirrus Real Estate Partners. During my more than 35 year career in real estate, I have served in various roles including: member of the Management Committee of Morgan Stanley; Global Head of Global Securitized Products of Morgan Stanley; Global Head of Real Estate of Fortress Investment Group, an asset manager with over $50 billion of AUM; and Chairman of CW Capital, one of the largest special servicers of commercial real estate loans in the United States. During my career, I have overseen the origination of more than $150 billion of commercial real estate loans and made more than $10 billion of real estate equity investments including controlling investments with respect to: Stuyvesant Town, Peter Cooper Village in New York City and Parkmerced in San Francisco. In addition to my previous experience, Cirrus is actively engaged in the development of workforce housing within New York City and the tri-state area utilizing both tax credits and tax abatements with respect to these projects.

First, I would like to thank the Public Subsidy Board for providing us with the opportunity to submit written testimony regarding the calculation of tax savings under New York Labor Law section 224-a and the Board's determination of if a private construction project is covered by prevailing wage requirements pursuant to NYS Labor Law 224-a.

The purpose of New York Labor Law Section 224-a is to require the payment of prevailing wages to workers engaged on certain private construction projects that are funded with taxpayer dollars. The State of New York should ensure that where public monies are being spent, workers are fairly compensated.

Additionally, public money should not be utilized to depress worker wages and benefits. New York Labor Law 224-a was enacted in 2020 and became effective on January 1, 2022. It is disappointing that we are here in October of 2024, over four years after the law was enacted and two years after its effective date addressing these issues. It is also disappointing that the public hearing process set forth in Labor Law Section 224-c is being utilized to delay full and effective implementation of the statute. The Public Subsidy Board and the public hearing process should not be deployed to weaken or diminish the clear statutory language. This process should not be engaged to minimize the scope of projects that require workers to receive the prevailing rate of wage.

Such efforts are in clear contrast to the purpose of the statute, the legislative history, and the clear language of the statute itself.

I. <u>When and how to use Present Discount Value in Calculating Future Tax Savings.</u>

New York Labor Law 224-a expressly states that:

> [a] 'covered project' shall mean construction work done under contract which is paid for in whole or in part out of public funds as such term is defined in this section where the amount of all such public funds, when aggregated, is at least thirty percent of the total construction project costs and where such project costs are over five million dollars except as provided for by section two hundred twenty-four-c of this article.

Among other things, the term "paid for in whole or in part out of public funds" includes:

> savings achieved from fees, rents, interest rates, or other loan costs, or insurance costs that are lower than market rate costs; savings from reduced taxes as a result of tax credits, tax abatements, tax exemptions or tax increment financing; savings from payments in lieu of taxes; and any other savings from reduced, waived, or forgiven costs that would have otherwise been at a higher or market rate but for the involvement of the public entity;

This is a straight-forward formula.

Any savings achieved from reduced tax credits, tax abatements, tax incentives count towards the calculation of the thirty percent threshold of aggregate public funds received by a project.

It is important to note that neither the statute, nor the legislature, makes any mention of valuing the savings achieved from tax credits, tax abatements, or tax exemptions at their present value. If the intention was to only account for the present value of future tax savings, the legislature could have clearly included such a calculation in the statute.

The fact that the statute references "savings" without limitation, as opposed to the present value of such savings, is a clear expression of the intent to include any and all savings in the calculation of tax savings.

Furthermore, there is no doubt that prospective tax savings are a tax savings. Developers rely on these prospective savings when they assess the value of a project and whether or not it is worth building. Public funds are public funds, and whether the savings are realized now or in the future, they are realized. Workers today should not be deprived of a prevailing wage as developers will continue to reap the benefit of a tax incentive twenty or thirty years down the road.

Given my varied historical real estate experience in banking, private equity and development and current focus on real estate credit and workforce housing development, I have been asked to provide testimony which will help contextualize the tangible benefits associated with various tax abatements and tax credit programs regularly utilized by developers and investors in the construction of housing in New York as well as to comment on the impact of these subsidies with respect to the viability and relative attractiveness of these projects.

If all benefits of tax abatements are properly taken into account, they regularly benefit the projects in which they are utilized at a level which is equal to or greater than the gross amount of tax savings provided by these abatements throughout the project life.

In summary this is because tax abatements facilitate development by increasing not just property cash flow on a yearly basis but also by increasing: (i) its ability to obtain financing from both a debt and equity perspective and (ii) increasing its ultimate value through increased exit multiples and tighter capitalization rates including but not limited to:

(1) ***INCREASED INITIAL DISTRIBUTABLE CASH FLOW -*** reducing future property tax burden on the owner of such developed property,
(2) ***MORE PREDICTABLE AND INREASED LONG TERM DISTRIBUTABLE CASH FLOW -*** making the forward net operating income or dividend cash flow from owning such a development more predictable and therefore more valuable,
(3) ***HIGHER CASH FLOW GROWTH RATES –*** similar to compounding of interest, causing forward project net operating income to increase at rates faster than other non-tax abated properties as taxes are not paid on not only year 1 cash flow but future rent growth, often for a number of decades and
(4) ***EXPONENTIALLY INCREASED PROJECT PROFITABILITY AND VALUE -*** facilitating the availability of higher rates of and more cost-effective financing that would have otherwise been at a higher or market rate to a given project given the higher and more predictable cash flow noted in (1) through (3) above.

As Einstein said - "Compound interest is the eighth wonder of the world. He who understands it, earns it … he who doesn't … pays it."

One thing to remember about tax abatements is that they are not one time.

Rather, like the compound interest mentioned by Einstein the quote above, they grow and generally compound in value every year, adding value and profit to a tax abated project exponentially similar to other compounding financial instruments but even more so given their role in facilitating extremely high levels of interest and debt cost savings on these projects that would have otherwise been at a higher or market rate.

In order to demonstrate this, please indulge me and let me take quickly take you through a simple thought experiment, which I have approximated based on the margins we see in places like New York City.

Assume a developer builds a project for $1,000, $300 is land and other costs, there are $700 of total construction project costs.

The project produces rent of $75 and has non-tax operating expenses of $12. If the project does not have a tax abatement, a reasonable assumption on first year taxes is $22 or more dollars a year, leaving less than ~$41 of income, a yield of ~4.0%....no rational person would incur the cost and risk of development for a yield of less than the 10-year treasury (~4.2% today).

However, with a tax abatement: you have increased initial cash flow, more predictable long term cash flow, higher project growth cash flow rates, exponentially higher project value and importantly, access to financing that would otherwise have been at a higher or market rate.

Let me explain in more detail:

(1) With respect to ***INCREASED INITIAL CASH FLOW*** – year 1 cash flow would increase ~$63 from $41, to a yield of 6.3%, ~50% higher than the unabated value and viable in today's rate environment. This yield facilitates the project financeability, significantly decreasing interest costs for the given project in both the short and long term that would otherwise have been at a higher or market rate.

(2) Next ***MORE PREDICTABLE AND INREASED LONG TERM CASH FLOW –*** Assuming a 4.0% growth rate in rents (lower than averages in places like New York City) and a 30 year abatement (the average we see), the gross value of this $22 first year tax savings over time is over $1,200, approximately 170% of the total construction project costs of $700 and more than 100% of the total cost of the project. Importantly, this is highly predictable and therefore highly valued in the markets.

(3) The tax abated project will also achieve consistently ***HIGHER CASH FLOW GROWTH RATES –*** similar to compounding of interest, each year as rents grow, tax savings associated with these abatements increase, exponentially over time, for example at 4.0% growth, by year 30, the $22 abatement savings has increased to over $68 per annum, nearly 10% of the total construction project costs per year.

(4) and finally you have ***EXPONENTIALLY INCREASED PROJECT PROFITABILITY AND VALUE –*** To the extent this project was built and held for thirty years and then sold at a 6.0% cap rate, the increased profitability to the project due to the tax abatement would be ~$1200 (~170% of the total construction project costs) and a greater than 35% increase in profitability of an unabated project with all other variables remaining the same.

It should be noted that this thought experiment does not reflect lower costs of capital available to tax abated projects that would otherwise have been at a higher or market rate due to their higher in place cash flow and more predictable return streams, if this was factored in at lets say 1% interest a year on 65% of the total project costs or approximately $650, the gross value of this savings facilitated by the tax abatement would be $195, ~30% of the total construction project costs.

Reasonable minds may disagree on the exact value of a tax abatement, but on any set of reasonable assumptions, when the overall project benefit in terms of its cash flow, value and financeability are taken into account, there is no instance where it is below the gross value of the tax abatement over its life, taking into account reasonable rates of market revenue and tax growth.

II. The average annual increase in property taxes in New York City vs. New York State

NYC Department of Finance's FY 2022 report on real property taxes shows that between 2003 and 2022, the growth rate on the citywide tax levy averaged 5.88%. At this level of growth, the present value of a typical Long-Term Abatement is ~40% of total project costs and will save the developer ~150-200% of total project costs over the term of the abatement.

Over this same time period (2003-2022), the growth rate on market rents for class A multifamily buildings in NYC was 2.23% per costar data.

Said differently – based on these metrics, taxes have consistently grown far above 2.0% (~200% above this) and far above the rate of rent growth in NYC, making any agreement on a cap at 2.0% quite favorable to landlords and a cap of anywhere below 5.0% inconsistent with historical data.

A 2.0% cap is simply nowhere near in line with average growth rates.

While we would advocate for a longer-term multi-city tax analysis to finalize these metrics, it should be noted that NYC's fiscal situation has begun to garner media attention as it is becoming increasingly clear that NYC will not generate enough revenue to cover its budget in the coming years, likely increasing overall property taxes and importantly, multi-family development's share of these real property taxes.

Even after budget modifications, the city is expected to face budget gaps of 8% of revenue in 2025 and 9% of revenue in 2026. The office of the state comptroller issued a report showing that this budget gap is meaningful despite the City's efforts to reduce the gap through more aggressive revenue projections and reliance on sources of revenue the City has historically not relied on in balancing the budget such as the water board rental payment.

This stress in the budget will likely result in the City turning to higher property tax rates as a means of balancing the budget.

Further, given the market wide stress in commercial properties, multifamily apartments will likely have to bear a disproportionate share of the increased burden of property taxes to offset losses from office space.

All this is to say that, while no one knows exactly what future taxes will be, there is little to no probability NYC taxes will fall and a large probability that multifamily property taxes will increase even more quickly than historically, potentially at compound annual growth rates of 4-7%.

This likely tax increase will make tax abatements even more valuable than ever before for multifamily development because: (i) total tax burden in NYC continues to accelerate and (ii) the multifamily tax base is one of the only large places to glean further property taxes from now that office properties are in such dire straits.

III. How to Calculate the Value of Tax Savings from PILOT Programs

In general, the value of Tax Savings from PILOT or tax abatement programs can be calculated as the sum of the yearly tax savings in each year of the PILOT (the "**Yearly PILOT Tax Savings**") added up through the duration of the PILOT to generate a sum which is the (the "**Total PILOT Tax Savings**").

In this equation the Yearly PILOT Tax Savings in any year is equal to the *difference* between A and B where:

A. Is equal to assessed value of the Property times the total prevailing tax rates if the PILOT was not in place (i.e., County, Local, School):
    a. (the "**Fully Valued Taxes**") where Fully Valued Taxes can be proxied the *product* of (i) and (ii) below:
        i. Dollar Value of New Development *less* Cost of Land ("**Assessed Value**") *times*
        ii. Aggregate tax rate (i.e., County, City, Local, Schools, etc.)
B. Is equal to the payment required under the PILOT in that year
    a. (the "**Yearly Pilot Payment**")

An example of a 10-year PILOT worksheet is below.

PILOT Estimate Table Worksheet

Dollar Value of New Construction and Renovation Costs	Estimated New Assessed Value of Property Subject to IDA (1)	County Tax Rate/1000	Local Tax Rate/1000	School Tax Rate/1000
$1,000,000	$650,000	3.0%	2.0%	1.0%

(1) Assumes Equalization Rate of 65%

PILOT Year	County PILOT Amount	Local PILOT Amount	School PILOT Amount	Yearly PILOT Payment	Fully Valued Taxes	Yearly PILOT Savings
1	$5,000	$3,000	$1,700	$9,700	$39,000	$29,300
2	$5,000	$3,000	$1,700	$9,700	$40,170	$30,470
3	$5,000	$3,000	$1,700	$9,700	$41,375	$31,675
4	$5,000	$3,000	$1,700	$9,700	$42,616	$32,916
5	$5,150	$3,090	$1,751	$9,991	$43,895	$33,904
6	$5,305	$3,183	$1,804	$10,291	$45,212	$34,921
7	$5,464	$3,278	$1,858	$10,599	$46,568	$35,969
8	$5,628	$3,377	$1,913	$10,917	$47,965	$37,048
9	$5,796	$3,478	$1,971	$11,245	$49,404	$38,159
10	$5,970	$3,582	$2,030	$11,582	$50,886	$39,304
Total	**$53,312**	**$31,987**	**$18,126**	**$103,426**	**$447,091**	**$343,665**

Total Project Cost (A)	Estimated Value of PILOT (B) (2)	Value of PILOT as % of Total Project Cost (A) / (B)
$1,000,000	$343,665	34.4%

(2) Excludes any Sales Tax or Mortgage Tax Incentives.

It is important to note that given, the calculations above, the value of any tax abatement or PILOT is directly proportional to three key metrics:

1. Yearly PILOT Tax Savings
2. Duration of abatement
3. Rate of Tax Growth within the taxable authorities in which the property benefitting from the PILOT and / or tax abatement resides.

With this in mind, it should be noted that within NYC a real estate tax abatement is a meaningful subsidy, almost always providing value that is above 30% of total project and construction costs in reasonable underwriting scenarios. Importantly, most NYC real estate tax abatements are materially longer (i.e., 30-40 years under 421-a / 485-x) ("**Long-Term Abatements**") versus

shorter, typically less valuable, payments in lieu of taxes ("**PILOTs**") provided by various Industrial Development Agencies ("**IDAs**").

The longer nature of Long-Term Abatements combined with NYC's comparatively high total property tax growth rates, make Long-Term Abatements typically utilized within NYC, particularly valuable to developers of NYC multifamily and commercial real estate versus most shorter-term PILOTs utilized and issued by IDAs.

For example, when accounting for the total value of tax savings over the span of a 35-year Long-Term Abatement and account for more than 100% of the total costs of the project.

The table below is from a real-time scaled development example in the four boroughs of New York City which was underwritten in June 2024.

Tax Abatement Impact					
Tax Growth	**2.00%**	**3.00%**	**4.00%**	**5.00%**	**6.00%**
Tax Abatement NPV*	$91,625,634	$96,413,261	$101,399,618	$106,591,045	$111,994,031
As a % of Total Project Costs	*30.33%*	*31.94%*	*33.61%*	*35.36%*	*37.17%*
As a % of Construction Costs	*35.78%*	*37.68%*	*39.66%*	*41.73%*	*43.87%*
Total Gross Abatement	$238,381,884	$297,368,553	$373,284,909	$471,308,157	$598,228,359
As a % of Total Project Costs	*78.90%*	*98.50%*	*123.75%*	*156.35%*	*198.57%*
As a % of Construction Costs	*93.08%*	*116.21%*	*146.01%*	*184.50%*	*234.35%*

**Tax Abatement value calculated as the incremental value of the abated taxes at a 5.5% cap rate*

Note, in almost all cases, the tax abatement is worth more than total construction costs in total and nearly half on a present value basis.

This fact pattern is not unique and makes tax abatements the most important and valuable subsidy provided in NYC multifamily development.

Finally, it should be noted that while the growth rate of real estate taxes is important for determining the value of these abatements, the methodology behind calculating the base tax savings is equally, if not more important.

A property tax abatement value should be determined only using the savings assuming a property has leased-up and a full assessment has been made incorporating value and revenue from a fully leased building.

Various services perform these estimates with their results nearly identical as the NYC tax methodology and NYC market rents are well-known.

To the extent developers were allowed to estimate this on their own or create a loop-hole to determine the magnitude of tax savings based on transitional assessments or by only growing taxes during construction by a few percent a year, the value of the tax abatement subsidy would be significantly understated and allow developers with an informational advantage to manipulate their submittals.

Further, property tax savings should be at their gross value or if a net present value is used it should be at the treasury curve flat as allowing developers to choose their own rates could also materially understate abatement savings.

Again, the entire purpose of Labor Law 224-a is to ensure that when a public entity provides public funds to an eligible private project, that those funds are utilized to ensure that workers receive the prevailing rate of wage and benefits. When a public entity receives federal funds to utilize for certain purposes, and the public entity decides to take such funds and provide them to a contractor, subcontractor, developer, or owner of a covered project, such funds must be included in the 30% aggregate and must require the payment of prevailing wages to workers.

Thank you for allowing me the opportunity to submit this testimony.

Anthony Iaparello