

Reengineering Municipal Service Delivery: 1994-2001 Housing Preservation

The Challenge

By 1994, the City owned and managed 5,458 buildings of mostly dilapidated multi-family housing occupied by a low-income population. Since 1978, the City had become “the landlord of last resort” when it foreclosed on residential buildings in tax arrears and took over management. However, the policy of *in rem* vestings (from the Latin for “legal action against property” and commonly used to refer to property acquired by the city through tax foreclosure) was tremendously expensive and led to a stockpile of City-owned, dilapidated housing. While some buildings were returned to private ownership, many more buildings were vested each year, maintaining a permanent inventory of distressed City-owned property.

In the 1970s and 1980s, the City suffered a surge of disinvestment and housing abandonment in many of its neighborhoods. As income decreased and costs increased, many owners were unable to pay the property taxes on their buildings, which ultimately led to City foreclosure.

The cycle of abandonment was particularly hard on tenants who had to endure lack of repairs, basic maintenance, and essential services as the buildings slid towards abandonment. The City had initiated the policy of foreclosure with two goals in mind: to encourage tax compliance and to intervene before these buildings deteriorated completely.

The costs associated with the *in rem* stock were staggering. When this Administration took office, it commissioned a pro bono study by the Arthur Andersen consulting firm that determined that the foreclosed properties had an average tax delinquency of \$36,000 at vesting, yet the City spent an average of \$2.2 million to acquire, manage, repair, and dispose of each vested building. The estimated total cost to the City was \$10.6 billion, excluding an additional average of \$209,000 per property in foregone tax revenues. In addition, despite the City’s large capital investment in these buildings, many of them continued to have significant physical maintenance deficiencies. The average length of City ownership was 19 years.

In rem vestings were stopped in 1993. While this prevented an increase in City-owned distressed property, no strategy was put in place to deal with the distressed housing stock.

The Solution

The City recognized that it could not afford to continue to divert scarce funds toward the management and maintenance of tax delinquent buildings. However, disposition alone would not address the underlying causes of abandonment. A two prong strategy was developed: 1) to return the City-owned inventory to responsible private ownership and 2) to prevent future disinvestment and abandonment of the City's low income housing stock.

HPD reorganized and developed new approaches to privatize the existing stock of City-owned property, to address building needs before they led to abandonment, and to transfer title of distressed properties directly to pre-qualified owners, thereby eliminating the costs to the City of taking ownership, managing the properties, and preparing them for sale. Buildings are fully renovated, and existing legal tenants are protected by ensuring that their rents remain affordable.

The City's privatization effort, known as Building Blocks, targets clusters of occupied and vacant City-owned buildings for renovation and disposition to community-based owners. The buildings' new owners are either qualified groups of low-income tenants, not-for-profit housing organizations, or local real estate professionals.

Public-private partnership is at the core of Building Blocks, and the strategy of leveraging private sector expertise is exemplified by the Neighborhood Entrepreneurs Program (NEP). NEP won an Innovations in American Government award in 1999, the country's most prestigious public sector recognition program. NEP enables small, locally-based real estate professionals to own and manage clusters City-owned buildings. By focusing on neighborhood-based private property managers, HPD rebuilds the local real estate capacity that had been decimated during abandonment and through financial and technical support to the new owners, along with monitoring, ensures long-term quality management and maintenance of the buildings. Entrepreneurs apply to participate in the program through a Request for Qualifications (RFQ).

The Agency would have been shortsighted if it only addressed its existing inventory of *in rem* buildings, but not the future pipeline of at-risk buildings. Therefore, the Agency restructured so it could identify and treat buildings earlier and prevent the need for the City to ever foreclose on them. HPD created tools to address the causes of property tax delinquency and abandonment.

HPD uses a carrot and stick approach: tools such as housing education and low-interest and no-interest building rehabilitation loans for owners who are working in good faith, and aggressive enforcement against owners who are recalcitrant.

In line with the programmatic movement from property management to housing preservation, HPD redeployed nearly 20% of its property management staff to support anti-abandonment.

The final programmatic change was to link tax enforcement with housing preservation. In a cooperative effort with the Department of Finance, HPD and DOF sought legislative change [Local Law 37 of 1996] to enforce tax laws without vesting more properties. In 1994, the administration gathered a group of tax and housing policy experts that recommended the City sell the liens on all tax delinquent properties.

Annual tax lien sales were instituted by the City's Department of Finance in 1996 and have been an effective revenue source on three fronts: net proceeds from the sales, cash received prior to the sale from owners who received notices from the Department of Finance that their properties would be included in the tax lien sale unless they paid their property taxes, and owners who started to pay regularly once they realized the City had resumed aggressive property tax collection efforts.

The policy experts recognized that tax lien sales were the solution for some, but not all, of tax delinquent real estate. Focusing only on tax collection would be insufficient for distressed – and often unoccupied or underoccupied - residential properties. The City has a 3.1 percent housing vacancy rate, and it could not afford to lose any residential housing.

The Administration advocated landmark legislation, passed by the City Council, which fundamentally changed the City's policy for addressing distressed housing. It excluded them from tax lien sales, and prescribed that instead the City would transfer title of distressed properties directly to pre-qualified owners. The buildings would be rehabilitated by the private sector using private financing leveraged with public funds. This fundamental change taps the experience and flexibility of the real estate community to more quickly return buildings to sound physical and financial condition.

At the same time, the Agency introduced its own form of Comstat, internal management and accountability through performance indicators. These key production performance indicators track quantitative objectives in its strategic plan such as Ending City Ownership and Preserving Housing.

Chronology of Implementation

- January 1994** as a result of *in rem* vesting, the City owned and managed 5,458 buildings of mostly dilapidated multi-family housing occupied by a low-income population.
- 1994** the administration gathered a group of tax and housing policy experts to determine a more effective strategy of property tax enforcement and housing rehabilitation
- September 1994** Building Blocks! (a systematic approach to privatizing the *in rem* housing stock) was introduced.
- December 1994** The Mayor launched ANCHOR, a comprehensive plan to foster homeownership and commercial development in underserved neighborhoods.
- April 1995** Pro Bono Arthur Andersen/Andersen Consulting study of the costs of the policy of *in rem* vesting was commissioned.
- May 1996** the City obtained historic legislation, Local Law 37, which transformed its property tax foreclosure authority to transfer title of distressed properties directly to pre-qualified owners, thereby eliminating the costs to the City of taking ownership, managing the properties, and preparing them for sale.
- June 1997** the City initiated the first pilot Third Party Transfer Program *in rem* action against 174 tax delinquent properties in tax map Section 10 of the Bronx.
- October 1997** The Agency created the Office of Anti-Abandonment to preserve affordable privately-owned housing and to reduce real estate tax delinquency in the City.
- August 1999** 46 properties (27 buildings and 19 vacant lots) in the Third Party Transfer Program Bronx pilot were transferred to Neighborhood Restore, with interim management provided by the designated owners.
- September 1999** The second Third Party Program *In Rem* Action was initiated against 298 properties.
- October 1999** The Neighborhood Entrepreneurs Program (NEP), a Building Blocks program, won the prestigious Innovations in American Government Award bestowed by the Ford Foundation and Harvard University.
- November 1999** The agency created the Owner Services Program which provides counseling and assistance to owners working in good faith to address problems with their buildings.
- February 2000** The 1999 Housing and Vacancy Survey (HVS) reported that housing and neighborhood physical conditions in the City were better than any other time in the 35-year history of the survey. The 1999 dilapidation rate was just 1.0 percent, the lowest ever since the first HVS in 1965.
- May 2000** The Third Party Transfer Program was recognized as an innovative program by Innovations in American Government award program for linking tax enforcement with housing preservation.
- August 2000** Neighborhood Restore completed the transfer of all 15 of its multi-family buildings in the Third Party Transfer Program Bronx pilot,

containing over 270 units, to the new for-profit and not-for-profit owners.

November 2000 The Third Party Transfer Program won the Pioneer Institute's Better Government 2000 Competition.

Outcomes

The result of the changes has been to markedly improve the housing conditions and quality of life of New York City residents, particularly those living in the most dilapidated buildings. The 1999 Housing and Vacancy Survey (HVS) reported that housing and neighborhood physical conditions in the City were better than any other time in the 35-year history of the survey. The 1999 dilapidation rate was just 1.0 percent, the lowest ever since the first HVS in 1965.

HPD accelerated its disposition efforts in order to end the City's role as "landlord of last resort," resulting in a 70% reduction in City-owned apartments from 44,000 units in 1994 to an all-time low of 13,278 units in occupied and vacant buildings. Through Building Blocks, this Administration funded the rehabilitation and return of all occupied units and most vacant units to responsible private ownership. In January, 2001, the Mayor announced funding for the remaining units in vacant buildings to end completely City ownership of tax-foreclosed residential real estate.

This editorial from August 6, 1997 dramatizes the transformation of entire City blocks. "A Daily News investigation found [West 140th Street] to be the "sickest block in New York" in 1994...now...West 140th Street is on the mend. Credit goes largely to Mayor Giuliani's Building Blocks program, a masterpiece of public-private partnership that has brought 140th St. – and blighted blocks in Central Brooklyn and the South Bronx – back from the dead."

Rehabilitation of the most distressed, tax delinquent buildings occurs sooner, providing the City with an additional source of decent, affordable housing. Compared to the average length of City ownership of *in rem* properties was 19 years, now buildings can be conveyed to responsible private owners within two years.

There has been a 50% drop in real estate tax delinquency rate from 1996 to 2001 valued at \$188 million, and \$1.4 billion cash to City as a result of tax lien sales from 1996-2001. This improved property tax collection has increased the funds that are available for City-wide services.

Another outcome is cost avoidance. Had the City taken ownership of the 174 properties in the Bronx Third Party Transfer pilot under the prior *in rem* foreclosure approach, they would have stayed in City ownership for an average of 19 years. During that time it would have cost the City as much as \$382.8 million to manage, and dispose of those properties. Through the Third Party Program the City avoided this cost by using its new *in rem* foreclosure process, returning the buildings to tax paying status with responsible new owners, and leveraging its financing with private sector funds to achieve building rehabilitation.

In one of the Bronx Pilot properties, 1203 Fulton Avenue, one elderly resident described the impact of the Third Party Transfer Initiative on her building and her life. Ethyl Moses said, "For the past 10 years this building has been in terrible condition. When the

new owner came in they started making major repairs. They did the floors, they replaced the windows and doors, and they are redoing the bathroom and kitchen. It is wonderful and I am very grateful that these repairs are being made. I will finally have a nice place to live.”

The City’s housing vacancy rate is approximately 3%, and the need for affordable housing is especially critical in the neighborhoods where the affected properties tend to be located. More than 6,000 units will be preserved through Third Party Transfer where the existing owner is either tax delinquent, irresponsible, and/or failing to maintain essential services for his/her tenants. These units will be transferred to new responsible owners with rehabilitation funding to ensure their long-term viability as quality affordable housing.

HPD targets the Third Party Transfer Initiative to neighborhoods where housing revitalization is a critical need, and where the Initiative will enhance other HPD investment. These neighborhoods are among the City’s poorest and most distressed, as evidenced by the following statistics in the 1996 Housing and Vacancy Survey: renter-occupied households below the poverty line (51.3% in neighborhoods with Third Party Transfer actions v. 20.6% City-wide), unemployment (30% v. 11.2%), and located on streets with a building with broken or boarded up units (41% v. 11.4%).

Since FY94, 73,090 apartments and homes have been constructed or rehabilitated through city-sponsored programs, including 12,850 homeownership townhouses, co-ops, and condos.

There was a net gain of 62,000 housing units between 1993 and 1999 according to the Housing and Vacancy Survey conducted by the U.S. Bureau of the Census.

HPD provided low-interest financing so that 22,937 units of housing in privately-owned buildings with primarily low-income tenants could be rehabilitated.

More than 11,600 owners, building managers, and maintenance staff attended free classes in management, systems maintenance, building finances, and tenant relations offered by HPD’s Housing Education Program. HPD’s preservation initiative focuses on education, investment, and enforcement in privately-owned buildings citywide.

The City has more Housing Maintenance Code Inspectors than at any time since New York State stopped funding Inspectors in 1991 and completed 1,063,570 inspections. The agency also initiated 1,799 cases in Housing Court against recalcitrant landlords and assisted tenants in bringing 46,424 actions against their landlords.

The Agency has institutionalized Comstat-like performance indicators. These indices are updated daily and discussed with the Commissioner monthly.

Further Challenges

The Agency is in the process of implementing the housing initiatives announced in the '01 State of the City Address, namely to complete the divestiture of the city's *in rem* vacant buildings, to prevent any additional housing units from falling into the city's hands due to tax foreclosure, and to build homes and apartments as mixed-use residential and commercial developments so that residents will be able to shop and work near where they live. Altogether, this approach will create or preserve more than 10,100 units of housing. This is a \$1.3 billion plan to transform the vacant shells of buildings you see across the city into quality affordable housing [1,100 units], to never again repeat that cycle of abandonment that devastated some of our neighborhoods in the 70s and early 80s [6,000 units], and to transform our under-served neighborhoods with 875,000 square feet of new restaurants, stores, and commercial services as well as housing [3,000 units].

- **ENDING CITY OWNERSHIP AND MANAGEMENT OF DISTRESSED HOUSING** Complete *in rem* privatization. What is newly funded is the rehabilitation and privatization of the remaining 133 vacant *in rem* buildings.
- **BREAKING THE CYCLE OF ABANDONMENT** Conduct annual *in rem* tax foreclosure actions and preserve an additional 6,000 units through Third Party Transfer where the existing owner is either tax delinquent, irresponsible, and/or failing to maintain essential services for his/her tenants. These units will be transferred to new responsible owners with rehabilitation funding to ensure their long-term viability as quality affordable housing.
- **ENCOURAGING ECONOMIC DEVELOPMENT IN DISTRESSED AND FORMERLY DISTRESSED NEIGHBORHOODS** Create an additional 3,000 units in mixed-use developments along with 875,000 sq ft. of commercial space.

The premise behind HPD's mixed-use initiative is to redevelop vacant, City-owned land, attract commercial businesses, and create employment opportunities in under-served areas. Combine this with concentrated homeownership development and you have the components of successful neighborhood revitalization. HPD calls this ANCHOR, as in Alliance for Neighborhood Commerce, Home Ownership, and Revitalization.

In neighborhoods where the City is making a significant investment in housing, that housing is only viable in the long term if the new homeowners have local places to shop, work, go to a movie, or get neighborhood-based commercial services.

ANCHOR uses a combination of City, State, Federal, and private funds to finance newly constructed retail space along targeted commercial corridors, generating over \$250 million in new private economic activity in distressed neighborhoods. Under this mayoral initiative, HPD is working with the NYC Partnership,

commercial banks, developers, and community-based organizations. ANCHOR creates a sound commercial environment that encompasses improved security, transportation, sanitation, and business assistance services. Public subsidies write down the high cost on new construction to produce rents that are affordable to local retailers and attractive to national and regional businesses.

Reducing the cost of construction and reforming the industry is a further challenge. The cost of construction in New York City is heavily inflated – between 21 and 55 percent higher than cities such as Los Angeles, Chicago and Dallas. Manhattan District Attorney Robert Morgenthau’s investigation of the interior construction contractors suggests that as much as 20% was added to the cost of projects undertaken in the 1990s. To create a favorable climate for housing construction for years to come, the Mayor has emphasized that the City must work to:

- **Remove organized crime** from the industry by passing an updated and improved version of the reform bill introduced in the City Council in 1998;
- **Rezone vacant manufacturing land for commercial and residential use;**
- **Reform the Building Code;**
- **Reform the Buildings Department;**
- **Reduce the number of “red tape” reviews** a housing plan must go through, including zoning, environmental, and permitting and land use review procedures.