



**Testimony of First Deputy Commissioner Michael Hyman**  
**Evaluating New York City's Real Property Taxation System**

**New York State Assembly**  
**Standing Committee on Real Property Taxation**

**January 22, 2016**

Good afternoon Chair Galef and members of the Assembly Standing Committee on Real Property Taxation. My name is Michael Hyman, and I am the First Deputy Commissioner at the New York City Department of Finance. With me today are Timothy Sheares, Deputy Commissioner for the Property Division; Carl Laske, Chief of the Real Property and Legal Counsel Unit; and Samara Karasyk, Assistant Commissioner of External Affairs.

The New York City Department of Finance (DOF) collects revenue for the City of New York. The property tax is the most important source of City tax revenues, generating \$22.6 billion this fiscal year — 42 percent of total City tax revenues. Overall, the City is projected to generate \$53 billion in tax revenues this year, \$34 billion of which is administered by the Department of Finance.

Under Commissioner Jacques Jiha, our work at the Department of Finance is guided by four principles integrated throughout our administration: fairness, excellent customer service, transparency and efficiency. We work to promote these principles while valuing more than one million properties annually and administering other parts of the property tax system. Explaining to the public how properties are valued and taxes are computed can be challenging. The New York State real property tax laws that govern the structure and fundamental workings of the City's property tax system are complicated, and it can be difficult to understand the system's intricacies. Thank you for giving us the opportunity today to discuss the City's property tax system and Department of Finance property tax-related initiatives.

The current-day NYC property tax system was established by the enactment of chapter 1057 of the Laws of 1981, known as S.7000A, in response to the Court of Appeals' decision in the landmark 1975 case, *Hellerstein v. the Town of Islip*. Prior to 1975, properties were valued unevenly, with small homeowners in particular being valued at a lower percentage of market value than other properties. The Hellerstein decision ruled that all property must be assessed at full market value. Six years later, S.7000A was enacted over a gubernatorial veto. This legislation prevented the major redistribution of property taxes that a strict

implementation of the Court of Appeals' decision would have produced. Instead, the law established a property tax system with:

- Multiple categories, or tax classes, of property in New York City and Nassau County
- Fractional assessments (assessed value is only a fraction of market value) that could vary by tax class
- Valuation restrictions
- Caps on the increases of assessments for certain types of properties
- Annual adjustments for determining the share of the tax levy paid by each of the tax classes, with mechanisms to prevent abrupt shifts in the share paid by each tax class

Many of the political decisions made as part of S.7000A and in the years since 1981 have underlying policy rationales to protect groups of property owners. But the combined impact of the decisions has raised issues about the fairness of the distribution of the property tax burden, both within and among the various categories of New York City properties.

Under the current property tax system, City properties are categorized into four different tax classes. The classification of properties has remained generally constant since 1981. Tax class 1 consists of one- to three- family homes and comprises two-thirds of all parcels in the City. Tax class 2 is comprised of all other residential properties: rental apartment buildings, cooperatives (co-ops), and condominiums. Class 3 is made up of utility properties, including "special franchise" property under the public rights of way, and Class 4 includes all other commercial properties, such as office buildings, stores and hotels.

The Department is charged with determining the market value of all of these properties annually, which it does through data collection, statistical modeling, property inspections, reviews of property owner income and expense filings, as well as other techniques. Class 1 properties are valued using a comparable sales approach. Most large class 2 and class 4 properties are valued using the income capitalization approach.

These are standard mass appraisal methodologies, but special challenges in valuing certain categories of properties emanate from State tax law restrictions. The most important valuation restriction is Real Property Tax Law (RPTL) section 581, which requires the Department to value class 2 co-ops and condominiums as though they were rental properties. This requires DOF to compare such properties to “similar” income-generating rental buildings in order to estimate a property’s potential net income, and then apply a capitalization rate to generate the property’s Department of Finance market value. DOF is prohibited from valuing co-ops and condominiums using sales data. Consequently, each year DOF must use statistical modeling and assessor reviews to develop rental comparables, which serve as the basis for valuing what are predominantly owner-occupied properties.

RPTL 581 creates parity issues regarding the valuation of different types of residential properties and of different subsets of co-ops and condos. Because DOF values rental properties based on annually submitted Real Property Income and Expense data and does not project the future cash flow of a property and potential future uses of a property — which investors generally do in valuing a property — class 2 property values are generally below their fair market value based on sales. And co-ops and condos tend to be undervalued more than rental properties — in part, because regulated or partially regulated apartment buildings can serve as comparables for co-ops and condos in prime real estate locations. RPTL 581 creates special issues in valuing high-end co-op and condo apartment buildings, for which finding adequate rental comparables can be problematic.

Understanding how comparables work and why they are used is not intuitive for property owners. Valuing properties by methods that are artificial and not used by property owners when they buy and sell their homes creates confusion for owners and major transparency issues for the Department of Finance in explaining values used for City property tax purposes.

As important as valuation is to the property tax system, it is only the first step in determining property taxes. After values are determined, market value is converted into assessed value — the value to which NYC property tax rates are

applied. As noted, the law allows fractional assessments of properties, and each tax class has a target assessed value-market value ratio — assessed value cannot exceed the target ratios. The current target assessed value ratio for tax classes 2, 3 and 4 is 45 percent, while the ratio for tax class 1 is 6 percent. Class 1's ratio is lower, at least in part, because the Department of Finance's values for small homes are closer to sales-based values than for properties in the other tax classes. The "effective" assessed value ratios — assessed value compared to sales-based market values — of larger residential properties and income-generating commercial properties are generally well below 45 percent.

To protect small homes and small residential apartment buildings (with fewer than 11 units) from large year-over-year tax increases, statutory restrictions limit the annual increases in assessed value that they can receive to: 6 percent a year or 20 percent over five years for class 1 properties and 8 percent a year or 30 percent over five years for small class 2 properties. While these caps were created to protect small property owners, they create inequities when market value growth exceeds assessed value growth in some neighborhoods but not others. And they create confusion when the assessed value increases in years when market value decreases or stays the same, which occurs when an assessed value rises to the target ratio (6 percent of market value for class 1) to catch up for caps imposed in more prosperous years.

After a property's assessed value is determined, exemptions are applied. Exemptions are enacted to serve public policy purposes, whether to incentivize construction or renovations, or to assist a vulnerable section of the population. But property tax exemptions add to the disparities in the effective tax rates paid by similar-type properties.

Once taxable assessed value is determined, there are additional steps to determine a property's tax liability. As noted, the City's four tax-class system was established in 1981 as a result of the Court of Appeal's decision in 1975 that all properties be valued at fair market value.

Each class is responsible for a share of the total tax burden (levy). The initial class shares were based on each class's share of total assessed value in Fiscal Year

1982, which codified historical inequities in assessment practices. Shares were to be adjusted annually to reflect exemption changes, reclassification of properties and physical changes, such as new construction and demolitions. The law also required periodic adjustments to reflect changes in market value, but this did not occur until 1993. In fact, due to political decisions, the levy share for tax class 1 small homeowners relative to its market values share decreased in the 1980s.

Beginning in Fiscal Year 1992, a mandatory adjustment to class shares based on market values was established. But the base year used for determining class shares was FY 1991, securing the reduction in the levy-share-to-market-value share ratio for class 1 that occurred over the prior decade. Statutorily, the annual adjustment to any tax class's share of the levy cannot increase more than five percent. But in many years since the new methodology was implemented, the City has sought legislation to lower the cap below five percent, primarily to the benefit of class 1 property owners.

A tax class's share of the levy is directly related to the tax rate computation for the class. Once the levy share is determined, it is then divided by the tax class's total taxable assessed value to compute its tax rate. The final step in computing liability is the implementation of abatements, which reduces the tax liability of eligible owners after taxes are calculated.

This brief overview of how tax liability is computed, and the impact of political decisions over the years, highlights that while the Department of Finance's job is to value properties fairly and equitably, the valuation methods are impacted by legal constraints. Most importantly, the ultimate tax burden of different types of property owners reflects both historical and current-day political decisions. To summarize:

- Issues regarding the relative tax burdens of different residential groups (homeowners, co-op and condo owners, rental properties) and the relative tax burdens of properties within the groups are primarily the product of:
  - Assessment increase caps adopted to protect select property owners from large annual tax increases;
  - Legally mandated restrictions on how co-ops and condos are valued;

- Political decisions regarding the relative shares of the tax levy borne by classes 1 and 2; and the
- Impact of exemptions and abatements adopted to address equity and housing stock issues.
- Issues regarding the relative tax burden borne by commercial versus residential properties also reflect political decisions regarding the tax levy shares borne by the different tax classes.

At the Department of Finance, our responsibility is to value properties accurately and to administer the property tax fairly, within the parameters that New York State and New York City laws allow. To return to my opening comment, our work at the Department of Finance is guided by the four principles of fairness, customer service, transparency and efficiency, which means we work hard to promote and bolster these principles as we administer the tax laws.

Therefore, we strive for fairness in our valuations. Our goal is to treat like properties similarly as we value properties. We have made great strides through the hiring of additional assessors, enhanced assessor training, empirical modeling and improved data collection. All of this has improved the accuracy of our values, including the quality of comparables selected for valuing co-op and condominium buildings.

We are also in the process of upgrading our technological infrastructure for property tax administration, which will provide a much more vibrant set of electronic services for the public. We are reengineering our exemptions processes to ensure that eligible applicants receive the benefits they deserve. We are streamlining our application processes to simplify filing requirements for property owners. As part of these efforts, last year, we launched a short form for some owners to use when they file their Real Property Income and Expense statements. This new form is available to 31,000 tax class 2 and 4 required filers, and makes it easier and faster for them to comply with the requirement to annually submit income and expenses to the department.

Another component of our mission to provide quality customer service was the creation last year of the Office of the Taxpayer Advocate. This independent office

within DOF assists the public with issues they may have regarding DOF's administration of the property tax, as well as with other City-administered taxes, and makes recommendations to address systemic agency issues.

The Office of the Taxpayer Advocate recently developed a Taxpayer Bill of Rights. This document clearly explains to New Yorkers what their rights are when interacting with the Department of Finance. This information is translated into multiple languages and is available on our website, at our public Business Centers, and elsewhere. In the last week, we sent every property owner in the City a copy of the Bill of Rights along with their January Notice of Property Value.

Our efforts in customer service extend to the outreach that we do to help people understand how property taxes work. The above-mentioned Notices of Property Value includes details about each property in the City and how the property was valued. It also informs the public how they can challenge their values if they believe they are not correct and when and where we will be holding public workshops throughout the five boroughs where we offer in-person assistance to anyone who has questions about their values.

We have developed property tax guides that use clear language and infographics to breakdown the property tax system for all residential property owners. These guides are translated into multiple languages, and our Outreach team uses them year-round at events with property owners. We are constantly improving our website to provide access to a variety of comprehensive materials that explain property valuation methods, assessed valuation rules, details on property roll data and general information on New York City property taxes. Last year, the agency released interactive web maps displaying property information for class 1 homes. In a few weeks, we will be releasing the same maps for class 2 residential properties as well.

In conclusion, we believe that we have made great progress at the Department of Finance in improving our business processes and customer service and we remain focused on additional enhancements. The improvements we are implementing are relevant even if components of the property tax system were to be changed.



Property tax reform obviously raises important and complicated political and policy issues. There are multiple, inter-related steps to determining a property's tax liability. So, changing one part must take into account the implications for other parts of the computation.

For example, as I have noted, class 1 properties are valued using comparable sales, and class 2 co-ops and condos are valued, as required by law, as though they are rental buildings, which results in lower-than-sales-based values. But the taxes paid by properties are also affected by assessed value rules, class share treatment and exemptions and abatements. Department of Finance studies have found that, although Department of Finance market values at the unit level are very different for small homes than for co-ops and condominiums, at least in some years, the median effective tax rate — taxes as a percentage of estimated sales-based values — paid by small homes is not that different than the median rate paid by co-op and condo buildings. Variability around the median, however, can be significant.

Reforming the New York City property tax system will require some hard political decisions. Balancing the goals of tax equity, tax burden stability at the parcel level and New York City tax revenue stability at the macro level will not be easy. Ultimately, tax reform will likely require at least some redistribution of the tax burden, and the “losers” will not be shy about expressing their opinions. Despite the challenges, today's hearing is an important step in highlighting issues regarding the property tax system.