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Racing to dig before 421-a code changes

Developers who won't make deadline get creative

By JAMES KELLY

Builders around the city are racing to get projects started in order to beat a looming deadline.

Upcoming changes in the 421-a tax abatement policy — which will make requirements for receiving benefits stricter, in addition to lowering the level of benefits — are driving builders to get multifamily developments in the ground prior to June 30.

Meanwhile, those who realize they won't make the deadline are figuring out creative ways that they can work around changes in the 421-a policy, like carving projects into small individual units and cutting back on monthly maintenance fees.

Alchemy Properties, for example, felt the pressure to get two new developments into the ground in the last two months: a condo building at 303 East 77th Street in April and luxury condos at the former Sony Studios at 800 Tenth Avenue in mid-May.

Another developer, who declined to be named, is building an 18-story, 60,000-square-foot mixed-use condo at the southwest corner of 14th Street and Third Avenue, and needed to take out a high-interest, \$10.24 million bridge loan in order to do demolition and get a foundation in the ground before June 30. A conventional construction loan would have taken three to four months to obtain, compared to the two weeks it took to get the bridge financing, said Gregg Winter, the principal of W Financial, who originated the loan.

"Even though the borrower had a construction loan lined up, it was just far too risky for them to count on it closing in time to commence on the foundation by June 30," Winter said.

One strategy that the assessed value change has spawned among perceptive developers who know they are going to miss the deadline: the division of projects

into more units of smaller size.

Real estate lawyer Paul Korngold, partner of the firm Tuchman, Korngold, Weiss, Lippman & Gelles, said he has already seen this from a client of his in Woodside who expects to break ground after July 1.

"If you have 42,000 buildable square feet, you are now going to be more inclined to make 60 apartments that are 700-square-foot studios, than 20 big 2,100-square-foot homes," Korngold said. The explanation: Projects started after the cutoff date will receive a cap on their tax abatements at an assessed property value of \$65,000 per unit.



Gregg Winter obtained bridge financing for a developer of a 14th Street project.

Since each smaller unit will have less value in excess of the \$65,000 cap, the builder will get the most amount of abatement for their money.

Another real estate attorney, Luigi Rosabianca of Rosabianca & Associates, also mentioned ways developers are "getting creative" with the impending changes in abatement policy.

He pointed out that while a developer might choose to build three adjacent one-bedroom units where he would have previously built one three-bedroom unit, the

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floorplans are often designed in such a way that if later on a buyer wanted to convert the three apartments to a single unit, it would not be difficult.

Of course, if the buyer wanted to combine the units to get a resulting three-bedroom, they'd have to forfeit the abatement received on two of the units that get combined. "Of course, if somebody is looking for a three-bedroom, [the abatement] is less of a concern than for somebody looking for a studio or a one-bedroom," Rosabianca noted.

Another strategy is for developers to hold down costs elsewhere. One of Rosabianca's clients, a developer in Murray Hill, realized he was going to miss the July 1 cutoff for his residential project, which wasn't a "high-scale" project, according to Rosabianca.

"Once he realized he wasn't going to make the deadline for uncapped tax abatement, the developer opted to scale back amenities, thus reducing the common charges," Rosabianca said. Due to the nature of the development, Rosabianca's client believes the cost of monthly fees is an important factor to potential buyers. The decrease in monthly common charges, the developer figured, somewhat compensated for the increased monthly real estate taxes.

Expanded area

Developers who don't get their projects in the ground before the June 30 cutoff date will be required to build 20 percent low-income housing within their projects in order to qualify for the tax breaks in more areas of the city. A low-income minimum is currently required to obtain the abatement from 96th Street south to 14th Street, as well as in the West Village. On July 1, this zone — known as the Geographic Exclusion Area, or GEA — is set to expand to include all of Manhattan and parts of the outer boroughs.

The new GEA will include parts of Long Island City, Astoria, Elmhurst, Jackson Heights, Flushing and Woodside in Queens; most of East Williamsburg, parts of Fort Greene, Crown Heights and Sunset Park, and all of Greenpoint, Wil-

liamsburg, Downtown Brooklyn, Brooklyn Heights, Carroll Gardens, Boerum Hill, Red Hook and Park Slope in Brooklyn; Mariners Harbor, Port Richmond, New Brighton and Clifton in Staten Island; and Crotona Park, Melrose and Mount Eden in the Bronx.

Low-income requirements in the GEA are designed to propel building of cheaper apartments in neighborhoods where it wouldn't normally be practical for a developer to build them. While the GEA expansion is intended to spur building of affordable housing in less affordable communities, almost every expert contacted by *The Real Deal* predicted it will have a negative effect on the industry. Developers previously took the abatements for granted, they say, and taking the benefits away will slow development in the new GEA, which is already dragging from the credit crunch. Development in some areas, they said, may grind to a halt.

"I think that fundamentally, this change makes market-rate housing more expensive ... and we're going to see housing production affected dramatically," said Francis Greenburger, founder and CEO of real estate investment company Time Equities, and no stranger to criticizing real estate tax policy. Greenburger openly criticized the city and state's taxing policies for condo conversions in a 1990 New York Times article.

Greenburger said that while he is very sympathetic with the city's need for affordable housing, he believes the amount of income a developer loses by making one-fifth of a project low-income housing will simply deter them from aiming for the abatement in many cases. If the developer did fulfill the 20 percent requirement, he noted, they would need to mark up the market-rate component of the project to compensate for the lost profit.

"In effect, it costs you more to build market-rate housing," he said. "It's always a very expensive step for people to buy a new home, so to be hitting them up with this extra cost, I think it's going to be a real issue."

Aptsandlofts.com president David Maundrell said that

the loss of abatements stands to make larger developments — 2,500-square-foot to 5,000-square-foot plots — prohibitively costly for many developers in Williamsburg.

Adding insult to injury, Maundrell said the overall market there is hurt by developers' rush to make the June 30 date. He said a sudden oversupply will likely decrease the value of units at these projects once they come to market.

"[The policy change is] forcing developments to come to the market all at the same time, and buyers notice this," Maundrell said. "And it's causing them to think, 'I'm just going to wait a little while.'"

A major goal of expanding the GEA was to push market-rate building activity farther out to so-called fringe neighborhoods, formerly passed over by such developments. Insiders who spoke to *The Real Deal*, however, were skeptical that the tax-regulation change would have this effect.

Nicholas LaPorte Jr., executive director of the Associated Builders and Owners of Greater New York, said that while the policy attempts to push developers farther into the boroughs, he doesn't think they are going to start projects there.

"[The new policy] is asking developers to put large projects in neighborhoods, communities that don't have the demand for that ... in Bushwick, for example," he said. "Developers just won't be able to get the prices for those units required to cover their building costs."

LaPorte added that between the credit crunch and rising costs of land acquisition and construction, he doesn't foresee any low-income housing produced under 421-a without additional government assistance.

Korngold believes that once the deadline to get in the ground passes, more creative strategies to deal with the new policy will surface.

"Most developers right now are just focused on beating July 1, and they don't focus on the details," he said. "Then, after July 1, I think they are going to get a lot more sophisticated on 421-a." **TRD**