

AFFORDABLE HOUSING NOW + NEXT

NIXON PEABODY LLP



The developers guide to “Affordable Housing NY Program” AKA the 421-a tax exemption

Introduction

In April 2017, New York enacted a new version of the Real Property Tax Law 421-a known as the Affordable Housing NY Program—the new tax exemption meant to spur development and create much-needed affordable housing. This client alert is meant to provide an overview of the Affordable Housing New York Program, as well as key considerations for developers looking to plan ahead for existing and future projects. Nixon Peabody’s nationally recognized Affordable Housing practice group stands ready to advise our developer clients on the new Program and how it may fit into both existing new projects on the horizon.

Summary of previously enacted changes applicable to the Affordable Housing New York Program

The Rent Act of 2015 made numerous changes to the existing 421-a tax exemption that are now law, including:

- Changes to the rent registration requirements for market-rate rental units in projects that receive the 421-a tax exemption. Previously, any rental unit in a building with the 421-a tax exemption was required to register with the New York State Division of Housing and Community Renewal. Going forward, only units with rents that are within the Rent Stabilization Laws will be registered. Units with rents that exceed the maximum permissible rents determined by the Rent Guidelines Board will be free-market.
- Affordability restrictions will be for a period of 35 years in buildings with affordability requirements.
- The current two-part application process for the 421-a tax exemption will be changed substantially. Benefits are applied for only after completion of construction (i.e., after issuance of either a full temporary certificate of occupancy or permanent certificate of occupancy for the building eligible for benefits), and **the benefits will be retroactive as opposed to available during construction as they were in the past**. Construction benefits are available for up to three years.

- The Affordable New York Housing Program is available for rental and homeownership projects if (1) construction was commenced on or before December 31, 2015, and (2) the projects did not receive benefits prior to the enactment of the Rent Act of 2015.

Summary of rental benefits for buildings with less than 300 units or outside of the enhanced affordability areas

Benefits are available primarily for rental projects and will include a 100% real estate tax exemption for up to three years during the construction period, and an additional 35 years thereafter. For the first 25 years, projects will receive a 100% tax exemption. During the remaining 10 years, the exemption will be equal to the percentage of affordable units in the project. Every rental project with less than 300 units or outside of the Enhanced Affordability Area are required to meet one of the following three affordable housing options in order to receive the 421-a tax exemption:

Option A

- 25% of the units must be affordable, with at least 10% affordable at up to 40% of the area median income (AMI), 10% at up to 60% of the AMI and 5% at up to 130% of the AMI; and
- This option also precludes the developer from receiving any governmental subsidies other than tax-exempt bond proceeds and 4% tax credits.

Option B

- 30% of the units must be affordable, with at least 10% affordable at up to 70% of the AMI and 20% at up to 130% of the AMI.

Option C

- At least 30% of the units must be affordable at up to 130% of the AMI;
- This option also precludes the developer from receiving any government subsidies; and
- The project cannot be located south of 96th Street in Manhattan or in any other area established by local law.

Summary of homeownership benefits

Although the Rent Act of 2015 was heavily focused on mixed-income rental properties, there are still options available for condominium and cooperative developers seeking to build homeownership projects outside of Manhattan. Under the Affordable Housing New York Program, certain homeownership projects are eligible for a 100% real estate tax exemption for up to three years during the construction period, with an additional 20-year exemption thereafter. For the first 14 years, projects will be eligible for a 100% exemption. Thereafter, projects will be eligible for a 25% exemption for the remaining six years, subject to an assessed valuation cap of \$65,000 per unit.

Homeownership project eligibility criteria

- Projects must be located within the four boroughs outside of Manhattan, including Brooklyn, Bronx, Queens and Staten Island;
- Homeownership segments or projects shall not contain more than 35 residential dwelling units;
- Condominium and cooperative homeowners must agree to use their home as their primary residence for at least five years after the date of purchase; and

- Upon the first tax assessment following construction completion, the condominium or cooperative project must have an average assessed value that does not exceed \$65,000 per dwelling unit.

Summary of wage requirements for projects with 300 or more units

Developers of rental projects with 300 or more units in an Enhanced Affordability Area¹ must pay certain wages and set aside a certain number of units as affordable housing in order to be eligible for the 421-a tax exemption.

To meet the wage requirement, the developer must pay an average hourly wage of \$45 for projects in Brooklyn and Queens, and \$60 for Manhattan projects. These hourly wages are set to automatically increase every three years at a rate of 3%. For these large projects, the value of the tax exemption is 100% for 35 years after the construction period. The affordability restrictions shall remain in place for 40 years from the date of commencement of benefits, which means that developers will be required to maintain affordability for an additional five years after the exemption expires.

While the wage and benefit requirements are aimed at large projects within an Enhanced Affordability Area, projects with 300 or more units outside such areas may also opt-in and take advantage of the extended benefits that are available under this new option.

Although the wage requirement is mandatory for large-scale projects in an Enhanced Affordability Area that wish to receive the 421-a tax exemption, there are two ways to opt-out: 1) set aside at least 50% of the units as affordable up to 120% of the area median income, or 2) enter into a Project Labor Agreement.

Summary of affordability options for projects with 300 or more units

Option E

- At least 25% of the units must be affordable, with at least 10% of those units affordable at up to 40% of the AMI, 10% at up to 60% of the AMI and 5% at up to 120% of the AMI.
- This option also precludes the developer from receiving any governmental subsidies other than tax-exempt bond proceeds and 4% tax credits.
- This option is available within enhanced areas, including Manhattan below 96th Street, Brooklyn Community Boards 1 & 2 and Queens Community Boards 1 & 2.

Option F

- At least 30% of the units must be affordable, with at least 10% of those units affordable at up to 70% of the AMI, and 20% at up to 130% of the AMI.
- This option is available within enhanced affordability areas, including Manhattan below 96th Street, Brooklyn Community Boards 1 & 2 and Queens Community Boards 1 & 2.

¹ Enhanced affordability areas include certain neighborhoods in Brooklyn, Manhattan and Queens, as defined in more detail in the actual text of the Affordable Housing New York Program.

Option G

- At least 30% of the units must be affordable at up to 130% of the AMI.
- This option is available within Brooklyn Community Boards 1 & 2 and Queens Community Boards 1 & 2.
- This option also precludes the developer from receiving any governmental subsidies.

Reporting and monitoring requirements for projects with 300 or more units

For large-scale projects with wage mandates, the proposal also requires developers to hire an independent monitor to provide a certified payroll report to the New York City Department of Housing Preservation and Development (HPD) annually. The proposed law also requires a third-party fund administrator to handle underpayment of benefits, and explicitly limits a private right of action in enforcing the reporting and monitoring requirements.

Summary of extended benefit program for certain existing projects receiving the Section 421-a tax exemption

In addition to the new benefits offered by the Affordable Housing New York Program, the Rent Act of 2015 also created extended benefits for rental projects that are now available for certain projects that: 1) commenced construction prior to July 1, 2008, 2) include affordable units and 3) previously qualified for either a 20-year or 25-year tax exemption under the previous version of the law.

In order to qualify for extended benefits, landlords would need to continue to maintain at least 20% of the units for households whose income does not exceed 100% of the AMI, and whose average income overall does not exceed 80% of the AMI; and the landlord must agree to rent an additional 5% of the units to households whose average income does not exceed 130% of the AMI.

Qualifying rental owners who participate in the extended benefits program will receive:

- A 50% tax exemption for an additional 10 years if the original tax exemption was for 25 years, or
- A 50% tax exemption for an additional 15 years if the original tax exemption was for 20 years.

Summary of new prevailing wage requirements

The Affordable Housing New York Program also changed the nature of the prevailing wage requirements for eligible projects as well. Prior to the enactment of the new law, prevailing wages were required for projects with 50 or more residential units, unless at least 50% of the residential units are receiving substantial governmental assistance and are set aside for households earning no more than 125% of the AMI. Now, eligible projects with at least 30 units must pay prevailing wages to building service workers unless 100% of the residential units are affordable to households earning no more than 125% of the AMI.

421-a (aka Affordable New York) Abstract

Affordability Option	40% AMI	60% AMI	70% AMI	120% AMI	130% AMI	AVG	Subsidy	Other Restrictions	MIH Analogue
Option A 25% of Total	10%	10%	-	-	5%	66%	None allowed; other than 4% LIHTC and TE bonds	Yes	Option 1 w/ 60% AVG
Option B 30% of Total	-	-	10%	-	20%	86.67%	Allowed	Yes	Option 2 w/ 80% AVG
Option C 30% of Total	-	-	-	-	30%	130%	None allowed	Not in Manhattan south of 96 th and potentially other areas. ²	None
Option D Homeownership	Homeownership (<\$65,000 Initial Assessment)							35 units or less; outside Manhattan; on-site; can be segment of building	None
Option E 25% of Total	10%	10%	-	5%	-	40%	None allowed; other than 4% LIHTC and TE bonds	Only >300 units or more in certain areas of Manhattan, Brooklyn and Queens (the “Enhanced Affordability Area”) ³	Options 1 and 3
Option F 30% of Total	-	-	10%	-	20%	86.67%	Allowed	Only within Enhanced Affordability Area.	Option 2 w/ 80% AVG
Option G 30% of Total					30%	130%	None allowed	Only >300 units or more within Brooklyn Enhanced Affordability Area or Queens Enhanced Affordability Area	None

² “Manhattan south of 96th Street and other geographic areas excluded by local law.”

³ There is no publicly available map yet, however the statute provides street boundaries. Voluntary opt-in is also available for projects outside the Enhanced Affordability Area.

Eligible properties

Tax lots containing one or more multiple dwellings in which all dwelling units are operated as rental housing⁴ (a “Rental Project”) or a multiple dwelling or portion thereof operated as “condominium or cooperative housing” (a “Homeownership Project” and with a Rental Project, an “Eligible Multiple Dwelling”):

- i. containing six or more dwelling units;
- ii. created through new construction⁵ or eligible conversion⁶;
- iii. for which excavation and construction of initial footings and foundations lawfully begins in good faith⁷ (the “Commencement Date”) after 12/31/2015 and on or before 12/22/2022; and
- iv. first TCO or PCO is issued covering “all residential areas” (the “Completion Date”) is before 6/15/2026.

Restriction Period

“Restriction Period” means a period commencing on the Completion Date and expiring on the 35th anniversary thereof.

During the Restriction Period, a Rental Project must comply with one of the Options (as set forth above). Each Rental Project must elect its Option in its application.

However, a Rental Project with more than 300 units in the Enhanced Affordability Area or any rental project not in the Enhanced Affordability Area that elects to comply with paragraph (c) of subdivision 10 of section 421-a of the real property tax law (the “Wage Requirements”) **must** comply with one of Options E, F or G (the “Wage Options”).

Tax benefits

Rental projects meeting the requirements receive a Thirty-Five Year Benefit.

A “Thirty-Five Year Benefit” means:

- A. During the Construction Period, 100% retroactive exemption from real property taxation, other than assessments for local improvements (“Full Exemption”) for up to three years;
- B. For the first 25 years of the Restriction Period, a Full Exemption;
- C. For final 10 years of the Restriction Period, a Full Exemption in proportion to the Affordability Percentage.

“Affordability Percentage” means the number of 40%, 60%, 70%, 120% and 130% Units (“Affordable Housing Units”) divided by the total number of dwelling units.

⁴ “Rental housing” is not defined but will be defined in the Rules.

⁵ “New construction” is not defined but will be defined in the Rules.

⁶ “Eligible Conversion” means the conversion, alteration or improvement of a pre-existing building or structure resulting in a multiple dwelling in which no more than 49% of the floor area consists of such pre-existing building or structure.

⁷ For Eligible Conversion, “the date upon which the actual construction of the conversion, alteration or improvement of the pre-existing building or structure lawfully begins in good faith.”

Rental Projects that are either fall under the Wage Options or elect to comply with the Wage Requirements receive a Full Exemption for [thirty-five years] (an “Enhanced Thirty-Five Year Benefit”).

Homeownership Projects receive a Twenty-Year Benefit.

A “Twenty-Year Benefit” for Homeownership Projects means:

- A. During the Construction Period, 100% retroactive exemption from real property taxation, other than assessments for local improvements (“Full Exemption”) for up to three years;
- B. For the first 14 years of the Restriction Period, a Full Exemption, provided that no exemption shall be given for assessed value > \$65,000;
- C. For final six years of the Restriction Period, 25% of a Full Exemption, provided that no exemption shall be given for assessed value > \$65,000.

Tax payments

Each Eligible Site must pay the following taxes (the “Mini Tax”):

- A. Real property taxes on the assessed valuation of the land and any improvements in effect during the tax year prior to the Commencement Date without regard to any exemption or abatement, calculated using the tax rate in effect at the time such taxes are due.
- B. All assessments for local improvements.

Wage requirements

Projects having more than 300 units in Manhattan south of 96th Street must have a minimum average hourly wage paid to construction workers of \$60/hour.

Projects having more than 300 units in Brooklyn enhanced affordability area and Manhattan enhanced affordability area must have a minimum average hourly wage paid to construction workers of \$45/hour.

Each escalates every three years by 5% but the applicable amount is fixed at the applicable commencement date.

Projects must engage an independent monitor, who will submit a project-wide certified payroll report. If the report shows that the average wages were less than the required amount, the owner must deposit the difference within 120 days with a third party fund administrator. If the actual average wages is more than 15% lower than required, the owner must deposit an additional 25% of the deficiency.

There is a penalty for failure to deliver the report or failure to deposit the deficiency of \$1,000/day capped at \$75,000.

Exemptions from Wage Requirements

- 1) Projects with greater than 50% of units at 125% AMI; and
- 2) Projects subject to project labor agreements.

Note that HPD cannot terminate or revoke any benefits due to a violation of the Wage Requirements⁸ and HPD cannot require that an applicant demonstrate compliance with the Wage Requirements as a condition to approving an Application⁹.

Other limitations

If aggregate floor area of commercial, community facility and accessory use space (other than parking that is located not more than 23 feet above the curb level) of an Eligible Site exceeds 12% of the aggregate floor area of the entire Eligible Site, benefits are reduced by a percentage equal to such excess. This is applied first pro rata to non-residential lots in the Eligible Site until they are fully taxable with the rest applied pro rata to the remaining residential lots.¹⁰

All rental dwelling units in an Eligible Multiple Dwelling must share common entrances and common areas with the Market Rate Units in such Eligible Multiple Dwelling and shall not be isolated to a specific floor or area of an Eligible Multiple Dwelling.

Affordable Units must have (A) a unit mix proportional to market rate units or (B) at least 50% of the Affordable Units shall have two or more bedrooms and no more than 25% shall have less than one bedroom.

No concurrent exemptions or abatements are permitted.¹¹

Rents

All unregulated units (“Market Rate Units”) with a rent at or below the decontrol threshold are subject to rent stabilization. Initial rents for Market Rate Units are determined by HPD.¹²

All Affordable Units are subject to rent stabilization and tenants holding a lease and in occupancy upon expiration have the right to remain as rent stabilized tenants for the duration of their occupancy. Specific language is required in each lease by including a 421-a rent lease rider.

Post-restriction period

See above regarding tenants in Affordable Units upon expiration of the Restriction Period.

Opt-in

Rental Projects or Homeownership Projects with Commencement Dates on or before 12/31/2015 that have not received benefits may opt-in to the new law.¹³

Effective Date

Deemed to be effective 1/1/2016¹⁴

⁸ Paragraph (l)

⁹ Paragraph (o)(iv)

¹⁰ In the alternative, a project may elect to place the commercial space in a separate condominium unit in order to qualify for an ICAP tax exemption for the commercial.

¹¹ However, a project can condo out a residential portion and receive an Article XI tax exemption at the discretion of the City Council.

¹² HPD has published a [421-a Rent Calculator](#). The HPD website should be closely monitored for updates.

¹³ Paragraph (r)

¹⁴ Section 7