Battery Park City: A Model for Financing Low-Income Housing?

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A major policy question facing local governments today is how to provide adequate financing for low- and moderate-income housing. An increasing number of Americans are living in physically inadequate and unaffordable units, while current national housing policies emphasize minimal federal involvement and greater reliance on private sector and local government resources. The Reagan administration drastically cut federal housing subsidies and eliminated many of the tax benefits of investing in rental real estate. In addition, the administration liberalized many of the regulations governing the savings and loan industry. Some critics contend that this deregulation has made obtaining mortgages more difficult for homeowners. All of these measures have forced local governments to develop alternatives to fill the gap in financing low-income housing.

1. Housing that requires an expenditure of more than 30% of a household’s income is generally considered by housing experts to be unaffordable. See Salins, Housing America’s Poor 8 (1987), which indicates that about 17 million households suffer from some housing disadvantage. Salins estimates that in 1987 nearly six million households were located in physically inadequate housing, slightly over one million were overcrowded, and nearly eleven million paid more than 30% of their income in rent. See also President’s Commission on Housing, Report, at xvii (1982).

2. The United States Department of Housing and Urban Development’s (HUD) new budget authority for assisted housing fell from $26.7 billion for fiscal 1980 to less than $10 billion for fiscal 1986. National Governors’ Association, Decent and Affordable Housing for All: A Challenge to the States, at i (1986).

3. The tax incentives for real estate investment have been decreased by restrictions on the ability to offset "passive" losses incurred by investments in real estate, lengthened depreciable life of real estate, and elimination of the preferential tax rate for capital gains. Kreps, 3d Quarter Sales of Housing Bonds Fall Off by 25%, To 2.25 Billion, The Bond Buyer, Dec. 9, 1987, at 1. See also I.R.C. §§ 168(b)(3), 168(c), 465, 469, 1245, 1250 (1988).

In New York City, the problem of adequate financing for low-income housing is particularly critical. New York City lacks adequate housing stock to provide decent living conditions for all of its residents, and some analysts project that 400,000 additional units will be required by the year 2000.\(^5\) To address such housing problems, New York State has pioneered creative financing techniques.\(^6\) One innovation by New York State is the Battery Park City Authority, which uses surplus revenues generated by private real estate developers on a state-owned site to fund low-income housing.\(^7\) The state-created public benefit corporation\(^8\) owns a 92 acre commercial real estate development situated on a landfill that it leases to private developers in lower Manhattan.

In 1987, Battery Park City Authority announced that one billion dollars of the surplus revenues generated by the development will be used to finance low-income housing in New York City. Approximately $400 million will be used to secure bonds issued by the Housing New York Corporation, a subsidiary of the New York City Housing Development Corporation (NYCHDC).\(^9\) Proceeds from the first bond sale will be used to rehabilitate and construct housing units in Harlem and the South Bronx. Thirty percent of the units will be allocated to the homeless; 45% will be designated for families with incomes below $19,000. The balance of the units will be

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\(^5\) The Commission on the Year 2000, New York Ascendant 16 (1987). Estimates of New York's housing shortage are controversial since the components are difficult to quantify. See C. Felstein & S. Knepper, Housing Need and Housing Production in New York City 4 (1985); Hinds, supra note 4, at 1.

\(^6\) For example, New York created the moral obligation bond, a housing bond that included a provision that the state had a moral, although not a legal, obligation to guarantee debt service requirements. This provision increased the marketability of the housing bonds and facilitated the creation of the nation's first state housing finance agency, the New York State Housing Finance Agency, in 1960. New York was also the first state to use large-scale application of tax-exempt bonds for housing. Rasey, HFAs the First Twenty-Five Years, The Bond Buyer, Oct. 7, 1985, at 8.


\(^8\) N.Y. Gen. Constr. Law § 66 (McKinney 1988) defines a public benefit corporation as "a corporation organized to construct or operate a public improvement wholly or partly within the state, the profits from which inure to the benefit of this or other states, or to the people thereof."

\(^9\) NYCHDC was created to address the inadequate supply of housing affordable to low-income persons and the large number of multifamily dwellings that required mortgages and low-interest rehabilitation loans by issuing bonds. N.Y. Priv. Hous. Fin. Law § 651 (McKinney 1976 & McKinney Supp. 1988).

Four hundred million dollars of the total one billion dollars in surplus revenues will be obtained from the net proceeds of bonds issued by the Housing New York Corporation. Telephone interview with Joni Brooks, vice-president of Housing New York Corporation and vice-president of New York City Housing Department (Dec. 6, 1988).
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reserved for families with incomes not exceeding $25,000. This project will create low-income housing units without using tax revenues or burdening the development with a mortgage. Some housing experts have hailed Battery Park City as a creative financing model that will help solve the nation’s housing shortage.

This Current Topic analyzes the Battery Park City experience to determine whether the model can be applied by other cities to solve their problems in financing low-income housing. The Current Topic concludes that certain aspects of the model are transferable: the use of a public benefit corporation; and the strategy of forming partnerships between local and state governments and private developers in order to generate revenues for low-income housing. Some cities may be able to apply some of the aspects of the model on a smaller scale by condemnation, by creating a landfill, or by transferring revenues generated by another development. However, the key to Battery Park City’s success—its ability to generate revenues of hundreds of millions of dollars that can finance low-income housing—is unlikely to be transferable, since it is linked to specific characteristics of Battery Park City.

Section I of this Current Topic discusses the problem of inadequate low-income housing in New York City. This analysis shows that the housing shortage has resulted from a number of factors: wide-scale abandonment of low-income properties by landlords, a renting population that cannot afford market-rate apartments, a low vacancy rate, high construction costs that make unsubsidized low-income housing developments unfeasible, cutbacks in federal subsidies, and changes in tax policies. This section concludes that neither private market forces nor current federal policies have been effective in solving New York’s problems of inadequate quality low-income housing stock and a growing homeless population. Section II describes Battery Park City, which was transformed from a stagnant development in danger of defaulting on its bond obligations to a highly successful real estate project that will generate hundreds of millions of dollars in surplus revenues to finance the construction of low-income housing. Section III concludes that Battery Park City is a creative and highly innovative model that offers some lessons that other cities might apply. Its general application, however, will be


11. In 1987, Battery Park City Authority won the National Council of State Housing Finance Agencies’ Award for Creative Use of State Funds.
limited since it is dependent on special market conditions. In spite of its success, neither Battery Park City nor other local solutions can adequately generate the massive amounts of capital needed to finance the construction of low-income housing without federal assistance.

I. New York's Low-Income Housing Problems

When the New York State legislature created the Battery Park City Authority in 1968, one of its objectives was to address the problem of inadequate low-income housing stock in New York City. The legislature recognized that private enterprise forces alone could not create adequate numbers of housing units affordable to low-income persons. The Battery Park City Authority was established to mitigate the problem of insufficient low-income housing stock by issuing bonds to finance low-interest mortgage loans and the construction of low-income units. Yet by 1979, due to a depression in the New York City real estate market, an overabundance of office space, and the financial crises of both New York State and New York City, Battery Park City had failed to attract a developer. New York City's low-income housing problems continued to escalate, reaching crisis proportions during the 1980s. Traditionally, the federal government had provided subsidies that lessened these problems. Under the Reagan administration, however, there was a radical shift in the federal government's housing policy, making New York City even more dependent on local solutions.

A. Federal Housing Cutbacks

The Reagan administration's housing strategy centered on two philosophies: minimal federal intervention; and reliance on local

12. See Battery Park City Authority Act, N.Y. Pub. Auth. Law § 1971 (McKinney 1981): It is hereby further found and declared that there continues to exist throughout the city of New York a seriously inadequate supply of safe and sanitary dwelling accommodations for persons and families of low income. The ordinary operations of private enterprise cannot provide an adequate supply of safe and sanitary dwelling accommodations at rentals which persons and families of low income can afford.

13. Id.


15. See Hinds, supra note 4, at 1.
government and private market forces to solve housing problems.16

The implementation of these philosophies resulted in a drastic re-
duction of federal government subsidies for new housing construc-
tion. Believing that the greatest housing problem facing low-
income persons was not an inadequate supply of quality housing but
rather affordability, the administration shifted the policy focus from
housing production to direct provision of subsidies to low-income
persons. As a result, the administration made large cuts in the con-
struction budget of the Department of Housing and Urban Develop-
ment (HUD). The Fiscal Year 1982 budget authorized HUD to make
commitments for only 154,000 units of subsidized housing, com-
pared to a peak of 517,000 units in 1976.17 In 1983, the Housing
and Urban-Rural Recovery Act repealed the new construction au-
thority of Section 8 of the Housing and Community Development
Act.18 The elimination of the new construction authority resulted in
the cancellation of all new construction obligations under Section 8,
although commitments made before January 1, 1984, and certain
housing projects for the elderly were continued.19 Between 1981
and 1988, HUD’s authorized budget shrank from approximately
$34.2 billion to approximately $15.4 billion.20

The Reagan administration did subsidize new construction
through the Rental Rehabilitation Program and the Community De-
velopment Block Grant Program.21 Neither of these programs,
however, focused on constructing new housing stock. For example,
the Rental Rehabilitation and Development Program emphasized
rehabilitation of existing units to correct substandard conditions but
generally limited the grants for this purpose to $5,000 per unit.
New construction grants were authorized only if a severe shortage

16. Many of the principles which influenced the Reagan administration’s housing
policies were developed by the President’s Commission on Housing, which was ap-
pointed in 1981. See President’s Commission on Housing, supra note 1, at xxiii, xxiv,
xxxiii.
17. Stanfield, Cashing Out Housing—A Free-Market Approach That Might Also
(Supp. III 1984). Section 8 had been the primary national housing assistance program.
19. The Housing and Urban-Rural Recovery Act of 1983 provided that projects fin-
canced under Section 202 of the Housing Act of 1959 would be exempt from the repeal
of the new construction authority of Section 8. Id. Section 202 assists private nonprofit
corporations in providing housing for the elderly by making low-interest loans available.
20. Executive Office of the President, Office of Management and Budget, Historical
of decent rental units existed with no affordable private market alternatives.22

Recent changes in federal tax policy have also discouraged investment in low-income rental housing. Prior to the Tax Reform Act of 1986 (1986 Act), certain tax benefits encouraged investment in low-income rental housing. Favorable depreciation methods, the ability to offset losses incurred against income from other businesses, and a preferential capital gains treatment of certain real estate transactions all benefited real estate developers.23 The Tax Reform Act of 1986 eliminated many of these incentives. By eliminating the preferential capital gains tax rate and drastically limiting the use of real estate as a tax shelter, the 1986 Act reduced the profitability of low-income housing developments.24 Moreover, the new tax laws placed greater restrictions on tax-exempt financing.25 Although the Tax Reform Act of 1986 also instituted a tax credit for low-income housing, the overall impact of current federal policies has been to discourage private investment in low-income rental housing.26

B. New York City’s Low-Income Housing Supply

Contrary to the premises of current federal housing policies, New York City has experienced a serious shortage of high quality low-income housing. By 1985, housing analysts were projecting that hundreds of thousands of housing units were required to fill the gap between supply and demand in New York City. A report by the Pratt Institute Center for Community and Environmental Development estimated that 231,000 new units were needed to meet the needs of 40,000 homeless people, alleviate overcrowded households, replace 62,000 severely dilapidated units, and increase the vacancy rate from 2% to 5%. An estimated total of 600,000 units was needed overall.27 One of the causes of the shortage was the rapid abandonment of low-income units by landlords. During the 1970s, landlords

22. Id. at § 301.
24. Id.
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abandoned an estimated 35,000 units per year. These abandon-
ments resulted from a number of factors that made low-income
units economically unfeasible. The fuel crisis and rising inflation in-
creased operational costs, while regulations restricted the ability to
raise rents. The increase in drug traffic resulted in vandalism and
more neighborhood crime. Many units were simply abandoned or
destroyed by suspicious fires.28

Although the loss of housing stock by abandonment has abated
due to new City programs, other factors have contributed to a con-
tinued lack of adequate housing. One factor is that a significant por-
tion of New York City’s population cannot afford market-rate
rents.29 The inadequate stock of low-income housing is also a result
of the cost of construction in the City, which is among the highest in
the nation. With development costs of multifamily rental housing
ranging from $150 to $200 per square foot, developers have no eco-
nomic incentive to build unsubsidized low-income units.30

C. The City’s Increasing Demand for Low-Income Housing

While the supply of low-income housing in New York City has
been falling due to abandonment, dilapidation, and decreases in
construction, the demand for low-income housing has been rising.
One reason for the increase in demand is the growth of the City’s
population. New York City is one of the major international centers
of the financial services industry. It is estimated that more than one-
third of all financial services jobs in the United States are located in
New York City.31 New York City is also the location of a large
number of corporate headquarters. Between 1979 and 1987,

28. Oser, Rehabilitation: ‘Public Housing’ in Abandoned Buildings, N.Y. Times,

Commission on the Year 2000 expects the problem of inadequate low-income housing
to get worse. For example, the Commission projects that single parent families will
comprise 15% of New York City’s population in 2000. The Commission on the Year
2000, supra note 5, at 19. In 1986, the median income of female-headed single family
renter households was $6,822. In 1986, 24.2% of all renters were below the federal
poverty line and the $16,000 median income of renters made market rate apartments
unaffordable. Stegman, supra, at 18, 20, 96.

30. Hinds, supra note 4, at 1. The Commission on the Year 2000 found that the
construction cost for rental housing was higher than for any other city in the United
States except San Francisco. The Commission on the Year 2000, supra note 5, at 148.

31. Woolard, Reality Comes to Wall Street and Brings a Closer Look at Costs, Chris-
reverses prior trends of population losses. See The Commission on the Year 2000, supra
note 5, at 9; Stegman, supra note 29, at 1.
300,000 new jobs were created in New York City; an additional 300,000 are projected to be developed by 2000.32

In spite of these new job opportunities, the ability of minorities—projected to comprise 60% of New York's population in 2000—to find adequate housing is unlikely to improve. Since it is projected that most of the new jobs will be skilled positions in the service industries, many minorities, who may not complete high school if present trends continue, may be unqualified to fill those positions.33 Minorities will continue to earn incomes lower than the median and will be forced to spend a disproportionately high percentage of their income on rent.34

II. The Battery Park City Model

The Battery Park City Authority was originally established in 1968 to help solve the problem of inadequate low-income housing. Battery Park City was planned as a massive coordinated community, a self-contained “New Town” with 5-6 million square feet of office space, 960,000 square feet of retail space, and 12,000-16,000 units of mixed-income housing.35 The development, located on 92 acres of landfill adjacent to the Hudson River in lower Manhattan, was to be a complex megastructure with overhead bridges and segregated decks for pedestrians and vehicular traffic.36 By 1979, however, anticipated development had not occurred. At that time it appeared that Battery Park City Authority would not be able to meet its expenses without a major restructuring.37 The Authority hired a team of consultants to review the original Battery Park City Master Plan and to reformulate the nature of the project.38 Today, Battery Park

32. The Commission on the Year 2000, supra note 5, at 4, 9.
33. Id. at 19, 20.
34. For example, in 1986, the median income of New York City renters by racial groups was:

<table>
<thead>
<tr>
<th>Group</th>
<th>Income</th>
</tr>
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<tbody>
<tr>
<td>White (non-Hispanic)</td>
<td>$22,000</td>
</tr>
<tr>
<td>Black (non-Hispanic)</td>
<td>14,325</td>
</tr>
<tr>
<td>Puerto Rican</td>
<td>9,000</td>
</tr>
<tr>
<td>Other Hispanics</td>
<td>13,000</td>
</tr>
<tr>
<td>Others</td>
<td>18,000</td>
</tr>
</tbody>
</table>

Stegman, supra note 29, at 94b. See also The Commission on the Year 2000, supra note 5, at 132.
36. Id. at 9.
37. Id. at 1.
38. Id. at 3, 4. The consultants were asked to evaluate the plan using the following guidelines:
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City is described as one of the most massive and successful real estate projects in the history of New York. In 1986, Battery Park City Authority announced that Battery Park City would be contributing $400 million in surplus revenues to the financing of low-income housing in New York. The following year the Authority pledged an additional $600 million.39

The transformation of Battery Park City from a failure to an innovative model for financing low-income housing resulted primarily from two events: the restructuring of Battery Park City in 1979; and the cooperation between New York City and the state resulting in the formation of the Housing New York Corporation. Before analyzing the applicability of the Battery Park City model, it is necessary to examine both how the project was transformed from a failure to a success and how the structure that generates the excess revenues operates.

A. Restructuring Battery Park City

In 1979, when consultants were called in to evaluate Battery Park City, a crisis situation existed. Seven years earlier, Battery Park City Authority had issued $200 million in bonds to finance infrastructure improvements.40 The bonds were to be secured by revenues from Battery Park City and were backed by a moral obligation of the state.41 Although Battery Park City Authority's original plan had anticipated revenues from ground rents beginning in 1976, without a developer the only income was investment earnings of approximately $7 million per year from the revenue bond proceeds.42 The annual debt service, on the other hand, was approximately $14 million.43 Battery Park City Authority faced default in 1979 because it

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42. Alexander Cooper Associates, supra note 14, at 10.
43. By 1979, Battery Park City Authority had approximately $85 million remaining in bond proceeds. Id.
could not meet its debt service requirements without emergency allo-
cations from the State. The project was unable to attract devel-
opers due to a variety of factors.

When Battery Park City was first planned, its concept was based
on existing theories of urban planning and its scope was based on
the New York real estate market of the mid-1960s. Battery Park City
was conceived in the late 1960s as part of the state’s plans for the
overall development of the Hudson River waterfront. The plan
called for a series of coordinated communities which would mix res-
idential and commercial development along with necessary support
and recreational services. The idea was to create a pleasant,
mixed-income environment that would spark office, retail, and resi-
dential development in lower Manhattan. Initiated during a boom
in the New York City office market, Battery Park City was to be a
model “New Town”: a massive megastructure, a single continuous
building, with a retail and circulation spine running its entire length.
Although the concept was simplified somewhat in 1973, the mega-
structure aspect remained.

By 1974, market conditions and urban planning concepts had
changed radically. The office boom in New York City had resulted
in over-building. Over 31 million square feet of office space were
vacant in Manhattan by 1973. This oversupply of office space was
exacerbated by the exit of many firms from New York City during
the 1973-1975 recession. A depression in the real estate market,
spiraling construction costs, and President Nixon’s 1973 morato-
rion on housing assistance created chaos. Construction of luxury
condominiums slowed down, and the development of middle-in-
come units was financially unfeasible. During this period, both
New York City and New York State were experiencing severe finan-
cial crises. The New York Urban Development Corporation’s near
default on its bond obligations caused a temporary erosion of inves-
tor support of the public housing market. The “New Town” con-
cept began to decline in popularity. Because of the tremendous

44. Battery Park City Authority had received $57.9 million in appropriations from
the state to meet its principal payments. Priest, Contracts Ensure 50% Occupancy of
46. Id. at 9.
47. Id. at 15, 16.
48. Id. at 16.
49. Id. at 33.
50. Id. at 17.
52. Rasey, supra note 6, at 8.
expense of the infrastructure, generally only non-profit or government institutions could afford to develop such massive projects.\textsuperscript{53} Developers, perhaps deterred by the complex and costly plan, market uncertainties, or doubts about the stability of the Battery Park City Authority, hesitated to commit themselves.\textsuperscript{54}

Faced with the potential default of the Battery Park City Authority, the state instituted radical changes. In January 1979, the state brought in a new management team for Battery Park City Authority. A group of consultants led by Alexander Cooper Associates was formed to develop a new master plan for Battery Park City. Despite the troubled history of the project, the consultants were confident that, with revision, the project could be successful.

Part of this confidence stemmed from significant changes that had occurred since the 1975 recession. First, the 1979 announcement by the American Stock Exchange that it had decided to build its new headquarters at Battery Park City indicated that commercial demand could be created.\textsuperscript{55} Second, the success of the World Trade Center, with 9.6 million square feet of office space that were nearly fully leased by 1979, indicated potential demand. More important, because the World Trade Center had over 40,000 employees and 65,000 visitors per day, it had created a demand for retail and recreational facilities in lower Manhattan.\textsuperscript{56} Third, due to zoning changes in 1976 that permitted residential lofts, the surrounding neighborhood had become the second largest neighborhood of loft conversions in the city.\textsuperscript{57} Finally, by 1979, both the office and housing markets had recovered from the real estate depression, although not to the level of the 1960s boom period. Although lower Manhattan had 3.3 million square feet of vacant office space, the consultants estimated it would be absorbed in one year, and only 200,000 square feet were available in buildings constructed since 1970.\textsuperscript{58} Both the rental and cooperative markets had low vacancy rates by 1979.\textsuperscript{59}

\textsuperscript{53} Alexander Cooper Associates, \textit{supra} note 14, at 15.
\textsuperscript{54} \textit{Id.} at 6. There were also some allegations of mismanagement. See Report on Battery Park City Faults Bidding, Auditing of Consultants, The Daily Bond Buyer, Oct. 30, 1981, at 3.
\textsuperscript{55} Alexander Cooper Associates, \textit{supra} note 14, at 8. Ultimately, however, the American Stock Exchange did not relocate to Battery Park City.
\textsuperscript{56} \textit{Id.} at 20.
\textsuperscript{57} \textit{Id.} at 22.
\textsuperscript{58} \textit{Id.} at 34.
\textsuperscript{59} \textit{Id.} at 18.
The consultants recommended that the “New Town” concept be dropped and that, instead, Battery Park City be developed as an integral part of lower Manhattan. They also recommended that the megastructure and complex decking of activities be replaced by street level circulation and more flexible development controls, thus enabling a greater number of developers to participate. Since the demand for commercial space was considered to be of great importance to the project, the commercial core was relocated to the area of the project closest to the World Trade Center. The revised plan maintained the original allocation of approximately 6 million square feet of commercial space and 12,000-16,000 residential units, but reduced the original 960,000 square feet of planned retail space to 150,000 square feet. The plan also called for 70% of the project to be committed to “open spaces,” streets, parks, esplanades, and courtyards.

Another major step in the restructuring of Battery Park City occurred in November 1980, when Olympia & York, a major Canadian developer, received the contract to build the World Financial Center, which was to contain six million square feet of commercial space. Olympia & York guaranteed that it could complete construction of all of the commercial space by 1987. This guarantee meant that the commercial space could be leased and thus could generate the revenues needed to pay the Authority’s debt service.

To provide incentives for tenants to occupy the World Financial Center, Olympia & York agreed to buy the old headquarters of some potential tenants. Olympia & York eventually purchased approximately four million square feet of office space to encourage major firms to relocate to the World Financial Center. When the World Financial Center opened in October 1985, it was the headquarters of Merrill Lynch, Shearson/American Express, Dow Jones & Company, and Oppenheimer & Co. Much of the demand for

60. Id. at 22, 46, 49.
61. Id. at 39.
62. Id. at 65.
64. Id.
65. Williams, Finally, the Debut of Wall Street West, N.Y. Times, Aug. 25, 1985, § 5, at 1. American Express sold its Bond Street headquarters to Olympia & York for $160 million and purchased its new headquarters at the World Financial Center for $370 million.
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des large areas of space was generated by the growth of the financial services industry.

The commitment of prestigious commercial firms to relocate their headquarters to Battery Park City was an important turning point for the development. Subsequently, construction began on Phase II of the residential component of the development, Rector Place. Rector Place consists of approximately 2,200 market-rate units, 1,665 of which are condominiums located south of the World Financial Center. Gateway Plaza, Phase I of the residential component, was completed in 1983 and consists of 1,712 rental units located on a 5 acre site. By 1984, 15 ground leases had been negotiated between the Battery Park City Authority as lessors and private developers as lessees. The project had been successfully restructured and was generating revenues.

B. Financing Low-Income Housing

By 1985, when Battery Park City began to generate millions of dollars in revenues, New York City was in the throes of a severe housing crisis caused by a growing shortage of adequate low-income housing stock, growing low-income and homeless segments of the population, and cutbacks in federal subsidies. Prior to the repeal of the Section 8 New Construction Program, developers had been able to rely on federal subsidies to bridge the gap between low-income tenants' rental payments and fair market rents. Without this federal assistance, there was a sharp decrease in the development of low-income rental projects built by private developers. Moreover, since Battery Park City was established originally to help address the problem of low-income housing, some critics questioned the use of state funds to finance a project that was providing primarily market-

68. Id. at B-1. Four leases, "severance leases," replaced an earlier lease between Olympia & York and the Battery Park City Authority that had been executed on September 1, 1981. The severance leases covered the four parcels which comprised the World Financial Center and were between WFC Tower A Company, Olympia & York Tower B Company, American Express Company and certain of its affiliates, and WFC Tower D Company, and the Battery Park City Authority as landlord. One lease between the Hudson Tower Housing Co., Inc., as tenant and the Battery Park City Authority as landlord covered the area comprising Gateway Plaza. Ten leases covered the twelve parcels which composed Rector Place. The principal developers of Rector Place are Related, Milstein/Goldstein, Zeckendorf, and Rockrose.
rate and luxury housing and generating profits for private sector developers.\textsuperscript{70} In May 1985, Governor Cuomo and Mayor Koch issued a Memorandum of Understanding whereby they agreed to undertake a 10 year program to increase the availability of low- and moderate-income housing in New York City.\textsuperscript{71} As part of the agreement Battery Park City Authority was to issue bonds in an amount adequate to provide up to $400 million to finance construction of low-, moderate- and middle-income housing within the City but outside of Battery Park City.\textsuperscript{72} The state legislature, however, balked at having a state entity issue bonds that would benefit only New York City. Consequently, another issuer had to be created.\textsuperscript{73}

1. Public benefit corporation bond issuer. In order to implement the Memorandum of Understanding, the New York State legislature created the Housing New York Corporation, a public benefit corporation that is a subsidiary of the New York City Housing Development Corporation.\textsuperscript{74} The Housing New York Corporation was authorized to issue tax-exempt bonds secured by excess revenues of the Battery Park City Authority.\textsuperscript{75} Excess revenues are defined as those in excess of bond obligations, debt service requirements, and funds necessary to fulfill the Authority's legal requirements, maintenance, and operating expenses. Proceeds from the bonds are to go to the City for the sole purpose of financing the Housing New York Program.\textsuperscript{76} The Housing New York Program was established by the New York State legislature to ensure that all monies received by the City from the Housing New York Corporation and from payments in lieu of taxes from the Port Authority of New York and New Jersey are used to construct or renovate housing for low- and moderate-income persons.\textsuperscript{77} The guidelines provide that any housing developed with funds from the Housing New York Corporation should be restricted to ensure that at least 40\% is occupied by persons and families whose income does not exceed 55\% of the median income.

\textsuperscript{70} Goldberger, Battery Park City Looks Inward for Innovation, N.Y. Times, July 24, 1988, § 2, at 28.
\textsuperscript{71} Memorandum of Understanding By and Between the Governor of the State of New York and the Mayor of the City of New York (May 23, 1985) (on file with Yale Law & Policy Review) [hereinafter Memorandum of Understanding].
\textsuperscript{72} Id.
\textsuperscript{75} Id.
\textsuperscript{76} Id. at § 12(c).
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of the area. Any individual or any family whose income exceeds 175% of the median income of the area is prohibited from living in housing financed by the Housing New York Corporation. The legislation stipulates that housing must remain affordable to the benefited income groups for a "substantially long period of time" and that funds should be used to increase housing and not to replace funds committed from other sources.

2. Generation of excess revenues. Since the legislation creating the Housing New York Corporation provides that its bonds are not an obligation of the state, the City, or the Battery Park City Authority, the bonds are secured solely by the excess revenues of the Battery Park City Authority. The excess revenues are derived from payments received from the ground leases between the private developers and the Battery Park City Authority, the landlord of the project. Each ground lease includes a series of payments in addition to the base rent. Leases for each sector are somewhat different, but all contain certain similar provisions. All lessees pay a base rent, which in the case of commercial developers increases incrementally until the year 2000 and then remains at a fixed rate. The project is owned by the state and therefore exempt from property taxes. Every lease, however, provides for either payments in lieu of taxes (PILOT) or tax equivalency payments. The amount generated by these payments is generally equivalent to the amount of assessed property taxes. Leases are also structured so that the Battery Park City Authority will receive payments that reflect the appreciation of the property or business.

78. Id.
79. Id. at §§ 6, 11.
80. Although no time period is specified during which units funded through the Housing New York Corporation must remain affordable to low-income groups, the City must assure that the accommodations are affordable for a "substantially long period of time" based on minimum standards provided by federal, state, or local law. Housing Program Act, supra note 77, at §§ 6, 8.
81. Prospectus, supra note 67, at C-2.
82. Id. at C-1. By the year 2000, the fixed annual base rental rate for the commercial sector will be $3.4 million each for parcels A and D, and $5.1 million each for parcels B and C. For Gateway Plaza, a fixed annual payment is received until either the payment of the HUD mortgage or the occurrence of certain anniversaries.
83. Tax equivalency payments are contained only in the ground lease of Gateway Plaza. These are payments equal to 10% of the total rents from the buildings less the cost of providing electricity, gas, heat, and other utilities, as long as the "HUD mortgage is insured, reinsured, or held by HUD." When these conditions change, the tax equivalency payment is the amount calculated by multiplying the assessed value of the premises as determined by the City of New York, i.e. the tax rate for such year. Id. at C-14.
84. A percentage of the rent from retail and uses other than office and parking spaces in the commercial structures is paid to the Battery Park City Authority. Payment
The project occupies a vast tract of land in an area in high demand for both commercial and residential space, so planners anticipate that revenues will constantly increase. Various executives associated with Battery Park City Authority have projected that the income from the project could range as high as $3-$10 billion.85 The development already has been able to repay its debt to the state through a 1986 bond issue and to increase its pledge to finance low-income housing from $400 million to $1 billion.86

3. Tax-exempt financing. In 1987, the Housing New York Corporation issued special obligation bonds of approximately $209.9 million to finance the initial Housing New York Program.87 Approximately $150 million of this amount went to finance housing; the remainder was allocated for the costs of the issue and debt service.88 Because the owner of the low-income housing development will be either the New York City Housing Authority or a nonprofit organization, and because the issuer is a public benefit corporation, the bonds are tax exempt and are not subject to the alternative minimum tax.89

4. Off-site low-income housing. Since a philosophy underlying the Battery Park City model is that rehabilitation or construction of low-income housing can be used as a catalyst to generate development in depressed neighborhoods, the two initial projects in the Housing New York Program are located in areas where large numbers of abandoned low-income housing units exist: Harlem and the South Bronx. Neither of these areas is in the neighborhood of Battery Park City. The development of this housing will combine government, private sector, and, in some cases, nonprofit resources.90

of a percentage rent begins during the twelfth year after substantial completion of the building. It is equal to 5% of the difference between the net fixed rent of the eleventh year and each subsequent year's net fixed rent. Net fixed rent is calculated by taking the sum of all revenues paid to the tenant (lessee) by office subtenants (sublessees) less an exclusion relating to sub-tenant reimbursements and debt service owed by tenant to landlord for landlord's financing of tenant improvements above building standard and less the pro rata share of "operating expenses" attributed to the office area. Id. at C-3. 85. See Peterson, supra note 39, at 1; Williams, supra note 65, at 1. 86. Schmalz, supra note 73, at B3. 87. Prospectus, supra note 67, at C-2. 88. Id. at 16. 89. Id. at title page. The housing units that are being rehabilitated by the proceeds from the first bond issue will be owned and operated by the New York City Housing Authority in Harlem and in the South Bronx by the Settlement Housing Fund, a nonprofit organization. Telephone interview with Judith Disla, supra note 10. 90. At the time of the Memorandum of Understanding, it was assumed that Battery Park City could make a more effective contribution to the problem of low-income housing by the maximum generation of revenues through the construction of commercial and market-rate housing. By infusing capital into depressed neighborhoods to develop
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In the South Bronx, 14 abandoned apartment buildings will be rehabilitated into 893 low- and moderate-income apartments. The Settlement Housing Fund, a nonprofit organization, will own and operate the development when it is completed. In Harlem, approximately 743 apartments will be created. The Harlem development will be owned and operated by New York City Housing Authority. Tenants will be selected by the operators. Homeless tenants will be referred primarily by the New York City Department of Housing Preservation and Development and the New York City Human Resources Department. From 30% to 40% of the other units will be set aside for members of the community development district. Construction is under way on both projects. The next rehabilitation financed by Housing New York Corporation bond proceeds will convert 41 city-owned buildings in the Bronx into 1,200 units.

III. Conclusions

The purpose of this Current Topic has been to examine the Battery Park City as a model for financing low-income housing. Because the federal government has drastically reduced its role in providing assistance to finance and develop low-income housing, the ability of local governments and the private sector to solve low-income housing problems has become crucial. The Battery Park City project is effective in that it will transfer $1 billion of private sector revenues to finance low-income housing in New York City. To determine the potential impact of the Battery Park City model on housing policy generally, the critical characteristics of the model, its ability to be transferred to other housing markets, and the general lessons to be learned from the Battery Park City experience must be assessed.

A. Central Characteristics of the Battery Park Model

There are five characteristics central to the Battery Park City model: (1) government ownership of the development’s land; (2) local government’s ability to share in the development’s appreciation;
(3) strong private sector demand to locate on the government-owned land; (4) tax-exempt financing; and (5) ability to generate massive amounts of capital.

1. State ownership of the development's land. One important aspect of the Battery Park City model is that the state must own the land on which the private sector development is located. Ownership of the land enhances the ability of the state to ensure that a steady cash flow will be transferred from the private sector to finance low-income housing because, as landlord, the state theoretically retains the option of evicting the developer.\textsuperscript{94}

Government ownership of the land is more likely to provide a stable, long-term partnership between the private sector and local government than ordinary inclusionary zoning or linkage programs.\textsuperscript{95} Typically in these programs, the local government requires a developer either to build a certain number of low-income units or to pay an assessment that will be used to develop low-income housing.\textsuperscript{96} Therefore, the relationship is usually short-term. The ability of the inclusionary zoning and linkage programs to provide either future low-income housing units or funds for their development depends on the consistency of the demand for commercial or market-site residential developments in the area. If changes in the economy soften the demand for development in an area relying on linkage or inclusionary zoning to supplement low-income housing, or if competing neighboring townships develop land that is not governed by linkage or inclusionary zoning, demand may fluctuate. When the government owns the developer's land, absent a major change in the economy, the developer may find it more cost effective to remain in the location and pay his rent than to incur relocation expenses.

\textsuperscript{94} The manner in which the revenues flow to the city varies depending on whether the sublease was executed before or after January 1, 1986. \textit{See} Goldman, Sachs & Co., Housing New York Corporation: A Presentation (undated) (on file with Yale Law & Policy Review).

\textsuperscript{95} Linkage programs require private sector developers to pay a fee in exchange for their right to develop property. The fee is contributed, typically, to a fund to develop low-income housing. Inclusionary zoning typically requires a developer to include a percentage of low-income housing units in his market-rate development.

\textsuperscript{96} Linkage and inclusionary zoning programs have been developed around a number of concepts. In San Francisco, where one of the earliest linkage programs, Office-Affordable Housing Production Program, was developed in 1981, developers are assessed a fixed fee per square foot of new office space created. \textit{See} Rosen, San Francisco: A Link to Cheaper Housing, N.Y. Times, May 29, 1988, § 8, at 1. An inclusionary zoning program in New York gives developers of low-income housing bonus floor area that can be used to develop market-rate housing either on the same site, within the same community district, or within one-half mile. \textit{See} Oser, Low-Income Housing: The 'Inclusionary-Zoning' Experiment, N.Y. Times, Mar. 15, 1987, § 8, at 9.
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2. Shared participation in appreciation of the development. The local government’s ownership of the developer’s land also enables the government to structure a relationship in which it can share in the appreciation both of land value and of the business located on the land. In Battery Park City, the state functions as a commercial landlord. Its leases demand constantly increasing rents that reflect the appreciating value of the land and percentages of the businesses’ revenues. This relationship is crucial in enabling the local government to derive a steadily increasing amount of revenue from the private sector. Generally, most local governments share in the appreciation of a business’ value by taxation. Pressures to be as competitive as neighboring communities may cause local governments to lower local property taxes, to keep property taxation assessments below the fair market value of the property, and to create other incentives in order to attract developers.

3. Strong private sector demand for state-owned land. Driving the Battery Park City model is the high private sector demand to locate on the state-owned site. This demand, to a great extent, was generated by the rapidly growing financial services industry. The history of Battery Park City shows that demand cannot be determined by location alone. Demand is the result of a complex interaction among various forces: vacancy rates, general economic conditions, and local industrial or residential growth patterns. In spite of the growth of the financial services industry in New York City, the decision of certain major firms in the industry to locate their headquarters at Battery Park City was heavily influenced by the incentives provided by Olympia & York, the quality and size of the space being offered, and the increasing development of the surrounding area.

4. Tax-exempt financing instrument. In the Battery Park City model, the private sector plays no role either in issuing the bonds that finance the low-income housing or in the ownership of the housing. Since the Housing New York Corporation, a public benefit corporation, issues the bonds and either the New York City Housing Authority or nonprofit organizations will own all of the low-income housing, the bonds qualify for tax exemption under the Tax Reform Act of 1986. Equally important, they are not subject to the Alternative Minimum Tax. Tax exemption increases the marketability of the bonds.

97. See supra notes 87-89 and accompanying text.
5. Generation of massive revenues. Battery Park City is significant because of its potential billion-dollar contribution to financing of low-income housing. Most linkage programs are unable to generate funds of this magnitude. Battery Park City's massive revenues are derived from the large scale of the development: 6 million square feet of commercial space and, when completed, approximately 10,000 housing units. The ability to generate tenants for a project of this size is directly related to the size and the dynamics of the New York City real estate market.

B. Transferability of the Battery Park City Model

Certain aspects of the model are applicable to other housing markets. The concept of a partnership between local government and private sector forces is not new and can be instituted elsewhere. The ability to develop a partnership mechanism that ensures a long-term transfer of funds from the private sector, however, will be more difficult; most communities are unlikely to have large tracts of commercially valuable land that are either unoccupied or owned by the state. It is also unlikely that other local governments can develop a project of the magnitude of Battery Park City, which exceeds the scope of most local real estate markets. Other communities may apply the revenue-transfer aspect of the model on a smaller scale. For example, a local government might condemn a smaller site for a commercial or industrial development, or create area with a landfill. Alternatively, local and state governments can work together to use a portion of an existing source of revenue to finance low-income housing. Any of these efforts may result in a steady stream of income to aid in financing housing. Whether substantial revenues will result is dependent on local conditions.

C. The Lessons of the Battery Park City Model

The Battery Park City experience offers three lessons: (1) partnerships between local governments and the private sector can create effective housing financing strategies; (2) revenue transfer financing is useful in funding low-income housing; and (3) local solutions cannot solve low-income financing problems without federal assistance.

98. The revenues generated by Battery Park City will greatly exceed those of the San Francisco linkage program, for example. Between 1981 and 1988 the San Francisco Office-Affordable Housing Production Program generated approximately $28.3 million that has resulted in the creation of 5,532 new units of housing of which 3,150 are reserved for low- and moderate-income occupants. Rosen, supra note 96, at 1.
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1. Local government and private sector partnerships. Battery Park City clearly demonstrates that local governments can develop creative financing solutions to housing problems. The cooperation between New York City and New York State to develop a mechanism to transfer surplus revenues guaranteed by private developers on a state-owned site was highly innovative. New York State and New York City have a history of developing and utilizing creative methods to finance low-income housing, including moral obligation bonds, state housing finance agencies, inclusionary zoning, tax abatements, and partnerships with nonprofit organizations. In this case, the participation of the private sector was important because it helped to increase the commercial value of the land.

2. Revenue transfer financing. One of the most innovative aspects of the Battery Park City model is the ability of the state, as a landlord, to transfer surplus revenues generated by private developers in order to finance low-income housing on another site. The model provides a two-pronged approach to address the problem of low-income housing. The history of Battery Park City shows that the financing of low-income housing and the provision of low-income housing units are separate problems that may require separate strategies for solution. Battery Park City in its original form was a massive and complicated development with many objectives: (1) the creation of a state-of-the-art "New Town"; (2) the provision of on-site low-income housing within an economically mixed environment; (3) the generation of funds from the development's revenues; and (4) the reduction of tension between vehicular and pedestrian traffic by segregated decks for traffic flow. The complexity of the plan, in addition to negative market conditions, prevented the project from reaching any of its goals.

When Battery Park City was restructured in 1979, its planners recognized that developing an effective financing strategy for low-income housing could be divorced from the on-site provision of low-income housing units. The primary objective became generation of the maximum amount of revenue, that could then be used to...
finance low-income housing. Battery Park City shows that the problems of low-income housing financing and the provision of housing can be treated as separate issues.

3. Need for federal assistance. The final lesson of Battery Park City is that even a highly successful development is incapable of generating the massive amounts of capital needed to solve New York City's low-income housing problems. Federal assistance in the form of subsidies and beneficial tax policies is needed to supplement local efforts. Although Battery Park City's potential contribution is substantial, and although experts disagree on the amount that would be needed to solve New York's low-income housing problems, massive amounts of additional capital are necessary. Particularly in a market with limited vacancies and inadequate housing stock, federal assistance to subsidize construction of new units is critical.