New York City Independent Budget Office

Focus On:
The Preliminary Budget

April 2022

Assessments & Revenue: Explaining the Unusual Swings in Property Tax Revenues for 2022 and 2023

The real property tax (RPT) is the city's largest source of tax revenue and is typically a steady source of growth for city coffers. From 2012 through 2021, collections increased about 6.4 percent per year, with rising property values and new construction driving the growth. (Unless otherwise noted, years refer to city fiscal years.) A little over a year ago, however, in anticipation of major declines in rental income for commercial properties and residential apartment buildings due to the pandemic, the Department of Finance (DOF) sharply reduced the assessments that it used to calculate the 2022 tax bills. Largely driven by these assessment reductions, IBO expects a 6.0 percent, $1.9 billion, decline in RPT revenue in 2022 compared with 2021. Our analysis of property tax collections in 2022, along with data from the recently released tentative roll for 2023 shows that for some property types, the reductions made by DOF were more than what was warranted. As such, IBO forecasts RPT revenue to increase by 8.0 percent in 2023 —the largest increase in the last five years.

IBO forecasts 2023 property tax revenues will total $31.8 billion in 2023, a $2.4 billion increase over 2022, largely due to some reversals in the market value decreases that DOF made to commercial and residential properties last year. IBO expects RPT revenue to grow at a much slower pace, averaging 1.2 percent annually from 2024 through 2026 to reach $33.0 billion.

Real Property Income and Expense Reports and Property Valuation. Unlike the market values of Class 1 properties (one-, two-, and three-family homes) which are based on sales transactions, the market values of Class 2 (apartment buildings) and Class 4 (commercial) properties are based on estimates of their income and expenses.[1] Every June, rental buildings and commercial properties (office, retail, hotel, etc.) are required to file annual income and expense statements with DOF, usually for the preceding calendar year.[2] DOF then uses this information to estimate properties' income and expenses for the current calendar year, which—along with assigned capitalization rates—become the basis for determining market values for the property tax assessment roll used for the upcoming fiscal year.[3] In other words, the market values on the 2022 roll were based on DOF estimates of income and expense for the calendar year 2020 using the filed income and expense reports for the calendar year 2019.[4] The market values of coop and condo buildings, which by law must be estimated as if they were income-producing properties, are determined using the net income of comparable rental buildings as a proxy of their income-generating ability and applying a capitalization rate.

The significant decrease in the market values on the 2022 tentative roll, released in January 2021, was mainly due to DOF projecting substantial decreases in Class 2 and Class 4 properties' incomes from calendar year 2019 to 2020—decreases that affected assessed values and tax bills for 2022 and subsequent years. For elevator rental apartment buildings in Manhattan, DOF projected a median decrease in buildings' income for the 2022 roll to be 8.1 percent from the prior year; for similar buildings in the other boroughs, DOF projected a median 6.5 percent decline in income. For office properties, the median projected changes in income were even larger —an 18.0 percent decline for Manhattan and a 15.9 percent decline for other boroughs. The median projected changes in income for retail properties were a 24.8 percent decline for Manhattan and a 17.6 percent decline for other boroughs. Hotel properties had the largest median projected declines in income—a 31.9 percent decline for Manhattan and 30.1 percent for other boroughs. Increases in capitalization (cap) rates assigned by DOF also contributed to decreases in market values, though the effect was relatively small.

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The finance department had a difficult challenge in estimating calendar year 2020 incomes given the pandemic's unprecedented effect on commercial property markets. DOF has acknowledged that it could not employ its usual methodology to adjust the reported calendar year 2019 data to 2020 conditions, in part because it was still not clear how atypical 2020 was for the income of commercial landlords.

IBO's tracking of property collections in calendar year 2020 and 2021 and the recently released 2023 tentative roll show that DOF likely overestimated the negative impact of Covid-19 on the rental incomes of some commercial properties. Had the actual incomes of commercial property owners in calendar year 2020 fallen to the extent that DOF predicted, an increase in tax delinquencies would have been likely. But the delinquency rate for most commercial properties did not rise significantly. Many office and retail owners continued to pay their property taxes, suggesting that tenants continued to pay rents even as many of them shifted to remote work arrangements. The delinquency rate for hotel properties, on the other hand, did increase and has stayed high, reflecting a sharp reduction in income caused by a plummet in occupancy rates due to the pandemic.

The accompanying table presents DOF's estimates of the median percentage change in income, expense, cap rates, and market values for office, retail and hotel properties. First, we show the change from 2021 to 2022 and then the change from 2022 to 2023—the latter is based on the calendar year 2020 income and expense report data that were not available the year before. For each category of property, projected increases in net operating income for 2023 were driven primarily by projected increases in income rather than decreases in expenses.

The median percent change in income and market value for Manhattan retail properties, which make up a relatively large portion of commercial spaces, were increases of 10.6 and 5.9 percent, respectively, from 2022 to 2023, compared with median income and market value decreases of 24.8 percent and 29.9 percent, respectively, from 2021 to 2022. Market value reductions for office properties made last year by DOF were also more than what was warranted. On the 2022 roll, the median percentage change of the market value estimates for Manhattan offices was a 25.4 percent decrease compared with 2021. On the 2023 roll, the median percentage change of the market value was an increase of 10.6 percent. The median market value for other borough retail properties increased by 13.8 percent on the 2023 roll compared to a decrease of 23.2 percent on the 2022 roll.

While the number of hotel properties is small compared with the total number of Class 4 properties, hotels were one of the Class 4 property types that were hit the hardest by the pandemic. The median change in net operating income for Manhattan hotels was -30.1 percent, leading to a median decrease of 30.9 percent in market values from 2021 to 2022. On the 2023 assessment roll, the median change in market values for hotels in Manhattan was an increase, but only 2.3 percent, and they still have a long way to go to recover from their market value decreases on the 2022 roll.

Market Values. Market values for New York City properties increased at a brisk pace over the last five years. From 2017 to through 2021, the total market value for all properties—including existing properties as well as newly constructed properties coming onto the tax rolls—increased at an average rate of 6.4 percent per year. On the final 2022 roll, however, total market value decreased by 5.6 percent. For Class 2 the aggregate market value decreased by 8.2 percent on the 2022 roll, the first decrease since 2010 when it decreased by 2.0 percent. For Class 4, aggregate market value decreased by 17.4 percent on the 2022 roll, the only decrease in the last 20 years.

After a period for appeals and review, the final roll for 2023 will be released in May 2022. Based on historical trends, IBO anticipates the final roll will show a 7.4 percent increase in total market values from the 2022 roll. Aggregate market value for Class 2 and Class 4 properties is projected to increase by 8.2 percent and 9.5 percent, respectively on the 2023 roll. The median price of Class 1 properties sold in the city increased by 11.3 percent during calendar year 2021 and IBO projects that the total market value of Class 1 properties will increase by 6.0 percent for 2023.

Assessed Value for Tax Purposes. For 2023, IBO forecasts that total assessed value for tax purposes will increase by 7.2 percent, from $256.6 billion to $274.9 billion. While we project that total assessed value in Class 1 will increase by 3.9 percent, we expect assessed values of Class 2 and Class 4 properties to increase by 6.3 percent and 7.8 percent, respectively.

For Class 2 and Class 4 properties, the billable assessed value—the value used for tax purposes—is the lower of the actual assessed value or a transitional value which phases in assessment changes over five years. Only one-fifth of

Median Percentage Changes in Valuation Variables From 2021 to 2023
By Fiscal Year

Property Type	Borough	Valuation Variables	2022 Over 2021 Median Percentage Change	2023 Over 2022 Median Percentage Change
Office	Manhattan	Income	-18.0%	15.8%
		Expense	2.5%	12.3%
		Net Operating Income	-24.2%	15.8%
		Base Cap Rate	2.3%	6.8%
		Full Market Value	-25.4%	10.5%
	Other Boroughs	Income	-15.9%	15.8%
		Expense	2.2%	6.8%
		Net Operating Income	-19.7%	17.8%
		Base Cap Rate	2.0%	6.8%
		Full Market Value	-20.7%	12.0%
Retail	Manhattan	Income	-24.8%	10.6%
		Expense	2.2%	10.6%
		Net Operating Income	-27.7%	10.6%
		Base Cap Rate	3.9%	6.8%
		Full Market Value	-29.9%	5.9%
	Other Boroughs	Income	-17.6%	14.0%
		Expense	2.2%	12.6%
		Net Operating Income	-21.3%	14.0%
		Base Cap Rate	3.0%	-0.2%
		Full Market Value	-23.2%	13.8%
Hotel	Manhattan	Income	-31.9%	8.3%
		Expense	-31.5%	8.3%
		Net Operating Income	-30.1%	8.3%
		Base Cap Rate	1.0%	6.1%
		Full Market Value	-30.9%	2.3%
	Other Boroughs	Income	-30.1%	10.0%
		Expense	-34.1%	10.0%
		Net Operating Income	-30.1%	7.5%
		Base Cap Rate	0.7%	4.1%
		Full Market Value	-27.0%	5.0%

SOURCE: Department of Finance fiscal years 2023, 2022 and 2021 Notice of Property Value Data

New York City Independent Budget Office the change in assessed value in any one year enters into the calculation of transitional assessed value for that year, and another fifth enters into the calculation for each of the four prior years. In most years, a property's transitional assessment is lower than the current actual assessment and thus becomes the billable assessed value. This feature of the property tax system makes the property tax revenue less immediately sensitive to business cycle shocks, spreading the revenue effect of a shock over several future years. When the economy is booming, it also allows the property owner to defer paying some of the tax on the full increase in their property's value in a given year.

The assessed value changes from the preceding four years that have yet to be recognized on the tax roll form a pipeline of assessment changes that can result in higher assessments, even when current market values are stable or declining. The strong growth in market values over recent years led to a robust buildup of the pipeline of prior assessment increases waiting to be phased in. However, the steep reductions by DOF in the market values of Class 2 and Class 4 properties for 2022 wiped out the entire pipeline leading to a reduction in the total assessed values for tax purposes in 2022. Even though the assessed values for tax purposes is projected to increase in 2023, the pipeline still has a $2.4 billion of assessment reductions to be factored into assessed value for tax purposes over the next three years, dampening the growth of property tax revenue during these years. With IBO projecting an average growth rate of 5.0 percent in market values for Class 2 and Class 4 properties from 2024 to 2026, we project the net value of assessment changes in the pipeline to return to being positive in 2024 and reach $22.3 billion by 2026.

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Endnotes

[1]Properties of utility companies make up Class 3, which is far smaller than the other classes.
[2]See https://www1.nyc.gov/site/finance/taxes/property-rpie.page for more information.
[3]A property's capitalization rate is the expected rate of return on a real estate investment property, and it is measured as the ratio of a property's net income to its estimated market value. Looked at another way, the market value of a property is estimated by the ratio of net income to the capitalization rate. All else equal, an increase in the cap rate results in a lower estimated market value estimated.
[4]Income and expense statements for calendar year 2021 will be filed in June 2022.