

FINANCIAL INCENTIVES TO ENCOURAGE DEVELOPMENT
THE CASE OF LONDON AND NEW YORK

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What are the right financial incentives to encourage development in the global city? What mix of such incentives will guarantee the public administration's social and urban agenda is realized alongside with the developers' much sought-after ROI?

These are questions development agencies and administrators in global cities such as London and New York are constantly trying to find an answer to. The role financial incentives are to play in the development of long-neglected areas of the modern city, such as the waterfront, is crucial. The outcome of these incentives, however, can sometimes be disappointing. This is the case for those public administrations which relied on such subsidies to encourage development of affordable housing but instead saw their cash benefits being used by developers to build more luxury apartments in well-off areas of the city.

The importance of the financial incentive structure to promote development in new areas of the city is twofold: on one hand the city needs these incentives to lure the private sector in areas which do not yet display strong demand for different real estate products (retail, residential, commercial, office, or industrial); on the other hand the public agency may need to give something more to the developer in exchange for such valuable public assets as affordable housing units and public spaces. In all scenarios, one thing is certain: neither public nor private sectors can carry through the development independently. This is particularly true for massive urban regeneration plans such as the Thames Gateway Initiative in London and similar waterfront projects in New York. The costs of such ambitious visions are simply unsustainable by either the private or public sector; especially where the aim of the development is to bring economic growth, new jobs, and better housing and civic spaces to disadvantaged areas of the city.

Collaboration between these two sectors is therefore inescapable; financial incentives can serve as a meeting point between the city's planners and the developers. The London Thames Gateway Development Corporation (LTGDC) has recognized the importance of cooperation between the key public sector agencies and developers to decide on how to best fund 40,000 new homes and 28,000 new jobs in two of London's "prime growth areas": Lower Lea Valley and London Riverside. At the basis of this cooperation is the general understanding that the planning applications envisioned "cannot be afforded by either party."¹

For the provision of affordable housing, the public authority may direct its financial incentives at both developers and future tenants to ensure both parties have the means necessary to achieve their goals: a satisfactory return on investment for the developer, and an affordable rent for the low to moderate income dweller. New York City has already experimented with subsidies to families with annual household incomes which inhibit them accessing rental units in hot real estate markets like Manhattan. The Battery Park City Authority has subsidized affordable housing units over the years in attempt to bring more middle-class families to this area of downtown. The tools used by the city to jumpstart the development process included: low-interest housing loan programs, tax-credits, and tax-exempt bonds for reserving 20% of new units for qualifying low-income renters.²

¹ Venning, Martin. "Thames Gateway Challenges Require Fresh Approach: New Charge Announced" Online. <http://www.ltgdc.org.uk/news/pressreleases/detail.asp?newsID=82>; Sept. 26th, 2006

² Pristin, Terry. "Battery Park City to Give Low Income Renters A Break" March 24th, 1998 Online. [Nyt.com](http://www.nytimes.com)

For vast urban regeneration initiatives, which involve new development as well as an economic growth agenda, a bond issuance program by the city and government can help generate the large funds needed to bring about this level of structural, economic, and social change to the urban landscape. The New York Liberty Bond program is a \$8 billion initiative which aim is “to provide low cost, tax exempt, bond financing, for major projects to revitalize Lower Manhattan and ensure the City’s long-term economic health.”³ These types of bonds represent a valuable source of financing for both city and developers: these bonds offer significantly lower interest rates than commercial loans and are more attractive than equity.

However, limitations may exist for the use of these bonds by the private sector to finance commercial and residential development. A common condition is the requirement that a percentage of new residential units be devoted to low income rents. In the aftermath of September 11, New York City was able to overcome some of the most challenging limitations to the use of traditional private activity bonds to help a fast and successful recovery of the Lower East Side with new development in all property classes: commercial, residential, retail, and office as well as public infrastructure. The City and State were able to approach the private sector with a favorable new bond program. The Liberty Bonds, unlike traditional tax-exempt bonds, allowed developers to avoid the low-income housing requirement (as percentage of new residential units) and keep any net earnings from investment of bond proceeds that could now be used to offset some of the project’s costs.

The Liberty Bonds are an example of how the public sector can provide significant financial incentives to developers—in the form of low-cost funding—to ‘regenerate’ a large urban area, such as the Lower East Side, which suffered the devastating effects of 9/11 and its aftermath. The LTGDC, together with other city and government agencies, may find it necessary to resort to this type of tax-exempt bonds in order to spur the desired level of economic activity and private development particularly in the most seriously run-down areas of the city.

Other types of financial incentives that can be made available to the private sector are lower permit-application fees and tax increment financing. Under the former scheme, a developer will find the process of obtaining the necessary permits from the local public administration less time-consuming and less costly resulting in a higher propensity to invest and bring plans to fruition. Through the use of tax-increment financing, the municipality can look at the contribution of future tax revenue, attributable to the increase in the local tax base from new businesses, as a way to publicly finance structural improvements such as public infrastructure.

Aside from subsidizing developers for new construction, cities have also recognized the importance of providing various incentives to the businesses and tenants which are looking to locate their operation in the areas affected by the new development. The LTGDC has various programs to provide incentives to small businesses interested in locating in the

³ “New York Liberty Bond Program” Online. <http://www.empire.state.ny.us/wtc/LibertyBonds/wtc-LibertyBonds-program.htm>

Thames Gateway. Such programs range from venture capital⁴, Soft Loans, training and recruitment initiatives, small business start-up support, technological support, sector-specific knowledge resources, to “skills matching” where the public council acts as a broker between local job seekers and employers.⁵

Government Grants are also available to eligible business looking to locate their operation in Thames Gateway. Qualification criteria for these public grants include, in general, projects that add to the local employment and which can bring significant investments in the local skill base. In addition, businesses must be located within the specified area, must invest in fixed assets such as property, plant or machinery, and are expected to find the majority of the required financing from the private sector.⁶

Tax-exemption programs are also used by public administrations to provide an incentive for business relocation in the desired area. The New York City Economic Development Corporation (NYCEDC), a twin sister of London’s LTGDC, currently offers four types⁷ of commercial incentives in the form of tax-abatements. These cuts can be in one of the following forms: a five-year reduction from commercial rent tax for large employers (125 employees or more), exemption from sales tax for lease improvements on newly signed leases for 10 or more years, and deductions in corporate taxes for employees relocated to the city from other company headquarters.⁸

In conclusion, whether tailored after the needs of developers, businesses, or low-income residents; all these financial incentives are part of the public administrations larger initiative to attract and retain new development in less-desirable areas of the city. While extremely important, these incentives will not yield the desired level of economic activity if they are not accompanied by other programs the public sector is empowered to provide. Some of the most important initiatives include: land assembly, zoning and variance modifications, public infrastructure investments, and marketing of the interested areas by the municipality to prospective tenants, residents, and businesses.

⁴ National Business Angels Network (NBAN) a not for profit company supported by UK Dept. for Trade & Industry

⁵ Gateway To London “Business Opportunities” Online. <http://www.gtlon.co.uk>

⁶ Gateway To London “Government Grants” Online. <http://www.gtlon.co.uk>

⁷ Commercial Rent Tax Savings, Sales Tax Savings, Lower Manhattan Relocation Employment Assistance Program, Special WTC Rent Reductions

⁸ New York City Economic Development Corporation “Financing & Incentives” Online. <http://www.nycedc.com>