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Unleashing the Private Sector: How Government Policy Can Facilitate Private Solutions to New York City's Housing Crisis

Richard T. Roberts

Richard T. Roberts, a Managing Director at Goldman Sachs, was Commissioner of the New York City Department of Housing Preservation and Development and Chairman of the Board of the Housing Development Corporation under Mayor Rudolph Giuliani. This is an edited version of his remarks at a Manhattan Institute Forum on September 19, 2002.

The gap between the supply of affordable housing and the demand for this housing is widening in the United States. This is particularly true in cities like New York where population has been increasing. The cost of construction is rising and the supply of developable land is dwindling. The convergence of these trends poses a great challenge to all of us.

Rather than dealing with the root causes of these problems, however, in New York City we seem to quickly revert to a reliance on subsidies to bridge the gap between affordability and cost. It's a very simple problem. It costs a certain amount to build the housing and to maintain it, and then people have to pay a certain amount to rent it or own it. As a general matter, there is a disconnection between what people can afford to pay and what it costs to build and maintain housing.

We ought to initiate a conversation about a series of different approaches to deal with that, particularly in a time of constrained resources.

Given what's going on in our economy, generally speaking, and the resource constraints on all levels of government, I think we will be forced to look at these issues in a much different way. And the onus is on the government to modify its programs in order to apply the limited subsidy dollars that exist to those projects that truly need it.

One of the things that was peculiar about my experiences as housing commissioner was that we were not subsidizing housing just at the low end of the market; we subsidized it all, from luxury development in the core of Manhattan to affordable low income housing that we built or sponsored in Central Brooklyn or in the South Bronx. Unfortunately, we continue to do more of the same subsidizing.

Over the last fifteen years, the city has worked tirelessly to rebuild New York's communities. Beginning in the Koch administration, the city, through its now-famous Ten Year Plan, spent about \$5.1 billion building or renovating over

180,000 units of housing during this 15-year period. This investment, buttressed by a variety of gains in public safety and quality of life initiatives, has been a significant factor in community revitalization. These neighborhoods—the South Bronx, Central Brooklyn, southeast Queens, and northern Manhattan—are now more vibrant, more stable, and more attractive from an investment standpoint. As a matter of fact, I oversee an effort at Goldman Sachs that is focused exclusively on trying to identify opportunities for us to deploy our capital into these markets, in order to generate returns that are competitive.

To give you one example, I think in my last year as housing commissioner of the city of New York, through HPD, we spent about \$270 million on investment in Northern Manhattan that leveraged another billion dollars in private investment just in construction of affordable housing and commercial development in the three community boards in Northern Manhattan (Community Boards 9, 10 and 11). But much of this gain in units has not alleviated the need for supply.

Cost of construction is a big impediment to increasing supply. One of the reasons we have to subsidize so greatly is because our costs are too high. If we could lower production costs, we could achieve greater affordability.

Peter Salins, in a Manhattan Institute study, estimates that New York City's housing gap is in excess of 140,000 units. The city's housing gap is even larger—over 400,000 units—if one takes into account the need to replace older housing stock. We would need to create or develop the equivalent of the city of Baltimore in order to fill that gap.

These facts play themselves out in the price of housing. Without a swift response to this widening gap, we will find ourselves in an even greater predicament. According to the 2000 Census, the population of New York City increased by roughly

686,000 people between 1990 and 2000. Yet the number of housing units increased by only 194,000 during that same period. Although the shortage of affordable housing is not a problem peculiar to New York, the situation here is particularly acute.

Housing experts generally agree that a housing market must have at least a five per cent vacancy rate in order to provide satisfactory opportunities for new and existing residents. During the last three decades, the city's vacancy rate has fallen below five per cent, a further indication of our limited supply in this city.

But there are significant affordability issues as well, as Professor Schill has demonstrated. According to the 1996 Housing and Vacancy survey, which is the definitive housing research document produced by the city of New York, more than one quarter of all renters in New York City face severe rent burdens, paying over half of their incomes for rent. This problem will escalate as demand increases.

Cost of construction is a big impediment to increasing supply. One of the reasons we have to subsidize so greatly is because our costs are too high. If we could lower production costs, we could achieve greater affordability. The way we've dealt with it historically has been to bridge the gap with public financing. A different way we could do it would be to reduce the cost associated with developing housing; and that's principally what I want to talk with you about.

The cost of housing construction in New York City is significantly higher than in comparable cities. The 1999 housing cost study done by New York University reported that the hard costs of construction in New York are between 21% and 55% higher than in Los Angeles, Chicago, and Dallas. We need to tackle this problem and adopt

overdue changes. We also need to face the reality of this shortage and the reality of escalating construction costs, and address these issues head on. However, this requires a true change in responsibility and expectations on the part of both the public and the private sector.

What can be done? I'm going to talk about three things. One is the building code. A variety of proposals have been floated, ranging from a complete overhaul to mild tinkering with our building code. I don't know the specific answer. I invest in real estate development projects and I oversaw them for the city. I never built one. But the current code is an exhaustive 2,000 pages. It was created in 1968 and mistakenly fails to take advantage of newer building technologies, perhaps at the expense of safety and reduced costs. The code's complexity presents a barrier to entry for developers who are unfamiliar with New York City, and increases the cost of housing production for developers who do decide to enter the market.

Part of the reason the code remains unchanged is that we've got an inside baseball game going. We have a building code that is extremely complex, and we've got a set of real estate developers who understand it—who have essentially created a cottage industry for themselves in interpreting the code. They are the same people who came to me in my former role and tried to get more subsidies. I believe the model building code should be adopted. There are only two jurisdictions in the country that have failed to adopt the model building code: the City of New York and the state of Wisconsin. And so, we ought to think a little bit about that and figure out some way to modernize and to streamline our process.

There's another situation that I think also merits discussion. And that is a specialized sub-code for

rehabilitation. In 1997 or 1998, the New Jersey rehabilitation sub-code won a John F. Kennedy School of Government Innovation in Government award. There are housing stocks available in many urban areas that remain untapped in part because rehabilitation projects are required to bring buildings into compliance with current building codes for new construction. So if you want to do a rehab project, the general mentality has been throughout the country—and I think even the model code calls for this—that instead of taking a perfectly good building and rehabbing it in a way that is safe and sound for the use that you have in mind, you should look at that building as if you were constructing it new for the purpose that it is now going to be used for. So if you're converting a manufacturing facility to a residential facility, you now need to look at that building as if you were doing new residential construction.

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Construction standards written for new buildings have been applied to rehabilitation work on existing buildings without demonstrable improvements in safety and often at prohibitive costs. Uncertainty plagues the process because developers and builders cannot predict or rationally assume the code requirements to build and to bring a building back into use; projects in existing buildings are often overlooked or dismissed as excessively risky. The bottom line is that building owners who want to improve their properties should not be discouraged from doing so.

In New Jersey they adopted such a rehabilitation sub-code, and they saw construction activity in their central cities increase by 30% as a direct result of adopting the rehabilitation sub-code.

Next issue: zoning. One of the underlying barriers to increasing housing production is the relative scarcity of land on which housing can be built. And developers continue to be saddled with the unpredictability and uncertainty of city planning, ULURP (the Uniform Land Use Review Process), and, in many cases, the environmental impact statement process. Particularly for affordable housing developers, who often operate on thin profit margins, the uncertainty and risk can be insurmountable. In particular, city planning has been very reluctant to rezone sites that are currently zoned as manufacturing to housing and residential use, notwithstanding the fact that in many of these areas, manufacturing is not coming back. In fact, I think there was a whole plank of the Ferrer campaign that was specifically focused on preserving manufacturing zoning for many of these sites—notwithstanding the fact that the sites are obsolete and they weren't going to be developed for manufacturing. We need to look at those sites as potential zoning sites.

Ultimately investors and developers look for certainty in the marketplace. In the current environment, we lack certainty. We either need to streamline our processes or eliminate uncertainty if we truly want to change the current climate to one where development is encouraged and profitable.

Now in ULURP, the Uniform Land Use Review Process, the layers of review are both burdensome and unpredictable—a deadly combination. Even in a straight-forward situation the reviews can take years to complete. In a process where time equates to cost, we have a serious problem.

Let's talk about the recent garden issue as an example of ULURP's unpredictable nature. If you're in the city of New York and you're going to dispose of a city-owned site, you must subject that site to the Uniform Land Use Review Process. That process actually is a little bit like a baseball

game. It requires nine steps. First HPD needs to approve the initial site. Then you have to get approval from the land use committee of the local community board, the full community board's approval, the approval of the local council member, the approval of the land use committee of the council, the approval of the full council and finally, the approval of the borough president. Ultimately it has to go back to the mayor, who initiated the process to begin with. All of these people get an opportunity to review and approve your project. If all goes well, you're in for nine months to a year, but often it takes much longer.

Years ago, with the community gardens, when many of these communities had been devastated, the Koch administration and the administrations that succeeded it decided to take sites and allocate them for *temporary* interim uses as gardens, all with the view that once the funding was available or approvals had been achieved, those sites would then be made available for development. Everybody knew the rules of the game.

The article in today's *New York Times* should have been recast: "Bloomberg and Spitzer change the rules of baseball." You now will play forever. It's not a nine-inning game. We will decide at the end of the day who wins. That wouldn't be a very interesting baseball game, and it was something we would not accept. Under today's deal gardeners get an opportunity at each step along the way to try to get their use approved on a permanent basis. We worked very extensively with the Parks Department on this and with Henry Stern when I was Housing Commissioner. At each step along the way, the gardeners lost. Nine sets of approvals. Note that I've got nothing against a garden, but we should have rules. There should be a process. Why should I invest if Elliot Spitzer can come in after everything is said and done and decide to sue because the process was faulty? We now have a due process right for gardens.

Secondly, the deal allows for further review. Jane Weissman was quoted as saying the great thing about this is even with the sites that we've agreed to build on, we're going to review those again. So we now have *another* inning to the game, and thus this is a classic example of why there is no predictability in the process. This is increasing costs and decreasing our ability to develop affordable housing.

Ultimately investors and developers look for certainty in the marketplace. In the current environment, we lack certainty. We either need to streamline our processes or eliminate uncertainty if we truly want to change the current climate to one where development is encouraged and profitable. Eliminating barriers to housing production is essential.

The notion that subsidies alone can entice developers into these markets is a short-sighted solution and one that is particularly unrealistic at this time. If we do not take swift measures to create or augment systems of housing finance that will

enable developers to build housing and consumers to purchase it, we will have allowed our current affordability and availability crunch to further jeopardize the future of our city. Without sustained investment, the momentum we have gained in community revitalization will dwindle.

We should make all the attempts to build on our gains. This is particularly important for those neighborhoods that have been the great beneficiaries of our more recent investment. I would encourage developers, government officials, investors and particularly our political leadership to search for ways to partner so that we can create a coherent strategy for change—but we can't stop there. It can't be like what happened with the recommendations of the housing cost study that, when I was Housing Commissioner, we helped to finance and that the NYU center, under Michael Schill's direction, put into place. Those recommendations created an excellent discussion, but very little action at the end of the day. We need to implement real change at a variety of levels to meet the needs of the city in this regard.

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