

Reducing the Burden of NYC's Commercial Rent Tax



MANHATTAN
CHAMBER OF
COMMERCE

EXECUTIVE SUMMARY

The Commercial Rent Tax is an onerous tax that only affects renters of commercial space in Manhattan below 96th street.

The tax is unfair because it narrowly targets one area of the city while favoring other neighborhoods; and it amounts to double taxation insofar as renters are already paying property taxes which are often included in the rental price.

Further, the tax increases as rents rise which is problematic in the current environment: rents have jumped 42% in Manhattan since 2012. All of this is threatening the stability of small, neighborhood businesses that cater to the needs of long-time residents. Too many are forced to relocate or close.

This paper presents several scenarios for targeting tax relief to help businesses thrive and drive economic growth. Now is the time for such change, as the City currently has significant cash reserves and tax revenue surpluses.



ABOUT THE MANHATTAN CHAMBER OF COMMERCE

The Manhattan Chamber of Commerce is a membership organization that provides resources, advocacy and networking opportunities to help businesses thrive and professionals advance their careers.

Our membership is comprised of a cross-section of 15,000 businesses and subscribers ranging from sole proprietors to large corporations.

Learn more at www.manhattancc.org.

AFFORDABILITY CRISIS

Not a day goes by where New Yorkers do not read about another business that is unique to the character of our city closing down. Small, neighborhood businesses that cater to the needs of long-time residents are disappearing. Rapidly escalating rents are forcing many to relocate or shutdown altogether.

The average asking rent for retail space in Manhattan rose nearly 42% between 2012 and 2015 (from \$110 per square foot to \$156 per square foot).ⁱ

Several neighborhoods in the city are "hot" -- attracting new commercial tenants willing to pay rents that long-time businesses cannot afford.ⁱⁱ

For example, in the West Village, rent spikes are nearly universally reported as the reason so many storefronts have closed over the past few years. Cafe Angelique reportedly closed when its \$16,000 rent increased to \$42,000 per month. A Gray's Papaya on Eighth Street closed after its owner reported a rent increase of \$20,000 per month.ⁱⁱⁱ Avignone Chemists, a Village institution dating back to 1929, was forced to shutter this year after the new building owner tripled the rent.^{iv}

Even large businesses are not immune. FAO Schwartz and Toys "R" Us' flagship STORE in Times Square recently closed because of escalating rents.^v Similarly, Crate & Barrel closed its Manhattan flagship store in Midtown East after more than 20 years.^{vi}

There is an affordability crisis throughout Manhattan -- for residents and businesses alike. Exacerbating the problem for businesses is the City's Commercial Rent Tax which is calculated based upon annual rent paid. Businesses pay a higher tax as their rents go up.

ABOUT THE COMMERCIAL RENT TAX

The Commercial Rent Tax (CRT) was enacted by a cash-strapped City back in the 1960s. When fiscal conditions later improved, the tax was eliminated for most parts of the city, including the outer boroughs and northern Manhattan. Today the tax is only imposed on commercial tenants south of 96th Street in Manhattan (except for areas near the World Trade Center) at an effective rate of 3.9% of base rent.

Tenants are exempt from the tax if their annual base rent falls below \$250,000. But fewer and fewer businesses in Manhattan fall below that threshold so a greater number end up paying the tax.



In 2003 the City collected nearly \$388 million from 5,858 businesses.^{vii} By 2013 CRT revenue had grown to \$652 million paid by 6,757 businesses.^{viii} Today 7,354 businesses are on the hook for the tax,^{ix} generating \$720 million in revenue for the City this fiscal year alone. That figure is expected to grow to \$770 million next fiscal year and \$805 million the year after that.^x

This is a significant amount of money to extract from businesses on top of the rising rents and other costly mandates that they face, such as the increasing minimum wage and requirements to provide paid sick leave.

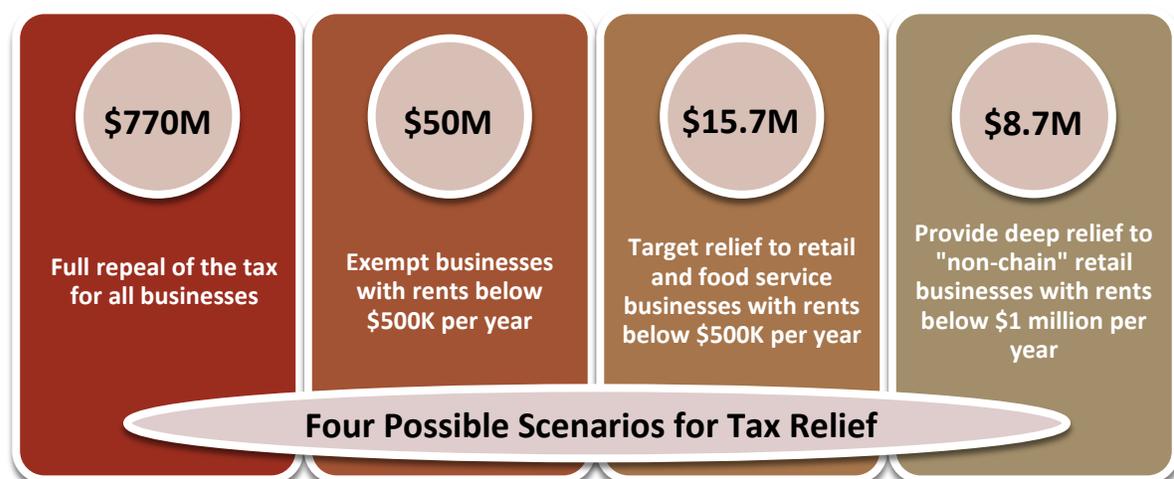
A growing number of thought leaders have acknowledged that the Commercial Rent Tax is burdensome, regressive and unfair. City Finance Commissioner Jacques Jiha recently said that, "It favors businesses in the outer boroughs [at the expense of] businesses in Manhattan. And it's also a double tax because businesses pay property tax, and on top of property tax they have to pay commercial rent tax."^{xi}

High-ranking officials including City Comptroller Scott Stringer, Manhattan Borough President Gale Brewer, and the City Council's Economic Development Chair Daniel Garodnick have called for reform of the tax.

OPTIONS FOR PROVIDING TAX RELIEF

Like most taxes in New York the Commercial Rent Tax falls under the jurisdiction of the state. However the City has the power to alter the effective tax rate (by changing the base rent reduction granted) so reforms could come from either level of government.

Below are four possible scenarios for moving forward.^{xii}



Scenario #1 - Full repeal of the tax

- *Businesses helped: ~7,350 / Foregone revenue for the City: \$770 million (but possibly phased out over time)*

In 2015, the New York State Senate passed legislation to fully repeal the Commercial Rent Tax in New York City.^{xiii} The bill did not advance in the Assembly, likely because the City did not want to forgo the significant revenue that will be generated by the tax next year. However, a full repeal could be phased in over time (so the revenue loss would not be drastic), perhaps by reducing the effective tax rate each year for ten years.

Scenario #2 - Raise minimum threshold to \$500K annual base rent

- *Businesses helped: ~3,000 / Foregone revenue for the City: \$50 million*

The threshold at which businesses are exempt from the tax could be raised from \$250,000 in gross annual rent (currently) to \$500,000 in gross annual rent. This would remove nearly 3,000 businesses from having to pay the tax. This option would treat all businesses the same regardless of industry or profit margins as the threshold is based solely on rent paid/size of space occupied by the business. City Councilman Daniel Garodnick has introduced legislation to this effect (bill number Int. 799-A).

Scenario #3 - Target relief to retail and food service businesses with rents below \$500K

- *Businesses helped: ~750 / Foregone revenue for the City: \$15.7 million*

Retail and food service businesses such as restaurants often have very low profit margins so they are particularly threatened by the Commercial Rent Tax. Targeting relief to these sectors would help ensure that businesses are protected without costing the City significant revenue losses.

Scenario #4 - Provide deep relief to retail businesses with rents below \$1M

- *Businesses helped: ~660 / Foregone revenue for the City: \$8.7 million*

In 2005, as part of an aggressive economic development package to attract and retain businesses to lower Manhattan after 9/11, the state permanently eliminated the Commercial Rent Tax at the World Trade Center area, and for all retail tenants in the area generally south of Murray Street between South and West Streets.^{xiv} Retail tenants have extremely low profit margins and are particularly vulnerable to closures when rents rise rapidly. In this scenario, "chain" retailers are carved out of the exemption to further target relief to those most likely to be in need.

A CALL TO ACTION

The Manhattan Chamber of Commerce urges Mayor de Blasio and the New York City Council to move quickly to implement needed relief from the Commercial Rent Tax.

Now is the right time for action, as the City will end the current fiscal year with a budget surplus of \$2.5 billion.^{xv} And in such flush times the City has an opportunity to begin phasing out this onerous tax. Over time, the resulting revenue losses will be offset by revenue generated from business expansion and economic growth. Indeed many businesses will reinvest the tax-savings into their companies by hiring new employees and increasing NYC sales and payroll taxes.



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