



**Testimony of Commissioner David M. Frankel
New York City Department of Finance
Before the New York City Council
Committees on Finance and Community Development**

On Intro 26A, in relation to the Sale of Liens on Property

February 18, 2011

Good morning, Chairs Recchia and Vann, and members of the Finance and Community Development Committees. I am Finance Commissioner David M. Frankel and appreciate greatly the opportunity to be with you this morning to discuss Intro 26A, which would reauthorize the City to sell liens on properties that are delinquent in property-related charges. My colleagues from OMB and HPD have already shared many of our reactions and I will try not to be repetitive.

Let me start by saying we must be as aggressive as possible in collecting unpaid funds. I certainly appreciate that the prospect of losing a home or other property is traumatic and the process must be absolutely fair and, to the extent possible, protect our most vulnerable citizens. However, our focus must be on the overwhelming majority of New Yorkers who pay their taxes, who pay their charges, who pay their fines. They are the ones suffering because of those that don't pay in the form of increased taxes or reduction of services. While we will work with individuals who may be in financial distress, we must be sure we collect the money that City residents depend on to provide their services. We must be mindful that every dollar owed that we choose to consciously forego, represents a real choice of not funding some other worthwhile service or raising revenue through taxes or some other source.

As has already been outlined, the lien sale is a critical collection tool for New York City. Over the last 15 years, the sale has been a true success story as we have collected over \$1.5 billion in property-related debts efficiently and relatively quickly, not to mention the billions more from

people who paid on time because of the strong enforcement threat. As the lead agency in conducting the annual lien sale, the Finance Department notices thousands of delinquent properties, and then works diligently to whittle that list down – by sending multiple notices, publishing and republishing lists of delinquent properties, holding outreach sessions with our sister agencies —before we ever get to the act of selling a lien to the Trust.

While we are fully supportive and appreciative of the inclusion of ERP charges as qualifying, the current draft of Intro 26A creates some significant and unnecessary new challenges for us. It also does not go far enough by failing to qualify other agency charges, such as those assessed by the Health or Buildings Departments for unhealthy or unsafe conditions. As I said earlier, most New Yorkers pay these charges. There should be no hesitation in protecting them by using all our tools to collect from those who don't pay.

Many of the proposed changes would make our work either harder or require significant new resources. In other aspects, the bill raises serious legal questions. I will outline our issues on both administrative and policy grounds. In doing that, I underscore that we are completely open and anxious to work with Council members and staff on addressing these issues to fashion a bill of which we can all be proud.

Administrative Challenges

Income Exemption

Under the current system, properties that have received certain homeowner property-tax exemptions – for senior citizens, disabled and those that qualify for what is known as the state circuit breaker – are ineligible for the lien sale. This bill expands these exemptions by including all properties with the veterans' exemption, as well as some of those seniors with the Enhanced STAR exemption.

While we can debate the policy merits of granting full exemption from the lien sale and thus from property tax obligations for whole groups of homeowners, I hope the Committees will recognize as unworkable a requirement that we split hairs with new income levels for removing properties. This bill would require that homeowners who get an Enhanced STAR exemption are ineligible for the sale, but only if they earn less than one and one half times the Senior Citizen Homeowners Exemption (SCHE) income limit. Enhanced STAR has an income limit at \$79,050 and SCHE's limit is \$37,400. This bill would force Finance to create a third category, where lien-sale staff would have to check private personal income documentation and then create a process to verify and audit the information.

While tying benefits to income has obvious merits, the process can be immensely complicated and costly to administer. At Finance, we learned this the hard way when we took over responsibility for the Senior Citizen

Rent Increase Exemption program. We thought we could turn SCRIE into a fully automated process. We were wrong. For example, Finance cannot simply “data match” to discover income. First, our income tax information is tax-secret and can only be used for income tax enforcement purposes if a resident signs a waiver. Second, when we went to the SCRIE population and asked for waivers to review their tax information, we found that most did not file income tax returns since their income was below the threshold. We then had to collect different kinds of income information from the entire group and analyze it separately. Third, reviewing income information, whether through tax returns or other submitted forms, is always problematic since definitions of “income” differ under different laws. For example, income for SCHE is reduced by some prescribed modifications while Enhanced STAR uses Federal or State Adjusted Gross Income for all eligible residents in the home, with no modification allowed. It is not clear which of these two definitions or perhaps a third would be used with respect to Intro 26A. In any event, it is problematic.

Before taking on SCRIE, we had concluded we could administer the program with little or no additional staff. However, we now have 12 full-time employees staffing the program. Many of you are more than familiar with the problems this caused before we cleaned up our act, and none of us would like to see that repeated here. The provisions of this bill would create a program that is more complicated and requires more resources than SCRIE.

Payment Plans

The legislation also requires that payment plans be created on a means-basis, which presents the same problem of obtaining, verifying and auditing income information from applicants. That is, Finance would have to create an income formula that would allow those with lower incomes to make smaller down payments to begin a payment plan, and collect and verify the income information.

As members of this Committee who have been past partners with us in lien-sale outreach events already know, Finance has traditionally been extremely flexible in providing payment plans to individuals who come forward to settle debts during the notice period. We offer a quarterly payment schedule that is tied to the payment schedule that we have established for the majority of homeowners who remain current on their debts. We also extend those payments out as far as eight years.

The new bill creates a monthly payment system and a 10-year window for payments, both of which add significant new administrative hurdles. Our Statement of Account, which is a quarterly billing system, has proven fairly effective. Our system would need to be reprogrammed for little added benefit.

Additionally, it appears that under this draft bill a property is permanently excluded from the lien sale once the owner has entered into a payment agreement – even if the owner later defaults on that agreement. I am sure that the Council did not intend this result. Our data shows that a high percentage of properties that entered into agreements in earlier lien sales are now in default of those agreements: Of the \$79 million currently outstanding in the approximately 4,000 open payment plans, some \$50 million – or 63% -- comes from properties that are in default on their commitment. The law needs to create incentives to keep up with payment agreements, not default on them.

New Notices and Mailings

The bill requires that DOF send quarterly mailings to all property owners informing them about the lien sale. We estimate that these provisions would require us to produce an additional 2 million pieces of mail annually at a cost of at least \$1.5 million. Given that 98% of property owners pay their taxes on time, this is not a sensible use of City resources.

Another challenge of the new legislation is a requirement to add a 100-day and a 120-day notice. Further lengthening the notice period would do little to enhance property owner's awareness and would do nothing in terms of getting people to pay.

Under the lien-sale reauthorization law that the Council passed in 2007, the previous 60-day notice period was extended to 90 days. However, our data shows little additional revenue was collected because of the increased time. In fact, 85% of debt is settled in the last 60 days prior to the lien sale and almost a third settled in the final ten days. The new notices and extended time frame would add significant cost and delay without any substantial benefit.

Certified Mail Noticing

As I mentioned, Finance already does extensive noticing of those properties eligible for the lien sale. In fact, by the time the average Class One property owner gets their first notice for the lien sale, they must have already received at least 12 statements in the mail. Once the lien sale process starts, the City will contact affected property owners at least three additional times with targeted messages. We send delinquent owners a notice of our intent to sell a lien if they do not resolve their debt within 90 days. We also publish this list of properties in a local major daily newspaper, place ads in other daily papers and community papers across the City, and post the list on our website. Thirty days later and sixty days before the sale, we send a second notice to owners. Thirty days after that we send a third notice. Ten days before the sale, we publish an updated list in the newspapers and advertise again. Our website is updated throughout this process.

Only after all of these notices and warnings, do we sell a lien for all the properties that have failed to address their debt. Over the past three years, of the approximately 25,000 properties that were initially noticed annually, less than 5,000 had a lien sold. And, as OMB noted, very few of these properties actually go into foreclosure.

An additional unnecessary burden of Intro 26A is a new requirement that a lien-sale notice must also be sent via Certified Mail (with return receipt) four months in advance of the sale to anyone with an interest in the property. First, the postage for this alone would range between \$250,000 and \$500,000. Second, the administrative burden of mailing and matching tens of thousands of return receipts is onerous. Finally and perhaps most troublesome, is the possible interpretation under the bill's language, that if an owner does not sign the certified return receipt, we would be unable to include the property in the lien sale. I am certain that the Council did not intend to create a provision where evading certified mail sent to your address became another means of evading your financial obligations to the City.

Defective Lien Provisions

There are also many questions raised by the language relating to liens being deemed defective at the time of the lien sale, if the owner would have been eligible for a specified exemption even though they never applied for it. Are applicants required to come in and prove their past or current eligibility for an exemption, or both? Is the City required to determine on its own whether a property would have received an exemption had the owner made a

timely application? What if the liens on a property that is eligible for one of the newly stated exemptions were sold and the servicer collected the money from the taxpayer--is the City now going to be required to reverse prior sales of tax liens and refund the Trust for the defected liens for an indefinite number of back years? Are the tests for eligibility those that may have existed in the relevant tax year or the current year? While the bill may not have intended to create this series of complex operational issues, they need to be addressed.

In addition, these provisions if not amended, will mean that the lien pool is potentially subject to change even after the liens have been sold. When the City declares liens defective after they are sold, the money to make the trust whole comes from the City's own tax levy. We leave it to OMB to calculate how much more this might cost, but warn that it could also drive down the Trust's payment to the City for the lien pool since a retroactive defect process could contradict the City's representation as to validity and enforceability of the liens.

Communication with Servicers

This bill requires Finance to continue playing a role as an intermediary after the lien sale date. Currently we are out of the process after the lien has been sold and we should remain so. We have serious legal concerns about the City maintaining a mandated role once a lien has been sold. Simply put, while our ombudsman unit remains helpful when inquiries come to us about properties where liens have already been sold, the remedies

we can offer are very limited. We are not and do not want to be privy to payments made or interactions with the servicer subsequent to the sale of the lien. We believe that having more than this arm's-length relationship with the servicer is inadvisable from a legal, administrative and cost perspective.

More burdensome SOA

The bill includes significant new language that would require the Statement of Account to be used as an enhanced collection tool. There are many issues regarding the Statement of Account that must be solved before we could efficiently include lien notifications. We acknowledge that the SOA could be more effective in communicating information to property owners and we have been working to re-cast the SOA to make it more helpful and understandable. Past changes made before my time have significantly improved the SOA. However, the property tax provisions are so complex that a more simple and understandable summary remains a true challenge.

There are more than 1 million properties in the City. Last year, we stopped mailing SOAs to property owners who did not owe anything – in other words, limiting SOA mailings only to those properties with outstanding charges. This saves over \$800,000 annually. Because property owners with no open balance no longer receive a quarterly SOA, fewer than half of the City's homes still receive it. This legislation would require us to give up those savings and more. In fact, going forward, we are seeking to expand the use of electronic mailing when owners opt for email over paper

documents. These beneficial changes and others that we have in the works would be precluded by the new statutory requirement that SOAs get mailed to every property.

Another issue involves the requirement that Finance add disputed charges to the SOA. This provision while appealing in concept is quite broad and alarming in scope. First, we interpret the bill's provision on disputed charges to mean that Finance cannot include disputed charges in determining whether a property has met the dollar threshold to be included in the sale. As you know, many property owners challenge their assessments each year before the Tax Commission or in court, and we encourage them to use their administrative remedies when they truly believe we have made an error in assessment. This language would preclude us from including as an eligible charge unpaid property tax that is the subject of a Tax Commission or court protest. This undermines a basic underpinning of tax law that while taxes may be in dispute, they are still fully payable. It is a long standing public policy, upheld by the courts, that delinquent taxpayers must first pay their taxes and then challenge them. Courts have upheld that a dispute about a tax bill does not stop enforcement proceedings. We must remain mindful of that basic obligation of all of the City's property owners. Given the administrative procedures in place for property owners to challenge Finance's assessments, DEP's water bills or other property-related charges there is no need for Intro. 26-A's requirement that Finance create yet another procedure. In fact, an additional tier of review would only cause confusion.

The provisions concerning other agency charges are problematic for other reasons. It creates an incentive for a homeowner to frivolously dispute a charge to get out of the lien sale. In addition to the policy challenges, there are significant practical issues in implementing these provisions. Today, 25 different charges appear on the SOA and each agency has a different method of resolving disputes. Tracking charges would require a complete change to the City's billing model, which now simply depends on agencies to pass along their charges by address. Given that each agency has its own due process procedures on disputing charges, it would be a monumental challenge to track them all.

Additional Costs of Compliance

The bill creates significant new costs for the City that we estimate at approximately \$400,000 on a one-time basis and \$3.5 million recurring annually.

The most significant one-time cost is the reprogramming of our IT infrastructure. We know the resources involved in the 2007-08 reprogramming after the law was last reauthorized, and this and other mandated additions within this bill lead us to an estimate that we may need four to six months for 5 full time IT programming staff to get our systems ready for the changes envisioned by this bill. Six months for 5 IT staff comes at a cost of over \$400,000.

The recurring costs are more dramatic. In addition to the costs of postage, and mailing that I have already mentioned, Finance will have to add staff to make the income determinations in exemptions and payment plans,

process certified mail, coordinate with the servicer staff, and with each agency whose charges might become in dispute after all due process hearings at the agency are concluded and the charge is sent to us. In total these recurring costs are: 18-23 staff at \$1.2 - \$1.7 million; approximately \$1.5 million for postage and materials; and, \$250-500,000 for the special certified mail process.

Finally, there is an addition to the bill which we believe would be extremely beneficial. Our estimates are that Intro 26A leaves \$56 million on the table this year along with a recurring \$21 million. Most of this is water debt which Commissioner Holloway will discuss in detail. However, more than \$17 million immediately and \$3 million in annually recurring collections will be foregone if the bill is not amended to qualify for the lien sale other stand-alone agency charges. Including such charges is not merely for revenue purposes. For example, property owners need to know that when the Health Department is forced to clean up your vacant lot or exterminate in your building to correct unsafe conditions, you will be held accountable. We have specific properties in many of your districts where such debts to the City are going unpaid because we do not now have this power. This bill already adds similar charges with respect to ERP, and we respectfully ask that you include the other stand-alone agency charges when considering changes to the bill.

Everyone recognizes that this is a difficult issue. I want to assure you that the Finance Department will continue to work with individuals who may be in financial distress to try to find ways for them to meet their obligations.

However, our primary focus must be on the vast majority of New Yorkers who pay their taxes, who pay their charges, who pay their fines. It is unfair to penalize them by either increasing their share of the cost of government, or reducing their services.

Thank you for this opportunity to share our thoughts, and I look forward to your questions. With that, I will turn the floor over to Commissioner Holloway.