



**Testimony of Commissioner David M. Frankel
New York City Department of Finance
Before the New York City Council
Committee on Finance**

On the Mayor's Preliminary Budget for Fiscal Year 2012

March 21, 2011

Good afternoon, Chairman Recchia and members of the City Council Committee on Finance. I am Commissioner of the Department of Finance David M. Frankel. I thank you for the opportunity to testify on Mayor Bloomberg's preliminary budget for fiscal year 2012.

I am joined today by my senior staff, including some new faces: Deputy Commissioner and Chief Information Officer Thomas Harty, Deputy Commissioner and Sheriff Edgar Domenech, Assistant Commissioner for Tax and Parking Program Operations Sara Meyers, Senior Budget Director Jackie James, Director of Policy Sarah Knapp, and Director of Internal Audit Celia Carino. Chief Investment Advisor Ranji Nagaswami, who is not here, is also new to our staff.

The Department of Finance has a proposed budget of approximately \$220M for fiscal year 2012. We collect City revenues, enforce the tax laws, register title to and value real property, serve on the board of City pension funds and the deferred compensation plan, provide a forum to contest parking violations and act as chief civil law enforcement officer for New York City.

First I will update the Council on what we are doing to improve and modernize our operations and will also address the tentative assessment roll. Finally, I will talk about some of our key new projects for fiscal year 2012.

I. Improving Agency Operations

As you know, earlier this month, we were directed by the Mayor to conduct the tenth Program to Eliminate the Gap (or PEG) exercise under his watch. At Finance, this calls for a 4% or \$10 million expense reduction. This PEG is one more factor we must account for as we remake the agency.

Over the past 18 months, we have begun the transformation from an organization reliant on paper and files to one that leverages better analytics, data mining and technology. This effort involves changing the skill sets we need from our employees. As many on this Committee know, we have reduced our headcount through attrition and layoffs. Our focus has been on reducing our support and administrative staff and increasing staff in revenue-raising positions while adding some key managers.

Most recently, I approved a reduction of 129 positions. There can be no understatement of the pain and disruption that layoffs bring to the affected employees and also to staff who remain. This past December, the Committee heard from some of the employees in the Office Machine Aide title who are in the City's 55-A program for employees with disabilities. The City Council and Administration agreed on a restoration of \$800,000 in funding that allowed us to keep employees in this title on the agency payroll from January through May 6.

When I started as Finance Commissioner in September 2009, the Agency had 1,960 employees. Without factoring in the current PEG, we expect to reduce our headcount to 1,800 employees; a reduction of over 8 percent of our staff, and \$11 million of our budget since FY 2010. We are

eliminating about 360 positions, and hiring about 200 staffers with different skill sets. We are hiring a planned 90 people in new revenue-raising positions as auditors, statisticians, modelers and others. In addition, we are hiring a planned 45 people to replace costly outside consultants, almost entirely in the IT field. We will also have added approximately 50 newly created positions to work with data, upgrade the sophistication of our analysis of pension investments and reform our operations and will continue to backfill in some key slots as people retire or move on.

With this newly assembled staff and reformed analytical approach, we will raise at least \$60 million more in revenue than the City would otherwise have collected. The revenue potential from more effective modeling and data-mining strategies in audit selection is significant. Let me give you two examples.

- First, we have created more than one hundred models designed to detect statistical anomalies or inconsistencies in how information is reported on tax returns. One recent model found situations where high-income individuals had not filed Unincorporated Business Tax returns for their self-employment income. When notified, most of those owing UBT came forward to resolve their tax situation within three months, generating more than \$1.2 million for the City. Other cases from this match are being pursued.
- Second, about one-third of our audit cases used to end with findings of no taxes due. These audits were arguably a waste of time for both the Agency and the taxpayer. Now, we are selecting cases with a higher probability of yielding additional assessments, and in

the current fiscal year, the percentage of cases closed with no additional tax due has declined to 23%.

We have also improved customer service in critical areas. For instance, we took over administration of the Senior Citizen Rent Increase Exemption (SCRIE) program in 2009. As you know from the complaints many of you received and from my testimony last year, our processing of SCRIE applications was, to put it generously, subpar. However, Assistant Commissioner Meyers and her staff have worked diligently to turn this around. We now respond to new or renewal applications in about 25 days compared to four months a year ago. In addition, working with staff from the Council, we have revamped the SCRIE application and separated it from the Disability Rent Increase Exemption or "DRIE" application. There is still improvement to be made, particularly in the checking and auditing of eligibility. Our current focus, however, is on processing SCRIE applications as quickly as possible, rather than on the relatively low probability of significant fraud.

Another example is our complete renovation of the unit responsible for collecting Payments in Lieu of Taxes, or PILOTs. Our internal audit team identified inaccuracies in our billing of PILOTs. Ultimately, we went through approximately 300 agreements and have already recovered \$12.5 million of the \$13.5 million shortfall we discovered. The balance is being disputed, and we are working to collect the remainder.

Criminal tax enforcement is a critical focus and we are looking to upgrade our strategies and organization. Last month, we merged our Office of Tax Enforcement with the Sheriff's Office. One of the many reasons I asked the Mayor to appoint Sheriff Domenech was because of his more than

25 years of experience in law enforcement. As the former Deputy Director of the U.S. Bureau of Alcohol, Tobacco, Firearms and Explosives, he will help us develop more large- scale multijurisdictional sales, excise, cigarette and business tax investigations with our City, State, and federal law enforcement partners.

The City's pension and deferred compensation plans have total assets of about \$115 billion, and their cost has risen dramatically. Over the past nine years, the City's annual contributions have risen from \$1.5 billion to over \$8 billion in fiscal year 2012. Last summer, Mayor Bloomberg created the Office of Pensions and Investments within the Department of Finance to safeguard plan assets and maximize returns at acceptable risk tolerances. His first appointment was Ranji Nagaswami as Chief Investment Advisor. Ranji has been in the investment profession for more than 23 years. Since her appointment in August 2010, she has provided valuable advice to the Mayoral trustees on all investment matters. She also works closely with Larry Schloss, the very able head of the Comptroller's Bureau of Asset Management and his staff, on investment decisions, risk management, and asset allocation.

Our Payment and Collections staff have also been reorganized to better carry out our mission. In regard to collections, we appreciate greatly the recent passage of the lien sale reauthorization by the Council. This is a critical enforcement tool in securing payment from the small minority of New Yorkers who fail to pay their taxes or other charges.

We are now doing more work at a higher level with fewer resources, which requires both creativity and tremendous management skill. I give

credit to the entire agency and the senior managers sitting behind me today for being open to change and doing that work day-in and day-out.

II. Tentative Assessment Roll

Before I move to the Tentative Assessment Roll, let me make a few general comments about property taxes and valuations.

First, as I have said in every meeting with property owners, community groups and elected officials, when we value property we are not considering fiscal impact. We are endeavoring to do valuations in the most professional and accurate way possible.

Second, the administration of property taxation is anything but simple. The laws that define the tax, mandate valuation methods, define classes and class shares, etc. are the product of years of political compromise that have left a convoluted system that creates substantial and significant inequities.

Third, Finance administers myriad property tax exemptions and abatements by which the City foregoes approximately \$4 billion in annual revenue. In addition to the many personal exemptions such as STAR and veterans' exemptions, and the 421-a and J-51 programs, the City grants PILOT and Shelter Rent agreements which account for millions of dollars in foregone revenue. There are also unique arrangements, some of which were negotiated decades ago. For instance, the Grand Hyatt Hotel, the Chrysler Building and Madison Square Garden are wholly or partially exempt from property tax. This is not to comment on the appropriateness of any particular exemption granted by a long-forgotten Board of Estimate resolution or by state law. Rather, these exemptions are among a

smorgasbord of political, legal and administrative decisions that have left us with a system that is inefficient to manage and simply cannot be optimal.

Finally, all that said, it is the Department's job to work within the laws as they currently exist and that is what we strive to do each year.

I will now turn to the tentative assessment roll that was published on January 14 and will be finalized on May 25. First let me thank the entire staff of the Property Division and many other Finance employees for their extraordinary efforts in producing the tentative roll. Each year, we value over 1 million properties worth more than \$1 trillion. Most of the work has to be completed in the short time from September through December.

Overall, our tentative roll showed market values for Class 1 homes, which are based on comparable sales, rose 0.86 percent citywide compared to a 2.82 percent decline last year. Assessed values increased 2.65 percent. Overall market values for Class 2 cooperatives, condominiums and apartment buildings rose 4 percent, while assessed values for this class increased 8 percent. These properties are valued based on income and expenses as are Class 4 commercial properties which saw a market value increase of 9.95 percent, while assessed values increased 7.34 percent.

This roll reflects some significant changes in how we assess properties, especially those in Class 2. In particular, we returned to the methodology for valuing larger Class 2 properties that had historically been used by Finance and is universally recognized as the textbook valuation methodology: income capitalization. Three years ago, we switched to the Gross Income Multiplier method, with a goal towards making our valuations more understandable. However, that system proved less accurate because it

compressed the values assigned to properties with different economic profiles, and it did not achieve our goal of being simpler to understand.

This was also the first year we produced the roll using the new computerized assessment application, known as CAMA 2, which has been in development since 2007. The application systematized how we select the comparable properties that are used to value co-ops and condos, using factors such as building class, location, size and building age.

We also improved our collection of income and expense data, which is used to create more accurate assessments. With outreach, publicity, and a warning that we would impose the statutory penalty of up to 3 percent of assessed value for failure to file real property income and expense (RPIE) information, we increased RPIE filing compliance from 67 percent to 90 percent. Class 2 compliance rose to 94%.

As a result of these changes, we identified and corrected past problems with values in our system, including under-assessments. Greater accuracy meant that more Class 2 properties than usual had large market value increases on the tentative roll. This issue is particularly acute for Queens co-ops, where the median market value increase was 24%, compared to 7% for co-ops city-wide. Of the 391 large co-op buildings city-wide with market value increases greater than 50%, 251 are in Queens. Co-op boards and State and local elected officials (including members of the Council) reached out to share their concerns about this anomalous situation. I appreciate the outreach and have taken into account the input from you in framing the steps we are taking to address this issue.

First, given that our return to the income capitalization methodology, our use of the new CAMA 2 system and the more comprehensive RPIE data

identified previously under-assessed Class 2 properties that now faced large market value increases, we determined it would be appropriate to limit the single year impact of the most significant Class 2 changes in value.

Therefore, Finance will not raise the market values that we call “equalization increases” on the final assessment roll in Class 2 by more than 50% this year.

Second, we are also reviewing individual assessments in Class 2, focusing first on the Queens co-ops, to ensure that our valuations are accurate. This is primarily a matter of reviewing the comparables used to value the co-ops.

As you know, Finance is not allowed to use sales prices to value co-ops and condos. We think it would be more transparent to value co-ops and condos in a way that the public understands: at their potential sales price, instead of the current state law requirement to value co-ops and condos as if they were rental properties. If we were calculating values based on sales, we would be using a measure that property owners are intimately familiar with and can immediately judge the fairness of. It is time to move to this more comprehensible system. Having said that, it is important to recall that the property tax and assessment system is very complex and there are lots of moving parts. This change will have to be developed carefully to make sure it works as intended.

Also to improve the quality of our assessments, we will propose a local law that will change the filing deadline for the RPIE statements from September 1 to June 1. A new deadline will allow Finance more time to analyze the data before producing the tentative assessment roll. A June

deadline still gives owners plenty of time to file after the close of the calendar year.

You should also know that Finance constantly participates in outreach events and many relate to the assessment roll. Last year we attended over 100 community meetings and other events. We are more than willing to meet with your constituents to explain our assessment process, the lien sale, property tax exemptions, parking issues or any other relevant topic. The meetings we have held this year have been particularly lively.

III. New Agency Initiatives

Finance's consolidated Citywide payments and receivables project, led by Sarah Knapp, is a major step in the modernization of City government. We are creating an electronic payment system that will make it easier for the public to pay the City by offering multiple payment channels that support multiple payment methods. This enhanced payment experience will offer consistency across agencies and leverage our expertise to create a more cost effective centralized system. City agencies that struggle to manage payments will no longer need to develop on-line systems and manage banking relationships. We will also centralize collection and enforcement efforts in Finance. There is no reason why each agency should have to become expert at collection of delinquent debt.

The agency is also working on a plan to upgrade IT systems which are very old. Our new CIO Tom Harty is working with our operating groups to develop a plan to upgrade our real property system, "RPAD" developed in 1983; our parking system "STARS," developed in 1985; and our tax and

accounting system, “Fairtax,” developed in the early 1990s. These important legacy systems are beginning to show their age, and their renovation will be a major focus for the agency in the next few years.

Turning now to one of everyone’s favorite topics – parking tickets. First, in my testimony last year, I promised that we would offer completely on-line hearings with evidence submitted through the web. We have gone live with this application and just demonstrated it at a press conference with the Mayor this morning. A new interface allows people to add digital pictures or other electronic evidence when they submit forms online to contest parking violations. This technology saves time, resources and money for both the City and the person challenging a ticket.

Second, we are about to pilot a change to our scofflaw program. I know I have made clear to you that I want to collect more of the money owed to New York City. If we can collect more money, using an enforcement method that is more efficient and that serves as a public deterrent, that’s a win for everyone. We think that a pilot program using booting instead of towing is worth exploring on all these grounds. Booting is simpler: With modern booting programs, drivers can pay by phone through a credit, debit or prepaid card or in person at a payment center. The driver is given a code and the boot can be removed on the spot. The owner then has to return the boot to one of several locations in the City. We will eliminate the immediate uncertainty of not knowing if the vehicle has been stolen or towed and the difficulty of getting a ride to the tow pound. In addition to being a more convenient enforcement tool, we believe booting will increase collections and the sight of booted cars on the street will serve as a deterrent to scofflaws. We are working closely with the Marshals and

DOI, who oversee the Marshals, to develop a pilot booting program. If it is successful, we will work with them to roll out booting Citywide.

Finally, we have made a number of changes to collect more of the money owed the City for unpaid parking tickets:

- We are working with DMV to suspend the registrations of drivers who get 5 or more tickets in judgment in 12 months using a tool in existing state law;
- We have incorporated the red light violations into our database and are enforcing those judgments through towing and other collection efforts;
- We are trying to make sure that City employees pay their parking tickets. We have asked all departments, agencies and elected officials to encourage employees to pay their fines and sent emails to individual employees. Revival of this 'CityScoff' program collected \$1.1 million or over 40% of what is owed so far this year. For those who do not pay voluntarily, we are once again garnishing employees' salaries.

As a last note, I will talk about two more initiatives of which we are very proud.

This year, we once again mailed tax returns to New Yorkers who we believe are eligible but did not claim the Earned Income Tax Credit, an initiative this Committee has strongly supported in the past. Most of the refund money due these residents comes from the federal government, with a smaller share from the State and an even smaller portion from the City. We sent the New Yorkers pre-populated amended 2007 returns asking that they only add their Social Security number, sign and mail the returns. We included the amount of the credit they are eligible for and supplied envelopes addressed to federal and State tax filing facilities.

If all these amended returns are processed, 7,000 New Yorkers will receive refunds totaling \$5.7 million – for an average refund of over \$800. Working with the Office of Financial Empowerment at the Department of Consumer Affairs, we are very proud once again to lead this effort.

Our City Register, Annette Hill and her team, partnering with the Mayor's Financial Crime Task Force, has led another important initiative. They have implemented a new Deed Fraud and Mortgage Protection program through which owners or other interested parties can receive electronic or mail notification when a document is registered affecting an ownership interest in their real property. Signing up is simple and easy, and we urge you to have your constituents take advantage of this free service.

Finally, I firmly believe that when we collect the taxes, fines and debts owed to the City, we are protecting the vast majority of New Yorkers who pay what they owe from the threat of reduced services or increased taxes.

One additional comment. Every Monday morning I meet with my Deputy Commissioners: our CIO Tom Harty and Sheriff Edgar Domenech whom you met today, and Liz Botwin, Deputy for Administration and Planning, Michael Hyman, Deputy for Tax Policy and Planning, Beth Goldman, Deputy for Legal Affairs and General Counsel and Andrew Salkin, Deputy for Operations. Together this group has almost 110 years of government service. These are people who are not just doing a job. Rather it is a group that has extraordinary passion for the City and its people. As we sit and talk on Mondays and in the hundreds of conversations, meetings and debates we have throughout each week, I am always mindful of how fortunate I am to have these wonderfully dedicated people as my colleagues.

They have very hard jobs and I thank them and all the staff at Finance for the dedication, commitment and professionalism they bring to their job each day.

With that, I thank you, and will be happy to answer your questions.