

9/11: Three Years Later

Securing the Federal Pledge



William C. Thompson, Jr.
Comptroller
City of New York

August 2004

WILLIAM C. THOMPSON, JR.
Comptroller

Deputy Comptroller / Chief of Staff
Gayle M. Horwitz

First Deputy Comptroller
Adam M. Blumenthal

Deputy Comptroller for Policy, Audit,
Contracts and Accountancy
Greg Brooks

Deputy Comptroller for External Relations
Eduardo Castell

Budget Chief
Eng-Kai Tan

Chief Economist
John Tepper Marlin

Project Coordinator
Manny Kwan

Bureau Chief
Tina Lubin

Assistant Director
Robert DeLaurentis

Staff

Kettly Bastien
Amitabha Basu
Millicent Budhai
Rosa Charles
Basil Duncan
Peter E. Flynn
Michele Griffin
Debbie Gutierrez
Michael Hecht

Farid Heydarpour
Dahong Huang
David Katz
Hope Lenzian
Irina Livshits
Marcia Murphy
Andrew Rosenthal
Michael Zhang
Marie Walsh

We acknowledge the contribution of Andrew M. Joseph the former Deputy Comptroller for Budget to this report.

TABLE OF CONTENTS

EXECUTIVE SUMMARY	i
I. STATUS OF FEDERAL DISASTER RELIEF ASSISTANCE TO NEW YORK CITY.....	1
A. FEMA ASSISTANCE.....	3
B. COMMUNITY DEVELOPMENT BLOCK GRANTS	4
1. Empire State Development Corporation	5
2. Lower Manhattan Development Corporation	6
C. THE LIBERTY ZONE ECONOMIC STIMULUS PACKAGE.....	7
1. The Liberty Zone Tax Incentive Package	7
2. Tax-Exempt Bonds	9
D. TRANSPORTATION AND OTHER FEDERAL FUNDING	11
1. Transportation.....	11
2. Other Federal Assistance	12
II. RECOMMENDATIONS.....	13
A. LMDC FUNDING	13
B. LIBERTY ZONE TAX INCENTIVES	13
C. LIBERTY BONDS.....	13
D. TRANSPORTATION INFRASTRUCTURE	14
E. OTHER FEDERAL FUNDING.....	14
III. CONCLUSION	15
APPENDIX — THE CONTINUING IMPACT OF 9/11 ON THE NEW YORK CITY ECONOMY	16
A. LOST JOBS.....	16
B. LOST NYC GROSS PRODUCT	17
GLOSSARY OF ACRONYMS.....	19

LIST OF TABLES

TABLE 1. FEDERAL DISASTER RELIEF ASSISTANCE TO NEW YORK CITY	2
TABLE 2. COMPONENTS OF FEMA ASSISTANCE	3
TABLE 3. ESDC ACTION PLANS	5
TABLE 4. LMDC PARTIAL ACTION PLANS	6
TABLE 5. PROGRESS OF LIBERTY BOND PROGRAM	9

LIST OF CHARTS

<i>CHART 1.</i> NYC LAGS BEHIND U.S. YEAR-OVER-YEAR MONTHLY PERCENT CHANGES IN JOBS, FIRST QUARTER 2000/SECOND QUARTER 2004.....	17
<i>CHART 2.</i> ACTUAL REAL GCP (NYC COMPTROLLER'S SERIES) AND ESTIMATED GCP IF NYC HAD GROWN AT THE SAME RATE AS THE NATION AFTER 9/11	18

Executive Summary

In the three years since the September 11, 2001 attack on the World Trade Center, New York City has received \$11.3 billion in federal aid to assist with clean-up, recovery and rebuilding efforts. This represents slightly more than half of the aid package that President George W. Bush pledged following the disaster. The President initially made a \$21.4 billion commitment, a figure that was subsequently reduced to \$20.8 billion as a result of program adjustments.

Some of the unreleased aid -- \$4.2 billion -- is expected to reach the City in the coming months and years. A greater portion of the aid, however -- \$5.2 billion, representing a quarter of the total aid package -- is in jeopardy.

An estimated \$4 billion may not reach the City due to longstanding programmatic delays and the federal government's failure to monitor the progress of large components of the aid package. This includes \$870 million in unprogrammed Community Development Block Grant (CDBG) funding, \$2.37 billion in unrealized tax benefits from the Liberty Zone program, and \$797 million in undocumented miscellaneous federal support. Even if immediate action is taken with regard to that portion of the aid, the City would still face a projected shortfall of \$1.2 billion, representing more than 5 percent of the President's \$20.8 billion pledge.

The first section of this report provides an update on the level of assistance that New York City has received, the allocations that are in place, and the aid that may not be realized. The second section offers recommendations to secure the funding and further improve the flow of aid to the City. The Appendix provides data on the ongoing impact of the September 11th attack on the City's economy.

Most of the aid that the City has received to date has been through the Federal Emergency Management Agency (FEMA), which has now released a total of \$7.8 billion. FEMA is expected to provide an additional \$1 billion for debris removal insurance. An additional \$2.3 billion, from sources other than FEMA, representing the full allocation for transportation funding, is expected to reach the City consistent with the long-term nature of most of the planned projects.

Another \$2.5 billion has reached the City through the Community Development Block Grant program, administered in part by the Lower Manhattan Development Corporation (LMDC). A 2003 report on the federal aid package prepared by this office noted that LMDC had not developed action plans for \$1.2 billion in CDBG funding. One year later, LMDC has approved only \$280 million of additional projects, leaving \$870 million in unused funding.

Gauging the success of the Liberty Zone package has been more problematic; despite the recommendations of this office and the urgings of many public officials, the Federal government has not provided any mechanism to track the benefits of this program.

Available data and anecdotal evidence strongly suggest, however, that the Liberty Zone program has not resulted in benefits to the City at the level expected at the time of the program's inception. Tax law changes regarding depreciation benefits and weak economic conditions in the downtown area appear to have greatly limited the ability of local businesses to take advantage of the program's tax credits and accelerated depreciation provisions.

The Liberty Bond portion of the program also has fallen short of expectations. The program encountered delays in bond issuance in its first three years. The original deadline for developers to issue bonds – December 31, 2004 – posed additional problems.

The 2003 report prepared by this office called for any unused benefits associated with the tax-benefit portion of the Liberty Zone program to be reprogrammed and for the Liberty Bond deadline to be reconsidered. In a recent development, the President has proposed a “swap” of \$2 billion in Liberty Zone tax incentives for a corresponding amount in tax incentives associated with transportation initiatives. This change, if adopted by Congress and fully utilized, would alleviate a significant portion of the potential shortfall in the Liberty Zone program.

Legislation also has been introduced to extend the Liberty Bond issuance deadline to December 31, 2009. Bills have been approved in the House and the Senate, and are now in conference committee. If legislation is enacted, the deadline extension will go a long way toward enabling commercial developers to take advantage of the remaining bonding authority in the program.

These are welcome developments. It is critically important, however, that in the process of readjusting the components of the aid package, the City is not deprived of the promised aid. Appropriate measures must be taken to ensure that the City receives the full aid package.

This report makes the following recommendations:

- The LMDC must act swiftly to develop action plans for all undesignated funds.
- Federal aid substituted for unused tax incentive Liberty Zone benefits should fully compensate the City for the unused portions of the allocation (\$2.9 billion), rather than just the \$2 billion currently proposed in the “swap.” Any proposed use of the funding must be subject to careful analysis to ensure that the funds are allocated to the project that will provide the greatest possible benefits to Lower Manhattan and to New York City as a whole.
- The Federal government must address the Liberty Bond program's projected shortfall of \$352 million, which results from slow issuance of bonds.
- The Federal government should establish a mechanism for tracking the benefits of the Liberty Zone initiative and all programmatic funding.

The federal aid that has reached the City to date has been essential in helping New York City recover and rebuild. It is vitally important, therefore, that the Federal government adhere to its commitment and that all government entities work together to ensure that the entire aid package of \$20.8 billion is realized.

Summary of Federal Aid

(\$ in millions)

Program	Current Commitments	Funding Released	Funding Expected	Funding in Question	Estimated Shortfall
FEMA Assistance	\$8,798	\$7,798	\$1,000	\$0	\$0
Community Development Block Grants	3,483	2,497	117	870	0
Liberty Zone Program	5,029	385	1,057	2,371	1,216
Transportation Projects	2,347	282	2,065	0	0
Other Federal Funding	1,159	362	0	797	0
Total	\$20,816	\$11,324	\$4,239	\$4,038	\$1,216

I. Status of Federal Disaster Relief Assistance to New York City

After the destruction of the World Trade Center (WTC), President Bush pledged \$21.4 billion in federal support to New York City to assist with the costs of clean-up, recovery and rebuilding efforts. The funding was to provide reimbursement for emergency costs, housing and business assistance, transportation infrastructure, and a range of tax incentives for a newly defined area known as the Liberty Zone in Lower Manhattan. The plan for the federal assistance is divided into four distinct elements: Federal Emergency Management Agency (FEMA) assistance, Community Development Block Grants (CDBG), the Liberty Zone Economic Stimulus package and all other federal support, primarily for transportation projects. The President's commitment was subsequently reduced to \$20.8 billion in September 2002, as a result of program adjustments.

In its May 2004 estimate, the Federal government still maintains it will provide New York City with \$20.8 billion for recovery and rebuilding efforts. The major components of the program have remained the same: FEMA assistance designated mainly for the initial response and recovery efforts totals \$8.8 billion.¹ The Federal government continues to project that the Liberty Zone package, which includes tax incentives and tax-exempt financing, will provide \$5 billion in benefits mostly intended for businesses in the downtown Manhattan area. However, there is now a new proposal from the President regarding the substitution of \$2 billion in additional transportation initiatives for some of the Liberty Zone benefits that have been difficult to document and that may have gone largely unused. The package also contains CDBG funding of \$3.5 billion. These funds are earmarked for rebuilding public and private infrastructure as well as temporary housing assistance through the use of the Lower Manhattan Development Corporation (LMDC) and the Empire State Development Corporation (ESDC). Finally, the federal package contains \$2.3 billion for the upgrade and integration of transportation systems in the downtown area and an additional \$1.2 billion for a range of programs in a number of different Federal agencies. A complete breakdown of the \$20.8 billion in federal commitments for 9/11 programs is shown in Table 1.²

¹ \$2.75 billion of the \$8.8 billion in FEMA assistance is dedicated towards intermodal transit projects.

² Released funds are defined throughout this report as funding that has already been distributed or has been approved and earmarked for distribution in the near future. In the case of tax benefits, the report refers to estimated benefits. Funds that have been committed, but the flow of which is either undetermined or projected to take place at an unspecified time in the future, are classified as "expected" or "in question" depending on the level of documentation available regarding their potential release.

Table 1. Federal Disaster Relief Assistance to New York City

(\$ in millions)

Program	Current Commitments^a	Funding Released	Funding Expected	Funding in Question	Estimated Shortfall
FEMA-Emergency Response and Recovery	\$5,048	\$5,048	\$0	\$0	\$0
Intermodal Transit	2,750	2,750	0	0	0
Debris Removal Insurance	1,000	0	1,000	0	0
Community Development Block Grants	3,483	2,497	117	870	0
Liberty Zone ^b -Tax Credits / Depreciation	2,864	0	0	2,000	864
Tax Exempt Bonds	2,165	385	1,057	371	352
Transportation Projects	2,347	282	2,065	0	0
Other Federal Funding ^c	1,159	362	0	797	0
Total	\$20,816	\$11,324	\$4,239	\$4,038	\$1,216

^a "Status of the President's \$20 Billion Commitment to New York City", The White House, May 2004.

^b As discussed later in this section, the Federal government has been unable to document the use of the tax credit and accelerated depreciation provisions in the Liberty Zone package, despite the recommendations of this office and other public officials to establish a mechanism to track these benefits. Given the weakness in the City's economy since the adoption of the program, it is likely that the benefits realized from these initiatives are nominal. The Comptroller's Office has therefore reduced the overall estimated savings realized from the Liberty Zone package to \$385 million, from \$450 million in our previous report, with the benefits now accounted entirely in tax-exempt bond savings.

^c The Federal government has indicated that these funds have been fully obligated through authorized agencies. However, there is no documentation on what portion of this total has been spent. Our tracking of these funds indicates that at least \$362 million has been released thus far.

Currently, slightly more than half, or \$11.3 billion of the federal commitments for 9/11, has been released. FEMA assistance of \$7.8 billion makes up the majority of the released funds, with the remainder primarily attributable to \$2.5 billion in CDBG funding for LMDC and ESDC. The \$1 billion in FEMA assistance for debris removal insurance is expected in the near future. An additional \$4.2 billion is anticipated to be released or irrevocably committed in the near future, including \$1.1 billion in tax savings resulting from issuance of Liberty Bond and municipal bond refunding savings, and \$2.1 billion in transportation funding.

At this time, however, about \$5.2 billion of the federal package represents funding that has not materialized, with \$4 billion still in question and \$1.2 billion as a clear shortfall.

The majority of this uncertain funding is attributable to components of the Liberty Zone program. Due to weak economic conditions in the downtown area and tax law changes, it is unclear what portion, if any, of the \$2.9 billion in Liberty Zone tax credits and accelerated depreciation provisions has been utilized since the inception of the program. In acknowledgement of the potential shortfall in these projections, the President has recently proposed the conversion of \$2 billion of the estimated benefits into federal funding support for transportation projects through as yet unspecified mechanisms. While the President's proposal is a major step in the right direction, a balance of \$864 million remains associated with tax benefits that are unlikely to be used. Furthermore, about \$371 million in tax-exempt bond savings may fail to materialize unless the issuance deadline for Liberty Bonds is extended. Legislation to extend this deadline to December 31, 2009 has been endorsed by the President and passed both houses of Congress, where it is in conference. In addition, the delay in the issuance of Liberty Bonds has already created a risk of \$352 million to the federal estimates. Therefore, in order for the President to fulfill the promised aid of \$20.8 billion to help

New York recover from the attack, the Federal government must take immediate action to address potential shortfalls in the Liberty Zone package

An estimated \$870 million in CDBG funds under the charge of LMDC have not yet been allocated to specific programs. Our previous report identified about \$1.15 billion of LMDC funding unassigned for specific uses. Thus the Corporation has made scant progress in developing additional action plans over the past year.

Finally, with respect to the other federal funding totaling \$1.2 billion a projected balance of \$797 million still remains. There is a clear need for the Federal government to provide better tracking mechanisms for the flow of these funds and to enact programs for any unspent funds. Although the Federal government has indicated that the entire sum has already been set aside (obligated) through the responsible agencies, the ability to trace the flow of these funds has been limited, because the Federal government has failed to provide documentation on these funding sources. Our data indicates that approximately \$362 million has been released.

A. FEMA ASSISTANCE

Under the federal pledge, a total of \$8.8 billion has been allocated through FEMA. To date, FEMA has distributed funds to government agencies, authorities, and organizations which oversee programs as shown in Table 2.

Table 2. Components of FEMA Assistance

(\$ in millions)

FEMA Assistance	
Debris Removal and Public Agency Assistance	\$2,486
Hazard Mitigation	426
New Jersey Emergency Declaration	87
Federal Mission Assignments and Other Administrative Costs	425
Pension Funding for Survivors of Police & Firefighter Officers	260
Expanded Health Monitoring for Workers at the WTC Site	90
Estimate of Additional Reimbursements to NYS and NYC	775
Sub total for Recovery, Response, and Other	\$4,549
Transportation Infrastructure	2,750
Human Services and Crisis Counseling	499
Debris Removal Insurance	1,000
Total	\$8,798

FEMA earmarked \$1 billion as an insurance fund to resolve health-related claims filed by workers who participated in the cleanup of the WTC site. A recent agreement between City and Federal officials would allow claims, including those arising from work performed between September 11, 2001 and September 29, 2001 during the recovery process, to be filed against the \$1 billion insurance liability fund. Pursuant to Federal and State legislation, the City of New York recently created a not-for-profit corporation known as the WTC Captive Insurance Company, Inc. (the “Captive”), which it anticipates will be licensed as a captive insurance company by the New York State

Insurance Department.³ The Captive will provide insurance coverage to the City, its contractors and subcontractors for liability claims arising from the clean-up of debris resulting from the destruction of the World Trade Center. It is expected that the City will fund the Captive with a grant of up to \$1 billion from FEMA.

Approximately \$4.5 billion out of the \$7.8 billion obligated or distributed by FEMA represents reimbursement of costs resulting from the World Trade Center attacks. The reimbursements include recovery and response expenses, personnel costs, vehicle and hardware replacements, and a wide range of other expenditures, such as pension funding for survivors of uniformed officers, health monitoring, and hazard mitigation. FEMA reimbursement for these expenditures has provided a revenue source of approximately \$2.5 billion to the City's budget over the past three years. In FY 2002 and FY 2003, the City's cash receipts reflected FEMA assistance of roughly \$780 million each year. During FY 2004, the City received \$960 million mainly as a result of the Federal government's decision to expand the scope of 9/11-related activities that are eligible for FEMA support.

FEMA has also transferred to transportation authorities \$2.75 billion to address transportation needs in Lower Manhattan. These funds are being used towards the construction of the new transportation hub at the World Trade Center site, the Fulton Street Transit Center, and the rebuilding of the South Ferry Terminal.⁴ The remaining funds of approximately \$499 million have provided assistance to individuals affected by the disaster. The major programs within this group include Mortgage and Rental Assistance (MRA), Individual and Family Grants (IFG) and Crisis Counseling. The latest estimates indicate that at least \$119 million has been distributed under MRA and IFG. In addition, FEMA has obligated \$155 million to the Project Liberty crisis counseling program, including \$33 million to counsel schoolchildren. The program was extended three times in the past because the benefits were not fully utilized. The program will expire on December 31, 2004.

B. COMMUNITY DEVELOPMENT BLOCK GRANTS

The Federal government has appropriated \$3.5 billion in CDBG funds through the Department of Housing and Urban Development (HUD) to fund the rebuilding and revitalization of Lower Manhattan. The projects, which are overseen by ESDC and LMDC, focus on infrastructure improvements, initiatives to attract and retain business throughout the area, and cultural and community developments. ESDC currently administers \$1.1 billion of this total, while LMDC is responsible for the allocation of the remaining \$2.4 billion in CDBG funds.

³ A "captive insurance company" means a company created to insure the risks of its owners who are not in the business of insurance.

⁴ See "Transportation" beginning on page 11 for a more detailed discussion of the transportation projects for Lower Manhattan.

Thus far, ESDC and LMDC have developed action plans and programs for \$2.6 billion of the \$3.5 billion allocated. Action plans are still needed for approximately \$870 million. The approved programs include \$750 million for the restoration and rebuilding of utility infrastructure and \$475 million for job creation and retention for both large and small firms. Another \$562 million has been allocated to reimburse small firms for economic losses and \$281 million in assistance has been approved for Lower Manhattan residents.

1. Empire State Development Corporation

ESDC's current allocation of \$1.1 billion reflects an increase of \$425 million from its original level of funding. The infusion of additional funds was reassigned from LMDC, because of overwhelming demand for the World Trade Center Business Recovery Grants (BRG) and the Small Firm Attraction and Retention Grants (SFARG), as well as the Job Creation and Retention Program (JCRP). As of March 2004, ESDC has approved and obligated \$944 million in financial assistance to businesses as shown in Table 3. The remaining \$181 million in funding will materialize mainly in the SFARG and JCRP programs.

Table 3. ESDC Action Plans

(\$ in millions)

	Program Commitments	Funds Released	Funds To Be Released
<u>Small Business Assistance</u>			
Business Recovery Grant (BRG)	\$562	\$546	\$16
Small Firm Attraction and Retention Grant (SFARG)	155	87	68
Recovery Loan Fund	41	31	10
Bridge Loan Program	7	6	1
Technical Assistance	5	5	0
Subtotal	<u>\$770</u>	<u>\$675</u>	<u>\$95</u>
<u>Large Business Assistance</u>			
Job Creation and Retention Program (JCRP)	\$320	\$249	\$71
Compensation for Economic Loss	16	16	0
Subtotal	<u>\$336</u>	<u>\$265</u>	<u>\$71</u>
Business Information Administration	\$5	\$4	\$1
	14	0	14
Total	\$1,125	\$944	\$181

Source: Empire State Development Corporation and Lower Manhattan Development Corporation.

The ESDC's approved funding includes \$675 million that has been released or obligated under small business assistance programs. The largest component of this group is the BRG program, which provides compensation to small businesses in Lower Manhattan that suffered losses as a result of the WTC attacks. Through March 2004, \$546 million has been distributed under this program.⁵ These funds have assisted close to 15,000 businesses. An additional \$87 million has been approved under the SFARG

⁵ \$546 million is the sum of regular BRG grants totaling \$539 million, plus reimbursement to date of \$7 million for Retail Recovery Grants paid to small businesses in November and December of 2001.

program that will provide benefits to about 1,400 businesses in the downtown area. The remaining \$42 million is comprised of low-cost financing to businesses through the Recovery Loan Fund, the Bridge Loan Program and grants for technical assistance.

ESDC has distributed \$265 million to companies with at least 200 employees. About \$249 million of this assistance is in the form of grants, low-cost financing for working capital, and loan guarantees through the JCRP program. Firms receiving JCRP assistance are required to remain in New York City for at least seven years. Funding of \$16 million has also been provided to compensate 94 companies that employ more than 500 people nationwide and suffered economic losses in the disaster.

2. Lower Manhattan Development Corporation

LMDC has developed partial action plans for \$1.5 billion of the \$2.4 billion that the corporation oversees, as shown in Table 4, of which all but \$117 million have been approved by HUD. Programs have not been developed for the remaining \$870 million. The largest component of the programs funded by LMDC is \$750 million for rebuilding utility infrastructure in Lower Manhattan. Approximately \$485 million of these funds will be used for the replacement and enhancement of utility equipment and infrastructure. Another \$250 million was earmarked for the reimbursement of costs associated with the stabilization of critical energy and communications services. The remaining \$15 million will be used for administrative purposes.

Table 4. LMDC Partial Action Plans

(\$ in millions)

	Current Action Plan	Obligated Funds
Programs Approved by HUD		
Utility Restoration and Infrastructure Rebuilding	\$750.0	\$250.0
Residential Grant Program (RGP)	281.0	242.0
WTC Memorial and Tourism	176.0	0.0
Short Term Capital Projects	69.0	56.7
Disproportionate Loss of Workforce	33.0	33.0
Employment Training (ETAP)	0.5	0.2
Cultural, Planning, and Administration	62.0	55.9
Subtotal	\$1,371.5	\$637.8
Other		
New Action Plans	\$116.8	\$0.0
Unallocated Funds	869.5	0.0
Total	\$2,357.8	\$637.8

Note: Current total excludes \$425 million transferred to ESDC for the BRG Program.

Source: Lower Manhattan Development Corporation Partial Action Plans and Quarterly Performance Report, August 2004.

Of the \$1.4 billion in approved action plans by LMDC, as of June 2004, \$637.8 million has been obligated. Approximately \$250 million of this amount is related to infrastructure rebuilding and utility restoration. Through June 2004, LMDC has set aside \$242 million towards the Residential Grant Program (RGP), which includes approved grants of \$226 million for 39,451 applicants. The RGP has also achieved significant success in attracting new residents to Lower Manhattan. Approximately 53 percent of the

applications approved were Zone 1 applicants who identified themselves as new residents.⁶

Among the other programs, \$56 million has been set aside for cultural programming and planning and \$33 million for companies that suffered a disproportionate loss of workforce. Approximately \$250 million has been set aside for utility infrastructure initiatives, representing one-third of the \$750 million committed to this area. An additional \$57 million has been obligated for various short-term capital projects.

C. THE LIBERTY ZONE ECONOMIC STIMULUS PACKAGE

The New York Liberty Zone Program, originally authorized in March 2002, consists primarily of a package of tax benefits to New York City businesses.⁷ It also includes a granting of authority to the City and the State for the issuance of tax-exempt bonds. The Federal government projected that the package would provide tax benefits totaling \$5 billion over an eleven-year period, beginning in 2002. A breakdown of the Liberty Zone package is shown in the figure above.

Components of the Liberty Zone Economic Package (\$ in millions)	
Tax Credits	\$ 631
Accelerated Depreciation	2,200
Liberty Bonds	1,228
Advanced Refunding	937
Net Other	33
Total	\$5,029

Measuring the benefits and gauging the success of the Liberty Zone package remains difficult. Despite the recommendations of the Comptroller’s Office and the urgings of various public officials, the Federal government has not provided any mechanism to track the benefits. In May, the White House released an update on the status of the President’s \$20.8 billion commitment to New York. This update indicated that \$1.9 billion of the Liberty Zone package has been set aside to date, but failed to provide any documentation in support of this figure. However, the economic conditions of the City, which had been weaker than expected at the time the package was adopted, suggest that very little of the \$1.9 billion in benefits has materialized.

1. The Liberty Zone Tax Incentive Package

The major elements of the tax incentive package are tax credits and accelerated depreciation. The tax incentive package was expected to provide \$2.9 billion in tax

⁶ Zone 1 is defined as the area south of Chambers Street and west of Nassau and Broad Streets and the entirety of Battery Park City.

⁷ The New York Liberty Zone is defined as the area located on or south of Canal Street, East Broadway (east of its intersection with Canal Street), or Grand Street (east of its intersection with East Broadway) in the Borough of Manhattan in the City of New York, New York (“Title II. Tax Benefits for Area of New York City Damaged in Terrorist Attacks on September 11, 2001,” *General Explanation of Tax Legislation Enacted in the 107th Congress*, Joint Committee on Taxation, 235; January 24, 2003).

savings over the 11-year period from 2002-2012. Under the tax credits portion of the package, small businesses inside the Liberty Zone with a staff of 200 or fewer employees are eligible to receive a credit of \$2,400 per worker. The provision also covers eligible businesses that were forced to move out of the Zone due to the attack. These credits, if realized, would result in foregone federal tax revenue of \$631 million between 2002 and 2007. In addition, the package allows accelerated depreciation of various properties, including personal, residential and non-residential real estate properties, and leasehold improvements. The accelerated depreciation would further reduce federal tax revenues by \$2.2 billion over the term of the Liberty Zone package.

The Comptroller's Office believes that there has been extremely limited use of these programs, for a number of reasons:

- As documented in our previous report, portions of the accelerated depreciation benefits were superseded by changes in the tax law. The Jobs and Growth Tax Relief Reconciliation Act of 2003 increased the first year bonus depreciation available to all companies to 50 percent for the 2003 and 2004 tax years, compared with only 30 percent under the Liberty Zone package, thus rendering unattractive, a significant portion of the depreciation benefits specific to the Liberty Zone.
- Local business groups have reported extremely light utilization of the tax credit provision. A study by the Alliance for Downtown New York showed that only 8.4 percent of retailers and 13.7 percent of commercial establishments applied for this credit.
- The major components of the package, such as tax credits and accelerated depreciation, require that firms be profitable before economic benefits are provided to companies. The Pace Downtown Index (PDI), which tracks economic and business progress in Lower Manhattan, was at about 112 in early 2001, fell to 103 before 9/11 and to 94 after 9/11. The PDI continued to decline until early 2003, to 92, and has since risen to 93. This suggests that whatever business assistance was utilized, it was not sufficient to bring about a significant recovery in the downtown economy.

Because the Federal government has not provided any documentation suggesting that these benefits have been used and because anecdotal and economic indicators suggest limited impact, the Comptroller's Office believes that benefits realized under the depreciation and tax credit components of the Liberty Zone package are not material.

In a recent development, the President has proposed swapping \$2 billion of the Liberty Zone tax incentives for a corresponding amount in transportation initiatives. The proposal results from months of negotiations among the Governor Pataki, Mayor Bloomberg and the Federal government and appears to be a clear recognition of the underutilization of these incentives. This change, if adopted by Congress, will alleviate a significant portion of the potential shortfall in the Liberty Zone program. However, because the full tax incentive benefit package was intended to be \$2.9 billion, the

Comptroller's Office believes a risk of \$864 million still remains for these provisions of the federal aid package.

2. Tax-Exempt Bonds

Since the inception of the \$8 billion Liberty Bond program, approximately \$5.45 billion of applications have been approved, and \$938 million of Liberty Bonds have been issued, as shown in Table 5.⁸ Among the recommendations in our previous analysis was extending the issuance deadline for Liberty Bonds to allow developers a further opportunity to take advantage of the program. Legislation, which was endorsed by the President, passed both the Senate and the House of Representatives and is in conference, extends the deadline to issue Liberty Bond financing to December 31, 2009, a five-year extension from the current deadline of December 31, 2004.⁹

Table 5. Progress of Liberty Bond Program

(\$ in millions)

<u>Description</u>	<u>Maximum Amount</u>	<u>Induced Applications^a</u>	<u>Liberty Bonds Issued</u>	<u>(Over) / Under-Subscribed</u>
Commercial:				
Inside Liberty Zone	\$4,400	\$1,734	\$0	\$2,666
Outside Liberty Zone ^b	2,000	1,244	114	756
Residential:				
Inside Liberty Zone	\$1,600	\$2,474	\$824	(\$874)
Outside Liberty Zone	0	0	0	0
Adjustment for Over-Subscription		(874)		874
Total	\$8,000	\$4,578	\$938	\$3,422

^a An inducement is an Internal Revenue Service code provision under which developers are allowed to include eligible project costs incurred in the first 60 days of a potential project. The inducement process commits neither the responsible government agency nor the developer pursuing the potential project. The value of approved applications may ultimately be lower than the total amount induced.

^b The \$2 billion designated for commercial projects outside the Liberty Zone are permitted to be re-programmed for projects inside the Liberty Zone.

Approximately \$6.4 billion of the Liberty Bond program is dedicated to commercial projects and \$1.6 billion to residential projects. To date, the program has been very successful in attracting residential projects within the Liberty Zone, the demand for which exceeds its \$1.6 billion allocation by an amount of \$874 million. The commercial component has projects with inducements totaling \$2.98 billion. Only one issue of \$114 million, for the newly opened Atlantic Terminal in Brooklyn, has been made under the commercial program. At this time, there is no indication that the

⁸ The \$5.45 billion of induced applications includes \$2.47 billion of residential applications, exceeding the \$1.6 billion allocation for residential Liberty bonds by \$874 million. This effectively reduces the amount that can be issued under existing guidelines to \$4.58 billion.

⁹ The House version of this legislation is known as the American Jobs Creation Act of 2004. The Senate version of this legislation is known as the Jumpstart Our Business Strength (JOBS) Act.

commercial/residential allocations will be adjusted to accommodate greater residential project demand.¹⁰

To date, there are \$1.734 billion of induced commercial projects within the Liberty Zone and \$1.24 billion outside the zone, or \$3.42 billion below the authorized commercial project amount. A breakdown of the induced commercial projects for Liberty Bonds is illustrated in the figure to the right. Although the commercial allocation represents the entire unused bonding authority, the proposed deadline extension for another five years will allow time for other projects to be developed over the longer term. Further, there have been indications that Liberty Bond financing may be used towards the redevelopment of the 16-acre WTC site, which could consume a significant portion of the remaining bonding capacity for commercial projects.

Induced Commercial Projects for Liberty Bonds	
(\$ in millions)	
Inside Liberty Zone	
Goldman Sachs-Battery Park City	\$1,000
World Trade Center	400
NYU Hospital / Pace University Facility	243
National Sports Museum	52
377 Greenwich Street Hotel / Restaurant	39
Total	\$1,734
Outside Liberty Zone	
Bank of America	\$650
Astoria Energy Power Plant	400
Brooklyn Atlantic Terminal	114
Other	80
Total	\$1,244

The Comptroller's Office estimates that the Liberty Bond program could face a shortfall of up to \$723 million if Congress does not extend the deadline.¹¹ Simply based on the amount of bonds issued to date the expected tax benefits through 2004 will total \$21 million, which is \$121 million less than the \$142 million projected by the Federal government. Over the eleven-year time horizon of the Liberty Zone package, the estimated shortfall resulting from this delay in bond issuance is approximately \$352 million for the program. This projection is based on the assumption that all currently-induced projects will be issued before the deadline.

In addition to Liberty Bonds for development, provisions in the Liberty Zone program allow under certain restrictions, a second advance refunding of up to \$9 billion of municipal bonds issued by the City, the Metropolitan Transportation Authority (MTA), the Municipal Water Authority, and New York City hospitals. It is expected that the full savings of \$937 million will be realized.

¹⁰ Federal legislation was introduced in November 2003 that would increase the allocation for residential development projects from \$1.6 billion to \$3 billion under the Liberty Bond program. However, no further action has been taken by Congress since the bill was introduced.

¹¹ On August 19, 2004 inducement resolutions were passed by the Liberty Development Corporation for \$1 billion for construction of an office tower in Battery Park City by Goldman Sachs and for \$52 million for the construction of a National Sports Museum. Given the potential imminent expiration of the Liberty Bond program on December 31, 2004 we have not assumed the issuance of debt as a result of these recent inducements in our risk assessment. If the bonds are issued before the current deadline the program shortfall would decline to \$579 million from our current estimate of \$723 million.

D. TRANSPORTATION AND OTHER FEDERAL FUNDING

1. Transportation

The Federal Government has committed funding of nearly \$5.1 billion for the upgrade of the existing transportation infrastructure in Lower Manhattan. The funding is comprised of \$2.75 billion of FEMA assistance for transit projects and \$2.3 billion in allocations to the Federal Transportation Administration (FTA) and Federal Highway Administration (FHA). About \$4.6 billion of the \$5.1 billion total is designated for intermodal transit projects, with the balance dedicated to other transportation projects such as street improvements and road re-surfacing in Lower Manhattan. The President has recently proposed replacing \$2 billion in unused tax incentives from the Liberty Zone package with other transportation initiatives through an unspecified mechanism. This development is seen as paving the way for the construction of a direct rail-link from Lower Manhattan to JFK airport.

To date, about \$3 billion in federal funding has been obligated for the permanent PATH station, the Fulton Street transit project, the South Ferry terminal, and miscellaneous street improvements. The construction of a permanent PATH station at the World Trade Center site is estimated to cost approximately \$2.03 billion, consisting of \$1.7 billion in federal transportation funding and a separate source of \$330 million from the Port Authority (PA). This project will be completed in six stages over the next five years and will be overseen by the PA. The Fulton Street Transit Center is estimated to cost \$750 million, with an expected completion timeline of three to four years. The MTA has already begun receiving funding for this project, with construction slated to begin at the end of 2004. The MTA also plans to redesign the South Ferry station to accommodate the full length of a ten-car subway train, in place of the current five-car platform. Additionally, new connections to the Staten Island Ferry and the Whitehall Street station will be built. These projects will cost a projected total of \$400 million. Construction is expected to begin by the end of 2004 with an estimated completion timeframe of three to four years. In addition, there are various street improvement projects totaling at least \$180 million that comprise the balance of the \$3 billion in transportation funding thus far obligated.

The remaining \$2.1 billion in transportation funding is not currently allocated to specific programs, although several proposals have been mentioned. One State transportation proposal that is expected to occur is the Route 9A (West Street) Promenade South project. This project, estimated at a cost of \$50 million, will enhance green space, improve pedestrian movement throughout Battery Park and West Street, and widen and beautify sidewalks. As noted above, another project that is currently being studied is the construction of direct rail access from Lower Manhattan to JFK airport and Long Island. This project, estimated at \$6 billion, would not only link Lower Manhattan to JFK airport, but would also connect the LIRR to lower Manhattan and allow an estimated 100,000 commuters to directly reach Lower Manhattan daily. However, for this rail link to be built, substantial funding must be identified. The President's proposal to redirect funding from the Liberty Zone package to Transportation initiatives, which requires Congressional approval and additional detail, may provide a portion of this

additional funding. Reprogramming of LMDC funding and support from the MTA are also potential sources. Any project would also require additional studies and analyses.

An additional project that has been discussed is the proposed West Street tunnel project, estimated to cost in excess of \$800 million. This proposal has become a controversial issue for numerous reasons including questioned utility and feasibility.

2. Other Federal Assistance

The federal assistance package was also intended to provide \$1.2 billion to New York City for programs such as Small Business Administration (SBA) loans, workers compensation and health-related projects. The Federal government has indicated that the entire \$1.2 billion has been obligated through authorized agencies such as the Health and Human Services, Labor, and Commerce. However, the Federal government has not provided documentation regarding the amounts spent in these areas. Our analysis indicates that approximately \$362 million of the total has been released. Among the highlights of funding released thus far is a federal subsidy of \$135 million in support of over \$500 million in SBA loans to more than 6,000 businesses. Another \$175 million has been released to New York State toward workers compensation claims, including \$25 million for volunteer workers. The balance, or \$797 million, is undocumented.

II. Recommendations

In order to assure that the City receives the full benefit of the Federal 9/11 aid package, the Comptroller's Office offers the following recommendations:

A. LMDC FUNDING

Over the past year, LMDC has made little progress in developing action plans for the remaining balance of its unallocated CDBG funds. In our previous report one year ago, the Corporation's partial action plans contained about \$1.15 billion in funds needing allocation. The latest plans indicate that LMDC still has \$870 million of these funds unprogrammed, representing an increase of about \$280 million in additional approved projects over the course of an entire year. As these funds could provide a vital boost and make an immediate impact on the downtown economy, we believe the LMDC approval process has been inadequate. This slow process raises concerns that the LMDC is not accomplishing its programmatic objectives in a timely manner, which includes redevelopment, infrastructure improvements, and initiatives to attract and retain businesses in the downtown area. Because of their importance and the impact that these funds could have on the local business climate, LMDC should adopt more expedited procedures for approving projects to provide the much-needed infusion of funds to the downtown economy.

B. LIBERTY ZONE TAX INCENTIVES

In our previous reports, the Comptroller's Office urged the Federal government to develop a unified and systematic accounting of the use of tax credits and accelerated depreciation benefits in the Liberty Zone package. These incentives, at a combined \$2.9 billion, are major components of the Liberty Zone program and represent the core of the intended financial assistance to businesses in the downtown area. For this reason, if the assistance is not utilized by downtown firms, the Federal government must identify ways to re-program these benefits in order to revive economic activities in Lower Manhattan. To a limited extent, the President's recent proposal has addressed this issue by suggesting that \$2 billion of these incentives be replaced with a corresponding increase in transportation initiatives. In doing so, the Federal government has also begun the process of addressing a significant risk in the disaster relief assistance package, pending approval from Congress. Yet, despite the welcome news, a residual portion of these tax incentives, totaling \$864 million, still needs to be addressed. This office reiterates the stance that developing a tracking mechanism to monitor the use of these tax incentives should still be a priority for the Federal government. Further, should these incentives remain unused or fail to reach their estimated savings, the President must act to ensure that the full value of the Liberty Zone tax incentives will be realized as originally promised.

C. LIBERTY BONDS

The Liberty Bonds program has encountered delays in bond issuance in the first three years of the program. The problem will be further compounded by the approaching

deadline of December 31, 2004 for developers to issue these bonds. There is currently proposed legislation to extend the issuance deadline to December 31, 2009. Bills which have been approved by the Senate and the House of Representatives are now in conference. The deadline extension would likely be sufficient to allow commercial developers to take advantage of the \$3.42 billion in remaining bonding authority in the program, but it will not address the expected shortfall of \$352 million as a result of issuance delays. The Federal government must take actions to make certain that the projected tax-exempt savings of \$1.2 billion from these bonds are kept whole.

D. TRANSPORTATION INFRASTRUCTURE

The President's proposal to swap Liberty Zone tax incentives could inject an additional \$2 billion towards the building of transportation infrastructure in the downtown area. If approved, the additional funding will bolster the chances that a direct rail-link service between Lower Manhattan and JFK airport will be built. The project, with an estimated cost of \$6 billion, is favored by both the Mayor and Governor Pataki. In addition to direct rail access to JFK airport, the LIRR will also be extended to Lower Manhattan. Thus, the rail-link will provide direct rides to out-of-town travelers and commuters alike, and will no doubt boost economic activities in the downtown area. However, this project would consume the entire transportation funding that is currently available and preclude the funding of other important projects for the downtown area. Therefore, despite the enthusiasm of the Mayor and the Governor, the decision to build the JFK rail-link should not be reached without adequate consideration. Further studies should be performed on the feasibility of the project and an open process should be established to prioritize projects in the downtown area. The integrity of an open process would assure the public that a decision to construct the JFK rail-link will be wholly based on its merits, as opposed to its popularity with senior officials.

E. OTHER FEDERAL FUNDING

As with the Liberty Zone tax incentives, the Federal government needs to establish a mechanism to track the programmatic funding in these categories. Even with the Federal government's insistence that the combined funding of \$1.2 billion has already been obligated through the oversight agencies for these programs, the scarcity of information regarding these initiatives remains a significant concern. Because of the lack of a more systematic accounting and reporting on the usage of these funds by the Federal government, the Comptroller's Office has shown \$797 million of these funds to be in question at this time.

III. Conclusion

As New York City approaches the third anniversary of the WTC attack, there are signs of a gradual but still fragile economic recovery for the City. The 9/11 disaster brought heavy economic and job losses to New York City, with the impact obviously most pronounced in the downtown area. The President's commitment of \$20.8 billion is essential in helping New York City recover and rebuild from the disaster. Therefore, it is critical for the Federal government to adhere to its level of promised aid in its assistance package.

Two major concerns that were raised by this office last year are being addressed, although concerns remain. The President's proposal to convert a portion of the Liberty Zone tax incentives into tax incentives associated with transportation initiatives, if approved by Congress and fully utilized, would both reduce the risk in the overall aid package and soothe skepticism over the realistic benefit of these incentives. Also, the extension of the issuance deadline for Liberty Bonds will allow developers more time to take full advantage of the tax benefits under this program. However, the Comptroller's Office believes additional actions are still needed, as more than one-quarter of the entire package, including the estimated shortfall of \$1.2 billion and the funding in question of \$4 billion, remain unrealized. The recommendations in this report point to the type of actions that are needed for the Federal government to fulfill its funding pledge and ensure timely and efficient usage of these funds.

Appendix — The Continuing Impact of 9/11 on the New York City Economy

The early estimates of economic losses incurred by New York City as a result of the 9/11 attacks are broadly consistent with the City's experience over the subsequent three years. New York City's recession has been far deeper than that of the nation's. The City has continued to lag the nation in year-over-year monthly percent changes in jobs since the second quarter of 2001. New York City suffered 11 quarters of negative economic growth whereas the nation suffered only two quarters of negative growth, as measured by gross product. Data published by the Comptroller over the past three years continue to illustrate the ongoing impact of 9/11. The damage from the 9/11 attack can be categorized into immediate capital loss and continuing economic loss.

1. Immediate Capital losses (Physical and Human). The immediate capital losses can be more readily estimated than the economic losses, in part because of the availability of insurance-company data. Property losses are largely covered by property insurance. Human capital losses are often covered by personal and business life insurance and disability policies. The September 2002 estimate of total capital losses by the Comptroller's Office was \$31 billion.

2. Continuing Economic and Business-Interruption losses. Economic losses are relatively harder to measure than capital losses, because business interruption insurance is less wide-spread and doesn't cover all losses and because the effects of 9/11 must be isolated from other factors that emerge over time. Two ways of assessing the economic damage from 9/11 are changes in jobs and gross product.

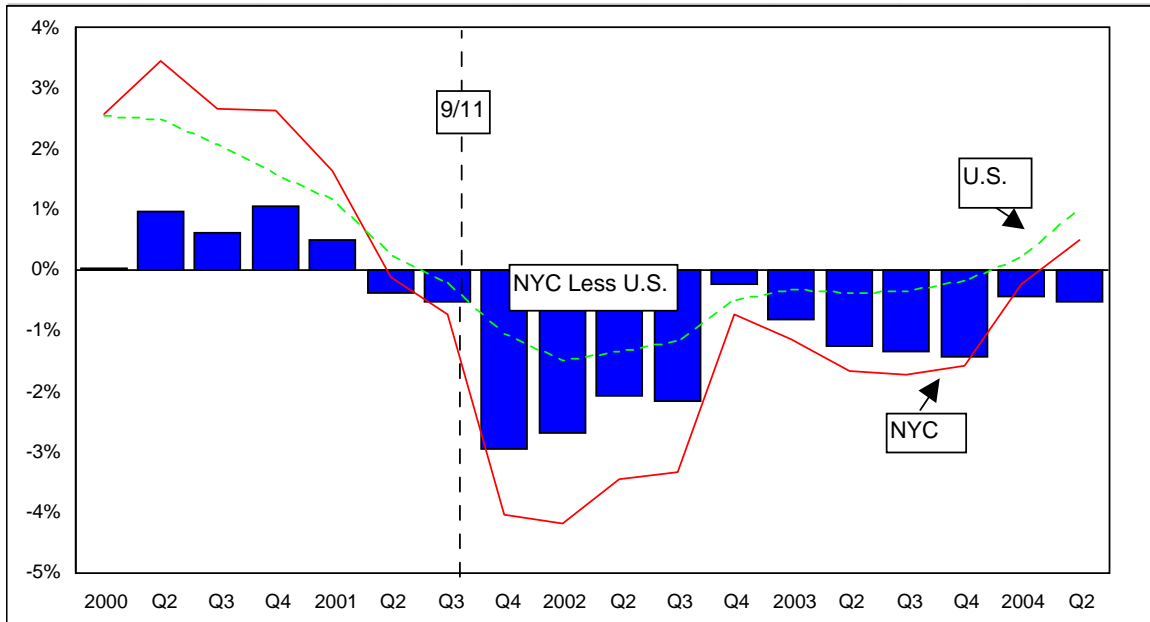
A. Lost Jobs. Comparing changes in NYC's jobs with changes in U.S. jobs since 9/11 provides an indication of the enduring impact of 9/11. The City has lagged the nation from 2001 through January 2004. From September 2001 to January 2004, when NYC first showed significantly positive job growth, the City had lost approximately 138,200 jobs. These jobs represented nearly two-thirds of jobs lost during the New York City recession, which started in January 2001.

B. Lost Gross Product. The gap between New York City's Gross City Product (GCP) and the U.S. Gross Domestic Product (GDP) persisted for nine quarters after 9/11.

A. LOST JOBS

NYC enjoyed higher quarterly job growth than the nation throughout 2000 and the first quarter of 2001. For the next two quarters prior to 9/11 and 10 quarters after 9/11, the City suffered higher year-over-year quarterly job losses than the nation. In the first quarter of 2004, i.e. the 11th quarter after 9/11, both the City and nation achieved positive job growth, but City year-over-year percentage job growth continued to lag the nation's, as shown on Chart 1.

Chart 1. NYC Lags Behind U.S. Year-over-Year Monthly Percent Changes in Jobs, First Quarter 2000/Second Quarter 2004



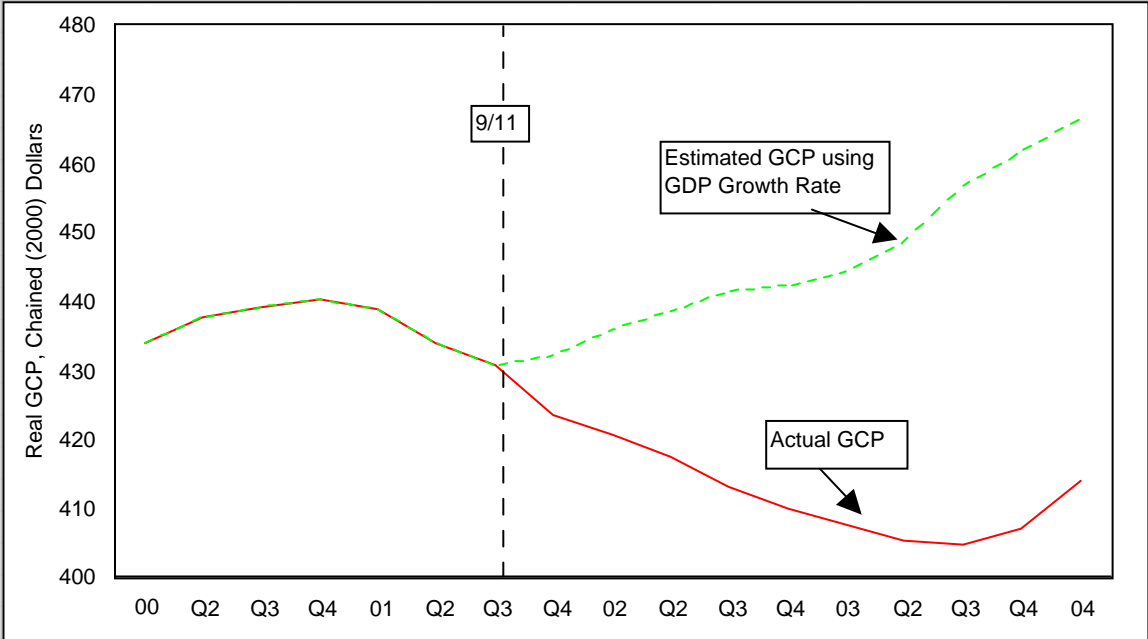
DATA SOURCE: Computations by the NYC Comptroller's Office based on data from New York State Department of Labor and U.S. Bureau of Labor Statistics.

B. LOST NYC GROSS PRODUCT

The weakness of New York City's GCP compared with U.S. GDP illustrates the continuing economic impact of 9/11. Although the unique distribution of New York City's economy relative to that of the rest of the nation will always result in differences between GDP and GCP trends, the divergence between the two since 9/11 is sharp, as shown in Chart 2. The solid line shows actual New York City GCP before and after 9/11, while the upper broken line applies the growth rate of U.S. GDP to GCP in the post-9/11 time period. U.S. GDP grew steadily after 9/11, while the New York City economy began to improve only in the first quarter of 2004.

Chart 2. Actual Real GCP (NYC Comptroller's Series) and Estimated GCP If NYC Had Grown at the Same Rate as the Nation after 9/11

(\$ in billions, 2000\$)



SOURCE: GDP from the Bureau of Economic Analysis. GCP data from the NYC Comptroller's Office

NOTE: If the GCP difference were calculated in nominal dollars, the dollar loss would be larger.

Glossary of Acronyms

BRG	Business Recovery Grants
CDBG	Community Development Block Grants
ESDC	Empire State Development Corporation
ETAP	Employment Training Assistance Program
FEMA	Federal Emergency Management Agency
FHA	Federal Highway Administration
FTA	Federal Transportation Administration
GCP	Gross City Product
GDP	Gross Domestic Product
HUD	Department of Housing and Urban Development
IFG	Individual and Family Grants
JCRP	Job Creation and Retention Program
JFK	John F. Kennedy International Airport
JOBS	Jumpstart Our Business Strength Act
LIRR	Long Island Rail Road
LMDC	Lower Manhattan Development Corporation
MRA	Mortgage and Rental Assistance
MTA	Metropolitan Transportation Authority
NYC	New York City

PA	Port Authority of New York and New Jersey
PATH	Port Authority Trans-Hudson Corporation
PDI	Pace Downtown Index
RGP	Residential Grant Program
SBA	Small Business Administration
SFARG	Small Firm Attraction and Retention Grants
U.S.	United States
WTC	World Trade Center