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When 421a Expired in January It Sent a Shiver Through a Lot of Multifamily Lenders

By Danielle Balbi and Terence Cullen April 6, 2016, 11 a.m.

The expiration of 421a not only has developers worried,
but has stopped the multifamily lending market in New York City.

Last week, an investment sales team announced it was marketing a development site—4002 10th Avenue—on the border of the Borough Park and Sunset Park sections of Brooklyn. The plot was listed for $12.8 million and was approved for a seven-story, 59-unit rental building.

A lot of investors and developers might steer away from a project like this because they can't finance a rental project without 421a, the tax break program that expired in January. Brokers Jeffrey Shalom and Aaron Warkov of Cushman & Wakefield said that the property's potential suitors initially shake off the chance of a development site because they don't want to hold it until they can feasibly afford to build.

However, 4002 10th Avenue has a secret weapon: It was already approved for the coveted 421a tax abatement.

"We explain to them whatever had to be done to secure that has been done already," Mr. Shalom said, adding that not having the break is "a deal breaker for a lot of people, because they don't see the viability of these projects without 421a."

But this instance is essentially a unicorn with many originators and brokers believing that financing new multifamily projects is dead in New York City until 421a is back. Plans for most new rental projects that didn't get clearance from the New York City Department of Buildings by mid-January will have to sit on the drawing boards collecting dust.

The rationale from developers is simple: Property taxes and the cost of land and construction are so high that it's impossible to make returns on rental projects without some sort of tax incentive. Affordable housing advocates, while not crazy about the exact terms of the tax break, have argued that setting aside 20 percent of a building's units below market rate (a key component of 421a) was critical to creating homes for working New Yorkers.

The blip in the new building application process for multifamily projects formerly covered by 421a will lead to a gap in development down the road, and thus a slowdown for both acquisition funding and construction financing. While many agree that developers will be hurt most by the expiration right now, the jury is still out on what long-term impacts it will have on the lending market. But until a new form of tax break is enacted, multifamily financing is at a standstill.

"Unless [lawmakers, the construction union and the Real Estate Board of New York] come to terms, development is going to be stymied in New York," said Michael Stoler, a managing director at Madison Realty Capital. "Lenders are not going to put money out unless it's a good deal for both [sides]."…….

But as builders of new product might be pulling their hair out, one expert said it's not necessarily a big loss to lenders who specialize in multifamily financing. Yes, in the recovery years, the residential sector of the industry has been king. If you walk around the Far West Side, Queens' Long Island City or Downtown Brooklyn, there are plenty of cranes in the air. So originators might find it a relief if there's a short-term cooling in the lending market, said Andrew Singer, the chairman and chief executive officer of The Singer & Bassuk Organization, a New York City debt brokerage.

"I don't think it'll break anybody's heart," he said. "From the lender's perspective they're all happy to take a deep breath at the moment."

Although construction and acquisition financing might decrease, lenders and debt brokers will instead focus on refinancing, Mr. Singer said. "There always seems to be somebody who needs or wants money," he said. "Sometimes it's construction, other times it's refinance."

But this lull in the lending market can't last forever, Mr. Singer said. Sooner or later something has to be enacted before the construction pipeline eventually runs out…….

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