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On Track or Off the Rails?

New York State's Plan to Use New Development to Fund Penn Station Improvements Leaves Many Open Questions for New York City and State

Summary

New York State has proposed a plan to develop 10 new, mixed-use towers around Penn Station in an effort to finance the reconstruction and possible expansion of Penn Station, the country's busiest, and arguably least-liked train station. Under the plan—announced by the Cuomo Administration and revised by the Hochul Administration—the state's Empire State Development (ESD) agency would take title to eight sites surrounding Penn Station and allow private developers to build greater density than city zoning currently permits, bypassing the city's normal land use processes. ESD would then use the property tax revenues and fees from the new development to help repay the debt funding Penn Station's improvements and nearby public space upgrades. The redesign and possible expansion of the train station itself is a separate, but closely related project led by the Metropolitan Transportation Authority, Amtrak, and New Jersey Transit and being planned in conjunction with the federal Gateway Program Hudson River Tunnel.

At the request of State Senator Brad Hoylman, Reinvent Albany, former City Councilmember Ben Kallos, BetaNYC, Manhattan Community Boards 4 and 5, Common Cause NY, and the Tri-State Transportation Campaign, the New York City Independent Budget Office (IBO) examined ESD's proposed General Project Plan for Penn Station and other related documents. IBO found that the plan, which is to be revised and presented to an ESD board vote in coming months, lacks many of the basic and important details needed for a robust analysis, and leaves many open questions about the impact on state and city finances. In this report, IBO examines what is included in the state's financing plan and highlights what information is still necessary for policymakers and others to evaluate the fiscal implications of the project. Among our findings:

- The total cost of the Penn Station improvement project and, therefore, the revenue needed to cover those costs remains unclear. ESD estimates the total public cost of the transit improvements, including the Hudson River Tunnel, to be \$30 billion to \$40 billion, with costs shared by the federal government, New York State, and New Jersey. New York State estimates its share of the cost from \$8 billion to \$10 billion, and thus far has authorized \$1.3 billion in capital funding for the project. Bond or other debt financing is expected to cover most of the remainder, although ESD has yet to provide details on how exactly this debt would be structured.
- ESD would use value capture financing, where payments in lieu of property taxes (PILOTs) and fees from the development sites are used to repay the debt funding the station project costs. Land owned by the state is exempt from city property taxes, and as a result, property owners would pay PILOTs to ESD, not property taxes to the city. The state has not released any revenue projections for these PILOTs, nor has it specified how the PILOTs would be structured, including, importantly, to what extent any property tax discounts would be offered.
- Currently, there are 55 property tax lots on the eight sites slated for new development. In fiscal



year 2022, the city collected \$60 million in property taxes on these sites, a very small share of the city's more than \$29 billion in total property tax revenue. ESD has indicated that it intends to reimburse the city for this lost tax revenue (with annual escalations), although this also has yet to be formalized. While such an arrangement would help keep the city fiscally whole, it reduces the amount of revenue ESD has to pay back the station project's debt.

- Without more data on projected costs and revenues, it is impossible to know whether revenues will meet debt service costs. The plan does not address what should occur if revenues fall short of costs, with no details on how those costs would be covered or by what level of government.
- ESD's plan would finance near-term station improvements with revenue from future private development, posing a timing risk. The station reconstruction and expansion projects are expected to be completed by 2032, but the development sites would not be fully completed until 2044. When there was a similar timing issue for the nearby Hudson Yards development—financed by the city in a similar manner—the city provided hundreds of millions in debt service payments from its own coffers until adequate revenue was available. While the state has acknowledged the timing issue, again, it has yet to provide information on how it would be resolved, leaving the impact on city and state finances far from certain.
- The Penn Station financing proposal does not include repealing Madison Square Garden's exemption to help fund the transit projects. The arena, located directly above Penn Station, is exempt from paying property taxes, saving the owners \$43 million annually.
- The majority of the proposed development is new Class A office space. Pandemic-related changes in work arrangements have raised questions whether there would be sufficient demand for such space in the future. High-end office space has fared favorably in the near term, and the transit-rich location of Penn Station may make the area particularly attractive to employers. There is potential, however, that new office space near Penn Station may erode demand for nearby Hudson Yards. It is difficult, however, to predict where the commercial real estate market will be in two decades, when the proposed Penn Station development is expected to be complete.

While few would argue about the need for improvements at Penn Station, many key questions remain unanswered under the state's current proposal, particularly around the construction cost, timing, financing, and risk management of the projects. This information is critical for the plan to be evaluated in terms of both potential risks and benefits to the state and the city—a necessary step before moving ahead with a plan that could impact city and state taxpayers for years to come.

Introduction

New York's Pennsylvania Station is the transit epicenter of the New York City region. In 2019, before the Covid-19 pandemic disrupted commuting patterns, it was the busiest transit hub in the Western Hemisphere. The station serves Amtrak's most well-traveled lines, as well as the largest and third largest commuter rail carriers in the United States—Long Island Rail Road and New Jersey Transit. It is expected to soon also serve the second largest commuter railroad when the Penn Station Access project brings some Metro-North Railroad service to the station by 2027. In addition, tens of thousands of daily passengers also travel through Penn Station via the city's subway system.

Designed to serve around 200,000 daily rail trips following the 1968 configuration which removed the majestic above-ground waiting rooms and train hall, the station is well above capacity and overcrowded, sometimes dangerously so. Pre-pandemic, daily ridership was around 600,000 rail and subway trips. Currently, ridership is around half of 2019 levels, but in the long term, the Metropolitan Transportation Authority (MTA) predicts a nearly 40 percent increase in ridership to over 800,000 trips by 2038.¹ Although central to the city and region, Penn Station and its surrounding blocks lack the amenities to make it an attractive area for commuters, visitors, workers, and residents. Despite its premium access to transportation, the area has not served as a major business district in decades.

Acknowledging the need to improve the station and meet projected growth in ridership, in February 2021 under Governor Cuomo's leadership, New York State's Empire State Development (ESD) adopted a General Project Plan (GPP) known as the [Empire Station Complex Civic and Land Use Improvement Project](#). The GPP outlined a plan to use mixed-use development in the area around Penn Station to generate revenues to finance, in part, the reconstruction and potential expansion of the underground train station. This development would be incentivized by greater allowable density through a zoning override and potentially discounted property taxes. In November 2021, Governor Hochul proposed revisions to the GPP and retitled it the [Pennsylvania Station Area Civic and Land Use Improvement Project](#).

Both the revised plan and the prior plan use value capture financing from eight development sites surrounding the train station to help finance the cost of improving and expanding the train station and making public space and transit investments around it. Governor Hochul's plan, however, changed the size and use of the proposed new buildings,

and revised the corresponding neighborhood amenities and public space requirements. Value capture financing uses property tax revenues and fees from nearby developments to back the debt financing used to fund infrastructure development. It is a financing strategy both the state and city have used to help pay for large transit infrastructure improvements such as Moynihan Train Hall and the extension of the Number 7 subway to Hudson Yards.

At the request of State Senator Brad Hoylman, Reinvent Albany, former City Councilmember Ben Kallos, BetaNYC, Manhattan Community Boards 4 and 5, Common Cause NY, and the Tri-State Transportation Campaign, the New York City Independent Budget Office (IBO) examined the Penn Station Area Project's GPP, proposed revisions, and related documents.² The GPP, which is currently undergoing additional revisions following a period of public comment, lacks many of the important details on the total cost of the station projects and related improvements, expected future revenues, and how the financing plan for the station renovation would work. Despite the limited information available, IBO has sought to provide context to what the state has outlined thus far and explain what additional information is necessary for a rigorous analysis of the cost of the plan and its fiscal impact on the city and state.

In this brief, IBO broadly defines the Penn Station Area Project as having four main components:

1. Upgrades and rehabilitation of the existing Penn Station;
2. Expansion of Penn Station to the south, in conjunction with the federal Gateway Program Hudson River Tunnel;
3. New privately-financed commercial and residential development on eight building sites adjacent to the station; and
4. Public transportation and neighborhood public space improvements.

The first two components are expected to have separate funding plans and be led by the MTA, Amtrak, and NJ Transit, and while an [overview](#) was presented to the MTA Board in April 2021, the Penn Station Master Plan detailing the reconstruction and expansion is still being formulated. The new development to help finance these transit and public realm improvements are covered in the GPP and will be led by ESD.

According to the state, preliminary estimates for the total cost of the public components: the reconstruction of the existing Penn Station; proposed station expansion; public realm improvements; and Hudson River Tunnel—which are separate from the privately financed developments—is

between \$30 billion and \$40 billion. These costs are to be shared among the federal government, New York State, and New Jersey using roughly a 50/25/25 percent split, assuming the costs for the Penn Station transit projects are shared using the same splits as under the Gateway funding agreement for a new Hudson River tunnel. Funding through the Federal Railroad Administration could allow for federal dollars to pay up to 80 percent of project costs, which would lower the financial burden on the states. This funding, however, is nationally competitive and subject to the whims in Washington, making it far from certain.

The GPP focuses on financing New York State's share of the rehabilitation of the existing Penn Station, the proposed station expansion, and public realm improvements, separate from New York State's contributions of the Hudson River Tunnel costs which is not part of the GPP. New York State expects its overall contribution for all of these projects to fall between \$8 billion and \$10 billion. In April 2021, the New York State Legislature authorized \$1.3 billion in the state capital budget towards the Penn Station railroad projects as an initial investment. ESD plans to use value capture revenue from the proposed development to finance the balance of its cost share for the various transit and neighborhood improvements.

This report begins by laying out the plan for the Penn Station Area Project transit improvement components as currently proposed. Next, IBO provides an analysis of what is known of the state's financing plan and identifies what remains unknown, and examines the potential risks value capture financing poses to both New York State and New York City taxpayers. Lastly, IBO provides some projections on real estate demand in relation to the proposed development at Penn Station, and considers the potential impact it may have on the nearby Hudson Yards and other new office developments.

Background

Former Governor Cuomo announced the original iteration of the Penn Station Area Project in January 2020, with the development component to be led by the New York State Urban Development Corporation, operating under the name Empire State Development (ESD)—a state public benefit corporation. Through two years of the pandemic, a new presidential administration, and a new governor, the project has evolved as it approaches an expected ESD board vote later this year. ESD has stated four goals for the project:

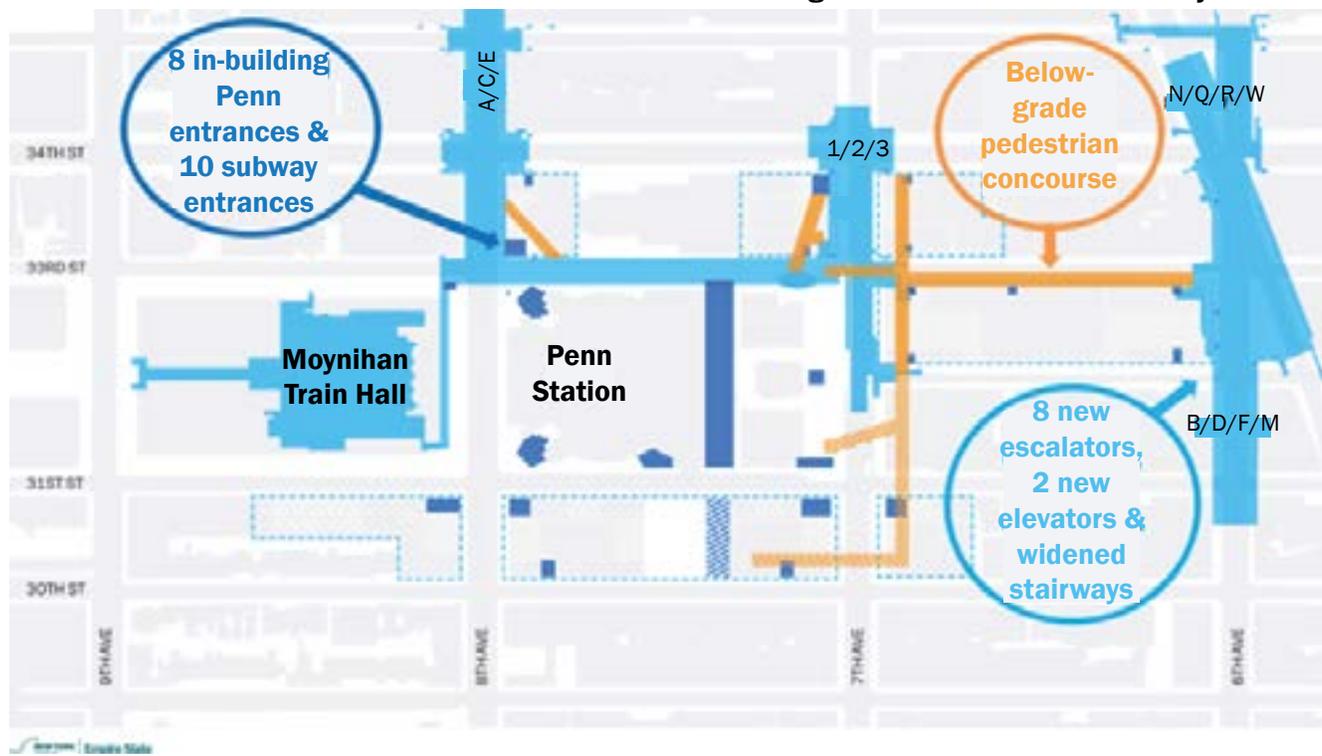
1. Improve passenger rail and transit facilities and pedestrian circulation, access, and safety

2. Support improvements to address substandard conditions at Penn Station
3. Support and accommodate future capacity increases at Penn Station
4. Revitalize the area surrounding Penn Station with new, sustainable, high-density mixed-use development.³

ESD projects require a GPP, a narrative description that presents the goals, parameters, and financing terms of a project, as well as alternative design guidelines if the plan calls for overriding local zoning laws. For Penn Station, the GPP is intended to provide a framework for how New York State proposes financing the reconstruction and potential expansion of Penn Station through a value capture financing model, and the parameters for connecting Penn Station into the city's subway system and public spaces and streets more broadly. The GPP does not cover specific designs for the reconstruction or expansion of the station itself, which are being advanced through their own review processes, led by a consortium of the stakeholder railroads: the MTA, Amtrak, and NJ Transit.

Penn Station Reconstruction Project. The most immediate component of the GPP is to provide a financing plan for the reconstruction of Penn Station. The reconstruction, likely to be led by the MTA in consultation with Amtrak, will renovate and improve the existing subterranean levels at Penn Station to facilitate train movements and improve the user experience. The reconstruction calls for raising the concourse ceilings and bringing in natural light via skylights to make the waiting areas and hallways more inviting. The renovation would also rebuild and expand the number of station entrances from the current 12 up to 20, and make them more prominent. Additionally, the new buildings on the development sites would be required to connect to Penn Station and nearby subway stations in an effort to reduce sidewalk congestion. The rehabilitation project includes new stairways and wider passageways to improve pedestrian traffic flow, clearer signage, and increased accessibility via elevators and escalators. As part of the public realm improvements outlined in the GPP, to connect Penn Station to nearby subways, the GPP calls for the creation of an underground pedestrian corridor network between the 34th Street-Herald Square subway station, the 33rd Street PATH station and Penn Station, and for subway platforms and stairs to be widened, among other transit improvements. The Penn Station reconstruction and station upgrades are expected to cost a total of between \$6 billion and \$7 billion.⁴

Station Renovations Would Include New Entrances and Underground Connections to Subways



SOURCE: Empire State Development Corporation *Penn Station Area Redevelopment Project* January 20, 2022

The railroads at Penn Station cite considerable urgency to complete these upgrades in the next few years. Amtrak and Long Island Rail Road trains now board from the recently opened Moynihan Train Hall, across 8th Avenue from Penn Station, which has reduced the pressure on the main station’s capacity. The connection of some Long Island Rail Road service to Grand Central Terminal through the MTA’s East Side Access project, expected to be completed later this year, will further help free up tracks and platforms to undergo improvements. The MTA has described this four- to five-year period before some Metro-North trains are brought into Penn Station in 2027 as a “window of opportunity” to complete the bulk of the structural work without major impacts on train service. Given that the MTA and Amtrak have not yet released a master plan, whether major upgrades will be accomplished within this timeframe remains uncertain.

Station Expansion in Conjunction with Gateway Program Hudson River Tunnel. In announcing revisions to the project plan in November 2021, the Hochul Administration emphasized fast-tracking the improvements to the existing Penn Station. The governor’s changes decouple station improvements from the proposed southward expansion of Penn Station, which requires additional layers of federal approval. The underground expansion one block south of West 31st Street would add eight to nine new

tracks and five platforms, primarily intended to serve NJ Transit. Initial estimates place the cost of the expansion component of the Penn Station Area Project at around \$10 billion. This separation between the renovation and expansion projects has yet to be formally included in an amended GPP, however.

New Development. A central aspect of the Penn Station Area Project GPP is the construction of 10 new commercial and mixed-use buildings at eight development sites between Sixth and Ninth Avenues and West 30th and West 34th Streets. According to the GPP, as an arm of the state, ESD would take title of the eight sites, thereby removing them from the city’s property tax roll, and in turn, ESD would enter into ground leases with private developers. Developers of the sites would make payments in lieu of property taxes (PILOTs) to ESD, and the state would use this income to service bonds or other debt issued to fund the station and neighborhood improvements and potential expansion, as discussed in more detail on page 9 of this report. Five development sites—Sites 4 through 8—are wholly or partially already controlled by one real estate company, Vornado Realty Trust (Vornado). Vornado owns numerous other nearby properties and was a partner in the redevelopment of the Farley Post Office Building into the recently-opened Moynihan Train Hall, a project also overseen by ESD.

Penn Station Expansion Project Would Tie Into Gateway Hudson River Tunnel

The station expansion is planned as a component of the Gateway Program, a series of major northeast corridor investments by Amtrak, the federal Department of Transportation, the states of New York and New Jersey, and the Port Authority of NY-NJ. The expansion would connect with a new Hudson River Tunnel, which is the centerpiece of the Gateway Program, allowing four mainline tracks to run from Newark to New York City, clearing up a historic bottleneck for trains crossing under the Hudson River. The station expansion was initially estimated to be completed in 2028 but incurred a lengthy federal review process. The expansion project would not become fully operational until the Hudson River Tunnel is completed, currently anticipated for 2032. Importantly, neither the reconstruction of the existing Penn Station nor the Hudson River Tunnel project are contingent on the station expansion going forward, although all of the components would mutually benefit from each other.

The new Hudson River Tunnel and accompanying rehabilitation of the existing North River Tunnel into Penn Station are expected to cost around \$12.3 billion, with costs at least initially anticipated to be split evenly between federal sources and state sources. With the recent passage of the federal Infrastructure Investment and Jobs Act, however, the states of New York and New Jersey may try to pursue additional federal funding. The federal share is being pursued through the Federal Transit Administration's Capital Investment Grant New Starts Program and Amtrak and other potential federal funding sources. The remainder is expected to be split equally between New York and New Jersey, with contributions from the Port Authority of NY-NJ. To date, the Port Authority of NY-NJ has committed up to \$2.5 billion, and the states are pursuing federal Railroad Rehabilitation and Improvement Financing (RRIF) loans for the local share. New York State's financing of its share of the tunnel costs is separate from the financing plan covering projects in the GPP.

Under the proposed ESD plan, the commercial and residential development would be privately financed, and the first building is expected to be completed and ready for occupancy in 2028 and all buildings by 2044. The development of Sites 1, 2, and 3 (the southernmost

development sites), are contingent on the Penn Station expansion southward passing federal environmental review. (See the map of development sites on [next](#) page.) Since the below-grade train station expansion would be led by the MTA, and above-grade new construction for Sites 1 through 3 by a private developer, in practical terms this presents challenges to designing both portions together as a cohesive design. According to the GPP, it has yet to be decided which entity involved in the expansion—ESD, Amtrak, or the MTA—would be responsible for the property acquisition of Sites 1, 2, and 3, and how ownership of the expanded station would be structured.

ESD would use its statutory authority to override local zoning laws and set its own standards for design aspects such as height, bulk, and building setbacks for the eight sites. ESD's proposal would only affect the eight specified development sites, and 1 Penn Plaza—an existing office building which sits directly in between Sites 4 and 5. The existing building at 1 Penn Plaza would have its tax lot redrawn in the process of creating Sites 4 and 5. All other property parcels in the immediate area would remain subject to their current city zoning.⁵

Under proposed revisions to the GPP made by the Hochul Administration, the total buildable space across all eight building sites would be 18.3 million gross square feet, around 6.9 million gross square feet more than current zoning allows. (The original Cuomo Administration plan called for 19.6 million gross square feet of development.) The floor area ratio equivalents under the proposed revision would range from 13.0 to 30.0, allowing for greater density than current city zoning. (Floor area ratio, or FAR, is the total building floor area on a zoning lot, divided by the lot area. For example, on a 2,000 square foot lot with a FAR of 5.0, a developer could build up to a 10,000 square foot building.) Presently, the development sites are zoned for FAR of 4.0 to 15.0, although many of the existing buildings are built to less than the maximum bulk allowed under city zoning. Additionally, ESD has established building design parameters to at least partially preserve street views of the Empire State Building, in particular along West 33rd Street.

The proposed development would be mainly composed of commercial Class A office space, with smaller amounts planned for residential, hotel, community facility space, and retail. (While the GPP as initially adopted broke out the planned buildings by use and square footage, ESD's proposed revisions under the Hochul Administration only discuss changes in height, use, and bulk—but not square footage.) Up to 1,800 rental units across Site 1A and

New Development Entails Ten Buildings on Eight Sites Surrounding Penn Station



Map prepared by Sarah Sayavong
New York City Independent Budget Office

some combination of Sites 1B, 4, and 8 are proposed, with 30 percent (up to 540 units) set aside as permanently affordable. ESD, however, has not indicated at what level of affordability these units would be. Displaced residents would have the right to return, although the timing and details of how this would work have yet to be provided.

Neighborhood Public Space Improvements. In addition to improving the underground transit infrastructure, and the new real estate development, the Penn Station Area Project contains public space upgrades.

Streets and Plazas: Sections of West 31st, West 32nd, and West 33rd Streets are proposed to become shared streets—streets on which pedestrians and bicyclists are prioritized, while allowing for slow-moving vehicular traffic.⁶ The New York City Department of Transportation or local business improvement districts would be charged with managing the shared streets, in keeping with shared streets elsewhere in the city. The plan also calls for protected bike lanes and widening of existing sidewalks, as well as a 30,000 square

foot new public plaza on the block just south of Penn Station (Site 2).

Vehicle and Bicycle Parking: Currently, the project area has around 2,500 parking spots; the proposed redevelopment would reduce this to no more than 800 spaces. New construction in the project area would be required to have bicycle parking in the building.

Public Space Requirements: Additionally, the eight proposed development sites would be required to provide public space, with the ratio of site area that must be public space ranging from 5 percent up to 44 percent. Two of the proposed development sites would disrupt an existing privately-owned public space at 1 Penn Plaza. Under Governor Hochul's proposed revisions to the GPP, 1 Penn Plaza would either be required to provide for new, equivalent square footage of privately-owned public space, or pay the fair market value of the current space's density bonus into the Penn Area Public Realm Fund—a local improvement fund the state would create as part

What Is Currently On The Eight Sites Slated for Redevelopment?

The eight development sites and the surrounding area are largely zoned as a general central commercial district, with smaller portions zoned as light manufacturing and medium density contextual residential.⁷ In the commercial districts, zoning also allows for residential buildings of a similar size to be built in lieu of commercial space. The eight proposed development sites consist of 55 property lots hosting around 4.7 million square feet of real estate. Businesses on these properties employ around 8,300 workers at an average size of 25 employees, primarily in the professional services, hospitality and food service, and the wholesale and retail trade sectors.⁸

The age of the buildings on these lots is striking—80 percent were built in the 1930s or earlier, and only six were built in the past 50 years. Furthermore, many of these buildings are underbuilt relative to what current zoning allows in terms of maximum square footage. More than half of the parcels have buildings of four stories or less, primarily small retail stores and walk-up apartments. Most of the taller buildings are office space, and only three buildings are 20 stories or more. Although old, none of the property lots have a building designated as historic under the New York City Landmarks Preservation Commission, or State or National Registers of Historic Places, although some buildings meet the eligibility criteria to be considered for these designations.

Existing Buildings on Development Sites Consist of Office Space, Small Condo Buildings, Hotels, and Other Uses

Site	Current Uses	Number of Property Lots	Gross Square Feet	Year Built	Building Heights (Stories)
1A	Garages	1	82,750	1972	8
	Educational Facilities	1	116,000	1953	4
1B	Garages	2	-	-	-
	Hotel	1	9,507	1920	4
	Stores	4	23,242	1901-1920	2-4
	Office Buildings	1	6,376	1901	4
	Mixed-Use Property	1	4,494	1901	3
2A	Walk-Up Apartments	2	15,528	1900	3-5
	Stores	6	45,380	1910-1930	1-7
	Group Quarters Facilities	1	6,462	1927	2
	Office Buildings	7	387,709	1923-1930	5-17
	Condominium Buildings	1	32,500	1986	12
	Utility Property	1	-	-	-
2B	Garages	1	245,542	1957	6
	Religious Facilities	2	53,110	1920, 1974	3-4
	Office Buildings	1	332,383	1921	17
3	Garages	1	-	-	-
	Hotel	1	473,391	1929	28
	Stores	1	16,821	1924	4
	Office Buildings	3	256,685	1912-1930	12-22
4	Stores	1	14,145	1967	1
5	Stores	1	34,000	1969	1
	Utility Property	1	-	-	-
6	Stores	10	159,118	1900-1932, 1972, 2002	1-3
	Office Buildings	1	67,114	1926	14
7	Condominium Buildings	1	1,213,324	1917	23
8	Office Buildings	1	1,105,991	2001	12

SOURCE: Department of Finance Property Tax System data

NOTE: Current uses reflect the Primary Building Class. Blank entries indicate the information is not available or applicable.

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Development Sites for Penn Station Area Currently Mix of Office Buildings, Residential, and Stores



Map prepared by Sarah Sayavong
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of the project. The Public Realm Fund would be directed by a cross-jurisdictional Penn Station Area Public Realm Task Force, modeled on the East Midtown Rezoning Public Realm Improvement Fund Governing Group.

Penn Station Area Project Financing Plan

New York State, through ESD, proposes using revenues generated by the new private commercial development around the station to finance the station reconstruction, neighborhood public space and transit improvements, and the potential station expansion. (Because the residential development will be required to have an affordable housing component, ESD has indicated that it is not planning to enter into PILOT agreements for the residential buildings.⁹) Under the proposed variant of value capture financing, ESD would override local zoning rules for the eight development sites, acquire title to the sites at the time they are developed, and then use at least some of the PILOT revenue—expected to increase due to the benefit of transit improvements and zoning change—to pay down the debt. ESD has indicated that it intends to provide the city with revenue equivalent to what the city’s Department

of Finance currently collects in property taxes on the eight development sites (with annual escalation based on expected growth without the new development) although such an arrangement has yet to be formalized.

The theory behind value capture is that the new development directly benefits from the station and public space and transit improvements—in terms of increased property values—and therefore should have a role in paying for those improvements. In the case of the Penn Station proposal, it is not a textbook value capture model; outside of the eight development sites, ESD’s plan does not capture revenue from other nearby properties that will also benefit from the transit improvements. Meanwhile, the eight development sites in the plan will gain value from the transit improvements, but also from ESD’s ability to override local zoning laws. Any added value (and therefore tax revenue) that these sites yield because of the superseded zoning rules is additional revenue that likely would not occur in the absence of ESD’s involvement. While the state has indicated that it plans to use some type of value capture financing, it has provided scant details on

What is Empire State Development?

Created in 1968 under the New York State Urban Development Corporation Act, the New York State Urban Development Corporation, doing business as Empire State Development (ESD), is a public benefit corporation that conducts economic development and civic projects on behalf of New York State. It is governed by a board of directors, comprised of two ex-officio members and seven members, all appointed by the governor with the consent of the state Senate, with the chair of the board selected by the governor. It holds the statutory authority to spur real estate development, specifically through the power to:

- Acquire real property, including by eminent domain;
- Exempt its properties from some state and local taxes, including real property taxes, but can collect or issue PILOT agreements which could be equivalent to actual taxes that would otherwise be owed or at a discounted rate;
- Override local zoning laws and issue its own design, use, and occupancy rules; and
- Issue tax-exempt or taxable bonds for private projects.

The New York Pennsylvania Station Public Safety Improvements Act (Penn Station Act), enacted in 2018 by the New York State Legislature, declared Penn Station “antiquated, substandard, and inadequate,” and tasked ESD, in coordination with the MTA, to head up improvements on behalf of the state.¹⁰

how it would be structured. Value capture financing can come with more risks than traditional public financing, a topic IBO covers in more depth on page 12.

New York State cannot issue general obligation debt without first putting it to vote via a ballot referendum. To bypass this, the state generally does its bond financing via public authorities, such as ESD and MTA. To fund the Penn Station Area Project, the state through ESD or the MTA (or some combination that may also involve the other railroads) could borrow through one or more federal loan programs such as the Transportation Infrastructure Finance and Innovation Act (TIFIA), Railroad Rehabilitation & Improvement Financing (RRIF) loans, or issue tax-exempt bonds. While New York State authorized \$1.3 billion in its capital budget last year to provide funding toward Penn Station transit work, looking forward ESD says it expects to need an additional \$4 billion to \$6 billion to pay up front

for the station improvements and proposed expansion and neighborhood amenities.¹¹ ESD then expects to pay down debt associated with the project using revenues from the development sites the new buildings open for occupancy.

ESD to Take Control of Development Sites. The state must hold ownership of the development sites in order to remove them from the city property tax roll and instead have the properties enter into PILOT agreements. Vornado Realty Trust controls nearly all of the land comprising five of the eight development parcels, Sites 4 through 8. The GPP states that ESD would acquire Sites 4 through 8 at the time of development for a nominal cost arranged with Vornado, and then turn over the land under a ground lease (presumably also set at a nominal amount) to Vornado for each site. Vornado, as the current holder of Sites 4 through 8, is expected to redevelop each of these five sites, although Vornado could choose to sell any of the sites and a different developer would enter into an agreement with ESD. Although not spelled out in the GPP, according to ESD, for each site, the private developer would negotiate a development agreement with ESD detailing payments for development rights and any required public benefits to be incorporated onsite, such as transit entrances.

The same process of land acquisition followed by a ground lease to a developer is proposed for Sites 1, 2, and 3, although the entity responsible for the initial property acquisition (ESD, Amtrak, or MTA) has yet to be decided. If the current property owners of Sites 1 through 3 are unwilling to voluntarily sell their properties, the state has indicated eminent domain could be invoked. Because development of Sites 1 through 3 would only proceed following the separate approval process for the station expansion underneath these sites, ESD’s GPP presently does not address using eminent domain to acquire any property interests for the proposed project.¹² In the GPP, ESD does anticipate it would become the ultimate title holder of these sites, even if it does not initially acquire them, and ESD would execute ground leases for each site. No developer or developers for Sites 1, 2, and 3 has yet been selected. For all eight sites, the developers would be expected to privately finance the construction of mixed-use buildings in accordance to the corresponding agreement with ESD.

Sources of Revenue Resulting from the New Development. While the GPP identifies potential financing sources, ESD has provided few details on how revenue would be structured, or even how much revenue it projects could be generated using this value capture financing

Development Would Provide a Mix of One-Time and Reoccurring Revenue Sources				
	Developer	Initial Land Acquisition	One-Time Revenue Sources	Reoccurring Revenue Sources
Sites 1-3	Unknown	Most likely ESD, or alternatively Amtrak or MTA	Land sale	Periodic ground lease payments
			Upfront lease payment	
			PILOMRT	PILOT
PILOST				
Sites 4-8	Vornado Realty Trust	ESD	Payments for development rights	PILOT
			PILOMRT	
			PILOST	

SOURCE: IBO analysis of Empire State Development Corporation documents

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structure. These open questions make it impossible for IBO to evaluate the financing proposal and quantify its impact on the city and state. Rather, we next discuss what information is provided in the plan and what additional information would be needed to assess the project.

Payments in Lieu of Property Tax. The likely largest source of ongoing revenue under ESD’s plan would be through PILOTs. ESD is exempt from paying local property taxes. When the corporation leases state-owned land to a private entity, that entity generally pays an amount equal to what the municipality would have received in property taxes. Under a value capture framework, instead of the PILOT revenue flowing back into city coffers, some or most of this revenue would be used by the state to pay off the debt issued to fund station improvement costs. ESD has released few details on the structure of the PILOTs, stating only that “the structure of any PILOT would be determined in consultation with the city,” and according to ESD, they are currently in negotiations with the city relating to PILOTs.¹³ As previously mentioned, ESD has reported that they intend to transfer to the city annually the amount of property taxes currently collected at the eight sites (discussed in greater detail on page 14). This transfer would help keep the city fiscally whole, but reduce the revenue available for debt service.

PILOT payments directed towards the financing of the Penn Station projects may be set for a period of time (typically such agreements remain in place until the debt has been serviced), and once the transit debt is paid off, ESD anticipates the ground leases would be terminated and the sites would revert to paying city property taxes. Like many details of this plan, however, the sunset period for any PILOTs, if they do sunset, have yet to be described. Without clearly delineated sunset provisions, value capture projects run the risk of expanding outside their original scope and taking on additional debt, which can morph into

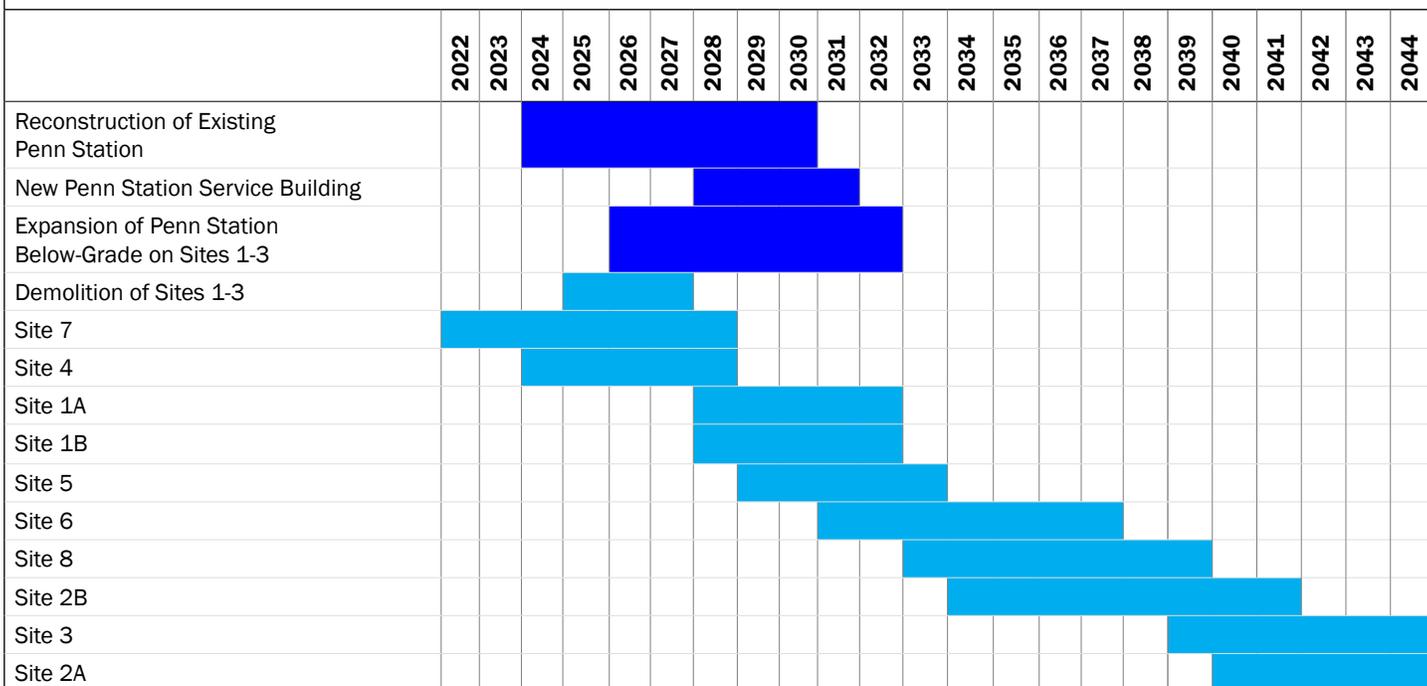
a permanent diversion of revenue from the municipality’s general fund, long after the initial project is paid off.

Other key details also remain unknown. These include the extent to which the PILOT structure provides any discount to developers from what the equivalent property taxes would be, how the discount would be set, how long any such discounts would last, and what if any—portion of the payments would be transferred to the city.¹⁴ Any discounts reduce funds available to support financing, so if discounts are given they must be set at a level that creates an incentive for the development projects, but not so steep as to give away revenue unnecessarily, or to give developments with PILOT discounts an advantage over other similar office buildings elsewhere in the city. In the case of several Vornado-owned sites, the company has already indicated its intention to redevelop, which may signal that little additional incentive is needed, if at all, for those sites.

For development proposed in the GPP, it remains unclear if discounts would be necessary to spur new investment. Unlike Hudson Yards—where the city is using the value capture model to pay for the extension of the Number 7 subway line and other improvements on the far west side—the location of the new sites close to Penn Station may itself be sufficient to attract developers. In the case of Hudson Yards, located only a few blocks north but extending several avenues farther west to 11th Avenue, the city determined that development in an almost entirely new neighborhood that far west would not be economically feasible on a schedule to meet the financing needs of the subway project without some level of public subsidy. Steep discounts relative to taxes in midtown Manhattan were offered with extra incentives for the earliest projects in the area, in an effort to ensure that PILOTs and other revenues would flow quickly in order to provide funding needed to service the debt on the subway extension bonds.

Transit Projects Expected to Be Completed Before Most Private Development Is Completed

■ Transit Projects Construction ■ Private Development Construction



SOURCE: Empire State Development, Vornado, MTA, Urban Atelier Group, January 2022 Draft Phasing and Illustrative Construction Schedule
New York City Independent Budget Office

While the Penn Station redevelopment would not have this location problem, it would likely face competition for tenants from Hudson Yards. Even in 2044, the earliest all the Penn Station development is projected to be complete, many buildings in Hudson Yards will still be paying discounted property taxes, which are passed through to tenants as lower rents. It is important to consider the impact PILOT discounts at Hudson Yards may have on how Penn Station’s PILOTs are structured.

Other Revenues. In addition to PILOTs, ESD identified several other potential sources of revenue for the Penn Station Area Project, although again little detail is provided on how these sources would be structured or any estimates at all on how much revenue they would bring in. For Sites 1 through 3, the state would take control of the properties and then sell or lease the development rights to yet-to-be-determined developers. Lease payments could be made upfront or periodically, or both, depending on how ESD structures the deals with each of these sites. For Sites 4 through 8, Vornado is expected to make additional payments in exchange for the right to develop these sites more densely than would be allowed under current city zoning rules.¹⁵ The developers of Sites 1 through 3 may make development right payments as well. Revenues from the sale of development rights could provide critical, one-time, upfront funding for the Penn Station projects while the

new development is under construction and likely not yet paying much in PILOTs. According to the GPP, properties may also make other potential sources of upfront revenues such as payments in lieu of sales and use tax on construction and outfitting materials (PILOST) and payments in lieu of the mortgage recording tax (PILOMRT).

Value Capture Financing Risks

Value capture financing is riskier than financing using traditional state and local debt, and therefore ESD should provide a clear justification for using a value capture or tax increment financing framework rather than traditional financing. IBO next outlines some of the risks presented by the proposed financing scheme.

Risk of Timing Gaps. A critical, open question for the project is one of timing. New York State’s plan would finance present day public improvements with revenue from future private development. One major question is how long is the expected gap between incurring the costs of the Penn Station improvements and when the revenues from new development are sufficient to pay for those improvements. Reconstruction of the existing Penn Station is expected to start in 2022 or 2023, followed by the start of the Hudson River Tunnel and the potential southern expansion component shortly thereafter. Recent ESD estimates pushed

back the completion timeline from what it presented last year, now anticipating that the transit projects—station rehabilitation, expansion, and a new service building—would be completed in about a decade, by 2032.

For the private development, ESD expects only Site 7 and Site 4 to be completed and making PILOT payments within that 10-year window. (Vornado recently started interior demolition on Site 7, the Hotel Pennsylvania.) Construction at the remaining development sites is expected to start around 2029 and all the buildings are anticipated to be completed by 2044. ESD estimates that any development revenue generated while construction on the transit projects is underway would be primarily from Site 7 and some upfront payments from other development sites.

Risk of Revenue Shortfalls. This timing gap and the uncertainty over future development increase the risk for revenue shortfalls, relative to projections. If PILOTs come up short relative to expected revenues, what level of government would be responsible to make up the difference? To boost the credit rating and ensure the station construction projects continue if development revenues fall short, additional funding, presumably from the state or city coffers, would be required to cover debt service costs until PILOT revenue can sustain the payments. Again, ESD has yet to provide any specifics relating to its expected need or potential sources of additional funding. Many institutional bond holders and federal transit loans require investment-grade ratings, and a commitment for additional funding has been needed for past value capture projects in New York City not only to boost the credit rating but to ensure that financing costs—interest, principal, or both—can be paid.¹⁶

The Hudson Yards development faced a timing issue similar to Penn Station, with an expected lag between the start of the subway extension construction and associated infrastructure construction and the completion of new buildings. Anticipating this timing gap, the mayor and the City Council agreed to make interest support payments to the Hudson Yards Infrastructure Corporation (HYIC) until the development revenue would be enough to support the annual debt service. For Hudson Yards, the city paid \$359 million from fiscal years 2010 through 2015 for interest support payments to support \$3 billion in bond financing. In the case of Moynihan Train Hall, the project had strong PILOT revenue projections for the commercial space planned at the Farley Post Office Building behind the train hall. Yet the borrowing backed by the PILOT and other developer revenues alone was not sufficient to earn the

investment-grade credit rating needed to secure a federal Transportation Infrastructure Finance and Innovation Act (TIFIA) loan ultimately totaling \$607 million. In order to boost the credit rating for this borrowing, the MTA agreed to guarantee regularly scheduled debt service payments during the construction and initial operating phases. When the project financing closed, the MTA set aside \$20 million tied to a debt service reserve account, which will remain in place until at least 2033 and until certain requirements are met: project completion, minimum credit rating levels, and specified PILOT coverage tests. In this way, the MTA guaranteed the loans in the event of construction delays or if expected commercial development did not materialize.

Descriptions of this sort of additional funding or credit enhancements for the Penn Station Area Project are notably missing from any of the financing discussions in the GPP and related documents. This likely need was acknowledged, however, in an ESD funding and financing presentation to the project working group. Importantly, neither the GPP nor the ESD presentation specified who would be paying for it. If New York State provides this support, the city would not be responsible if value capture financing did not meet expectations, but it could potentially leave state taxpayers, which includes New York City residents, to pay for it.¹⁷ A related but more optimistic consideration is what happens if the PILOT revenue exceeds original estimates—would surplus revenue remain with ESD, revert to the city, or be shared? As an example, HYIC is required to remit surplus revenue back to the city, and in recent years the city has received \$663 million in surplus payments. Again, however, for Penn Station none of this has been defined in the state's plan.

Risk of Cost Overruns. ESD has supplied no information for the Penn Station reconstruction and expansion projects on how the MTA would identify savings, or how ESD would cover additional costs in the event of insufficient revenue or cost overruns. The Number 7 subway construction related to Hudson Yards experienced cost overruns. In response, the city with the MTA adjusted the construction plan, scrapping a planned station altogether to provide offsetting savings, and the city committed to cover the balance of construction costs with its own capital funds.

Risk of Recession. Value capture financing, as are most types of financing, is exposed to the risk of a recession. In the case of Penn Station, there is risk that the anticipated pace of the private development is disrupted by a recession and risk that the value of those buildings (and their PILOTs) afterwards will be subject to market fluctuations. As an

example, in 2006, the value capture financing for the Number 7 subway line extension was stress-tested by Cushman & Wakefield against the possibility of a modest economic downturn. The Great Recession, however, provided a bigger economic shock than what was modeled in the risk evaluation, and the city's interest support payments were larger than all the initial projections.

Financial Baseline Projections and Stress Tests Needed.

As described above, any financial projections must be stress tested against combinations of potential pitfalls. Future revenues depend on demand for the office space and to a lesser extent the hotels and housing, an issue we explore later in this paper. Revenues may not come in as predicted due to changes in interest rates, economic downturns, or simply project delays in construction of the development sites—potential issues that affect the credit rating of the debt. The station expansion is contingent on federal approvals, and as a result, the development of Sites 1 through 3 remains uncertain. If the expansion location is not approved or faces major delays, the debt burden of the station reconstruction and neighborhood improvement components would be relying on revenues from Sites 4 through 8 alone. This contingency should be built into revenue projections to protect against the risk that expansion and the development of Sites 1 through 3—and its associated revenues—does not materialize. In order to evaluate the credit-worthiness of the value capture framework, New York State must provide more information about what revenues it is projecting and how it has modeled baseline projections against a variety of potential unfavorable conditions.

Potential Fiscal Implications for New York City

Current Property Taxes for Development Sites. As described in the previous section, the GPP lacks detail on what would happen if the revenues proposed under the value capture financing strategy fall short of debt service costs—and what level of government would cover those costs—leaving an open question about the impact of the project on the city's finances. There are other also implications for the city. The most direct risk to the city under ESD's proposal is the potential loss of the property taxes paid by properties on the eight development sites. While ESD has indicated that it intends to provide the city with revenue equivalent to what the city currently collects on the sites (with escalation amounts to adjust payments over time), such an arrangement has yet to be formalized. Furthermore, any revenue returned to the city would mean less reoccurring revenues to put towards paying off the

transit project debt, a factor that will impact the credit rating and the ability to pay down debt.

In city fiscal year 2022, the New York City Department of Finance set the fair market value at \$1.3 billion for the eight development sites and New York City assessed \$60 million in property taxes, which is a very small share of the \$29.4 billion in property tax forecast for the year. Assuming the current buildings on Sites 1 through 8 remain unchanged, using historical increases in value over the last decade for each site, IBO estimates the present value of the property tax revenue over a 30 year period to total \$3.7 billion. Of the \$3.7 billion, \$2.3 billion is associated with Sites 4 through 8, which would be redeveloped if ESD's proposal is approved, and \$1.4 billion is associated with Sites 1 through 3, which would only happen if the underground expansion of Penn Station receives federal approval.¹⁸

It is reasonable to assume little change in the property use in the absence of the Penn Station Area Project going forward, as historically there has been little new construction in the area. In the 16 block area in and immediately surrounding the project area—about 270 property lots—only 18 new building construction permits have been issued in the past 20 years; none of these new building permits were on the same blocks as the eight development sites.¹⁹

Other Tax Revenue Considerations. ESD's plans include the possibility of payments in lieu of sales tax (PILOST) and payments in lieu of the mortgage recording tax (PILOMRT) as revenue streams to pay for the Penn Station Area Project. In the no-development case, by definition, there would be no related construction sales tax revenue generated and, therefore, no loss from the city's revenue baseline. The city would lose MRT revenue for mortgages that would have occurred in the absence of the proposed ESD development. IBO lacks the data quantify this impact; however, given the small share of the city tax parcels included in the project, we would not expect it to have a large effect on the city's baseline MRT revenue. Unlike the property tax, however, ESD has not indicated whether it would make the city whole for the MRT revenue it would have received in the absence of the development.

Potential Costs for Capital and Expense Budgets. The area around Penn Station is already integrated into the city in terms of water and sewer service, curbside refuse and recycling collection, and other routine city services, although the greater density would cause greater rates

of usage. This is in contrast to Hudson Yards, which introduced a whole new section of Manhattan to routine city services. The city had to spend capital dollars to create open space improvements and upgrade water and sewer connections. In the case of Penn Station, the creation of the three proposed shared streets would be coordinated with the city's Department of Transportation, although whether the city would be responsible for the ongoing maintenance is unclear. Some shared streets elsewhere in the city are maintained through local Business Improvement Districts or community-based organizations.

City-led Rezoning of Area Surrounding ESD Development Sites Could Boost Property Taxes.

Under the proposed plan, ESD would override city zoning rules and the city's Uniform Land Use Review Procedure (ULURP). This would allow for taller buildings than current city zoning permits for eight sites, currently comprised of 55 property tax lots. New York City would maintain control of zoning elsewhere in the area. The city, in theory, could decide to rezone a larger area around Penn Station through ULURP to bring zoning for the surrounding area closer in line to what ESD is proposing for its eight sites. If city-led upzoning spurred new development, this potentially could yield more valuable properties and therefore more property tax revenue for the city. Changes in zoning coupled with major transit improvements would make the area more attractive to developers than it has been for years, although development is far from guaranteed. To date, New York City has given no indication of plans to rezone this area.

Potential for Positive Revenue Impacts from Personal Income and Sales Taxes.

ESD projects the Penn Station Area Project's development of Sites 1 through 8 would employ some 89,800 direct and indirect "person-years" in construction-related jobs; nearly 85 percent of these jobs would be based in New York City.²⁰ (Person-years measures employment over a period of time. One worker employed on a full-time basis for five years is counted as five person-years.) ESD further estimates that the completed development would host 59,300 employees. These person-year employment estimates predate the Hochul Administration's proposed GPP revisions, which reduced the square footage of commercial space in the new developments. Estimates of construction employment for the transit components of the project were not included in the Draft Environmental Impact Statement, as the MTA will be taking the lead on the transit construction projects and will put forth its own employment estimates separately. For the proposed development around Penn Station, so long as at least some of these are new jobs and not just

relocations of workers from elsewhere in the city, the Penn Station developments would have a net positive impact on personal income tax receipts for the city and the state.

The creation of new, attractive retail spaces may have positive impacts on the city's sales tax receipts. Multiplier effects of induced economic activity through construction materials, supplies, transportation, among other areas, may also produce potential benefits to the city beyond income and sales tax directly tied to the Penn Station Area Project. Because the Penn Station Area Project is in the planning stages still, and so little is known about project construction and future tenants, IBO is unable to estimate these ancillary impacts.

Consideration of Plan Alternatives

Taxing or Relocating Madison Square Garden. The Penn Station Area Project does not propose any changes to Madison Square Garden, which sits directly atop the existing Penn Station train complex. The Garden operates under a special zoning permit that allows for an arena on that lot. The permit is set to expire in 2023, and will be up for renewal by City Council.²¹ Madison Square Garden is another property for which New York City forgoes property taxes, but this time by its own devising. Under the Koch Administration, the city gave Madison Square Garden an annual tax exemption in perpetuity, presently valued at \$43 million annually. IBO estimates that the collective tax expenditure has exceeded \$875 million dollars (adjusted for inflation) since the exemption was granted in 1982.²² IBO views this as a conservative estimate of the foregone revenue, since—knowing the property has a full tax exemption—the Department of Finance does not have a strong incentive to accurately estimate the fair market value of the arena, which is the first step in determining the tax liability for the property.

This exemption is granted through state law and remains in effect unless the state amends the section of the law or the arena is no longer the home to professional major league basketball and hockey teams.²³ If the state were to repeal this exemption, the city could then collect Madison Square Garden's property taxes or the arena could enter into a PILOT agreement as an additional source of revenue for the Penn Station Area Project. Neither of these options are discussed in the GPP or related documents.

Several planning and civic groups have rallied to move the arena, which would enable more dramatic changes to Penn Station. In its current configuration with Madison Square Garden above, Penn Station reconstruction plans

Proposed Development Would Be Mainly a Mix of Commercial, Hotel, and Residential Space



SOURCE: Empire State Development

must account for structural support of the arena, putting constraints on the station redesign and limiting options to build a grand station entrance at street level. Nevertheless, both ESD and the railroads are seeking to advance the Penn Station Area Project without moving Madison Square Garden. ESD cited three main barriers to relocating the arena: the urgent need to finish renovations before the completion of the Hudson River Tunnel; the limited window to take advantage of federal infrastructure funding; and the estimated \$8.6 billion cost of buying out, demolishing, and relocating the arena.²⁴ Additionally, relocating the arena would not increase track or platform capacity for trains serving Penn Station. ESD has emphasized that the Penn Station Area Project would not preclude moving Madison Square Garden in the future.

New York City Rezoning in Lieu of ESD Development.

Earlier, IBO discussed the potential for addition revenue if the city were to rezone a larger area around the ESD development. Another possibility would be for New York City itself to rezone the entire neighborhood with no involvement by ESD. There would be several key differences from the financing plans laid out in the GPP. New York City would collect property taxes as usual and the state would have to identify other revenue streams to pay for the Penn

Station Area Project components. Alternatively, the city itself could enter into agreements with buildings in the rezoned area to divert revenue towards the transit projects, similar to what ESD is proposing for Penn Station, or to what the city did for the Number 7 subway extension to Hudson Yards. If the city were to initiate PILOTs, however, any shortfalls in PILOT revenue would likely then be borne by the city. (In contrast, under ESD’s proposal, it is not clear which level of government would be obliged to pay if PILOT revenues prove insufficient.) The zoning of the eight development sites and 1 Penn Plaza would remain within the purview of New York City. The city’s ULURP process would be in effect for those eight sites—in contrast to ESD’s ability to override existing zoning right away. The ULURP process would provide a formal voice for Community Boards, the City Council, and local residents to weigh in on zoning changes, but would also extend the project’s timeline. Neither the de Blasio or Adams administrations have publicly expressed any interest in the city of New York financing the Penn Station renovations or expansion itself.

Future Demand for Proposed Real Estate Development

For value capture to provide a reliable stream of revenue, there must be sufficient demand for the project’s office,

hotel, and residential space when these buildings are completed. As noted previously, under the current draft timeline, all of the Penn Station Area Project developments are expected to be completed by roughly 2044. In the wake of the pandemic, the Hudson Yards Infrastructure Corporation hired Cushman & Wakefield to perform a new development and real estate study as part of refinancing its existing debt.²⁵ This study, released in September 2021, forecasts rents and property tax assessments in the Hudson Yards area from city fiscal year 2023 through fiscal year 2047. It concluded that future demand for premium office space, hotels, and housing in New York City would rebound from the effects of the pandemic and remain strong in the long term. This assessment, while more likely optimistic than pessimistic, is not out of line with IBO's own more near-term forecast of the local economy and real estate projections.

Demand for Commercial Office Space. Up to nine of the 10 buildings in the Penn Station Area Project may include office space—the majority of the proposed development. Following the pandemic and the switch to greater use of remote and hybrid work, there has been much concern about future demand for commercial office space in the city. While asking rents declined during the pandemic and availability rates shot up, there have recently been signs that the market for commercial real estate has rebounded, at least in the short run. IBO has found that commercial rent tax revenues (levied on the value of certain commercial property leases in parts of Manhattan) have remained resilient throughout the pandemic, suggesting that commercial tenants are generally maintaining their leases and paying their rents. Over time, however, if expiring leases are not renewed, or renewed for less space, tax revenue would likely decline. An additional positive sign: in January 2022, the Department of Finance largely reversed a decrease in value it had forecast for the city's commercial properties just a year earlier, as the pandemic has had much less severe near-term impact on rental income than anticipated.

The Penn Station office development is planned to be Class A, or premium, office space. Class A office buildings have fared better in terms of rents and occupancy during the pandemic, as they are often leased by large companies as flagship locations—an office presence these companies would like to continue even if the pandemic causes some permanent shifts towards more remote work. The Cushman & Wakefield report, commissioned for Hudson Yards, found that new leases since the pandemic have been primarily in Class A office space, indicating a “flight to quality.” According to their analysis, most of the impact of any long-term shifts in office workers moving to remote work is expected to

hit older office Class B and Class C buildings with fewer amenities. While IBO's forecast assumes only a modest change in demand for office space at least in the next five to 10 years—the period as the proposed towers around Penn Station will be under construction—there certainly is a risk of a larger and quicker shift in work arrangements in the longer term once buildings are complete.

Possible Hollowing Out of Existing Office Space. The introduction of millions of square feet of new Class A commercial office space brings up questions not only about whether there would be sufficient demand for the new space due to changing work caused by the pandemic, but also about the value of existing commercial office space. Several major office tenants in Hudson Yards relocated from other parts of the city, primarily the Financial District downtown and central and east Midtown, indicating that new office districts in the city can draw from existing office areas elsewhere within the city. While the Cushman & Wakefield study done on behalf of HYIC included discussion of the renovation of Penn Station as a draw for potential tenants, it did not consider the impact on Hudson Yards from an increase of Class A office space in its backyard through the Penn Station Area Project.

IBO examined property income associated with Class A office space before and after office space at Hudson Yards was built to see if the introduction of Hudson Yards led to price changes in other high-end office markets, in particular, Midtown East's Plaza District. Our results were inconclusive, however. Because Hudson Yards just started leasing office space in 2017—and then the pandemic began relatively shortly after in 2020—the full extent of the impact of Hudson Yards leasing on other areas of the city is still unknown.

While we could not draw any definitive conclusions on how Hudson Yards impacted other Class A office space, or know how the proposed Penn Station Class A office space would similarly play out, the latter development would be particularly attractive in terms of location and transit accessibility. Given the number of direct commutes straight to these buildings—NJ Transit, Long Island Rail Road, soon Metro-North, PATH trains, and city subways—this could be an even more desirable location for companies that wish to attract or retain an in-office staff by offering shorter, easier commutes.

What PILOT discounts, if any, would be given to Penn Station Area Project developments may also play into how competitive it is compared to other similar buildings that

provide discounts in nearby Hudson Yards. Any downward pressure new commercial office space may have on other existing commercial office space, could in turn negatively impact the city's property tax collections, as the Department of Finance uses building income (consisting mainly of rents) as one of the components for calculating the tax base for commercial office buildings.

Residential Real Estate. In a change from what the Cuomo Administration had originally proposed, Governor Hochul's development plan includes up to 1,800 residential units as part of the Penn Station Area Project. One third of the residential units would be set aside as affordable housing, although the level of affordability planned for the units has not been announced. The reduction of planned commercial office space and requirement of residential housing was a response to community input; it also serves to diversify the uses of the planned development to spread out the risk, given the greater uncertainty around the impact of the pandemic on the commercial real estate. The residential real estate market took a nosedive in 2020 due to the pandemic, but since has rebounded. IBO has found that low mortgage rates and pent-up demand from the first year of the pandemic led to an all-time high in residential sales in 2021, and rents are approaching pre-pandemic levels. Again, the convenient, transit-rich location and amenities that come with new construction may make the market-rate housing at the Penn Station developments particularly attractive. Demand for affordable housing is strong in the city, so interest in below-market units should also be robust.

Hotels. Under Governor Hochul's revised plan, the amount of proposed hotel space would be reduced from two sites to one. Before the pandemic struck, the city's tourism and the closely allied leisure and hospitality industries were a major part of the local economy. IBO's forecasts have found that while restaurants, bars, and entertainment venues have re-opened, full recovery in these industries depends in large part on the return of international tourism and business travel. Although hotel occupancy has started to inch upwards, IBO's near-term five-year forecast does not expect business travel in particular to return to pre-pandemic levels, and that the pandemic will have a long-lasting impact on business travel, for which hotel space near Penn Station would be a prime location. IBO's forecast, however, expects general economic growth and pent-up demand for leisure travel to further fuel tourism. Where demand for hotels will be by the time the Penn Station hotel development would be ready for occupancy—at least eight to 10 years out—remains hard to predict.

Recent changes to city zoning rules have made development of new hotels in the city more difficult. In December 2021, New York City amended the city Zoning Resolution to now require the construction or expansion of hotels in higher-density commercial or mixed-use areas to go through the Uniform Land Use Review Procedure (ULURP) to receive a special permit—requiring a time-intensive review before new hotel capacity can be developed. This change is expected to reduce the supply of new hotels in the city.²⁶ Because the state's plan includes the suspension of city zoning rules for the eight development sites, however, the hotel planned for the Penn Station Area Project would bypass this change.

Looking Down the Line

The planning around the Penn Station Area Project remains a work in progress, and IBO expects future revisions and additional information to be released as the project proposal makes its way through the review process. Public hearings and comment periods on the Penn Station Area Project wrapped up in February 2022. Next, ESD will review and respond to any substantive public comments, and then anticipates presenting a Final Environmental Impact Statement and modified GPP to its Board of Directors for approval this spring or summer. The modified GPP (if affirmed by the ESD board) and final Environmental Impact Statement (if accepted by the board) would reflect the proposed revisions put forth by the Hochul Administration last fall as well as input from public review of the project.

While New York State has presented a framework for financing the improvements and expansion of Penn Station's transit infrastructure, the draft GPP and supporting documents are just that—a framework—and not a full blueprint. ESD has indicated that each development site will negotiate individual site-specific PILOT agreements, but no overarching requirements or guardrails for those financing deals have been presented in the GPP. Many other key questions remain unanswered, particularly around the construction cost, timing, financing, and risk management of the projects. Without this information, a rigorous analysis of the project is not possible—and such analysis is a necessary step for a plan that could impact city and state taxpayers for years to come. Few would dispute the need to improve Penn Station, and any comprehensive overhaul of the transit hub will have long-reverberating changes to New York City's transit landscape. The proposed value capture financing, however, requires much further detail in order to be evaluated both in terms of risks and benefits to the state and the city, as well

as weighing it against other ways Penn Station transit improvements might be financed.

Furthermore, New York State is only one of multiple government partners with a stake in the Penn Station Area Project. The transit infrastructure components involve cooperation with New Jersey, the federal Department of Transportation, Amtrak, the MTA, NJ Transit, and the Port

Authority of NY and NJ, among others. The state of New Jersey and other partners also need to be more transparent about how they plan to finance their portions of Penn Station improvements to allow for a more complete picture of how likely this project is to be fully funded beyond just New York State's contributions.

Prepared by Sarah Stefanski

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Appendix: Further Considerations

Introducing Through-Running Trains at Penn Station.

A frequent topic of discussion relating to Penn Station is whether the train complex can be configured to accommodate through-running, which advocates say would reduce or eliminate many of the overcrowding problems at the platform level. Through-running refers to train station operations in which trains entering a station continue moving in the same direction to exit the station, thereby remaining in service. This is in contrast to how Penn Station currently operates as a terminal station for regional commuter rail service; Long Island Rail Road and New Jersey Transit trains must unload all passengers and then either reverse direction to exit the station or continue to a railyard. This process requires more time at the platform (“dwell time”) than running service through the station, and also adds to the layover time spent in a railyard. Commuter service operates this way because Penn Station was originally designed to serve as an intercity hub, with only a portion of trains traveling through to other cities as they still do for Amtrak’s Northeast Corridor service.

Through-running can increase a station’s capacity by reducing dwell times, primarily through eliminating track crossing conflicts that occur when trains reverse course to exit the station. Reducing railyard layover time increases the amount of time a train is available to provide revenue-generating passenger service. Finally, through-running opens the possibility of one-seat regional trips; for example, a through-running model at Penn Station would allow for a no-transfer connection between New Jersey and Long Island.

Some through-running advocates see potential capacity improvements for the existing train station as a way to bypass the need for expanding the station southward, and to that end, it is expected to be studied as one of the

alternative scenarios in the environmental review of the proposed Penn Station expansion. While through-running is a more efficient way to operate high-volume commuter stations, there are several barriers to its introduction at Penn Station. The railroads serving Penn Station (MTA, Amtrak, and NJ Transit) oppose commuter through-running as infeasible in the existing station. They specifically highlight three main challenges:

1. Station platforms are too narrow and stairs and elevators between platforms and the train hall above are too limited to accommodate simultaneous loading and unloading of passenger trains.
2. Only 12 of the station’s 21 tracks could accommodate through-running, which would limit any increases in capacity to levels that fall short of projected demand in 2038. The four southernmost tracks are stub tracks that MTA argues are infeasible to extend for through-running, because they would require grade reductions to avoid the Sixth Avenue subway lines that are too steep for NJ Transit train cars. The two northernmost tracks end in the West Side yard and cannot connect to cross-Hudson tunnels. The remaining three tracks were ruled out for unspecified “operational reasons.”
3. Modifications to Penn Station’s platforms and tracks would cause untenable service disruptions in a station that has already been operating above maximum capacity.

Without the transit providers at Penn Station on board, through-running for the existing Penn Station seems unlikely even if the engineering were found feasible. The railroads instead support the expansion of Penn Station to the south in a way that could accommodate the introduction of through-running in the future.

Endnotes

¹Penn Station Master Plan: A Joint Effort of Amtrak, NJ Transit, and the MTA. MTA Board Briefing, April 21, 2021. [37416 \(mta.info\)](#).

²For this paper, IBO reviewed the February 2021 Empire Station Complex Civic and Land Use Improvement Project General Project Plan and ESD's proposed revisions to the project, retitled as the Pennsylvania Station Area Civic and Land Use Improvement Project. We also reviewed other supporting documents, including but not limited to: [December 2020 Final Scope of Work for the Preparation of an Environmental Impact Statement, February 2021 Draft Environmental Impact Statement](#), presentation documents and meeting minutes from the [Community Advisory Committee Working Group](#), as well as ESD's public hearings and press conferences held by state and local officials.

³See further details on stated goals in the February 2021 Adopted GPP, pages 12-13.

⁴While original estimates had the reconstruction cost estimates at \$6 billion, Governor Hochul at a [press conference](#) in November 2021 presented a \$6 billion to \$7 billion estimate.

⁵This differs from the city's Hudson Yards project, where a zoning district was established encompassing all of the lots in the district.

⁶Under the most recent proposal, shared streets are proposed for 31st Street between 7th and 8th Avenues, 32nd Street between 6th and 7th Avenues, and 33rd Street between 6th and 9th Avenues.

⁷The eight development sites are currently zoned as: C6-3X, C6-4, C6-4.5, C6-6, M1-5, M1-6, and R8B.

⁸IBO analysis of 2019 Quarterly Census of Employment and Wages data.

⁹ESD has not given any indication on whether the residential buildings would make tax equivalency payments, similar to how the city structured residential building payments in the Hudson Yards financing area.

¹⁰New York State 2018-2019 Fiscal Plan, S07509-C/A09509-C, Part MMM.

¹¹ESD "Funding and Financing Considerations" presentation and minutes from the Community Advisory Committee Working Group meeting on May 25, 2021.

¹²Sites 4 through 8 are owned by Vornado and are anticipated to be redeveloped by Vornado, making them a willing participant. In contrast, Sites 1, 2, and 3, may be acquired through eminent domain, a power which ESD holds. The Penn Station Expansion must go through a federal National Environmental Protection Act (NEPA) review, which will be commenced this year with the MTA as the lead agency. NEPA rules prohibit preemptively acting on an assumed review outcome, and therefore engaging with owners and tenants of potentially impacted properties prior to the completion of the Expansion Project NEPA review would risk the expansion project's eligibility for federal funding. Therefore, no approvals necessary for eminent domain will be initiated while the NEPA review is underway.

¹³February 2021 Empire Station Complex Civic and Land Use Improvement Project General Project Plan, page 14.

¹⁴While providing discounts of any sort on PILOTs is a deviation from the pure value capture framework, they are a common feature in practice.

¹⁵Hudson Yards also used revenue from the sale of density bonuses.

¹⁶Federal Transportation Infrastructure Finance and Innovation Act (TIFIA) requires an investment grade rating for the borrower in order to qualify for the loan. Railroad Rehabilitation & Improvement Financing (RRIF) requires borrowers to pay a credit risk premium between 0 and 5 percent, depending on the risk of defaulting on the loan. Bonds issued by ESD or the MTA would need to achieve an investment grade bond rating to attract investors.

¹⁷ESD "Funding and Financing Considerations" presentation to the Community Advisory Committee Working Group, May 25, 2021.

¹⁸IBO calculated this assuming the property tax levy for each lot would grow by the median growth of the levy seen from 2013 through 2022, a ten-year period. We also assumed 3 percent annual inflation. These property tax estimates do not include the portions of Manhattan tax block 783, lot 70 that will be redrawn to incorporate small portions of the current lot into Sites 4 and 5, as the majority of this lot is not included within the development sites.

¹⁹IBO examined the 16-block area bordered by Sixth Avenue and Ninth Avenue and West 29th Street up to West 35th Street.

²⁰Empire State Development, "Empire Station Complex Civic and Land Use Improvement Project Draft Environmental Impact State (DEIS)," February 2021.

²¹When the special permit for Madison Square Garden was last up for renewal in 2013, the City Council voted to extend it 10 years as a window in which the arena could relocate, as recommended by the City Planning Commission. The arena did not relocate, however, and currently meets the criteria for the permit to be extended again.

²²IBO only has parcel-level property tax information going back to 1984, so \$875 million is the expenditure estimate back to 1984.

²³Section 1 of L.1982, c.459.

²⁴ESD estimates included \$1.15 billion to buy out MSG and its unused air rights, \$3 billion to buy a new arena site, \$360 million to demolish existing structures on the new site, \$2 billion to build a new arena, \$75 million to demolish the existing MSG, and \$2 billion to reconfigure Penn Station after demolition.

²⁵The full Cushman & Wakefield report can be found as Appendix E in the October 21, 2021 bond Official Statement: [Hudson Yards Infrastructure Corporation \(msrb.org\)](#).

²⁶For more details on the Department of City Planning assessment of the impacts associated with this zoning change, see NYC [Hotel Market Analysis: Existing Conditions and 15-Year Outlook](#).