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FINANCIALIZING URBAN GOVERNANCE:  
CITIES, CAPITAL MARKETS AND PROPERTY TAX LIENS

By

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## ABSTRACT OF THE DISSERTATION

### FINANCIALIZING URBAN GOVERNANCE: CITIES, CAPITAL MARKETS AND PROPERTY TAX LIENS

By IRENE TUNG

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This dissertation investigates the growing integration between global capital markets and municipal finance. In the United States, financial activities make up an increasingly large proportion of overall economic activity, an expansion which is often referred to as financialization. One of the primary ways that financial markets have grown is through the transformation of various income streams into new financial instruments. In recent decades, financialization has drawn land, local governments and the built environment into relationships with capital markets in unprecedented ways. I examine a key and under-explored moment in the financialization of urban governance: the first experiments in municipally-sponsored property tax lien securitization beginning in the 1990s. Most cities that engaged in this form of financial engineering quickly abandoned it, with the notable exception of New York City, which has continued its tax lien securitization program for almost two decades. My study considers the experiences of these cities, how and why they undertook securitization, and the results of their efforts. Examining qualitative and quantitative data including ratings agency documents, private placement memoranda for tax lien backed securities, and the New York City Department of Finance annual lien sale lists, I contend that municipalities' varying experiences with

this practice can reveal important insights about what this form of financial engineering offers to local governments. Analyzing tax lien securitization transactions, I show how financial intermediaries relied on the accounting and legal idiosyncrasies of asset-backed securitization to adapt the technique for municipal sponsorship. However, given high transactional costs, tax lien securitization failed to provide viable policy and financing solutions for most local governments. This study suggests that the practice endured in New York City in part because it served to reconfigure the local government's capacities and institutions in ways that met its particular needs for centralized administrative control and regulatory arbitrage.

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### **List of Acronyms and Abbreviations**

ABS	Asset-backed securitization
CDBG	Community Development Block Grant
DEP	New York City Department of Environmental Protection
DOF	New York City Department of Finance
HPD	New York City Department of Housing Preservation and Development
HUD	United States Department of Housing and Urban Development
MBS	Mortgage-backed securitization
NYCTL Trust	New York City Tax Lien Trust
OMB	New York City Office of Management and Budget
TPT	Third Party Transfer Program
TIL	Tenant Interim Lease Program
TLBS	Tax lien backed securitization

## **Chapter One - Introduction**

In the United States, financial activities increasingly make up a large proportion of overall economic activity and generate a larger proportion of overall profits (Harvey, 1989; Brenner, 2002; Krippner, 2005; Leyshon and Thrift, 2007; Arrighi, 2010; French, Leyshon and Wainwright, 2011; Pike and Pollard, 2010). Technological advances and regulatory changes at every level of US government have made the expansion of the financial sector possible (Coval et al., 2009; Gotham, 2006; Krippner, 2011). One of the primary ways that financial markets expand is through the transformation of income streams from assets such as mortgages and credit card debt into new financial instruments. This expansion has relied on new techniques to "disaggregate and continually reassign ownership to allow for more and faster-paced exchanges". The term "financialization" has been used to describe these "institutional forms and the processes leading to them" (Weber, 2010: 252; Krippner, 2005; Leyshon and Thrift, 2007). In recent decades, financialization has shaped the contours of urban change, drawing municipal governments, urban land and the urban built environment into global capital markets in unprecedented ways (Weber, 2010; Botein and Heidkamp, 2013; Pacewicz, 2013; Ashton, Doussard and Weber, 2014).

This dissertation focuses on how this process of financialization has impacted urban governance in the United States. I examine a key moment in the financialization of

urban governance: the first experiments in municipally-sponsored securitizations. These began in 1993 when Jersey City, New Jersey securitized \$44 million dollars in property tax liens. Several other cities including New Haven, New York City, and Philadelphia sponsored similar tax lien securitization transactions shortly thereafter (Alexander, 2000). Most of the localities abandoned their programs after their first attempts failed to meet their expectations. My study considers the experiences of these cities, how and why they undertook securitization, and how their efforts did or did not meet their needs.

My research focuses in particular on New York City, the only locality that currently engages in this practice. Many have lauded New York City's transformation over the last thirty years from the fiscal collapse and large-scale housing abandonment to a city with relatively sound finances and ever-increasing real estate prices. Some commentators have pointed to changes that Mayor Rudolf Giuliani made to New York City's policy on tax-foreclosed properties in the 1990s as a turning point in that history (Salama, Schill and Roberts, 2003). Beginning in the 1970s and during a period of extreme housing abandonment and vacancy, the City assumed ownership of tax-delinquent properties in unprecedented numbers. In subsequent years, the City transferred some of that property into private hands (including limited equity cooperatives and affordable housing in partnership with non-profit and for-profit housing developers), but for a variety of reasons also retained ownership of more properties than it had originally anticipated. By the 1990s the City was the largest landlord in New York City. It owned and managed thousands of multi-family residential buildings, many in moderate to severe states of physical deterioration and largely occupied by low-income tenants of color (Braconi, 1999; Saegert and Winkel, 1998).



The Giuliani administration continued the efforts of prior administrations to reduce the stock of city-owned and managed properties (Polner, 2005). But the administration also went further by proposing that the City would no longer take title to tax delinquent properties in the future, and would instead sell property tax liens for a majority of these properties. For a subset of distressed residential properties, the City would not sell liens, but would transfer the properties to new private owners for rehabilitation, without ever directly taking title. According to the administration, this new approach would ensure that the City would no longer become a landlord of last resort (City of New York, 1995). While New York had sold property tax liens in the past, the Giuliani administration planned to use a different process. Similar to what Jersey City had done a few years prior, the City would use the financial technique of securitization to repackage tax liens into bonds which would then be sold to institutional investors. While all of the other localities that also sponsored tax lien securitizations abandoned their programs, New York has continued to securitize its property tax liens for almost two decades. Since the first securitization transaction in 1996, New York City has securitized over a billion dollars in liens for property taxes and other municipal charges.

## **1.2. Problem Statement**

While there are rich bodies of literature on financialization and neoliberalization, there are few empirical studies which explicitly articulate the dynamics between these processes at the urban scale. I seek to further elucidate the mechanisms through which the processes of financialization and neoliberalization worked through and against each other

in cities. Studying the first experiments in municipally-sponsored securitizations will allow me to address the following gaps in the literature:

1. First, the specific pathways of financial integration in urban governance, and the reasons for those particular pathways are still relatively unexamined. Without close study of historical contingency, the process of financial integration takes on an unwarranted teleology (van der Zwan, 2014). Examining why and how *particular* municipal assets were first targeted, my study demonstrates how new applications of financial integration are highly path-dependant, relying upon contextual embedding in the pre-existing practices of specific localities.

Furthermore, there is little research that examines applications of municipal financial engineering that proved unviable, and compares them to applications that endured. Which arrangements endured and why? What were the outcomes of local governments' attempts to use financial engineering to help them manage risk and uncertainty? What were the limits of early attempts of local governments to create new subjectivities for themselves in an evolving financial landscape? By examining both enduring, and non-enduring experiments in municipally-sponsored securitization, this study helps to delineate not only the key role the local state plays in making securitizable assets legible to investors (Newman and Wyly, 2004; Fox Gotham, 2006; Ashton, 2010; Weber, 2010), but also the role it plays in ensuring the viability of new financial instruments. Additionally, in my case study of New York, I go further by exploring how state action in the service of these ends can itself be the product of political negotiation and fragile compromise. Examining the actual mechanisms on which financial integration

relied demonstrates how the process is much more idiosyncratic than universalizing and uniform, and relies on more than just the availability of new income producing assets.

2. Second, existing research has documented the increasing degree of integration between global financial markets and local governments (Weber, 2010; Botein and Heidkamp, 2013; Pacewicz, 2013; Brash, 2011). However, much of this literature does not differentiate between different kinds of capital, and the distinct relationships with local governments that arise as a result of such differences. Investigating changes in tax lien practices, I explore differences in *which* kinds of capital sought integration with local governments and *how* local governments were differentially integrated into capital markets.

3. Third, while a large body of scholarship debunks the notion of state retreat in the process of neoliberalization and in the transition to Post-Keynesian state forms (Clark and Dear, 1984; Lake, 2002; Jessop, 2002; Brenner, Peck and Theodore, 2010; MacLeod, 2012; Gilmore, 2007), there is little research that explores the role of financial engineering in reconfiguring state power and developing new state capacities at the urban scale. The few studies that do exist focus largely on local governments' needs to relieve fiscal stress, or on their endeavors to channel capital into particular places or projects (Weber, 2010; Botein and Heidkamp, 2013; Pacewicz, 2013; Brash, 2011; Marchiony, 2012; Roin, 2011; Gelfand, 1996; Sbragia, 1996; Ashton, Doussard, Weber, 2014).

My research explores how financial integration offered more than simply access to new and greater quantities of capital for local government. I show how it also offered institutional forms and logics which had the effect of regulatory and political arbitrage, allowing city government to reassert and centralize control over policy and public

expenditure. In the case of tax lien securitization, this control of public expenditure allows local government to borrow and spend more in the years of economic downturn, thus enhancing counter-cyclical state capacity. As such, greater integration between local government and global financial markets had the effect of replacing political and regulatory constraints with new financial liabilities. While local governments can use financial engineering to gain a greater ability to control outcomes and protect their interests, they do so with minimal public oversight and little public understanding of their role in such arrangements.

4. Finally, there is a significant literature that focuses on neoliberalization in New York City in particular (Fitch, 1994; Fainstein, 2001; Sites, 2003; Moody, 2007; Angotti, 2008; Brash, 2011). Much of this work details the role of the local state in shepherding the dramatic ascent of the city's real estate market after its high-profile fiscal crisis in the 1970s. With regard to the city's role in delinquent property enforcement and housing development, most of the New York City literature foregrounds the battles over city-owned tax-foreclosed housing throughout the 80s and 90s in the context of changing real estate market conditions and makes only passing reference to the City's critical shift in property tax enforcement policy in 1996.

My work aims to fill this gap by exploring the actual mechanisms by which the complex history of the City's struggle with housing abandonment, arising from various local and extra-local circumstances such as long-term structural racism, federal disinvestment and deindustrialization, was recast into a narrative about municipal dysfunction, a narrative that persists nearly two decades later. I aim to show how that narrative in turn provided the political momentum necessary for the City to obtain legal

authorization necessary for tax lien securitization. As such, I document how the legacies of structural racism, in part, drove the production of a new financialized form of governance to which all New Yorkers then became subject. In sum, my project aims to shed light on the material and ideological conditions shaping New York City's foray into this particular form of financial engineering, and its attendant consequences for the City.

### **1.3. Research questions**

In order to address the issues outlined in the above problem statement, I ask three sets of empirical research questions. First, why and how did certain localities decide to sponsor tax-lien securitizations beginning in the 1990s? How did this relate to broader trends around municipal asset and service privatization? I delve deeper into how and why some local governments connected tax liens sales to broader financial markets and how and why financial institutions became involved in the tax lien industry. I am interested in better understanding what the various stakeholders hoped to achieve and why their involvement may not have met their expectations. As such, I am interested in understanding how and through what mechanisms, institutions, relationships, forms of knowledge and technologies market makers attempted to integrate tax liens into broader capital markets. How were financial institutions, that act as long-time creditors of local governments, involved in facilitating that change? Why did performance ultimately not match the expectations of municipalities, financial institutions and investors? Why was New York City's situation exceptional?

With respect to New York City, how did its tax lien securitization program develop given particular historical and political circumstances? What kind of ideological

work on the part of the state and industry actors was necessary to make these changes possible? How did efforts to enact tax lien securitization relate to the City's earlier responses to large scale housing abandonment in the 1970s and 1980s? How were the particular needs of New York City different from those of other cities that decided not to continue sponsoring securitizations, and how did securitization meet those particular needs? I investigate the particular circumstances shaping the form that tax lien securitization took in New York City.

The second set of questions investigates the shifts in New York City's tax delinquency policy within the context of trends in financial integration in local governments and the transition from Keynesian to post-Keynesian state forms. How did New York's tax lien securitization program evolve with respect to various constraints that New York City has faced? What are the various components of the securitization process and what does each accomplish for New York City? How does securitization restructure ownership, assets and debts? Who are the actors in the transaction, what are their roles and how do they benefit from their participation? How does securitization compare to other financing options available to New York City? How can we understand financial engineering in relation to other older governance forms used by New York City? I critically examine the various steps, actors and entities involved in securitization to unpack how this form of financial engineering restructures ownership, and what the implications of that restructuring are for governance.

The third set of questions interrogates the record of New York's tax lien securitization program with regard to property tax enforcement. What trends are identifiable in the kinds of properties which have liens sold? How have collection rates

faired? What factors have impacted collections on delinquent property taxes and property taxes in general? How do New York City's tax delinquency rates compare to other cities? How has tax lien securitization impacted people and the neighborhoods in which they live? What neighborhoods are most impacted by tax lien sales in New York City? I investigate the various outcomes related to New York's tax lien securitization program and what the consequences have been for the City.

#### **1.4. Data and methods**

In this dissertation, I used a mixed methods approach. I combined primary data from semi-structured interviews with secondary data from archival research and quantitative datasets, which allowed me to triangulate data sources and findings.

##### ***1.4.1. Case selection***

I selected New York City from 1992-2011 for a number of reasons. First, of the various localities that experimented with municipally-sponsored tax lien securitization beginning in the 1990s, New York City is the only city that has chosen to continue this practice. Thus, studying this case provides an opportunity to investigate the factors that made New York City's experience different than that of other cities. Second, the amount of variation within the New York City housing market provides rich material to compare the ways that tax lien securitization affects different constituencies. New York City's housing landscape includes homeowners, a vibrant public and private affordable housing infrastructure, private market rate landlords and housing developers of various sizes. Finally, a rich body of past scholarship about racial disparities in housing in New York

City allows me to identify continuities, discontinuities, long-term trends, patterns, and geographical expressions.

Social science theorist Bent Flyvbjerg lays out a typology of case study sampling with four different categories: "extreme/deviant cases"; "maximum variation cases"; "critical cases"; and "paradigmatic cases". Cases are selected on the basis of expectations about their information content. Using his definitions, I envision a case study of tax lien securitization in New York to be useful as an extreme/deviant case. Extreme/deviant cases are selected "to obtain information on unusual cases, which can be especially problematic or especially good in a more closely defined sense" (Flyvbjerg, 2006: 230).

While I will briefly address longer historical trends in tax lien investment in New York and the United States, the empirical portion of case study will focus on the years 1992-2011. My selected time period will thus capture the early 1990s recession, the mid-1990s expansionary period, the recession in the early 2000s, the run-up to the recent housing bubble and the aftermath.

#### ***1.4.2. Archival sources and document collection***

I searched historical documents including news articles, publications by non-profit organizations and investor publications to provide context about the evolution of practices and discourses related to tax sales over the last century in New York. I made use of the LaGuardia and Wagner Archives at Fiorello H. LaGuardia Community College/CUNY in Long Island City, Queens whose holdings include the personal papers and official documents of former Mayor Rudolf Giuliani. This yielded hundreds of



documents about decision-making including internal memos between the Mayor's office and various agencies, meeting notes and minutes.

For information about current practices, I examined sources including finance and legal journals, journalistic accounts, industry press releases, government press releases, JP Morgan's private placement memoranda for securitized bonds, minutes from public meetings, court cases, language from local and state statutes governing tax sales, City council committee reports, and correspondence between the Office of Management and Budget and the Securities and Exchange Commission. I also examined media coverage and hearing testimony from the 1996 passage of Local Laws 26 and 37 (permitting changes in the city's tax sale practices) and from the renewal and amendment of these laws in the intervening years. I also examined documentary sources including finance, public administration, and legal academic journals, journalistic accounts, industry and government press releases, statutory language, proceedings from public meetings and hearings, and industry publications.

#### ***1.4.3. Interviews***

I conducted semi-structured interviews with employees of the City, financial institutions, community organizations, legal service agencies, and non-profit housing developers. I began my interviews with key participants and used a snowball sampling methodology. I first attempted to speak with people who have been quoted in the press or have testified publicly about the issue. I attempted to triangulate my data so that at least two other sources confirm statements made by any one interviewee. I sought additional interviewees until I reached data saturation and no new or relevant information emerged.

(Appendix D contains interview protocols.) Every participant gave either verbal or written informed consent to participate in the study as a confidential subject. A majority gave permission to be audio recorded (the study was approved under IRB # 12-507M).

All of the interviews lasted from between 15 minutes and 2.5 hours, with the average being around 45 minutes. I conducted a total of 24 interviews which included 11 interviews with property owners delinquent on their property taxes, five interviews with City officials involved in the program, two interviews with non-City employees involved in the program and six interviews with staff members of non-profit and legal service organizations.

In the semi-structured interviews, I asked a series of open-ended questions. If the respondent found it difficult to answer a particular question or provided only a short response, I would encourage the interviewee to consider the question further. I would ask the respondent to elaborate further, or ask additional questions about a topic introduced by the respondent.

#### ***1.4.4. Quantitative data analysis***

I compiled data on New York City property tax liens, water and sewer liens, Emergency Repair Program liens and Alternative Enforcement Program liens from the New York City Department of Finance lien sale lists for various years. I also compiled data from tax valuation rolls for various years, ratings agencies reports, private placement memoranda for tax lien backed securities and New York City general obligation bond issuances.

I analyzed data from ratings agency reports and private placement memoranda to identify trends in overcollateralization, interest rate spread and lien-to-value ratios. I analyzed lien sale lists to determine sizes of debts for Class 1 and 2 properties. In order to calculate rates of lien sale per neighborhood, I used ArcGIS to geocode both liens sold and the entire Class 1 tax valuation roll. I joined each data table to Census tract and neighborhood shapefiles. Dividing liens per thousand Class 1 taxable properties in each neighborhood, I generated a map showing percentage rates of Class 1 liens sold. Neighborhoods in the bottom quartile with regard to numbers of Class 1 properties were excluded. Rates were mapped using natural breaks. I then compared the ten neighborhoods with the highest lien sale rates to neighborhoods with rates of sub-prime mortgages and high foreclosures, according to an analysis done by the Office of the New York State Comptroller.

Finally, I analyzed administrative data from private lien servicers for the 2004 lien sale for the years 2004-2011 to produce descriptive statistics on rates and speeds of payment and foreclosure. Data were only available for properties serviced by the company Xspan. Data for properties serviced by other companies during this period were not available.

## **1.5. Outline of the dissertation**

This dissertation is organized as follows. In Chapter 2, I situate this research within several relevant bodies of literature including literatures on financialization, neoliberalization and urban public finance. Chapter 3 examines how local governance financialization unfolded, looking at the evolution of asset-backed securitization in the

1990s and its concurrence with difficult fiscal circumstances facing local governments. I interrogate how and why tax liens were the first site for experimentation with municipally-sponsored securitization and demonstrate how these early projects relied on certain pre-existing discursive mechanisms regarding debt sale and privatization. Documenting the successes and failures of municipally-sponsored lien securitization programs, I delineate differences between the categories of capital that sought integration with local governments and examine how various local governments were differentially integrated into capital markets.

After laying out the national landscape as context, I conduct an in-depth case study of New York City. In Chapter 4, I examine in detail the factors that led policymakers in New York City to choose the path of tax lien securitization. Tracing the history of the City's programs for tax delinquent property from the late '70s to the '90s, I explore how and why political support for those programs dissipated. Within this context, I document the ways that actors in New York City made tax lien securitization possible, and explore how shifts in tax delinquency policy evolved in the context of particular political, policy and regulatory constraints.

Chapter 5 elucidates how and why securitization has allowed the City to continue to play a central role in both managing and funding its tax delinquent property program while maintaining a low profile. I revisit the political, policy and regulatory constraints facing the City and the mechanisms by which it was able to marshal financial engineering to address those constraints. I show how in addition to simply offering greater access to capital, financial engineering also offered institutional forms and logics which allowed city government to reassert and centralize control over policy and public expenditure

while reducing transparency and public accountability. This had the effect of enhancing state capacity in a variety of ways and replacing previous political and regulatory constraints with new financial liabilities. I contrast New York City's experience with that of other cities that embarked on lien securitization programs, all of which ultimately abandoned their programs.

Chapter 6 evaluates various outcomes of New York's tax delinquency program. I investigate the extent to which New York City and its partners were able to successfully construct a market for tax-lien backed securities, and meet revenue goals. I discuss various factors affecting collection rates and evaluate New York City's practices in comparison with other cities that have pursued different policies. Finally, I identify trends in the characteristics of tax delinquent properties including size of delinquency and geographic incidence.

In Chapter 7, I conclude by discussing how the case of New York City's tax delinquency program offers new ways to understand financialization, privatization and the municipal state.

## **Chapter 2 - Perspectives on financializing urban governance**

In this chapter, I situate the dissertation in a set of literatures from human geography and other social sciences. Various perspectives from geography, urban studies, sociology, history and political science are useful for understanding the phenomenon of tax lien securitization in context. In developing my project, I have found three overlapping bodies of literature particularly helpful. The first is literature on financialization, the second is on the neoliberal city, and the third is on the financializing urban state. I draw from each of these literatures to understand the actual mechanisms through which the local state shapes and is shaped by financialization.

### **2.1. Pathways of financialization**

Scholarly work from various disciplines has employed the concept of financialization to describe changes over the last several decades in the advanced political economies. The literature on financialization interrogates how global finance has transformed the "underlying logics" of the economy (van der Zwan, 2014:1). No longer focused primarily on providing credit for industrial production, financial activities have increasingly represented a larger proportion of overall economic activity and generated a larger proportion of overall profits in the US economy (Harvey, 1989; Brenner, 2002; Krippner, 2005; Leyshon and Thrift, 2007; Arrighi, 2010; Scharfstein and Greenwood, 2012; Callon, 1998; Brenner, 2002; MacKenzie, 2006; McNally, 2011; French et. al., 2008; Stein, 2010).

Scholars have shown that the US state ushered in the conditions for financialization in its attempts to resolve parallel social, fiscal and legitimation crises that it was facing beginning in the late 1960s (Krippner, 2012; O'Connor, 1973; Habermas, 1976; Epstein, 2005; Froud et al., 2006; Krippner, 2005). Land, especially urban land markets, played a key role in the process of financialization, with property owners increasingly treating property and land as a financial asset (Harvey, 1974; Haila, 1988; Haila, 1991; Beauregard, 1997; Charney, 2002), and attempting to “unlock” financial value “trapped” within property (Christophers, 2010). Using mortgage lending, financial institutions connected global capital markets to place in urban neighborhoods (Wyly, 2004; Newman, 2009).

Financial integration creates new incentive structures that propel its expansion (McCoy and Engel, 2011; Lapavistas and Powell, 2013). For example, as the subprime mortgage market expanded in the 2000s, mortgage lenders stopped "securitizing [loans] in order to lend". Instead they started to "[lend] in order to securitize" (MacKenzie, 2011: 30; Pacewicz, 2013). The use of securitization which began with the secondary mortgage market soon expanded beyond it, as financial intermediaries sought more and varied income streams to integrate into global circuits of capital (Leyshon and Thrift, 2007). My work extends the work of scholars showing how social and spatial relations have shaped the contours of new financial market expansion (Pryke and du Gay, 2007; Thrift, 2001; van der Zwan, 2014).

A subset of the financialization literature examines the assimilation of public goods into financial markets (Ashton, Doussard and Weber, 2010; Ashton 2009; Botein, 2013; Pacewicz, 2013; MacKinnon, 2000). Finance capital and financial institutions

have long played a critical role in structuring public priorities in cities during good times and times of fiscal crisis through threatening to withdraw credit, lower bond ratings or shifting the projects for which they are willing to make loans (Tabb, 1982; Gurr and King, 1987; Shefter, 1985 Hackworth, 2002; Gilmore, 2007). The role of financial intermediaries evolved as they increasingly facilitated the production of new financial commodities backed by public assets (Dymski and Veitch, 1996). Torrance (2008) delineates the growing role of financial intermediaries in producing a market for infrastructure leases. O'Neill (2013) examines how infrastructure such as airports, motorways, telecommunications and the electricity grid have become integrated into financialization processes which privilege financial rather than material performance.

The specific pathways of financial integration in urban governance, and the reasons for those particular pathways are still relatively un-examined. This dissertation responds to the call to understand the processes of local financialization as "policy project[s]", and to integrate state theory into such study (Ashton, Weber, Doussard, 2014). To take seriously this call, it is necessary to consider another key body of literature which addresses transitions in the urban state and political economy in recent decades. I turn my attention to that literature in the next section of this chapter.

## **2.2. Post-Keynesian municipal governments**

In recent years, a large body of scholarship has theorized the collapse of the post-war Keynesian political economic system and the neoliberalization of the global political economy. Beginning in the 1970s, policymakers adopted various strategies to respond to emerging crises, as the Keynesian-Fordist project of high employment and consumption



slid into overproduction, stagnation and inflation. Supranational institutions, as well as national and local states, introduced policies with the goal of spreading free market principles throughout various sectors of society (Brenner and Theodore, 2002 ; Jessop, 2002; Hackworth, 2007; Peck and Tickell, 2002; Prasad, 2006; Green and Huey, 2005).

### *2.2.1. Keynesianism's demise and racism*

Scholars have theorized various aspects of this transition. First, they have shown that for neoliberal agendas to become hegemonic and embedded, Keynesianism had to be discredited in various ways. Government dysfunction is a central theme of this project (Meier, 1993; Chang, 1997). Scholars such as Colin Hay have suggested that "the ascendancy of a spectacular and normative neoliberalism in the late 1970s and 1980s was predicated on the success of the new right in mobilizing widespread perceptions of a crisis of overload and ungovernability" (Hay, 2004: 503; Keil, 2009).

Relatedly, a growing body of literature demonstrates that in the US and the UK, racism played a significant role in creating the material and ideological conditions for the neoliberal turn (Hall, 1978; Woods, 2007; Gilmore, 2007; Roberts and Mahtani, 2010; Spence, n.d.). I ground my study in a rich body of scholarship showing how various forms of structural racism and segregation in concert with other factors such as de-industrialization and federal dis-investment from cities produced particular dilemmas for urban areas like New York, including large scale housing abandonment and fiscal crisis (Wilson, 1996; Sugrue, 1998; Reiss, 1997; Denton and Massey, 1998; Wilder, 2000). I follow other scholars who clarify racism's central role in these events, events which in turn shaped the subsequent rise of neoliberal movements. Scholars have shown how, for

example, racial attitudes among voters were essential in propelling the 1978 passage of California's Proposition 13 (Sears and Citrin, 1982), which signaled the growth of a broader tax revolt in the country that was increasingly destabilizing the Keynesian regime (Blyth, 2002). As Spence notes, "If we take into account the work race performs in norming individuals and spaces we can better explain the where, the when, and the why of neoliberalization" (Spence, n.d.: 6).

### *2.2.2. New state capacities*

The shift to a neoliberal state represented a paradoxical reconsolidation of state power (Lake, 2002; Jessop 2002), as the "anti-state state" which "grows on the promise of shrinking" developed new capacities and re-purposed old capacities (Gilmore and Gilmore, 2008: 141). Markets have not replaced the state, but neoliberalism restructures and rescales the past forms of governance and produces new forms of governance.

Peck writes that "in the process, new institutional and regulatory landscapes are being created and animated by new functional logics and political imperatives" (Peck 2003: 222). Proceeding from the notion that this process is "variegated", "geographically uneven" and "path dependent" (Brenner, Peck and Theodore, 2010: 182), my project aims to document how financial engineering offered institutional forms and logics that shaped the development of new neoliberal state capacities.

Peck and Tickell (2002) have termed the process by which Keynesian policies and institutions are dismantled, "rollback" neoliberalism. They suggest that this process is followed by "rollout" neoliberalism, in which new policies and institutions are established. Hackworth (2007: 11) writes:

Neoliberal destruction consists of the removal of Keynesian artifacts (public housing, public space), policies (redistributive welfare, food stamps), institutions (labor unions, U.S. Department of Housing and Urban Development), and agreements (Fordist labor arrangements, federal government redistribution to states and cities), while neoliberal creation consists of the establishment of new, or cooptation of extant institutions and practices to reproduce neoliberalism in the future (government-business consortia, workfare policies).

### *2.2.3. Entrepreneurial cities*

Scholars have delineated how cities are of particular significance in the process of neoliberalization (Hackworth, 2007; Marcuse and van Kempen, 2000). While the Keynesian system privileged the nation-state as the engine of capitalist expansion and the primary site of government action, the collapse of this system engendered a process of "glocalization", which instead implicates global markets and local state structures in regulatory roles that the nation-state previously held (Swyngedouw, 1997). As such, city governments have moved from a managerialist role under Keynesianism to an entrepreneurial one under neoliberalism (Harvey, 1989). Scholars have shown that local governments are ill-suited to take over many of the tasks devolved to them from the national state (Lake, 2002). However, in the wake of urban deindustrialization, diminishing federal funding for US cities and a rightward-shifting political climate over the last three decades, many city leaders have attempted to meet these challenges by recasting their role into that of competitive actors seeking to maximize revenues while minimizing expenses in a quest to attract mobile capital (Hall and Hubbard, 1998). Neoliberal perspectives on urban governance reify the city as a "thing", a "bounded and socially unified economic unit in competition with other such units" (DeFilippis, 2004: 24; Brash, 2011: 135). Thus, entrepreneurial cities "pursue innovative strategies intended to maintain or enhance [their] economic competitiveness vis-a`-vis other cities and

economic spaces, adopt an entrepreneurial discourse, narrate their cities as entrepreneurial and market them as entrepreneurial" (Jessop and Sum, 2000: 5).

Neoliberal views of the entrepreneurial city generally discount the limitations that extra-urban social, economic and political relations impose on local governments (Lake, 1994; DeFilippis, 2004). The emphasis on inter-urban competition also accelerates the copycatting of policies perceived to be successful in other places (Peck, 2002). While neoliberal ideology overstates local autonomy in general, my work proceeds from the notion that some degree of autonomy does exist for city governments, albeit with considerable disparity between different localities. This study seeks to delineate the actual contours of that autonomy for different cities within the context of financialization, which I understand to be a simultaneously local and extra-local phenomenon.

Privatization has been a hallmark of neoliberal governance with methods that encompass two primary categories. The first is "delegation", where government "retains responsibility and oversight but uses the private sector for service delivery, for example, by contracting for services" or establishing public-private partnerships. The second is "divestment", where government completely "relinquishes responsibility" through sale of assets (Savas, 2005: 2). Pursuing public-private partnerships and alliances has been a favored strategy of some urban policymakers long before the advent of neoliberalism, but these alliances have taken on new forms and meanings as governments are increasingly expected to facilitate markets rather than simply remedying market failures (Fainstein et al. 1989; Sites, 2003). Entrepreneurial cities aggressively pursue public-private alliances for a variety of purposes. In many instances, this has produced a "hollowed-out" city

government functioning increasingly through contracts with private operators (Jessop, 2002).

Overall, these shifts have also led to a transformation of urban politics (Macleod, 2011). As Hay (2006: 502) writes:

From the 1990s onwards, however, the normalization and institutionalization of neoliberalism and its depiction as a largely technical set of devices for managing an open economy has served to depoliticize and de-democratize economic policy-making. This, I suggest, has contributed to a process of disengagement and disenfranchisement.

My work seeks to contribute to this scholarship by showing how financialization intersected with attempts of the entrepreneurial local state to reimagine itself. Botein and Heidkamp (2013:3) write that:

Neoliberalism evolved during this period, as Peck and Tickell (2002: 37) have noted, shifting from the destruction of the Keynesian state to ‘the purposeful construction and consolidation of neoliberalized state forms, modes of governance, and regulatory relations’. Financialization facilitated this evolution by giving local governments the illusion of greater and more flexible resources.

While I follow these authors in recognizing that the processes of neoliberalization and financialization worked in concert, I also document how they produced a central contradiction at the site of the local state in that financialization's main imperative of increasing debt, in this case, public debt, was anathema to neoliberal ideology. Still under-explored is how, given the strong anti-public borrowing exhortations of neoliberalism, the kinds of debt-encumbering solutions that financialization offered to municipalities became a reality. I seek to further articulate the actual material and ideological mechanisms through which the processes of financialization and neoliberalization worked through and against each other at the urban scale.

### 2.3. Financializing municipal governments

A growing body of literature examines the financialization of the local state showing the active role the local state plays in bringing about and maintaining these arrangements. This literature confirms that financialization and neoliberalization are not coterminous with a retreat in state involvement (Weber, 2010; Gotham, 2006; Botein and Heidkamp, 2013, Jessop, 2002). On the federal and state level, various practices and regulatory changes paved the way for the growth of financialization. As Gotham (2006:256) writes:

State action, in the form of public creation of institutions and legal regulation, has created and enhanced the liquidity of residential and commercial real estate assets. As a result, domestic and foreign investors have been persuaded to invest in real estate once commercial and residential mortgages could be standardized and pooled together as securities for sale in global markets. In both cases, the state has deliberately created pressures for governance transformations as an actor by redefining property rights and establishing rules of exchange within the residential and commercial securities sectors.

In addition to national state regulatory changes which paved the way for financialization (Krippner, 2005; Gotham, 2006, 2009), local state action was necessary as a means to create liquidity out of previously non-liquid assets such as land, to reconfigure risk at key moments in order for financial markets to continue functioning, to create new “techno-political” arrangements through which new practices are performed, and to produce or disseminate certain kinds of knowledge in order to buttress the legitimacy of such actions (Ashton, 2010; Christophers, 2010; MacKenzie, 2006; Callon, 1998). Whether making local assets legible for global capital markets, flexing political muscle, granting regulatory approvals or exemptions, providing locally specific knowledge about market conditions, or sponsoring securitizations, many local

governments have attempted to actively engage in financialization as a policy project (Sokol, 2013; Weber, 2010). My work seeks to further explore the extent of the various material and ideological resources mobilized in the service of financial integration and the limits of that mobilization.

For what purposes did local governments participate in market-making and deploy resources in the direction of financialization? Much of this literature shows how financialization of public assets, often in the form of infrastructure privatization, essentially offers municipal governments a new tool in an old toolbox of inventive strategies to mask borrowing from the public. While proponents argue that infrastructure privatization offer long term fiscal benefits by generating efficiency, cost savings and improved services, these studies demonstrate how the primary fiscal impact of such privatizations is to merely re-profile a stream of revenues by front-loading future receipts into a single lump-sum (Marchiony, 2012; Roin, 2011; Gelfand, 1996; Sbragia 1996). Such practices result in new municipal debt that is not reflected on municipal balance sheets as debt. Roin (2011: 1969) explains the potential harms to the public of municipal debt that is not understood as such:

Debt masquerading as privatization costs governments more than conventional debt on two main fronts. First, governments are unlikely to borrow at rates as favorable as the rates they would obtain when issuing conventional debt. Second, privatization debt limits government flexibility more significantly than other forms of debt. Further, privatization debt is less transparent to voters, and perhaps even politicians.

Many of these studies approach financialization as offering local governments new, often short-sighted strategies to relieve fiscal stress (Botein and Heidkamp, 2013; Torrance, 2008). Other studies demonstrate that certain cities like Chicago are not

motivated primarily by fiscal stress, but are able to harness and achieve desired real estate market outcomes (Weber, 2010). In their study of Chicago's infrastructure leases, Ashton, Weber and Doussard (2014: 4) argue that such arrangements reposition the local state, simultaneously providing it with new powers and "enmeshing" it in new liabilities:

[We] ask how that uncertainty is structured within the transaction – both in investors' assumptions about revenue streams that justify a particular purchase price, and in the various roles that the local state may play in bounding or managing uncertainty within the transaction."

My analysis confirms that financial engineering reapportioned uncertainty in various ways which served some localities better than it did others. Furthermore, I show that in some instances, cities shed political and regulatory liabilities through taking on new financial liabilities.

In sum, this study offers an opportunity to bring literatures on financialization, neoliberalization and the urban state into further constructive dialogue with each other. By critically examining changes in property tax enforcement practices, my project investigates the dynamic relationship between global financial integration and neoliberal urban state-building over the last several decades.



### **Chapter 3—Urban crisis and financial innovation: the emergence of tax lien securitization in the 1990's**

"Our business plan at that time was: `The world's our oyster if we can get the Jersey City deal done.'"

-Douglas Breen, founder of Breen Capital, one of the initiators of the Jersey City tax lien securitization

In the last three decades, local governments in the United States have played a critical role in the increasing financialization of the US and global economy. Weber (2010: 257) describes various elements of this role:

Municipalities extended the power of financial markets throughout the economy by issuing and purchasing vast amounts of debt. They also developed new domains of governance (e.g., special districts), new instruments, and new asset classes that could be bought, sold, and securitized. They financed and lent their legitimacy to the creation of new secondary markets where assets once thought to be valued only for their uses (infrastructure, pensions, and tax revenues) were converted into securities and traded at a distance...and, with the blessing of state governments, they created instruments through which anticipated revenue streams could be sold off to investors, such as public asset leases and TIF.

A key part of this history that remains little explored is the series of experiments with the municipally-sponsored tax lien securitization beginning in the 1990s.

Securitization, a financial process in which income-producing assets are pooled and then repackaged into interest-bearing securities, emerged in the early 1980s and has entered into increasingly widespread use in the last three decades. In the early 1990s, local governments, with the help of financial intermediaries, began sponsoring securitization transactions.

In this chapter, I use the case of municipally-sponsored tax lien securitization to explore how neoliberalization and financialization worked through and against each other in cities in the early 1990s, focusing on four aspects of this dynamic in particular. In the first part of this chapter, I trace the transfer of the use of securitization from its inception in the secondary mortgage market to municipal governments seeking to monetize property tax liens. I situate the innovation of municipally-sponsored tax lien securitization within broader trends in the use securitization as a financial technique, and the evolution of modern banking and finance. Second, I argue that this innovation depended on forms of privatization and debt sale that predated both neoliberalism and financialization, showing that new applications of financial integration are highly path-dependant, relying upon contextual embedding in the pre-existing practices of specific localities. Third, I document how particular actors in the municipal bond industry shepherded municipal financial innovation as neoliberalizing governments made cuts in public spending and borrowing that undermined the industry's past business models. Fourth, I document the process through which different localities were integrated into different kinds of global capital markets, which in turn provided different kinds of risks and benefits for those localities. Eschewing a monolithic notion of global capital markets, I seek to differentiate between the various kinds of capital that sought deeper integration into the operations of local governments.

### **3.1. The evolution of securitization**

Scholars have detailed the way that the technique of securitization has served as an engine of expanding financialization in the private sector (Leyshon and Thrift, 2006).

In most securitizations, an entity such as a mortgage lender aggregates individual loans into a bundle and transfers that bundle to a special purpose vehicle (SPV), which is usually its subsidiary and incorporated as a business trust. In some cases, this SPV issues bonds backed by the bundle of loans which it sells to investors. In other cases, the bundle of loans is then transferred again to another trust entity which issues bonds. This process of separation from the mortgage lender allows bond purchasers to feel confident that the assets in question will be protected in the event that the mortgage lender goes bankrupt.

Typically, securities are divided into various levels of priority for incoming cash flows. These are called "tranches" and are usually labeled with consecutive letters. Tranche A will have priority over tranche B and so forth. If collections are insufficient to cover interest payments for all tranches, subordinate tranches will absorb the loss, lowering its cash flow, while the highest tranche remains unaffected. The lowest tranches thus carry more risk than the higher tranches. As such, lower tranche securities are priced lower and return higher interest yields to reflect the level of associated risk (Jobst, 1997). Most securitizations depend upon credit agency ratings to be able to market securities to investors. One or more of the major ratings agencies--Moody's Investor Services, Standard & Poors (S&P) or Fitch's Ratings--will issue a rating for each of the tranches (Litan, 1991; Schwarcz, 1994; Ranieri, 1996; McCoy and Engel, 2004).

The use of securitization began in the 1970s and grew in the 1980s when the Federal National Mortgage Association (Fannie Mae), the Government National Mortgage Association (Ginnie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), corporations established by the federal government, began securitizing mortgages in order to make more capital available for mortgage lending

(Sellon and VanNahmen, 1988). In 1984, changes in federal law facilitated the issuance and purchase of private label mortgage-backed securities which paved the way for securitization to happen without the involvement of Freddie Mac and Fannie Mae. This development eventually led to a larger transformation of the banking system in which various non-bank financial institutions have taken an increasing role in providing credit in a variety of sectors (Pozsar et al, 2013).

Various additional state actions and regulatory changes paved the way for the increasing use of securitization beginning in the 1970s and 1980s. A key development in the evolution of securitization as a financing technique occurred in 1989, when the savings and loan crisis led the federal government to create the Resolution Trust Corporation (RTC). The RTC was tasked with disposing of the assets of troubled financial institutions. The majority of the assets the RTC was charged with disposing of were mortgage loans. A particular challenge the RTC faced in its portfolio was dealing with so-called "non-performing mortgages" in which borrowers were behind on payments. Working with the investment bank, Salomon Brothers, as its financial advisor, the RTC began issuing mortgage-backed securities that included non-performing loans in 1991 (*Business Week*, 1992). With these transactions, Salomon Brothers and the RTC pioneered a model for using securitization to repackage and market so-called non-performing assets (FDIC, 1998; Ashton, 2011). Ashton writes:

[The] RTC looked instead to innovations in securitization to maximize disposal of those "toxic" assets while minimizing direct costs to taxpayers. It pooled loans into independent trusts, which then issued securities with a hierarchy of claims on the underlying stream of interest generated by the pooled mortgages. These claims were divided into risk classifications, or tranches, each defined by the degree of exposure to underlying risk of loss; those classes least exposed to credit risk resembled investment-grade assets and were able to qualify for good credit ratings (FDIC, 1998, pp.413). These securities were similarly priced according to risk

exposure, with tranches most exposed to credit risks earning a much higher return. This structure, which had been used with car loans or other assets since the mid-1980s, allowed RTC to issue the first mortgage-backed securitization that included non-performing loans. (FDIC, 1998, pp.415).

Ashton describes how through this innovation the RTC "created the basis for transformation of the exceptional space of non-performing or 'toxic' loans into a market space integrated with broader capital markets and thus open to a wider group of investors" (Ashton, 2011: 15). In this way, the work of Salomon Brothers and the RTC pioneering the securitization of so-called "toxic" assets lay the groundwork for tax lien securitization (Interview, 5/2012). Gotham (2006:263) further describes the significance of the RTC's actions:

The agency's actions promoted a standardized framework for understanding commercial mortgages as units of a large class of comparable assets, and promulgated a formalized understanding and category system through which commercial mortgages became more easily transparent, more homogeneous, and less idiosyncratic.

Concurrent with the establishment of the RTC, another important development occurred in 1988 when Delaware, which has a long history of permissive business corporation laws, enacted a business trust act affording liberal provisions for companies seeking to form trusts. The act created the Delaware Business Trust, which has become one of the favored forms of special purpose vehicles used in asset-backed securitizations (Langbein, 1997).

### **3.2. Second wave of asset-backed securities and tax liens**

Partially as a result of the RTC's work, the technique of securitization spread from the mortgage industry to other kinds of income streams such as credit cards and auto

loans in the early 1990s. These instruments were called asset-backed securities (ABS). In the early 1990s, the ABS market mushroomed as corporations issued \$75 billion worth of asset-backed securities in 1994 and \$108 billion in 1995. ABS offerings grew almost twice as fast as corporate bonds, driven by investment banks and investor demand.

"There is a huge investment-banking community going after this business and an insatiable demand from investors," the head of Standard & Poor's New Assets group told *Businessweek* in 1996. At the beginning, ABS primarily dealt with credit card, home equity and auto loans. As margins began to shrink in those markets, investment banks began searching for new asset types where they could charge higher fees and also could obtain higher yields for investors. It was at this moment that securitization deals began targeting property tax liens along with other exotic income streams such as royalty streams from films and aircraft leases, as well as home-improvement loans, auto loans to borrowers with bad credit, and student loans (Woolley, 1996).

Concurrently, changes in the fiscal circumstances faced by cities and the spread of certain financial innovations between the 1970s and the 1990s produced certain pressures for cities, the municipal bond industry, and the relationships between the them.

Nationally, the federal government abandoned Keynesian principles of large centralized expenditures on social welfare beginning in the 1970s (Mills, 1987). Cities, already sapped of resources from decades of post-war policies promoting suburbanization and de-industrialization, faced increasing fiscal challenges as the federal government slashed funding and increased un-funded mandates (Drexler, 1994; Sugrue, 2005). However, in addition to state restrictions governing local tax policy, cities were also constrained by state level constitutional limits on debt, many of which date back to the late 19th century,

when rural political interests sought to limit the growth of emerging cities (Macchiarola, 1966). Simultaneously, a rightward political shift characterized by growing anti-tax sentiments led to more voter discontent with public spending and borrowing. The passage of Proposition 13 in California and the Colorado Taxpayer's Bill of Rights of 1992, limiting local tax levies, reverberated across the country and launched a new era of measures constraining state and local taxing and spending. Anti-tax forces consolidated themselves as a powerful political interest group (Gilmore, 2007; Nelson, 2012). In response to these shifts, many city leaders began to see themselves as competitive actors seeking to maximize revenues while minimizing expenses in a quest to attract mobile capital (Hall and Hubbard, 1998; Harvey 1989). Privatization of public functions became a key part of that strategy (Savas, 1987).

As a result of these shifts, municipal governments turned to growing financial markets for resources. As Weber (2002) writes:

In the last quarter of the twentieth century, certain changes stand out as marking a new era of increasing integration between financial markets and the day-to-day operations of local governments. Local governments moved beyond simply financing collective infrastructure and doing so with general obligation bonds, backed by their full faith and credit...Municipalities added new, risk-laden instruments to their debt portfolios, including variable rate debt, interest rate swaps, auction bonds, and derivatives—often with disastrous effects. They also added the personnel necessary to execute these complex transactions, increasing the size of their comptrollers' offices, hiring graduates of MBA (Master of Business Administration) programs, and contracting out to specialized financial advisors.

Within this context, Bret Schundler was elected as mayor of Jersey City in 1992, the first Republican mayor since 1917. Like many other cities, Jersey City had experienced decades of urban decline as many of its well-to-do residents left for surrounding suburbs. Between 1950 to 1980, 75,000 residents left Jersey City. In the late

seventies it lost thousands of jobs, representing almost a tenth of all jobs in the city (Jacobs, 2000). Prior to his election, Schundler had worked on Wall Street as a bond salesman for Salomon Brothers. Schundler's chief of staff Michael Cook also had financial industry experience, having worked in pension consulting at Chase Manhattan Bank (Stanton, 1996). During his campaign, Schundler promised to use his private sector experience to introduce so-called "market solutions" to urban policy.

At the time, Jersey City had a \$40 million budget deficit. In addition, the City was at risk of having the State of New Jersey take over its finances. Its collection rate on property taxes was only 78%, a rate that approached the 75% threshold at which the state could take over tax collection and impose fiscal constraints. Together with Douglas Breen, a former Paine Webber government-bond salesman, Schundler proposed a new approach to the city's tax enforcement policy (Beckett, 2000). The City would bundle tax liens and securitize them similar to the way in which mortgages were securitized.

The proposal was significant because it was the first time that a local municipal government would act as the actual sponsor of a securitization transaction. Schundler cites his previous work as a bond salesman at Salomon Brothers as the inspiration for his tax lien securitization proposal:

I was at Salomon when they effectively initiated the mortgage bond market. Before that time most mortgages were actually held by the original lender, and the secondary market didn't really take off until the early 1980s. First they developed mortgage backed securities, then you saw things like auto loan receivable securities. They even packaged things like mobile homes. I would argue that Salomon was the pioneer in asset-backed securities. When I came to Jersey City as mayor, [liens were] just another receivable, and you can certainly make them into an institutional investment (Bondweek, 1995).

### **3.3. Why tax liens?**



Many accounts of expanding financial integration depict the process as ever-versatile, one-size-fits-all, and capable of proliferating almost as a virus would, as long as new income streams are available. "You can securitize virtually everything", one structured finance expert told Business Week in 1992, "the imagination is our only constraint -- and time because you can't chase every deal." However, while local governments have a variety of different kinds of assets and income streams all of which are theoretically securitizable, the first local government-sponsored securitizations in the US involved relatively obscure income streams: delinquent property tax bills.

While Schundler states that tax liens were "just another receivable", in fact cities have many different kinds of receivables. Why were property tax liens well-suited for this project? I argue these property tax liens were particularly compatible with this kind of securitization project because they were simultaneously a form of debt sale and a form of privatization which had a long institutional history in the United States. As such, tax lien certificates already had an institutional and legal framework to support their sale and securitization.

While privatization of government functions and public assets has been a hallmark of neoliberal governance, privatized tax collection has a long pre-neoliberal history in the United States and an even longer history around the world. It was common in almost all pre-modern states and empires including ancient Greece, Egypt and Rome. A similar practice occurred in England during the Middle Ages in which the state sold tax collection rights through Italian banking syndicates. Privatized property tax collection was also common in the US in the nineteenth century, with localities selecting a town collector working on commission to perform these duties (Alexander, 2000). Tax title

sales became more common in the United States during this period and the legal rights for property tax title claimants over the original property owners became more established. The Civil War represented a watershed moment in the history of tax sale policy. Fiscal crises in the aftermath of the war led to a crackdown on tax delinquency and greater legal standing for tax title purchasers after 1860 (Swierenga, 1971).

While policy and practice have varied according to circumstance in various localities over time, most jurisdictions hold tax sales in which they either sell the tax liens or sell the deed to the underlying property. While there is substantial variation in policy and practice, localities generally follow four steps when enforcing on properties delinquent on taxes: first, the creation of a lien on the property if the taxes are not paid within a certain time period; second, the sale of the tax lien or tax deed; third, the redemption period during which property owners can remove the lien if they pay the full amount owed which includes not only back taxes, but also penalties, interest attorney fees and other costs; fourth, foreclosure (Rao, 2012). By law a property tax lien has “super-priority” status, which allows local governments to collect it before other creditors can collect debts secured by the same property. The property tax debt thus has priority over mortgage liens and Federal income tax liens (Alexander, 2000; Marchiony, 2012; Miller, 2012).

By selling property tax liens to private investors, local governments receive money for the taxes owed immediately. The private investor then receives the advantage of a “super-priority” first lien on the property and stands to profit from high rates of interest and penalties. Interest rates are often as high as 18% or more (Alexander, 2011).

Different localities seek to balance tax collection and housing objectives in their tax enforcement processes in various ways. For localities, tax sales can yield revenue and serve as an enforcement mechanism but may also result in adverse impacts for properties and neighborhoods. Alternately, choosing to enforce property taxes without selling tax liens or tax deeds may mean that a locality must take responsibility for owning and managing tax-foreclosed property.

Lien buyers can be individuals but groups of investors forming investment syndicates, where investors pool their money to jointly purchase tax liens, also have a long history of participating in tax sales (Tax Lien Company of New York, 1911; New York Times, 1917). By the 1930s in the US, there was a well-developed tax lien investment industry, buoyed by the rise in tax delinquencies during the Great Depression.

Schundler and Breen's proposal to securitize tax liens used this long-standing institutional practice of privatizing delinquent tax debt as a foundation for financial innovation. They saw property tax liens as an attractive investment vehicle for the same reasons that others did: first, their legal priority over mortgages and other claims and second, the fact that the vast majority of owners or the holders of the mortgages would eventually pay off the liens. Given that a property is typically worth many times the amount of the tax lien, the threat of tax foreclosure on the property ensured that lien holders would be paid (Interview, 2012; City of New York, 1995; Marchiony, 2012).

### **3.4. Surplus capacity**

By securitizing tax liens, Jersey City hoped to reap certain benefits by accessing a new market for tax liens. In the past, navigating tax lien markets required specific and

extensive knowledge of local laws and real estate dynamics resulting in a market made up of largely local investors. A tax policy expert in the 1930's remarked (Rodney, 1936:10):

The purchase of tax liens for investment purposes is a highly-specialized and technical business... In the first place, in the proper conduct of the tax investment business, it is necessary to examine each and every parcel offered individually. When a list of delinquent taxes is advertised for sale, a complete check-up of this entire list must be made. This includes an examination of the tax rolls disclosing the valuations of the properties, an examination of the tax arrears, very often a title examination and physical inspection. This requires a staff of competent and experienced investigators.

This remained the case throughout the twentieth century as tax lien investment was largely dominated by individuals or companies operating locally (Beckett, 2000).

Through securitization, Schundler and Breen sought to shift tax lien investment away from companies operating locally towards larger scale institutional investors. To help him structure the deal, Schundler reached out to his former colleagues from Salomon Brothers who had worked on the RTC securitization of non-performing mortgages, some of whom now worked at WR Lazard & Company, a Wall Street investment firm founded by a former Salomon Brothers employee. Gilmore has written about the different innovations that public financiers made during this period as cuts in public spending and borrowing undermined their previous business models (Gilmore, 2007). WR Lazard specialized in managing pension funds and arranging bond issues for large municipalities but was struggling for a number of reasons, including the overall decline in municipal bond issues (King, 1996). In the early nineties, it was looking for new business lines, and advising municipalities such as Jersey City on how to securitize their tax liens seemed promising. Michael Luther, chairman and chief executive officer of WR Lazard stated in reference to tax lien securitization, "We see these types of transactions as being sort of a buffer

against the good times and the bad times in the municipal industry" (Stanton, 1996: 3).

Sharon King (1996: 7), a financial reporter writing in 1996, directly attributed WR

Lazard's foray into tax lien securitization to this need to diversify as a result of

retrenchment in the municipal bond market:

Meanwhile, municipal volume continued to wane, slipping 3% from the previous year to the lowest level in the past five years. Several large firms, such as CS First Boston, Chemical Bank and Lazard Freres, have dosed out their municipal business...As the municipal bond market dries up, firms are finding a new way to boost business by adding corporate finance and asset management arms to their existing operations...Diversification at WR Lazard also has meant a strong push for its financial advisory business, WRL Advisory Group. To grow the business, WR Lazard is focusing on the asset side of the balance sheet. They help issuers gain more value from existing assets by selling, privatizing or securitizing them. This is opposed to the more traditional forms of financial advisory directed toward municipal clients, advising them on the issuance of new debt or refinancing existing liabilities. In this area, WR Lazard pioneered a real property tax lien securitization deal for Jersey City, N.J..

For the first tax lien securitization, Jersey City bundled \$44 million in tax liens. The idea was the following: the city would create a trust which would purchase the tax liens at a discount. Subsequently, the trust would issue bonds backed by the liens, and give the city a part of the money raised from the bond sale. Although sale price was discounted, the city would benefit from receiving payment right away, thus being able to meet immediate budget shortfalls.

The deal was structured in the following way. The City formed a subsidiary (commonly referred to in securitizations as a special-purpose vehicle or SPV). This subsidiary was incorporated as a Delaware Business Trust. Although the local government remained the beneficial owner of the trust, the trust was considered a separate legal entity from the city. The trust and the municipality would have a contractual relationship (Poindexter, 1996).

After establishing the trust, a pool of liens serving as collateral was constructed. A firm serving as the underwriter—in the case of Jersey City, the investment bank CS First Boston (now Credit Suisse)—would arrange the transaction. It was responsible for, sizing each tranche, selecting the debt-to-equity ratio, ensuring the collateral was sufficient, working with the credit rating agencies to obtain the desired ratings for each tranche and finding buyers for the securities.

The trust would then hire private servicers, in this case, Douglas Breen's company, Breen Capital and an investment bank, Banker's Trust. Credit ratings agencies would issue ratings for the various tranches by examining factors such as the composition of the pool of tax receivables and the individual characteristics of each such asset, the geographic diversity of the underlying properties, and assessments of default risk and competency of the selected private servicer (Dechert, 2009).

After the ratings agencies issue their ratings, the trust would issue bonds backed by tax lien receivables and sell them to investors, primarily institutional investors. In order to assure potential investors and ratings companies of the likelihood that the bonds would be repaid, the transaction was overcollateralized, meaning the face value of the tax liens sold would be significantly higher than the dollar amount of bonds issued.

In the Jersey City deal, the City sold a bundle of 2,520 tax liens, with a face value of \$43.7 million to the Trust. The Trust purchased the liens from Jersey City for \$25 million dollars. Then First Boston marketed a tranche of single A-rated senior notes issued by the Trust (and backed by the overcollateralized pool of liens) to institutional investors. The senior notes had a coupon rate of 8.25% and had an average life of 1.5 years. The theory was that collections from delinquent property tax principal and interest

would be sufficient to repay \$25 million in bonds plus interest, as well as cover fees to the servicers. Similar to other asset-backed securitization transactions, in addition to the cash it received, Jersey City also received \$19 million in the form of subordinate notes. If collections turned out to be in excess of the amount necessary to meet the amount due to bondholders in principal and interest, the municipality could collect that surplus (Bond Buyer, 1995; Schwimmer, 1993).

### **3.5. Potential advantages of securitization**

On the part of a municipality like Jersey City, there were several potential advantages to using the securitization structure over a traditional tax lien sale in which liens were sold individually. First, selling the liens in bulk was much less administratively burdensome than selling thousands of liens individually. According to Schundler, the tranching structure and overcollateralization involved in lien securitization were critical for Jersey City to be able to market the liens in bulk because it made tax lien investment appealing to a growing market of institutional investors (Schundler, 2002). In the decades leading up to the Jersey City deal, the institutional investor market had grown tremendously with the expansion of pensions, private retirement funds and insurance company holdings (Hawley and Williams, 2000). Schundler described the dilemma in the following way:

The problem we had was we couldn't get banks to buy liens because each lien was so small. It may be a \$3,000 or \$4,000 lien. So by putting \$44 million liens together, we got a sizable pool which was worth doing some due diligence on...The outside investor who bought the senior note, he's got a senior note which has \$25 million in face value, collateralized by \$44 million worth of lien. Now that you have an investment which has got a face value of \$25 million, it's worth investing in for institutional investors (Bond Buyer, 1995:5).

This growing institutional investment market sought fixed-rate "investment grade" bonds (often in the form of asset backed securities). Investment grade bonds are defined as bonds that credit rating agencies have labeled "BBB" or higher. The institutional investment market was entirely distinct from the municipal bond market, which was traditionally made up of individual investors looking to invest small sums in low-risk, low-yield bonds subsidized by their federal tax-exempt status (Interview, 2012). Tax lien-backed securities would be high yield, higher risk products that would be taxable. Moreover, global capital surpluses meant that investors were eager for new outlets, including municipal debt instruments that had been ignored in the past. Weber writes:

When municipalities sought assistance from the financial markets, they encountered purveyors of private capital with a new taste for public debt. Municipal debt instruments previously had been viewed as marginal and low yield. But in the late 1990s, investment banks were flush with cash from global capital surpluses (mainly from Asia, the United States, and Europe), with relaxed underwriting criteria and low interest rates adding to the volume of money (Weber, 2010:257).

A second perceived benefit of using a structure involving a trust was that it allowed the issuance of bonds without the technical incurrence of debt on the part of the municipality (Poindexter, 1996). This was especially significant for many municipalities bound by state-imposed debt limits, which added securitization to their arsenal of creative off-budget strategies to evade these limits. Other strategies aimed at such evasion included the creation of special districts and leasing agreements (Sbragia, 1996).

Finally, by using a trust, a municipality could secure a higher rating for bonds than if the municipality were to directly issue the bonds (O'Hara, 2011; Poindexter, 1996). This was due in part to the legal separation of the trust's assets from the city's assets for the purposes of bankruptcy. Property held by a Delaware Business Trust is not



considered property of its beneficial owner (in this case, the municipality) during the owner's bankruptcy. Using a structure involving a trust shielded investors from the risk that in the event of bankruptcy by the municipality, creditors would obtain possession of tax lien receivables. Ratings agencies considered this to be grounds for a higher credit rating because bondholders did not have to fear any possible interruption of payments in the event that the city became insolvent.

After Jersey City completed its first tax lien securitization transaction in 1993, a number of other cities followed its lead in structuring similar transactions with property tax liens between 1994 and 2003. In particular, New York City's decision to securitize its tax liens represented a watershed moment for the entire concept of tax lien securitization. With the New York transaction completed, the financial industry saw an opportunity and began to organize around the expansion of lien securitization to other places. WR Lazard hired Michael R. Cook, former chief of staff to Jersey City Mayor Bret Schundler, as a senior vice president in its WRL Advisory Group. Very soon after, other cities began to follow suit. These included New Haven , Fulton County/City of Atlanta, Washington, D.C., Philadelphia, Puerto Rico, and upstate New York (a combined effort that included Syracuse, Buffalo, Binghamton, and Plattsburgh). Standard & Poor's began rating tax lien securities and servicers in 1995. In 1999, New York State even considered requiring municipalities to securitize their liens (Investors Digest Daily, 1999).

### **3.6. Failed experiments**

Neither the Jersey City experiment nor the others that followed it lived up to original expectations as collections were lower than expected and properties with liens

suffered further physical deterioration. Of all of the localities that sponsored tax-lien securitizations only New York City continues the practice. All other localities have abandoned their own programs after their first or second attempt. In the next several chapters, I will explore the circumstances that made the New York City project different. But first, let's look at what happened to the securitization projects in these other cities.

The experiences of Jersey City, New Haven, Philadelphia and upstate New York provide insight into some of the challenges that these transactions faced.

Jersey City's transactions ended in extensive litigation between the servicers, the City and the delinquent property owners. Property owners sued under state law challenging a number of aspects of the arrangement, including the right of private servicers to enter into installment payment agreements with debtors in the same way that municipalities routinely do. Although these questions were eventually resolved in the servicers' favor, the litigation drew negative attention to the deal, was expensive for the servicers and created difficulties in maintaining timely collections.

Lower than anticipated collection amounts also threatened the repayment of bonds. In order to avoid default on the bonds, another Breen company purchased the bonds from bondholders at par before their 7.5 year maturity. In addition, inadequate collections meant Jersey City would not receive payment on its subordinate note as it had originally anticipated which generated further litigation between the City and the servicers over whose fault it was that collections were inadequate. According to the City, the servicers dragged their feet on collections because they stood to receive higher fee payments the higher the balance of outstanding payments. According to the servicer, the pool of liens did not have sufficient value to pay both the bondholders and the

subordinated notes given to Jersey City. The servicer and the City ultimately settled out of court, with the City giving up a majority of the value of its subordinate notes (Beckett, 2000). While Jersey City did benefit from a substantial increase in property tax collections after it announced its plans to sell off the tax liens (Schwimmer, 1993), the City did not continue lien securitization after 1994.

In 2004, the City of Philadelphia and the Philadelphia School District ended up defaulting on \$46.3 of \$75.5 million in securitized bonds that had been issued in 1997. The City of Philadelphia and the Philadelphia School District had sold approximately \$106.3 million in tax liens, issuing \$75.5 million in bonds via the Philadelphia Authority for Industrial Development (PAID). After fees, expenses, and reserves, the City and the Philadelphia School District received \$70 million. In 1997, at the time of the transaction, Moody's Investors Service's rated the bonds AAA based on insurance provided by MBIA Insurance Corporation, a bond insurer. The ratings were issued by Moody's structured finance group, not its municipal finance group. Neither of the other two large ratings agencies, Fitch and Standard and Poor's issued ratings on the deal (D'Ambrosio, 2004). Three years into the securitization, an audit was conducted. It cited the poor quality of the tax liens as the primary obstacle to collections (Philadelphia City Controller, 2000). The City and School District ended up settling out of court with bondholders in order to avoid litigation (D'Ambrosio, 2004).

New Haven completed a deal for about \$18 million in 1995. The City ended up further subsidizing the transactions by buying back some of the least profitable liens before the bonds matured in order to avoid default and prevent the properties from becoming even more physically and financially distressed (Bass, 2001). The City then

foreclosed on those buildings itself and worked with developers to rehabilitate the buildings. New Haven's bond holders were paid back, but the city suffered bad press and political scandal as a result of securitization due to abandonment and deteriorating conditions in many of the properties (Bass, 2001).

In the year 2000, the New York State Legislature authorized the State of New York Municipal Bond Bank Agency or (MBBA) to create a program to aid any New York State municipality that wanted to securitize delinquent tax receivables. Only one transaction was ever realized under the program. In 2003, the MBBA sold approximately \$15.1 million worth of bonds to institutional investors, backed by \$22.5 million of unpaid tax liens from Syracuse, Buffalo, Binghamton, and Plattsburgh. The program generated immediate revenue for these cities: \$4.3 million for Buffalo, nearly \$6.4 million for Syracuse, almost \$1.9 million for Binghamton and \$109,000 for Plattsburgh.

Collections and sales of properties foreclosed by the trust did not meet expectations. MBBA cited the difficulties with the liens from the City of Buffalo. Many properties with liens sold remained vacant or abandoned. Approximately 64% of the liens in the trust were in properties with lien-to-value ratios in excess of 20%. The majority of the lien pool came from Buffalo, and 75% of those were ultimately determined to have no value.

The localities settled out of court with the bondholders in order to avoid litigation. Before the settlement, \$8.6 million of the bonds had still not been repaid. In 2007, the MBBA settled with the bondholders for \$5.34 million. It also succeeded in obtaining reductions in fees from the legal and financial advisors involved in the transaction. As part of the settlement, the MBBA also returned the outstanding liens to the cities, which

could then apply for state funding to demolish or rehabilitate vacant, abandoned, condemned and surplus properties (New York Housing Finance Authority, 2007).

While administrative difficulties impeded collections in some cases, the high lien-to-value ratio for properties in the pool has been cited as a main obstacle in all of the above cases. Thus, securitization was not a viable way to offload "toxic assets" for localities without consequence. When I asked one industry insider why municipally-sponsored tax lien securitization was no longer popular, the response was that for "these smaller cities, it's just not worth it to them" (Interview, 5/2012). The process of securitization is expensive. The up-front costs associated with a securitization transaction are substantial and include due diligence, rating agency fees, underwriting fees, and a reserve account. (Poindexter et. al, 1996) As one tax lien fund manager stated:

Converting liens into bonds goes through a number of steps, with each participant taking a piece of the pie. By the end of the process, investors often find bond yields are roughly equivalent to comparably-graded corporate [bonds] (Uhlfelder, 2004).

For the top 20 underwriting firms in the country, the average fee charged for underwriting asset-backed securitization transactions between 1999 and 2006 was .34% of the value of the total bond amount (Puskar and Gottesman, 2012). As for the cost of obtaining credit ratings, in 2011, Moody's charged a standard fee of .05% of the total amount being raised, with a minimum of \$73,000. Standard & Poor charged .045% with an \$80,000 minimum (Faux, 2011).

Essentially, the combined costs of administering collections and foreclosures, interest yield for bondholders, fees to ratings agencies and other financial intermediaries were more than the transaction could bear. Without significant public subsidy through

removal of less valuable liens, municipally-sponsored tax lien securitization could not deliver the kinds of high yields it had promised for investors, nor the financial risk management it had promised cities. Cities had accepted partial financial risk in the transaction by holding subordinate notes with the chance to retain greater monetary returns after the bonds matured. This largely did not materialize, as municipalities had to relinquish their subordinate notes to make up for inadequate collections. Localities and their financial intermediary partners looked to other ways to harness capital markets for their tax enforcement purposes. At the time of writing, no other municipalities have pursued municipally-sponsored tax lien securitization since these first failed experiments.

Table 3.1

*Selected tax lien securitization bond issues and tax lien collateral amounts*

<b>City</b>	<b>Year</b>	<b>Bond issue amount</b>	<b>Tax lien collateral amount</b>
Jersey City	1993	\$25 million	\$43.7 million
MBBA	2003	\$15.1 million	\$22.5 million
Philadelphia	2004	\$75.5 million	\$106.3 million

### **3.7. Different kinds of capital, shifting subject positions**

However, the failure of municipally-sponsored securitization as a model did not mean that tax liens were not integrated into global capital markets during this period. This also did not mean that there was not money to be made for companies acting as intermediaries between local governments looking to raise cash through lien sales and various forms of global capital. Financial intermediaries switched the kind of capital they were targeting and the kinds of arrangements they attempted to make. These early experiments demonstrated to localities and their partner financial intermediaries that

investors looking for "investment grade" bonds were not always the appropriate market for the tax lien market. This was the case primarily because the costs associated with municipally-sponsored securitization were too large to make the transaction worth it for both localities and investors. Thus localities and their partners turned to other arrangements which differed in two main ways. First, they sought to engage different kinds of capital markets - often hedge funds that were seeking higher yields from higher risk investments. Second, the locality occupied a different subject position vis-a-vis the capital markets. They were no longer the sponsor or issuer, but simply the seller of receivables. Often the bulk sales were conducted with the same financial intermediaries as the municipally-sponsored securitization, however the institutional form was different (Brown, 1996; City of New Haven, 1995).

Much of the scholarship on the financialization of local governance documents the degree to which local governments are integrated into global capital markets, treating those markets as monolithic. I argue that elucidating *which* capital markets and *how* local governments are integrated matters. Since the 1990s, companies akin to earlier lien-buying syndicates have increasingly used the hedge-fund as a vehicle for tax lien investment (Ip, 2005). As a repository for capital from investors interested in higher risk investments, hedge funds focused on "short-term derivatives including futures, options, swaps, interest rate spreads and other arbitrage strategies" (de la Torre and Martinez, n.d.:6). Tax lien hedge funds have grown in popularity, often catering to accredited investors. These companies are part of a broader growing debt-buying industry that deals in other receivables that aren't investment grade (Federal Trade Commission, 2013). These funds employ a variety of business models, but share the characteristic of

searching for higher yields for their investors than municipally-sponsored securitization could provide. In the mid-2000s, some of these companies reported annualized returns that ranged between 8.9 and 13.5 percent (Uhlfelder, 2004). Bloomberg Businessweek reported in 2012 that a portfolio of “quality” tax lien assets (i.e. liens that redeem before the lien buyer can pursue foreclosure) might typically return about 6 percent to 9 percent annually (Ody, 2012). Compare this to the less than 2% return on the investment grade 2013 New York City Tax Lien Trust. These funds also often receive financial backing from larger financial institutions which either purchase the liens directly or lend to the funds (Schulte and Protes, 2010).

Some of these liens are securitized into bonds, but it is private actors such as Citibank and Bank of America that sponsor the securitizations, not local governments (Business Wire, 1999; Schulte and Protes, 2010). These liens can be sold and resold to a variety of operators. Liens are aggregated either by the locality through a bulk sale or by companies who bid on and buy a large number of liens. There is evidence that these securitizations are becoming more popular given that the ratings agency Moody's issued new standards for rating such securities in 2014.

Many cities have found while they receive more cash upfront from bulk sales than they would through securitization, and they are able to at least nominally pass on financial risk through these transactions, selling liens to these higher risk funds has come with a host of other problems such as large numbers of properties entering legal limbo and blocking redevelopment and revitalization (Center for Community Progress, 2013; Mallach, 2006). In sum, neither securitization of tax liens nor bulk sales overcame certain perennial problems with tax sales, problems that predated financialization and



neoliberalization. In any tax sale, investors have incentive to focus their energies on collecting or liquidating the most valuable properties--and neglecting the most distressed properties on which debts have accumulated higher than possible sales prices (Bass, 2001). As Frank Alexander (2011:51) writes:

The sale of tax liens to private investors divides the incentives and functions inherent in the core governmental power of taxation. The incentives of a private tax lien investor are simply to maximize its rate of return, most easily accomplished by undertaking the least possible efforts to allow the property owner to redeem the property from the tax lien. The private tax lien investor has no formal obligation to invest further in the property, and certainly little incentive to promote the general welfare or the common good. It is not uncommon for tax lien investors to allow subsequent years of taxes to go unpaid or to wait years before electing to enforce their liens.

As a result, some localities have turned to land-banking and other strategies in an effort to counter the ill-effects of tax sales and some have decided to maintain public control of delinquent tax collection and use it as a way to finance those land-banking strategies (Alexander, 2011).

### **3.8. Conclusion**

The emergence of municipally-sponsored tax lien securitization in the 1990's was the result of the convergence of particular fiscal challenges facing cities, changes in municipal finance and innovations in the secondary mortgage market. Local sales of tax liens were long considered a legitimate form of public asset privatization and debt sale, making them good candidates for these first experiments in municipally sponsored asset securitization.

However, for the localities and their financial intermediary partners, municipally-sponsored securitization failed to deliver on its promise for two reasons: the high

transaction costs associated with securitization and the fact that the securitization arrangement did not pass on risk from non-performing assets to a degree that merited the high transactional costs borne by localities. As the market for investment grade bonds failed to meet localities' needs, private funds and debt buyers stepped in that were willing to buy the liens without the related fees associated with creating investment grade bonds. In selling tax liens to hedge funds instead of packaging them as investment grade bonds, localities received a higher upfront payment. But they had to accept the liabilities associated with hedge funds which were looking for higher yields and which had the resources and willingness to take certain steps necessary to realize those yields. The experiences of these localities makes clearer the differences between the kinds of capital markets involved in the financialization of local government operations during the period and the implications of those differences.

Of all of the localities that experimented with municipally-sponsored tax lien securitization, New York City was the only one to adopt the practice on a long-term basis, accepting the high transaction costs associated with it. In the following chapters, I will explore the particular political and historical circumstances that resulted in a different calculus for New York than for the other localities that also attempted lien securitization. Exploring New York City's so-called successful experiment will shed further light on what sponsoring securitization can and can not accomplish for municipalities.

## **Chapter 4: The Path to Tax Lien Securitization in New York City**

"The city was nervous about the PR, but moved forward because they were desperate for cash. There were some egregious cases that helped sell the public."

-Charlie Henneman, Standard and Poor Structured Finance analyst, 1996 (quoted in Long, 2013)

In this chapter, I investigate the particular circumstances that propelled the adoption of tax lien securitization in New York City and shaped the form that it took. I examine why then-New York Mayor Rudolf Giuliani pursued lien securitization, and how he overcame political opposition to the idea. In particular, I document the means by which the Giuliani administration recast a complicated history of housing abandonment in New York into a narrative about chronic municipal dysfunction. Additionally, in explaining why New York City's program developed differently from that of other cities, I clarify the critical role the local state plays in ensuring the viability of new financial instruments, and how this role itself is contingent on political negotiation and compromise.

The chapter is organized as follows. First, I examine the fiscal circumstances in the early 1990s that drove New York City (under the administrations of both Mayor David Dinkins in 1993 and Mayor Giuliani in 1995) to explore short-term financing options involving New York City's delinquent tax receivables.

Second, I elucidate the primary reasons that sponsoring tax lien securitization was attractive to the Giuliani administration, which included accessing immediate off-balance-sheet financing as well as allowing the City to enforce property taxes without having to directly take title to any properties.

Third, I examine the political challenges facing the Giuliani administration as it sought the legal authorization it needed to conduct tax lien securitization. I argue that given these challenges, the Giuliani administration chose to embed its proposal to securitize tax liens within a broader reform effort targeting distressed residential property. In order to generate support for its proposal, the administration tapped into residual public anxieties about large-scale housing abandonment in the 1970s and fueled a growing crisis of confidence about the public sector's ability to manage tax-foreclosed residential properties. It also drew on longstanding ambivalence towards the City's commitment to using tax-foreclosed property as a low-income housing resource.

Fourth, I argue that these particular political contestations produced a less risk-laden form of tax lien securitization than in other cities, which ultimately ensured the viability of New York's tax-lien backed bonds as financial instruments.

#### **4.1. Prior opposition to tax lien sales**

New York City had sold individual tax liens to investors for the first half of the twentieth century, but stopped selling them in the 1950s after a series of corruption scandals (Braconi, 1999). As New York City's real estate market became more attractive to investors in the 1990s, they lobbied the City to begin selling tax liens again. In 1991, for example, investors interested in buying property tax liens formed Citizens to Collect Real Estate Debts Owed New York City in order to lobby the City to allow tax lien sales. These efforts gained momentum after the 1993 Jersey City tax lien securitization. The fiscally conservative City Journal published articles in favor of replicating the Jersey City model and some City Council members introduced a proposal to do so as part of the

city's fiscal 1994 budget. However, the proposal met with opposition both within the Council and from the administration of then Mayor David Dinkins because of concerns over the welfare of both property owners and tenants and loss of public control over the tax foreclosure process (Public Hearing, 1996; Silber, 1993).

Like many other US cities in the 1990s, New York City faced tremendous fiscal pressures. De-industrialization and disinvestment, cuts in federal funding and the exodus of many wealthy and middle class New Yorkers to the suburbs had squeezed the city's coffers. Mired in recession in the early 1990s, New York City faced mounting fiscal pressures and declining revenues partially as a result of rising property tax delinquency. However, the Dinkins administration, leery of the potential consequences of tax lien sales for residential properties, decided to borrow against uncollected tax receivables instead of selling tax liens. It was the first time in history that New York City had borrowed against delinquent property taxes. For fiscal year 1994, Chemical Bank lent the city \$215 million at about 5 percent interest, according to city officials, taking \$400 million in unpaid property-tax obligations as collateral. The Bank subsequently securitized the income stream it received from the liens. In this deal, the City still remained the tax collector and retained the right to foreclosure. While City Council opponents to tax lien sales and housing advocates preferred this form of borrowing to a tax lien sale, the plan was heavily criticized by fiscal monitors as borrowing against future revenue (McKinley, 1993). However, one public finance industry professional did defend the practice in a *New York Times* letter to the editor (Stach, 1993:1):

A Jan. 30 article reports criticism of Mayor David N. Dinkins's proposal for New York City to borrow \$215 million from Chemical Bank, using unpaid city property taxes as collateral. Far from being "financial gimmickry," as you call it, the proposal makes good financial sense. The process underlying this proposal is

securitization -- the structuring of nontradable financial transactions into tradable securities. While the securitization and sale of uncollected receipts is common practice in industry (and has also been used by the Federal Government), it is a technique that most municipalities have not yet discovered. New York City officials should be commended for recognizing that the securitization of property tax liens is both an appropriate and an advantageous way to borrow against short-term receivables.

#### **4.2. Out of short-term financing possibilities**

In 1994, Rudolf Giuliani was elected Mayor of New York City, the first Republican mayor in thirty years. Like many Republican office-seekers in the 1990s, he was largely elected on the promise of reducing government spending on entitlements such as public assistance and reining in budget deficits. Giuliani's ideological commitment to cutting spending on social programs dovetailed with real fiscal constraints facing the City at the time. New York City faced particular scrutiny over its fiscal circumstances because of its high profile history of near default in the 1970s. Since the 1970's fiscal crisis, New York State law mandated that the City maintain a balanced budget and prepare a four-year financial plan that outlines proposed gap-closing programs for fiscal years with projected gaps (Shefter, 1985; Tabb, 1982). These plans were carefully reviewed by fiscal monitors and bond raters. In the 1990s, budget deficits grew as the national recession lingered longer in New York City than in many other places in the country and the City began to face intense pressure from bond rating agencies and Wall Street creditors to fix its fiscal problems.

By the mid 1990s, the situation reached a breaking point with a projected \$2.6 billion budget deficit for the fiscal year 1997 budget, and looming deficits in subsequent years that were unprecedented in the city's history. A *New York Times* editorial in 1996 stated that those numbers "set off alarms in the office of every fiscal monitor and bond

rater in the city". Early in 1995, Standard and Poor's threatened to downgrade \$23 billion of the city's outstanding debt. One Wall Street analyst remarked, "New York is a credit that one is always worried about...But the level of worry has ratcheted up a bit in the past six months" (Dunstan, 1995: 8).

Modest revenues had very recently begun flowing to the City from a nascent Wall Street boom; but in 1995, it was still too early for many to have foreseen the spectacular ascent that would take place over the next decade. At the end of 1996, the Democratic chairman of the City Council Finance committee would say, "The gods of Wall Street smiled on us this year, but we don't know if they will do so next year" (Levy, 1996: para. 7).

For the administration of Mayor Rudolf Giuliani, growing fiscal pressures had created opportunities to push through large-scale cuts in public expenditures. These included large cuts to social services and entitlement programs. However, even with very large cuts to spending, budget shortfalls persisted due to the fact that expenditures nevertheless continued to rise faster than revenues, and the Giuliani administration refused to consider working with New York State to raise city taxes (Levy, 1996).

In the early 1990s, the city's bond offerings were quickly bought up, in part because buyers were attracted to the high interest rates that the city had to pay given relatively low ratings from bond-rating firms (Levy, 1996). However, many such traditional financing options were closing as the City was bumping up against its state-mandated debt ceiling (Braconi, 1999). New York State and many other states in the US added constitutional debt limits during the 1870s after the depression of the 1870s led to large-scale defaults on municipal bonds (Sbragia, 1996). Under the state constitution,

New York City may not borrow in excess of ten percent of the five-year average full value of real property within its boundaries (Gelfand, 1978). In 1995, the City owed \$26.6 billion, approaching its overall debt limit of \$35 billion at the time (Stern, 1996).

It was in this context that the company WR Lazard and the Giuliani administration began working together to explore the possibility of a municipally-sponsored tax lien securitization in New York City. Sponsoring a securitization via a tax lien sale would allow Giuliani to avoid adding debt to the City's balance sheet.

WR Lazard was a New York-based investment firm long active in the municipal bond business, and at the time, was managing New York City's pension funds. The firm had served as financial adviser to Jersey City for its property tax lien securitization (Beckett, 2000). WR Lazard staff approached Giuliani budget staff about the proposal. Some of Giuliani's high-level aides had previous employment experiences in finance. The proposal was therefore easily understood and accepted within the administration (Interview 8/17/12). WR Lazard explained the value of sponsoring a securitization in this way:

There are investors willing to step into the shoes of delinquent taxpayers and payoff their debts to the City, and they should be permitted to do so. The City benefits, responsible property owners benefit and delinquent taxpayers are no worse off (WR Lazard, 1995: 3).

WR Lazard argued that securitization would produce more revenue, and sooner than a traditional tax lien sale. In November of 1995, New York City officially hired WR Lazard as its financial advisor on the deal. WR Lazard compared securitization to the strategy of selling "whole liens" outright, which was the traditional form that lien sales took in which investors would purchase the entire lien, instead of a share from a pool of bundled liens, as is the case with securitization. The firm argued that securitization had



the benefits of retaining upside potential, partial transfer of risk to third party, and producing an optimal amount of cash given the collateral available. The company produced a chart similar to the one shown in Table 4.1 as a summary of these arguments.

Table 4.1

*Chart summarizing advantages and disadvantages of tax lien securitization*

<b>Characteristic</b>	<b>Current Practice</b>	<b>Securitization</b>	<b>Bulk Lien Sale</b>
Asset Sale	No	Yes	Yes
Retain Upside Potential	Yes	Yes	No
Transfer of Risk to Third Party	No	Partial	Yes
Change in Collection Procedures (Specialized Servicer)	Possible	Yes	Yes
Collateral Efficiency (Cash/Collateral)	0%	60-80%	31%

*Note.* Adapted from *Tax Lien Collection Strategies*, by the WR Lazard & Co, Inc., 1995.

As the asset-backed security market continued to expand, Wall Street and institutional investors had expressed significant interest in tax-lien backed securities

(Schundler, 2002). The firm also argued that there was a high demand for these types of securities. A report prepared by the firm for the City stated:

Institutional investors now compete feverishly with one another to purchase municipal tax liens. In recent years, investor demand for tax liens has expanded dramatically, providing a ready and liquid market for New York City's tax liens, and for securities backed by tax liens (City of New York, 1995: 5).

Additionally, the administration had been looking for a way to enforce property taxes without having to take title to tax-foreclosed properties. As property tax delinquency and property abandonment began to increase in the 1990s as a result of the recession, both the Dinkins and Giuliani administrations had quietly stopped confiscating tax-foreclosed properties. Securitizing the tax liens was appealing to the administration because it meant that the City could avoid directly taking title to tax-foreclosed properties, and being directly accountable for its management and disposition. Also creating urgency at that time was the fact that the City was facing federal cuts in Community Development Block Grants, which largely had paid for the costs of managing tax-foreclosed properties (Allred, 2000).

### **"Nervous about the PR, but desperate for cash"**

The administration originally decided to begin implementing lien securitization as a pilot program with a small number of liens. But as ramifications of the impending budget crisis grew, the administration decided to attempt securitization on a large scale immediately to raise funds to fill the upcoming fiscal year's budget gap (Interview, 8/17/12).

Given the political opposition to earlier attempts to initiate tax lien sales, the Giuliani administration knew it had to tread carefully (New York City Department of Finance and Housing Preservation and Development, 1995). According to one ratings agency employee involved in the 1996 transaction, "The city was nervous about the PR, but moved forward because they were desperate for cash" (Long, 2013). Internal documents also show that the administration had hoped to avoid legislation altogether and pursue lien securitization and privatization through an administrative route. The administration explored various legal avenues to conduct the lien sale without having to pass legislation through the City Council because it knew that the legislative process would delay the sale and draw more public scrutiny (Wright, 1995). However, legally, it was unable to do so, and ultimately had to obtain City Council legislation in order to move forward.

Proposed legislation to authorize a lien sale had not passed political muster in the prior attempt because of concern about the implications for the city's housing stock (Silber, 1993). In order to overcome the potential political opposition it anticipated, the administration did two things. First, it embedded the lien sale in a broader policy overhaul with regard to housing abandonment and distressed residential housing. Second, in order to generate political support for that broader overhaul, it fueled a growing crisis of confidence about the city's ability to manage tax-foreclosed properties.

### *The compromise*

The administration thus embarked on embedding its lien sale proposal in a broader overhaul of its policy towards distressed property and housing abandonment. For help in

crafting a proposal, the administration reached out the City's Department of Housing Preservation and Development (HPD), whose responsibility it was to manage and rehabilitate tax-foreclosed properties. Officials at HPD at the time had strong concerns about the potential impact of the lien sale on distressed residential property (Allred, 2000: 3), but saw an opportunity to make changes to improve the overall system for addressing distressed residential properties. As Harold Shultz, a former HPD official who helped to conceive of the new City policy to intervene with regard to distressed properties remembers it:

So Finance come to us and says, "We're going to enforce the tax laws and we're going to do it by tax lien sale. We want you to help build the system." So we were like, "Ok, we'll help you build the system", [but] we had issues... We put it in a different way because we weren't putting it in terms of "We're going to help your tax lien sale." We put it in the context of there are a lot of properties out there that are still in terrible shape that don't have an economic value, and if you put them out there, no one will fix them because they're simply not worth the cost of fixing. They are in neighborhoods in which the market is too weak...leaving these properties in a non-rehabbed state tossing them into the private market, you'll still have properties that are going nowhere...To some extent, the Finance folks kind of recognized this in their own way (Interview, 2012).

HPD proposed a set of reforms in which the agency would still play a role in rehabilitating distressed properties. HPD argued that distressed properties should be removed from the lien sale and rehabilitated through an HPD-supported process. Shultz also described the need for the administration to acknowledge political support for the City role in the intervention and rehabilitation of distressed buildings:

Our first argument, which we basically won within the administration was that there needed to be two systems...The political infighting on this was kind of an issue...people wanted HPD to rehab more and more buildings...you probably could not have gotten through the Council a system in which HPD stepped aside and stopped rehabbing properties.

Thus, the administration embarked on a designing a program in which there would be two separate systems: a lien sale for the majority of tax delinquent properties, and a separate system for residential properties deemed to be distressed. One consequence of excluding distressed residential properties from lien sale and securitization was that New York City's lien securitization transactions would be less risky than similar programs in other cities.

In the plan that was devised, the lien sale was paired with a new "Third Party Transfer" program in which HPD would shepherd distressed properties excluded from the lien sale through a rehabilitation process with private or non-profit developers. By excluding buildings from securitization that were less likely to pay their taxes, the City could create a pool of liens with greater overall value, removing risk and making it more attractive to investors. Distressed multi-dwelling residential properties whose assessed value was low in relation with the amount of tax arrears or those with significant physical deterioration would be excluded from the sale on the principle that their owners had less economic incentive to pay off their tax debt.

The City embarked on research to decide which liens to exclude from the pool. The combined years of HPD's experience and its resulting knowledge and expertise dealing with distressed housing meant the City also had more capacity and commitment to accurately screen and identify distressed property than other cities pursuing lien securitization. A trade publication of housing professionals reported in 1995 that:

An investment bank has analyzed a sample of properties in the foreclosure pipeline on behalf of the city, and concluded that once tax arrears reach 30 percent of assessed value, there would be little investor interest in purchasing the tax lien. HPD also studied the characteristics of buildings taken in rem in the past and found that, when tax delinquency reaches the same 30 percent of assessed value threshold, there is relatively little chance that it will be redeemed by

owners. Combined with other indicators the city collects, including information on code violations, emergency repair orders and the like, officials believe it is possible to predict fairly accurately which buildings would be destined for city ownership (CHPCNY, 1995: 1).

Consensus was achieved on the criteria for excluding buildings from the lien sale which accounted for both the property's debt load in relation to its market value, and the property's physical condition. Properties that had a fifteen percent or more tax lien-to-market value ratio, and had a certain number of code violations or had in the past had hazardous conditions which required the City to make emergency repairs would be excluded. More specifically, a property would be excluded if it had five or more Class B (such as rodent infestation) or Class C (such as lack of heat or hot water) code violations per unit. Alternately, a property could be excluded if the property owner owed \$1,000 or more to the City on the building because HPD had made emergency repairs to correct hazardous conditions when the landlord had failed to do so (City of New York, 1996) .

When presenting its proposal publicly, the administration emphasized the problems with distressed properties and highlighted the new resources the City would commit to intervention with distressed properties. In fiscal year 1994, Giuliani's first year in office, New York City managed 30,358 housing units in previously tax-foreclosed properties. In October 1995, the administration published and disseminated a document entitled, "Breaking the "In Rem" Cycle: The Giuliani Administration's Proposal to Reshape NYC's Property Tax Enforcement and Housing Preservation Policies." In that document, the tax lien sale was relegated to a minor bullet point while pages were devoted to other interventions the city would make with regard to distressed properties. In addition, the administration made very little mention of securitization. The document

mentions the possibility of securitization only once in a parenthetical phrase, although it does make several oblique references to Jersey City facing similar challenges with property tax enforcement (Giuliani administration, 1996; City of New York, 2001).

When publicly questioned about the proposed lien sale, the administration emphasized that it was primarily an enforcement tool to encourage property owners to pay their taxes on time, not a short term off-balance-sheet financing tool to plug urgent holes in the budget. A senior official publicly stated, "We view this as an enforcement tool; it just happens to have the effect of producing revenue" (Johnston, 1996: 35). However, internally the administration acknowledged that the city's previous enforcement mechanisms had been "extremely effective" and "relatively inexpensive", with collection rates hovering between ninety-five and ninety-eight percent in previous years (New York City Department of Finance and New York City Department of Housing Preservation and Development, 1995: 1). While there was a small rise in property tax delinquency during the recession beginning in 1990, delinquency rates were far from the levels they had been in the 1970s.

The administration was more in need of a short term infusion of cash that would be generated by selling the liens than it was in need of a new tool to address widespread tax delinquency or enforce property taxes in general.

With a proposal in hand to overhaul policy towards distressed housing that included the sale of property tax liens, the administration's next task was to generate enough political will to obtain City Council authorization for its proposal. In this vein, a growing public concern about the City's management of tax-foreclosed properties provided an opportunity for the administration.

### **Housing abandonment, New York's response and structural racism**

In the decades of the mid-twentieth century, the long-term effects of structural racism (including federal policies resulting in redlining, residential segregation and labor market segregation) compounded by capital flight and deindustrialization produced large scale disinvestment in cities resulting in economic hardship for urban residents and fiscal crisis for municipal governments (Marcuse, 1985; Denton and Massey, 1998; Wilson, 1996; Shefter, 1992; Sugrue, 1998; Wilder, 2000; Sites, 1997; Keenan, Lowe and Spencer, 1999).

In New York City in particular, Frank Braconi describes how this produced massive waves of housing abandonment in New York City in the 1970s as it became harder for owners of rental housing to meet expenses.

The fundamental cause of housing abandonment was demographic change and the steady impoverishment and depopulation of many inner-city neighborhoods. As middle- and working-class whites sought more attractive housing options...black and Puerto Rican migrants replaced them in the city's older, more densely built neighborhoods...These minorities tended to have lower incomes and far higher rates of joblessness, making it more difficult for owners of marginal rental buildings to collect rents commensurate with building maintenance and operating expenses (Braconi, 1999: 94).

Another scholar of housing abandonment in New York City writes:

Abandonment hit New York City neighborhoods like a firestorm. Cash flow problems have arisen for the City's landlords for a variety of reasons: incomes among the poor and working classes have not kept pace with inflation, public assistance programs have generally fallen behind housing costs, housing costs have increased dramatically, rent regulation has limited revenue in some buildings and the City's population has declined. Adding to the severity of the problem, many of the abandoned buildings are occupied or partially occupied, while abandoned buildings in other cities are largely vacant (Reiss, 1996: 787).



The combination of soaring heating oil prices and other operating costs throughout the seventies and slow-growing rents as per New York's rent regulations also contributed to housing abandonment (Stegman, 1985; Braconi, 1999). In this context, many property owners sought to strip the last bits of value from buildings by setting fire to their properties in an effort to collect insurance payments (*Time Magazine*, 1977).

In an effort to increase public revenues and short circuit the decline of conditions in abandoned buildings, New York City changed its policies on tax enforcement in 1978. It adopted a new law in 1978, which allowed properties to be foreclosed on for tax arrears once their owners were one year behind in payments rather than three years as was previously the rule. As a result of the new law, the quantity of buildings eligible for city takeover increased substantially. The City also stopped auctions of tax foreclosed properties, after realizing that these auctions were counterproductive, as they failed to generate revenues because purchasers failed to pay taxes and properties continued to deteriorate. Instead, the City chose to take title to these properties itself with the goal of mitigating the worst effects of abandonment. The city's inventory of *in rem* buildings quadrupled between 1976 and 1978, increasing from 2,500 to 9,500 buildings (Braconi, 1999:98). Between 1978 and 1981, the City took over more than 16,500 residential properties, both vacant and occupied. These properties become commonly referred to as "*in rem*" properties, in reference to the Latin term describing the legal process used to foreclose. Eighteen percent of the occupied *in rem* units were in buildings categorized as dilapidated, a rate four times that in the city as a whole. Eighty-one percent of the tenants were people of color. They were mostly poor, with a median income of \$6,865, which was only 62 percent of that of all renters (Lawson, 1986; Stegman, 1982).

The management of these properties became even more difficult in the 1980s, as the City began placing homeless individuals and families in the properties. Inadequate income supports for recipients of public assistance fueled the rapid growth of family homelessness in the 1980s. Frank Braconi (1999: 103) argues that the City's *in rem* housing challenges were compounded by the failure of a broader welfare policy on the part of the federal government, state and city:

As family homelessness emerged as a major social problem during the early 1980s, the Koch Administration, under intense pressure from the advocacy community, the media and the courts (Kircheimer 1990), desperately sought permanent housing resources into which homeless families could be placed. Meeting disinterest by private housers and resistance from the New York City Housing Authority, the Administration focused on HPD's inventory and in 1983 adopted a policy of filling all vacancies in *in rem* buildings with referrals from the city's shelter network. The decision to use *in rem* buildings as the city's "housing of last resort" greatly complicated subsequent management and disposition efforts. Between 1987 and 1995, the city placed almost 13,000 families into *in rem* buildings, representing about 40% of all homeless families relocated to permanent housing.

Braconi (199: 103) also explains the relationship between public assistance policy and the challenges facing the *in rem* housing program:

Family homelessness has been a direct and predictable outcome of the state and city's unrealistically low welfare grants...with options for placing homeless families in private and conventional public housing thus limited, the *in rem* stock served as a relief valve for the state and city's myopic welfare policy

From the inception of the City's *in rem* housing program in 1978, frustration about the challenges the city faced with managing *in rem* residential buildings was often directed at the tenants who inhabited those buildings. As early as 1979, Mayor Koch publicly maligned low-income tenants of color living in city-owned buildings. New York Magazine reported:

A testy Mayor Koch on several occasions has gone out of his way to antagonize the minority constituency in [City-owned *in rem* buildings]. During one televised appearance, the mayor told a group of *in rem* tenants, "Pay your rent or get out." During another Koch recalled, "I grew up in a neighborhood where people didn't burn down the buildings in which they lived" (*New York Magazine*, 1979: 58).

Beginning in the Koch administration, the City began to reduce the number of properties it owned and managed and focused instead on selling buildings and minimizing interim management costs while maximizing sales prices (Lawson, 1986). The City developed a series of aggressive programs to dispose of properties and sold them to for-profit owners, to community-based organizations, and to limited-equity tenant cooperatives (Sierra, 1993). Through the Tenant Interim Lease Program (TIL), established in 1978, tenants of city-owned buildings could go through an interim period managing the building while they received training and support to prepare them for co-op ownership. In many cases, these tenants were already de-facto managers of their landlord-abandoned buildings. The city performed major capital improvements to the building before the tenants bought their apartments at a low cost (Urban Homesteading Assistance Board, n.d.). TIL was initiated at the behest of the Urban Homesteading Assistance Board, which pioneered the model and successfully persuaded the City to develop programming that would support the transformation of city-owned properties into owner-occupied limited equity co-ops (Cotton and Reiss, 1996). HPD during this period came to be recognized as one of the best municipal development agencies in the country as it rehabilitated hundreds of thousands of severely distressed residential units (Polner, 2005).

Throughout the 1980s, well-organized tenant constituencies and a strong housing advocacy lobby influenced City disposition efforts in a variety of ways, pushing for City-owned properties to be turned into affordable rental housing and limited equity co-ops

and organizing and mounting legal challenges against disposition programs that could lead to rent increases or displacement. They used a variety of strategies and took advantage of legal provisions mandating extensive public review procedures for city property disposition.

While many units were transferred out of city ownership through a variety of disposition programs, the scale of property abandonment and other obstacles to disposition (including political opposition) meant that the City continued to manage and maintain thousands of *in rem* properties for the next decade (Angotti, 2008; Sites, 2003). Many of these were concentrated in communities of color such as Central Harlem, Bedford-Stuyvesant, western Harlem, the South Bronx, East New York, Bushwick and South Jamaica (Chen, 2003). Late in the 1980s, a commissioner of HPD remarked of the *in rem* program, "We'll be in the business of providing housing for low-income New Yorkers for the foreseeable future. It's not a business we like to be in, but there is no alternative" (DePalma, 1986: 1). Another later commissioner stated "We don't ever expect to be in a position where we are out of the housing business" (DePalma, 1988: 1).

Well into the 1990s, these properties continued to be concentrated in the poorest neighborhoods in New York City and housed some of the city's poorest residents (Blackburn, 1995; Schill and Scafidi, 1996). In fact, *in rem* tenants were getting even poorer in the early 1990s. *In rem* household incomes in 1992 averaged \$6,420, declining 14 percent from 1990. This was significantly lower than average incomes for public housing residents which was \$7,800 at that time. The average for all New York renters was \$19,000. A 1994 survey of Brooklyn *in rem* households showed that tenants were

overwhelmingly African-American and Latino, as were the neighborhoods where *in rem* housing stock was concentrated (Saegert and Winkel, 1998).

By the mid-1990s, as with other public programs which were largely seen to serve poor people of color, political will to continue managing *in rem* buildings as a housing resource waned significantly. Consistent with neoliberal principles of reducing government's role in providing for people in need, the Giuliani administration sought to dismantle the *in rem* housing program. Harold Shultz, a former senior HPD official describes the shift in attitude towards this stock of housing in the early 1990's:

[For many years], the assumption had been that HPD would continue indefinitely to run some large number of the acquired *in-rem* housing units as some kind of alternative housing authority for low-income folks. That concept changed with the Giuliani administration (Interview, 2012).

Renewing the City's efforts towards aggressive disposition of the inventory of City-owned dwellings, the Giuliani administration sold thousands of properties. Gentrification and an improving real estate market in many areas made disposition easier than it had been previously.

### **Municipal dysfunction**

As gentrification gathered momentum in many previously disinvested areas, housing abandonment and tax delinquency had become much less widespread problems than in earlier decades (Smith, 1996; Reiss, 1998). Nonetheless, some of New York's poorest neighborhoods still struggled with new cases of abandonment in the 1990s.

Braconi (1999: 231) writes:

Despite a decline in rental building values, property tax assessments continued to increase in low-income neighborhoods while soaring water and sewer fees

became a major new source of financial stress. From 1989 to 1995 aggregate property tax arrears for walk-up apartments--the building type most often foreclosed by the city--increased from \$28 million to \$71 million. Although the population of buildings in serious tax trouble has not increased significantly, about 14,000 endangered buildings have fallen deeper into delinquency. In 1996, federal welfare reform legislation further dimmed the financial prospects of low-income housing.

This reality drove political opposition to the prospect of tax lien sales that could further aggravate abandonment issues. In the face of political opposition to tax lien sales, the Giuliani administration and its partners commissioned a private firm to evaluate its programs for city-owned tax-foreclosed properties, many of which the City had taken title to in previous decades. Using as its analytic sample the most distressed properties from the 1970s wave of abandonment, the report made generalizations about projected future costs. It presented alarming figures about the cost of the city's existing *in rem* program, stating that the city spent on average \$2.2 million per building taken, and that buildings were in city ownership for an average of 19 years. It projected that these buildings would cost the city \$10.6 billion over the next twenty years (Arthur Andersen Consulting, 1995: 8). The administration incorporated these findings into a document outlining its proposal for tax lien sales. In this document, it attributes the costs associated with the City's long term ownership of buildings with City policy, stating:

Over the last 18 years, the City's inflexible vesting tools and time-consuming and expensive disposition process have resulted in long-term ownership and management by the City of *in-rem* properties. While many of these buildings would likely have been lost without City action, the resulting impacts on neighborhood quality-of-life and on local real estate markets have been devastating (City of New York, 1995: 4).

While it is impossible to prove or disprove the report's hypothetical predictions about future costs to the City, it is important to point out that some of the data

assumptions made by the report had the effect of exaggerating the projected costs of the program. First, the report estimated average City ownership time of 19 years using HPD's current portfolio of buildings at the time, the buildings left over from the 1970s wave of housing abandonment which had been the hardest to dispose of because of severe financial or physical distress. It did not look at the average amount of ownership time for the entire universe of buildings that had been owned by the City since the 1970s. Second, the report states "average holding period for vacant properties was derived from average holding periods for occupied properties" (Arthur Andersen Consulting, 1995: 4). However, in the City's experience, the rehabilitation and disposition of vacant units was much faster than occupied units. Thus, assuming that vacant properties had the same holding period as occupied properties exaggerated the average amount of time the City had held properties. According to Braconi, the City gut-rehabilitated approximately 40,000 housing units within seven years, "a record that ranks among the most successful urban redevelopment initiatives in the country's history" (1999:105). As one former HPD official told me, "We knew very well how to get properties out the door, we just didn't know how to keep them from coming in" (Interview, 2012).

Indeed, examining the outcomes of Giuliani administration's own disposition programs might very well disprove the reports findings on timelines of disposition. By 1995, when the administration proposed the lien sale, the inventory had already been steadily declining for several years (Oser, 1996). While exact data on average holding times are not available, available figures show that from fiscal year 1994 to October 1998, the City reduced previously tax foreclosed housing units 41% (from 30,358 to 17,941). This was the smallest number of units owned by the City since 1978 when HPD

first took control of *in rem* housing (New York City Mayor's Press Office, 1999). During his term from 1994 to 2001, Giuliani would ultimately privatize more than 20,000 previously confiscated, city-owned units, 78% of the total stock of such properties (Polner, 2005).

By framing its proposal around housing abandonment, the administration's political strategy to obtain tax lien sales relied on a somewhat ahistorical logic. The long-term effects of deindustrialization, federal urban policy and structural racism in New York City housing and employment had produced the abandonment crisis of the previous decades. The administration's political strategy relied to a certain extent on a logic which conflated those historical circumstances with the distinct conditions of New York City in the mid-1990s. However, the shock value of the report's findings generated headlines and most of the media covering the report failed to discuss the data assumptions made by the report. Henneman sums up the strategy, stating, "The[re] were some egregious cases that helped sell the public" (Long, 2013:1).

While the challenges facing the *in rem* housing program were serious and should not be understated, the administration's strategy of exaggerating the program's costs played a large role in recasting a complicated history, which involved both local and extra-local circumstances such as federal disinvestment and long-term structural racism, into a narrative about municipal dysfunction. Indeed, almost two decades later, the Arthur Andersen report's findings have a continuing effect of framing the City's record of *in rem* housing as one of failure and astronomical cost. These findings continue to be cited and misconstrued in reference to the costs of the *in rem* program and used as the primary justification for New York City's tax lien securitization program (IBO, 2014; New York



City Comptroller, 2012). A report issued by the New York City Comptroller in 2012

states:

However, by the early 1990s, the Department of Housing Preservation and Development (HPD) had become the City's largest landlord, consuming substantial resources. The City spent \$2.2 million to manage, repair, and sell each building, and on average, the City would own a property for 19 years.

The Giuliani administration strategically deployed the findings of the report to generate headlines and stoke public concern about the rising costs of City ownership (Hearing testimony, 1996; Giuliani administration, 1995). Internal documents also show that the administration temporarily withheld the report findings from the City Council and strategically timed the public release of information from the report to optimize political momentum for its plan. Deborah Wright (1996), then commissioner of HPD wrote in an internal memo to the Mayor's office:

On October 12th, I testified before the City Council...Based on intense questioning, I promised that we would soon be submitting this legislative initiative [on property tax enforcement policy] to the Council. You should be aware that Council members expressed a keen interest in receiving a copy of the Arthur Andersen study on the City's *in rem* stock, which as you know we have held back pending release of the Administration's new policy...It is crucial for the Administration to surface our own proposal soon if we are to avoid the appearance of responding to the Council's initiative.

By holding back the results of Andersen study, so, the administration was able to pre-empt potential significant internal and external political opposition of its proposal, and to emphasize reform of the *in rem* housing program as its primary goal, as opposed to the less politically popular objective of generating a short term cash infusion.

Fortunately for the administration, in order to lay the legal groundwork for securitization, the City Council simply had to approve bulk sales, in which one party

could purchase a large bundle of liens, as opposed to the more conventional method of individual lien sales. The City's Department of Finance was then authorized to sell to whomever it deemed appropriate. As such, public discussion around the passage of the legislation enabling tax lien securitization focused primarily on the crisis of the City-owned housing, the new Third Party Transfer system, and the composition of the lien sale but very little on the specifics of securitization. In public addresses, Giuliani made oblique references to the need to "modernize" an "archaic" system (Public Hearing, 1996). But the administration made no public announcement about securitization. In fact its plan to securitize tax liens was made public only when its circulation of the Request for Proposals (RFP) for an underwriter was first reported in a financial industry publication (Johnston, 1996).

The Council added a small number of protections, carving out properties that had standalone water and sewer liens and housing units that had been produced under city affordable housing programs, and passed the bill by a large majority (Public Hearing, 1996). The bill did not change interest rates for delinquent taxes (which had been set at 18% compounded daily in 1991), but did allow for the addition of a 5% surcharge to the total amount due from property owners at the time of the sale (City of New York, 1995; New York City Administrative Code, 1996). The Council also obtained an agreement from the administration that it would not sell liens on one-to-three family residential properties in the first lien sale, but at some point in the future it might if those properties accumulated a delinquency of three years or more (Cerullo, 1996). As such the City could avoid displacing homeowners. Charles Henneman, an Standard & Poor analyst involved in the deal, stated that the City made this decision "so it wouldn't have to evict

anyone" (Long, 2013). In the meantime, such properties would continue to have their taxes enforced directly by the City and would not be subject to the 5% sales tax. At the same time, the Council passed a companion bill establishing the new "Third Party Transfer" program in which HPD would shepherd distressed properties excluded from the lien sale through a rehabilitation process with private or non-profit developers.

In sum, the Giuliani administration and its partners successfully drew on public anxieties in the aftermath of earlier waves of housing abandonment to generate momentum for the proposal to sell and securitize New York City property tax liens. As such, it is possible to trace the legacies of structural racism from the roots of housing abandonment through the tribulations of the City's *in rem* housing program in order to better understand the conditions producing both neoliberalization and financialization in urban governance.

#### **4.3. Building the technical infrastructure**

Parallel to the process of clearing these political hurdles, the proponents of lien securitization in New York City also faced technical challenges. Key to being able to launch the program was the role of certain private financial intermediaries in crafting the securitization proposal and designing the legal, technical and administrative infrastructure necessary to implement it.

On the administration's side, Seth Cohen, the Director of the Mayor's Office of Pensions and Public Finance and Special Advisor on Public Finance was the main champion of lien securitization. Cohen had previously worked in the financial industry, most recently at Dean Witter in housing securities and municipal finance. He developed

the securitization plan in close consultation with staff at WR Lazard who had engineered the previous lien securitization in Jersey City. Documentary evidence suggests that WR Lazard's government finance consulting arm the "WRL Advisory Group", played a role at every stage of the process: helping to draft the legislation, drafting the RFP for an underwriter, evaluating applications for underwriters and servicers and hiring Morgan Stanley as the underwriter. One piece of internal correspondence (Response to the City Council's Proposed Amendments to the Tax Lien Bill, 1995, para 3) between City Hall and the City Council noted: "The WRL Advisory Group aided Finance in producing the bill, relying on months of research and years of securitization experience to design the legislation. The bill is modeled after similar laws in other states and municipalities."

By the early 1990s, the technical know-how to structure such transactions was well developed in the private sector, but was still relatively unknown in the public sector. The City had a longstanding relationship with WR Lazard in the municipal bond and pension business and was able to rely on the firm's expertise to design and execute the securitization. In addition, several high level Guiliani administration officials had previously worked in the financial industry, and their familiarity with such transactions facilitated the adoption of these new practices.

With WR Lazard's help, the City issued a Request for Proposals on January 2, 1996 for investment banks to serve as underwriters for the lien securitization. While the RFP was issued on Department of Finance letterhead, the text was largely drafted by WR Lazard staff, and inquiries and proposals were to be sent directly to Joel Cooper at WR Lazard, who was in charge of selecting the underwriter from the large pool of interested parties (New York City Department of Finance, 1996; Commercial Mortgage Alert,

1996). One investment bank would be selected as the lead underwriter, and three other banks would be selected as co-underwriters. This team would be responsible for structuring the transaction, obtaining ratings from ratings agencies and marketing the bonds.

The text of the original 1996 Request for Proposals offers a glimpse into tax lien securitization in its embryonic stage. Along with standard questions about an applicant's relevant past experience, the RFP also asks, “what do you see as the advantages/disadvantages of requiring the servicer to purchase a portion of the City’s interest in the non-cash consideration received in the sale of the liens.” It asks the respondent to “describe the legal structure you propose to accomplish the tax lien securitization. Are there any alternative legal structures that should be considered?” It also asks the applicants, “For this first sale, do you believe that only the high quality liens should be included or should a representative pool be sold.” Other questions point to the concerns considered in the first round, such as how to “establish a broad and liquid market for tax lien securities” and what amount “the market could comfortably absorb”. The document also asks respondents, “What key institutional factors, e.g., the court system, in your opinion will have the greatest effect on the program?” (New York City Department of Finance, 1996). Thus, although the decision to enact lien securitization was swift, the necessary administrative, legal and technical infrastructure necessary was still very much in development as the process unfolded.

Even with these unresolved questions, fiscal pressures pushed New York City's first lien securitization ahead on a tight timeline. The pressure to meet the budget deadline for the coming fiscal year was tremendous. As one person involved in the

transaction recalled, "We were scared to death we weren't going to be able to get it done in time. But Rudy Giuliani is not someone you want on your bad side" (Interview, 8/17/12).

#### **4.4. Success as a financial instrument**

New York City's first lien securitization was completed just a few short months after the legislation was passed, and the Giuliani administration succeeded in raising funds from the sale to fill part of its immediate budget gap for fiscal year 1996-1997. The tax-lien backed bonds did not prove difficult to market, although the buyers for these bonds were significantly different than the buyers for conventional municipal bonds. These bonds were taxable bonds, as opposed to tax-exempt bonds and had higher yields than conventional municipal tax-exempt bonds such as general obligation bonds. The securities were divided into four tranches, with the City holding the most subordinate bonds. (The Jersey City transaction used only two tranches.) At 6.81% to 7.11%, interest rates for New York City's tax-lien backed securities were even higher than the relatively high rates ranging from 4-6% that New York City was paying on its general obligation bonds in fiscal year 1996 (City of New York, 1995). In 1996, the Class A tax lien backed bonds carried an interest rate of 6.81%.

Before the first lien securitization in 1996, New York City had essentially stopped enforcing property taxes when it quietly stopped confiscating buildings for tax arrears in 1993 (Braconi, 1999). News about the impending enforcement actions generated an immediate boost in collections. Charles Henneman commented:

Once they decided to do a deal, a lot of interesting things started to happen. Money started pouring in just from coverage of the deal in the paper (and it

made the tabloids). An initial \$500 million pool of collateral at the time of the announcement paid down to \$251 million by the time the deal closed six or eight weeks later. Morgan Stanley was the lead and my counterparts had tons of stories, and told me a guy in a limo showed up to their offices with a suitcase full of cash to pay back taxes on several apartment buildings.

That first securitization was considered a success as collections more than paid for the bonds that were issued, in contrast to the experience of other cities that sponsored tax lien securitizations. In 1999, the ratings agency Moody's Investor's Service stated that New York City tax lien transactions had performed better than initially expected (Moody's, 1999). As other cities' programs teetered on default and produced concerns about blight, New York City's program has widely been considered a success. Bondholders in each of transactions have been paid back in full. New York City has continued to securitize its property tax liens. Between 1996 and 2011, New York City sold almost \$2 billion in delinquent property tax bills. The City's screening of troubled properties has been credited with the program's success:

The ability of [New York] City to separate from the lien pool residential buildings in need of greater public sector intervention has been a significant reason for the programs' overall success. It has helped to maximize the return to the City from the securitization of the tax liens while preserving and improving a critical housing resource. Thus, we find that to maximize the financial benefits of tax lien securitizations, they must include a well constructed screening process which excludes properties that require other forms of intervention (Perrine, Marrazi and Shultz, 2011).

This success has been predicated on the willingness to invest public resources and subsidize continued public sector involvement in the least valuable properties, a willingness which was borne of a particular set of political contestations. Given that opposition to tax lien sales was strong in New York City, the Giuliani administration needed to incorporate a robust program of intervention for distressed properties in order

to obtain the political support necessary to pass the City Council legislation it needed. Unlike other cities that tried and failed to use securitization to transfer the risk of non-payment from bundles of properties that likely included distressed properties, New York City's objectives were different. New York City instead invested significant public resources in identifying such properties in order to remove them from the lien securitization pool, ensuring both the viability of securitization transactions, and the possibility of effective rehabilitation of those properties.

#### **4.5. Conclusion**

In the early 1990s, confronted with revenue shortfalls due to a lingering recession and motivated by an ideological commitment to changing the role of government, New York City's Mayor at the time, Rudolf Giuliani, looked to securitizing its tax liens as a possible financing solution. Given its political and historical circumstances, New York's city-sponsored tax lien securitization ultimately took a distinct form from that of other cities, a form that arguably ensured the viability of the City's tax-lien backed securities. While all of the other localities that sponsored tax lien securitizations beginning in the 1990s abandoned their programs for the reasons described in the previous chapter, New York has continued to securitize its tax liens for almost two decades.

A particular set of political contestations in New York lay the groundwork for a tax lien securitization program that would be more viable than securitization schemes in other cities. By removing distressed residential properties from its lien sale, the City removed much of the financial risk that had imperiled other cities' lien securitization programs and ensured the viability of its securitized bonds as a financial instrument. In



addition, the City's years of experience, knowledge and expertise dealing with distressed housing meant it had the capacity and commitment to accurately screen and identify distressed property that should be excluded from the lien sale, something that other cities may not have had the capacity to do.

New York City's exclusion of distressed residential property from its tax lien securitization program was rooted in the City's earlier experiences with large scale housing abandonment. Given this troubled history and significant political opposition to tax lien sales, the Giuliani administration might not have obtained legal authorization to sell tax liens without a parallel strategy around distressed housing. To build support for its plan, the administration capitalized on a public crisis of confidence in municipal management of the city's *in rem* housing program that had developed despite the HPD's significant accomplishments given the formidable challenges that New York City's 1970s wave of housing abandonment presented. The administration's efforts also coincided with a waning of public will during this period to continue providing this form of subsidized housing to the tenants of those buildings, who from 1970s to the 1990s were overwhelmingly poor and people of color. While the challenges facing the *in rem* housing program were serious and should not be understated, the administration's actions played a large role in recasting a complicated history, which involved both local and extra-local circumstances such federal disinvestment and long-term structural racism, into a narrative about municipal dysfunction. That narrative persists almost two decades later.

Housing abandonment and the difficulties the City faced in mitigating its effects became a powerful trope and motivating factor for the Giuliani administration's reform efforts. Consequently, tracing the legacies of structural racism—from the roots of

housing abandonment through the City's various attempts to address it— provides important insight on the relationship between the long term effects of racism and the material and ideological conditions producing both neoliberalization and financialization in urban governance.

**Figure 2. Timeline of major events related to property tax enforcement in New York City**

**Post-Civil War** - Like other localities around the US, New York City adopts tax lien sales to raise revenue.

**1950s** - City ceases to use tax lien sales after a series of scandals, and adopts tax foreclosure and tax deed auctions as its primary property tax enforcement mechanism.

**1970s** - City struggles with large scale abandonment, arson, and fiscal crisis. Public auction system for tax-foreclosed property becomes a revolving door.

**1978** - In an attempt to raise revenue and address abandonment, City adopts new *in rem* foreclosure practices, taking title to properties directly and rapidly increasing the numbers of buildings eligible for city confiscation as a result of tax arrears.

**1978** - Working with tenant organizations and housing advocates such as the Urban Homesteading Assistance Board and the Task Force on City-Owned Property, the City establishes Tenant Interim Lease Program (TIL) allowing tenants of city-owned property to form limited-equity co-ops.

**1981** - *Callahan v. Carey* consent decree establishes the legal right to shelter for homeless individuals in New York City.

**1980s** - *City ownership* - Using *in rem* foreclosure, City takes ownership of thousands of properties. It becomes the largest landlord in the city and third largest in the nation. Occupants are largely low-income people of color, many of whom receive public assistance.

*In rem housing as shelter* - To meet legal mandates for sheltering the homeless, the City places thousands of individuals and families into *in rem* property.

*Disposition efforts* - In addition to TIL, City establishes various other programs to transfer properties into private hands many of which are opposed by existing tenants.

**1990s** - Federal cuts to Community Development Block Grants which fund *in rem* program. City initiates large scale disposition to non-profits and for-profit developers.

**1996** - City adopts dual strategy of tax lien securitization and Third Party Transfer.

## **Chapter Five - Selling liens on paper: financialization and new state capacities**

In this chapter, I further explore New York City's experience and critically examine the role of financial engineering in reconfiguring municipal institutional forms and capacities, and the consequences of that reconfiguration.

I suggest that while lien securitization employs the idiom of a tax lien sale, the legal and accounting idiosyncrasies of securitization allow the City to essentially sell tax liens to itself via a subsidiary. I argue that while the City publicly claims to relinquish all responsibility through its lien sale and securitization program, and is commonly understood to do so, in actuality, it only transfers the liens on paper, retaining both the financial risk associated with collections and significant control over administration of the liens. This is in stark contrast to a conventional lien sale in which a local government actually transfers the responsibility for collections and the financial risk associated with administering the lien. I contend that the de-facto monopoly the City maintains on tax lien purchasing via securitization may be to the detriment of tax debtors who often benefit from competitive bidding between purchasers in conventional lien sales.

Finally, I discuss the implications of this arrangement for understanding financialization and the changing municipal state. For New York City, the technique of securitization has not only served as a gateway to new capital, but has also had the effect of fundamentally changing municipal institutional form. I argue that rather than a retreat or reduction of state capacity, the effect of securitizing tax liens is to expand the local government's capacity to raise resources, spend public money and exercise centralized

administrative control over certain aspects of property tax enforcement. With regard to borrowing and spending, tax lien securitization operates with a counter-cyclical logic in that it allows the City to borrow more during times of economic downturn, and to do so without contributing to debt that is counted against its state constitutional limit. When compared to a conventional or bulk lien sale, securitization gives a local government a greater ability to control outcomes and protect its interests. However, it does so with minimal public oversight and little public understanding of the City's role in the arrangement or the public expenditures that are embedded in the transaction.

As such, I suggest that securitization achieves some of the same effects as previous institutional innovations such as public authorities, but with even less transparency. I follow Ashton, Doussard and Weber in documenting how financialization simultaneously grants local governments new powers and further "enmeshes" them in financial relationships and liabilities (2014: 1). In sum, I posit that this arrangement has the effect of trading previous political and regulatory constraints for centralized administrative control and new financial liabilities.

## **5.1. Anatomy of New York's tax lien securitization**

### *5.1.1. Constructing the lien pool*

The rules governing the properties that the City may include in the lien sale have changed with each City Council reauthorization of the process. New York City divides properties into four categories for the purposes of tax collection. Class 1 properties represent residential property of up to three units and most condominiums that are not more than three stories. Class 2 properties are all other property that is not in Class 1 and

is primarily residential such as multi-family residential rentals, cooperatives and condominiums. Class 3 properties are those classified as utilities. Class 4 properties are all commercial and industrial properties, such as office, retail, and factory buildings.

In its initial form, the lien pool included only properties with delinquent property taxes but allowed other charges such as water and sewer fees to be added on if the property had outstanding property tax. Since 2008, stand-alone liens for water and sewer charges have been allowed in the lien pool. In March 2011, the City Council authorized that standalone liens for the Emergency Repair Program (ERP) or the Alternative Enforcement Program (AEP), under which HPD performs repairs on properties with immediately hazardous violations at the owner's expense, would also become eligible for inclusion in the lien pool (New York City Administrative Code, 2012; IBO, 2013).

Currently, liens can be sold on properties that have at least \$1,000 in property tax debt. For Class 1 properties, the taxes must be at least three years overdue, and for Class 2, 3, and 4 properties the taxes must be at least one year overdue. In general, Class 1 properties with at least \$2,000 of water or sewer debt can have their liens sold. For other classes, the limit is \$1,000 of water or sewer debt. In 2010, the City amended its lien sale law to reduce the interest rate charged on tax liens on properties assessed up to \$250,000 from 18% per year compounded daily to 9% per year compounded daily. For properties with an assessed value more than \$250,000, interest remains at 18% per annum, compounded daily. In 2012, it also allowed the sale of tax liens on affordable housing rental properties in the HDFC program, which had been previously excluded.

The City must provide the property owners notice by mail four times before the date of the sale: 90, 60, 30, and 10 days before the sale. As a result of advocacy on behalf

of tax debtors during recent reauthorization of the lien sale, the city has created quarterly and monthly payment plan agreement system that property owners can opt to use to prevent their lien from being sold (Interview, 2012). By law, there is no downpayment required on the installment agreement. The repayment period can range from between eight years and ten years; or if the property owner desires, that period can be shorter. By law, if agreed upon payments are not made for six months, the tax lien may then be sold (Rao, 2012).

Over the years, New York City has instituted a number of exemptions and safeguards to ensure that certain vulnerable populations are protected from the lien sale. The City exempts one-family properties on which only water or sewer charges are owed, but no property taxes are owed. Senior citizens, disabled homeowners and veterans who own and occupy Class 1 properties can also apply for exemptions from the lien sale. Those who receive the State Real Property Tax Credit for Homeowners in the particular tax year can also be excluded. Active military duty personnel may also request that their property be excluded from the lien sale (New York City Department of Finance, 2012).

As per 2011 City Council amendments to the law, the City Department of Finance must be proactive in identifying property owners who may qualify for exemptions. The four notices that the City sends to property owners must include an “exemption eligibility checklist”. This checklist details conditions that could mean that the property or owner is eligible for various exemptions. If the property owner returns the checklist to the Department of Finance and it determines possible eligibility, the Department of Finance must send an application for whatever exemption it deems appropriate. By law, if the owner does not return the application within 20 business days, the Department must send

another application and follow up with a phone call, if the owner's phone number is available. If it turns out that a lien is sold on an exempt property, the sale will be considered defective if the City is notified within 90 days (Rao, 2012).

In addition, as discussed in previous chapters, the City also excludes certain multi-family residential properties which it deems to be financially and physically distressed. It places these buildings into a city-sponsored rehabilitation program, with the goal of avoiding further distress for those properties and ensuring an optimum rating from ratings agencies. The City's Department of Housing Preservation and Development largely carries out the significant work of identifying these properties.

Other than these categories of excluded liens, the remainder of property tax liens enter the pool of liens to be securitized.

### *5.1.2 Structuring the transaction*

New York City's tax lien securitizations have employed a typical securitization structure. For each securitization (usually annual), the City has established a Delaware business trust to which it has sold its pool of property tax liens. In 1996, this Trust was called the New York City Tax Lien (NYCTL) 1996-4 Trust. In order to fund a purchase of New York City's tax liens, these Trusts have issued bonds which have been widely distributed to mortgage, corporate, municipal, and money market investors (Poindexter, 1996).

A variety of entities have been involved in helping New York City conduct the transaction. As in other securitizations, the transaction involves the participation of underwriters, credit ratings agencies and servicers. Lepercq, de Neufelize & Co (which now employs some of the tax lien securitization experts formerly employed at W.R.



Lazard) works with the City's Department of Finance and Office of Management and Budget to select the companies serving as underwriters and lien servers, and ongoing monitoring and supervision of the program. The underwriter is responsible for working with credit ratings agencies to determine pricing and interest rates for bonds, as well as marketing the bonds. See Table 5.1 for a listing of roles and responsibilities.

Table 5.1

*Roles and responsibilities in New York City tax lien securitization transactions*

<b>Role</b>	<b>Responsibilities</b>	<b>Companies which have served this role</b>
Lead Underwriter	Administers public issuance and sale of securitized bonds to its investor network	JP Morgan Chase, Morgan Stanley Dean Witter, Lehman Brothers, Salomon Smith Barney, Bear Stearns & Co, Inc.
Indenture Trustee and Collateral Agent and Custodian	Processes principal and interest payments and maintains bondholder records	Bank of New York Mellon
Owner Trustee	"Owns" the Trust	Wilmington Trust Corporation
Servicer	Communicates with debtor about payments, initiates legal action on behalf of Trust if payments are not forthcoming	JE Roberts, MTAG, XSPAND, Tower Capital Management
City's financial advisor/Project Manager	Oversees all aspects of the lien sale, securitization and servicing	Lepercq, de Neuflyze & Co.

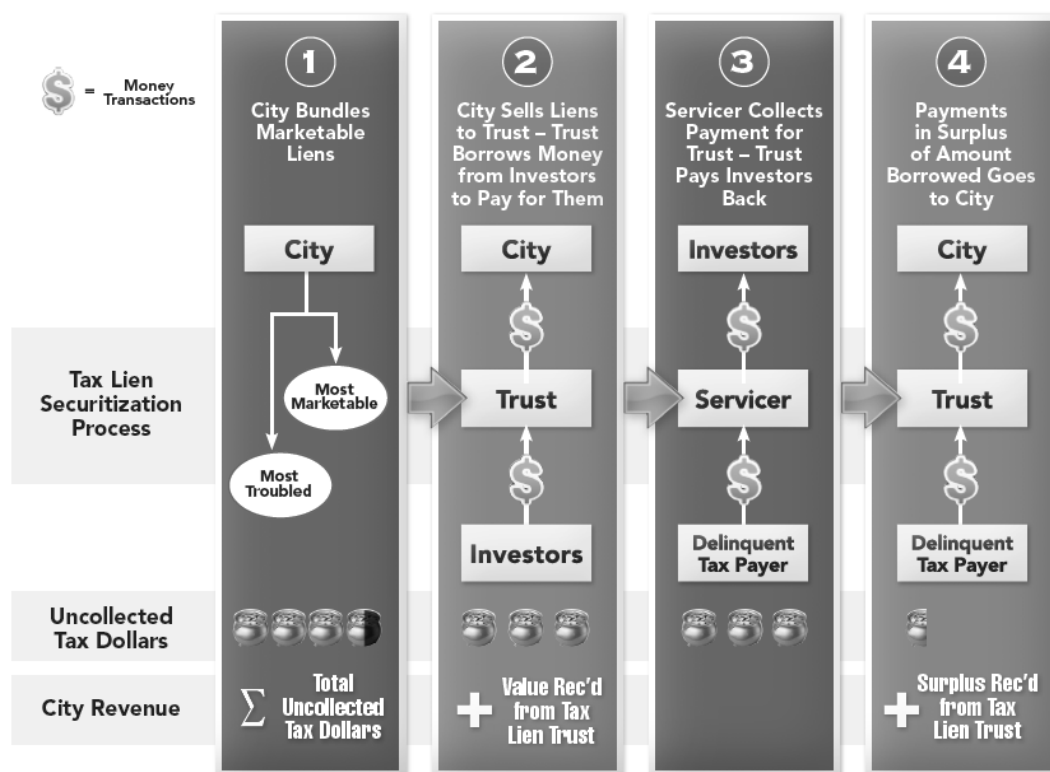
*Note.* Adapted from JP Morgan Chase (2010).

As is standard in securitization transactions, as money was collected on the liens, bondholders have been paid back in order, with those holding Class A bonds being paid

back first. This kind of ordered payback scenario is typically referred to as a "waterfall structure" in securitization transactions. In each of its securitizations, New York City has retained a portion of ownership in the liens as a junior lienholder of a certain amount of subordinate bonds, upon which it could collect once other bondholders had been paid. Thus, if the proceeds collected from property owners exceeded the amount necessary to pay off the senior bonds, the City would recoup some of that surplus. Between 1996 and 2008, New York City recouped \$89.3 million in surplus revenues following repayment of the bondholders.

In order to obtain high ratings from ratings agencies, these transactions have employed various credit enhancements common in securitizations. They have employed over-collateralization, meaning that the dollar value of the liens sold is significantly higher than the dollar value of the bonds issued, reducing risk to bondholders. These transactions have also employed interest reserve accounts in which some of the bond proceeds have been allocated to cover 3 months of interest for Class A bondholders in the event of a shortfall from collections (Poindexter, 1996). Finally, these transactions used a technique called "excess spread" in which the coupon interest rate issued to investors was set at a significantly lower rate than the interest rate and fees collected on the liens themselves.

Figure 5.1

*New York City tax lien securitization process***How the Lien Sale Works**

*Note.* Reproduced from *New York City Tax Lien Sale History and Impact*, by New York City Comptroller, 2012. Reproduced with permission.

### 5.1.3. Direct transactional expenditures by the City

One person involved with the securitization program estimated direct expenditures on the transactions for the City totaling about \$2 million per lien sale and securitization. About 30% of these expenses go to underwriting, another 30% to financial advisors, 20% to associated legal costs, and 10% to ratings agencies. However, these

figures do not include other expenditures indirectly embedded in the transaction through credit enhancements, which I will discuss further below.

#### *5.1.4. Collecting on liens*

The Trusts have hired private servicing firms to administer collection. Servicers earn a flat fee based on the balance of the pool, and are entitled to additional compensation as more liens are paid off. Once a lien is sold, the Trusts are entitled by law to charge debtors the following:

- A 5% surcharge on the entire lien amount
- Interest, compounded daily and payable semi-annually
- Administrative costs associated with the lien sale, including an estimated \$300 to cover the costs of any advertisements and notices

As such, the amount of money owed increases very quickly after the sale, with the addition of interest and fees. For example, a \$47,000 lien against a home in 2008 increased by approximately \$27,000 over the course of a year and half with approximately \$15,000 of that amount in interest on the debt and an additional \$12,000 in fees (Yager, 2010).

In response to advocacy on behalf of tax debtors, the New York City Council amended the law in 2011, establishing a minimum amount threshold capping the interest rate on tax lien certificates at 9 percent annually for properties valued at less than \$250,000.

The Trust can initiate foreclosure on a property under three conditions:

1. if a debtor misses his or her first interest payment due six months after the lien sale; or

2. if the lien is not paid in full within a year and the debtor has not entered a payment agreement; or
3. if current taxes or charges remain unpaid for six months before the lien is paid in full.

The administrative costs incurred by the Trust include servicer fees, trustee fees, financial advisor/management fees, and other expenses. The vast majority of expenses are servicer fees. For example, in the first year of its existence, the 2011 Trust incurred about \$1.6 million in total expenses of which about \$1.3 million was paid to servicers (NYCTL Trust 2011-A, 2012) (See Table 5.2).

Table 5.2

*NYCTL 2011-A Trust Administrative Expenses*

<b>Category</b>	<b>Amount</b>
Servicer fees	\$1,295,914
Trustee fees	\$52,500
Financial advisor/management fees	\$133,778
Lien and other expenses	\$115,637
Total administrative expenses	\$1,597,829

*Note.* Adapted from NYCTL 2011-A Trust Statement of Activities July 15, 2011 to June 30, 2012

## **5.2. Selling liens on paper**

Closely examining this arrangement sheds light on what securitization accomplishes for a local government and how it is fundamentally distinct from conventional lien sales even though it shares certain aspects. In a conventional lien sale, a local government transfers

all of the responsibility for collections and financial risk associated with administering the lien. For example, Nassau County, New York auctions individual tax liens each year. Purchasers pay the full face value of the lien to the County and are entitled to collect on the taxes owed or initiate foreclosure proceedings. Below, I argue that the legal and accounting ramifications of securitization allow the city to transfer tax liens on paper through sale, while still maintaining a large financial stake and significant control over administration of the liens. I suggest that another way of understanding the arrangement is that the City creates an intermediary in order to borrow money and outsource collections and enforcement. The effect is of expanding the local government's capacity to borrow, spend and exercise centralized administrative control on property tax enforcement. When compared to a conventional or bulk lien sale, the local government has a far greater ability to control the outcomes and protect its interests. However, it does so with very little public oversight or public understanding of the City's role in the arrangement.

### *5.2.2. Special purpose vehicles*

Examining the question of who is selling what to whom in New York's lien securitization program sheds further light on this dynamic. When City entities describe the program, they emphasize the sale and transfer of tax liens to a new lien holder. The Department of Finance website states the following:

When you don't pay your property taxes, water charges, and other charges against your property, these charges are tax liens that may be sold in a tax lien sale. Each year Finance sells tax liens. If your property has unpaid debt that qualifies for the lien sale, we will sell your lien debt (the amount owed) to an authorized buyer. A lien servicing company, on behalf of the buyer, adds more fees and interest to your debt, so it is much better to take care of your debt before we sell the lien. We

send you at least four notices before your lien is sold telling you about the sale and advising you to pay your debts so that your property's lien does not get sold.

A City Council report describes the process in the following way:

The City, together with its financial advisors, sells the liens to an independent private entity, the lien sale Trust. The Trust packages the liens into security-backed assets, which are sold to investors on the private placement market. The Trust pays the City a certain portion of the value of the liens upfront, usually around 90 percent of the lien value. At this point, the City no longer "owns" the liens and has no role in the post-lien sale process. The Trust hires private collection agents or servicers to collect the debt from the owners and to handle foreclosure proceedings and property auctions (New York City Council Committee Report, 2010:6).

In this way, the City takes great pains to distance itself from the new lien-holders, the special purpose vehicles referred to as "New York City Tax Lien Trusts" (NYCTL Trusts) or "Trusts". (A new one is created with each securitization.) Both of the accounts above emphasize the City's non-involvement in delinquent tax collection as a result of sale of the liens to a private independent buyer. However, even after the lien sale, the City remains a central actor.

It does this by employing the features of securitization that restructure ownership, assets and liabilities, features which depend on certain aspects of accounting procedure and corporation law in the United States. When structuring a securitization, a company or municipality creates a Special Purpose Vehicle (SPV), a new corporation that is legally separate and sanctioned by accounting protocol and state and federal law. This SPV acts as borrower and purchaser of the assets to be securitized.

While they are considered legally separate from their sponsors, SPVs are only shell corporations, "essentially robot firms that have no employees, make no substantive economic decisions, have no physical location, and cannot go bankrupt" (Gordon and Souleles, 2004, p. 550). In many structured finance transactions including New York City

tax lien securitization, SPVs are Delaware Business Trusts, which as per the Delaware Business Trust Act of 1988 afford a sponsor a high degree of latitude with regard to its legal relationship to its Trust.

In securitization, the legal separation achieved by establishing an SPV can have a variety of benefits for the sponsors of securitization including balance sheet management and various forms of regulatory arbitrage (McCoy and Engel, 2011; Ranieri, 2000; Litan, 1991; Follain and Zorn, 1990; Gordon and Souleles, 2004). For example, legal separation between an SPV and the sponsor of a securitization transaction also protects bondholders in the event that the sponsor of the securitization ever faces bankruptcy (Poindexter, 1996). This can allow sponsors (via their SPVs) to access financing at lower interest rates than might otherwise be available to them. As such, SPV's are wholly-owned subsidiaries of the sponsor but "bankruptcy-remote" in relation to the sponsor.

In using this structure with SPVs, the technique of securitization produces a certain ambiguity between a loan and a sale. Entities that use securitization use a legal concept called "true sale" to differentiate their transactions with SPVs from similar transactions that are considered loans. However, existing law distinguishing a true sale from a loan is murky at best, with one legal expert writing that: "those looking for certainty and consistency will find true-sale law maddening" (Gaddis, 2009: 6).

As with other SPVs, I would argue that each NYCTL Trust is fundamentally an appendage of the City, created to borrow money and carry out policy on behalf of the City. As such, municipally-sponsored securitization is significantly different from a conventional tax lien sale, in which the City sells liens to independent investors. Instead, the City sells the liens to its own shell corporation. This shell corporation borrows money



from bondholders to purchase the liens. To state this in another way, the City uses a special purpose vehicle, an NYCTL Trust, to borrow money in order to buy liens from itself. For accounting purposes, the Trusts are referred to as "blended component unit [s] of the City of New York" (NYCTL Trust 2011-A, 2012: 3). The accounting firm that conducts the independent audit of each Trust, uses the *Government Auditing Standards* issued by the Comptroller General of the United States, as the basis for the audits (NYCTL Trust 2011-A, 2012: 3).

The fact that the City's "blended component unit" (or in other words, its subsidiary) purchases all of the tax liens in this way may be disadvantageous to tax debtors in comparison to conventional tax lien sales that generally employ competitive auctions. In many conventional lien sales, would-be lien buyers bid down either the interest rate that tax debtors will pay on the tax lien principal or the percentage ownership the lien buyer would receive upon foreclosure. The municipality agrees to sell the tax lien for the amount of taxes owed to the lien buyer willing to accept the lowest interest rate from the tax debtor, or the lowest percentage of ownership in the event of foreclosure (Rao, 2012). In contrast, with tax lien securitization, the City via its subsidiary in effect maintains a monopoly on the purchase of tax liens, and reserves the right to charge high fixed interest rates (9% for small residential properties and 18% for all other properties) and assume full ownership of tax foreclosed properties.

After the liens are transferred to an NYCTL Trust, the Trust contracts with private servicers to administer the liens. The Trust pays servicers with proceeds from collections made on liens. However, given that the NYCTL Trusts have no employees and no offices, in practice it is the City that hires and supervises those servicers. The City's

Office of Management and Budget and a private firm contracted by the city to be the Program Manager handle the RFP's for servicers. The Program Manager oversees the day-to-day operations of the servicers (Interview, 2012). The City signs off on the servicers' "chargeoffs", accounts which they deem un-collectable. The City's approval or disapproval determines the rate of incentive compensation paid to the servicer:

The Servicer shall identify the Tax Liens with respect to which estimates of the related Lien Administration Expenses exceed the anticipated Collections with respect to such Tax Liens. At any time following the Closing Date, the Servicer may deliver to the Issuer and the City notice of the Tax Liens so identified, which shall include a list of such Tax Liens and materials in support of the Servicer's determination that the related Lien Administration Expenses exceed the anticipated Collections with respect to such Tax Liens. Within 90 days from the receipt of such notice by both parties, the City shall deliver to the Servicer written acceptance or rejection of any items contained in the list of Tax Liens described in the notice from the Servicer (JP Morgan Chase, 2010).

The companies hired to service the liens act less as debt collectors in the conventional sense, and more as a conduit for information, and a payment processing clearing house. Given that the amount of money charged to delinquent owners is narrowly prescribed by statute, the servicers simply perform basic arithmetic and communicate it when interested parties inquire. This process is automated on the servicer's website. Anyone, whether they own a property being serviced or not, can access this information from the Mooring Tax Assets Group's website. Franklin Romeo, an attorney with Queens Legal Services describes his experience navigating the system for his clients:

What I typically find is they usually have a date by which they are supposed to collect. They have a contractual date by which they are obligated to collect the money and turn it over to the Trust. If you're trying to negotiate a payoff plan, they give you a plan, but they have very little leeway in what they'll negotiate with you. They have a date. If that date is eight months away, they'll take that balance divide it by eight. And the next month, if you're still talking to them, they'll take that number and divide it by seven and give you a slightly higher payment. They don't seem to have any real discretion with how to structure any

payoff plan if people have some ability to pay but can't pay it off all at once (Romeo interview, 2012).

Thus, even though the City characterizes the lien sale and subsequent securitization as a shift away from City involvement in delinquent tax collection, in fact the City still retains significant control over the process. In this way, securitization allows the City to protect its interests and control certain outcomes to a greater degree than in conventional tax lien sale or a bulk sale. I discuss this in further depth later in this chapter.

### *5.2.3. Risks and revenues*

In addition to maintaining a considerable amount of control over the liens after they are sold, the City also retains virtually all of the financial risk and a substantial portion of the potential profits involved in delinquent tax collection and administration. There are two main risks to investors purchasing conventional tax liens. One risk is that collection costs exceed proceeds from liens that can be collected. The second risk is that for liens that are not collectible, proceeds from the eventual sale of foreclosed properties are less than the principal and interest on the tax lien plus administrative, management and foreclosure costs. Conversely, if those costs do not exceed the purchase amount of the lien, the investor pockets the difference. In contrast, in municipally-sponsored tax lien securitization, both the potential risks and potential profits are largely retained by the City.

In its private placement memorandum for tax-lien backed securities, JP Morgan Chase details some of the following risks in tax lien investment:

- "the nature of foreclosure proceedings, which may involve significant delay and expense, which in turn may result in a diminution of the net proceeds of a foreclosure sale of a Property or a later sale of an REO Property" and;
- possible "adverse changes in local economic and demographic conditions, neighborhood characteristics, real estate values generally and in the locale of the property, interest rates, real estate tax rates, other operating expenses (including the cost of energy), inflation and the strength or weakness of the national and regional economy, the supply of and demand for properties of the type involved, zoning laws or other governmental rules and policies (including environmental restrictions), competitive conditions (including changes in land use and construction of new competitive properties) which may affect the ability of a purchaser of the Property to obtain or maintain full occupancy or use of the property or to charge rental rates high enough to cover expenses of operating and maintaining the Property" (JP Morgan Chase, 2011: 14).

How are such risks and associated costs embedded into the structure of the transaction? I contend that it happens in two main ways: in the discounted sale price of the liens (total dollar amount of bonds issued) and in the agreement to hold a certain amount in subordinate bonds. As such, the City absorbs all of the potential losses through credit enhancement at both the beginning and the end of the transaction. These credit enhancements (discounted sales price and agreement to hold subordinate bonds) represent a significant commitment of public resources that neither appear as expenditures on any public documents, nor are deliberated through any public process.

Instead, credit agencies play a crucial role in determining the level of credit enhancement necessary on the part of the City in order to earn an investment grade rating.

By determining the amount of over-collateralization necessary for them to deem the bonds worthy of receiving triple AAA ratings, the ratings agencies effectively determine the sale price of the package of bonds. From the perspective of the ratings agencies, the determination of risk for the bondholder is zero sum with the sale price. The higher the sale price, the lower the bond-rating and vice versa. On average, the total face value dollar amount of the bundle of liens for New York City sponsored lien securitizations has been 42 percent, a little less than one and half times the total dollar amount issued in bonds since 1996 (JP Morgan Chase, 2010). Conventionally for mortgage backed securities, AAA ratings are based on 20 percent to 30 percent overcollateralization (Conard, 2012).

Ratings agencies also determine the percentage of subordinate bonds that are issued to the City. Through holding subordinate bonds, the City effectively agrees to cover the cost of any unanticipated problems with collections. The subordinate bonds are allocated any losses before other bondholders. That amount has reached as much as 40% where only AAA-rated bonds are issued (Page, 2011). In other words, New York City held as much as 40% of the bonds issued, and those bonds were last in line to be paid from delinquent tax collections. The City has been able to collect some proceeds from those subordinate bonds, which I will discuss in more detail in the following chapter.

Table 5.3

*Levels of Overcollateralization for New York City Tax Lien Securitizations*

<b>Bond series</b>	<b>Level of Overcollateralization</b>
1996-1 Bonds	1.16
1997-1 Bonds	1.06
1998-1 Bonds	1.06
1998-2 Bonds	2.64
1999-1 Bonds	1.07
1999-R Bonds	2.04
2000-A Bonds	1.55
2001-A Bonds	1.16
2002-A Bonds	1.11
2003-A Bonds	1.91
2004-A Bonds	1.09
2005-A Bonds	1.16
2006-A Bonds	1.09
2008-A Bonds	1.51
2009-A Bonds	1.52
2010-A Bonds	1.51

*Note.* Data from JP Morgan Chase (2010).

In conventional lien sales, investors turn a profit if costs of administering the liens do not exceed the amount they pay for the lien. In New York City's lien securitization program, it is the City that retains the ability to receive that profit, however, the costs of the program include not only administering the liens but also the financing costs of securitization. The administrative costs include costs of collection and foreclosure, management and resale of REO properties. Financing costs include fees paid to the financial advisor, to the underwriters, ratings agencies and the costs of various credit enhancements. As other research suggests, conventional forms of municipal borrowing

such as general obligation bonds may be less expensive and more transparent than financing arrangements using delinquent tax receivables (Marchiony, 2012).

To date, these costs have been more than accounted for by payments made by debtors in the forms of the 5% surcharge levied at the point of sale, various fees, and interest on the amount due. There is a significant interest rate spread between the 18% daily compounded interest paid by debtors (and authorized by the City) and the comparatively modest interest rate earned by bondholders. It is important to note that the former is governed by city and state statute and does not change in relation to interest rate fluctuations on US Treasury Bonds, while the later has fluctuated significantly as interest rates in general have increased and decreased. In recent years, the coupon rate for these bonds has been between 1% and 2%, meaning the interest rate spread has grown considerably between this rate and the 18% charged to debtors. This has meant that even when only a portion of liens are redeemed, proceeds are sufficient to repay bondholders with interest, cover costs and return revenue to the City (See Table 5.4). The fact that the City maintains a virtual monopoly on tax lien purchasing may be worse for tax debtors in comparison to conventional tax lien sales in which competitive bidding can significantly drive down interest rates on delinquent taxes, or the percent ownership of a property that a tax lien purchaser can assume in the case of tax foreclosure (Rao, 2012).

Table 5.4

*Interest rates for Class A Bonds in New York City's tax lien securitizations since 1996*

	<b>Interest rate for Class A Bonds</b>
96-1 Sale	6.81%
97-1 Sale	6.46%
98-1 Sale	5.93%
98-2 Sale	7.98%
99-R Sale	8.21%
99-1 Sale	6.35%
Series 2000-A	7.52%
Series 2001-A	5.59%
Series 2002-A	4.23%
Series 2003-A	2.13%
Series 2004-A	3.47%

*Note.* Data compiled from Moody's Investor Service (1996; 1997; 1998; 1999; 2000; 2001; 2002; 2003; 2004).

New York City is the only locality that compounds interest on tax liens daily (Miller, 2012). As such the City has received significant residual payments from the Trust. Between 1996 and 2008, the City received \$89.3 million (Perrine, Shultz, Marazzi, 2011). Although the City has ostensibly turned a "profit" in these transactions, that amount is not necessarily more than the amount the City would have received had it used alternative collection methods and not securitized its liens. However whether or not this is the case is extremely difficult to ascertain. I will discuss this more in the next chapter.

Table 5 below summarizes information about the amount of revenue in excess of the original sale revenue that the City has received from recent lien sales.



Table 5.5

*Lien face value, bond dollar value, City proceeds and total collections*

	<u>2008-A</u>	<u>2009-A</u>	<u>2010-A</u>
<b>Total face value of liens sold including 5% surcharge</b>	\$78,771,234	\$90,335,754	\$101,983,400
<b>Total dollar value of bonds issued by Trust</b>	\$52,264,000	\$59,350,000	\$73,428,000
<b>Total amount received by New York City as of end of FY2011</b>	\$32,968,000	\$38,493,000	\$46,088,000
<b>Total Collections (as of July 31, 2011)</b>	\$57,872,432	\$67,230,826	\$48,198,317

*Note.* Data compiled from NYC Office of the Comptroller (2008; 2009; 2010; 2011) and JP Morgan Chase, 2011.

In sum, although municipally-sponsored tax lien securitization follows the overall format and idiom of a conventional tax lien sale, in actuality, it is a process in which the municipality retains both a large financial stake and significant administrative control even after the sale. Instead of a tax lien sale in the conventional sense, it might be more accurately understood as a public program administered by private contractors.

### **5.3. Financialization and expanding municipal capacity**

Participating in this arrangement has the effect of expanding the City's capacity in a few ways.

First, using securitization has the effect of giving the City the capacity to make expenditures on administering the collection of delinquent taxes, and managing and disposing of tax foreclosed properties with the appearance of no cost to the taxpayer and without having to engage in city budgetary processes.

Second, using securitization affords the City the flexibility to subsidize the costs related to non-performing liens with proceeds from well-performing liens. For example,

Moody's has determined that liens on residential property in New York perform on the whole better than liens on commercial property. Commercial properties also have higher liquidation costs after tax foreclosure than do residential properties (Moody's, 2014). This suggests that through tax lien securitization, residential property tax debtors subsidize the costs related to commercial property abandonment.

Third, just as securitization affords private sector entities the ability to move assets and debts off balance sheet in order to achieve certain accounting objectives and comply with regulatory mandates (Pozsar et al, 2013), this arrangement affords New York City a means of managing its balance sheet to avoid regulatory constraints on municipal debt. This is of particular use to the City because of constitutional debt restrictions, as discussed in Chapter 3.

Fourth, tax lien sale and securitization has a counter-cyclical logic, giving the City a means to borrow more and spend more on its tax delinquency program during the years of economic downturn in which it most needs to do so, regardless of state constitutional debt limits. Moreover, borrowing via tax lien securitization has not appeared to negatively impact the City's credit ratings, which have steadily increased since the 1990s, despite the City's growing debt obligations. Moody's upgraded New York City in 2001 from A3 to A2 (Chou, 2001). In 2006, the City earned its highest credit rating from the ratings agency Standard & Poors in the sixty years that the agency had been issuing ratings for New York City, making reference to New York City's "good internal management" of its finances (Kuttner, 2006:1). In recent years, the City's debt management strategy has earned explicit approval from credit ratings agencies. The credit ratings agency Fitch stated:

Fitch considers [New York City's debt] exposure to be manageable given the hedge provided by the city's substantial short-term assets and its sophisticated management, diversity of liquidity providers, and strong demonstrated access to the capital markets (Fitch Ratings, 2014).

While using securitization has given the City flexibility in borrowing, it is possible to contend that the City could use alternative means other than tax lien securitization to borrow needed funds. Indeed in recent years, external factors have driven down the costs of municipal borrowing in general. As the Office of the New York City Comptroller stated in 2012 (15):

[T]he municipal bond market experienced strong supply and demand fundamentals as investors sought the safety of municipal bonds amid news of European fiscal and banking turmoil and the slow global economic recovery. Strong investor demand and historically low interest rates created a favorable environment for the City's bond financings.

However, it is difficult to evaluate the financing costs of tax lien securitization in comparison to other financing options available to the city which are affected by a variety of factors at any given time. In 2004, interest rates on New York City's general obligation bonds ranged from 2-5% (City of New York, 2004), while the NYCTL 2004 Class A bonds had an interest rate of 3.47%. However, comparing interest rates is not necessarily sufficient in terms of evaluating the cost of financing to the City given the cost of credit enhancements such as overcollateralization. NYCTL 2010 Class A bonds carry a low interest rate of 1.68%. However, the overcollateralization rate is high at 51%. NYCTL 2013 Class A Bonds carry an interest rate of 1.190% in 2013 bond series, but have similarly high levels of overcollateralization.

Moreover, the dollar amount represented by tax lien securitization transactions is small in comparison to other bond issues from the City. Thus, a broader question to ask

is, given the small dollar amounts involved and a recent history of timely collections on delinquent taxes, whether the City even needs to borrow against its delinquent tax receivables at all as opposed to directly enforcing collections.

Fifth, the arrangement has the effect of allowing the City to overcome previous regulatory and political constraints on property disposition. While fewer buildings have been tax-foreclosed upon in comparison to the large waves of abandonment in New York City in previous decades, there are still properties that are confiscated for tax arrears. Part of the reason that it is advantageous to avoid direct City ownership of property is to avoid the regulatory hurdles that come with selling that property. The City Charter mandates a protocol called the Uniform Land Use Review Process (ULURP) which stipulates a series of opportunities for public deliberation by way of Community Boards and the City Council. In past decades, these public review processes have given opportunities to organized constituencies to exercise influence over the fate of these properties, often to ensure affordability. This land use review process is part of the City Charter, which was approved in 1975. The New York City Department of City Planning describes in a description of city planning history on its website, the convergence of both local and national circumstances that produced a land use review process that incorporated a high level of public participation:

The establishment of ULURP reflected two trends underway in the 1950's and 1960's: the increasing involvement of the city's Community Boards in the development of the city and a substantial increase in community participation in many aspects of government. In the late 1960's, there was a significant upsurge in community participation, aided in part by a requirement of community participation in Federal programs such as Model Cities.

Although the City was able to circumvent ULURP in some instances by using an expedited process called the Urban Development Action Area Program (UDAAP), this process also required City Council review and approval. Securitizing tax liens meant the City presumably could avoid both UDAAP and ULURP, which was considered particularly cumbersome and lengthy (Berey, 1997). The Citizens Housing and Planning Council (1995: 2) also recognized the importance of this in 1995, writing:

Once the city takes title [to a property], several procedural impediments to rapid disposition are triggered such as the Uniform Land Use Review Process (ULURP) which applies to all city dispositions of real property. Furthermore, the city becomes subject to a variety of political pressures, as *in rem* disposition process over the past 20 years demonstrates.

As discussed in the previous chapter, since the 1970s wave of housing abandonment, city policy on tax-foreclosed property has been a greatly contentious political issue. In the 1970s, 80s and 90s, tenants of city-owned properties formed a large and well-organized constituency which was able to effectively leverage protest and political pressure to win major victories which not only included stopping the private disposition of countless city properties, but also successfully pressuring the City to create programs for affordable housing and limited equity co-ops (Sites, 2003). Urban scholar Thomas Angotti (2011: 99) documents the history and the impact of this organizing. He describes how and why tenants organized:

From the start, tenants organized to fight the city's policy. Some resisted attempts to sell their buildings to landlords, others resisted attempts to sell buildings to tenant-run coops, fearful that self-management would lead to higher rents (in rem tenants paid modest rents). They organized building by building and neighborhood by neighborhood. At one point they formed a Union of City tenants. Eventually hundreds of thousands stayed on as tenants in the nation's largest pool of municipally owned low-income housing.

He goes on to describe the tactics used to stop sales of occupied buildings:

In the throes of the abandonment crisis, communities mobilized to stop the city's auctions. Protests ranged from demonstrations at the auction sites to political campaigns to force borough presidents, City Council members and community boards to intervene to stop the sales.

Through their organizing, tenants and housing advocates were also successful in persuading HPD to establish the Department of Alternative Management (DAMP) and the Tenant Interim Lease Program (TIL) which create limited equity co-ops in which former tenants became co-op owners. As a result, the Urban Homesteading Assistance Board has helped to set up limited equity co-ops for 1,300 buildings benefiting approximately 30,000 households to date (Urban Homesteading Assistance Program, n.d.).

In addition to occupied buildings, vacant city properties were also the target of effective organizing efforts through squatting and other tactics. In the early 1990s, hundreds of vacant city owned residential buildings were occupied. These tactics produced city support for rehabilitation of squatted buildings that would become part of a locally controlled mutual housing association (Angotti, 201: 99). As such, the city's inventory of tax foreclosed properties became the fulcrum of a major social and economic justice movement in New York City during the 1970s, 80s and 90s.

Through its current delinquent property tax collection program, the City avoids taking title to any tax-foreclosed properties. Although it never takes title to properties, current practices still allow the City to maintain a high degree of control of the terms of property disposition, while "circumventing its intricate land-use rules and blunting the political pressures that have constrained disposition policy" (Braconi, 1999: 107). It is able to exercise this control largely away from the public eye and without regulatory

constraints like ULURP which mandate public review. This is the case for properties that go through the lien sale and end up in foreclosure and for properties that are diverted away from the lien sale to the Third Party Transfer (TPT) program, although the process and mechanisms are different for each group of properties.

For the properties that actually go through the liens sale and end up in tax foreclosure, the City still plays a role in disposition even though it doesn't take title. The City dictates the terms by which a tax foreclosed property is sold and who is allowed to purchase it. Only "Responsible Purchasers" are allowed to purchase tax foreclosed property. Responsible purchases must submit a sworn affidavit to the City via the servicer prior to purchasing a property (JP Morgan Chase, 2010). A "Responsible Purchaser" of a tax foreclosed property is defined through rule-making by the Department of Finance. A "Responsible Purchaser" is a person or entity which:

- "is not the owner or an affiliate of the owner of the related Property;
- has not been convicted of fraud, bribery, grand larceny, arson, tenant harassment, or other felony under the New York Penal Law, within seven years of the date of sale"
- "is not delinquent in the payment of real property taxes, water and sewer charges and assessments, or other taxes, charges and assessments in the City for over one year and in an aggregate amount exceeding \$20,000,"
- "has not lost title to real property by reason of a tax lien foreclosure proceeding or other tax enforcement proceeding within five years of the date of the sale"
- "is not the owner or holder of real property, and is not an affiliate of a person owning or holding real property, that has an average of five or more hazardous or immediately hazardous violations of record per dwelling unit under the City Housing Maintenance

Code, or that is subject to a lien or liens for the repair or the elimination of any dangerous or unlawful conditions pursuant to the City Administrative Code in an amount equal to or greater than \$1,000; and"

-"is not suspended or debarred from contracting with the City or any City agency pursuant to the City Charter" (JP Morgan Chase, 2010).

The private servicing companies administer the marketing and sale of the small handful of buildings that do end up in tax foreclosure auctions. If there is no bidder that is willing to bid the minimum bid price, the Trust must pay the minimum bid and the private servicer conducts a sealed bid auction. The process is made even more non-transparent by the fact that the Trust itself often uses its own SPVs to hold title of any properties that are foreclosed upon, in order to avoid environmental liabilities (Moody's, 2014). While little information is publicly available about these properties, the financial statements of Trusts from recent years show that they have been able to easily absorb any losses from disposing of these REO properties. However, often owners or residents of these properties undergoing enforcement by the Trust are in the dark about who actually controls the process. Evidence shows that the property disposition process after lien securitization has confounded property residents who have in the past successfully exerted influence on the City with regard to fate of their homes through organizing, squatting or other tactics (Starcheski, 2014).

For properties that were excluded from the tax lien sale because of their distressed status but end up in tax foreclosure through the City-supervised process, the City uses a program called Third Party Transfer. The City never takes title to the properties but instead transfers the ownership of tax foreclosed properties directly to a city-sponsored



non-profit called Neighborhood Restore which then manages the properties and prepares them for sale. Neighborhood Restore is fully funded by the City, and many of its staff have worked for the city. One person close to the process explained:

It's all driven by the city's unwillingness to take title to buildings. Ever since the 1970's and 80s and the in rem stock. The city has been driven by an axiom that it won't take title to private buildings...They won't do it, they don't want to do it and they never will do it....Through TPT, you get all the benefits of having the city involved but none of the drawbacks...that's the purpose they serve of being a non-governmental governmental pass through (Interview, 2012).

A staff person at an association of non-profit housing developers comments on the relationship between Neighborhood Restore and the City:

The city is *de facto* on the hook for all of it. Neighborhood Restore has no balance sheet...if they screw something up, there is an implicit backing from the city. It kind of strange because it is a non-governmental governmental arm. It's not like Neighborhood Restore is going to go off getting creative on their own without backing from the city (Interview, 2012).

In sum, under post-1996 tax lien policy, the City avoids taking title to any tax-foreclosed properties but still maintains a high degree of control of the terms of property disposition via the city-sponsored entities Neighborhood Restore and the NYCTL Trusts. It is able to exercise this control largely away from the public eye and without regulatory constraints which mandate public review. As such, the City has been able to take advantage of largely favorable real estate market conditions in recent years without having to engage in a lengthy or politicized property disposition process.

#### **5.4. Transparency**

In securitization, New York City achieves an effect similar to another kind of governance arrangement: the public authority, a kind of quasi-governmental entity which the City has long used to borrow money and avoid political and regulatory constraints (Nehemkis, 1937; Sbragia, 1996). First established in the late nineteenth century, public authorities are "corporate instruments of the State created by the Legislature to further public interests" (Office of New York State Comptroller, 2013, para 1). Created to manage infrastructure and deliver various public services, public authorities in New York and around the country often take on large amounts of debt on behalf of local and state governments with little taxpayer input (Sbragia, 1996; Schwarcz, 2012). New York City has made extensive use of authorities throughout its history.

While local governments' use of public authorities has often been criticized for problems of transparency and accountability to the public, using securitization may be even less transparent and accountable than using public authorities. Public authorities are at the very least created with a public purpose and governed by boards made up partially of elected officials. In contrast, NYCTL Trusts, as private Special Purpose Vehicles, have no such statement of public purpose or transparent governance structure. In 1998, two years after it began securitizing tax liens, New York City created the Transitional Finance Authority (TFA) to issue new debt on behalf of New York City. While the debt issued by the TFA is not subject to the City's state constitutional debt limits because it is not directly issued by the City, it is still commonly understood to be New York City debt.

In contrast, securitization removes de-facto public debt and public expenditure related to delinquent tax administration from public oversight and deliberation, embedding it within credit enhancement procedures determined by ratings agencies.

Neither the administration costs nor the financing costs of securitization appear to be City expenditures. In tax lien securitization, determination of the amount of public money spent on delinquent tax collection becomes the product of a ratings-agency constructed calculation of investor risk and is divorced from public conversations about whether the City actually needs to borrow or spend at a particular rate at any given time. During City Council hearings in 2010 and 2011 reauthorizing legislation for the lien sale, the City Council did not address credit enhancements such as rates of overcollateralization at all.

As discussed in Chapter 3, securitization can be a relatively expensive form of financing because of the various parties involved that require compensation. These costs, in addition to the costs of credit enhancements, are not readily apparent to the public. It is worth noting that the discounted price at which the liens are sold is not even readily apparent to those in city government who work on the lien sale. Several staff people at both the Department of Finance and at the Comptroller's Office with whom I spoke were under the impression that New York City received the full face value of the liens sold through the securitization, when in fact each bundle of liens securitized was sold at a steep discount. Overcollateralization in 2009, 2010 and 2011 was over 50 percent (See Table 5.2 above).

For a variety of reasons, the City's finances have fluctuated since 1996, with both deficits and surpluses throughout the Giuliani years and mainly surpluses under Bloomberg. In addition, New York City's amount of borrowing in relation to its debt limit has also fluctuated. Municipalities have a range of short- and long-term borrowing options, the advantages and disadvantages of which can shift in relation to economic conditions, interest rates and other factors. By obscuring the fact of municipal borrowing

against delinquent tax receivables, as well as the cost of that borrowing, tax lien securitization makes difficult any public evaluation of whether or not the City actually needed to borrow in this way in any given year.

## **5.5. Conclusion**

By combining the financial technique of securitization with the idiom and format of a tax lien sale, New York City's property tax enforcement program represents a new municipal institutional form. This form has the effect of expanding local state capacity to borrow and spend and overcome certain regulatory and political constraints. Unlike in a conventional lien sale--after which a local government completely transfers risk, profit and responsibility to investors, in a tax lien securitization, New York City retains a large financial stake, primary administrative authority and a significant ability to protect its interests. This is made possible by the legal and accounting features of securitization which allow the City to transfer the liens on paper to a shell corporation that it controls.

As a result, New York City has been able to avoid state constitutional debt limits and city budgetary and procurement protocols. In addition, it has been able to take advantage of a mostly strong real estate market since 1996 without the hindrances of regulatory mandates and political pressures connected to disposition of city-owned property. For New York City, using securitization shares similarities with the strategy of using public authorities to achieve certain governance goals. However, in many ways, using securitization is even less publicly transparent and accountable than using public authorities, which are at least nominally committed to the public interest.

Even though lien securitization is fundamentally distinct from a conventional lien sale, the idiom of tax lien sale is still strong in the public discourse about the process. The notion that the City washes its hands of property tax enforcement after liens are transferred is central to most descriptions of the process. A recent article in the New York Daily News described the process in this way, "Tax liens — unpaid property taxes, water bills and other property-related charges — are sold annually by the city to third parties who charge hefty interest payments and fees (Furman, 2013:8). One recent academic publication states, "Today the city no longer holds tax-delinquent properties and now sells the tax liens fairly promptly to private entities" (Angotti, 2011:100). And a report by the City's Independent Budget Office states, "After the sale, the city no longer owns the liens and no longer has a role in the collection process" (New York City Independent Budget Office, 2013:2).

In sum, for the evolving Post-Keynesian municipal state, engagement with expanding financial markets has altered the institutional forms through which day-to-day operations such as tax collection are conducted. These changes have produced a reconsolidation of municipal control and an expansion of state capacity, even while the urban state maintains the appearance of retrenchment and retreat. These changes have also had the effect of substituting older political and regulatory constraints with new financial liabilities, further implicating the urban state in relationships with creditors and financial intermediaries.

## **Chapter Six-- Lien securitization and collections: Evidence from New York City**

In this chapter, I discuss the outcomes of New York City's lien securitization program from the standpoint of revenue collections for the city. Given data and resource limitations, I do not engage in an exhaustive empirical study. Instead I offer a broad discussion and a possible framework for interpreting the outcomes of the program.

First, I look at redemption rates for securitized tax liens and discuss the factors that impact tax lien redemption. I argue that it is important to contextualize these redemption rates by looking at factors contributing to redemption (such as the legal status of liens, lien-to-value ratios and real estate market conditions), as well as compare them with delinquent tax collection rates achieved by other enforcement methods.

Second, I examine collection rates from regular non-delinquent property taxes which have increased slightly since the early 1990s. I discuss the various factors that affect these collection rates, and compare New York City's collection rates to general trends of property tax collection historically in New York and more broadly in the rest of the country. I suggest that in this area, the program has performed adequately, but not exceptionally.

Finally, I identify trends in the characteristics of properties that have had liens sold and securitized, including size of delinquency, geographic location, and association with previous high-cost mortgage lending.

## 6.1. Collecting delinquent tax revenues

Between 1996 and 2011, New York City securitized almost \$2 billion in delinquent property tax bills (See Table 6.1). The dollar amount of tax liens securitized, varied from year to year, ranging from about \$35 million in 2006 to \$250 million in the first lien sale in 1996.

Table 6.1

### *Initial Tax Lien Principal Balance by Bond Series 1996-2010*

<b>Bond series</b>	<b>Initial Tax Lien Principal Balance</b>
1996-1 Bonds	\$250,402,077
1997-1 Bonds	125,984,912
1998-1 Bonds	103,882,598
1998-2 Bonds	144,983,333
1999-1 Bonds	48,315,973
1999-R Bonds	142,188,722
2000-A Bonds	243,035,445
2001-A Bonds	161,777,627
2002-A Bonds	117,291,975
2003-A Bonds	164,021,162
2004-A Bonds	54,682,860
2005-A Bonds	57,952,556
2006-A Bonds	35,892,660
2008-A Bonds	78,771,234
2009-A Bonds	90,335,754
2010-A Bonds	110,759,716

*Note.* Data compiled from JP Morgan Chase (2010).

The 1998-2 and the 1999-R Bond series were backed by tax liens with much higher LTVs (weighted average LTV of 138% versus less than 30% for the previous pools). These pools consisted of "leftover" properties not included in the previous

securitizations. The ratings agency Moody's (1998: 1) explains the need for greater credit enhancement measures in order to justify an investment grade rating:

The higher LTVs in this pool suggest that most of the underlying properties will not redeem, but instead will go through foreclosure and REO liquidation. Because fewer liens are expected to voluntarily redeem, cash flows off of the liens will be significantly impaired during the first two years after closing while the servicer files foreclosure proceedings. The larger proportion of commercial and industrial properties (70% in this pool versus 50% in the previous deals), and a long history of delinquencies, also suggest higher loss frequency and severity than in the City's previous tax lien deals. As a result, the credit enhancement level is significantly higher than that of the City's previous tax lien securitizations.

These two transactions carried higher interest rates (7.98% and 8.21%), and higher levels of overcollateralization than other lower LTV securitization transactions.

For each of the securitization transactions between 1996 and 2011, collections from tax liens have been sufficient to repay all bond holders. In fact, for many of the bond issues, bond holders have been repaid at least five years before the stated maturities of the bonds and the City has collected money in surplus of the original face value of the lien (Perrine, Shultz and Marrazi, 2011). Given high interest rates and penalties charged to debtors, full bond repayment can occur even when only a portion of delinquent accounts are paid off (New York City Independent Budget Office, 2014).

Liens are generally paid off quickly. Analyzing private servicer data from the 2004 lien sale shows that the median amount of time it takes property owners to redeem their liens is 11 months citywide.

## **6.2. Rates of redemption and default**

In the period since the first lien sale in 1996, very few properties in New York City have been confiscated as a result of tax arrears as the overwhelming majority of liens have



been redeemed. It is estimated that only 5% of the total number of properties with liens sold ended up defaulting, and the vast majority of those were from the first few years of the lien sale (Interview, 8/17/12; Interview, 2012; Zinner interview, 2012.).

Analyzing private servicer data from the 2004 lien sale shows that as of 2011 only eight properties out of 1426 serviced by Xspand had their titles transferred as a result of tax foreclosure, even though the Trust had taken legal action against thousands of these properties.

However, there is some evidence that there has been a decrease in timely payments since the economic downturn beginning in 2008. After forty-four months 73 percent of owners with properties the 2009 lien pool, comprised of 4,792 liens, had paid their liens in full, 7 percent had made partial payments and 21 percent had not made any payments at all (Independent Budget Office, 2014).

### **6.3. Factors affecting redemption rates**

How can we interpret New York City's rates of redemption? There is very little scholarly literature comparing redemption rates, redemption speed, enforcement strategies or factors affecting tax lien redemption rates, likely because of the lack of data available to academic researchers on actual redemption rates. However, based on data available, it is likely that four main factors affect redemption rates: the legal status of liens, lien-to-value ratios, real estate market conditions and types of properties.

#### *6.3.1. Legal status of liens*

Debtors have few legal defenses when it comes to the liens. Franklin Romeo, and attorney at Queens Legal Services who has represented clients in both mortgage and tax foreclosure cases stated that:

We take very few of these cases, because often there isn't much you can do for people, other than recommend that they try and take out a loan if they can. Unlike other kinds of foreclosure cases with residential mortgages, there are often lots of defenses, and you can try and settle them. But with a tax lien, it's pretty impossible to defend them on their merits (Romeo Interview, 6/12).

Similarly, Sara Manaugh, an attorney at South Brooklyn Legal Services remarked that in her experience working with clients who have had their liens sold, "There is no negotiating. You just have to pay them off" (Manaugh interview, 6/12).

A unique characteristic of certain debts to a municipality (property tax, water and sewer charges) is that by law, it has priority over many other kinds of debt and encumbrances secured by that property, including mortgage liens and some Federal income tax liens (Alexander, 2000; Marchiony, 2012). This "super-priority" also includes any fees, including legal fees connected to foreclosure. Therefore, even if the property owner is unable to fulfill his or her obligation, the creditor is still very likely to be reimbursed. The priority that the law affords to property tax debt ensures that whomever is servicing this debt, the government or a private institution, will eventually be successful.

As such, private servicers that New York City's tax lien trusts hire to service property tax liens play a different role than collection agencies servicing debt to private entities such as credit card companies, which can be noted in the difference in their activities and tactics. Property owners and attorneys representing property owners that I spoke with all remarked on the relatively passive approach the lien servicers take. One

property owner said, “Actually they don’t call, they don’t harass you. It’s not like other collection agencies. I’ve barely heard from them at all” (Interview, 2012). Servicing companies do provide written notice to property owners about their growing debt, and when they will begin foreclosure actions. The companies hired to service the liens act less as debt collectors in the conventional sense, and more as a conduit for information, and a payment processing clearing house. Given that the amount of money charged to delinquent owners is narrowly prescribed by statute, the servicers simply perform basic arithmetic and communicate it when interested parties inquire. This process is automated on the servicer's website. Anyone, whether they own a property being serviced or not, can access this information from the Mooring Tax Assets Group's website.

Servicers are paid both a base fee and an incentive fee based on the collections made. The servicing fee is graduated, with the servicer receiving higher compensation as the pool of outstanding liens becomes smaller, reflecting the increased effort required to collect on the poorly performing liens.

### *6.3.2. Lien-to-Value ratios*

Repayment of liens is closely related to a property's lien-to-value ratio (the amount of debt owed compared to the total value of the property.) The lower the lien-to-value ratio, the greater the incentive for applicable parties to redeem liens. Properties with higher lien-to-value ratios are less likely to be redeemed than those with lower lien-to-value ratios. The ratings agency Moody's Investor Service (2014:3) states with regard to evaluating risk in tax lien securitizations:

The LTV of a tax lien at the time of securitization (the “initial” LTV) is an important factor in assessing the likelihood that a tax lien will be redeemed by the property owner. In addition, it is an important determinant of the amount likely to be recovered through foreclosure of those properties that are not voluntarily redeemed. Generally, tax liens with lower LTV ratios, everything else being equal, are more likely to be redeemed or, if they are not redeemed, to have higher recovery rates in foreclosure. Moody's believes that the LTV is the primary indicator of the property owner's willingness to redeem the tax lien certificate. In general, high LTV properties are more risky than low LTV properties as recovery rates will likely be higher for low LTV properties, holding other factors constant. As described below, we utilize three approaches in evaluating the final enhancement levels. All three approaches focus on LTV as the primary driver of credit risk.

On average, New York City's lien pools have been comprised of more than 80% of properties with lien-to-value ratios of 100% or less. In 2003, the city imposed a large real estate tax increase which resulted in a 16.7% increase in the amount of taxes due, resulting in higher levels of delinquency and a lower percentage of tax liens with lien-to-value ratios of 100% or less.

Lien-to-value ratios predict the likelihood that a willing party will "redeem" (the term the city and the servicing companies use to mean "pay off") a tax lien, whether it is the property owner, a new owner who purchases the property or a mortgage lender. Many property owners I spoke with were planning to sell their properties in order to pay off their liens. Some debtors also described how aggressively they had been pursued by potential buyers after the City publicized the list of addresses with liens to be sold (Interviews, 2012).

Table 6.3

*Percentage of tax liens with Lien-to-Value Ratio of 100% or less by bond series*

<b>Bond Series</b>	<b>Percentage of Tax Liens with Lien-to-Value Ratio of 100% or Less**</b>
1996-1 Bonds	100.00%
1997-1 Bonds	100.00
1998-1 Bonds	100.00
1998-2 Bonds	40.44
1999-1 Bonds	98.51
1999-R Bonds	50.13
2000-A Bonds	49.44
2001-A Bonds	87.18
2002-A Bonds	94.46
2003-A Bonds	52.64
2004-A Bonds	93.48*
2005-A Bonds	83.02
2006-A Bonds	95.53
2008-A Bonds	97.15
2009-A Bonds	99.75
2010-A Bonds	99.99

*Notes.* \*Does not reflect Subsequent Taxes and Assessments in the aggregate amount, as of August 31, 2004, of \$11,829,094 that became liens on the Properties after June 30, 2004.\*\*Calculated as a percentage of Initial TLPB. Rounded to the nearest 2<sup>nd</sup> decimal place. Adapted from JP Morgan Chase (2011).

In many cases, the lender pays off the tax arrears to protect their investment, even when the property is also in mortgage arrears or mortgage foreclosure (De la Torre and Martinez, 2011; Poindexter et al, 1997). Zinner (Interview, 2012) explained:

Even when [mortgage lenders] weren't escrowing [taxes], they would go ahead and pay off the taxes and then the person. They would pay \$5000 in taxes and then that person would be in default on their mortgage. If people fell behind on their taxes, it didn't lead to liens, it led to them falling far behind on their mortgage....even if that person was current on their mortgage [the lender] would pay a \$5000 tax bill, suddenly that person would be \$5000 delinquent [on their mortgage] [and] that would trigger [mortgage] foreclosure also.

New York City maintains public online records of property tax payments and balances due for all properties so mortgage lenders or any other interested parties can easily access information about the tax delinquency status of particular properties.

The interests that mortgage lenders have with regard to tax liens is also recognized by those who evaluate tax lien securitization transactions for bondholders.

The ratings agency Standard & Poor's (Standard and Poor's, 1996) states in their

"Methodology For Rating And Surveilling U.S. Tax Lien Securitizations":

Since tax liens are generally senior to other claims against real property (with the exception of previously imposed federal tax liens), loan servicers would have an incentive to pay tax liens on mortgaged properties...[The lender thus] maintains first right to foreclose on the property.

A number of other sources confirm that mortgage lenders routinely pay off tax liens when their collateral is threatened by tax foreclosure (Ody, 2013). Real estate attorney Leon Bayer writes:

Lenders can protect themselves from losing their collateral at a tax sale by monitoring the tax delinquency status on every parcel they have loaned against. If the borrower fails to pay the property tax, the lender will advance the money to pay the taxes. That removes any danger of a potential tax sale, and then the lender

can bill the owner for the taxes that the lender has paid. Paying the taxes also allows a lender to take their sweet time in foreclosing on the borrower. For example, a bank won't rush through a foreclosure if it already has too many repossessed condos in their inventory (Bayer, 2012).

### *6.3.3. Real estate market conditions*

Of course, the significance of strong real estate market conditions in New York City (in combination with low interest rates and easy access to capital) during this period can not be overstated. The lien-to-value ratio of a property with tax arrears is clearly affected by real estate market conditions. Both sale prices and rents have risen dramatically since 1996 with a relatively rapid recovery after the post-2008 recession. Property prices in the New York City metropolitan area, which includes the boroughs of New York City, Northern New Jersey and Long Island, rose steadily during the 2000s . This has meant that property owners owing back taxes are often able to raise revenues through raising rents or finding buyers for their properties. Property owners with back taxes are often the target of real estate speculators (George interview, 5/5/12; Audrey interview; 5/5/12; Lois interview, 5/7/12).

Harold Shultz described the way that the underlying value of multi-family residential property in New York City has driven collections on delinquent taxes both in the early 2000s and more recently:

In the early 2000s, when the market was the hottest...one could argue that you couldn't really do anything wrong...During the post-crash era...the real value of multi-family dwellings has not really declined...And what I mean by the real value is that these properties have still substantial income flows and revenues that could support taxes, maintenance, operation and a reasonable level of debt.

### *6.3.4. Types of properties*

In examining historical data, Moody's has identified differential rates of collections based on property type. For example, vacant land properties, hospitals and healthcare facilities tend to perform worse than other property types. In addition tax liens secured by commercial properties perform more poorly than residential properties. They tend to have "longer potential liquidation timelines, greater potential for environmental risk exposure and higher likelihood of property owners seeking bankruptcy protection, which can further lengthen asset liquidation timing as well as possibly result in adjustments to the amount owed by the property owner under the tax lien obligation" (Moody's, 2014:1).

#### **6.4. Securitization versus other enforcement strategies**

It is impossible to fully evaluate whether or not the City's redemption rates would have been different if it had used another method of enforcement, since one cannot definitively prove a hypothetical of this type. However, some evidence suggests that the securitization program has not produced exceptional redemption rates. Other large US cities using alternate property tax enforcement methods routinely collect almost all of their delinquent property taxes in subsequent years after the initial levy. While it is difficult to do a definitive comparison given different methods of data collection and reporting in each city and complex differences in real estate market dynamics, a few examples can at least provide context. For example, Los Angeles, in which the locality forecloses on property in tax default after three years, has high rates of delinquent tax collection. Rates of collection are also high in Boston, in which the locality forecloses on property in tax arrears after three years. Both of these cities routinely collect almost all of delinquent taxes in years subsequent to their levy (See Tables 6.4 and 6.5).



In addition, New York City's own alternative property tax enforcement program for potentially distressed property (Third Party Transfer) has resulted in payment of a vast majority of delinquent taxes owed before city-administered foreclosure was completed. On average, between 1997 and 2006, eighty-two percent of owners of properties excluded from the lien sale paid their tax arrears in full. Between 1997 and 2012, properties in the program generated \$443 million in revenue (HPD Division of Property Disposition and Finance, 2012). While the enforcement mechanisms of the Third Party Transfer program are not a perfect comparison to those of the lien sale and securitization, the comparison is instructive in that it demonstrates that even for the most distressed properties, the City has been able collect full tax arrears from a large majority of properties upon threat of foreclosure given strong real estate market conditions.

Table 6.4

*Property tax levies and collections, Los Angeles, Fiscal Years 2002-2011*

Fiscal Year	Total Tax Levy (1) for the Fiscal Year	Collected within the Fiscal Year of Levy		Collections in Subsequent Years (2)	Total Collections to Date	
		Amount	Percent of Levy		Percent of Levy	Amount
2001-02	591,029	560,750	94.88%	\$27,199	\$587,949	99.48%
2002-03	624,633	599,921	96.04%	28,939	628,860	100.68%
2003-04	673,417	645,697	95.88%	27,328	673,025	99.94%
2004-05	730,495	688,993	94.32%	30,932	719,925	98.55%
2005-06	784,864	708,009	90.21%	45,693	753,702	96.03%
2006-07	862,415	814,880	94.49%	80,748	895,628	103.85%
2007-08	935,881	872,254	93.20%	64,845	937,099	100.13%
2008-09	1,008,578	948,294	94.02%	110,519	1,058,813	104.98%
2009-10	1,009,256	947,165	93.85%	86,089	1,033,254	102.38%
2010-11	984,897	941,070	95.55%	73,905	1,014,975	103.05%

*Notes.* 1. Includes 1 percent basic levy only, which is a General Fund revenue, excludes City levy for debt service 2. Includes collections on adjustments for undetermined prior fiscal year(s). Adapted from City of Los Angeles (2011).

Table 6.5

*Property Tax Levies and Collections, Boston, Fiscal Years 2002-2011*

Fiscal Year Ended June 30	Taxes Levied for the Fiscal Year (1)	Collected within the Fiscal Year of the Levy		Collections in Subsequent Years	Total Collections to Date	
		Amount	Percentage of Levy		Amount	Percentage of Levy
2002	\$972.7	\$958.8	98.6%	6.9	\$965.7	99.3%
2003	1035.9	1016.3	98.1%	8.9	1025.2	99.0%
2004	1094.2	1071.1	97.9%	19.6	1090.7	99.7%
2005	1150.1	1127.2	98.0%	13.2	1140.4	99.2%
2006	1208.2	1184.5	98.0%	11.3	1195.8	99.0%
2007	1270.8	1245.2	98.0%	13.3	1258.5	99.0%
2008	1334.6	1317.2	98.7%	7.2	1324.4	99.2%
2009	1398.9	1382.3	98.8%	7.9	1390.2	99.4%
2010	1465.5	1447.2	98.8%	7.7	1454.9	99.3%
2011	1541.1	1523.5	98.9%		1523.5	98.9%

*Notes.* (1) Includes omitted assessments billed in June of each fiscal year and subsequently reduced residential exemption. Adapted from City of Boston, (2011).

## 6.5. Improving on-time property tax collection

Before it began selling liens again in the 90s, New York City did not have significant problems with property tax enforcement, as confirmed by an internal memo authored by both Department of Finance and HPD officials in 1995:

[The] in-rem tax foreclosure process has proven to be an extremely effective and relatively inexpensive mechanism for coercing the voluntary payment of the City's \$7 billion in annual real property tax assessments, (See the attached chart reflecting a 1994 City-wide tax delinquency rate of less than 5%) (City of New York Department of Finance and City of New York Department of Housing Preservation and Development, 1995).

However, proponents of the City's tax lien securitization program have argued that providing an effective deterrent to delinquency is one of the most useful aspects of the program (Perrine, Shultz and Marrazi, 2011; Page, 2010). Those I spoke with at both the Department of Finance and the Office of Management and Budget cited the effectiveness of the lien sale as an enforcement tool as the primary reason for doing it.

Has selling and securitizing liens helped New York City to improve property tax collections? One way to measure property tax collection is to examine collection rates of property taxes in the first year of billing. Given the unavailability of suitable data to compare the impact of various local policies, evidence is sparse on effectiveness of tax lien sales on on-time collections. In theory, tax lien securitization would have the same effects as a regular tax lien sale on tax payer behavior. Many factors contribute to collection rates including economic conditions such as unemployment, income and property value (DeBoer, 1990; DeBoer and Conrad, 1988a). As such, it is difficult to conclusively determine what effect the lien sale has had on overall collection rates. There is only one study that estimates the responsiveness of taxpayers to tax lien sales. Miller

(2012) has shown that localities that hold tax lien sales improve property tax collections by about 2% .

In New York City, after lien sales and securitization began in 1996, overall collection rates did increase very slightly, from 91.3% in 1994 to about 93.2% to 1998. Between 1996 and 2011, the average rate of collection in the first year of the tax levy was 92.4% (Office of the Comptroller of New York City, 2011) (See Figure 6. As mentioned above, there was a slight downturn in 2003 when the city imposed a large real estate tax increase which resulted in a 16.7% increase in the amount of taxes due. However, part of this slight increase may be attributed to the fact that in the four years prior to the 1996 lien sale and securitization, New York City had ceased aggressive enforcement of property taxes through foreclosure and confiscation of delinquent buildings (Poindexter, 1996; Oser, 1996).

In addition, other factors may have contributed to improved rates of on-time collection during this period. In 2002, the City instituted a \$400 property tax rebate incentive to owners who paid on time. New York City also conducts rigorous outreach and noticing of delinquent tax payers leading up to the sale. As Shelby Kohn, Senior Project Manager (Interview, 2012) for the lien sale says:

[The lien sale] is an extremely effective tool...The best part of the liens sale is the amount of money we bring in before the lien sale just from doing noticing, outreach, and having Council Members talk to their constituents...Our goal is for the lien sale to be as small as possible.

It may also be instructive to contextualize New York City's rates with respect to property tax collection rates in other cities and nationwide. How do New York City's collection rates compare with other cities? According to a study conducted by the Pew

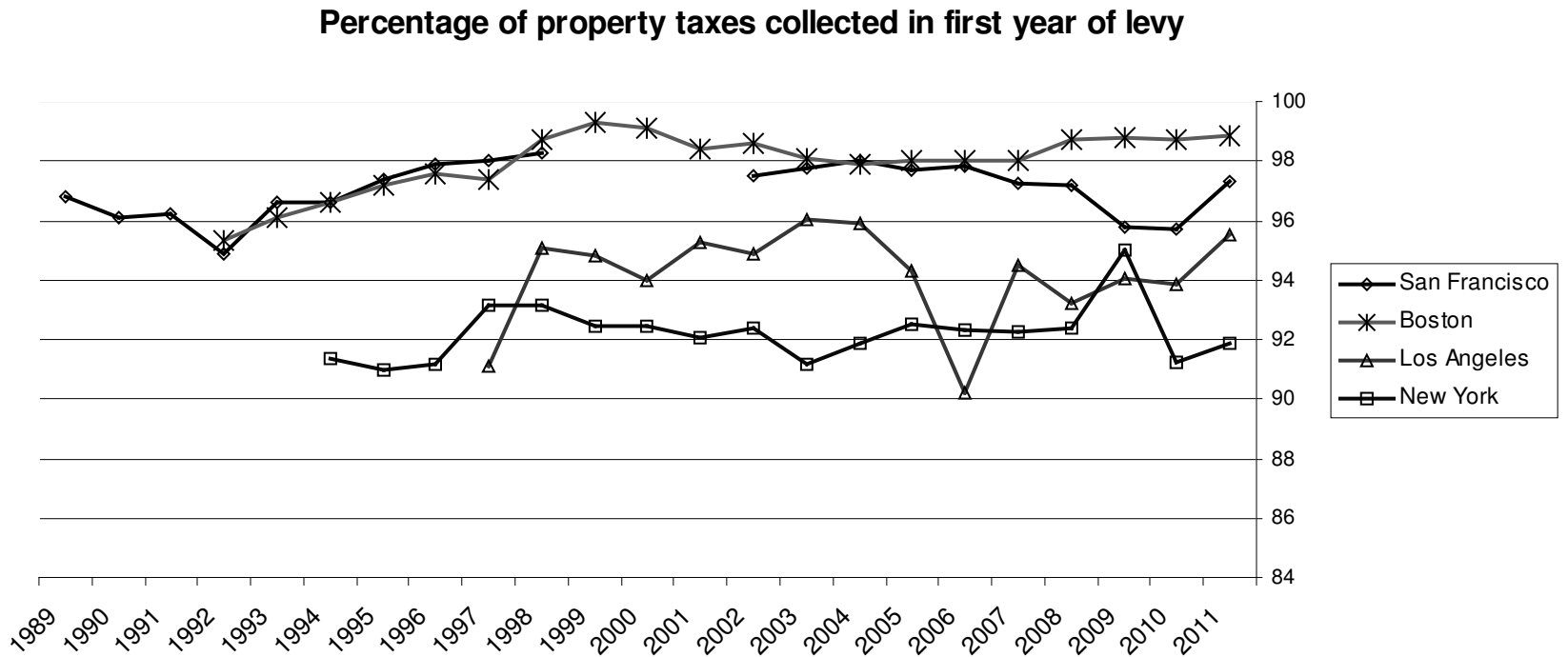
Charitable Trust, the median rate for cities around the US is 96.9%. For further context, Los Angeles, Boston, and San Francisco all have tax collection rates that are comparable to or above New York's. Los Angeles' average collection rate between 1996 and 2011 was 94%. San Francisco's average in those years was 97%. Boston's average was 98% .

While New York City did experience a bump in collections during the period right after the lien sale started, all of these cities saw a rise in collection rates after the end of the early 1990s recession. New York saw a net increase of 1.84 percentage points between 1994 and 1998. San Francisco saw a net increase of 1.7 percentage points. Boston saw a net increase of 2.1 percentage points. Los Angeles saw a net increase of 3.9 percentage points between 1997 and 1998, the first years for which data are available (City of New York Office of Comptroller, 2004; City of Boston Auditing Department, 2003; City of San Francisco Office of Controller, 2003; City of Los Angeles, Office of Controller, 2006).

These cities use a variety of tax enforcement measures. San Francisco and Los Angeles both enforce their tax laws with a tax deed sale in which the taxing body sells the tax delinquent property at auction (San Francisco Office of Treasurer, Los Angeles County Treasurer, 2012). The City of Boston conducts in-rem foreclosures and auctions properties (City of Boston, 2012). These trends suggest that lien sale and securitization is not necessarily more effective than other kinds of property tax enforcement strategies.

Figure 6.2

*Percentage of property taxes collected in the first year of levy*



*Note.* Data from City of New York Office of Comptroller (2013), City of Boston Auditing Department, (2013), City of San Francisco Office of Controller (2013), City of Los Angeles, Office of Controller (2013).

## 6.6. Residential properties, small debts, neighborhoods of color

Since 1996, the vast majority of liens that have been sold are for Class 1 properties (one-to-three family residential properties), however Class 4 (commercial and industrial) properties account for the greatest percentage of liens in dollar value. For example in 2011, there were 2,045 liens sold for Class 1 properties, representing about \$15 million in delinquent payments. That same year, there were 1,601 liens sold for Class 4 properties representing more than \$40 million in delinquent payments (Department of Finance, 2012) (See Table 6.6). Many newer multi-family rental and condominium properties in the City qualify for tax abatements, with owners owing no property taxes at all for a fixed period of time.

With regard to residential properties which have liens sold, the dollar amounts for delinquencies are typically small. I focus my analysis primarily on Class 1 and Class 2 tax liens, which represent the numerical majority of liens sold. For example in 2011, out of 2,045 Class 1 properties with liens sold, 60 percent had delinquencies that were less than \$10,000. Out of 1,507 Class 2 properties, 45 percent had delinquencies that were less than \$10,000 (New York City Department of Finance 2010; New York City Department of Finance 2011; New York City Department of Finance 2012 ).

Table 6.6.

### *Count and Amount of Delinquent Property Taxes by Tax Class (2011)*

<b>Tax Class</b>	<b>Count</b>	<b>Amount of Property Taxes Owed</b>
1	2,045	\$14,984,658.54
2	1,507	\$23,783,998.70
4	1,601	\$40,866,962.87
Total	5,153	\$79,635,620.11

*Note.* Compiled from New York City Department of Finance (2011).



Table 6.3

*Count and amount of total lien principal balance (TLPB) by property type (2011)*

Type of Property	Count	Initial TLPB
Asylums and Homes	1	\$427,068
Condominiums	290	4,096,849
Educational Facilities	16	428,029
Elevator Apartments	40	4,430,747.20
Factories and Industrial	81	2,157,260
Garages and Gasoline Stations	434	6,900,256
Hospitals and Health Facilities	5	1,778,932
Hotels	14	1,732,153
Indoor Public Assembly and Cultural Facilities	10	474,723
Loft Buildings	10	1,952,150
Miscellaneous	101	818,016
Office Buildings	92	3,469,094
One Family Dwelling	260	3,566,580
Outdoor Recreational Facilities	7	172,995
Primarily Residential - Mixed	458	8,007,128
Religious Facilities	18	837,036
Store Buildings	347	14,063,319
Theatres	1	41,109
Transportation Facilities	2	31,124
Two Family Dwellings	1,300	10,880,401
Vacant Land	590	6,732,706
Walk-Up Apartments	1,247	26,122,279
Warehouses	92	1861445
Total	5,416	101,983,400

*Notes.* Adapted from JP Morgan Chase (2011).

Table 6.4.

*Amount Owed On Properties in the 2011 New York City Lien Sale (Means and Standard Deviations)*

<b>Amount owed in dollars</b>	<b>Class 1 properties n=2045</b>	<b>Class 2 properties n=1507</b>
0-4,999	0.293 (0.455)	0.256 (0.437)
5,000-9,999	0.310 (0.462)	0.193 (0.394)
10,000-24,999	0.312 (0.463)	0.317 (0.465)
25,000-49,999	0.066 (0.248)	0.130 (0.336)
>50,000	.0176 (0.131)	0.102 (0.303)

*Notes.* Data from New York City Department of Finance (2011).

Given the small size of most of these liens, the City's declining rates of property tax delinquency in recent years have also reflected the increasing marginality of tax debtors to the real estate market. Tax delinquency rates are measured as a percentage of delinquent tax amounts of the total tax levy. With overall increases in property prices, New York City's property tax levy has dramatically increased in the recent decade, growing 108% between 2001 and 2011, outpacing the growth of the City's budget, which only grew by 66%. In those years, the Real Property Tax levy also grew to 26.7% of the City's total budget, from 22% (Real Estate Board of New York, 2011).

While redemption rates have been high in general, for some property owners this has caused considerable financial strain. Joshua Zinner (interview, 2012), an attorney and Co-Director of the New Economy Project, an organization that has worked with delinquent property owners describes the ways in which some owners redeem their liens:

People along the way are managing to pay them off. It's probably a combination of reverse mortgages, borrowing from friends and family, pulling together every dime they can, getting into high cost unsecured credit. Back in the old days, people would get into subprime mortgages, and they'd keep refinancing. There would be repeated refinancing. The lender would come around and say you have this tax lien foreclosure, we can get you into refinancing, and then they'd gouge them. The tax liens were a big feeder of predatory refinancing. It was a huge feeder of predatory refinancing. But since the crash, those loans haven't been as available, not in the same way. There's a lot of different ways that people are getting access to the funds that creates all kinds of financial strain on families including not being able to pay their current tax bill.

Others fall deeper into a cycle of high cost borrowing. I spoke with a number of property owners who had taken out high interest rate loans to pay their property tax debt (Interviews, 5/5/12). While their experiences may only be anecdotal, some literature

suggests that property owners with tax liens are often the target of predatory lenders (Ababon, 2006).

By and large, New York City's lien sales since 1996 have been comprised of properties in the Bronx and in Brooklyn in neighborhoods where a majority of residents are people of color. A large body of research has shown that in neighborhoods of color, decades of lender dis-investment in the mid-twentieth century were followed by an influx of high cost capital in the early twenty-first century that has produced high rates of mortgage defaults and foreclosure in these areas during the mid 2000s (Avery et al, 2000; Wyly et al 2001; Newman and Ashton, 2013). The financial distress for property owners that results in difficulty with mortgage payments also manifest in tax delinquency. This was corroborated by many property owners I spoke with. One resident of Brooklyn that I spoke with has owned his home since 1997. He is a veteran. Upon retiring from the military, he returned to Brooklyn. In 2000, he was convinced to refinance his home through Ameriquest Mortgage, the largest sub-prime mortgage lender in the US at the time and ended up with an Adjustable Rate Mortgage. In his own words:

We originally got duped into refinancing with Ameriquest Mortgage. They got us in an adjustable rate loan, and that killed us...Our neighbor across the street, she was getting refinanced, so she told him to come across the street. This guy sat down, and he was the best snake oil salesman I ever met...He painted it so nice. He said, 'You could consolidate all your bills. In a year you could get a fixed rate. We'll just give you an adjustable rate now.' He screwed me, and I guess I have nobody to blame but myself... I went from paying \$1100 a month mortgage, by the time they got through with me, I was paying \$2000 a month...Ameriquest sold the loan to Optimum. Then Wells Fargo got the loan. They were letting the whole thing drag on, so the interest would keep on compounding...We had two houses at the time. We had another house in Yonkers, and we lost that house, it was my father's house (Interview, 6/2012).

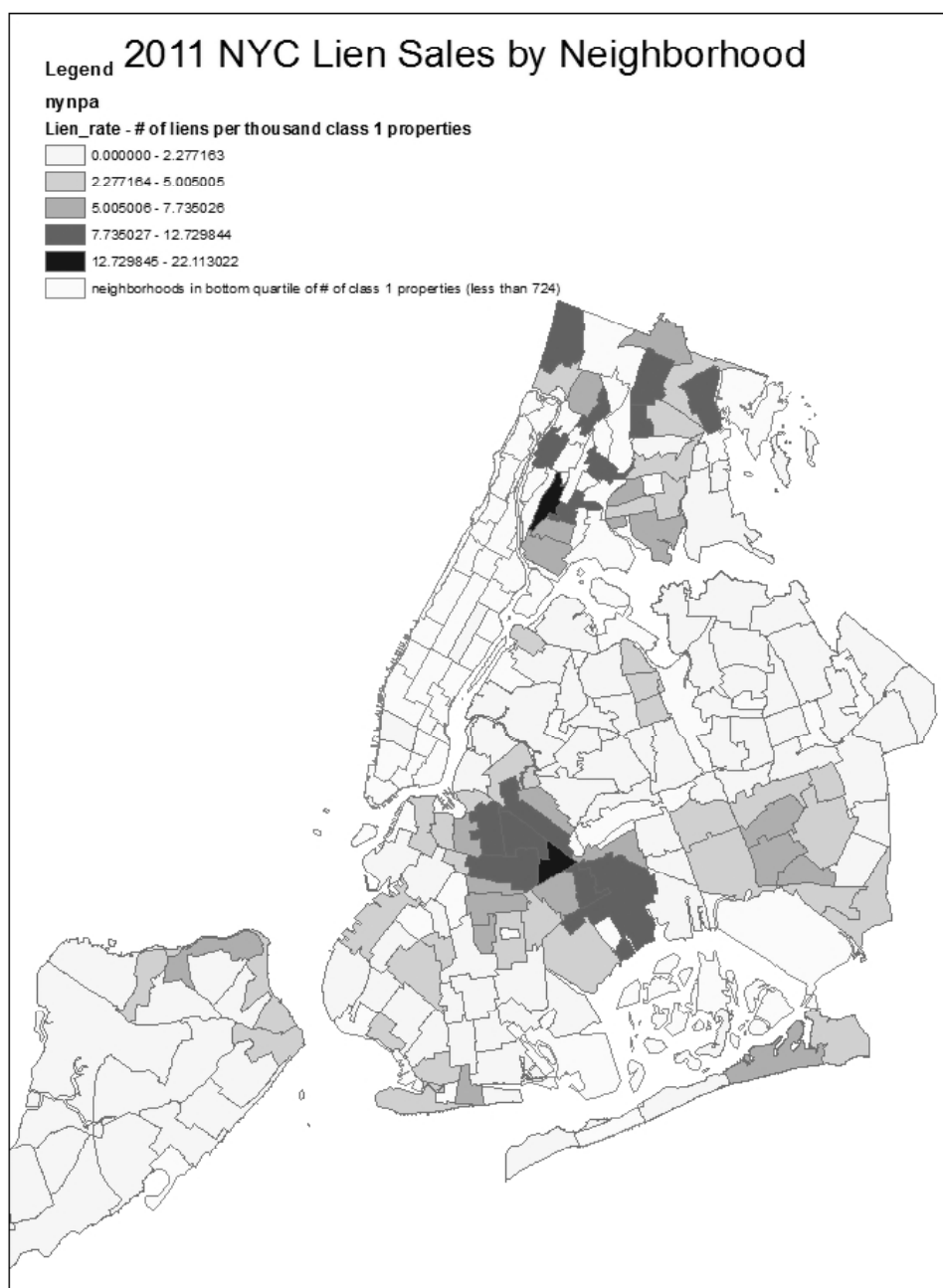
With the increased costs on his mortgage, this property owners fell behind on his property taxes and water charges. His water lien was sold in 2008; the amount was \$12,995.75. The total fees were \$8,865.05. The interest was \$4,859.18. The Trust filed a foreclosure against his home in 2009. At the time his mortgage lender had also filed for foreclosure. Ultimately, he obtained a low-interest loan to help him redeem the lien and avoid foreclosure with the help of a legal services provider, South Brooklyn Legal Services and a credit union, the Lower East Side Federal Credit Union.

Another property owner of color with whom I spoke owned a three-family house in Canarsie. He had an adjustable rate mortgage with Chase, and his interest rate increased at the same time that he lost his job during the Great Recession. As a result, he fell behind on his mortgage and was facing bank foreclosure. He estimates that he owes about \$6,000 dollars to the city.

While the experiences of these property owners may only be anecdotal, data on mortgage lending and tax lien sales confirm the coincidence of expensive mortgages and mortgage default with tax delinquency. Many of the neighborhoods with large numbers of Class 1 liens sold also had the highest rates of loans from sub-prime lenders in the 2000s and the highest rates of mortgage foreclosure beginning in 2008 (See Table 6.8). Table 6.8 ranks the top ten neighborhoods in the city according to the rate of lien sales. Rows shaded in dark gray represent neighborhoods also ranked within the top ten for the highest percentage of mortgages from sub-prime lenders in 2006. Neighborhoods shaded in light gray ranked within the top ten neighborhoods with the highest rate of mortgage foreclosures in 2009. Neighborhoods shaded with diagonal lines ranked in the top ten neighborhoods for both sub-prime mortgages in 2006 and mortgage foreclosures in 2009.

Figure 6.6

*Map of rates of liens on Class 1 properties sold, by neighborhood (2011).*



*Notes.* Data from New York City Department of Finance (2011).

Table 6.8

*Neighborhoods with the highest rate of Class 1 lien sales in 2011*

<b>Lien sale rate rank (2011)</b>	<b>Borough</b>	<b>Community District</b>	<b>Neighborhood Name</b>	<b>High rate of subprime mortgages (2006)</b>	<b>High rate of mortgage foreclosures (2009)</b>
1	The Bronx	BX14	East Concourse - ConcourseVillage		
2	Brooklyn	BK79	Ocean Hill	Yes	
3	The Bronx	BX35	Morrisania - Melrose		Yes
4	The Bronx	BX22	North Riverdale-Fieldston-Riverdale		
5	Brooklyn	BK85	East New York (part B)	Yes	Yes
6	Brooklyn	BK75	Bedford	Yes	Yes
7	The Bronx	BX17	East Tremont		Yes
8	The Bronx	BX44	Williamsbridge - Olinville	Yes	
9	The Bronx	BX13	Co-Op City		
10	Brooklyn	BK35	Stuyvesant Heights	Yes	Yes

*Note.* Data from New York City Department of Finance (2011) and New York Office of the State Comptroller (2011).

Moreover, there are important implications for neighborhoods with regard to how a lien is redeemed, whether by the original property owner, a mortgage lender, a new owner or through foreclosure and liquidation. Unfortunately, private servicers do not collect data on what parties redeem liens, making it difficult to identify broad trends and whether or not there are adverse effects related to speculative real estate activity, rates of owner occupation or affordability and displacement in certain neighborhoods.

### **6.7. Conclusion**

The issue of housing abandonment and high rates of tax delinquency, which was so central to original arguments for establishing the lien sale, has been made largely irrelevant by the booming New York City real estate market since 1996. Collections on liens since that time have been more than sufficient to repay the bonds issued, in part as a result of the across-the-board 5% surcharge, rapid accrual of interest on delinquent accounts as well as significant overcollateralization. It is likely that these collection rates can be attributed to legal imperatives associated with property taxes and a strong real estate market rather than to the practice of tax lien securitization per se.

While it is difficult to assess whether New York's lien securitization program has produced higher delinquent tax collection rates than other enforcement strategies would have, New York City's collection rates are not exceptional in comparison to delinquent tax collection rates in other cities that employ different methods. In addition, a majority of properties excluded from the lien sale have paid their arrears in full upon threat of foreclosure from the City. This suggests that to the extent that some entity (whether



public or private) engages in strong enforcement via high penalties and foreclosure, delinquent taxes are eventually paid.

In addition, on-time tax collection rates in New York City since lien securitization began in 1996 have been adequate but not exceptional, and are slightly below the median rate for other comparable cities. A modest increase immediately after 1996 might be attributed to the fact that the City had not been aggressively enforcing property taxes in the few years prior to 1996. Declines in tax delinquency in relation to the City's overall tax levy might also be in part a result of rising real estate prices and the relatively small amounts owed by tax debtors.

The majority of liens securitized have been for Class 1 properties, with relatively small debt amounts of \$10,000. Liens securitized have been concentrated in outer borough neighborhoods of color, the same neighborhoods which have historically experienced difficulties with mortgage lenders.

## **Chapter Seven - Conclusions**

As discussed in the introduction to this dissertation, a number of scholars have theorized the process of local financialization as a series of policy projects. Proceeding from this notion, I have explored the extent of the various material and ideological resources mobilized in the service of financial integration and the limits of that mobilization for various localities. Regarding New York City's experience with tax lien securitization, I have aimed to investigate both the local and extra-local processes that produced the particular practices that the City adopted and the implications of those practices for public finance, housing policy and governance practices.

After reviewing the key findings from each chapter of this study, I conclude this chapter and the dissertation with questions that remain and areas for future research.

### **7.1. New markets and new attempts at financial engineering**

I began in Chapter Three, by examining the processes which produced the emergence of tax lien securitization in various localities beginning in the 1990s and documenting the reasons for its abandonment in most localities. I traced the convergence of two trends: expanding capital markets seeking new income streams for asset-backed securitization, and the struggles of local governments in a post-Keynesian era to identify new sources of income. Going beyond the truism of growing integration between financial markets and local governments, I delineated the differences between various kinds of capital which sought integration into municipal public finance during this period.

I contended that there are important consequences as to *which* kind of capital and *how* local governments were integrated.

Municipally-sponsored securitization offered local governments the opportunity to connect to a growing institutional investment market, financial institutions the opportunity to broker that connection, and investors the opportunity to buy a new kind of fixed-rate investment-grade security. However, this particular form of financial engineering reapportioned uncertainty in ways that did not always meet the needs of local governments or their constituencies. I showed that municipally-sponsored tax-lien securitization did not meet the needs of most localities for two primary reasons. First, sponsoring securitization did not allow local governments to meaningfully transfer the risk of non-payment in the same way as conventional lien sales. Second, given this drawback, sponsoring securitization was not worth the significant expense of engaging various financial intermediaries necessary to produce investment grade securities (including underwriters, credit ratings agencies and financial advisors). As such, many local governments turned to an alternative set of globalizing capital, investment funds such as hedge funds, which were willing to take on higher risks and pay high premiums upfront to purchase tax liens in bulk. This arrangement much more closely resembled a conventional tax lien sale than municipally-sponsored securitization in which the localities retained a financial stake in the transaction. While some companies purchasing tax liens in bulk have aggregated tax lien holdings from various localities and securitized them, most local governments are no longer parties to the securitization process. By engaging in bulk sales to investment funds, some localities have achieved tax lien

financing and risk transfer objectives. But in doing so they gave up a certain amount of control over housing and urban redevelopment outcomes.

## **7.2. The financializing urban state: a New York City case study**

In Chapter Four, I turned my attention to New York City, the only locality that adopted securitization as a long-term practice. I analyzed the politico-economic circumstances that produced unique characteristics in New York City's municipally-sponsored tax lien securitization program. The most notable characteristic of New York's program is the removal of potentially risk-laden distressed residential properties from the pool of liens to be securitized, which ensured the financial viability of the eventual securitized bonds. Through archival research, I documented how this aspect of New York's program was the product of a particular political compromise emerging from the City's history of severe housing abandonment, a dynamic tenant movement, and active government involvement in distressed housing rehabilitation. I showed how, in need of an immediate source of funds to address budget shortfalls, the Giuliani administration leveraged concerns about the costs of the City's *in-rem* housing program—which largely housed very low-income tenants of color—to push through its proposal for tax lien securitization. I contended that the legacies of long-term structural racism were central to the production of a new financialized form of governance to which all New Yorkers then became subject.

Political imperatives at the time required the removal of distressed properties from the pool of liens to be securitized. This removal had the further consequence of significantly reducing the risk of New York's tax lien-backed securitization transactions

in comparison to similar transactions in other cities and making its financial viability possible. Hence, New York City did not attempt to transfer risk of non-payment from distressed properties to outside parties via securitization in the way that many of the other municipalities sponsoring securitization programs had attempted. While for other cities, lien securitization proved unhelpful in offloading financial risk and thus was too expensive to be worth adopting on a long-term basis, for New York City, the particular political compromises necessary meant that the imperatives and goals of the program were different from the outset. As such, the endurance of financialized governance practices has been contingent upon local political negotiation and compromise.

In Chapter Five, I closely examined the mechanics of New York City's program, and its implications for understanding evolving institutional forms in post-Keynesian urban governance. I showed that financial engineering offered institutional forms and logics that shaped the development of new neoliberal state capacities, intersecting with attempts of the local state to reimagine itself as more entrepreneurial. Following other scholars, I confirmed that the shift to a neoliberal state reconsolidated state power, producing new forms of governance and showed how financialization intersected with that process. I showed that through securitization, New York City retained significant control and financial stake in its tax liens even after their sale.

I contended that the sale of assets at the center of the lien securitization transaction is only nominally a transfer of assets, given that the entity to which tax liens are transferred is a wholly-owned subsidiary of the City with no office, employees or *raison-d'être* other than serving as a vessel for City assets and debts and as a proxy for the City in hiring private contractors and holding title to tax-foreclosed properties. Given that

the City retains significant administrative authority and financial concern, I argue that municipally-sponsored tax lien securitization should be considered a delegation of property tax enforcement to private contractors, rather than as a full divestment through asset sale and total relinquishment of responsibility. Even though this is the case, I demonstrate that the City attempts to portray the transaction as such a divestment by distancing itself from both its subsidiary and the tax liens in question and by employing the familiar idiom of a tax lien sale.

Additionally, I discussed the implications of this arrangement for understanding financialization and the changing municipal state. For New York City, the technique of securitization has not only served as a gateway to new capital, but has also had the effect of fundamentally changing municipal institutional form. I argued that rather than a retreat or reduction of state capacity, the effect of securitizing tax liens has been to expand the local government's capacity to raise resources, spend public money and exercise centralized administrative control. Securitization has afforded New York City a greater ability to control fiscal and housing development outcomes than conventional tax lien sales would have, but it has also meant that there is both minimal public oversight over property tax enforcement and little public understanding of the City's role in the arrangement or the public expenditures that are embedded in the transaction.

The powers that the City has gained through using securitization are various. They include: increased counter-cyclical capacity to increase its liquidity and make public expenditures outside of budgetary oversight processes; the ability to conduct outsourcing to private servicers outside of regular city procurement and contracting requirements; and the ability to dispose of tax foreclosed properties without having to

comply with regulatory mandates for public review and with less likelihood of effective political opposition. Consequently, I posited that this arrangement had the effect of trading previous political and regulatory constraints for centralized administrative control and new financial liabilities. I also argued that securitization achieves some of the same effects as previous institutional innovations such as public authorities, but with even less transparency. In sum, I contended that where such financial engineering largely failed to help other local governments to meaningfully relieve fiscal stress and manage uncertainty, it did allow New York City to generate new institutional forms and new state capacities and reconfigure use of its resources.

In Chapter Six, I explored the outcomes of New York City's program, with regard to its revenue goals and with attention to the geographic incidence of liens sold. I found New York City's delinquent tax collections and its on-time tax collections to be adequate but not exceptional.

What emerges throughout the New York City case study is the story of a property tax enforcement program that was born of the necessities of a particular historical moment for the City, and that took advantage of the eagerness of expanding financial markets to extend capital via securitization in the service of a variety of ends. Using securitization, the City was able to construct an essentially public property tax enforcement program while avoiding many of the encumbrances of public programs. Compared to conventional lien sales and bulk lien sales, tax lien securitization is preferable with regard to municipal control over delinquent tax revenues and housing and development outcomes. However, the City's use of securitization precipitated changes in

municipal institutional form that had significant consequences for public transparency and accountability with regard to the City's fiscal and housing policy.

It is possible to argue that tax lien securitization has outlived its usefulness in certain ways. Given the small size of overall delinquent tax amounts in comparison to the overall tax levy, it may not make sense for the City to use such an expensive mechanism to enforce its property taxes. Nowadays, the dividends offered by avoiding public review and political battles over tax-foreclosed property disposition are much lower than when rates of housing abandonment were higher and the movement of tenants in city-owned property stronger. With regard to the need for financing, the City is also in less danger of exceeding its state constitutional debt limits is also than it was in the 1990s.

As I have shown, many of the substantial costs of the program are subsidized by property owners in the margins of the city: small debtors in outer borough neighborhoods. There are alternatives available to the City. While the high and escalating penalties and interest rates charged to debtors are necessary to enforce payment, New York could choose collect those penalties and interest payments directly without securitizing its tax liens. In that way, the program would not incur the transactional costs associated with securitization. The City could also choose to contract with private servicers directly, instead of via the tax lien trusts.

Although the City's alternative property tax enforcement program for distressed residential properties, Third Party Transfer, is not a perfect comparison, it does demonstrate that delinquent property tax collection directly enforced by the city yields revenues and is neither administratively burdensome, nor expensive. City-initiated foreclosure has not been lengthy, with foreclosure proceedings initiated by the housing



agency's Law Department taking on average 2.25 years. Third, the costs of administering the program have not been prohibitively high. Rehabilitation costs about \$5,000 per unit and the overall program costs the City between \$35 million and \$50 million per year (HPD Division of Property Disposition and Finance, 2012). However, if the city did choose to go that route, it would have to face the possibility that increased transparency would result in new costs and delays.

It is almost a cliché to say that things have changed greatly in New York City since the 1990s. Despite the very different circumstances facing New York City in recent years, the tax lien securitization program has persisted, likely in part due to the convenience of inertia. As one of the original architects of the program that I spoke with, said, "If it ain't broke..".

### **7.3. Future research**

My research has had various limitations; as such, it is important to be clear about what I have and have not accomplished in this dissertation. While I have documented the emergence of municipally-sponsored tax lien securitization in the United States, I have not thoroughly investigated the securitization of tax liens by other non-municipal entities such as banks and other financial institutions, particularly in its post-2008 financial crises iterations. It remains to be seen what the outcomes are of recent large scale multi-jurisdictional tax lien securitizations conducted by financial institutions.

With regard to New York City, I have attempted to provide broad guidelines for understanding what the investment of public expenditures is into this program. While I have attempted to provide clarity about the structure and chain of accountability to guide

public discourse and public discussion in the future, a more in-depth accounting of the monetary costs to the public, taking into account the various factors involved including opportunity cost and a comparison with other strategies such as delinquent tax revolving funds, would provide useful insight.

In addition, I have not conducted an in-depth study into the empirical impacts on neighborhoods. I have given a broad overview of the geographic extent of liens sold, but a more in-depth study of the housing policy impacts of lien sale would provide further insight on how lien securitization has affected property owners and tenants of residential buildings. Do debtors wind up in further high cost debt in order to pay liens? Do conditions improve or deteriorate? Does the lien sale result in the displacement of tenants? Does the lien sale fuel real estate speculation? What happens to the properties that are confiscated by the Trust? Do they end up in tax arrears again?

Much of the data that would be useful for this kind of analysis are not currently readily available. The reporting documents that private servicers provide to the City do not track whether the liens are redeemed by the current owner or a new owner. The City might consider requiring certain kinds of data to be tracked by servicers. If New York City began requiring private servicers to collect such data, which it could, future research might determine what those trends are, and how they impact the city, its neighborhoods and its residents.

Finally, I have not conducted an analysis of the outcomes of the Third Party Transfer program. While much quality scholarship has been done on this program, a close empirical examination of the Third Party Transfer program alongside the lien

securitization program would undoubtedly yield new insights about the relative merits of tools available to New York City to enforce its property taxes.

#### **7.4. Conclusion**

By tracing financial integration to the early experiments in municipal sponsorship of securitization, it has been possible for this study to shed further light on the mutually constitutive nature of global financial integration and neoliberal urban state building over the last several decades. Throughout this study, the financialization of urban governance has emerged as a contingent, uneven and politically-dependant project. It has become clearer that in some instances, the financializing urban state connects to financial markets not only for the purposes of financing debt in the face of fiscal stress, but also to circumvent democratic processes in order to reconsolidate centralized administrative authority and assert greater control over public borrowing and spending. As such, one of the enduring effects of greater connection between financial markets and local government has been the replacement of the often arduous work of democratic accountability and public process, with greater financial liability.

## Appendix A. Tax lien sale procedure by state

Table A.1

*States That Allow Lien Sales By Type of Lien Sale, Maximum Interest and Redemption*

*Period*

<b>State</b>	<b>Type</b>	<b>Max Interest</b>	<b>Redemption Period</b>
Alabama	Overbid	12%	2.5 years
Arizona	Interest Rate	16%	3 years
Colorado	Overbid	10%	3 years
District of Columbia	Overbid	18%	0.5 year
Florida	Interest Rate	18%	2 years
Illinois	Interest Rate	18%	2.5 years
Indiana	Overbid	10%	1 year
Iowa	Percent Ownership	24%	1.75 years
Kentucky	Lottery	12%	1 year
Louisiana	Overbid	12%	3 years
Maryland	Overbid	20%	0.5 year
Mississippi	Overbid	18%	2 years
Missouri	Overbid	10%	1 year
Montana	Overbid	10%	3 years
Nebraska	Percent Ownership	14%	3 years
New Jersey	Interest Rate	18%	2 years
New York**	Negotiated	18%	1 year
Ohio**	Overbid	18%	1 year
Pennsylvania**	Overbid	18%	3 years
Rhode Island	Percent Ownership	16%	1 year
South Carolina	Overbid	12%	1 year
South Dakota	Overbid	10%	3 years
Tennessee	Overbid	10%	1 year
Texas	Negotiated	-	2 years
Vermont	Overbid	12%	1 year
West Virginia	Overbid	12%	1.5 years
Wyoming	Lottery	15%	4 years

*Notes.* \*\* Data was collected from the largest taxing jurisdiction due to within state variation (New York City, NY; Cuyahoga County, OH; Philadelphia, PA). Adapted from *The Cost of Delinquent Property Tax Collection* by Joshua Miller, 2012.

**Appendix B. Lien composition tables for selected sales**

Table B.1

*Selected Characteristics of Liens Transferred to 1996-1 Trust Including Charges, Initial Total Lien Principal Balance (TLPB), and Weighted Average Lien-To-Value Ratio (LTV)*

Tax Class	Count	Delinquent Taxes				5% Surcharge	Initial TLPB	Percent of Total	Wtd Avg LTV
		Real Property	Water & Sewer	Other Charges					
Class 2	1,635	\$40,829,203	\$13,164,406	\$1,065,543	\$2,752,957	\$57,812,111	23.09%	18.53%	
Class 4	3,010	164,819,523	16,059,074	2,540,417	9,170,950	192,589,965	76.91	26.31	
<b>Totals</b>	<b>4,645</b>	<b>\$205,648,726</b>	<b>\$29,223,481</b>	<b>\$3,605,961</b>	<b>\$11,923,908</b>	<b>\$250,402,077</b>	<b>100.00%</b>	<b>24.52%</b>	

*Note.* Adapted from JP Morgan Chase *NYCTL 2010-Trust Private Placement Memorandum*, 2010.

Table B.2

*Selected Characteristics of Liens Transferred to 2000-A Trust Including Charges, Initial Total Lien Principal Balance (TLPB), and Weighted Average Lien-To-Value Ratio (LTV)*

Tax Class	Count	Delinquent Taxes				5% Surcharge	Accrued Interest	Initial TLPB	Percent of Total	Wtd Avg LTV
		Real Property	Water & Sewer	Other Charges						
Class 1	1,285	\$11,312,643	\$4,802,388	\$3,626,325	\$952,334	\$2,200,164	\$22,893,853	9.42%	130.42%	
Class 2	1,525	36,284,636	12,616,918	3,372,327	2,403,112	5,068,617	59,745,609	24.58	82.53	
Class 4	2,847	100,049,243	16,544,480	13,357,957	5,986,135	24,458,169	160,395,983	66.00	153.90	
<b>Totals</b>	<b>5,657</b>	<b>\$147,646,521</b>	<b>\$33,963,785</b>	<b>\$20,356,609</b>	<b>\$9,341,581</b>	<b>\$31,726,950</b>	<b>\$243,035,445</b>	<b>100.00%</b>	<b>134.14%</b>	

*Note.* Adapted from JP Morgan Chase *NYCTL 2010-Trust Private Placement Memorandum*, 2010.

Table B.3

*Selected characteristics of Liens Transferred to 2004-A Trust Including Charges, Initial Total Lien Principal Balance (TLPB), and Weighted Average Lien-To-Value Ratio (LTV)*

Tax Class	Count	Delinquent Taxes				5% Surcharge	Initial TLPB	Percent of Total	Wtd Avg LTV	Wtd Avg Age
		Real Property	Water & Sewer	Other Charges						
Class 1	938	\$6,210,460	\$2,267,969	\$1,589,761	\$731,658	\$10,799,848	19.75%	56.25%	84.00	
Class 2	822	10,763,491	5,024,324	417,737	1,009,919	17,215,471	31.48	16.21	49.40	
Class 4	1,533	18,692,755	3,513,015	2,820,608	1,641,163	26,667,541	48.77	31.88	38.94	
<b>Totals</b>	<b>3,293</b>	<b>\$35,666,706</b>	<b>\$10,805,308</b>	<b>\$4,828,106</b>	<b>\$3,382,740</b>	<b>\$54,682,860</b>	<b>100.00%</b>	<b>31.76%</b>	<b>51.13</b>	

*Note.* Adapted from JP Morgan Chase NYCTL 2010-Trust Private Placement Memorandum, 2010.

Table B.4

*Selected characteristics of Liens Transferred to 2004-A Trust Including Charges, Initial Total Lien Principal Balance (TLPB), and Weighted Average Lien-To-Value Ratio (LTV)*

Tax Class	Count	Delinquent Taxes				Initial TLPB	Percent of Total	Wtd Avg LTV	Wtd Avg Age
		Real Property	Water & Sewer	Other Charges	5% Surcharge				
Class 1	2,041	\$9,724,152.91	\$8,936,333.39	\$899,490.92	\$1,560,522.49	\$21,120,499.71	26.81%	5.78%	80.50
Class 2	905	16,309,633.29	3,225,469.40	823,672.39	1,274,229.41	21,633,004.49	27.46	11.09	45.60
Class 4	1,412	28,418,300.83	3,589,108.08	1,922,487.53	2,087,832.88	36,017,729.32	45.72	24.51	46.49
<b>Totals</b>	<b>4,358</b>	<b>\$54,452,087.03</b>	<b>\$15,750,910.87</b>	<b>\$3,645,650.84</b>	<b>\$4,922,584.78</b>	<b>\$78,771,233.52</b>	<b>100.00%</b>	<b>15.03%</b>	<b>55.36</b>

*Note.* Adapted from JP Morgan Chase *NYCTL 2010-Trust Private Placement Memorandum*, 2010.



## Appendix C. Tax Delinquency Rates

**Table C.1**

*Tax Delinquency Rates in Selected Cities for Selected Years*

	2011	2009	2006		2011	2009	2006
Flint, MI	21.2%	17.6%	15.0%	Minneapolis	3.7%	2.4%	2.0%
Cleveland	20.2%	16.3%	13.0%	Baltimore	3.5%	7.8%	3.7%
Detroit*	20.1%	13.2%	7.3%	Waterbury, CT	3.1%	2.5%	3.2%
St. Louis	9.9%	11.8%	13.9%	Riverside, CA	3.1%	2.5%	1.4%
Philadelphia	9.0%	7.5%	6.6%	San Antonio	3.1%	1.7%	1.6%
Cincinnati	8.8%	9.1%	7.5%	San Francisco	2.7%	4.2%	2.2%
Kansas City, MO	8.4%	8.0%	6.3%	Dallas	2.6%	4.3%	2.8%
New York City	8.1%	5.0%	7.7%	Atlanta	2.4%	4.0%	8.2%
Pittsburgh	6.9%	2.9%	1.8%	Nashville	2.3%	1.4%	3.5%
Miami	6.7%	3.6%	3.2%	Houston	2.3%	3.5%	4.3%
Portland, OR	6.4%	7.3%	6.2%	Sacramento (County)	2.2%	3.8%	2.3%
Tampa	5.6%	4.3%	4.1%	Denver	1.9%	1.7%	0.7%
Memphis	5.3%	6.2%	6.3%	Washington, DC	1.8%	5.9%	3.1%
Buffalo	5.3%	5.3%	6.1%	Seattle	1.6%	1.9%	1.8%
Phoenix	4.6%	4.2%	2.6%	Las Vegas	1.6%	1.8%	0.7%
Los Angeles	4.4%	6.0%	9.8%	Orlando	1.2%	1.7%	1.0%
Newark, NJ	4.4%	n/a	n/a	Boston	1.1%	1.2%	2.0%
Milwaukee	3.9%	3.8%	2.2%	Chicago	n/a	16.0%	12.3%

*Note.* Adapted from *Delinquent Property Tax in Philadelphia: Stark Challenges and Realistic Goals*, by Pew Charitable Trusts, 2013.

## **Appendix D. Interview Protocols**

### **Script 1**

The following is a script for semi-structured interview with current or former staff of financial institution in New York City. I asked questions in the following categories. As a semi-structured interview, the questions were tailored to each particular respondent, but I have included sample questions below.

-Thank you again for agreeing to be interviewed. As I mentioned earlier, the interview will last no longer than 45 minutes, and if you prefer, your answers can remain confidential. Do you have any questions before we start?

#### **1. Role of Interviewee**

##### **Sample questions:**

- What is your current position at the company? (Or what was your position at the company?)
- How long have you worked at your current position? Have you held any other positions at this company in the past? What did you do before you came to the company?
- What is the role of the company you work for with regard to the New York City property tax enforcement system?
- How and why did the company first get involved?
- Who at the company was responsible for making the agreement with New York City?
- Has anything about your company's role or the way enforcement happens changed since you've worked here? Have things changed as housing market conditions have changed? If so, how?
- What are your job responsibilities as they relate to the New York City property tax enforcement system? Describe for me your day to day activities.

#### **2. Questions about Process**

##### **Sample questions:**

- How important is the work your company does in New York for the company as a whole? (i.e. what percentage of overall business does it represent?)
- What are the biggest challenges for the company in meeting its goals? What are the biggest challenges for you in your job?
- Who in your company was involved in this issue when New York City changed its practices in 1996, or when the law was renewed early in 2011? If so, can you describe your/their involvement for me, and what the process was like in general? Was there any difficulty or opposition?
- To the best of your knowledge, how does the process in New York City differ from the process in other places? Have you worked on other securitization deals either of tax liens or other kinds of debt? How was this deal similar or different from those other deals?
- Do you think the system works well in New York? Why or why not? Do you think the way enforcement is done benefits the city? Why or why not?

- If you could change the system in any way, what would you change?
- What is the most surprising thing that has ever happened to you as part of your job?

### **3. Other**

#### **Sample questions:**

- Whom else do you think it might be useful for me to talk to?
- Anything else you would like to share?
- Any questions you have for me?
- For the purposes of the study, I need some demographic information. What is your race or ethnicity?
- Thank you for your time.

## Script 2

The following is a script for semi-structured interview with current or former staff of government agency. I asked questions in the following categories. As a semi-structured interview, the questions were tailored to each particular respondent, but I have included sample questions below.

-Thank you again for agreeing to be interviewed. As I mentioned earlier, the interview will last no longer than 45 minutes, and if you prefer, your answers can remain confidential. Do you have any questions before we start?

### **1. Role of Interviewee**

#### **Sample questions:**

- What is your current position at the agency? (Or what was your position at the agency?)
- How long have you worked at your current position? Have you held any other positions in the past at the agency? What did you do before you came to this agency?
- What is the role of the agency you work for with regard to the New York City property tax enforcement system?

### **2. Questions about Process**

#### **Sample questions:**

- What responsibilities does your agency have, and what responsibilities do MTAG and JP Morgan Chase have with regard to property tax enforcement?
- Who at the agency is responsible for interfacing with MTAG and JP Morgan Chase?
- Has anything about the way enforcement happens changed since you've worked here? Have things changed as housing market conditions have changed? If so, how?
- What are your job responsibilities as they relate to the New York City property tax enforcement system? Describe for me your day to day activities.
- What are the biggest challenges for the agency in meeting its goals? What are the biggest challenges for you in your job?
- Who in your agency was involved in this issue when New York City changed its practices in 1996, or when the law was renewed early in 2011? If so, can you describe your/their involvement for me, and what the process was like in general?
- To the best of your knowledge, how does the process in New York City differ from the process in other places?
- Do you think the system works well in New York? Why or why not? Do you think the way enforcement is done benefits the city? Why or why not?
- If you could change the system in any way, what would you change?
- What is the most surprising thing that has ever happened to you as part of your job?

### **3. Other**

#### **Sample questions:**

- Whom else do you think it might be useful for me to talk to?

- Anything else you would like to share?
- Any questions you have for me?
- For the purposes of the study, I need some demographic information. What is your race or ethnicity?

### **Script 3**

The following is a script for semi-structured interview with current or former staff of a community organization or legal services agency. I asked questions in the following categories. As a semi-structured interview, the questions were tailored to each particular respondent, but I have included sample questions below.

-Thank you again for agreeing to be interviewed. As I mentioned earlier, the interview will last no longer than 45 minutes, and if you prefer, your answers can remain confidential. Do you have any questions before we start?

#### **1. Role of Interviewee**

##### **Sample questions:**

- What is your current position at the agency? (Or what was your position at the company?)
- How long have you worked at your current position?
- How does your job relate to the New York City property tax enforcement system?
- Are you or is your agency directly in contact with property owners who are delinquent in their property taxes? If so, what kinds of situations do you usually see with regard to people who are tax delinquent? What are their experiences with the private servicers?
- Would you be willing to put me in touch with any of them?

#### **2. Questions about Process**

##### **Sample questions:**

- Has anything about the way enforcement happens changed since you've worked here? Have things changed as housing market conditions have changed? If so, how?
- Were you or anyone at your agency involved in this issue when New York City changed its practices in 1996, or when the law was renewed early in 2011? If so, can you describe your/their involvement for me, and what the process was like in general?
- To the best of your knowledge, how does the process in New York City differ from the process in other places?
- Do you think the system works well in New York? Why or why not? Do you think the way enforcement is done benefits the city? Why or why not?
- If you could change the system in any way, what would you change?

#### **3. Other**

##### **Sample questions:**

- Whom else do you think it might be useful for me to talk to?
- Anything else you would like to share?
- Any questions you have for me?
- For the purposes of the study, I need some demographic information. What is your race or ethnicity?

## **Script 4**

The following is a guide for semi-structured interview with a current or former property owner for whom tax delinquency has been an issue. I asked questions in the following categories. As a semi-structured interview, the questions were tailored to each particular respondent, but I have included sample questions below.

### **1. General background**

Sample questions

- How long have you/did you own(ed) this property?
- Why did you first purchase this property?
- Who lives in the property?

### **2. Experience with tax-delinquency**

Sample questions

- When did you first find out you owed taxes?
- How much did you owe?
- How did you find out?
- How long have you had trouble paying your property taxes and why?
- What happened?
- What has been your experience with the city?
- What has been your experience with the private servicer?
- Did you have to pay interest or fees?

### **3. Experience with mortgage lending**

Sample questions

- Who is your mortgage lender?
- What kind of mortgage was it?
- Did you have difficulty paying your mortgage at any time? What happened?
- Did you ever have to take out additional loans to pay for your taxes?

### **4. Other**

Sample questions

- Do you think this practice benefits the city? Why or why not?
- If you could change the practice in any way, what would you change?
- Is there anyone else you would suggest that I speak with? Do you know anyone else who has had trouble with their taxes?
- For the purposes of the study, I need some demographic information. What is your race or ethnicity?
- Thank you for your time.

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