Zoning Case 21-05

Testimony by the DowntownDC Business Improvement District

Presented Orally on June 28, 2021, and In Written Form on September 27, 2021

Chairman Hood, Zoning Commissioners and Zoning Staff, thank you for the opportunity to testify today.

My name is Gerry Widdicombe. I am the Director of Economic Development for the DowntownDC Business Improvement District (BID), having served in this role since the Fall of 2000. Prior to that I worked for the DC government's Office of the Deputy Mayor for Planning and Economic Development and the Office of the Chief Financial Officer. In all those roles, creating a "Living Downtown" with more housing was an important goal.

The DowntownDC BID does not support the expansion of Inclusionary Zoning (IZ) to all building conversions (the subject of today's hearing) or to the D Zones because IZ XL Phases 2 and 3 are not in the best interests of the residents and businesses of DC.

The DowntownDC BID is one of the city's eleven business improvement districts. Our boundaries are roughly from 16th Street NW on the west, Massachusetts Avenue NW on the north (including the Walter E Washington convention Center), Louisiana Avenue NE on the east (to Union Station) and Constitution Avenue on the south. Most of the BID area is in a D Zone. See attached map.

The DowntownDC BID is a significant economic and fiscal contributor to the well-being of the District of Columbia. Though the DowntownDC BID is a just one square mile or 1.6% of DC's land, the DowntownDC BID

- Is home to
  - 24% of DC's pre-pandemic jobs
  - 33% of DC hotel rooms
  - 18% of pre-pandemic restaurant sales
  - But only 2% of DC residential units
- Had a net fiscal impact (revenues generated less expenditures made) of $750 million in FY 2020 and $881 million in FY 2019 based on generating 15% of the city's annual Gross Local Revenue.
  - The FY 2020 net fiscal impact of $750 million was available to fund the city's many important and successful social programs, including many affordable housing programs, like the Housing Production Trust Fund, the Local Rent Supplement Program and the Home Purchase Assistance Program)
- Staffs and funds a significant portion of the Downtown Services Center that serves hundreds of our fellow citizens experiencing homelessness and food insecurity every day.

Thus, it is not DowntownDC <u>or</u> the neighborhoods, it is DowntownDC <u>and</u> the neighborhoods.

The DowntownDC BID strongly supports the city's goal of increasing the supply of affordable housing at all income levels according to Mayor Bowser's current goal of 36,000 new units by 2025, of which 12,000 are to be affordable. We look forward to working with the city to establish the next set of housing goals now that the Comprehensive Plan 2021 amendments have been approved.

The BID is encouraged by recent statements by the Zoning Commission and the Office of Planning that much care is need in consideration of applying IZ XL to the D Zones. Because of the significant impact of the "IZ XL Deliberation Overhang" on the office to residential conversion market in DC zones, the DowntownDC BID would strongly recommend that that the Zoning Commission discontinue any further discussion of the removal of the exemption for the D zones at the same time that it renders a decision on the pending conversion case. That will allow currently stalled conversion projects to go forward to supply much needed housing in DowntownDC and grow the city's tax base which would allow for additional funding of the HPTF and other affordable housing programs.

The DowntownDC BID does not support the expansion of Inclusionary Zoning (IZ) to all building conversions (the subject of today's hearing) or to the D Zones because IZ XL Phases 2 and 3 are not in the best interests of the residents and businesses of DC for the following reasons:

1. IZ XL is inconsistent with DC's original concept of IZ: extra height, lot occupancy and density are provided (in most cases) to compensate for the lost revenue of IZ units compared to market-rate units. When a government entity, like the Zoning Commission, changes the rules, investors and developers will add an additional risk premium for doing business in that jurisdiction or avoid it all together. There are still prominent multi-family developers that will not build in DC due to TOPA and the potential changes to rent control being contemplated by the Council.
2. The loss of revenue from IZ XL without compensation may result in "takings lawsuits" that will further cloud the city's development reputation.
3. The loss in revenue in a 250-unit conversion (a 250,000 SF office building) can range from $5 million to $8 million. This is real money and, thus, increasing the likelihood of a takings lawsuit.
4. The "IZ XL Deliberation Overhang" is currently holding up 500 to 900 units in D Zone conversions and another 600 to 1,500 units in D Zones of ground-up construction. Thus, depriving the city of many housing units and millions of dollars a year in tax revenues.
5. The Zoning Commission's current deliberations will delay the recovery of the city's office market and potentially cause further declines in office building assessments, which, in turn, will cause further declines in office building property taxes which currently help support the funding of the Housing Production Trust Fund and other affordable housing programs.
    a. The current office market is very weak and is impacting DC property tax revenues.
        i. See attachments:
            1. The city's existing 22 million SF of vacant office space is concentrated in the DowntownDC and Golden Triangle BIDs, and the high likelihood that the vacant office space total will increase to over 26 million SF when the current 2.7 million SF of office construction that is under construction is completed.
            2. The city's vacancy rate and total of vacant SF has increased dramatically over the past few years.
        ii. The Office of the Chief Financial Officer's February 2021 Revenue Estimate letter highlighted the 9.7% reduction in the assessed values of large office buildings (which based on 2019's $66.3 billion of assessed values—translates into a $121 million reduction in FY 2022 revenues).
        iii. A recent DC office-building portfolio sale by WashREIT to Brookfield Properties was sold at 79.3% of the buildings FY 2022 assessed values. After factoring in an appropriate discount for a portfolio sale, it appears another reduction in the assessed values of large office buildings is likely.
        iv. JBG Smith and Boston Properties stocks are down 20% to 30% as of September 24, 2012, compared to February 14, 2020, so it appears that another reduction in the assessed values of large office buildings is likely.

Thus, IZ XL is a strong disincentive for both conversions in and out of the D zones and ground up construction in D zones. As a result, The Zoning Commission's current deliberations of disincentives are hampering the city's recovery from the economic decline caused by the COVID-19 pandemic.

There is a very good alternative to the proposed IZ XL Phases 2 and 3: Make IZ XL Phases 2 and 3 contingent on the City providing compensation for affordable units.

The DowntownDC and Golden Triangle BIDs and several property owners are working with Councilmember Pinto for a tax abatement pilot program to create middle-income housing in D zones (modeled on the recently enacted and funded Middle Income Housing Program) through a pilot office to residential conversions with middle income units.

An effort to include a pilot conversion program (with workforce housing at 80% of AMI) in the FY 2022 budget failed by a Council vote of 9 to 4. However, several councilmembers said they would like to see this legislation come back after going through the traditional legislative process (with its own hearing) rather than being included in the budget process (without its own hearing).

The remainder of this written testimony includes several comments on the overall Zoning Commission discussion of June 28, 2021:

1. IZ XL is just one tool to support the creation of affordable housing and the Zoning Commission needs to be aware of its potential unintended consequences and its need to be paired with other policies to avoid being a disincentive to conversions that would create new housing for the city and likely increase the city's tax base.

2. Buzzards Point Office to Residential Conversion projects. There were two conversion projects that have just been completed and have spurred several other projects to catalyze a critical mass of a new residential community in a previously undeveloped section of the city. These two projects moved forward because the owners were able to buy the buildings for approximately $80 to $85 per SF. If IZ XL had been in place at the time, the purchasers may have lost out to an office developer who was willing to pay a slightly lower price and today's office market would be in even worse condition.

3. There has been no office to residential conversions in DowntownDC in the past 20 years because the market for empty office buildings has been higher for office projects than for residential projects. Today, the two markets are very close to being equal: an empty office building has a market value of approximately $180 to $250 per SF (it was $300 to $350 per SF as recently as the Fall of 2019). The current market for an occupied office building is in the $500 to $600 per SF range. It appears that residential developers are only willing to pay $100 to $200 per SF for an office building to convert due to the lower rents per SF for residential ($42 to $48 per SF annual rents for a Class A apartment building compared to $50 to $60 per SF annual rents for a Class A office building when the office market recovers), a larger non-income common area compared to office and a lack of history on exact costs of and experience with conversions.

4. Middle Income Housing Program. This program, that is intended for high opportunity zones like Rock Creek West, is funded with a total tax abatement of $4 million per year for 40 years, beginning on October 1, 2024.

5. Wardman Park, Lord & Taylor and Mazza Gallerie. The Office of Planning has been working with the various parties involved and it is highly likely that all these projects will include substantial affordable housing. The proposal for Mazza, for example, is a new building that will be subject to IZ. In addition, several of the projects would be captured under IZ if they entail demolition and new construction. The unintended consequences of applying IZ XL to all conversions to avoid allowing these projects to "slip through" with no affordable units has significant unintended consequences for the rest of the city.

6. Downtown Development District History. Please note that after the creation of the new Downtown Development District (a significant rules change), there was a dramatic impact of little new development in the newly zoned areas for over ten years until the Williams Administration and the DC Council, led by Chairman Linda Cropp, created specific tax incentives or other city funding for residential, cultural and retail projects required by zoning. Thus, creating a successful example of zoning paired with other city government incentives. <u>It did not "just all work out".</u> Specifically, regarding Downtown Development District housing overlay, the new residential zoning requirements of the early 1990's contributed to the delay in residential development for over ten years and required property tax abatements and zoning relief regarding combine lot developments to incent residential development. Residential development Downtown then allowed for the market to price land for residential use in the Mount Vernon Triangle, NoMa, Union Market, Capitol Riverfront and Near Southwest DC, which has provided tens of thousands of new housing units bringing new residents to DC and taking pressure off existing market-rate affordable housing.

7. When looking at all the city's affordable housing efforts, it appears that the city is doing more than any U.S. city in investing in affordable housing, and the current IZ structure is contributing 300 to 500 units a year to this effort. The current IZ XL Phase 2 and Phase 3 proposals will not add to that total for many years because they create a disincentive to converting all buildings to residential and for new construction in DC zones. The Downtown DC BID believes it is in the best interests of the city's residents and businesses to not enact IZ XL Phase Two and Phase Three unless any affordable housing zoning requirements are combined with sufficient legislated compensation to pay for the affordable units.

8. Lastly, it is best to let DMPED structure the conversions of DowntownDC office buildings to residential to reflect current market conditions through a competitive RFP process rather than issue inflexible zoning rules in an "after-the-fact" manner. Under such a process, an economically sensitive office to residential conversion program requiring 8% affordable units at 80% of AMI, the city could produce an estimated 940 units of middle-income housing and an estimated 10,825 units of market-rate housing over the next five to ten years (based on the assumption that 10 million SF of office converting to residential, with an average residential unit size requiring 850 SF of office space).

Thank you for the opportunity to submit oral and written testimony on the important subject of increasing both the supply of market-rate and affordable housing in the District of Columbia.