



Office Competitiveness/Conversion

City Council Legislative Meeting
May 9, 2017

Background & Project Scope

- Growing the commercial tax base as an alternative to raising taxes or decreasing services has been identified as a top priority
- An increasingly competitive office market, the lack of high quality office properties, and the potential for office conversions are threats to Alexandria's competitive position in the region
- Goal of the study is to produce policy recommendations and guidelines to preserve and encourage commercial development and to maintain/improve the City's competitiveness in the regional economy



Forces & Circumstances Driving Conversions

- Conversions are driven by market and economic forces and circumstances unique to each property
- When all of these factors come together it may result in a building declining in economic value and it may be more financially compelling for a residential developer to purchase and convert an office building
- The City's current zoning regulations contain limited barriers to stopping this event
- Every significant conversion project identified in Alexandria was preceded by the sale of a building; only one required special approval through a public hearing

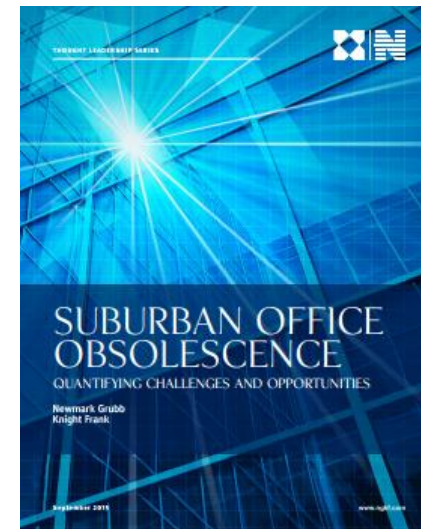
Market and Economic Forces

- Office rental rates, vacancy rates, and values
- Residential rental rates, vacancy rates, and values
- Credit Markets
- Tenant preferences

Office Obsolescence

- Obsolescence is the decline in the economic value and desirability of an office building
- Net operating income is not sufficient to offset costs for building operations and land value
- Factors contributing to obsolescence include a building's age, size, location, and access to transit and amenities
- Changing tenant use and preferences, technology, and economic considerations also play a role

14%-22%
of the U.S.
suburban
office
inventory **is**
obsolete





Highly Desirable Factors for Office Tenants

Desirable	Metrics
Location & Access <ul style="list-style-type: none">• Distance to Metrorail Station• Transit availability• Highway access• Parking Ratio	<ul style="list-style-type: none">• ¼ mile walking distance to Metrorail station• Transit Score• 1 mile to highway access• 1.5-4.0/1,000 SF
Amenity Base <ul style="list-style-type: none">• In-building amenities• Walkable dining, retail and public spaces	<ul style="list-style-type: none">• Fitness center, conference/shared space, and/or food service (2 or more)• Walk score rating, mixed land uses
Building Age <ul style="list-style-type: none">• Year built or renovated	<ul style="list-style-type: none">• Constructed or renovated within the last 15 years
Building Characteristics <ul style="list-style-type: none">• Elements of design and construction	<ul style="list-style-type: none">• 8'6"+ ceiling heights• < 20,000 SF floor plates• LEED certified (Silver or above)• Modern buildings systems• Natural light



Unique Property Circumstances

- Pending capital events (lease expirations, renovation/replacement, loan maturity, etc.)
- Layout and Design
- Location
- Vacancy
- Nature of ownership

Regulatory Environment

- Conversions can take place in a variety of ways depending on the zoning and/or existing approvals
- Current zoning regulations provide few barriers to conversion
 - Many zones allow office and residential as “Permitted Uses” versus requiring special approval or review
 - Some zones allow a higher Floor Area Ratio (FAR) maximum for residential than office (no known conversions have taken advantage of this)
 - Many zones permit rooftop areas or other amenities to function as open space thus diminishing the ground floor open space requirements of residential uses
- No discernable zoning pattern among known conversions, except all were uses permitted by right

Findings Overview

- Conversions to date have resulted in:
 - Net positive impact to General Fund
 - Significant private investment in Alexandria
 - Change of obsolete office buildings to a higher and better use
 - Minimal impact on the neighborhood mix of uses
- Market/economic forces and unique circumstances are driving decisions to convert commercial to residential; current City zoning regulations offer limited barriers to influence conversion decisions
- Difficult to predict if and when conversions will occur; commercial leasing trends may result in more frequent conversions of obsolete office
- Options are available to help inform and influence conversion decisions



Conversion Impact on Tax Base

- Conversions to date have adjusted the commercial/residential tax ratio but will likely generate higher revenue returns to the city
 - 4 major office properties converted (or are under construction) to residential
 - Totals 420,000 SF or 2% of the City's 20 million SF of office stock
 - Conversions may increase levels of required City services, however, analysis indicates conversions increased building value eclipses cost of services

Address	Total SF	Location	\$ Value Before*	\$ Value Today*
601 N. Fairfax	129,000	Old Town North	\$21M	\$126M
515 N. Washington	26,000	Old Town North	\$5.2M	\$9.6M
Brightleaf & Cooper	32,000	Old Town North	Tax Exempt	\$TBD
4501 Ford Avenue	235,000	Park Center	\$20M	\$55M

*Assessed value



Conversions Positively Impact City Competitiveness

- Encourages private investment in real estate that has likely not seen investment in recent years
- Takes excess office space off market which may drive new development in commercial corridors
- High quality and unique residential properties bring human capital into Alexandria
- Prevents obsolete office buildings from potential years of high vacancy, special servicing, or foreclosure



Policy Recommendations

- Consider conversion projects on a case by case basis for properties >3,000 SF
 - Calculate fiscal impact to City
 - Evaluate project competitiveness and circumstances
 - Consider impacts to mix of uses in neighborhood and public need
- Public intervention to enhance competitiveness
 - RE Tax Credits for Capital Investments in Legacy Properties (25+ years old)
 - Consider RE Tax Abatements for new office development or uses the City deems important to promote/maintain land use mix and other priorities
- Option not recommended:
 - Prevent office to residential conversions by eliminating by-right residential uses in commercial zones the City wants to protect (downzoning)



Next Steps

- Consideration of policy recommendations- May 23rd Legislative Meeting