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To revitalize downtowns, cities need to stop making this big mistake

Editorial Board

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(Rob Dobi for The Washington Post)

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Cities across the nation face a dilemma: Downtown office buildings are empty as workers prefer to stay home. Nearly all local leaders agree part of the solution is an office-to-apartment conversion boom. Cities have started rolling out tax incentives to encourage developers to begin this transformation. This strategy is straight out of the playbook that revived center city Philadelphia and Lower Manhattan in the past quarter century. But there's a problem: City leaders aren't doing enough.

No mayor or city council member wants to hand a lavish deal to real estate developers. But the urgency and scale of the downtown crisis in many major metro areas mean local leaders need to give away a bit more than they probably would prefer. Consider the nation's capital city. Downtown D.C. is more than 90 percent commercial buildings. The vibrancy and workers are largely gone.

Crime and grime are increasing, while property tax revenue is quickly decreasing as building values plummet. Mayor Muriel E. Bowser (D) has put out an ambitious "Comeback Plan" that calls for 15,000 new residents living downtown by 2028. To make that a reality, the city needs developers to convert roughly 7 million square feet of office space to apartments and condos. Her team estimates about 1 million square feet is on track for conversion so far. There's a long way to go. The situation is similar in Chicago, San Francisco, New York and Atlanta, among other cities.

Interest rates aren't helping. Building makeovers that looked attractive a year ago, when the typical mortgage rate was around 3.75 percent, look far less appealing with rates above 6.5 percent and likely to stay there for a while. The easy-to-convert buildings — ones that are vacant and on lots with ample light and alleys — are largely scooped up already. Buildings such as the former Peace Corps headquarters in D.C. and 25 Water Street in New York City are being transformed into residential units. What remains are difficult properties that need significant reworking or tearing down. The costs add up.

D.C. recently announced details of the Housing in Downtown Tax Abatement program. In exchange for 20 years of reduced taxes, builders are required to make 15 percent of units affordable housing and utilize local contractors and workers for at least 35 percent of the construction. But many developers say the math doesn't work. They can't meet all of these priorities — costly conversions, affordable housing and certain contractor requirements — and still make a profit.

A harsh conversation about trade-offs is beginning to happen in many city halls. How much are mayors and city council members willing to cut the "strings attached" on tax incentives to rapidly transform comatose downtowns?

We urge city leaders in D.C. and around the country to put revitalizing downtowns first. That doesn't mean giving in to every developer's whim, but it does mean being realistic. The longer cities wait to get conversions underway, the more tax values drop and crime goes up, and the more people see no value in living in the heart of the city — or even visiting.

One way or another, cities are going to pay. D.C. is already staring at $464 million in lower revenue for 2024 to 2026 mainly due to lower commercial property taxes downtown. San Francisco is facing a $728 million shortfall over the next two fiscal years for similar reasons. Buildings constructed in the 1980s, 1990s and early 2000s are quickly becoming distressed. It's far better to invest now than to spend years overseeing stagnation and decline. As D.C.'s Chief Financial Officer Glen Lee warned, this is "a serious long-term risk to the District's economy and its tax base."

The sooner these buildings can convert to residential, the sooner the city can generate some tax revenue again from an area that once brought in hefty commercial property revenue. Cities will have to rely much more on residential income tax revenue from downtowns.

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Several developers shared with us their cost estimates on converting various buildings. While there's always some grumbling, many developers conceded they can make the affordable housing requirements work. Some developers would prefer closer to 8 percent affordable units, while the city wants 15 percent, but there's room for cooperation to ensure low- and moderate-income residents have opportunities to live in this new downtown.

More burdensome are requirements regarding hiring local contractors and workers. It's a worthy idea to want D.C. residents, especially workers of color, to benefit from a building boom. But there could be other, more cost-effective ways to achieve that goal, such as apprenticeships and job training. City leaders should also look into lowering transaction taxes and expediting the change from commercial to residential property tax collection on buildings slated for conversion.

State governments and the Biden administration have a role to play, too. Many states, including Ohio and Michigan, have beefed up tax abatement programs for historic buildings to encourage builders to convert older buildings. Thirty-seven states now have a program like this, according to the National Trust for Historic Preservation. Properties built before air-conditioning existed are often easier to transform because they have windows that open. Similarly, the Biden administration could help D.C. and other cities by assessing what the federal government's leasing and property needs are and letting go of properties that are unlikely to be used, so that mostly empty buildings can be transformed, rather than contributing to the downtown's desolate atmosphere. The federal government owns or leases a quarter of downtown office space in D.C.

Downtowns are at a crossroads. Seeing cranes and scaffolding go up soon is essential to success. City leaders have to start thinking that way.

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