

Government of the District of Columbia  
Office of the Chief Financial Officer



**Fitzroy Lee**  
Interim Chief Financial Officer

**TAX ABATEMENT FINANCIAL ANALYSIS**

**TO:** **The Honorable Muriel Bowser**  
**Mayor, District of Columbia**

**The Honorable Phil Mendelson**  
**Chairman, Council of the District of Columbia**

**FROM:** **Fitzroy Lee**  
**Interim Chief Financial Officer**

**DATE:** **June 24, 2021**

**SUBJECT:** **Redevelopment of the Center Leg Freeway (Interstate 395)**  
**Amendment Act of 2021**

**REFERENCE:** **Fiscal Year 2022 Budget Support Act of 2021, Subtitle (II) (M), Bill 24-285**

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**Findings**

The proposed subtitle would amend the existing legislation authorizing payments in lieu of taxes (“PILOT”)<sup>1</sup> for the Capitol Crossing project (“Project”) with respect to three yet to be constructed buildings. This proposal would provide an additional 10-year PILOT period beginning with fiscal year 2028 (which begins October 1, 2027) through fiscal year 2037 and would reduce the PILOT payment to 25 percent of real property taxes otherwise due. The Office of the Chief Financial Officer (OCFO) finds that this additional PILOT period and real property tax abatement is financially necessary. The continued development of the Project is unlikely to occur without the reduced PILOT payments and abatement provided by the proposed subtitle.

Please refer to the separate Fiscal Impact Statement for the effect of the proposed subtitle on the District’s financial plan.

**Background**

Capitol Crossing is a three-block, mixed-use project built on a deck constructed over Interstate 395. It broke ground in May 2015. Two office buildings within the Project’s footprint have been completed, 200 Massachusetts Avenue NW and 250 Massachusetts Avenue NW (“CC I” and “CC II”, respectively), and are taxable. Three buildings remain to be developed. The remaining development includes two buildings on the Center Block site and one building on the South Block site. The Center Block site has

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<sup>1</sup>Redevelopment of the Center Leg Freeway (Interstate 395) Act of 2010, effective October 26, 2010 (D.C. Law 18-257; D.C. Official Code § 47-4640).

a Stage 1 Planned Unit Development (PUD) approval for a 180,000 square foot multifamily residential building with 50 affordable housing units (“CC III”), to be developed on Lot 862 in Square 566, and a 297,000 square foot office building or hotel (“CC IV”), to be developed on Lots, 50, 862, 864 and 7001 in Square 566.<sup>2</sup> The South Block site, comprised of Lots 865, 44 and 7001 in Square 568, has Stage 1 and 2 PUD approvals for a 650,000 square foot office building (“CC V”).<sup>3</sup>

To catalyze the Project, in 2010, the DC Council enacted the Redevelopment of the Center Leg Freeway (Interstate 395) Act of 2010 (“Act”).<sup>4</sup> The Act authorized PILOT payments to financially assist the Project by reducing its real property tax liability during its development phase. The Project’s developer, Property Group Partners (PGP) and the Office of the Deputy Mayor for Planning and Economic Development (DMPED) have advised the OCFO that the period during which PILOT payments under the existing law are made (“PILOT Period”) will end in fiscal year 2023.<sup>5</sup> Thereafter, the full real property tax will be imposed on the lots.

PGP is requesting an additional PILOT Period to improve the Project’s continued financial viability in light of unanticipated costs. According to PGP, the District Department of Transportation (“DDOT”) and the neighboring properties have imposed additional costs on the Project resulting in the cost of the sitework increasing by more than \$100 million since 2012. These costs included scope changes affecting spaces adjoining the tunnel, deck, and bridges, and general material and labor cost escalation.

This subtitle to the Fiscal Year 2022 Budget Support Act of 2021, as introduced, seeks to amend the Act to provide an additional PILOT Period of 10 years, beginning on October 1, 2027 (fiscal year 2028), and will set annual PILOT payments at 25 percent of the real property taxes for CC III, CC IV, and CC V.

## **Financial Analysis**

The Exemptions and Abatements Information Requirements Act of 2011 requires the analysis provided by the OCFO to contain certain information. The required information is included below.

### **(A) Terms of the Additional PILOT Period**

The proposed legislative changes provide for a ten-year PILOT period in addition to the period provided under the existing PILOT Act as it pertains to the CC III, CC IV, and CC V properties. Starting in fiscal year 2028, the proposal provides for PILOT payments at 25 percent of the real property taxes otherwise imposed on these properties.<sup>6</sup> Eligibility for payment of the reduced PILOT amount is contingent upon satisfaction of several conditions:

- Receipt of a final certificate of occupancy for CC III, the residential building, before September 30, 2027;
- Completion of all remaining development, including CC IV and CC V, by September 30, 2033;

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<sup>2</sup> The developer, PGP, intends to develop CC IV as a hotel.

<sup>3</sup> PGP provided the squares and lots (SSLs) in this paragraph. They differ from the squares and lots identified in the subtitle as introduced. Differences may be due to subdivisions and retirement of certain lots.

<sup>4</sup> Effective October 26, 2010 (D.C. Law 18-257; D.C. Official Code § 47-4640).

<sup>5</sup> The PILOT Period is defined in D.C. Official Code § 47-4640(a)(5).

<sup>6</sup> Pursuant to D.C. Official Code § 47-4640(b)(1)(D), buildings that are completed are no longer subject to PILOT and are taxed at their assessed value.

- By October 1, 2022, amendment of agreements between PGP and the District governing the transfer of the PILOT area to PGP to reflect the terms of the amended legislation, including the construction completion conditions and any economic inclusion requirements as required by the Mayor;<sup>7</sup>
- PGP’s compliance with the amended agreement terms; and
- A cap of \$100 million on the real property taxes that may be abated.

(B) Value of the Additional PILOT Period

As shown in table, the additional PILOT period is valued at \$0 through the financial plan period and totals approximately \$100 million over the proposed 10-year additional PILOT period.

**Value of the Additional PILOT Period:**

|                             | FY 2022 | FY 2023 | FY 2024 | FY 2025 | FY2022-<br>FY2025 | FY2026-<br>FY2037 | Total<br>Value |
|-----------------------------|---------|---------|---------|---------|-------------------|-------------------|----------------|
| Real Property Tax Abatement | \$0     | \$0     | \$0     | \$0     | \$0               | \$100,000,000     | \$100,000,000  |

(C) Purpose of the Additional PILOT Period

According to PGP, the proposed additional PILOT period is intended to allow the remaining portion of the Project to compensate PGP for approximately \$100 million in cost overruns incurred to date, thereby allowing the entire Project to achieve better financial performance.

(D) Summary of the Proposed Community Benefits

PGP provided a summary of community benefits to be offered in connection with developing the three buildings. In addition, DMPED identified additional community benefits that will be required in connection with amending the Project’s transactional documents to allow for the additional PILOT period and abatement.

(E) Financial Analysis and Advisory Opinion

The OCFO’s Office of Finance and Treasury finds that the real property tax abatement connected to the proposed additional PILOT period improves the financial performance of the Project overall by reducing the Project’s operating expenses. Based on the OCFO’s analysis of the information provided by PGP, without the proposed abatement of real property taxes, the return on investment for the remaining portion of the Project is unlikely to be sufficient to attract the investment needed, given current market conditions and current construction cost levels. The OCFO’s analysis also indicates that the proposed abatement does not over-subsidize the Project. Return on investment for each component of the Project improves with the abatement, and thereby improve prospects for investment in the Project. Only CC V has projected cash flows, with the abatement yield of the forecasted return meeting the 7 percent unleveraged internal rate of return, or IRR, that PGP is seeking. Although the OCFO’s analysis shows projected returns on CC III and CC IV are below that

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<sup>7</sup> DMPED intends to strengthen the completion requirements in the transactional agreements, requiring completion of the hotel (CC IV) by September 30, 2030.

threshold, PGP would receive the abatement of real property taxes only if the Project were completed within the required timeline, providing incentive for PGP to complete the Project in full in order to retain the abatement on any completed portions of the Project subject to the additional PILOT period.

Therefore, the OCFO finds that the abatement of real property taxes within the proposed additional PILOT period is financially necessary for the continued development of the Project.

## **Attachment A**

### **Summary of Community Benefits Provided by Applicant**

The PILOT Extension will improve the financial feasibility of developing the buildings on the CC III, CC IV, and CC V sites. Each site will have its own set of community benefits, which are listed below by site.

#### **CC III Site (200 G Street)**

- Housing – approximately 166 for-rent residential units, with 50 of the units rented at 80% of the area median income level
- Environmental - LEED Gold, energy efficient building with photovoltaic panels, site-wide storm water retention and management
- Employment - hundreds of construction jobs using District labor per the terms of Capitol Crossing’s First Source and CBE agreements
- Ground Floor Retail Space along G Street
- Public space enhancements along G and 2nd Street

#### **CC IV Site (201 F Street)**

- Increased Tax Base – approximately 222-key hotel
- Environmental - LEED Platinum, energy-efficient building with site-wide storm water retention and management
- Employment – hundreds of construction jobs using District labor per the terms of Capitol Crossing’s First Source and CBE agreements, plus permanent hospitality jobs
- Ground floor retail space along F Street
- Public space enhancements along F and 2nd Street
- Restoration of the F Street view corridor from the Treasury Building to Union Station

#### **CC V Site (200 F Street)**

- Increased Tax Base - 670,000-square foot office building
- Environmental - LEED Platinum, energy-efficient building with site-wide storm water retention and management
- Employment – hundreds of construction jobs per the terms of Capitol Crossing’s First Source and CBE agreements
- Ground floor retail space along E, F, and 2nd Streets
- Public space enhancements along E, F, and 2nd Streets
- Restoration of the F Street view corridor from the Treasury Building to Union Station

PGP has already provided several community benefits that are due to the future development of the Capitol Crossing III, IV and V sites. These in-place benefits include the following items:

- Restoration of the L’Enfant Plan between Massachusetts Avenue and E Street from 2nd to 3rd Street Northwest
- Construction of the Platform/Tunnel over I-395
- Construction of new, less invasive on and off ramps to I-395
- Re-Opening of F and G Streets to pedestrian and vehicular traffic
- Upgrades to the 3rd Street Tunnel south of E Street and north of Massachusetts Avenue Northwest

- Modernization of utilities, roads, and District-owned infrastructure around the CC III, CC IV, and CC V sites that service the Georgetown Law Center, the Communications Workers of America building (501 3rd Street), and the General Services building (633 3rd Street).
- Relocation of the Adas Israel Synagogue from District owned land along 3<sup>rd</sup> Street to the southeast corner of 3rd and F Street.
- Allocation of a portion of the CC V site to the Capital Jewish Museum for the relocation of the Adas Israel Synagogue and the construction of a new museum
- Relocation of the rectory and Casa Italiana Language School from an obsolete building that was located within F Street to a new building, which was built as part of the project to the east of the existing church and fellowship hall
- Allocation of a portion of the CC IV site to the Archdiocese of Washington for the construction of the new Holy Rosary Church rectory and language school
- Urban Design, Landscaping and Creation of Open Spaces
- Transportation Management Measures for the Capitol Crossing sites, the Holy Rosary Church, and Capital Jewish Museum
- Allocation of fifty parking spots to the Holy Rosary Church for its use during services to alleviate 3rd Street congestion during services
- Construction of a linear park for the Communications Workers of America building
- Reconfiguration of the electrical service and loading dock for the Communications Workers of America building so that these services are no longer on District-owned land.

### **Summary of Additional Benefits Required by DMPED**

DMPED has provided the following community benefits that will be required of PGP as a condition of receiving the amendment to the transactional documents associated with the PILOT to reflect the PILOT extension and abatement.

- PGP shall enter into the DC Community Anchor Partnership MOU with CNHED prior to effective date of the PILOT amendment legislation. This MOU shall be in place during the term of the PILOT amendment. PGP shall use best efforts to achieve the goals of the MOU during the term of the PILOT amendment.
- A minimum of ten percent (10%) of all Certified Business Enterprise (CBE) dollars shall be earned by entities that are also certified as a Disadvantaged Business Enterprise (DBE).
- A minimum of four thousand (4,000) square feet of retail square footage in buildings subject to the PILOT amendment shall be reserved for entities that are certified as DBEs. PGP shall also provide at minimum a ten percent (10%) benefit in tenant improvement allowance as part of these tenancies.