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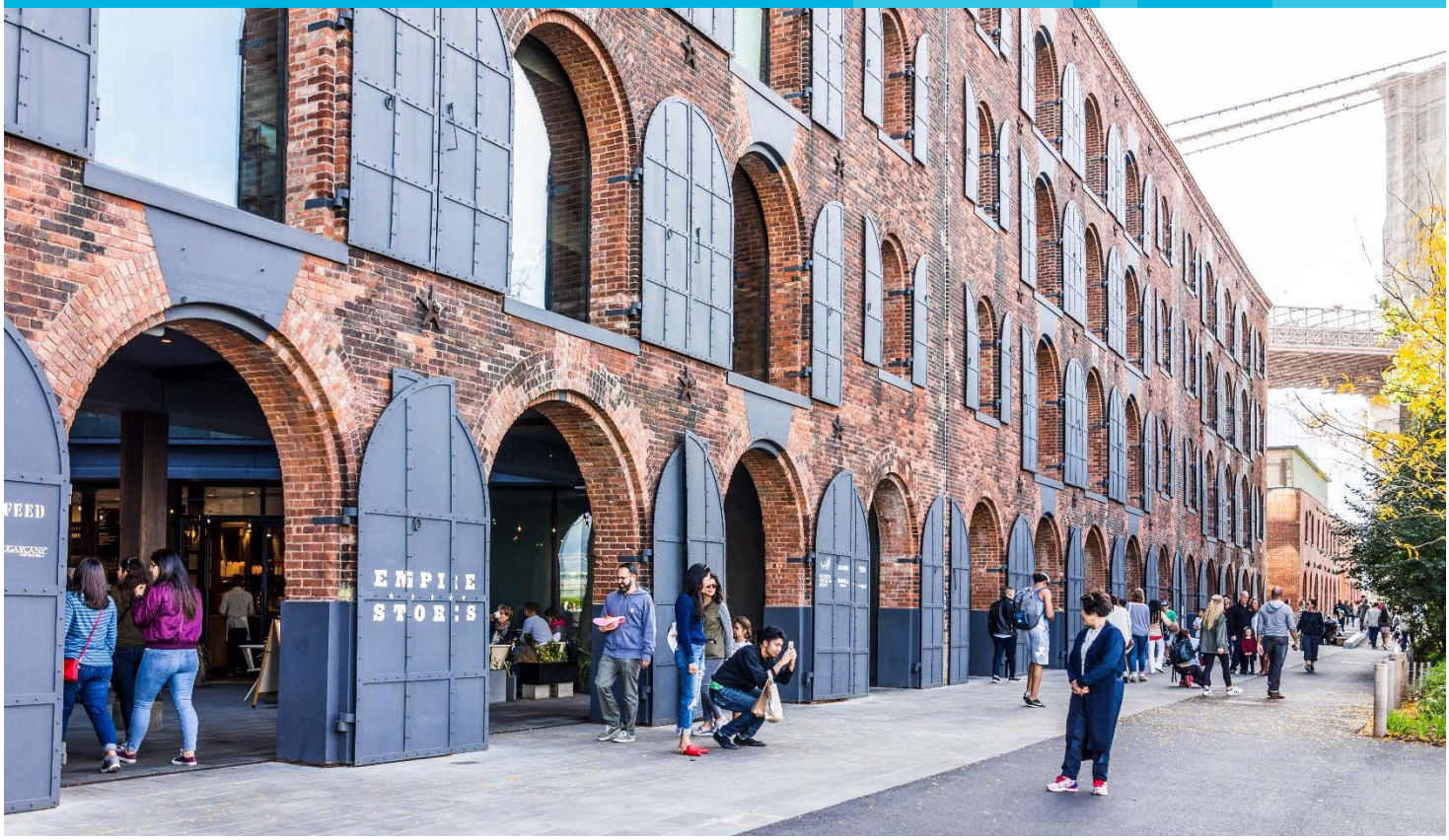
An Avison Young Topical Report

APRIL 2018



Dumbo, Brooklyn *Source: Shutterstock.com*

Adaptive Reuse Projects – What's Old is New Again

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Executive summary

Adaptive reuse projects take many forms; however, in its simplest definition, adaptive reuse is the redevelopment of a functionally, or financially, obsolete real estate property into a newer and better use. Every city in the U.S., Canada and many other parts of the world has its own examples of successful transformations of older, obsolete structures into creative, viable alternative-use projects. With this increasing trend, especially in established areas in the U.S. where vacant and developable land is scarce, many cities and communities welcome these transformations as they usually spread to other buildings and public spaces, often revitalizing an entire area.

Never before has adaptive reuse been so prevalent in both urban and suburban areas. In many neighborhoods, service stations are being transformed into fast-food establishments, and vacated elementary schools into condos or hotels. As land becomes scarce and as towns and cities age, creative developers are stepping in to meet growing demand and are repurposing older, outmoded buildings into much needed residential, office and retail spaces.

Rather than tearing down and starting from scratch, repurposing and reusing existing buildings is often the best option. There are many issues to consider when planning and working on an adaptive reuse project. These issues can include zoning and financial considerations, physical attributes and structural impediments, layout and floor-plan considerations, among other factors.

Red Hook, Brooklyn *Source: Shutterstock.com*

Brooklyn Bridge *Source: Shutterstock.com*

Perhaps the best example of this trend in the New York area is the borough-wide transformation of Brooklyn, which is still going strong as of this report. On Long Island, the growing demand for live-work-play lifestyles has triggered the transformation of an area long utilized for industrial, manufacturing and distribution into retail and multi-residential properties.

Today, the integration of office space, retail services and vibrant residential communities is sought-after by communities, residents and corporations alike.

To date, the projects that have been completed on Long Island are almost too numerous to count. These projects have area-wide benefits to employees, residents and the entire community. These mixed-use projects provide a live-work-play environment, which offers not only convenience and amenities, but an environmentally friendly footprint on the community.

According to the *Commercial Observer*, in the Long Island neighborhood of Bushwick, industrial buildings are experiencing "a second life as bars, theaters, music venues, specialty gyms and just about anything boutique or hipster-approved."[1] This trend has enticed investors and developers to capitalize on the new and increased demand.

Benefits of adaptive reuse projects

Adaptive reuse projects offer many advantages to communities, residents, occupants and developers. Utilizing existing structures with character and historical significance often paves the way for an area-wide renaissance. Developers are able to recycle, or breathe new life into, an otherwise old and obsolete structure. Although projects sometimes require creativity, imagination and patience, the many benefits include:

- Revitalization of blighted areas;
- Lower impact on the environment due to public transportation and shorter commutes, which can include biking and walking to work;
- Preservation of a city's identity and cultural and historical significance;
- Combined acquisition and redevelopment costs typically fall below replacement costs in certain markets offering financial incentives to complete these projects;
- Ability to capitalize on locations that cannot be redeveloped, such as waterfront or parkside spaces;
- Incentives often offered by local and state governments make projects more financially viable;
- Ability to achieve LEED status through construction with green materials and techniques; easier commuting patterns.

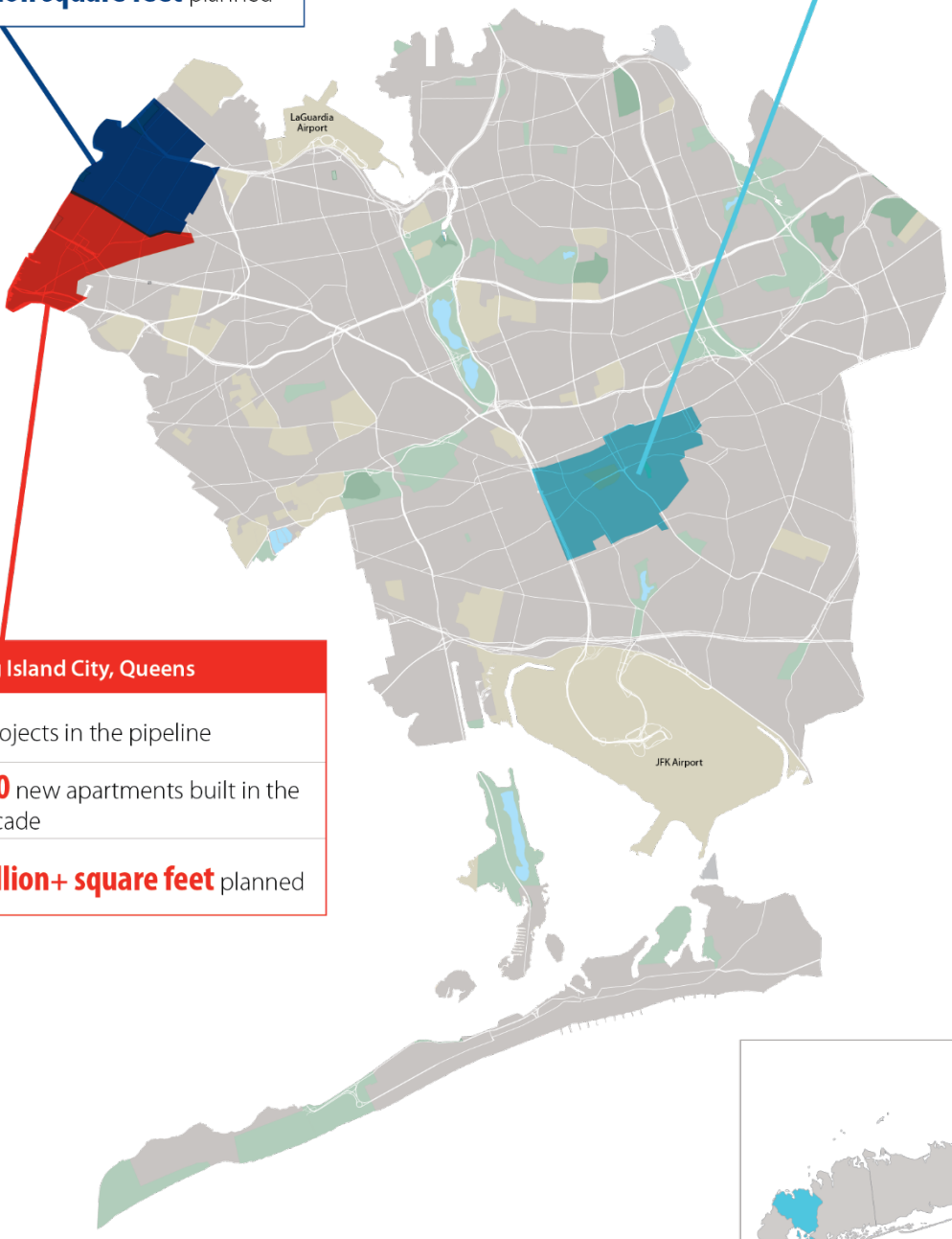
Adaptive reuse takes over Queens[2]

Astoria, Queens

- **$1.5 billion** Hallets Point complex
- **4,000** residential units in the pipeline
- **3.5 million square feet** planned

Jamaica, Queens

- **160** projects in the pipeline
- **4,536** residential units in the pipeline
- **6.48 million square feet** planned



Long Island City, Queens

- **200** projects in the pipeline
- **11,000** new apartments built in the last decade
- **23 million+ square feet** planned

Source: The Real Deal

History of adaptive reuse

What is today referred to as adaptive reuse is not a new concept. In fact, some of the most iconic buildings in the world were born from it. One great example is the Louvre in Paris, France. Originally a 12th-century castle and residence for French royalty, the Louvre was converted to a museum in the late 1700s and now ranks among the world's largest.

Another U.S. region that has welcomed the repurposing of older buildings is New England. Throughout New England, many old mill buildings have become highly sought-after for redevelopment. These historical buildings have a rich past that involved milling, manufacturing and other industrial uses, and typically have signature brick and arched-window architecture.

One great example is a complex of historic mill buildings that were completely renovated and redeveloped for office and retail uses by Arnold Marcus, President and CEO of The Marcus Organization, with whom Avison Young spoke in late 2017.

The complex was redeveloped to attract companies seeking new office headquarters, including support-retail amenities and services, to complement a multi-purpose redevelopment program on the Charles River as part of a public/private partnership with the City of Cambridge, Massachusetts.

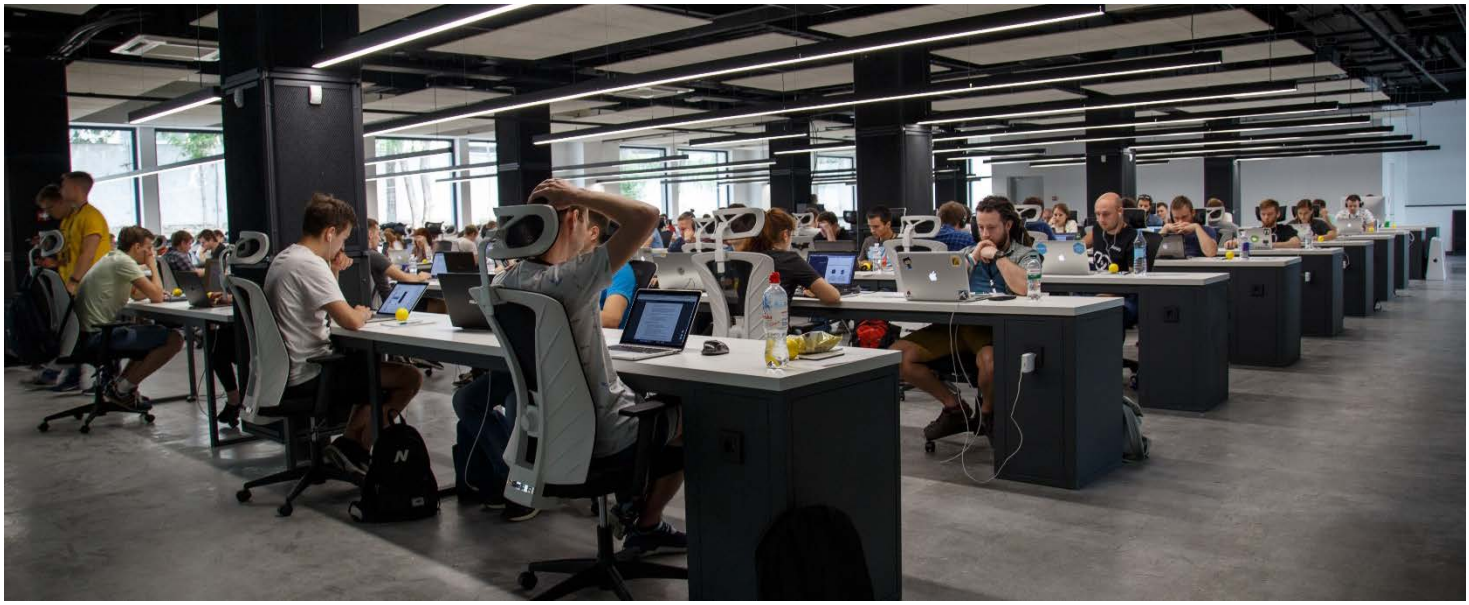
"Prior to completion, we leased 240,000 square feet (sf) to software and consulting companies that sought proximity to renowned institutes of higher education, access to public transportation, first-class amenities and a unique identity," said Marcus.

"Although they had many choices, which included being in the glass towers in the downtown Boston area, being a part of something truly unique with good amenities is what they ultimately chose."

The development, a three-building, 460,000-sf complex in Cambridge, offered the corporation and its employees a downtown feel along with many nearby amenities and quick train access to downtown Boston. This building met many of the operational needs of the tenants and brought the rich architectural history of other parts of New England to the Boston area, where employees and clients live.

"While the project presented its challenges, the conversion of this three-building complex exceeded the community demands and corporate expectations of the clients it served," noted Marcus.

The Louvre; Paris, France *Source: Shutterstock.com*



Warehouse Conversion *Source: Unsplash.com*

Another interesting case study is an adaptive reuse project in the historic Washington, DC Navy Yard district undertaken by real estate investor Forest City Realty Trust. This once historic neighborhood had been reduced to an expanse of dilapidated industrial facilities, but this eyesore was transformed after Forest City won the bid to repurpose the site for mixed-use development in the early 2000s. The developers embraced the challenge of retaining the historic architecture and landmarks of The Yards, especially since the site was on the National Register of Historic Places. As a result, today, this award-winning waterfront development is the recreational, residential and retail hub for the expansive Capitol Riverfront community.

Considerations

Mechanical and architectural obsolescence is inherent in many older buildings. Sometimes, an area changes or matures, and the former use of the building is no longer viable. The obvious first consideration for any adaptive reuse project is financial. The project must be financially viable for the intended end use. Many additional considerations affect the decision-making process when investors and developers are evaluating whether to proceed with a project.

Feasibility study

This is one of the first steps in the decision-making process. A developer/investor must determine whether the finished use can be successful and either lease up (in the case of a rental property) or sell out (in the case of an end sale). The project's developer needs to establish an accurate projection of current and future market demand. In order to do that, the following questions must be considered:

- Where will the development funds come from?
- Will equity partners be needed?
- What are the vacancy rates?
- What are rents for the asset class?
- What are similar buildings or units selling for?
- What is the competition (both existing and planned)?
- How long will it take to complete the project?
- What is the state of the permanent financing market?

A developer has an obligation to assess the situation honestly; therefore, it is critically important to provide conservative answers to all of the aforementioned questions. Obviously, it is better to be pleasantly surprised by lower costs rather than be in a position where more money is needed because cost projections were underestimated.

Zoning

Will it be possible to obtain approvals for the new intended use? Despite the logic behind repurposing an older building (which may even be a blight in the community) to something new and useful, some people and organizations will oppose the proposed project for a variety of reasons. The project must be feasible based on the current or anticipated changes to future zoning codes. In most cases, a rezone or, at the very least, a zoning variance will be required to obtain approvals for the intended use. Depending on the location, this can sometimes be a lengthy process and, in some cases, take up to two years and beyond. It is necessary to consult with knowledgeable real estate zoning attorneys to determine whether the proposed use has a good chance of being approved over time. Therefore, it is important that consultation be the first consideration in this part of the process. It is important to meet with planning officials, lawyers and civic groups to understand what is necessary and what is possible. Without completing this step, a lot of time and money can be wasted.

Physical attributes

Determining whether a building can be adapted to the new use is another important consideration. This is where a good architect comes in handy – someone who can evaluate the structure, focusing on floorplates, entrances, placement of elevators and mechanical equipment, etc., to determine whether the new use is something that will work. For example, converting a warehouse to office use is much easier than converting it to residential. Considerations such as depth from the window line and ceiling heights have to be considered.

Environmental impact studies and traffic studies

Most municipalities will require these studies to be done if the project includes a change of use. The results can be helpful in addressing community-group concerns.

Site and environmental remediation

Many older buildings have environmental issues to address due to their age. For example, prior to 1979, asbestos was permitted, and widely used, to fireproof buildings. During the renovation, all of the environmental issues should be addressed, and sufficient funds need to be allocated in projections.

Site work

Upgrades and site engineering to the existing property are sometimes required to accommodate run-off and sewer requirements.

Historical significance

Some older buildings are rich in history, and the preservation of design features often enhances a project's appeal. When a building is given a heritage designation, other issues come into play – and may increase costs.

Structural issues

An engineer should be brought on early in the process to assess structural issues, not only for the existing building, but also for any planned changes. Items like floor-load capacity, structural supports and areas for new elevators all have to be considered early in the project.

Timing

The period from contract signing to closing on a building to a finished product affects the financial feasibility of a project. Zoning entitlements can sometimes take more than a year, depending on the municipality. This factor adds to a project's carrying costs.

Hard costs

Considering the costs associated with new construction, the purchase and redevelopment of an existing building may make more financial sense than constructing a new building. In some markets, entitlement, design and development costs are almost always below replacement costs. Construction costs are sometimes the hardest aspect of the development to anticipate. There is inherent value in the existing foundations, structure, power and sanitation lines, which can be reused with modifications. However, the uncertainty of not knowing what is behind the walls can escalate projected costs. A good architect and engineer are vital parts of the process to help make good financial assumptions and to keep costs in line.


Converted Warehouse

Source: Unsplash.com

Mechanical systems

In most adaptive reuse projects, the existing mechanical systems (electric, heating ventilation, air-conditioning plumbing, etc.) will likely be upgraded to serve the new intended use.

Technology

Today's technology is moving at a fast pace. New projects will need wireless connectivity, and many of the new LEED projects will advance things a step further with computerized energy-management systems.

Incentives

Many municipalities will offer incentives, especially in areas that are undergoing area-wide transformation. While slightly more complicated, incentives such as tax credits and lower entitlements sometimes make a project viable.

Union vs. non-union labor

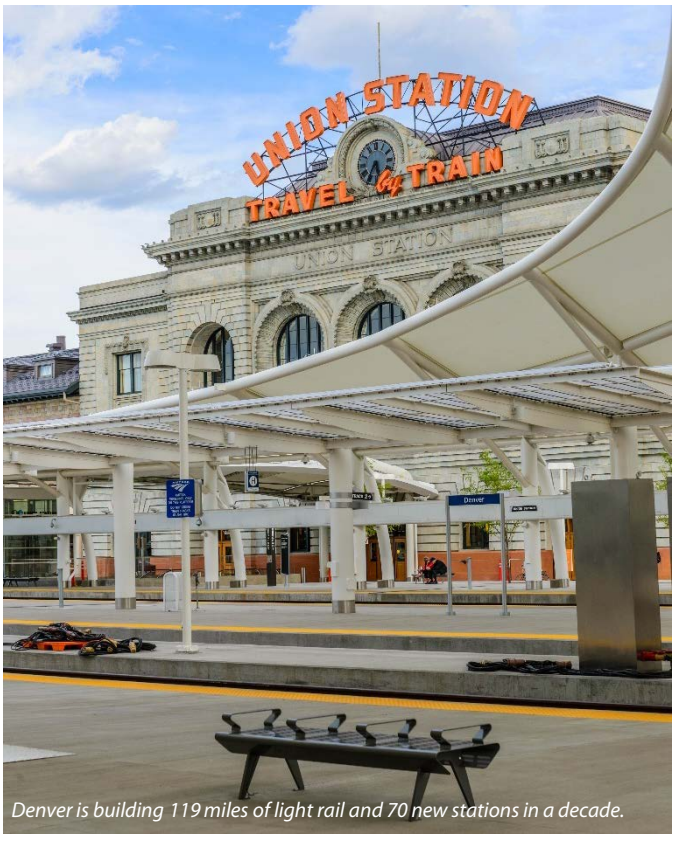
While costs can vary depending on the location and scope, it is estimated that building with union labor can have a 20%-30% effect on costs, but using union labor is sometimes necessary due to local codes and/or practices.

Parking

Parking is a more important factor in suburban areas, but even projects in cities often have some form of parking, especially residential projects.

Transit lines and TOD

Many of the adaptive reuse projects in urban areas have developed around transit lines – i.e., trains, buses, subways, etc. Based on the increasing desire of today's workforce, a finished project's proximity to transit is often a major selling point when developers are trying to attract tenants and buyers.



Denver is building 119 miles of light rail and 70 new stations in a decade.

Source: Shutterstock.com

Conclusion

Although there are numerous considerations to address, the concept of adaptive reuse has significant positive benefits for developers, investors, the community and the environment. Adaptive reuse prolongs and improves the usefulness of a building in its surroundings. Renovation of existing structures should always be the first consideration – the end result could yield a cohesive blend of old and new. As long as sound underwriting and proper planning are taken seriously, the outcome of a renovation and adaptive reuse project is often better than a new development.

As communities mature and as technology continues to advance, there will always be a need to consider the reutilization of properties. Much like spring, which is a renewing, rejuvenating force in nature, adaptive reuse of older projects can revitalize a building, a community and even a city. What was once obsolete will become new and relevant again, answering the needs of today's businesses and people alike.

End Notes

1. Guerre, Liam La. "Bushwick's Warehouse Conversions Are Hitting Never-Before-Seen Heights." *Commercial Observer*, February 11, 2016.

2. Bockmann, Rich. "A Real Estate Investors Guide to NYC's Most Expansive and Diverse Borough." *The Real Deal*, February 1, 2017.

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Platinum member

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