

Sales and Use Tax Deferral for Office to Residential Conversions

Office of Planning and Community Development (OPCD)
Land Use Committee Briefing
December 4, 2024

Overview of the Proposal

- Incentivize the conversion of office space to housing and affordable housing
- A component of Mayor Harrell's Downtown Activation Plan
- Establish a deferral of sales & use taxes on the construction costs of conversions to housing



Background

Washington State legislature passed ESSB 6175 during the 2023/24 session

- Authorizes deferral of construction sales and use taxes on conversions of underutilized commercial space to housing.
 - Requires 10% of the housing units to be affordable at the 80% AMI level.
 - If affordability is maintained for 10 years, the sales and use taxes are permanently waived.
 - Cities must take local action to implement.
- ➔
- Step 1: Resolution stating intent to adopt. (Today)
 - Step 2: Public hearing and Ordinance adopting regulations into the City's code. (Q1 2025)
 - Seattle would be the second city to implement, after Spokane.



Policy Goals of Implementing ESSB 6175 in Seattle

- **Addresses Affordable Housing Shortage**

- Increases supply of housing and affordable housing
- OPCD estimates that 1,000 – 2,000 housing units would be produced in a 7-year timeframe (100 - 200 affordable units). If combined with the popular Multi-family Tax Exemption (requiring 20% affordability), the policy would encourage 3,000 – 6,000 units (300 – 600 affordable units)*

- **Supports Downtown Recovery**

- Improves the balance of housing and commercial spaces to solidify downtown as a 24-hour neighborhood
- Complements Mayor Harrell's Downtown Activation Plan and other recent legislation to spur investment and livability downtown
- Seattle is among the US cities with the highest potential to benefit from office to residential conversion based on office distress and housing supply needs

- **Promotes Environmental Sustainability**

- Reduces vehicle miles traveled, encourages transit use, and promotes energy efficiency

* MFTE affordable housing units must be in addition to the ESSB 6175 affordable units.



Affordable Housing Requirement

- **Requirement**

- 10% of the housing units must be rent- and income-restricted to serve householders at 80% of Area Median Income (AMI).
- Market rate rent for a 2-bedroom apartment in Downtown ranges from \$3,357- \$4,004 whereas an equivalent affordable unit under this program would be rented for a maximum of \$2,712.

MAXIMUM RENT, INCLUDING FEES AND BASIC UTILITIES (30% OF MONTHLY INCOME)

Unit Size	Percent of Area Median Income									
	30%	40%	50%	60%	65%	70%	75%	80%	85%	90%
0-BEDROOM	\$790	\$1,054	\$1,317	\$1,581	\$1,712	\$1,844	\$1,976	\$2,108	\$2,239	\$2,371
1-BEDROOM	\$847	\$1,129	\$1,411	\$1,694	\$1,835	\$1,976	\$2,117	\$2,259	\$2,400	\$2,541
2-BEDROOM	\$1,017	\$1,356	\$1,695	\$2,034	\$2,203	\$2,373	\$2,542	\$2,712	\$2,881	\$3,051
3-BEDROOM	\$1,175	\$1,567	\$1,959	\$2,351	\$2,547	\$2,743	\$2,939	\$3,135	\$3,330	\$3,526
4-BEDROOM	\$1,311	\$1,749	\$2,186	\$2,623	\$2,842	\$3,060	\$3,279	\$3,498	\$3,716	\$3,935

Seattle Office of Housing 2024 Rent Limits for Affordable Housing

Sales and Use Tax Amounts

- Of the total 10.35% sales and use tax rate, 1% goes to the City of Seattle.

Jurisdiction / Purpose of Sales Tax Revenue	Amount
State of Washington	6.5%
King County	1.45%
Transit District (Sound Transit)	1.4%
City, Unrestricted	0.85%
City, Transportation Benefit District	0.15%
TOTAL	10.35%

Conversions are expensive. Public support is necessary to make them feasible.

- Conversion development costs are equal or greater than for new construction of comparably sized buildings.
- Developers must attest that "but for" the sales tax deferral they would not build the conversion to qualify for the deferral.



$\leq 85'$ (or $75'$)



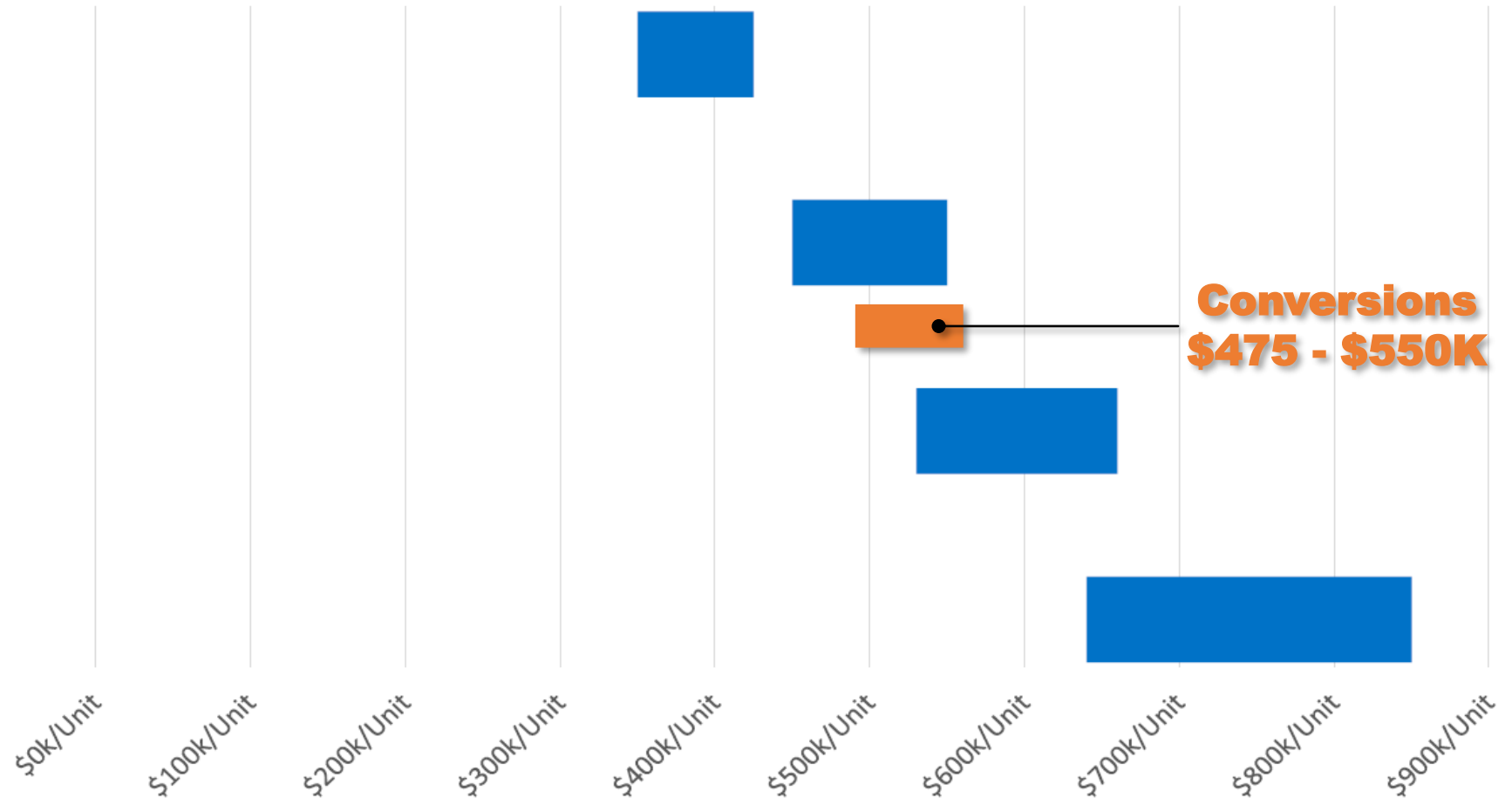
$\leq 160'$



240' (ish)



400' +



Conversion Incentive Example

- Example based on a 200-housing unit conversion of a 1920's era office building.
- Deferral would reduce overall project costs by about 7.1%, or \$10M.

Project Costs	With Sales Tax	Sales Tax Deferred
Land Acquisition	\$9,000,000	\$9,000,000
Hard Costs	\$100,000,000	\$100,000,000
Sales & Use Tax	\$10,000,000	Waived
Tenant Improvements	\$2,000,000	\$2,000,000
Soft Costs	\$14,000,000	\$14,000,000
Financing	\$5,000,000	\$5,000,000
Project total:	\$140,000,000	\$130,000,000

Illustrative cost side of a forma for a \$140 million conversion project with and without a sales and use tax exemption.

Financial Impacts

- **Administered by OPCD**

- OPCD will manage the application process with existing staff, in partnership with the Washington State Department of Revenue. No administrative impacts on Office of Housing or SDCI.
- Program sunsets after 10 years.
- If a conversion ceases to qualify, all back sales & use taxes plus interest are immediately due.

- **Positive Financial Impacts**

- Adds residents that support downtown businesses and recovery
- Stabilizes rapidly-declining property valuations in downtown
- Increases revenue from property, and business and operation (B&O) taxes compared to if buildings are vacant
- Decreases public safety and code enforcement costs often associated with vacant structures

- **Costs**

- Little to no loss of revenue because the deferral applies to projects that would not occur without the tax deferral. Owners must attest that the project would not proceed "but for" the tax deferral; however, it is possible that developers will choose to build a tax deferred project rather than a different project that would have generated tax revenue.
- Very small number of overall conversions anticipated. (6 – 12 within 7-years are projected). No conversions have submitted complete permit applications since the pandemic.



Potential Conversion Examples

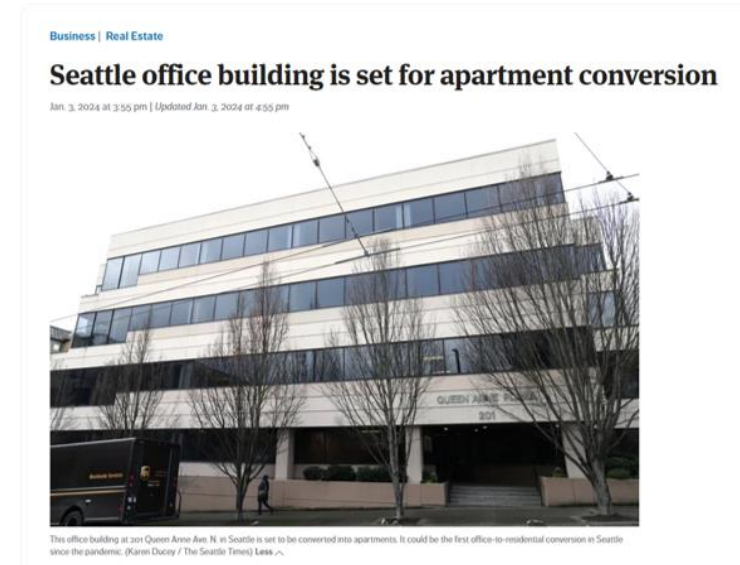
- OPCD received a series of creative proposals during the 2023 call for ideas competition.
- Several conversion proposals are in the pre-submittal, feasibility analysis phase.



Colman Building



Vance Building with Conversion Concept



201 Queen Anne Ave. N.

Thank you.

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