

City of Independence, Ohio

"THE HEART OF CUYAHOGA COUNTY"

6800 BRECKSVILLE ROAD

INDEPENDENCE, OHIO 44131

(216) 524-4131

MEMORANDUM

To: Mayor Gregory P. Kurtz
Members of Council

From: Finance Director Vernon Blaze

Date: Friday, July 8, 2022

Re: Finance Office and Related Topic Updates

Office Buildings, Office Space and Office Market Dynamics

In a community such as Independence whose primary revenue source (local income taxes paid by employees who work in Independence but don't necessarily live in Independence) is highly correlated to office type employment, news regarding office buildings and office space and current dynamics in that market are always reviewed and analyzed quite intently by the Finance Office.

Crain's Cleveland Business ran an article this week titled "New Lives Set For Local Office Buildings." It went on to identify some office buildings in the eastern suburban office market along Interstate 271 that are being repurposed to other uses than for continued office space.

One investor indicated that a recent purchase of an eight-story office building that will be repurposed into 147 apartment units was because "Cleveland is distinguished by an abundance of office space" and "Much of the Cleveland office product is from the 1970's."

In another recent east-side transaction, an existing office building will be demolished in order to construct a self-storage center.

Think about the economics of that dynamic for that community. The former office building employed people who paid local income taxes to that community. A self-storage center? It may employ a small staff to manage the property, but otherwise will employ a very small fraction of the employees that the office building used to.

The article indicated that all of these adaptive re-uses (or razing and constructing new) are being driven by "the body blow the pandemic gave the office markets across the U.S."

Even owners of somewhat older office buildings that want to keep the existing office uses within them are running into headwinds in doing so.



City of Independence, Ohio

"THE HEART OF CUYAHOGA COUNTY"

6800 BRECKSVILLE ROAD

INDEPENDENCE, OHIO 44131

(216) 524-4131

Office Buildings, Office Space and Office Market Dynamics

Jeremy Steiger, a partner at Lee & Associates in Beachwood said *“Rising construction costs are a factor in deciding the next phase for some older suburban office buildings. Renovating office space for new tenants is expensive. You can’t easily make up the cost [of renovating existing space] given prevailing rent rates.”*

Both of the re-purposings that are noted above are effectively not options for Independence at this time.

To convert an older office building into residential apartment use in Independence would require a majority affirmative vote of the electorate, which historically hasn’t looked too kindly on any proposal that might be construed as “apartment” in use.

So the converting of aging Independence office buildings into residential use isn’t a likely option in Independence – even if current owners of older office buildings are finding it too cost-prohibitive to complete costly renovations that would attract tenants given the fairly low rental office space rental rates in Northeast Ohio.

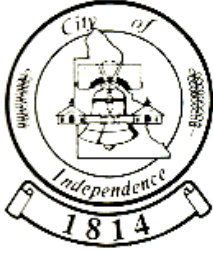
The other option cited in the *Crains* article – demolishing an office building to construct a self-storage center - is a very unappealing option. Besides producing very little in the way of local income taxes, such uses would be very incompatible with surrounding properties in the Rockside Road Business Corridor.

What should Independence do then? The cost to renovate aging office buildings is getting too cost prohibitive to be economically feasible. Alternative residential or self-storage uses of these aging office buildings aren’t economically viable or desired in Independence.

Although Independence isn’t a “big” city, a front-page article in today’s *Wall Street Journal* was on the this exact subject of what drives Independence’s primary income source – local income taxes paid by office workers. It was titled *“Big Cities Can’t Get Workers Back to the Office.”*

Headwinds abound for Independence’s long-term financial health due to the office dynamics outlined above. But standing pat and doing nothing isn’t really an option or a strategy.

Perhaps one solution to consider and discuss with Council is for Independence to pro-actively partner with the owners of aging, Class C office buildings in the City to help the economics “work better” in upgrading these older, Class C buildings into say Class-B office space.



City of Independence, Ohio

"THE HEART OF CUYAHOGA COUNTY"

6800 BRECKSVILLE ROAD

INDEPENDENCE, OHIO 44131

(216) 524-4131

In exchange for job creation grants that would pay out only if new employment occurs within these buildings, and for some possible investment in the buildings themselves, perhaps the City's Community Improvement Corp. could receive an equity stake in some of these office properties.

It could be a win-win-win for all concerned:

- The owners of these formerly Class C office buildings would now have Class B office buildings
 - These buildings would now be more marketable and economically viable
- New tenants to these buildings would have fresher, upgraded space to occupy within Independence
 - They would also be incentivized to grow because of the job creation grants
- The City itself would receive multiple benefits:
 - Increased income taxes – predicated and conditioned on office workers being in those offices
 - A small equity stake in some of these buildings
 - A true partnership with local office building owners
 - Additional employees working out of these offices would provide additional vehicular and possibly foot traffic to Independence's local retail business establishments

If more and more office buildings in Downtown Cleveland and other Northeast Ohio suburban office markets are taking older office buildings off-line and either demolishing them or converting them to other uses, perhaps that presents an opportunity for Independence to become the logical landing pad for the remaining businesses in Northeast Ohio that still want and need a nice, fresh, appealing physical office environment for their employees to actually work out of.

If so, a discussion on the merits of creating a program to incent Class C office building owners in Independence to partner with the City to upgrade these buildings and attract tenants that are finding less and less office space to occupy in Northeast Ohio couldn't hurt.

Take those current headwinds and negative office market dynamics and do our best to turn those headwinds and negative dynamics into a competitive business advantage for Independence!