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COVER STORY

LA's boom brings clamor for development rights

Alexander Drecun / Special to the Daily Journal

Loeb & Loeb LLP partner Paul Rohrer says market conditions have made building downtown L.A. high-rises more appealing.

By Andrew McIntyre / Daily Journal Staff Writer

Prior to the housing collapse, developers in Los Angeles were keen on erecting high-rises and buying the necessary building rights from the city to do so, buoyed by a certain degree of confidence in their ability to land tenants who could pay the rental prices such towers demand. Then the recession hit, high-rise projects halted, and in Los Angeles, costly transfer of floor area ratio — known as TFAR — stopped entirely.

Now, as the real estate market recovers, the city has three so-called TFAR applications in process, the same number it approved over the past three years, and it's negotiating with developers on seven more, according to a city official.

"We see seeds starting to sprout. ... L.A. has not been that much of a high-rise city. We had a brief moment prior to 2008 when some high-rise projects were constructed," said Los Angeles Loeb & Loeb LLP partner Paul Rohrer, who has worked on a number of TFAR projects. "We're seeing confidence that you'll be able to get a price per square foot that would compensate you for building a high-rise."

Each downtown Los Angeles property is zoned at a specific floor area ratio, and much of the city is at 6:1 FAR, which allows a floor area of six times the size of the lot. That would mean, for example, 240,000 allowable square feet on a 40,000-square-foot lot.

Developers pay two fees to purchase additional rights: a community benefit fee — money that goes toward city improvement in the environs of the project — and a transfer fee. The community benefit fee is based on property purchase price, lot size, current FAR zone and additional square feet desired, while the transfer fee, assuming the developer is buying TFAR from the city, which is most often the case, is 10 percent of the community benefit or $5 per square foot purchased, whichever is greater.

TFAR projects require a variety of legal counsel. Lawyers work with developers to obtain the necessary entitlements for the project, and lawyers help developers ensure the project complies with the California Environmental Quality Act, or CEQA; the additional density developers seek under TFAR is subject to CEQA review. Lawyers also help developers determine where the floor area transfer will come from and help document that transfer.

Developers may buy unused TFAR from private parties, in which case the parties negotiate the transfer rate, although the city still gets the community benefit fee.

"Certainly, with the improving economy, we're seeing more interest among our clients for the potential for increasing floor area," said John Bowman, a land use partner at Elkins Kalt Weintraub Reuben Gartside LLP in Los Angeles who has been involved in projects that explored TFAR transfers. "All the fundamentals are there. An improving economic climate as well as a lot of development in and around central Los Angeles."

Cities across the country have their own versions of Los Angeles' TFAR. In San Francisco, downtown development sites can transfer unused rights from preservation properties. In New York, unlike Los Angeles, rights transfers occur mainly between private parties.

"The one that came through a couple years ago, Wilshire Grand, that was the first in a long time," said Shana Bonstin, a Los Angeles senior city planner, referring to Korean Air's 1,100-foot, 900-room hotel — with 400,000 square feet of office space — that will replace the U.S. Bank Tower as the tallest building on the West Coast. "In the last year, there's been an uptick in the number of projects being submitted."

That $365 million project received approval for a transfer of 325,145 square feet, and the developer paid a $2 million community benefit fee and $1.6 million transfer fee.

Before 1970, Los Angles was zoned at 13:1 FAR, which is how, for instance, 32-story City Hall, the tallest building in Los Angeles when it was built in 1928, could be built, and 13:1 FAR is still the maximum density allowed in Los Angeles. But in an effort to give itself more authority to control development, L.A. in the mid 1970s re zoned much of downtown to 6:1 and 3:1 FAR.

"TFAR is basically an attempt to reverse that decision but meanwhile make some money off of it," said Hamid Behdad, president of Central City Development Group, who's currently working on a TFAR proposal. "You could consider it a smart public policy or you could call it highway robbery."

The projects currently under city review are two seven-story, mixed-use buildings looking to transfer a combined 139,585 square feet at 416 W. Pico Blvd., and smaller projects at 1130 S. Hope St. and 534 S. Main St. each seeking less than 50,000 additional square feet.

The city planning director can approve TFARs of less than 50,000 square feet, and those for 50,000 square feet or greater go to the Planning Commission.

These and various other potential TFAR projects come at a time when Los Angeles, as Rohrer put it, is concerned "downtown will be built out at seven stories so we end up with a sort of neo-Tuscan Paris of apartment buildings at 75 feet," the critical construction level above which building becomes significantly more expensive.

Indeed, despite TFAR activity picking up of late, there are still hurdles for developers to clear.

"You have CEQA issues. You have delays. You have uncertainty with respect to whether or not the vacancy rate in downtown for office and residential will start to climb," said Douglas A. Praw, a partner at Goodwin Procter LLP in Los Angeles who has worked on TFAR projects in the past. "You need to find those open spaces. There's just not that many that are available."

Los Angeles councilman Jose Huizar, whose district is downtown, last month urged the city to provide various incentives to developers who wish to build downtown high-rises.

"Immediate efforts must be taken to protect potential development sites viable for high-rise development and to ensure opportunities remain to build the high-rise structures needed to meet the needs of our growing city," Huizar wrote in a motion on Sept. 10.

To the extent that developers are seeking more density, "most of the development that would take advance of transfer of floor area would be residential and hotels," said Patrick A. Perry, a Los Angeles partner at Allen Matkins Leck Gamble Mallory & Natsis LLP who's worked on projects that investigated TFAR. "Those are the two big market areas downtown in development."

But while some developers are indeed still skittish about investing in high-rise construction, increased confidence in the market writ large — and in the future of the downtown Los Angeles market — is spurring some high-rise development, say brokers.

"I think what we're seeing is that, especially in South Park, the Financial District, Entertainment District, developers are looking to go high-rise," said Bradford P. McCarthy, a senior associate at CBRE Inc. in Los Angeles. "That means they'll go out and will find a way to secure TFAR. That's the economics of the next phase of the development cycle."

And Loeb & Loeb's Rohrer is seeing that next phase play out.

"I looked at something the other day in which the property's TFAR payment was going to be approaching $5 million," Rohrer said. "People are coming back to it. Now that the market has hit a certain point, people are buying them."