

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



Jeffrey S. DeWitt  
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:** Jeffrey S. DeWitt  
Chief Financial Officer

A handwritten signature in black ink that reads "Jeffrey S. DeWitt".

**DATE:** July 5, 2019

**SUBJECT:** "MLK Gateway Real Property Tax Abatement Emergency Amendment  
Act of 2019"

**REFERENCE:** Draft Legislation Provided by DMPED on June 27, 2019

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**Findings**

The proposed bill would provide real property tax, recordation and transfer tax abatements to the property at 1201-1215 Good Hope Road, S.E. (the Property) to assist the financial feasibility of this property's redevelopment.

The real property tax abatement would last for up to 15 years and cannot exceed \$3 million in total, and it is conditioned on approved ownership. The recordation and transfer tax abatements are not limited in duration, not limited in tax amount, and not conditioned on the Property's approved ownership.

Based on the OCFO's analysis of the information provided by the project's developer, it is unlikely that the project could be financed without the proposed abatements. However, the recordation and transfer tax abatements are not necessary beyond the period that the Developer owns the property.

Please refer to the separate Fiscal Impact Statement for the effect of the proposed legislation on the District's budget and financial plan.

**Background**

The Property is part of a development project known as MLK Gateway. It is located in the Historic Anacostia neighborhood of Ward 8 and is known for tax and assessment purposes as Lots 1017, 847, 864, 866 and 867 in Square 5769. The District, which owns a fee title interest in the Property,

authorized its disposition to MLK Gateway Partners LLC (the Developer) in December 2017 as a 50-year ground lease with an option to renew.<sup>1</sup> The Developer is comprised of two separate entities, the Menkiti Group (Menkiti) and Enlightened, Inc (Enlightened). The Developer will renovate the existing storefront retail properties and construct new mixed-use space, yielding a total of approximately 35,000 square feet of gross building area when completed.

Enlightened, a CBE technology company, will be the anchor tenant for the office space, and the remainder of the leasable space is planned as ground floor retail. Enlightened will lease approximately 20,000 square feet for its cyber-technology business. In addition to its business operations, Enlightened will run a cyber-technology incubator, offer mentoring services to local companies, and offer job training to local residents. The remaining building area will be leased as retail space and offer new retail amenities to the neighborhood.

### Financial Analysis

District of Columbia Code §47-4701 requires the analysis provided by the Office of the Chief Financial Officer (OCFO) to contain certain information. The required information is included below.

#### Terms of the Exemption or Abatement

The proposed legislation abates the property’s real property tax liability, up to a maximum of \$3 million in total, for up to 15 years. The proposed legislation also exempts the property from transfer and recordation taxes for an indefinite period and indefinite tax amount. Receipt of the abatement is conditioned upon the Developer maintaining a lease agreement with Enlightened or another mayoral approved, locally-owned and operated business, and meeting CBE participation and other requirements to encourage employment of District residents<sup>2</sup>.

#### Annual Proposed Value of the Exemption or Abatement

The table below provides the estimated value of the abatement.

	FY 2020	FY 2021	FY 2022	FY 2023	Total to 2023	2024 - 2034	Total to 2034
Exempted Real Property Tax and Possessory Interest Tax	\$0	\$0	\$275,000	\$298,925	\$573,925	\$2,426,075	\$3,000,000
Exempted Transfer and Recordation Tax	\$275,000	\$0	\$0	\$0	\$275,000	\$496,500	\$771,500
<b>Total</b>	<b>\$275,000</b>	<b>\$0</b>	<b>\$275,000</b>	<b>\$298,925</b>	<b>\$848,925</b>	<b>\$2,922,575</b>	<b>\$3,771,500</b>

<sup>1</sup> MLK Gateway Disposition Approval Resolution of 2017, approved December 5, 2017 (Resolution 22-319; 65 DCR 33).The disposition includes adjacent property, 1901-1913 Martin Luther King Jr., Avenue S.E. (known for tax purposes as Square 5770, Lot 82). A subsequent resolution amended the terms of the disposition, reducing the ground lease payments for the 1201-1215 Good Hope Road, S.E. property and allowing a fee simple disposition of the 1901-1913 Martin Luther King Jr. Avenue, S.E. property.

<sup>2</sup> The abatement is not conditioned on actual use and therefore may not strictly need to be occupied to receive the abatement.

Menkiti provided a cash flow model for the Property’s redevelopment, and the estimate is based on the assumptions provided in the model.<sup>3</sup> Because the legislation does not extinguish the transfer and recordation tax abatement after a set time period, the sale of the property, or other conditions, the value of the abatement could extend past the period modeled by Menkiti.

### Summary of the Proposed Community Benefits

A summary of the proposed community benefits as submitted by the Developer is attached to this analysis.

### Financial Analysis for Development Projects

Given the estimated real property tax liability and all other assumptions provided in the cash flow model, the equity required to fund all of the estimated redevelopment costs does not yield a sufficient return to be an attractive investment. Because the tax abatement increases the project’s net operating income (the amount of revenue received from rent, net of operating expenses including real property taxes), the abatement increases the cash flow available from the operation of the project. With the abatement, the project can also fund a greater portion of its redevelopment costs through debt, which reduces the amount of equity needed. These cash flow effects from the real property tax abatement increase the project’s return on equity. According to the cash flow analysis provided by Menkiti, the projected internal rate of return (IRR)<sup>4</sup> is approximately six percent without the real property tax abatement, an amount that the OCFO agrees is below the threshold likely necessary to attract equity to the project. With the real property tax abatement, the projected IRR increases to 11 percent<sup>5</sup>. At that level, the real property tax abatement does not over-subsidize the project.

The estimated value of the transfer and recordation tax payments, if not abated, also decrease the project’s cash flow and are estimated to further reduce the project’s IRR. The impact of the transfer and recordation tax abatements on project’s financial feasibility is much less significant than the real property tax abatement but this tax liability could also impede the project’s financing.

The Developer has worked closely with the Deputy Mayor for Planning and Economic Development (DMPED) on the project’s financing since the commencement of the competitive property disposition process. According to the Menkiti Group and DMPED, grant funds that were proposed as a source of funding for redevelopment costs at the time of award were ultimately not available for this project, and alternate sources that could fill the subsidy gap have not been found.

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<sup>3</sup> The estimate assumes that the project receives a certificate of occupancy in early FY 2021 and that real property taxes are abated beginning in FY 2022, in accordance with the legislation. Estimates on the annual growth rate of real property tax assessment were provided by the OCFO’s Office of Revenue Analysis. The estimate assumes abatement of recordation tax liability on loans and property transfers identified in the Developer’s pro forma.

<sup>4</sup> IRR is defined as the discount rate at which future cash flows equals zero. More broadly, it is used as a metric to assess return on equity investment over time.

<sup>5</sup> Menkiti’s cash flow model IRR is slightly higher, at 12 percent, due to a difference in the year the real property tax abatement begins.

**Conclusion**

Based on the OCFO’s analysis of the information provided, it is unlikely that the project could be financed without the proposed abatement. However, it is not necessary to abate transfer and recordation taxes beyond the period that the Developer owns the Property.

**Attachment: Summary of Community Benefits Provided by the Developer**

The MLK Gateway project, developed by the 100% CBE team of MLK Gateway Partners LLC (“Developer”), is designed and programmed as a public benefit that creates a vibrant, sustainable, and architecturally significant MLK Gateway at the intersection of Good Hope Road SE and Martin Luther King Jr. Avenue SE. MLK Gateway Partners’ commitment to community benefits is outlined below:

*Technology Jobs, Training for Anacostia Residents & Scholarships*

As a community benefit inherent to the project, Developer will bring Enlightened, an award-winning, Certified Business Enterprise (CBE), HUBZone certified Information Technology (IT) and Management Consulting firm, as the anchor tenant to Anacostia’s MLK Gateway. Enlightened has expertise in Cyber Security, System Integration, Curriculum Development, and Training, and will relocate its headquarters from Connecticut and L downtown to Good Hope Road and MLK in Anacostia. In doing so, Developer will bring 150 tech-sector employees to the MLK Gateway, establishing Enlightened as one of the largest private employers east of the river. Enlightened will also establish a technology incubator at the site where they will mentor growing technology companies and provide shared office space. As a result of Enlightened’s relocation, MLK Gateway will gain credibility as a technology innovation corridor. It is expected that the addition of Enlightened’s business and employees will improve the economic conditions in the Anacostia Gateway, allowing new businesses to locate and thrive in the Anacostia neighborhood. In short, relocating Enlightened will have a transformative and catalytic effect on the MLK Gateway corridor.

As an additional community benefit, Enlightened will form a nonprofit entity that will host an annual training program for individuals with a focus on those in Wards 7 and 8. The expected outcome is to create career opportunities in Information Technology. The training curriculum will include:

- Cybersecurity and certifications
- Network infrastructure and certifications
- Software development/coding

The IT training program will be delivered in two cohorts, each lasting for approximately six months. The cohorts will each have 15 slots for participants. Total cohort participants during the six-month training period will be up to 30. Additionally, Enlightened will encourage nonprofit organizations within Wards 7 and 8 to also participate in the training.

Upon participants’ completion of the six-month training program, Enlightened and the following organizations will work with participants to assist with job placement:

- DC Chamber of Commerce
- Greater Washington Black Chamber of Commerce
- DC Hispanic Chamber Companies
- Howard University Cybersecurity Education Research Center - Board Members (e.g. AT&T, KPMG, DXC).
- Developing Economic Opportunities, Inc.
- Potential DoD Mentor Protégé Partners
  - IBM
  - HP
  - SAIC

- Enlightened Protégé Companies
  - Jasint
  - Myriddian
  - PMCS
  - Other CBE IT Companies

To ensure access to the technology workforce training, Developer will provide scholarships for qualified residents to access Enlightened’s workforce training programs free of charge. Developer will work with the ANC, area schools, the faith community, and neighborhood nonprofits to identify qualified candidates from the neighborhood.

#### *Job Creation, CBE Participation, First Source*

The project will be a significant creator of jobs for the Anacostia neighborhood. It is anticipated that the project will create 191 permanent jobs after stabilization as well as 139 temporary construction and design related jobs during the project<sup>6</sup>.

The project will also support local and small businesses by having at least 35% CBE participation in the project and by complying with a First Source hiring agreement. Furthermore, Developer is committed to encouraging local participation in the Project and to this end will conduct two employment fairs in Ward 8 to make local residents aware of job opportunities in the redevelopment of the Property and in the businesses that will occupy the Property after completion of the redevelopment.

#### *Community-Focused Retail*

The proposed retail program at the MLK Gateway is also a significant community benefit and part of our commitment from the conception of this project. In spending nearly four years working with the Anacostia community on the MLK Gateway plan, we realize that access to high quality goods and services is a significant need for the neighborhood, and one which we are committed to addressing. Therefore, we plan to program price-point sensitive retail with a focus on a restaurant, a fresh foods market, and a coffee shop.

#### *Historic Preservation & Collaborative Design*

A core element of Developer’s community benefits package is our commitment to restore the vacant, blighted properties on Good Hope Road in accordance with the Historic Preservation Review Board, which is a substantial cost to the project. In furtherance of this initiative, Developer worked with the ANC, the Historic Anacostia Preservation Society, and the Historic Preservation Office on the historic concept design elements which include the detailed brick work featuring Flemish bonding, window articulation and detailing, storefront articulation, and rooftop mechanical placement and screening.

With respect to historic preservation, Developer also agrees to the following:

1. Developer will work with the community to reduce displacement of residents, and in particular, seniors who wish to remain in historic homes, by directly providing up to \$10,000 of value in light carpentry and painting services to elderly residents.

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<sup>6</sup> Source: *MLK Gateway Market Analysis* report by Jon Stover & Associates

2. Developer will provide up to 15 hours of man-power to conduct a visual conditions assessment survey of the Anacostia Historic District in partnership with the National Trust for Historic Preservation.
3. Developer will work with its General Contractor to ensure that there are workforce development opportunities for neighborhood residents within the historic preservation trades, and will work with the ANC and Historic Anacostia Preservation Society to identify eligible residents.
4. Developer will assist the Historic Anacostia Preservation Society and the National Trust for Historic Preservation in executing an initial convening of residents and experts regarding preservation and economic development within the Historic District.

Made up of two DC-based, minority-owned CBEs, Developer values being able to develop and deliver a project that serves the community’s needs and integrates physically and socially into the Anacostia neighborhood. We look forward to a continued partnership with the Anacostia community as we design, deliver, and operate the new MLK Gateway site.