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In Slow Times, Rezoning Appeals to Developers

By ALISON GREGOR

Property developers generally earn their money by putting up new buildings, but when the real estate market cools, making it difficult to obtain financing, they often look for other ways to help turn a profit.

Some developers — and their real estate lawyers — say that rezoning property is one of them. Juan D. Reyes III, a partner in the law firm of Riker, Danzig, Scherer, Hyland & Peretti, said he had clients seeking zoning changes with hopes of developing or selling the property once the market improves. This particularly applies in areas zoned for manufacturing.

“In the height of the market, a lot of developers just wanted to buy it, develop it and get out,” he said.

Getting a change in zoning, however, can be time consuming. “With zoning, even if you’re doing a variance, it’s a minimum of a year,” he said. “A rezoning can take two to three years. Now is a good time to be doing that.”

Because obtaining any kind of discretionary city approval can take time and resources, developers may shy away from doing it during a go-go market, said Mitch Korbey, a lawyer with the firm of Herrick Feinstein.

“Their focus is often elsewhere, on other projects, for a variety of reasons,” he said.

But when the real estate market comes to a virtual halt, as it has currently, many developers cannot get development financing on favorable terms. An attractive option is to wait out the torpid market while trying to add value to their property with a rezoning, Mr. Korbey said.

Herrick Feinstein has several clients doing just that, specifically on properties zoned for manufacturing. “These are areas that are not zoned in a way that permits residential, because you can’t do residential development in a manufacturing zone,” he said. “Yet residential is nearby, and you’ve got a manufacturing zone that’s not so productive, that’s not generating income, that’s adding very few jobs.”

Mr. Korbey said he was currently handling a case involving several blocks of contiguous vacant lots and warehouses that were once part of a Rheingold brewery in the Bushwick neighborhood of Brooklyn. The developers, Forest Lots L.L.C., recently applied for a zoning change to permit hundreds of residential units and retail development.

“We’re at the beginning of a process that’s going to require an environmental review and public input,” Mr. Korbey said.

The developers are gambling that they will get the rezoning as the real estate market picks up, making their land ripe for development.

Though the developers want to build, another option would be to sell the land — most likely at a premium, Mr. Korbey said. “Obviously, there’s tremendous upside to changing the rules to allow new low- and medium-density housing,” he said.

During a sluggish market, the city may be more willing to approve zoning changes, said Stuart M. Saft, a partner with the firm of Dewey & LeBoeuf.

“The city’s tax revenues fall during a recessionary market, and what the city is looking for is increased taxes,” he said. “If the zoning change will improve the value of the property after the building is constructed, the city will get an increase.”

Lawyers said that developers who seek rezonings when the market is troubled have typically owned their land for a while. Often, while developers were otherwise occupied in a flourishing market, the land was earning income as a parking lot or a one-story “taxpayer” (so-called because the revenues pay the property taxes).

Though not unheard-of, it is rare for developers to buy land in a slow market with the aim of getting it rezoned, said Gary Tarnoff, a partner at Kramer, Levin, Naftalis & Frankel.

“As far as buying a piece of vacant land in a down market and seeking a rezoning in the hopes that the market will turn by the time that they’re ready to develop it, I can’t think of any instances of this during this economic cycle,” he said.

But there are some developers — those who build affordable housing — who routinely use this strategy in both hot and cold markets. “It’s cheaper to buy property that’s zoned in a way that undervalues the real estate,” said Ken Olson, president of POKO Partners, a development company that specializes in affordable housing. “You’re willing to accept some level of risk, because you could go through the city’s planning process and be denied.”

POKO recently filed for a variance on two lots zoned for manufacturing and commercial use on Broadway in Bushwick. Mr. Olson said he hoped to develop both affordable housing and commercial space.

“We’ve done it before,” he said. “If you find the right location — that being a place where City Planning and the community support the idea of creating housing — it’s a good strategy.”

As the real estate market flags, market-rate housing developers are adopting the same strategy, said Randolph H. Gerner, a principal at Gerner Kronick & Valcarcel, an architecture firm that does site planning for developers.

Mr. Gerner said he was seeing developers form alliances with landowners to get parcels rezoned. His firm is handling one such case involving a swath of industrial land in Sunnyside in Queens.

When the real estate market was roaring, “if you couldn’t get something done quickly, developers weren’t doing it,” he said. “Now, they’re saying, ‘It’s going to be a down cycle, but let me prepare for when demand will increase.’

“People are using this opportunity to spend the two years that it takes to seek relief from zoning,” he said.

William Procida, a longtime Bronx developer serving as restructuring adviser to mortgage companies, said developers should use the quieter market to get all their discretionary approvals, not just rezonings.

He said, however, that when the real estate market returns, it may be hard to predict what will be in demand. "When you go get your approvals, make sure they're for the right thing," he said. "Somebody with a warehouse approved for high-rise mixed-use, it actually might be worth more in the next 10 years as a warehouse than as condos. Or maybe that residential land will be worth more with fewer units.

"It's not just upzoning that's lucrative," he said, meaning the addition of more units or higher buildings. "Depending on the market, sometimes it's downzoning."