FOR AGENDA

EBAP/92/129

July 22, 1992

To: Members of the Executive Board

From: The Secretary

Subject: Long-Term Office Space Study

Attached for consideration by the Executive Directors is a study on long-term office space. Conclusions and recommendations appear on pages 14-15. This subject is now tentatively scheduled for discussion on Friday, August 7, 1992.

Mr. Cole (ext. 38206) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

Long-Term Office Space Study

Prepared by the Administration Department

Approved by Graeme Rea

July 20, 1992

I. Introduction

In June 1991, Executive Directors approved in principle the management's proposal in EBAP/91/159 (6/20/1991) to construct Phase III of the Headquarters building. The increases in staff resources authorized since that discussion have altered the space management equation that existed twelve months ago, by substantially increasing the Fund's need for office space. It is now clear that, even with the addition of Phase III, the Headquarters building will not be large enough to meet all the Fund's space needs, and this calls for a thorough re-examination of how best to meet these needs over the long term.

The purpose of this paper is (i) to review the development of the Phase III project and the space demand assumptions on which it was based; (ii) to describe the current situation, comparing the supply of owned and leased space with the known demand; (iii) to analyze the impact of the Phase III addition upon the overall supply of space, noting that it will be inadequate to meet the Fund's needs; and (iv) to review alternative strategies for meeting the known and foreseen space needs of the Fund over the long term. The paper concludes that the most suitable strategy for the Fund to pursue would be to proceed with the Phase III project, and supplement this by the acquisition of additional space close by. A recommendation is included specifying steps for implementing this strategy.

The analysis contained herein focuses upon orders of magnitude designed to facilitate strategic decision making, rather than on detailed costing. The latter, which has been developed in support of the analysis, would be presented at a later date, when budgetary approval is sought for a specific proposal.

II. Background

Historically, the long-term space strategy of the Fund has been to house all of its Washington-based staff in a single, owned, Headquarters building located in the central business district. This strategy was justified on three grounds: (i) it is less expensive to house staff in owned than in leased space over the long term; (ii) because of the highly centralized style of management in the Fund and the need to respond quickly to changing situations, there are strong operational advantages to housing all staff under one roof; and (iii) there are significant advantages to a location in the downtown area, close to embassies, the World Bank, and other institutions, and to the amenities (hotels, restaurants, shops, etc.) that are readily available in this part of the city. The strategy has been endorsed by the Executive Board on several occasions, most notably when the building plan for the current Headquarters building was authorized in the late 1960s. The Board endorsed at that time a long-term plan, whereby the Headquarters building would be expanded in stages as and when the need for space dictated. Consistent with this plan, Phase I was completed in the early 1970s, and Phase II ten years later. Thus, the Phase III project was conceived as a continuation of a strategy that the Fund has been pursuing for over 30 years.

Development of the Phase III project has itself proceeded in stages. The first was initiated in 1988, when the Executive Board authorized an expenditure of up to $30 million for the acquisition of the Western Presbyterian Church (WPC) property, construction of a new church elsewhere, and application for the necessary rezoning of the property to permit construction of Phase III. 1/ The second stage was to seek the Executive Board's approval in principle to the Phase III addition, and its authorization to spend up to $8.3 million for the preparation of construction drawings and other space planning activities. This approval and authorization were given in June 1991. 2/ The third and final step in the process, at least as envisaged until recently, was to occur after final designs and cost estimates had been prepared, at which point the Executive Board would be asked to give a firm authorization to proceed with construction of Phase III. The actual construction would not be scheduled to begin before December 1993, at the earliest.

Pursuant to the authorizations that have already been given, the Fund has acquired the former WPC property, zoning approval for Phase III has been obtained, and preparatory work has begun on the construction of the new church building. Work has also proceeded on the preparation of construction

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1/ See EBAP/88/197, 8/9/88 and two subsequent supplementary papers, namely: EBAP/88/257, 10/25/88 on Fund space requirements and EBAP/88/265, 11/1/88 on financing options.
2/ See EBAP/91/159, 6/20/91 on need for Phase III.

drawings for Phase III, although this work has now been put on hold pending a further discussion with Executive Directors of the Fund's long-term space needs.

During the June 1991 discussion of Phase III several Executive Directors emphasized the importance they attached to accommodating all the Fund's staff in the Headquarters building. The staff agreed to make detailed studies of the capacity of the expanded building and of measures that might reasonably be taken to utilize that capacity fully; but even at that time, it was becoming increasing doubtful whether it would be feasible to meet this desired objective. The projections made at the time the Phase III plan was being developed, reflecting views expressed by a number of Executive Directors, had envisaged only very modest growth in the size of the Fund. However, in presenting the FY 1992 budget in April 1991, the Managing Director outlined a three-year program for recruiting additional staff primarily to correct the imbalance that had arisen between the demand being made on the Fund and available staff resources, and made clear that any increase in demand would have to be matched by further increases in manpower. In the supplementary budget presented in November 1991, the Managing Director recommended a substantially expanded recruitment program which took into account the rapidly increasing responsibilities the Fund was being called on to assume in Eastern Europe and the former Soviet Union. In response, the Executive Board authorized an additional 174 staff-years in late 1991 and 106 staff-years in May 1992; and in the view of the management further staff resources will need to be added before the Fund is adequately staffed to meet all its current responsibilities.

The total number of persons requiring accommodation in the Fund's premises in Washington, once the additional positions authorized by the Board have all been filled, will be over 2,725. 1/ This number includes staff members and contractual employees, staff of Executive Directors' offices, and employees of outside service firms who are located on our premises. The resulting pressure on space has been compounded by internal reorganizations which have increased the number of independent units to be housed. At present some 1950 persons are located in the Headquarters building, more than the building was designed to accommodate. Recently the Fund's leasehold space at International Square has been expanded to 400,000 sq. ft., and plans are in hand to move several further units, including two more major departments, to International Square before the end of next year, thereby relieving some of the overcrowding at Headquarters and providing a limited amount of expansion space for the departments that will remain here. As a result of these moves, the Fund population at International Square, by the end of next year, will increase to slightly more than 800 persons, or nearly one-third of total staff resources.

1/ A summary of staff resources (demand for space) and the supply under various scenarios, forms Appendix I. That Appendix also indicates the space surplus (deficit) given different assumptions of growth.

On the basis of detailed space planning studies, it has been determined that the total design capacity of the existing Headquarters is 1,800 persons, and that Phase III will increase the design capacity to 2,400 persons. 1/ Even if design capacity could be fully realized in practice, without any wasted or "left-over" space, this means that at currently authorized staffing levels, over 325 persons would still have to be housed outside the expanded Headquarters. After allowing for a certain inevitable wastage of space in laying out offices and departmental floor plans, and after also providing some minimal swing space, a more realistic number requiring to be housed outside would be closer to 400 persons. How many would need to be housed outside in, say, five years time--i.e., by FY 1998--would depend primarily on the rate of growth in staff resources in the interim, on the extent to which new organizational units are created or existing ones consolidated, and on the amount of expansion that occurs in support facilities such as cafeteria space and meeting, lecture, and training rooms. 2/ If, for example, staff resources were to grow at only 0.5 percent per annum, the number of staff outside the Headquarters in FY 1998 would have increased by about 70 (to a total of 470). A 1.0 percent growth rate would result in an increase of about 140 (to 540).

This situation makes it necessary to reassess the long-term space strategy of the Fund. Since a significant number of staff will have to be housed outside the Headquarters building in any event, should the completion of Phase III continue to be an integral part of our long-term space plan? If so, how should we plan to accommodate those who cannot be fitted into the expanded Headquarters building? If Phase III is not to be proceeded with, what alternative plan should we pursue for housing the Fund's personnel?

III. Examination of Options

As previously noted, one of the principles underlying the Fund's long-term space planning has always been that the Fund should aim to accommodate its staff in premises owned by the institution, rather than relying on commercial leasing. This policy is based upon the fact that owned space is much more economical for the Fund than commercial leasing where the real estate tax liabilities of the lessor are passed on in lease costs. 3/ This principle was reaffirmed by the Executive Board in June 1991, after reviewing an analysis of the relative costs of leasing versus building

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1/ See Appendix II for a discussion of factors affecting the number of staff who can be accommodated in a given area.

2/ See also Appendix II, footnote 1, concerning the average per capita space needed, at Headquarers and at International Square.

3/ Commercial lease prices include the owner's tax liability, debt service, and some margin for profit which amounts to about 20 percent of overall lease costs. On the basis of a 400,000 sq. ft. leasehold at International Square, the tax portion of the Fund's rental payments amounts to approximately $2.4 million per year.

Phase III (see EBAP/91/159). While examining and comparing various possible options for the Fund to meet the increased need outlined above, the staff have used as a benchmark the estimated cost of leasing the required space on commercial terms, the possibility that the Fund might wish to meet its long-term needs by continuing to lease in the commercial market is not among the options discussed in this paper because of the excessive costs involved. All the options envisage that the Fund's objective would continue to be to acquire the space it needs either as an outright owner, or on terms equivalent to outright ownership, in order to minimize the cost of housing staff.

The other principle underlying the Fund's long-term space planning, at least up to now, has been that the Fund should aim to house all of its personnel in a single building, located in the central business district of Washington. Given the recent growth of the Fund, we can no longer expect to house all our personnel in a single building located at 700 19th Street: we must either locate some of our personnel permanently in another building, while retaining our present Headquarters; or we must relocate the Headquarters to another building large enough to accommodate all the long-term space needs of the Fund. It also seems clear, however, that while we can expect to find on the market at any given time a number of buildings which might suitably accommodate staff who cannot be fitted in to our present Headquarters, it is very unlikely that we would find an existing building which is itself suitable to serve as the Headquarters of the Fund. Few, if any, buildings available in the market are likely to have, in addition to offices, facilities of the type and standard that are required for the Headquarters of a public international organization with a global mission. For planning purposes, therefore, the space planning staff have proceeded on the assumption that the most feasible way for the Fund to acquire a complete new Headquarters would be to find a suitable site and construct for itself a building that meets its particular requirements. In view of the density of existing buildings and the cost of land in the inner area of Washington, this implies the acquisition of a site in the north-western suburbs of Maryland or in Northern Virginia.

Given these assumptions, three options have been carefully examined:

- Under <u>Option One</u>, the Fund would sell the present Headquarters and the Fund's Concordia apartment building, acquire a suitably large piece of vacant land in the suburbs, and build a new Headquarters complex with all the necessary facilities and with adequate room to expand in future if this proves necessary.

- Under <u>Option Two</u>, the Fund would retain the present Headquarters as it now stands (i.e., without the addition of Phase III) and would acquire a nearby office building to accommodate all the staff who currently are located in leased premises, as well as all further staff who may subsequently join the Fund.

- Under <u>Option Three</u>, the Fund would proceed with its plan to complete the Headquarters building by constructing Phase III, and would supplement this by acquiring a nearby office building to serve the same purpose as in Option Two, but on a smaller scale.

The approach taken in analyzing the cost implications of each option has been to measure each against the cost of continuing to lease commercially. The objective has been to discover which alternative provides the most cost-effective method for housing staff. Two measures were used to evaluate the alternatives: (1) the computation of costs of their Net Present Value (NPV) to take account of the cost of capital over time, and (2) the Internal Rate of Return (IRR), where the return on investment is the savings in rents. The simulations upon which the analysis is based have been developed in consultation with three firms: the Oliver T. Carr Company, a well-known local real estate firm; the Arthur Andersen Company, which has assisted particularly in reviewing the financial aspects of each option; and the Kling-Lindquist Partnership, a leading architectural firm. The basic assumptions, and the results of the analysis are set out in tabular form in Appendix III. 1/ While these estimates take account of the depressed market conditions and provide a reasonable basis for decision making, detailed negotiations would most probably reduce the costs somewhat.

<u>Option One: Build a New HQ Building</u>

Given the current depressed prices of land suitable for commercial development in the outer suburbs of Washington, the possibility of building a totally new Headquarters complex in a suburban location is an option that must be considered. A number of available sites have been looked at for purposes of this study. Most are located along the access corridor to Dulles International Airport, in an area which, besides its proximity to the airport, provides relatively direct access to central Washington.

Our real estate advisors and architects estimate that suitable land could be acquired and a building or buildings capable of meeting the Fund's currently foreseeable space needs (a building of about 2.7 million gross sq. ft. in order to net 1.9 million sq. ft. of usable space) could be constructed for a net cost of $280 million, after deducting the proceeds of sale of the current Headquarters and Concordia properties. 2/ These costs

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1/ Appendix III contains two tables: (i) Basic Data and Assumptions, and (ii) Cost Comparisons and Return on Investment.

2/ For the purposes of this analysis, it is assumed that the current Headquarters building could be sold, at a favorable price of $250 per sq. ft. of rentable office space. The assumption is not without risk in the current market in which sales of such a magnitude are not occurring.

can be broken down to: \$10 per FAR foot for land; 1/ \$10 per sq. ft. for land improvements (sewage, water, etc.); \$180 per sq. ft. for construction; for a total of \$200 per sq. ft. gross. It would be possible to design an attractive complex, in a park-like setting, with ample room to expand if necessary. The direct financial advantage of this option is considerable, in comparison with the cost of long-term commercial leasing (see Appendix III, Table 2). As an investment it would generate an internal rate of return of 13.5 percent which is attractive on the surface but implicit in this option is the requirement of an upfront expenditure of \$540 million.

One of the sites reviewed is Landsdown, in Loudoun County, Virginia. It is located about fifteen minutes from Dulles airport and has a very sophisticated and state-of-the-art conference center/hotel, and several large tracts of land available along the banks of the Potomac. According to the Joint Meetings' Office, the conference facility could meet most of the Institution's requirements for meeting and hotel space, with the exception of the Annual Meetings.

It must be acknowledged, however, that such a removed location has some major disadvantages in comparison with a location in the central business district. The property is about one hour's drive from downtown Washington, far from embassies, the World Bank, and other institutions with which the Fund requires constant close contact. The suburban location would be particularly inconvenient for officials visiting the Fund, who will often also have business in central Washington. There is virtually no infrastructure as yet developed that could support the varying needs of the Fund staff and visitors (no shops, restaurants, etc.). There would be extensive relocation costs for the staff who have chosen housing with access to the downtown area as an important consideration, and the institution would have to consider sharing these costs with the staff, as is common practice in the private sector. This would significantly increase the total cost of the move. It is the view of the staff that the various disadvantages, and risks, attendant upon the suburban headquarters option, fully offset the direct financial advantages, making of it the least attractive alternative.

The World Bank made an extensive study of similar possible sites as an alternative for its present large construction/renovation project and concluded that it was simply not a viable option, as an investment, and for many of the logistical reasons stated above. No doubt, development of the necessary infrastructure in terms of housing and amenities could follow in time, but our financial consultants advise, as the World Bank study concluded, that the risk of experiencing a devaluation of the asset, particularly if the Fund were to sell, is sufficiently high for them to

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1/ \$10 per FAR foot (the vertical building potential of each square foot of land acquired). In the vicinity of the Headquarters building, the comparable measure is about \$120 per FAR foot.

recommend against adopting this option. (By contrast, experience indicates that real estate values in the central business district, and those close to Pennsylvania Avenue in particular, hold their value over the long term.)

Options Two and Three

The common feature of both these options is that the Fund would remain in its present Headquarters, and would acquire another building in the vicinity to house on a permanent basis the personnel who could not be accommodated at Headquarters. The difference between them is that, under Option Two, the Fund would abandon its present plan of expanding the Headquarters building, while under Option Three it would proceed with the Phase III project and expand the Headquarters building to its full permitted capacity.

The choice between the two options will depend, in part, on the weight that is attached to the desideratum of housing as many staff as possible in the main Headquarters, together with the management and Executive Board, and in part on the nature of the second building that the Fund might be able to acquire. The building itself will need to meet four basic criteria: its cost must be reasonable relative to the other options available to the Fund; it must be large enough to house comfortably all the "overflow" personnel and to provide reasonable allowance for possible future expansion; it must be of a quality that is broadly comparable with the main Headquarters building; and it must be located within a few blocks, at most, of the main building.

Enquiries in the local real estate market have identified two buildings that might be available for acquisition by the Fund on reasonable terms, each offering some features that warrant special attention. One is the International Square building three blocks from the Fund. Because International Square is large enough to house all the overflow personnel currently employed by the Fund--and is indeed housing them, in leased premises--while also providing more than adequate space for any future expansion that might reasonably be envisaged, it will serve as a model for Option Two. The other is the PEPCO building, which occupies the block immediately across H Street from the Fund Headquarters. The PEPCO building by itself is not large enough to accommodate all the overflow staff currently authorised, but by combining completion of Phase III with the acquisition of the PEPCO building the Fund could meet its present and reasonably foreseeable future space needs, in the most convenient possible way. This will therefore serve as a model for Option Three.

Each of these options is examined in more depth in the following paragraphs.

Option Two: Abandon the Phase III Project and Acquire a Large Building

As was noted earlier in this paper, we expect to be housing over 800 personnel in the International Square building by the end of next year. By that time, the organizational units located at International Square will include three major operational departments (the Monetary and Exchange Affairs Department, the Research Department, and the Department of Statistics); the IMF Institute; most of the Administration Department, including all the personnel divisions, the Joint Bank-Fund Library, and the travel office; the whole of the Bureau of Language Services; and a number of smaller units and groups, including the Office of Internal Audit and Review. In view of the very considerable expenditure already incurred by the Fund in providing offices, lecture rooms, and facilities at International Square, the option of acquiring the building must be seriously considered. The Fund has invested approximately $19 million in unrecoverable fit-out costs at International Square to date.

At present, the land upon which the International Square building sits is owned by one entity, and the building itself is owned by a consortium of three different entities. Preliminary contacts with several of the interested parties lead us to believe that a purchase of both the land and the building would be possible, but the asking price of $270 million is relatively high given the present market. In addition, approximately $30 million would be required to upgrade the building's HVAC systems that are old and in need of repair. The reason for the high asking price seems to be the rather complex ownership structure, and the fact that several of the owners are not anxious to sell given the taxes that would apply to the transaction.

The potential acquisition of the International Square building raises a number of complex legal and business issues. The building contains 1 million sq. ft. of office space, of which the Fund is currently leasing 400,000 sq. ft. The total space is substantially more than the Fund is likely to require in the next few years. Given that the Fund is not authorized to engage in commercial leasing per se, a determination would have to be made concerning the use of the excess space. If it is concluded that this excess space may be needed in the future to accommodate the Fund's needs, the excess space could be leased out on an interim basis to cover the costs incurred in connection with its ownership. However, if it were found that the excess space will never be needed for the Fund's activities, it would be appropriate to consider outright disposition of a portion of the building.

The leasing out of excess office space on an interim basis is the practice of other international organizations located in the District of Columbia, including the Inter-American Development Bank and Intelsat. In this connection, it should be pointed out that these organizations, like the Fund, enjoy immunity from all taxation. Accordingly, the rents derived from their leasing activities are exempt from income tax, and the owned premises of the organization are not subject to real property tax. 1/ This affects the financial analysis of the proposed acquisition, which assumes that the leasing activity would likewise not give rise to any tax on the Fund.

In order to compare the purchase of International Square with other alternatives, two columns are presented in Table 2, Appendix III. One represents the return on the 600,000 sq. ft. that would be leased, and the other, the 400,000 sq. ft. that would be occupied. Because the former generates a positive return, combining the two would be misleading for analytical purposes. It is the view of the staff that, while the estimated rates of return are favorable, the potentially difficult legal and business issues attached to this alternative make it much less attractive than the numbers alone would indicate.

It may be possible to find another building of suitable quality which, while of a size sufficient to accommodate all present and future staff who cannot be housed in the existing Headquarters, would not constitute as large an investment as International Square and would not involve the Fund so heavily as a landlord in the local leasehold market. However, at best, the range of choice will not be very great, given the close proximity to the main Headquarters that must be observed if we are to keep within reasonable bounds the inconvenience caused by splitting the staff between two locations. It must also be recognized that, under this Option, none of the departments, offices, and facilities now located or scheduled for location at International Square will return to the main Headquarters, and as space is acquired outside further organizational units will have to be moved out of the main building to bring it within its design capacity of about 1,800 persons. The disfunctionalities that the departments located at International Square are now experiencing would become a permanent condition.

A decision not to proceed with building Phase III would also have to take into account the contractual arrangement that is already underway with the Western Presbyterian Church (WPC). The Executive Board's decision in 1988 authorized the Fund to acquire the remainder of Square 120 in order to secure the option to enlarge the building at some future time. Accordingly, the Fund has acquired title to the existing church property adjacent to Headquarters and, in return, is obligated to construct a new church at the new location in Virginia Avenue, which it transferred to the WPC. The Fund may terminate the arrangement and reverse the property exchange that has already occurred only if it fails, after diligent pursuit, to obtain the

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1/ A bill, now inactive, was introduced in the U.S. Congress last year to remove the real property tax exemption conferred on international organizations under the International Organizations Immunities Act to the extent that such organizations engage in "commercial activities." The introduction of such a restriction would raise various questions in relation to the Articles of Agreement and the immunity from taxation conferred under Article IX, Section 9.

necessary governmental approvals for Phase III or if the WPC were to violate the contract. Absent these contingencies, and regardless of whether Phase III is eventually built, the Fund is obligated to undertake construction of the new church and take possession of the land adjacent to Headquarters currently occupied by the WPC. Thus, if Phase III is not built, the Fund would nevertheless have spent the full $30 million appropriated for the WPC acquisition for which the Fund would gain no additional office space.

Option Three: Proceed with Phase III and Acquire a Smaller Building

Under this Option, the Fund would proceed with the WPC arrangement, and when the land currently occupied by the WPC is vacated would construct the Phase III extension so that its Headquarters building would extend over the whole block. The cost of construction is estimated to be about $80 million, in addition to the $5-6 million already authorized for design, 1/ and the $30 million authorized for acquiring the land, moving the church, and applying for zoning. The enlarged Headquarters building would have space to house some 2,400 individuals, which at the staffing level approved in the FY 1993 budget would leave some 350 to 400 employees requiring accommodation elsewhere. The objective, therefore, would be to acquire or construct another conveniently located building of a size sufficient to house this number of employees, and to provide a reasonable margin for such further growth as may occur in the Fund in the indefinite future. This suggests a building with some 300,000 to 400,000 sq. ft. of office space.

Several sites appear to be available in fairly close proximity to the Headquarters which would provide this amount of space. However, the one which most closely meets the Fund's needs, particularly in terms of proximity, is the PEPCO building. Containing approximately 365,000 sq. ft. of office space, it is located directly across H Street from the side of the Headquarters where Phase III would be constructed. Because this offers the possibility of developing a Headquarters complex spanning two adjoining blocks separated only by a narrow and relatively quiet side street, it seems to be a particularly attractive option, and one that most closely conforms to the established space strategy of the Fund. It has, therefore, been studied in considerably more detail than some of the other options discussed in this paper.

The PEPCO building is owned by George Washington University (GWU). PEPCO holds an extremely favorable lease that does not end until the year 2002, but if it knew in advance that it would be obliged to vacate the building as soon as the lease expired then PEPCO might well find it in its interests to move to a less expensive property while real estate prices are low. There is thus a reasonable prospect that, for a price, PEPCO could be induced to vacate the building by FY 1998, when the Phase III project is

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1/ EBAP/91/159--$8.3 million was appropriated for Phase III design and long-term space planning work. Of this, $5-6 million is for design work.

coming on stream. Though the building is basically sound, it would require extensive renovation to bring it to Fund standards.

Preliminary discussions indicate that the George Washington University could be induced to sell the land and building outright. However, the University views the site--which is on a prime location on Pennsylvania Avenue--as a desirable long-term investment and, most importantly, is very reluctant to reduce its campus area, which it has been expanding aggressively for some time, by selling the PEPCO block. The University, is therefore, asking a price for outright sale that is high, 1/ and while still less expensive than continuing to lease, is between 30 and 40 percent above its fair market value. On the other hand, the discussions do indicate a strong possibility of negotiating, at a reasonable cost, an arrangement under which the Fund could obtain the use of the land and building on terms comparable to ownership for a period of, say, 60-70 years. 2/ Financial analysis establishes that an arrangement could be worked out that would be significantly less expensive than continuing to lease commercially (GWU, like the Fund, is not subject to real estate tax), with a net present cost after 60 years of about half that involved in leasing. At 12.1 per cent, the internal rate of return would be broadly comparable to that generated by a conventional ownership arrangement.

Acquisition of the PEPCO building has been discussed at sufficient length with George Washington University to lead the Fund team to believe that it is a very real option. The advantages are considerable.

1. The attractiveness of PEPCO as an asset has been carefully appraised. Its location on Pennsylvania Avenue makes it a prime piece of real estate in the city, a property that will hold its value and an address that would make it easy to lease in whole or part should the Fund's requirements so dictate.

2. The location (it could most probably be connected to the Headquarters building by tunnel or skyway) is of particular importance. Not only would it be possible to service both buildings as one, the important interrelationships that need to be maintained between departments would be much enhanced as compared with the other, separate building options.

3. A sufficiently detailed space study has been conducted of this option (Phase III plus PEPCO) to make the following observations:

a. The expanded Headquarters building with PEPCO could house approximately 3,200 persons.

1/ Appendix III, Table 2.
2/ Several arrangements could be considered from a fixed period ground lease in which the University leases the land for 60-70 years and the Fund owns the building, to a sale of the land and building with a commitment to sell back following a given period.

b. A review of office layouts suggests that at existing staffing levels almost all operational staff could be housed in the expanded Headquarters building, with some vacant space distributed throughout for future expansion, reorganizations, etc. Thus, PEPCO could be used primarily to house the support and service departments, again with space for future expansion.

c. The total space provided by this option would accommodate the current demand of between 2,700 and 2,800 employees, and contains expansion space for some 400 to 500 additional employees.

d. The PEPCO building would be renovated and designed in a way that would permit subleasing of any excess capacity.

While the combined Phase III/PEPCO option would provide space for current needs plus expansion space for approximately 500 additional persons, the question remains whether that is sufficient for the long term. Discussions on space in the Fund have been marked by a reluctance to acknowledge the possibility that the Fund might grow further, and the growth forecasts that have found acceptance have often been unrealistically low. As a result, inadequate owned space has been provided, and the Fund has been forced to rely on the commercial rental market to meet its needs on a regular basis. However, now that the Fund has become a truly global institution, it seems reasonable to assume that the demand on its resources may soon reach a plateau, and that once the institution is fully equipped to meet this demand it will have reached a "steady state" manpower situation that will endure for the longer term. Other considerations lend support to the view that a Headquarters complex housing up to about 3,200 persons should be large enough to meet institutional needs on a long-term basis. For example: indications are that, as a result of widespread automation, gradual changes in work practices can be expected, that could reduce the demand for space. One such development currently being reviewed is the possibility of having some functions performed in the home. Even if this assessment proves unduly conservative, the development of such techniques as video-conferencing means that a discrete unit such as the Institute could, if necessary, be later relocated in premises of its own outside the Headquarters complex, without undue inconvenience. Given these trends, a scenario that envisages only a limited amount of further growth for the Fund (in terms of increasing demands for space) seems more realistic at this time than has hitherto been the case.

Alternatives to the PEPCO Building

If the Fund were unable to negotiate with George Washington University acceptable terms for acquiring the PEPCO building, there are other possibilities that could be explored. It would probably be possible, for example, to acquire and demolish two or three older buildings adjoining each other and on the site to build a satellite Headquarters building designed to house those staff who could not be accommodated in the expanded Headquarters building: a particular site has been identified on Pennsylvania Avenue which would seem broadly suitable for the Fund's purpose. The total cost, exclusive of Phase III itself, might be in the vicinity of $150 million. Unfortunately, the location would not be as convenient as in the case of PEPCO, since none of the sites that might be available are closer than three or four blocks from the main Headquarters. They thus share one of the drawbacks of the International Square building. Given the very real benefits that would accrue from expanding the main Headquarters and bringing back to a central location as many as possible of the departments now located outside, however, it is believed that completion of Phase III should be given the highest priority even if a satellite building has to be acquired in a less convenient location than PEPCO.

IV. Conclusions and Recommendations

The rationale for the space strategy that dictated the housing of all employees in a single building owned by the Fund in downtown Washington remains valid. Recent staffing increases, however, make it impossible to pursue that course using the current Headquarters building, even as expanded by Phase III. While the direct costs of moving the entire Headquarters to the suburbs make that option an attractive one on the surface, it is felt that the level of disruption and dislocation attendant upon that solution, and the absence of supporting infrastructure in the suburbs, are sufficient to offset the direct financial benefits. Similarly, the hard and soft costs attached to the current practice of housing overflows from the headquarters building in satellite offices some blocks from the Headquarters are not insubstantial, even if the Fund were to become the owner of the satellite offices. The option that comes closest to meeting the Fund's established objectives (all employees under one roof, in owned space in downtown Washington, D.C.) is to complete Phase III, and to supplement this by acquisition of the PEPCO building. In addition, as will be seen from Table 2, Appendix III, this option will minimize the capital outlays required to meet Fund space needs. If the Fund were to fail in acquiring the PEPCO building, the next best option would be to acquire or construct an alternative satellite building as close to the present Headquarters as possible, and sized to meet the Fund's needs.

It is, therefore, recommended that the Fund proceed with development of construction drawings for Phase III within the approved $8.3 million, it being understood that, subject to approval by the Board of a construction budget in about 15 months time, the Phase III addition remains at the core of the Fund's space strategy. In addition, approval is sought to enter into firm negotiations with George Washington University for the acquisition of the PEPCO building. To accomplish this, a budget of $200,000 is required to cover the legal, financial, and real estate consulting fees. It is proposed that the $8.3 million previously approved be increased to $8.5 million for this purpose. The intention would be to return to the Board later in the year with a specific proposal for the acquisition of the PEPCO building, assuming that reasonable terms can be negotiated, and if not then with an alternative proposal for meeting long-term space needs. 1/ Appendix IV reviews scheduling issues connected with this recommendation.

Appendices (4)

1/ A paper on the financial consequences of large capital expenditures, such as the Phase III construction project or the acquisition of PEPCO, will be issued in conjunction with the first of those proposals to be submitted for consideration by the Executive Board.

The Supply of and Demand for Space

Demand: Total Staff Resources Requiring Office Space FY 1993 (in staff years)			Supply: Design Capacity of Various Buildings (in staff resources housed) HQ	HQ Phase III	HQ Phase III PEPCO	HQ ISq.
Total Authorized Staff Resources 1/		2,567				
Additions:						
Executive Directors and their staff (inc. IBRD)	236					
Other resources requiring office space 2/	207					
Subtotal:	443					
Reductions:						
Staff not requiring office space 3/	(81)					
Experts in the field	(89)					
Replacement staff and overtime	(115)					
Subtotal:	(285)					
Net Additions	158					
Adjusted Total Demand		2,725	1,800	2,400	3,200	3,800
Space Surplus (deficit) FY 1993			(930)4/	(330)	470	1,070
Projections:						
FY 1998 with growth of 0.5 percent p.a.		2,793	(993)	(393)	407	1,007
of 1.0 percent		2,861	(1,061)	(461)	339	939

1/ EBAP 92/68, 3/25/92.
2/ Special Appointees, ADM & BCS vendors, contractuals charged to capital projects.
3/ Resident Representatives, Paris, and Geneva.
4/ The current space deficit is met by some overcrowding in the HQ building and by accommodating approximately 800 persons in leased space.

Design Capacity and Space Standards

As indicated in EBAP/91/159, 6/20/91, the total design capacity for the population of the Headquarters building with Phase III added, is approximately 2,400 persons. Several Executive Directors questioned whether that capacity could be expanded to house all staff then at International Square. In June 1991, the total of staff, contractuals, consultants, and vendors requiring housing was in excess of the 2,400 design capacity ceiling. The constraints on design capacity were thus reviewed to determine whether the expanded headquarters capacity could be increased significantly.

Building capacity is determined by several key factors, the most relevant being: (1) office size standards, and (2) building code requirements governing air ventilation and fire exit capacity. The factors are fundamentally interrelated and early in the process of designing a building, the owner and the architect make important decisions regarding each. In the case of the Fund's Headquarters building, when the Master Plan for Square 120 was being developed in the late 1960's, the Fund established objectives which would provide standard size offices for the various tasks to be performed as well as allowing for both ease of space planning and efficiency in implementing office renovations.

Reflecting these objectives, the Fund's architect designed floors two through thirteen of the Phase I and Phase II buildings with a unique 5 X 5 foot modular concrete ceiling system with the light fixtures, electrical wiring, and ductwork for the air ventilation system built in. In parallel with the design of this module, the Fund established a set of three interchangeable office size standards. 1/ Over the last 20 years, substantial economic and efficiency gains resulting from this concrete ceiling design have been realized by the Fund. One important benefit of this design is that it allowed the Fund to construct a building with 13 floors in 130 feet, the maximum height allowed by zoning, rather than 12 floors if a traditional "hung" ceiling were used. In addition, renovation costs in the Headquarters building average $10-15 per sq. ft., compared with $30 in the majority of modern buildings with hung ceilings, including International Square and the floors below the second floor in Headquarters. In addition, most typical office suites in Headquarters can be fully renovated over one weekend with little disruption to staff, whereas the same scope of work in a building with hung ceilings can take many months. However, the concrete modular ceiling system has one major drawback, namely the size of the ductwork that distributes air throughout the office space is literally fixed in concrete and, because its size cannot be increased, there is no means to distribute additional air supply. The Fund's architect has

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1/ The Fund's basic office size standards are: 10 X 15 foot office (150 sq. ft.) for A9-A15 staff; 15 X 20 foot office (300 sq. ft.) for B1-B4 staff; and, 20 X 20 foot office (400 sq. ft.) for Directors.

carefully examined this issue and concluded that the current system is at maximum output and cannot be increased. It should also be noted in this regard, while the building's ventilation system was designed for 1,800 people, the heat generating impact of computers was not foreseen. The ventilation system must now provide air for not only 1,800 people but also for close to 1,800 computers which has stretched the capacity considerably.

Another determinant of design capacity is related to safety and the speed at which a structure can be evacuated: specifically, the size of fire stairways and the number of fire exits on the ground floor of the building. The design of fire stairways and fire exits is calculated based on maximum population. While more fire exits could conceivably be constructed, it is not possible to increase the size or the number of fire stairways without (1) major expenditures and, (2) the loss of existing offices. It is these factors that determined the placement of major gathering places, such as the Meeting Hall and cafeteria, on the lower floors, for ease of evacuation in the event of fire or other emergency.

Despite the structural limitations to expanding design capacity, reduction of office size standards in order to accommodate more staff in the building has been analyzed. Over the past few years, in order to accommodate staff increases, office sizes have been reduced on a limited basis, primarily through the use of open plan furniture in lieu of closed offices, without materially affecting air ventilation and fire exiting regulations as they have been viewed as temporary conditions. Currently, over 100 persons work in offices or workstations that are smaller than standard. As a possible new scenario, a full space study has been undertaken, analyzing the gains that might be realized if the larger size offices were systematically reduced for staff at the B1-B3 levels, which number approximately 240. The concept was to reduce the 15 X 20 offices (300 sq. ft.), to 15 X 15 (225 sq. ft.), gaining 75 sq. ft. per office, for a total of 18,000 sq. ft. The theory does not work very well in practice. Only 50 additional 10 X 15 foot offices would result because much of the gain would have to be absorbed for circulation and outer office areas. The cost would be significant because of the extent of renovation that would be required.

Currently, the Headquarters building accommodates close to 2000 persons, 200 over design capacity. There is obviously some leeway in the theoretical design capacity ceiling and perhaps, with a change in office standards another 50 persons could be accommodated. The real limit is clearly being reached, however, and a substantial increase in the building's capacity cannot be viewed as a realistic alternative to the acquisition of additional space over the long term. 1/

1/ In discussing design capacity, the question of average per capita space utilization invariably arises. In responding, a variety of answers may correctly be given depending upon the basis of the calculation. One common measure used in commercial leasing is to divide the total square footage of each floor (less elevators and stairs) by the number of staff being housed. In the Fund, that average is relatively high because of the need to accommodate such support space as the Meeting Hall, training rooms, cafeteria and the Executive Dining Room, and a Visitors Center, in space that otherwise would be available for offices. Another measure is to delete the support space, looking only at the square footage of space that is in fact used for housing staff. Referring to the former concept as "gross" space utilization, and the latter as "net", the average per capita space usage for the Headquarters building plus International Square is 480 sq. ft. gross, and 270 sq. ft. net.

Table 1. Basic Data and Assumptions

Square footage of buildings (000 sq. ft.)

Net Office Space	Gross Building	
1,000	1,300	HQ space
400		Leased at I Square
350	410	Phase III building
365	580	PEPCO, 1900 Penn. Ave.
400	560	Other downtown building
1,000	1,400	Total I Square
1,900	2,700	Dulles corridor

Design capacity

Phase I and II	1,800 persons
Phase III	600 persons
PEPCO	800 persons
International Square	2,000 persons

Rent at International Square

$33 per sq. ft.

Landlord costs at International Square

$6 tax per net sq. ft.
$6 maintenance per net sq. ft.

Value of prime space in CBD (Central Business District)

$250 per net sq. ft.

Cost of site (per FAR sq. ft.)

$120 Washington CBD
$20 Dulles corridor ($10 purchase, $10 improvement)

Building costs (includes base costs, tenant build-out costs, soft costs)

$180 per gross sq. ft.

Suburban building site

$540M Acquisition and construction
($260M) Sale of Concordia and Headquarters
$280M Net cost

Phase III capital costs

$30M Site acquisition
$85M Construction and design

Pepco acquisition costs

- Lease for 60 years

  $120M acquisition, building upgrade and tenant buy-out

- Buy

  $150M acquisition, building upgrade and tenant buy-out

Residual value

0.5 percent p.a. real increase in value of land
2.0 percent p.a. real decrease in value of building

Long-term inflation rate of 4 percent
Rents keep pace with inflation
Discount rate of 7 percent in nominal terms.

Table 2. Cost Comparison and Return on Investment

	I. Sq. Lease	I. Sq. Invest 1/	I. Sq. Buy 2/	Suburb Build	PEPCO		Other Build	Phase III Build
					Buy	Long Term Lease		
				Cost of Lease/Purchase/Construction (in Millions of Dollars)				
Capital	0	-180.00	-120.00	-540.00	-150.00	-120.00	-168.00	-115.00
Year 1	-13.20	16.20	-2.40	-11.40	-2.19	-2.19	-2.40	-2.10
2	-13.73	16.85	-2.50	-11.86	-2.28	-2.28	-2.50	-2.18
3	-14.28	17.52	-2.60	-12.33	-2.37	-2.37	-2.60	-2.27
...	...	...	...					
60	-133.52	163.86	-24.28	-115.31	-22.15	-22.15	-24.24	-21.24
61 3/	0	1367.91	911.94	2324.44	914.06	0	1001.71	820.49
61 4/	0	130.03	86.69	220.96	86.89	0	95.22	78.95
				Cost Per Square Foot of Office Space Obtained				
Square feet of office space	400	600	400	1900	365	365	400	350
Net Pres. Value 5/	-841.41	663.62	-398.99	-400.16	-499.31	-460.24	-507.76	-424.29
Internal Rate of Return		13.0%	13.0%	13.5%	10.5%	12.1%	10.3%	12.2%

1/ That portion, 600,000 square feet, that would be leased commercially.
2/ That portion, 400,000 square feet that would house Fund staff.
3/ Residual value of site and building in nominal terms.
4/ Residual value of site and building in real terms.
5/ Using a discount rate of 7 percent.

Scheduling

The leases at International Square are currently phased in such a manner that 277,000 sq. ft. of the leasehold will be up for renewal in January 1998, when full occupancy of the Phase III addition is possible. The remaining space (96,000 sq. ft.) at International Square is leased to the year 2002. The staggered timing of the leases reflects the fact that Phase III is recognized as not providing sufficient space for the recent expansion of manpower.

As noted earlier, Phase III could be ready for occupancy by the end of 1995, and occupancy would take about 12 months and be completed during 1997. The acquisition and construction of a totally new Headquarters in the suburbs could also be completed within that same time frame. The PEPCO acquisition which, combined with Phase III is the preferred course of action, is somewhat more problematical. While it is likely that the acquisition could be accomplished during the course of FY 1993, and the renovation is estimated to require about two additional years, the cost/benefit of moving PEPCO out immediately will need to be examined. PEPCO will certainly require an incentive to leave that building before 2002 when its current lease expires. They do have an interest in breaking the lease early in order to take advantage of the depressed rental market in negotiating a long-term lease in much less expensive space. It is, therefore, anticipated that PEPCO could be induced to move out, and the building refitted, by the year 2000. The Fund would have to carefully weigh the costs of an earlier buyout, however, against needs, given the fact that the current leasehold at International Square extends to 1998 in part, and to 2002 for the remainder.