

## **Proposed Workforce Housing Development on City of San Diego Land**

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The purpose of this memorandum is to summarize the results of a research assignment focusing on the housing shortage in San Diego County as well as a suggested proposal to alleviate the shortage.

Last year, the San Diego chapter of Lambda Alpha International (LAI) created an internship program for a student at a local university to complete a research assignment which included a determination of how the use of underutilized city owned land could be developed with non-subsidized sale and rental housing and generate funds for the city to fund additional housing.

LAI is a land economics society. The membership of LAI includes outstanding individuals from many parts of the world who have distinguished themselves in all of the various disciplines and activities that relate to the use and re-use of land.

These individuals include not only those who are involved in the ownership, management, regulation and conservation of land, but also those who are involved in its development, redevelopment and preservation. The membership includes architects, engineers, real estate developers, planners, government officials, professors, bankers, attorneys, real estate consultants, and officials of organizations and national and international associations.

The diversity of this membership provides an unusual reservoir of talent, knowledge and expertise to draw upon for educational programs and discussions.

I would like to express my gratitude to Ian Gill and his team at Silvergate Development, Jesse Kleist with KB Homes, Nathan Moeder with London Moeder Advisors, Lin Martin with Perry Commercial and Alan Nevin with Xpera Group, all whom are members of the San Diego chapter of LAI and who provided me with development background that was critical input for the project underwriting and analysis.

The sources of data contained in this report include the City of San Diego, industry publications, San Diego Building Industry Association, building experts, developers, building industry consultants and LAI members.

## **Background**

Housing price appreciation in San Diego continues to significantly outpace wage growth. According to the National Association of Realtors (NAR) and a study released August 15, 2018 by mortgage website HSH, San Diego was one of the least affordable US metropolitan areas to purchase a home. The median home price is currently \$645,000 in the San Diego metro area according to NAR.

The HSH study concludes that San Diego is the third least affordable area out of the 50 studied in the U.S. and a homebuyer would need to make \$131,000 per year to qualify to purchase a median priced home assuming a 20% down payment, while the 2018 Area Median Income (AMI) for San Diego County is \$81,800 according to San Diego Housing & Community Development Services.

Based on the calculations by San Diego Association of Governments (SANDAG), San Diego County indicates a shortage of 100,000+ housing units. The housing shortage in San Diego consists primarily of workforce middle income housing both for sale and rental housing.

The lack of affordability in the for-sale housing arena is creating an unusual level of demand for apartments in San Diego County. In addition, there has been a long-time dearth of apartment construction due to the great recession resulting in extremely low vacancy rates while rents have dramatically increased.

HUD recently published a comprehensive market study of housing in San Diego County. The study concluded that the current demand for single-family homes is 6,333 units annually and for multi-family units 6,033 units, a total of 12,367 units annually.

## **Site Selection**

The methodology used to select the subject site for this study involved reviewing the list of city-owned parcels which are potentially underutilized and then setting criteria for site selection including parcel size, development potential and proximity to downtown, employers and mass transit. A summary of the inventory follows. This inventory does not include surplus land parcels owned by the San Diego Metropolitan Transit System.

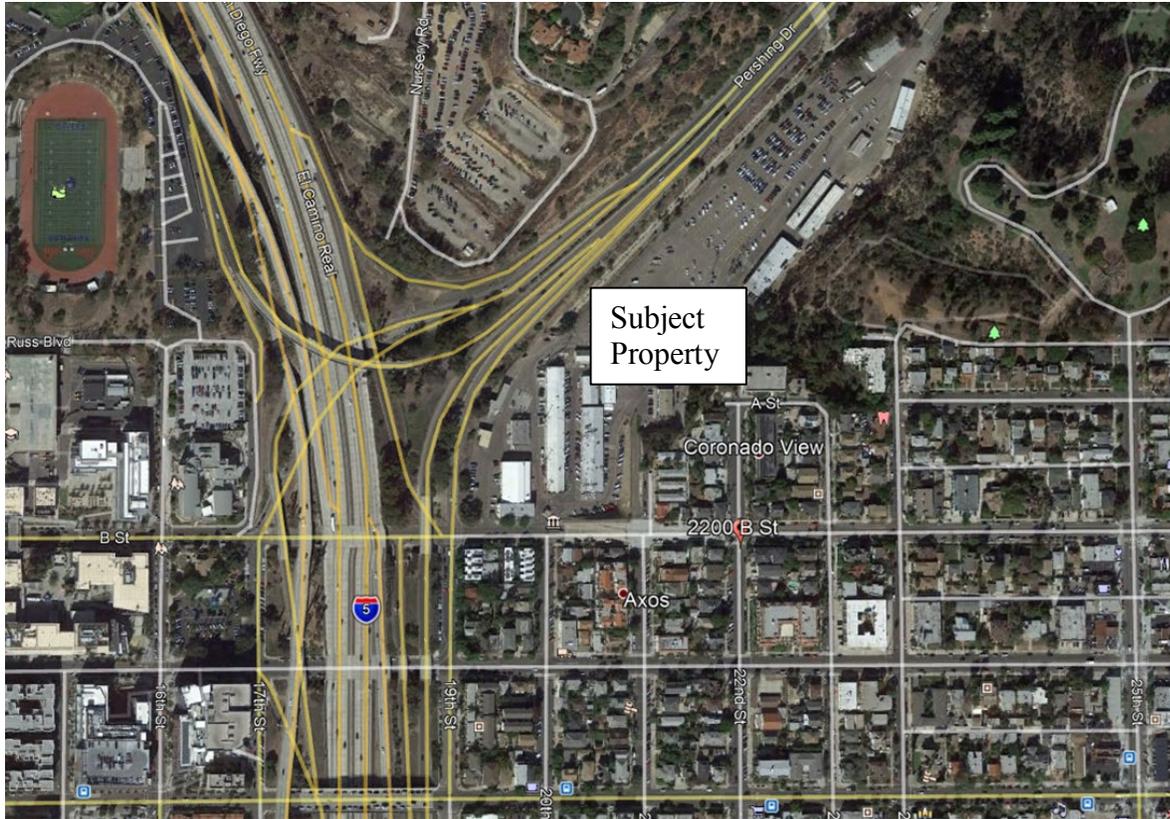
**Summary  
Developable City Owned Land  
City of San Diego  
as of Fall 2018**

<b>Designated Use</b>	<b>No. Parcels</b>
Commercial	2
Hold for Development	27
Hold for Study	33
Lease	13
Not designated	45
Sale Exclusive	33
Sale General	22
Sale Public Auction	13
Sale Specified	2
<b>Total</b>	<b>190</b>

Note: excludes land designated as water drainage, etc.  
Source: City of San Diego

The City-owned site selected for this study contains approximately ten acres and is located at 20<sup>th</sup> and B Street, San Diego. The current use of the subject site is a maintenance yard for city vehicles and not presently designated for residential use.

The City has not been contacted to ascertain the availability of the property.



## Study Methodology

The basis for the study was to determine the benefits of using City-owned land for residential development. This analysis includes both rental and sale townhome product.

It was assumed that the City would contribute the land to the developer at a zero basis. With the land at a zero basis, the rent for apartments and price for sale housing could be produced for substantially less than if the developer would had to pay market prices for the land.

When the development (apartment project or individual townhomes) are eventually sold, the city would recapture the value of the initial land contribution as well as a portion of the profits. The City would then be able to use those funds to produce additional housing.

The methodology to estimate land values uses a land residual analysis which is detailed on the attached For Sale and For Rent pro formas.

The analysis involves estimating a market value of the For Sale units based on market comparables and a value of the For Rent units based on market comparables, market rents, expenses, and capitalization rates.

The total project costs are estimated to include construction costs, development fees, professional fees (architect, engineers, etc.), financing costs, on-site and off-site development costs, and a market rate developer profit.

The difference between the market value of the project and the total costs (without land) results in a land residual value.

The proposed housing development is one hundred For Sale townhomes and two hundred For Rent apartments on ten acres outlined as follows:

### **For Sale Townhomes**

The townhome pro forma demonstrates new For Sale product delivered below the area median home price and providing the city with a significant upside on land value compared to its current use as a maintenance yard.

The exhibit below shows that the 1,750 square foot homes, absence the residual land value, could be sold for \$455,286, or \$260 per square foot, significantly below market-rate housing of a similar type.

Assuming twenty units per acre on five acres, the For Sale project generates a residual land value of \$69,872 per unit, \$1,397,444 per acre or \$32.08 per square foot.

The \$32.08 per square foot value is a significantly higher value than the value of the land in its current use as a maintenance yard. Industrial land values in San Diego currently range approximately for \$12 - \$18 per square foot based on data provided by Cushman and Wakefield.

A detail analysis of the pro forma appears in the Appendix of this report.

**Summary: Townhome Development  
City-Owned Land  
20th & B Street ProForma**

Land Area (Acres)	5	
No. Units	100	
Units/Acre	20	

	Per Unit	Total
Avg. Unit Sq.Ft.	1,750	175,000
<b>Sales Price - Market Rate</b>	<b>\$ 525,000</b>	<b>\$ 52,500,000</b>
Price/Sq.Ft.	\$ 300	\$ 300
		-
Direct Costs	\$ 331,303	33,130,300
Closing Costs	\$ 23,625	2,362,500
G&A	\$ 27,626	2,762,606
Sales & Marketing	\$ 18,750	
Finance Costs	\$ 23,982	2,398,200
Total Costs w/o Land	\$ 425,286	42,528,606
Developer Profit (Fixed)	\$ 30,000	3,000,000
Total Cost w/o Land	\$ 455,286	45,528,606
Land Value (Residual)	\$ 69,872	6,987,221
Per Acre	\$ 1,397,444	
Per Sq.Ft.	\$ 32.08	

<b>Home Sale Price w/o Land</b>	<b>\$ 455,286</b>
<b>Home Price/Sq.Ft.</b>	<b>\$ 260</b>

### Market-Rate Apartments

The apartment pro forma demonstrates delivery of two hundred apartments providing much needed workforce housing to a market with vacancy rates at record lows.

The apartments, absence the cost of land, could be rented for \$2.50 per square foot, \$.50-1.00 per square foot less than new downtown apartment units.

Assuming a density of fifty units per acre on four acres and rents of \$2.50 per square foot, the project generates a residual land value of \$61,286 per unit or \$12,257,267.

**Summary: Apartment Development  
City-Owned Land  
20th & B Street ProForma**

Land Area (Acres)	4	
No. Units	200	
Units/Acre	50	

Unit Type		Rent psf	Monthly Rent
Studio	20%	\$2.50	\$1,650
1Bed/1Bath	30%	\$2.50	\$2,200
2Bed/2Bath	50%	\$2.50	\$2,750
Total	100%		

	Per Unit	Total
Avg. Unit Sq.Ft.	860	172,000
Effective Gross Income	25,026	5,005,200
NOI	16,767	3,353,484
Capitalization Rate	4.5%	4.5%
<b>Capitalized Value</b>	<b>\$ 372,609</b>	<b>\$ 74,521,867</b>
Price/Sq.Ft.	\$ 433	\$ 433
<b>Total Costs w/o Land</b>		
Direct Costs	\$ 257,685	51,537,000
Marketing G&A	\$ 15,461	3,092,200
Finance Costs	\$ 18,177	3,635,400
Total Costs w/o Land	\$ 291,323	58,264,600
Fixed Development Fee	\$ 20,000	4,000,000
<b>Total Costs w/o Land, including Development Fee</b>	<b>\$ 311,323</b>	<b>62,264,600</b>
<b>Land Value (Residual)</b>	<b>\$ 61,286</b>	<b>\$ 12,257,267</b>
<b>Total Costs with Land</b>	<b>\$ 372,609</b>	<b>74,521,867</b>

<b>Apt. Cost w/o Land</b>	<b>\$ 311,323</b>	<b>\$ 62,264,600</b>
<b>Apt. Cost w/o Land per Sq.Ft.</b>	<b>\$ 362</b>	<b>\$ 362</b>

The rental and sale projects combined will generate a residual land value at time of completion of \$19,234,414.

<b>Residual Land Value at Time of Completion Sale and Rental Projects 20th &amp; B Street</b>			
<b>Project</b>	<b>No. Units</b>	<b>RLV Per Unit</b>	<b>Total</b>
Sale	100	\$ 69,872	\$ 6,987,221
Rental	200	\$ 61,236	\$ 12,247,193
<b>Total</b>	<b>300</b>	<b>\$ 64,115</b>	<b>\$ 19,234,414</b>

As an example of the revenue that the City could obtain by contributing this parcel of land, we calculated the increase in value at a pace of 3.0% annually for ten years. At that point, we “sold” the properties, returning the residual land value to the City and then divided the sale profit 50/50 with the property owner.

The total revenue that the City would receive at that 10-year sale totals almost \$30,000,000. In addition, they would have received property taxes as well as the initial fees that the City levies on new construction.

**Estimated Value at Time of Sale - 10 Years  
Sale and Rental Properties  
20th and B Streets**

	For Sale Townhomes		Apartments	
	Per/Unit	Total	Per/Unit	Total
No. Units		100		200
Estimated Value at Completion	\$525,000	\$52,500,000	\$372,609	\$74,521,867
Appreciation Rate	3.0%	3.0%	3.0%	3.0%
Years	10	10	10	10
Total Increase in Value	30.0%	30.0%	30%	30%
Future Value	\$682,500	\$68,250,000	\$484,392	\$96,878,427
Estimated Appreciation	\$157,500	\$15,750,000	\$111,783	\$22,356,560
City's Land Residual (Recaptured)	\$69,872	\$6,987,221	\$61,236	\$12,247,193
<b>Total Appreciation for Homeowner &amp; Apt. Developer</b>	<b>\$87,628</b>	<b>\$8,762,779</b>	<b>\$50,547</b>	<b>\$10,109,367</b>

<b>City Land Value in 10 Years</b>				
Recapture of LRV	\$69,872	\$6,987,221	\$61,236	\$12,247,193
<b>Percent of Appreciation in Value</b>	50%	50%	50%	50%
Total Appreciation	\$87,628	\$8,762,779	\$50,547	\$5,054,684
City Participation in Upside	\$43,814	\$4,381,390	\$25,273	\$5,054,684
<b>Total City Benefit</b>	<b>\$113,686</b>	<b>\$11,368,610</b>	<b>\$86,509</b>	<b>\$17,301,876</b>
<b>Total City Benefit - Apts &amp; TH</b>				<b>\$28,670,487</b>

Development of the subject site provides a means of achieving important goals for the city of San Diego:

- adds three hundred new housing units which incrementally moves the City towards its housing goals;
- providing affordable housing close to downtown, employers and transit;
- helping to meet Climate Action Plan (CAP) goals by placing housing close to transit and employers;
- Substantially increases the property tax for the new property owners;
- The project will pay full property taxes (which supports the schools);
- Will pay more than \$11,000,000 to the City for fees and exactions; and

- maximizing the monetary value of a non-revenue producing city asset by realizing approximately \$30,000,000 that can be applied to new residential development of “work force” housing.

In conclusion, repurposing the existing use of city owned land to workforce housing is beneficial to City of San Diego residents by providing affordable much needed supply in closer proximity to employment and is beneficial to the city by maximizing value of city land and generating revenue which can be utilized to provide additional housing.

**Appendix – Detailed Development Exhibits**

**Detailed ProForma  
Apartment Project  
20th & B Street**

**Apartments**

<u>Land Allocation</u>	
For Sale Townhomes	5 Acres
Apartments	4 Acres
Common Area 10%	1 Acre
<b>Total Land</b>	<b>10 Acres</b>

Unit Type	# of Units	Unit SF	Total SF	Rent psf	Monthly Rent	Annual Rent
Studio 20%	40	600	24,000	\$2.50	\$1,500	\$720,000
1Bed /1Bath 30%	60	800	48,000	\$2.50	\$2,000	\$1,440,000
2Bed/2Bath 50%	100	1000	100,000	\$2.50	\$2,500	\$3,000,000
<b>Total 100%</b>	<b>200</b>		<b>172,000</b>			<b>\$5,160,000</b>
<b>Average</b>		<b>860</b>				

**INCOME & EXPENSES**

Annual Rent		\$5,160,000
Vacancy	3%	<u>\$154,800</u>
Effective Gross Income		\$5,005,200
Operating Expenses	33%	<u>\$1,651,716</u>
Net Operating Income		<u>\$3,353,484</u>
Market Value at CAP Rate	4.5%	<u>\$74,521,867</u>

Value/Unit \$372,609

Direct Cost

Base Constructiton psf (1)	\$215	\$184,900
Fees (2)		\$33,434
Property Tax (3)		\$4,471
Site Development psf/site (4)	\$20	\$17,424
Insurance & Bond		\$3,500
Consultants/Architects/Engineers		<u>\$14,000</u>
Total Direct Cost		\$257,729

Marketing/G&A

Marketing/lease up Costs		\$500
Field Overhead (5)	2%	\$5,155
Developer Fee/Overhead	4% of direct costs	<u>\$10,309</u>
Total Marketing/G&A		\$15,464

Finance Costs

Interest Expense (6)		\$14,072
Due Diligence Costs		\$500
Loan Fee. (7)		<u>\$3,608</u>
Total Finance Costs		\$18,180

Total Costs w/o Land/Dev Margin		\$291,373
Land Value (residual)		<u>\$61,236</u>
Total Costs with Land Value		\$352,609

Developer Margin	Fixed Developer Margin	\$20,000
<b>Value/Unit</b>		<b><u>\$372,609</u></b>

(2) Fees cacluated on a per unit base		per unit
Development Impact Fees(8)		\$13,555
Transportation Fees (9)		\$2,314
Inclusion Affordable Housing Fee psf (10)	\$10.82	\$9,305
City permit fees (11)		\$775
Water and Sewer(12)		\$4,733
School psf (13)	\$3.20	<u>\$2,752</u>
Total		<b><u>\$33,434</u></b>



**Detailed ProForma  
For Sale Townhomes  
20th & B Street**

<u>Land Allocation</u>	
<b>For Sale Townhomes</b>	<b>5 Acres</b>
Apartments	4 Acres
Common Area 10%	1 Acre
<b>Total Land</b>	<b>10 Acres</b>

	<u>Townhomes</u>	
	<u>per unit</u>	<u>total</u>
		5 acres
Number of Homes	20/acre	100
Square Footage	1,750	175,000
Sales Price	\$525,000	\$52,500,000
Base Price Per Sq Ft	\$300	
<b>Revenues and Expenxe Summary</b>		
<u>Revenues</u>		
Sales Price	\$525,000	\$52,500,000
<u>Direct Cost</u>		
Base Construcion psf (1)	\$120	\$210,000
Fees (2)		\$49,553
Property Tax (3)	1%	\$5,250
Site Development (4)		\$35,000
Insurance & Bond		\$6,000
Consultants/Architects/Engineers		\$15,000
Warranty	2%	\$10,500
<b>Total Direct Cost</b>		<b>\$331,303</b>
<u>Closing Costs</u>		
Closing Costs	0.5%	\$2,625
Internal Commissions	2.5%	\$13,125
External Commissions	1.5%	\$7,875
<b>Total Closing Costs</b>		<b>\$23,625</b>
<u>Construction/Project G&amp;A</u>		
Field OH (5)	2%	\$6,626
G&A/MNGT Fee	4%	\$21,000
<b>Total G&amp;A and Field</b>		<b>\$27,626</b>
<u>Sales &amp; Marketing</u>		
Sales and Marketing	3%	\$15,750
Model & Sale Office		\$3,000
<b>Total G&amp;A Costs</b>		<b>\$18,750</b>
<u>Finance Costs</u>		
Interest Expenxe (6)		\$20,673
Due Diligence Costs		\$500
Loan Fee (7)		\$2,650
<b>Total Finance Costs</b>		<b>\$23,824</b>
<b>Total Costs w/o land</b>		<b>\$425,128</b>
<b>Developer Profit (Fixed)</b>		<b>\$3,000,000</b>
<b>Total Costs including Dev. Profit</b>		<b>\$45,512,779</b>
<b>Land Value (residual)</b>		<b>\$69,872</b>

<u>(2) Fees on per unit basis</u>		<u>per unit</u>
Developer Impact Fee (8)		\$13,555
Transportation Fee (RTCIP) (9)		\$2,314
Affordable Housing Fee psf (10)	\$10.82	\$18,935
City permit fees (11)		\$1,978
Water and Sewer (12)		\$7,171
School 3.20psf (13)		\$5,600
<b>Total</b>		<b>\$49,553</b>

	<b>Footnotes for Townhomes</b>			
	(1) Construciton psf estimate per KB homes			
	(3) Estimate during construction 1% of value			
	(4) Estimate per KB Homes			
	(5) 2 % of Direct Costs			
	(6) Interest Expencc assumes Loan Amount 80% of Direct Costs, Interest			
	(7) Estimate 1% of loan amount (80% of direct costs)			
	(8) San Diego Planning Department Fiscal Year 2019 Impact Fee Schedule page 2 Golden Hill			
	(9) San Diego Planning Department Fiscal Year 2019 Impact Fee Schedule page 3			
	(10) City of San Diego Developmental Services Department Inclusionary Affordable Housing July 2018 Informational Bulletin 532			
	(11) BIA Schedule page 32			
	(12) City of San Diego Water and Sewer Fees Public Utilites Department			
	(13) BIA Schedule page 52			

**Curriculum Vitae**  
**Jack Ryan**  
**Burnham Moores Center for Real Estate**

Jack is attending the University of San Diego and is planning on graduating in the fall of 2019 with a major in Business Administration and a double minor in Accounting and Art. He holds a California Department of Real Estate Salesperson License for the past two years and has successfully closed several residential real estate transactions and is working towards obtaining his Broker's license.

He has also worked with his father who is a real estate investor/developer in Northern California. Jack enjoys outdoor sports of surfing, skiing, hunting and fishing and has been on the USD Golf Club, the Accounting Society and has played four years of Rugby with Rugby clubs and USD.

