MEMORANDUM

To: Sara Lillevand, City Administrator
Kevin Jackson, Planning and Building Director

From: Ashleigh Kanat and Snow Zhu

Subject: Civic Center Housing Strategic Considerations; EPS #221053

Date: Revised October 24, 2022

The Economics of Land Use

Economic & Planning Systems, Inc.
1330 Broadway
Suite 450
Oakland, CA 94612
510 841 9190 tel

Oakland
Sacramento
Denver
Los Angeles

www.epsys.com

Economic & Planning Systems, Inc. (EPS) has been retained by the City of Piedmont (City) to evaluate the feasibility of developing Moderate or Above Moderate-income housing on a City-owned site located in the Civic Center. The analysis will inform a decision whether to include the site in the Site Inventory of the 6th Cycle Housing Element update.

The site, 801 Magnolia Avenue (0.31 acres), is shown in **Figure 1** and is adjacent to 120 Vista Avenue (0.83 acres). Both sites are currently improved with civic facilities. The Piedmont Center for the Arts is located at 801 Magnolia, and City Hall, the police and fire stations, and Veteran's Memorial Hall are located at 120 Vista. Each of these facilities is in need of substantial upgrade and modernization, if not full redevelopment. The City, thus, has the dual objectives of identifying sites to meet 6th Cycle RHNA and redeveloping its core civic facilities.

Background and Context

To meet requirements set forth by the 6th Regional Housing Needs Allocation cycle (2023-2031), the City must identify sites with capacity for 587 units, comprised of 163 Very Low-income units, 94 Low-income units, 92 Moderate-income units, and 238 Above Moderate-income units.

On August 1st, City Council considered whether 120 Vista Avenue and 801 Magnolia Avenue should be included in the Sites Inventory of the Housing Element. EPS presented a "Civic Center Housing Feasibility Analysis" memorandum that discussed the feasibility of accommodating 40 Low-income units and 13 Moderate-income units on the City-owned parcels, in addition to the civic uses.

The outcome of the August 1st meeting was direction from City Council to Staff to further explore the feasibility of 13 to 18 Moderate or Above Moderate-income units at 801 Magnolia. At 0.31 acres, achieving 13 to 18 units requires a density of about 42 to 58 units per acre. Building on the prior analysis, this memorandum discusses the feasibility of this scenario and describes several strategic considerations.

Figure 1 120 Vista Avenue and 801 Magnolia Avenue

Key Findings

1. While new residential development of 13 to 18 units could fit at 801 Magnolia at densities that would not require higher than five stories, the project would not be an attractive opportunity to an affordable housing developer. An affordable housing developer would be seeking deeper levels of affordability to access funding and a minimum of 30+ units to achieve economies of scale and development efficiencies.[1]

2. At the Moderate-income level, a developer would find a 13- to 18-unit housing project infeasible. The analysis demonstrates that even at moderate-income levels, there is an affordability gap, resulting in a negative or low (i.e., positive but below market) residual land value, and the small size of the project does not achieve the required economic efficiencies.

3. At the Above Moderate-income level, a developer may find a 13- to 18-unit project to be feasible. The analysis results in a positive residual land value, with a per acre land value that is consistent with Bay Area land transactions. However, a project of so few units is unlikely to result in a land payment (envisioned as a capitalized ground lease) that would contribute meaningfully to the redevelopment of the civic center.

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[1] Recent conversations with a range of affordable housing developers indicate that affordable housing developers typically seek opportunities that allow for at least 60 to 75 units to create economies of scale, both in terms of construction and operations. That said, one developer indicated a minimum of 30 units would provide sufficient scale, while another developer indicated they are seeking sites that offer minimum capacity of 100 units, suggesting a broad range.

4. Taking the time during this planning cycle to complete a Civic Center Master Plan that seeks to accommodate redeveloped civic facilities and below-market rate housing prior to committing to the disposition of 801 Magnolia will allow the City to optimally plan to meet both objectives.

Feasibility Analysis

To consider whether the 13 to 18 Moderate or Above Moderate-income units could be built on the 801 Magnolia Avenue parcel, EPS evaluated feasibility from a physical, design, and financial perspective.

Physical and Design Feasibility

Assuming the Piedmont Center for the Arts is demolished, the 0.31-acre parcel at 801 Magnolia Avenue can physically accommodate 13 to 18 units of housing at a density of 42 to 58 units per acre. It is further possible that the Center for the Arts could be integrated into the design of the new housing or it could be accommodated as part of a redeveloped civic center sites at 120 Vista.

As an example, housing development at 42 units per acre could resemble 2-story townhomes with patios and some shared green space. At 58 units per acre, housing development could be a 3 to 4-story apartment building with ground floor retail or shared community space. The exact physical configuration of the housing units would vary depending on design choices. For example, a skilled architect could work with the site topography and setbacks to improve cohesion with the existing neighborhood and surrounding buildings.

Financial Feasibility

EPS was asked to evaluate the potential for housing development on 801 Magnolia Avenue at Moderate (up to 120 percent of Area Median Income) and Above Moderate-income levels (greater than 120 percent of AMI, which is, effectively, market rate). It is highly unlikely that an affordable housing developer would pursue a project aimed at moderate-income households because there are very few funding resources and no tax credit opportunities to help address moderate-income housing. The following analysis, therefore, assumes participation of a for-profit, market-rate developer.

The following analysis solves for what is referred to as the residual land value. The residual land value reflects the amount the developer would be able to pay for the land based on the prospective economics of the development. A negative residual land value means that the developer would not be able to pay for the land and may even require some subsidy on the vertical construction. A positive residual land value may be an indication of feasibility if the land owner is willing to sell (or negotiate a ground lease) at the resulting value. Typically, the residual land value not only needs to be positive but needs to be sufficiently positive to incentivize the sale or disposition of the land.

<u>Moderate Income</u>

At the Moderate-income level, the prior EPS study[2] found an affordability gap, meaning that the cost to construct a Moderate-income housing unit is greater than the value of the unit based on the rents a Moderate-income household can afford.[3] As shown in **Figure 2**, a pro forma analysis of a 13-unit project returns a negative residual land value, and an 18-unit Moderate income projects shows a low

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[2] EPS memorandum "Civic Center Housing Feasibility Analysis" presented at August 1, 2022 City Council meeting.
[3] Assumptions discussed in EPS memorandum "Civic Center Housing Feasibility Analysis" presented at the August 1, 2022 City Council meeting.

residual land value of $1.6 million per acre. In Piedmont, an acre of residentially-zoned land in the Civic Center is worth more than $1.6 million. There are not a lot of appropriate land value comps available, but an acre of residentially-zoned land in Piedmont would be expected to cost between $5 and $10 million. Given the negative, low residual land values for both scenarios, a Moderate-income housing project of 13 to 18 units is *infeasible* without additional funding sources or other development incentives.

Above Moderate

At the Above-Moderate income level, EPS found no affordability gap, meaning the rents that an Above Moderate-income household can afford translate to a unit value that would cover the cost to construct an Above Moderate-income housing unit.[4] Since Above-Moderate units function effectively as market-rate units, and there are no funding resources for Above-Moderate-income housing, it would be a market-rate developer, not an affordable housing developer, that would carry out the project.

As shown in **Figure 3**, a pro forma analysis of a 13-unit and 18-unit, Above-Moderate project shows sufficient residual land values for feasibility.[5] In the Above-Moderate project scenarios of 13 and 18 units, the residual land value is about $7.7 million and $14.3 million respectively, which is consistent with the sales prices of recent residential land transactions in the Bay Area.

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[4] EPS memorandum "Civic Center Housing Feasibility Analysis" presented at August 1, 2022 City Council meeting.

[5] Assumptions discussed in EPS memorandum "Civic Center Housing Feasibility Analysis" presented at the August 1, 2022 City Council meeting.

Figure 2 Pro Forma for 13 to 18 Units of Moderate-Income Housing

DEVELOPMENT PROGRAM ASSUMPTIONS	ASSUMPTION/FACTOR		13 UNITS	18 UNITS
Development Site (Square Feet)			13,504	13,504
Dwelling Units			13	18
Gross Building Area (Square Feet)	950	GBA / DU	12,350	17,100
Net Rentable Square Feet	90%	Efficiency Factor	11,115	15,390
Total Parking Spaces	1.5	Spaces / DU	20	27
Surface Parking Spaces	0%	of total parking	0	0
Structured Parking Spaces	100%	of total parking	27	27
BUILDING OPERATING INCOME (ANNUAL)	**ASSUMPTION/FACTOR**		**TOTAL**	**TOTAL**
Gross Potential Rent	$4.51	per SF/Month	$601,544	$832,907
Losses to Vacancy	3.0%	of Gross Income	-$18,046	-$24,987
Gross Residential Revenue			$583,497	$807,920
Operating Expenses	$12,000	per Unit/ Year	-$156,000	-$216,000
Net Operating Income (NOI)			$427,497	**$591,920**
Value of Units	**4.5%**	**Cap Rate**	**$9,499,944**	**$13,153,769**
PROJECT DEVELOPMENT COSTS	**ASSUMPTION/FACTOR**		**TOTAL**	**TOTAL**
Construction Cost				
Basic Site Work	$50	per SF (Site)	$675,180	$675,180
Building Direct Cost	$400	Cost/SF (GBA)	$4,940,000	$6,840,000
Surface Parking Direct Cost	$5,000	per Space	$0	$0
Structured Parking Direct Cost	$50,000	per Space	$1,350,000	$1,350,000
Total Construction Cost			*$6,965,180*	*$8,865,180*
Indirect Costs	25.0%	of Direct Costs	*$1,741,295*	*$2,216,295*
Developer Return	14.0%	of Direct & Indirect Costs	*$1,218,907*	*$1,551,407*
Total Project Cost			**$9,925,382**	**$12,632,882**
			13 UNITS	**18 UNITS**
Residual Land Value			**-$425,437**	**$520,887**
Residual Land Value per Acre			*-$1,372,379*	*$1,680,282*

Source: CA HCD; Alameda County; Economic & Planning Systems, Inc.

Figure 3 Pro Forma for 13 to 18 Units of Above Moderate-Income Housing

DEVELOPMENT PROGRAM ASSUMPTIONS	ASSUMPTION/FACTOR		13 UNITS	18 UNITS
Development Site (Square Feet)			13,504	13,504
Dwelling Units			13	18
Gross Building Area (Square Feet)	950	GBA / DU	12,350	17,100
Net Rentable Square Feet	90%	Efficiency Factor	11,115	15,390
Total Parking Spaces	1.5	Spaces / DU	20	27
Surface Parking Spaces	0%	of total parking	0	0
Structured Parking Spaces	100%	of total parking	27	27
BUILDING OPERATING INCOME (ANNUAL)	**ASSUMPTION/FACTOR**		**TOTAL**	**TOTAL**
Gross Potential Rent	$5.64	per SF/Month	$752,263	$1,041,595
Losses to Vacancy	5.0%	of Gross Income	-$37,613	-$52,080
Gross Residential Revenue			$714,650	$989,515
Operating Expenses	$12,000	per Unit/ Year	-$156,000	-$216,000
Net Operating Income (NOI)			$558,650	**$773,515**
Value of Units	**4.5%**	**Cap Rate**	**$12,414,445**	**$17,189,232**
PROJECT DEVELOPMENT COSTS	**ASSUMPTION/FACTOR**		**TOTAL**	**TOTAL**
Construction Cost				
Basic Site Work	$50	per SF (Site)	$675,180	$675,180
Building Direct Cost	$400	Cost/SF (GBA)	$4,940,000	$6,840,000
Surface Parking Direct Cost	$5,000	per Space	$0	$0
Structured Parking Direct Cost	$50,000	per Space	$1,350,000	$1,350,000
Total Construction Cost			*$6,965,180*	*$8,865,180*
Indirect Costs	25.0%	of Direct Costs	*$1,741,295*	*$2,216,295*
Developer Return	15.0%	of Direct & Indirect Costs	*$1,305,971*	*$1,662,221*
Total Project Cost			**$10,012,446**	**$12,743,696**
			13 UNITS	**18 UNITS**
Residual Land Value			**$2,401,999**	**$4,445,536**
Residual Land Value per Acre			*$7,748,384*	*$14,340,438*

Source: CA HCD; Alameda County; Economic & Planning Systems, Inc.

Strategic Consideration

Given the infeasibility of a small Moderate-income project and the feasibility of a small Above Moderate-income project, the City will want to consider if offering City-owned land for Moderate or Above-Moderate units is the best use of publicly-owned land given the depth of need in the lower-income categories.

Housing developers are often interested in building on City-owned and controlled parcels, which allow for more flexible zoning (e.g., height, setbacks, parking requirements) and allow the developer and the City to negotiate directly around structuring a land payment and work towards a shared goal of providing affordable housing or housing in general.

At the same time, the City will be in a position to be explicit about what it is seeking if/when it offers 801 Magnolia (or any other City-owned site) for housing. The City can decide if it wants to offer the land for below market consideration to be a partner in trying to achieve more affordable housing or if full market value for the land is required. Similarly, the City can specify the number of units it expects, the size of the units, the affordability targets, any special populations to be served (seniors, families, disabled, etc.). These terms may need to be further negotiated with a selected developer, but the City can express its objectives in a Request for Offers (RFO) or a Request for Proposals (RFP).[6]

Because City-owned/controlled land is valuable, and because affordable housing at the deepest levels requires all the tools in the toolbox (including below-market consideration for land), the City will need to make a policy decision if offering City-owned land for Moderate or Above-Moderate housing is a good use of a scarce and finite resource.

If the City is interested in having Moderate-income units at the 801 Magnolia Avenue site, one alternative scenario is to consider a housing development composed of mostly Above Moderate or market-rate units and a few Moderate units. The revenues from the Above Moderate or market-rate units would effectively subsidize the comparatively lower rents in the Moderate units. Resulting revenue from the land could be used to partially fund Civic Center renovations; however, as demonstrated in Figures 2 and 3, the amount that could be available to put towards the Civic Center is not likely to exceed $5 million. At the same time, if 801 Magnolia is included in the Sites Inventory and made available for housing, it would no longer be available to be part of a more comprehensive Civic Center Master Plan.

Recommendation

Given the complexities described above, EPS recommends the City exclude 801 Magnolia (and 120 Vista) from the Sites Inventory at this time and instead include a program in the Housing Element to prepare a Civic Center Master Plan that includes the incorporation of affordable housing as a primary objective of the Plan. As part of the master planning process, the City will seek to optimize the configuration of both parcels to achieve the dual objectives of civic uses and new affordable housing.

When the Master Plan is completed in the next planning cycle, the City can proceed with identifying an appropriate development partner. Any units that are developed during the 6th Cycle will count

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[6] A senior-housing project would not be eligible for the state density bonus of 20 percent unless it is at least 35 units or greater. (https://www.meyersnave.com/wp-content/uploads/California-Density-Bonus-Law_2021.pdf)

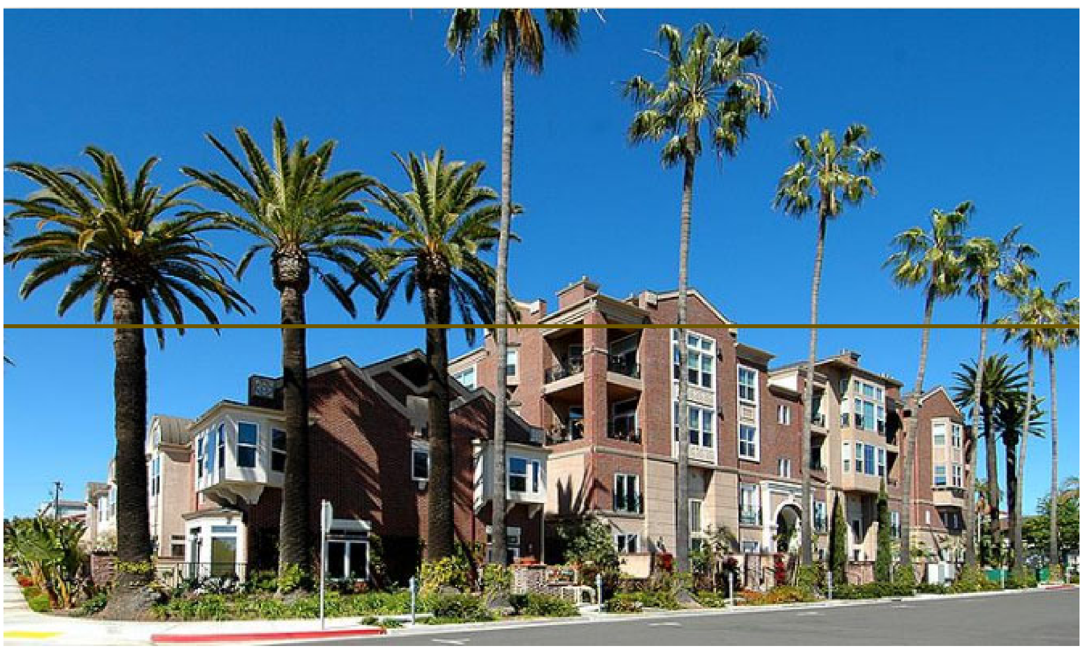
towards the City's RHNA. If development of the units does not occur during the 6th Cycle, at a minimum, the site planning will have occurred, and the parcel(s) can be included in the 7th Cycle Sites Inventory.

APPENDIX A:
Examples - Visualizing Density

Figure A-1: Multifamily at 26 to 40 Units per Acre *(with surface parking, tuck-under rear parking, or parallel on-street parking)*

Source: JHP Architecture

Figure A-2: ~~Multifamily~~ Condominiums at Approximately 49 Units per Acre *(with underground parking)*



Source: M.W. Steele Group and City of San Diego Planning Department

Figure A-3: Multifamily at 55 Units per Acre *(with multi-level parking structure)*

Source: CalCities, page 26.

Figure A-4: Multifamily at 44 to 75 Units per Acre *(with multi-level parking structure)*

Source: JHP Architecture