



City of South San Francisco

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Legislation Text

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Item #: 14.

Study Session regarding a ballot measure to adopt an ordinance authorizing the City of South San Francisco to develop, construct, or acquire affordable, low-rent housing units pursuant to Article XXXIV of the California Constitution, subject to the approval of the voters. (*Sky Woodruff, City Attorney and Mike Futrell, City Manager*)

RECOMMENDATION

Staff recommends the City Council review and consider the provided analysis on the development, operation and maintenance of low-rent housing by the City as possible under an Article 34 authorization and direct staff on next steps.

BACKGROUND

At the City Council study session on February 16, 2022, ECD staff and the City Attorney's Office presented a draft ballot measure regarding Article 34 authorization which, if approved by the voters, would authorize the City to develop, construct, or acquire low-rent housing for a period of thirty (30) years. The City Council provided direction to move forward with placing the proposed measure on the November 2022 election ballot, but directed that the proposed percentage of housing units allocation that may be authorized by the proposed measure to be referred to the Housing Standing Committee for further review and comments. The City Council also desired to further understand the methodology used to determine the allocation proposed by the draft ballot measure.

At its study session on March 21, 2022, the Housing Standing Committee reviewed these issues and directed that the time period proposed under the ballot measure be modified to eight years and that the measure, as modified, be presented to the City Council for consideration. Specifically, the Committee proposed the ballot measure to authorize the City to be able to construct or acquire 1% of the total number of existing housing units in the City for eight years, instead of thirty years. The eight-year period is intended to align with the City's Housing Element adoption cycle and the associated Regional Housing Allocation (RHNA) obligations. The Committee also desired to receive information about potential impacts on property tax revenue, use of commercial linkage fees, or other City financing to develop or acquire units.

As amended based on Committee comments, the specific ballot measure question was written as follows:

Without increasing local taxes, shall the City of South San Francisco be authorized to develop, construct, and/or acquire affordable, decent, and safe rental housing for low-income persons, including families, seniors, people with disabilities, and veterans, in an amount up to 1% of the total number of existing housing units in the City of South San Francisco annually for an eight (8) year period, with any year's unused units being carried over each year?

Finally, at the City Council's recent meeting on May 11, 2022, the Council requested additional analysis of the financial impacts, benefits, and drawbacks of developing, operating, and maintaining a social housing project under Article 34 authorization.

DISCUSSION

Since the May 11, 2022 hearing, staff has hired BAE Urban Economics to conduct such an analysis for the City. Attached for the City Council's consideration is a thorough examination of the costs to construct and operate two development prototypes-a 100% affordable housing project and a mixed-income development-as well as some variations in funding for the prototype projects and revenue generation potential to support additional housing projects. Representatives from BAE Urban Economics will be prepared to discuss their analysis and impacts of variables that could make such a development more or less feasible.

No other action or consideration of potential ballot measure is proposed for discussion at this meeting.

CONCLUSION

Staff recommends the City Council review and consider the provided analysis on the development, operation and maintenance of social housing as possible under an Article 34 authorization and direct staff on next steps.

Attachments:

1. Social Housing Development Financial Feasibility Analysis (BAE Urban Economics)

Memorandum

To: Tony Rozzi, Chief Planner/Acting ECD Director, City of South San Francisco
Sky Woodruff, Principal, Meyers | Nave

From: David Shiver, Principal
Matt Fairris, Senior Associate

Date: July 7, 2022

Re: Social Housing Development Financial Feasibility Analysis

Introduction

To meet the growing demand for affordable housing in South San Francisco, the City is interested in understanding the financial implications of developing or acquiring affordable housing within the City. This model, called “social housing,” assumes the City would leverage their own financial resources to finance, build, own, operate, and maintain the property. In order to understand the one-time capital cost and ongoing operating and maintenance costs of a social housing project, the City contracted with BAE Urban Economics, Inc. (“BAE”). BAE recently provided technical assistance in an assessment of the inclusionary housing ordinance, as well as a high-level assessment of the potential development on the City-owned Municipal Services Building site.

The following analysis provides an assessment of the expected one-time capital costs to build the affordable housing units, potential funding mechanisms to minimize the city’s funding, as well as the ongoing financial implications of operating and maintaining the properties after construction. While the City is most interested in delivering housing units that will be affordable to lower-incomes, BAE also analyzed the potential for the City to build and operate a mixed-income development, with half of the units affordable to lower-income households and the other half rented at market-rate rents. For the purposes of this analysis, as will be discussed below, BAE assumes the lower-income units will be affordable to households at 50 percent of the Area Median Income (“AMI”), also known as “very low-income households.” For reference, the household income for a four-person household at 50 percent of AMI in San Mateo County is roughly \$91,350.

Residential Development Prototypes

To estimate the financial implications of social housing built by the City of South San Francisco, BAE created three financial feasibility pro forma models that represent a range of options for the City. To allow a comparison across the project types, all of the financial

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feasibility models assume a 150-unit residential prototype on a one-acre site intended for higher-density development. The differences between the models are the affordability levels of the rents and the financing plan for the development. The prototypes include:

Prototype 1: 150-Unit 100% Affordable Project using City Funding and Permanent Debt –

This development prototype assumes a mix of one-, two-, and three-bedroom units, all affordable to households at 50 percent of AMI. To fund the development of this 100 percent affordable development, this prototype assumes the City would take out a permanent loan against the revenue generated by the project. Due to the restricted rents, this loan is insufficient to cover the full development costs, similar to all affordable housing projects, leaving a “funding gap.” For this prototype, the remaining funding gap is assumed to be filled with exclusively City funding.

Prototype 2: 150-Unit 100% Affordable Project using Low-Income Housing Tax Credits, City Funding and Permanent Debt – Similar to Prototype 1, this prototype assumes all units are affordable to households at 50 percent of AMI, including a mix of one-, two-, and three-bedroom units. This prototype would similarly assume a permanent mortgage supported by the rental revenue. Unlike Prototype 1, however, this prototype assumes the use of Low-Income Housing Tax Credits (“LIHTC”). These credits are awarded by the California Tax Credit Allocation Committee to support the development of affordable housing. These funds are awarded based on the project costs and unit mix and help fill the funding gap associated with affordable housing developments. However, these funds do not cover the full funding gap, therefore, this prototype assumes the City funding would support the remaining funding gap after the use of permanent debt and LIHTC.

Prototype 3: 150-Unit Mixed-Income Project using City Funding and Permanent Debt –

This mixed-income prototype assumes half of the units are affordable to households at 50 percent of AMI, while the other units are rented at market rates. The affordable units include a mix of one-, two-, and three-bedroom units, while the market rate units include a mix of studio, one-, and two-bedroom units, due to the challenges with delivering three-bedroom market rate units. In terms of the assumed funding sources, this model strictly uses permanent debt supported by the rental income and City funding.

In addition to these three baseline prototypes, BAE also tested the financial impacts of various sensitivities, including other City funding contributions, different affordability levels, and alternative funding schemes.

Cost and Revenue Assumptions

The following section summarizes the assumed development cost and operating cost assumptions used in the financial feasibility model. BAE leveraged information from prior analyses recently conducted for the City, as well as review of publicly-available applications for

LIHTC in the City and surrounding jurisdictions. This is typical in affordable housing development, especially those with the use of federal, state, and local funds, due to the requirements set forth in those funding programs. One critical assumption is the use of prevailing wage in all aspects of the development process.

Development Cost Assumptions

Site Acquisition Cost – The estimated site acquisition costs is based on developer interviews and a review of recent land transactions for infill development parcels. Based on the research, the estimated land price for all of the prototypes is \$125 per site square foot, or nearly \$5.5 million for the one-acre site.

Site Work – According to developers, the cost of any required site work will be similar for each prototype, at \$20 per site square foot. This includes costs associated with utilities, concrete slabs, and preparing the site for the high-density development.

Residential Hard Construction Costs – Due to the assumed public involvement in the development process, BAE assumes the use of prevailing wage for all development costs. This is particularly important for the hard costs, where the use of prevailing wage can increase the total cost significantly. Based on interviews and review of recent development costs, the hard cost is estimated at \$400 per square foot across all prototypes.

Parking Hard Costs – Due to the relatively small site size and the desire to achieve higher densities, all of the prototypes assume podium parking. Based on conversations with developers, the podium parking hard costs roughly \$45,000 per space.

City Impact and Permitting Fees – City impact and permitting fees are based on the City's master fee schedule. As is typical for most City fees, and particularly impact fees, per unit rates depend on the unit type and density. Inclusive of all City impact fees, the total fee per unit for the prototypes is approximately \$30,000 per unit. As will be discussed in the sensitivity section, the City could choose to waive these fees for these developments in order to reduce the overall cost. However, the baseline feasibility models assume all City fees are paid during the construction period.

Soft Costs – Softs costs, which are typically estimated as a percentage of hard construction costs, include the costs associated with engineering, legal, and accounting services. Based on developer feedback, soft costs typically amount to roughly 20 percent of hard costs for both higher-density prototypes.

Developer Fee – In traditional affordable housing developments, the developers are eligible for a developer fee to cover staff overhead and other internal project costs. Although these prototypes assume the City is acting as the developer, the City may wish to

assume a developer fee in order to cover internal project costs. In addition, this fee may also be needed if the City wishes to partner with a more experienced development partner. Similar to other costs above, however, the City may wish to waive any developer fee in order to reduce the overall costs. Reducing any developer fee would require that the City development staff is paid using other pools of funding.

Financing Costs – While the City may be able to use their funds during construction, these baseline models assume the City takes out a construction-period loan to fund the construction of the project. BAE assumes a loan valued at 65 percent of construction costs and to pay a loan fee of one percent of the loan amount. The construction period interest is estimated based on an annual interest rate of 5.5 percent and a drawdown factor of 65 percent. Due to the size and complexity of the prototypes, the loan period is assumed at 24 months. As discussed in the sensitivity section, the City could reduce or eliminate the need for a construction loan by using City funds to finance the construction period.

Operating Cost and Revenue Assumptions

Affordable Residential Rental Rates – While the City may wish to deliver housing affordable to various income levels, BAE assumes the prototype will include units affordable at 50 percent of AMI which is roughly \$91,350 for a four-person household. Using the official rental rates published by the California Housing and Community Development Department (“HCD”), the affordable rents range from \$1,643 to \$2,251 depending on the assumed size.¹

Market-Rate Residential Rental Rates – Given Prototype 3 includes market-rate housing, BAE compiled market-rate rents for newer apartment projects in the city. Based on these comparable properties, BAE assumes the following market-rate rents:

- Studio unit - \$2,318 (\$5.15 per square foot) per month
- 1-bedroom unit - \$3,244 (\$4.99 per square foot) per month
- 2-bedroom unit - \$3,613 (\$4.25 per square foot) per month
- 3-bedroom unit - \$4,125 (\$3.75 per square foot) per month

Residential Rental Operating Expenses – In order to calculate the Net Operating Income (NOI) of the rental prototypes, BAE assumes different operating costs for the affordable units and the market rate rents, due to the services provided to each unit type. For the affordable housing units, the costs to operate the building, including property management and on-site services, are estimated at roughly \$12,500 per unit per year. This would include any City costs of managing the property, either via a partnership with a

¹ HCD income and rental rate limits by unit type are available at: <https://www.hcd.ca.gov/grants-funding/income-limits/state-and-federal-income-limits.shtml>

management entity or through a new internal property management team. Note that these operating costs do not include the payment of property taxes because all deed-restricted housing units affordable to households at 80 percent of AMI or less are exempt from property taxes.

For the market-rate units, property taxes comprise a large portion of the ongoing operating costs. Based on input from City staff, it is assumed that market-rate units included in a city-developed building would be exempt from property taxes. As such, BAE assumes a much lower annual operating cost, at \$4,125 per unit per year. As discussed in the following sections, this property tax exemption does have implications for all tax receiving entities in the City, as new households would be added without new revenue streams to those service-providing entities under this development model. Additionally, the tax exempt status of the market-rate units could be disputed by the County Assessor. A final determination that the market-rate units are subject to property tax would significantly increase the annual operating costs.

Capital Funding Assumptions

Due to the complex nature of affordable housing development, and the various options available to the City of South San Francisco if they choose to build affordable housing, BAE assumed a variety of funding plans for each prototype. This includes:

Permanent Debt– All units assume the use of permanent debt supported by the projects' rental revenue. This permanent debt reduces the City's gap funding by raising a modest amount of up-front revenue to fund the construction of the project. BAE assumes a debt service coverage ratio of 1.15, meaning the City would leverage up to 85 percent of the expected revenue to support a permanent debt amount. The lending terms also assume a five percent interest rate for a 30-year term.

Low-Income Housing Tax Credits – The most common source of revenue to support affordable housing development is the Low-Income Housing Tax Credits ("LIHTC"). LIHTC funds are allocated to affordable housing developers in order to fill the expected funding gap due to the reduced revenue generated by restricted rental rates. LIHTC are competitive and allocated by the California Tax Credit Allocation Committee ("TCAC"). In order to be eligible for LIHTC, the applicant must have recent development experience using LIHTCs, meaning the City would need to partner with an experienced developer until they meet the requirements set forth by TCAC.

In order to estimate the amount of LIHTC allocated to these prototypes, BAE reviewed recent LIHTC applications in the area and used similar assumptions. These models assume the development would receive an allocation of the less-competitive four-percent tax credit program. This program allocates LIHTC at a rate of four percent of the eligible project costs, for 10 years, essentially covering 30 to 40 percent of the project costs. One

additional nuance of the LIHTC program is being located in a Qualified Census Tract (“QCT”) or Difficult to Develop Area (“DDA”), which increases the amount of funds the project can receive. Unfortunately, only a limited part of South San Francisco qualifies for this “boost,” so these models assume the project is not eligible for the increase in LIHTC funds.

City Gap Funding – Due to the City’s interest in delivering affordable housing in a relatively short period, BAE assumes the remaining funding gap associated with the prototypes is filled by City funds, such as the funds generated by the Commercial Linkage Fee. Typically, the City has contributed these funds to other affordable housing developers at between \$50,000 and \$75,000 per unit. Under these models, the City’s contribution would be notably larger on a per-unit basis due to the cost and lack of additional funding sources that other affordable housing developers receive, such as State funds from HCD.

Financial Feasibility Summary

The following section summarizes the financial feasibility of the three baseline housing prototypes. This includes the total development cost, estimated permanent debt, and required City gap funding. The detailed financial feasibility summary models are included at the end of the document in Appendix A.

Prototype 1: 100% Affordable with City Gap Funding

Prototype 1 is estimated to cost roughly \$104.5 million to construct, or nearly \$700,000 per unit. This includes a site acquisition cost of nearly \$5.5 million, as well as site preparation costing nearly \$900,000. As is typical, the vertical construction costs account for the majority of the total construction cost, or roughly \$90.6 million in total vertical construction costs. The largest source of vertical construction costs is the hard cost, which is estimated at \$65 million in total. At a ratio of one parking space per unit, the total parking costs is projected to cost roughly \$6.8 million. Soft costs, such as architecture and engineering fees, are estimated at \$14.4 million, while City impact fees account for nearly \$5 million in cost. Aside from vertical construction costs, the remaining costs are associated with construction financing and a developer fee to cover overhead costs, whether that be City staff or a co-developer partner. In total these additional costs amount to \$7.6 million, the majority of which is associated with the construction loan interest.

In order to estimate the total City gap funding required to develop this prototype, BAE assumes the City would leverage the projects’ rental income to support a permanent debt payment. Based on the lending terms outlined in the previous section, this prototype can support a permanent debt amount of nearly \$20 million. This is based on the project’s net income, which includes \$3.5 million in revenue, and nearly \$2 million in operating expenses, including City costs to operate and maintain the property. Assuming the permanent debt is the only source of funding, the City would need to allocate funds to fill the remaining funding gap.

Based on the financial model, this 150-unit project would require nearly **\$84.8 million in total City gap funding**, or roughly \$565,000 per unit.

With the City gap funding, revenue from rents would likely be sufficient to pay for operation of the building, including debt service on the assumed loan that is in addition to the gap funding. There would **not** be sufficient revenue from rents to produce a surplus that could be used to assist in financing an additional residential development project.

Prototype 2: 100% Affordable with LIHTC and City Gap Funding

The development cost of Prototype 2 aligns with the costs outline above in Prototype 1, as this prototype simply adjusts the funding sources used to finance the project. As noted above, the total development cost amounts to \$104.5 million, or nearly \$700,000 per unit. The rental income generated by the units, which are affordable to households at 50 percent of AMI, can support the same \$20 million in permanent debt. However, for this prototype, the City would seek an allocation of LIHTC, which are used to reduce the required City funding. Based on the assumptions outline above, this project would be eligible for roughly \$37.6 million of LIHTC, which would be sold to a tax credit investor to generate LIHTC Equity to the project. This funding source decreases the amount of City gap funding required to develop the project.

More specifically, the 150-unit Prototype 2 would require roughly **\$47.1 million in total City gap funding**, or roughly \$315,000 per unit. This is still well above the typical City funding contributed to affordable housing projects, ranging from \$50,000 to \$75,000 per unit, due to the lack of additional Federal and State gap funding sources.

With the LIHTC and City gap funding, revenue from rents would likely be sufficient to pay for operation of the building, including debt service on the assumed loan that is in addition to the gap funding. There would **not** be sufficient revenue from rents to produce a surplus that could be used to assist in financing an additional residential development project.

Prototype 3: Mixed Income with City Gap Funding

While incorporating market-rate units increases the amount of revenue generated by the project, these market-rate units still require an additional source of funding to supplant the typical investor equity included in these types of projects. Unless the City intends to find an investor partner to fund the market-rate component of this mixed-income prototype, the City would need to use City funds to replace the lack of traditional equity contribution.

In terms of development cost, Prototype 3 is projected to cost roughly \$98.8 million, or \$632,000 per unit. This prototype has a slightly lower development cost relative to the prior prototypes due to the smaller unit sizes of the market-rate units. As noted above, to maximize revenue and the value of the market-rate units, this prototype assumes the market-rate units are a mix of studio, one-, and two-bedroom units, rather than the affordable unit mix, which also includes three-bedroom units. In general, the distribution of costs is comparable to the prior prototypes, with a \$5.5 million land acquisition cost, \$81.7 million in vertical construction

costs, \$4.4 million in construction financing, and \$2.5 million in a developer fee to cover staffing overhead. As noted previously, the inclusion of market-rate units will increase the total project revenue, to an estimated \$4.5 million in gross revenue. After accounting for the operating expenses, estimated at \$1.3 million per year, the projects' net operating income is roughly \$3.0 million. This revenue can support a significant permanent debt amount, of roughly \$41 million, or roughly double the supportable loan amount in the prior prototypes.

Assuming this prototype solely leverages a permanent debt amount, the remaining funding gap would require City funding. Based on the financial feasibility model, this 150-unit mixed-income prototype would require a total of \$53.8 million in total City gap funding, or roughly \$360,000 per unit. As the financial pro forma shows in Exhibit 3 below, the required funding gap amount differs significantly based on the affordable units and market-rate units. Similar to Prototype 1, the affordable housing units require roughly \$570,000 in total City gap funding per unit, while the market-rate units only require \$146,000 per unit. Because the project is half affordable units and half market-rate units, these blend to create a project-wide gap funding requirement of \$360,000 per unit.

In this prototype, rents from the market-rate units help to reduce the City funding gap, but the City must still add funding to make the project financially feasible. With the City gap funding, revenue from rents would likely be sufficient to pay for operation of the building, including debt service on the assumed loan that is in addition to the gap funding. There would not be sufficient revenue from rents to produce a surplus that could be used to assist in financing an additional residential development project.

Exhibit 1: Financial Feasibility Summary by Prototype

	Project Type and Funding Plan		
	Prototype 1: 100% Affordable City Funding	Prototype 2: 100% Affordable LIHTC and City Funding	Prototype 3: Mixed-Income City Funding
150-Unit Project			
Total Development Cost	\$104,500,044	\$104,500,044	\$94,818,247
<i>TDC Per Unit</i>	<i>\$696,667</i>	<i>\$696,667</i>	<i>\$632,122</i>
Supportable Debt Amount	\$19,739,777	\$19,739,777	\$40,985,297
LIHTC Equity	\$0	\$37,620,016	\$0
City Gap Funding	(\$84,760,267)	(\$47,140,251)	(\$53,832,951)
<i>Per Unit</i>	<i>(\$565,068)</i>	<i>(\$314,268)</i>	<i>(\$358,886)</i>

Sources: City of South San Francisco; BAE, 2022.

City Funding Requirements

The following section summarizes the critical City cost implications of the various prototypes discussed above. This includes the one-time capital costs, called out above, and the ongoing annual costs to the City.

Capital Costs

As discussed above, the baseline feasibility models require a City gap funding amount ranging from \$47.1 million to \$84.8 million, depending on the affordability levels of the units and the additional funding sources assumed to finance the project. Of the two prototypes including only affordable housing units, affordable to households at 50 percent of AMI, the major difference in the required City gap funding subsidy is the inclusion of LIHTC dollars. This funding source would add some complexity to the deal, due to the funding timelines set forth by TCAC, as well as the need to identify development, finance, and operating partners that meet TCAC regulations. However, as shown above, the LIHTC funding program can significantly decrease the required City gap funding subsidy. If the City pursues the idea of social housing, the decision to seek LIHTC is critical to balance the City's subsidy requirements and the speed and flexibility of the final delivered product, as well as ongoing monitoring requirements that come with LIHTC.

Although the inclusion of market-rate units in Prototype 3 does increase the rental revenue and supportable debt amount, the City would still be required to provide a significant amount of funding to fill the financing gap. This includes a more limited amount of City funding to fill the gap associated with the market-rate units, estimated at roughly \$11 million, or \$150,000 per market-rate unit. The only way for the City to recoup these funds would be to refinance the property after several years or sell the market-rate component to an investor. Similar to Prototype 1, the affordable component of Prototype 3 would require roughly \$570,000 per unit in City gap funding. In total, this mixed-income project requires a total of \$53.8 million of City gap funding, or \$359,000 per unit.

Ongoing Annual Costs

As noted above, the City would have upfront costs associated with planning, entitling, and constructing the project, as well as ongoing annual costs to operate and maintain any social housing development.

Predevelopment Costs and Staff Overhead

In order to navigate the development process of the social housing project, the City would incur costs associated with staff time to plan, entitle, and begin construction. In traditional affordable housing development, built by for-profit or non-profit affordable housing developers, these costs are covered by the Developer Fee at the end of construction. BAE estimates that the City costs to oversee the delivery of the 150-unit project, which could take three to five years, would cost at least \$2.7 million in funding. While this could be recouped after construction, this overhead repayment would increase the cost of construction, therefore increasing the required City subsidy. One way or another, the City would need to identify a funding mechanism to cover the project management staffing.

Ongoing Operations and Maintenance

Whether the City creates an internal property management team or contracts with a third-party operator, all of the social housing developments will require ongoing operating and maintenance. Depending on the revenue generated by the projects, this ongoing cost would likely be covered by the revenue generated by the specific property. Even affordable housing developments at very low-income levels typically generate sufficient revenue to at least cover annual operating costs for property management, maintenance, and on-site services. BAE estimates the total cost to operate and maintain an affordable housing unit to be roughly \$12,500 per unit. For the 150-unit fully affordable complexes, this amounts to roughly \$1.9 million in annual costs. Operating costs for market-rate units is somewhat lower, at just \$4,125 per unit, due to the assumed property-tax exemption. For the mixed-income development envisioned in Prototype 3, the mix of units decreases the overall operating costs to just \$1.3 million per year. Even with the City gap funding, none of the prototype projects generate sufficient rental income to produce a surplus that could be used to assist in financing another housing project.

Foregone Property Taxes

Affordable housing properties that are deed-restricted at rents below 80 percent AMI are property tax exempt, meaning that any affordable units delivered in the City, regardless of the developer and owner, do not pay property taxes to the City. For the purposes of this analysis, the City assumes that market-rate units delivered as part of this social housing model would also be property tax exempt. This increases the net revenue generated by the project, and therefore the supportable loan amount, but it also increases the amount of expected property tax revenue that would not be produced by development for tax receiving entities. As shown below, the 75 units of market-rate housing included in Prototype 3 would typically generate roughly \$463,000 in annual property tax. The largest share of these funds flow to the South San Francisco Unified School District (\$203,800 per year) and San Mateo County (\$120,000 per year). Assuming the market-rate housing units within the social housing development are property tax exempt, these tax-receiving entities would forego expected property taxes in order to support the delivery of this mixed-income social housing project, in addition to the property tax that they would forego from the affordable units regardless of the developer and owner of the project.

Exhibit 2: Expected Property Tax by Prototype and Development Model

Tax-Receiving Entity	Prototype 1 & 2: 150 Affordable Units		Prototype 3: 75 Market-Rate Units / 75 Affordable Units	
	Traditional	Social Housing	Traditional	Social Housing
City of South San Francisco	\$0	\$0	\$77,823	\$0
South San Francisco Unified School District	\$0	\$0	\$203,822	\$0
San Mateo County	\$0	\$0	\$119,977	\$0
SMC Community College District	\$0	\$0	\$34,279	\$0
County Office of Education	\$0	\$0	\$17,603	\$0
Special Districts	\$0	\$0	\$9,728	\$0
Total Property Taxes	\$0	\$0	\$463,231	\$0

Sources: City of South San Francisco; BAE, 2022.

Alternative Funding Mechanisms

While the social housing development model is an option to expand the inventory of affordable housing in the South San Francisco, the City also has several additional options for supporting housing development. The following section summarizes these alternative funding mechanisms, including the potential positive and negative aspects of each option.

Gap Funding to Affordable Housing Developers

Similar to recent trends, the City can continue providing gap funding to third-party affordable housing developers building affordable housing in the City. Based on input from City staff, the City typically provides roughly \$75,000 per unit to affordable housing developers progressing with projects in South San Francisco. This funding mechanism is less expensive to the City, as experienced affordable housing developers will also apply for additional State and Federal funding programs. By reducing the required City gap funding subsidy amount, the City can support more affordable housing units. For example, if the City were to use all of the projected Commercial Linkage Fee revenue, estimated at \$122 million through 2036, the City could support the delivery of approximately 1,600 affordable housing units over that timeline. The major drawback of this funding scheme is the City is dependent on the outside development community to identify, purchase sites, and pursue development of projects within the city. Affordable housing developers often have several ongoing projects at various phases of development but given the extreme need for affordable housing in the Bay Area, it is possible that developers may overlook South San Francisco projects in place of easier deals in other Bay Area cities. While the City can provide additional incentives to attract developers to projects in South San Francisco, discussed in more detail below, strictly providing gap funding to developers will take time to meet the pressing need for affordable housing in the city.

Land Contribution

One of the most significant challenges to affordable housing development is the acquisition of suitable sites for development. Given affordable housing development teams do not have significant cash reserves, they often are unable to compete with the private market for the

acquisition of multifamily development sites. As such, public jurisdictions can support affordable housing development by leveraging publicly owned sites, such as excess sites from the City, School District, and other public land owners. In addition to identify existing publicly owned sites, the City could leverage City funds to locate and acquire additional sites in the City and reserve them for future affordable housing development through a partnership with an affordable housing developer. While the projected value of the land only accounts for five percent of the total development cost, the City would create additional value by reducing the risk and burden on the affordable housing development community on securing buildable sites and ensure a constant pipeline of affordable housing projects. If the City pursues acquiring sites for affordable housing, it is critical to understand the geographic components that make sites suitable and competitive for affordable housing funding. This includes proximity to transit, schools, grocery stores, among other amenities. Sites that are near these amenities are more competitive for funding programs and are more likely to attract affordable housing developers to pursue housing development opportunities.

Impact Fee Waivers and Deferrals

The City may waive or defer impact fee waivers to reduce the overall cost of development, whether in the social housing model or to third-party developers. Based on the financial feasibility models, the City's impact fees amount to roughly \$30,000 per unit, or roughly 4.3 percent of the total development costs. While these support critical City services, such as parks, public safety, transportation, among others, the City could waive or defer these fees to affordable housing developments to reduce the overall cost of development. Although these fees only account for a small portion of the overall development cost, a large portion of the remaining development costs are relatively fixed, meaning City has limited options to reduce the overall development cost and associated gap funding required to deliver the units.

Build Units at Higher Incomes

While the above financial feasibility analysis shows the large gap funding required to support the social housing development model, the City could build units affordable to households at higher incomes in order to improve the overall economics of the project. For example, if the City were to build units affordable to households at 80 percent of AMI, rather than 50 percent AMI modeled above, the required City gap funding would decrease to roughly \$290,000 per unit, much lower than the initial \$565,000 in the prior models. The City could further increase the affordability levels of the units included in the social housing development to 100 percent or even 120 percent of AMI, though rents at these levels are comparable to market-rate rents and may not provide much benefit to South San Francisco households. Although the projected \$290,000 per unit is still well above the historic gap funding provided by the City, the City would maintain ownership of the units and could decide to change the affordability levels of the units in the future.

City General Obligation Bond with Pay-Go Funding

Based on discussions with City staff, South San Francisco could support a General Obligation (GO) bond to support the social housing concept in the City. These funds could be used in a variety of ways. First, these funds could be spread out across several development projects in coordination with other funds to deliver more housing units in the near term. Secondly, these funds could be used to fully support the delivery of one social housing development without the need for construction-period or permanent debt financing. This scheme would then allocate all net income generated by the project back to the City, or roughly \$1.5 million annually. The City could then use these annual ongoing funds to support additional housing development throughout the City. On a “Pay-Go” basis, where the City accumulates the income and only uses the cumulative funding to support additional housing development, the City would accumulate roughly \$15 million of net income over the next ten years. Assuming the City leverages these funds to provide gap funding to other affordable housing development after the ten-year period, these funds could support the development of between 20 and 50 units of affordable units.

APPENDIX A: DETAILED FINANCIAL FEASIBILITY MODELS

See Next Page

Appendix A-1: Financial Feasibility Summary, Prototype 1: 100% Affordable with City Funding

Development Program Assumptions								Cost Assumptions				Development Cost Analysis				Feasibility Analysis			
Site Size - acres / square feet		1.0	43,560		Site Acquisition Cost (per Site SF)		\$125	Project Cost		Feasibility		Project Income		Gross Scheduled Rents		\$3,513,000			
Total Units			150		Construction			Site Acquisition		\$5,445,000	Less Vacancy		(\$175,650)						
Affordable (% - count)		100%	150		Site Prep Costs (per site, sq.ft)		\$20	Site Preparation		\$871,200	Less Operating Expenses		(\$1,875,000)						
Market Rate (% - count)		0%	0		Hard Cost per residential sf		\$400	Vertical Construction			Net Operating Income		\$1,462,350						
Leasable sq.ft.			130,000		Parking cost per space, Podium		\$45,000	Hard Cost		\$65,000,000	Feasibility								
Circulation & Communal Space			20%		Soft Costs (% of hard costs)		20%	Parking Cost		\$6,750,000	Total Development Costs		\$104,500,044						
Total Project sq.ft			162,500		Impact Fees (per unit)		\$29,963	Soft Costs		\$14,350,000	Per Unit		\$696,667						
Total Parking Spaces			150		Developer Fee (% of hard and soft)		3%	Impact Fees		\$4,494,479	Supportable Debt Amount		\$19,739,777						
Parking spaces per du			1.00					Subtotal		\$90,594,479	LIHTC Equity		\$0						
Residential Characteristics								Rental Revenue											
Unit Mix		Sq. Ft.		AMI-Level		Monthly Rental Rate by AMI-Level		Construction Financing		LIHTC Equity		\$0							
Studio		450	0	0	0	0	0	0	Unit Type	50%	60%	80%	100%	MR	Const. Loan Fees	\$594,527			
1-BR		650	50	0	0	0	0	50	Studio	\$1,529	\$1,849	\$2,489	\$3,127	\$2,318	Const. Loan Interest	\$4,250,867			
2-BR		850	50	0	0	0	0	50	1-BR	\$1,643	\$1,985	\$2,671	\$3,356	\$3,244	Developer Fee	\$2,743,970			
3-BR		1,100	50	0	0	0	0	50	2-BR	\$1,961	\$2,372	\$3,195	\$4,017	\$3,613	Total Development Cost	\$104,500,044			
All Units		150	0	0	0	0	0	150	3-BR	\$2,251	\$2,726	\$3,677	\$4,626	\$4,125	Per Unit	(\$84,760,267)			
																(\$565,068)			
Summary								Operating Costs				Annual City Cash Flow							
Number of Units (# - %)		150	100%	0	0%		150	Annual op. cost - per Affordable du		\$12,500	Excess Cash Flow to City		\$190,741						
Avg. Affordability (% AMI)		50%					n.a.	Annual op. cost - per Market Rate du		\$4,125	Foregone Property Taxes		\$0						
Leasable Sq. Ft.		130,000					0	Vacancy Rate, Residential		5.0%	Net Revenue to City		\$190,741						
Total Sq. Ft.		162,500					0	Market Rate Cap Rate		3.85%									
Parking Spaces		150					0	Financing											
Parking Space/du		1					1	Construction-Period											
								MR Loan-to-Cost		65%									
								Loan Fees		1%									
								Draw down Factor		65%									
								Interest rate		5.50%									
								Loan Term (months)		24									
								Permanent Debt											
								Debt Service Coverage Ratio		1.15									
								Interest rate		5.00%									
								Loan Term (Years)		30									
Low-Income Housing Tax Credits (LIHTC)																			
QCT/DDA Boost Eligible								No											
QCT/DDA Adjustment								100%											
Tax Credit Term (years)								10											
Tax Credit Type								4%											
Tax Credit Rate								4.00%											
Tax Credit Price								\$1.00											

Note:

(a) Estimates eligible basis as 90 percent of total development cost. If available, eligible basis also accounts for the 30% basis boost for being located in a QCT or DDA.

Sources: City of South San Francisco; BAE, 2022.

Appendix A-2: Financial Feasibility Summary, Prototype 2: 100% Affordable with LIHTC and City Funding

Development Program Assumptions								Cost Assumptions					Development Cost Analysis			Feasibility Analysis		
Site Size - acres / square feet	1.0	43,560						Site Acquisition Cost (per Site SF)	\$125				Project Cost	Feasibility				
Total Units		150						Construction		Site Acquisition	\$5,445,000	Project Income						
Affordable (% - count)	100%	150						Site Prep Costs (per site. sq.ft)	\$20			Gross Scheduled Rents	\$3,513,000					
Market Rate (% - count)	0%	0						Hard Cost per residential sf	\$400			Less Vacancy	(\$175,650)					
Leasable sq.ft.		130,000						Parking cost per space, Podium	\$45,000	Site Preparation	\$871,200	Less Operating Expenses	(\$1,875,000)					
Circulation & Communal Space	20%							Soft Costs (% of hard costs)	20%	Vertical Construction		Net Operating Income	\$1,462,350					
Total Project sq.ft		162,500						Impact Fees (per unit)	\$29,963	Hard Cost	\$65,000,000	Feasibility						
Total Parking Spaces		150						Developer Fee (% of hard and soft)	3%	Parking Cost	\$6,750,000	Total Development Costs	\$104,500,044					
Parking spaces per du		1.00								Soft Costs	\$14,350,000	Per Unit	\$696,667					
										Impact Fees	\$4,494,479	Supportable Debt Amount	\$19,739,777					
										Subtotal	\$90,594,479	LIHTC Equity	\$37,620,016					
Residential Characteristics								Rental Revenue					Construction Financing					
Unit Mix	Sq. Ft.	50%	60%	80%	100%	MR	All	Monthly Rental Rate by AMI-Level					Const. Loan Fees	\$594,527				
Studio	450	0	0	0	0	0	0	Unit Type	50%	60%	80%	100%	MR	Const. Loan Interest	\$4,250,867			
1-BR	650	50	0	0	0	0	50	Studio	\$1,529	\$1,849	\$2,489	\$3,127	\$2,318	Developer Fee	\$2,743,970			
2-BR	850	50	0	0	0	0	50	1-BR	\$1,643	\$1,985	\$2,671	\$3,356	\$3,244	Total Development Cost	\$104,500,044			
3-BR	1,100	50	0	0	0	0	50	2-BR	\$1,961	\$2,372	\$3,195	\$4,017	\$3,613	Per Unit	(\$47,140,251)			
All Units	150	0	0	0	0	0	150	3-BR	\$2,251	\$2,726	\$3,677	\$4,626	\$4,125	Per Unit	(\$314,268)			
														Annual City Cash Flow				
Summary	Affordable	Market-Rate					Total	Operating Costs						Excess Cash Flow to City	\$190,741			
Number of Units (# - %)	150 100%	0 0%					150	Annual op. cost - per Affordable du	\$12,500	Total Development Cost	\$104,500,044			Foregone Property Taxes	\$0			
Avg. Affordability (% AMI)	50%						n.a.	Annual op. cost - per Market Rate du	\$4,125	Per Unit	\$696,667			Net Revenue to City	\$190,741			
Leasable Sq. Ft.	130,000						130,000	Vacancy Rate, Residential	5.0%	Per Net SF	\$804							
Total Sq. Ft.	162,500						162,500	Market Rate Cap Rate	3.85%	Per Gross SF	\$643							
Parking Spaces	150						150	Financing										
Parking Space/du	1						1	Construction-Period										
								MR Loan-to-Cost	65%	LIHTC Eligible Basis (a)	\$94,050,040							
								Loan Fees	1%									
								Draw down Factor	65%									
								Interest rate	5.50%									
								Loan Term (months)	24									
								Permanent Debt										
								Debt Service Coverage Ratio	1.15									
								Interest rate	5.00%									
								Loan Term (Years)	30									
								Low-Income Housing Tax Credits (LIHTC)										
								QCT/DDA Boost Eligible	No									
								QCT/DDA Adjustment	100%									
								Tax Credit Term (years)	10									
								Tax Credit Type	4%									
								Tax Credit Rate	4.00%									
								Tax Credit Price	\$1.00									

Note:

(a) Estimates eligible basis as 90 percent of total development cost. If available, eligible basis also accounts for the 30% basis boost for being located in a QCT or DDA.

Sources: City of South San Francisco; BAE, 2022.

Appendix A-3: Financial Feasibility Summary, Prototype 3: Mixed-Income with City Funding

Development Program Assumptions						Cost Assumptions				Development Cost Analysis				Feasibility Analysis															
Site Size - acres / square feet		1.0		43,560		Site Acquisition Cost (per Site SF)		\$125		Mixed-Income Development				Mixed-Income Development															
Total Units				150						Affordable		Market Rate		Total Project		Affordable		Market Rate		Total Project									
Affordable (% - count)		50%		75		<u>Construction</u>										<u>Project Income</u>													
Market Rate (% - count)		50%		75		Site Prep Costs (per site, sq.ft)		\$20		Site Acquisition		\$3,111,429		\$2,333,571		\$5,445,000		Gross Scheduled Rents		\$1,756,500		\$2,752,050		\$4,508,550					
Leasable sq.ft.		113,750				Hard Cost per residential sf		\$400		Site Preparation		\$497,829		\$373,371		\$871,200		Less Vacancy		(\$87,825)		(\$137,603)		(\$225,428)					
Circulation & Communal Space		20%				Parking cost per space, Podium		\$45,000		Vertical Construction								<u>Less Operating Expenses</u>		(\$937,500)		(\$309,375)		(\$1,246,875)					
Total Project sq.ft		142,188				Soft Costs (% of hard costs)		20%		Hard Cost		\$32,500,000		\$24,375,000		\$56,875,000		Net Operating Income		\$731,175		\$2,305,073		\$3,036,248					
Total Parking Spaces		165				Impact Fees (per unit) (a)		\$29,963		Parking Cost		\$3,375,000		\$4,050,000		\$7,425,000		Development Feasibility											
Parking spaces per du		1.10				Developer Fee (% of hard and soft)		3%		Soft Costs		\$7,175,000		\$5,865,000		\$12,860,000		Total Development Costs		\$52,706,343		\$42,111,905		\$94,818,247					
<u>Residential Characteristics</u>						<u>Rental Revenue</u>						Subtotal						Supportable Debt Amount											
AMI-Level						Monthly Rental Rate by AMI-Level																							
Unit Mix		Sq. Ft.		50%		60%		80%		100%		MR		All															
Studio		450		0		0		0		0		25		25															
1-BR		650		25		0		0		0		25		50															
2-BR		850		25		0		0		0		25		50															
3-BR		1,100		25		0		0		0		25		50															
All Units		75		0		0		0		0		75		150															
<u>Summary</u>						<u>Operating Costs</u>						Total Development Cost						Annual City Cash Flow											
Number of Units (# - %)		75		50%		75		50%		150		Annual op cost - per Affordable du		\$12,500		\$52,706,343		\$42,111,905		\$94,818,247		Excess Cash Flow to City		\$95,371		\$300,682		\$396,032	
Avg. Affordability (% AMI)		50%				n.a.						Annual op cost - per Market Rate du		\$4,125		\$42,111,905		\$561,492		\$632,122									
Leasable Sq. Ft.		65,000		48,750		113,750						Vacancy Rate, Residential		5.0%		\$702,751		\$864		\$934		Foregone Property Taxes		\$0		\$463,231		\$463,231	
Total Sq. Ft.		81,250		60,938		142,188										\$811		\$864		\$867		Net Revenue to City		\$95,371		(\$162,569)		(\$87,199)	
Parking Spaces		75		90		165										\$649		\$691		\$687									
Parking Space/du		1		1.2		1.1																							
						Construction-Period						Per Unit						Per Net SF						Per Gross SF					
						MR Loan-to-Cost						65%																	
						Loan Fees						1%																	
						Draw down Factor						65%																	
						Interest rate						5.50%																	
						Loan Term (months)						24																	
						Permanent Debt																							
						Debt Service Coverage Ratio						1.15																	
						Interest rate						5.00%																	
						Loan Term (Years)						30																	
						Low -Income Housing Tax Credits (LIHTC)																							
						QCT/DDA Boost Eligible						No																	
						QCT/DDA Adjustment						100%																	
						Tax Credit Term (years)						10																	
						Tax Credit Type						4%																	
						Tax Credit Rate						4.00%																	
						Tax Credit Price						\$1.00																	

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Item # 14

bae urban economics

SOCIAL HOUSING FINANCIAL FEASIBILITY ANALYSIS

City of South San Francisco

July 13, 2022

DEVELOPMENT PROTOTYPES

	<u>Prototype 1</u>	<u>Prototype 2</u>	<u>Prototype 3</u>
Site Size (Acres)	1.00	1.00	1.00
Number of Units	150	150	150
Affordability Levels			
50% AMI	100%	100%	50%
Market Rate	0%	0%	50%
Unit Type			
Studio	0.0%	0.0%	16.7%
1-BR	33.3%	33.3%	33.3%
2-BR	33.3%	33.3%	33.3%
3-BR	33.3%	33.3%	16.7%
Capital Funding Assumptions			
City Gap Funding	Yes	Yes	Yes
Low -Income Housing Tax Credits	No	Yes	No

FINANCIAL FEASIBILITY SUMMARY

150-Unit Project	Project Type and Funding Plan		
	Prototype 1:	Prototype 2:	Prototype 3:
	100% Affordable City Funding	100% Affordable LIHTC and City Funding	Mixed-Income City Funding
Total Development Cost <i>TDC Per Unit</i>	\$104,500,044 \$696,667	\$104,500,044 \$696,667	\$94,818,247 \$632,122
Supportable Debt Amount	\$19,739,777	\$19,739,777	\$40,985,297
LIHTC Equity	\$0	\$37,620,016	\$0
City Gap Funding <i>Per Unit</i>	(\$84,760,267) (\$565,068)	(\$47,140,251) (\$314,268)	(\$53,832,951) (\$358,886)

Sources: City of South San Francisco; BAE, 2022.

FUNDING CAPITAL STACK COMPARISON



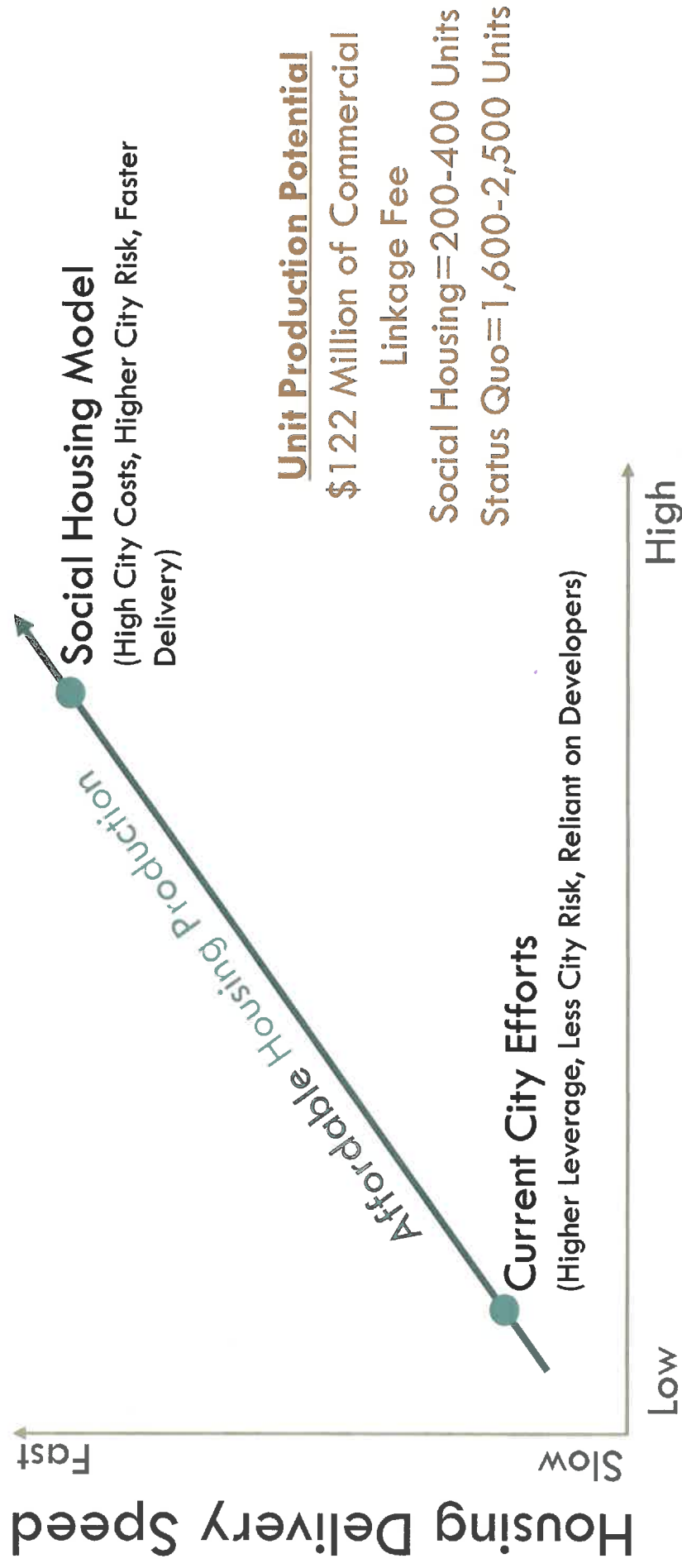
SOCIAL HOUSING ASSESSMENT SUMMARY

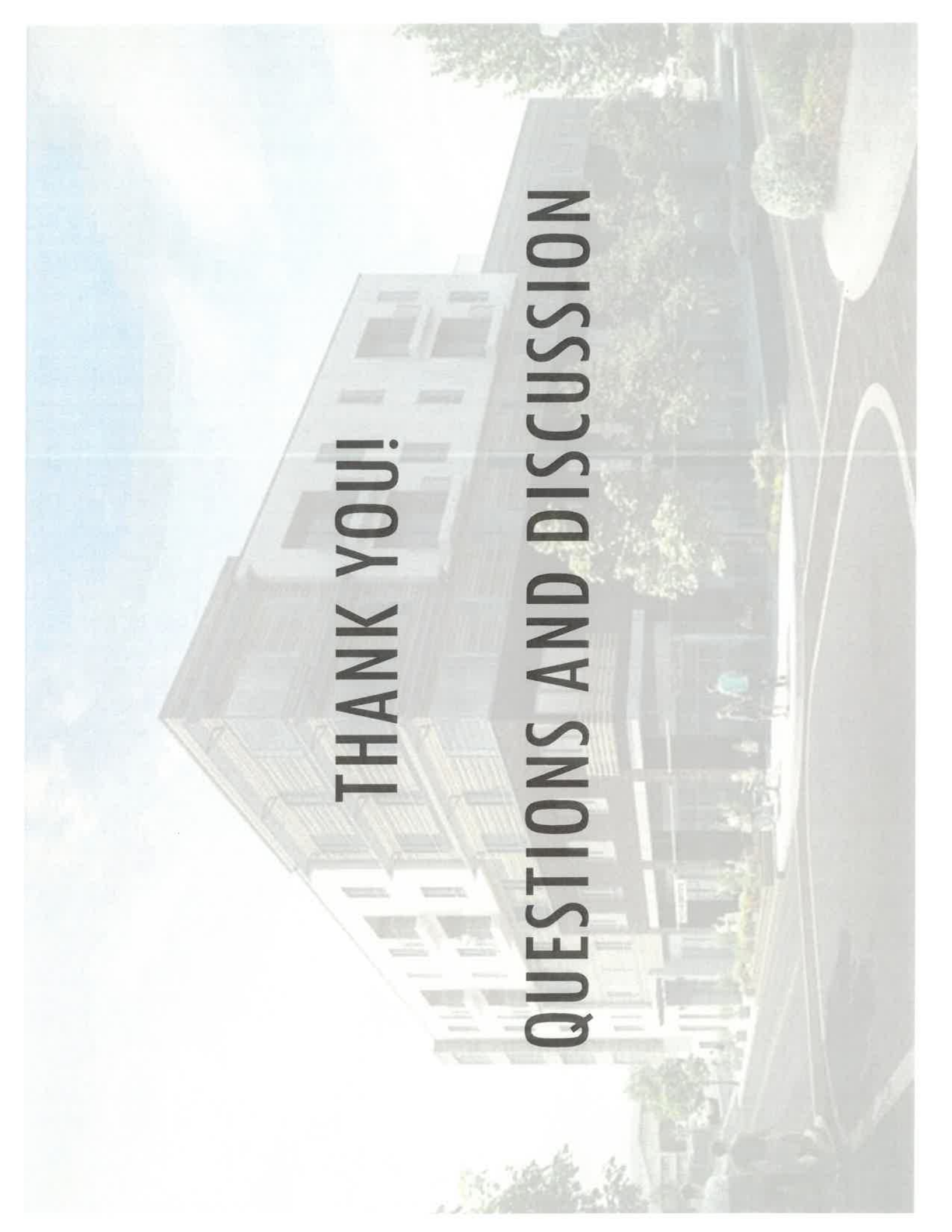
Social Housing Model

Status Quo – City Support

- Potential for Faster Delivery
 - Long-Term City Control
 - High Upfront Costs
 - High Capital Costs (\$300k-\$565k per unit)
 - More Complex Transaction Documents (Co-Developer and Management Partners)
 - Higher Development Risk
- Dependent on Developers
 - Less City Control
 - No Upfront Costs
 - Low Capital Costs (\$75k per unit)
 - Less Complex Transaction Documents (Standard Loan Agreements, DA, DDA)
 - Limited Development Risk

AFFORDABLE HOUSING COST V. SPEED



An architectural rendering of a modern, multi-story building with a mix of wood and brick facades. The building features a central courtyard with a paved area, trees, and a few people walking. The text "THANK YOU!" is overlaid in the center of the image.

THANK YOU!

QUESTIONS AND DISCUSSION

