THE CITY OF SAN DIEGO

# REPORT TO THE CITY COUNCIL

DATE ISSUED: February 2, 2007 REPORT NO: 07-035

ATTENTION: Committee on Land Use and Housing
Agenda of February 7, 2007

SUBJECT: Review of Consultant Report for Best Practices Methodology for Real Estate Assets Department Performed by Grubb & Ellis Corporate Services Dated January 31, 2007

REFERENCE: Advise on proposed modification to City Practices regarding the sale of the City's real estate assets; Council Policy 700-10

REQUESTED ACTION: None. Advisory Information

STAFF RECOMMENDATION:

COMMUNITY PLANNING GROUP RECOMMENDATION:
None

SUMMARY:
The Real Estate Assets Department of the City of San Diego was in need of a new business model. Until recently, it applied methods and policies to situations as they arose without a clear plan. There was no portfolio plan for the City's income producing real estate. Facilities for municpal uses were provided on an as needed basis without considering how they might best be integrated into an overall fadility plan. The organization lacked direction, the authority to manage its portfolio and the support systems necessary to provide a timely flow of information to its decision makers.

To help remedy the situations, Grubb & Ellis Corporate Services was engaged to do the following:

- Provide a best practice methodology based on private and governmental real estate industry standards for the management of the Citys real estate assets.
- Provide performance measures for the department and its real property inventory.
- Provide an assessment of the organizations real property management practices and its ability as a lessor and provide recommendations to improve efficency and accountability.

- Provide a review and analysis of existing authority (statutes, regulations, policies and other authority) that govern the management of real property and recommend changes to the existing authority to improve required processes and maximize efficiency.
- Provide a real property abstracts suitable for tracking each site in the Citys real estate inventory.
- Provide a brief summary of available information technology systems with recommendations as to which system would be best suited to support the department.

BACKGROUND

**Grubb & Ellis Report**

The City of San Diego is unique among municipalities in the size and diversity of the real estate portfolio that it owns and manages. The City's assets include:

- 120,000 acres
- 3,400 properties
- 680 ground leases
- Facilities for 11,000 employees

No other real estate organization, either public or private, has the size and diversity of the City's portfolio. Therefore, the best practice model for READ is a hybrid of public and private sector practices.

The mission of READ has three major components:

- Acquire/manage real estate required for governmental functions and services.
- Generate revenues through leasing and sale of surplus assets.
- Maximize the overall financial return to the City's real estate portfolio.

To effectively accomplish its mission, READ has recently been reorganized to reflect its core lines of business:

- **Acquisition / Disposition** (acquiring and disposing of City's properties)
- **Asset Management** (Managing the City's ground lease portfolio)
- **Corporate Services** (Managing the facilities needs for governmental functions and services)
- **Support Functions** (Valuation and Administrative Support)

The following (in outline form) is a brief summary of the pertinent findings of the Grubb & Ellis Report. The full report will be posted on the City's website.

**CURRENT STATE OF READ:**

**People:**

- Need improvement in knowledge of real estate techniques
- Need training from outside sources (CCIM, MAI, CPM).

**Operations:**

- Current computer systems are out of date. New system needed to improve efficiency, standardization and accountability.
- Access to information about properties is dependent on paper files.
- Lease forms and other documents need to be standardized.
- Time for legal review is excessive due to attorneys' work load.
- No definitive library of legal forms.
- Need effective event reminders and means to record communications with tenants.
- Need greater use of databases and websites.
- No receptionist at the department.

**Authority and Governance:**

- Council approval required virtually all transactions, adding time to transaction.
- No formal agenda to review and evaluate portfolio.
- Authority to negotiate transactions scattered throughout City departments.
- No clear leasing policy for leases with non-profit organizations.

**DESIRED STATE:**

**Institution of a Portfolio Plan:**
A comprehensive portfolio plan should be presented and approved by Council on an annual basis. It should include:

- A review of the portfolio
- An operating plan for corporate property
- A disposition plan for surplus property
- Market research to support anticipated transactions
- A request for authority to act within defined parameters

Once the Portfolio Plan is approved by Council, no further approvals needed for transactions within the defined parameters of the Plan. Plan is to be revised and reviewed by Council on a periodic basis.

**Major elements of a Portfolio Plan**

- Property evaluation and characterization
- Strategy for City occupied real estate
- Investment portfolio plan (leases to for profit tenants)
- Review of Not-For-Profit leases
- Disposition Plan for surplus assets
- Business case development
- Legal document development and review

**Corporate Services (Occupancy) Strategy**

- Gather Data: current portfolio, utilization, departmental changes, market data
- Analysis: eliminate redundancies, improve functionality reduce cost, identify underutilized areas, consolidation.

- Business case development by user groups
- Recommendations: long and short term facility solutions

**Asset Management Strategy**

- Analyze current leases
- Hold/Sell analysis
- Leasing strategy and plan
- Value enhancement strategy
- Standardize leasing policies (for profit)
- Standardize Not-For-Profit leasing policies

**Acquisition/ Disposition Strategy**

- Determine if property is surplus
- Appraise Value
- Determine best disposition strategy (sell, lease, other)
- Execute strategy

**Technology**

READ requires a modern system that supports:

- Portfolio monitoring
- Performance measures
- Project tracking
- Information necessary for property agents to accomplish their work

Technology going forward should:

- not upgrade CORP and LIBS
- Translate the data
- Map it into the new systems
- Create a bridge to the accounts payable and accounts receivable systems
- Migrate to modern system

This system will allow READ to have:

- Central repository for documents and formats by scanning documents and storing originals off-site
- Database tools or shared environment rather than spreadsheets for shared data
- Organization-standard spreadsheets, databases and word processing tools
- Electronic document management, including hosting of scanned versions of lease and property documents
- Departmental views of portfolios, as well as data on individual properties

**Authority**

For READ to achieve superior performance of its real estate, it requires improved authority:

- **Batched approval** – Presentation of groups of properties or entire strategies for City Council approval
- **Authority Within a Box** – Pre-approval of transactions that meet defined standards
- **Management by Exception** – Approvals should be required only for departures from standards established by the Portfolio Plan.

**SALE OF SURPLUS REAL ESTATE: Council Policy 700-10**

As part of an overall portfolio management plan, READ is currently reviewing the City's property inventory to determine which properties are no longer needed for public use and can be declared surplus. At the appropriate time, these properties will be brought before Council for approval to be sold. The benefits to the City are the following:

- Provide revenue for the capitol improvement fund.
- Relieve the City of potential liabilities and the cost of maintenance.
- Return the properties to the tax rolls.
- Stimulate the economy by providing opportunities for private sector development.

According to current procedures, the preferred method for the sale of City property is by auction. This process has two main drawbacks.

- The property does not receive the broadest exposure to the market place.
- The pool of potential buyers is limited to those in the market the day of the auction.

To maximize the value received for the City's real estate the following process is proposed:

1. Once a property is deemed to be surplus and all statutory requirements are met, the property will be presented to Council for approval to be sold at a price established by a current appraisal.

2. If Council determines that the property should be sold, it shall approve the sale as long as the sale price is either equal to, or greater than the appraised value. The pre-approved sale price will be valid for a twelve month period.

3. Properties approved for sale may be listed with real estate brokers, who will selected for the assignment by a combination of RFP and bid process. This will ensure that the property receives the widest exposure to the market place.

4. If a valid offer is received, that is equal to or greater than the appraised value, staff will be authorized to execute the transaction without further action by Council.

5. If staff believes it is in the City's best interest to accept an offer at less than the property's appraised value the transaction will be returned to Council for approval.

This process for the sale of property is consistent with the best practices of the private sector and has two principal advantages over the City's current process.

- Listing the City's properties will increase its exposure to the market and provide for the possibility of multiple offers which will drive up the price.

- A greater number of buyers will be willing to make offers on City properties because if their offer is accepted, they know that they have a deal and not risk having the transaction later disapproved by Council. This reduction of risk will lead to more aggressive offers.

By Council Policy and Municipal Code, READ must take every property intended for sale to Council, justify each sale, and seek direction as to how the property will be sold. Because all questions regarding the right to sell and manner of sale will be predetermined by an enabling resolution, no conflict exists between the Municipal Code and Council Policy, no waiver is needed and no formal policy change is required to implement this new process.

FISCAL CONSIDERATIONS:
The recommendations outlined in the Grubb & Ellis Report will enable READ to manage the City's real estate portfolio in a manner that will maximize its value. The revised process for selling real estate will create an efficient system that will maximize the value of the City's surplus properties.

PREVIOUS COUNCIL and/or COMMITTEE ACTION:
None.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:
None.

KEY STAKEHOLDERS AND PROJECTED IMPACTS:
None.

Respectfully Submitted,

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BARWICK/TM