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## OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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**Date Issued:** December 31, 2008

**IBA Report Number:** 08-124

**City Council Docket Date:** January 6, 2009

**Item Numbers:** 105

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# Disposition of City owned Real Property

## OVERVIEW

On Tuesday, January 6, 2009 the City Council will consider approving the sale of City owned property located on the corner of Del Mar Heights Road and Mercado Drive for a minimum price of \$500,000. If approved, this will be the twenty-ninth City property authorized by the Council for sale over the last three fiscal years. Currently, the sale of City owned property is governed by City Council Policy 700-10. The purpose of this report is to provide an overview of the City's land sale program and the current status of property sales.

## FISCAL/POLICY DISCUSSION

In 2006, the Real Estate Assets Department engaged Grubb & Ellis Corporate Services to provide a study on best practices methodology to achieve optimal performance from the City's assets. On January 31, 2007, Grubb & Ellis delivered the report to the City of San Diego. The report noted that the "Real Estate Assets Department of the City of San Diego is in need of a new business model. Until recently, it has functioned in a stewardship role, continuing to apply methods and policies to situations as they arose, without a clear plan." A significant recommendation from the Grubb & Ellis report was the institution of a Comprehensive Portfolio Plan which would be presented and approved by the City Council on an annual basis. The major elements of the Portfolio Plan include:

- Property evaluation and characterization of real estate assets
- 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

Although the Real Estates Assets Department had not completed the overall Portfolio Plan, staff elected to move forward with disposition of City properties deemed to be surplus. On May 21, 2007, staff requested authorization from the City Council to sell nineteen City properties that were deemed to be surplus. To establish if the properties were surplus, staff used the following criterion that they had developed based on industry best practices:

- The property is not currently used by a City department or does not support a municipal function.
- The property is vacant and has no foreseeable use by the City.
- The property is a non-performing or under-performing asset and greater value can be generated by its sale.
- Significant economic development opportunities can be generated by selling the property.

Additional factors that are also considered:

- Will the City be relieved of potential liabilities and/or cost of maintaining property that does not generate income or provide public benefit?
- Property tax increment that will be created by returning the properties to the tax rolls.
- Stimulation of the economy by providing opportunities for private sector investment.
- Generation of revenue for the Capital Outlay Fund or an Enterprise Fund.
- The sale of the property will generate greater economic value than a ground lease, if a ground lease is a feasible option.

The City Council authorized the sale of eighteen of the nineteen properties for a combined minimum value of \$38.0 million. Since May 2007 an additional eleven properties have been approved for sale by the City Council. It is important to note that the Real Estate Assets Department continues to work on a Comprehensive Portfolio Plan and anticipates completion sometime in Fiscal Year 2009.

### **City Council Policy 700-10**

The purpose of City Council 700-10 is to establish a procedure by which unused and marginally used City-owned real estate is reviewed for its potential public use, and for designating unneeded parcels for lease or sale. In addition, the policy also provides a methodology for the sale or exchange of City-owned real estate and establishes policies for the leasing of City-owned real property.

In 2007, based on recommendations from Grubb & Ellis and a comprehensive internal review of Real Estate Assets Department procedures, staff determined that Council Policy 700-10 was in need of updating. The goal of updating Council Policy 700-10 was

to ensure that the City had an effective program to manage the City's real estate assets in a manner that would maximize their value. The recommended changes to the Council Policy integrated the criterion discussed above with other significant process changes including:

- Inclusion of Government Code Section 54222 which requires that a local agency must first notify all governmental agencies operating within the City as to the availability of the property. The agencies are then given 60 days to respond with intent to acquire the property.
- The requirement that an economic analysis of the benefits of lease vs. sale if the property is of the type and location that would make a ground lease feasible.
- The requirement of an appraisal that is less than six months old that is used by the Real Estate Assets Department to establish a minimum sale price. If the property cannot be sold at a price equal or greater than the minimum price approved by the Council the property will be returned to Council for further consideration prior to disposition.
- The requirement that the proposed Real Estate Broker Commission rates be contained in the enabling resolution for the property's sale.
- The requirement that the Mayor report out on the price, terms and conditions of all transactions.

On September 16, 2008, the City Council approved the recommended changes to City Council Policy 700-10. The updated Council Policy went into effect on October 17, 2008.

### **San Diego City Charter Section 77 – Capital Outlay Fund**

As briefly discussed in the Background section of City Council Policy 700-10, the proceeds from the sale of City-owned properties are utilized for Capital Improvements Program projects, as required by the City Charter, Section 77. Charter Section 77 states:

“There is hereby created a fund in the City Treasury, to be known as the Capital Outlay Fund. Into this fund each year there shall be placed all moneys derived from taxation required or needed for capital outlay expenditures and all proceeds received from the sale of city-owned real property.

*The moneys in the Capital Outlay fund shall be used exclusively for the acquisition, construction and completion of permanent public improvements, including public buildings and such initial furnishings, equipment, supplies, inventory and stock as will establish the public improvement as a going concern. This fund may also be used for the acquisition, construction and completion of real property, water and sewer mains and extensions, and other improvements of a permanent character and also the replacement or*

*reconstruction of the same*, but not the repair or maintenance thereof, and shall not be used for any other purpose or transferred from said fund, except with the consent of two-thirds of qualified electors of said City, voting at a general or special election.”

To be consistent with Charter Section 77, the Fiscal Year 2008 and 2009 Annual Budgets included a combined total of \$32.10 million in revenue from the sale of surplus property. The revenue has been programmed to fund deferred maintenance projects (\$5.3 Million), Americans with Disabilities Act (ADA) related projects (\$20.0 Million), and design of future deferred maintenance projects (\$6.8 Million).

**Status of Land Sales**

Since the initial authorization to sell surplus City properties on May 21, 2007, the City has sold a total of 17 properties. The Real Estates Assets Department provided the IBA with an update on the properties that have been sold on December 16, 2008 (see Attachment A). The following table provides a breakdown of the revenue to the General Fund received from the sale of surplus property by Fiscal Year:

| Fiscal Year      | Total Revenue Budgeted<br>(General Fund) | Actual Revenue Received |
|------------------|--|-------------------------|
| Fiscal Year 2008 | \$15,300,000                             | \$23,961,876            |
| Fiscal Year 2009 | \$16,800,000                             | \$427,000               |
| Total**:         | \$32,100,000                             | \$24,388,876            |

\*\*Two properties that were owned by the Water Department (Silkes Adobe and Plaza Del Lago) were sold generating a total of \$5,560,000 in revenue for the department.

Staff has indicated that the current economic climate could have an impact on the value of the properties that have been authorized for sale but have not been sold. As outlined in Council Policy 700-10, if the department is having difficulty selling the property at the approved price then the department would return to the City Council with a recommendation on the future actions related to the property.

**CONCLUSION**

The IBA continues to support the sale of City properties that are deemed to be surplus. The IBA will continue to work with the Real Estate Assets Department to keep the City Council updated on the status of land sales.

**[SIGNED]**

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 APPROVED: Andrea Tevlin  
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Attachment A