KEYSER MARSTON ASSOCIATES.
ADVISORS IN PUBLIC/PRIVATE REAL ESTATE DEVELOPMENT

MEMORANDUM

To: Brad Richter, Assistant Vice President - Planning
Civic San Diego

From: KEYSER MARSTON ASSOCIATES, INC.

Date: October 28, 2016

Subject: The Beacon – 1425 and 1431 C Street
Peer Review of Economic Alternative Analysis

I. INTRODUCTION

In accordance with your request, Keyser Marston Associates, Inc. (KMA) has undertaken a peer review of the economic feasibility analysis prepared for alternative development scenarios for the 0.19-acre site at 1425 and 1431 C Street (Site).

The Site is restricted by a Declaration of Covenants, Conditions, and Restrictions (CC&Rs) that was recorded against the property in 1996 by its former owner, Episcopal Community Services, in accordance with a loan and grant from the San Diego Housing Commission. These restrictions require any development on the Site to be set aside and reserved as "affordable units" until September 2034.

Civic San Diego (CivicSD) has received a development proposal from the Site's current owner, Wakeland Housing & Development Corporation (Developer). The Developer proposes to demolish two existing multi-family rental properties, known as the W.G. Reinhardt Apartments, to develop 44 permanent supportive housing units on the Site. The existing W.G. Reinhardt Apartments are a locally designated historical resource. San Diego Municipal Code Section 126.0504(i) requires that developers seeking a Site Development Permit for the demolition of historic resources must provide findings that the denial of the Permit would result in an economic hardship for the Developer.

To that end, an economic analysis has been prepared by The London Group (London) on behalf of the Developer to demonstrate the comparative economic feasibility of three (3) alternative development scenarios proposed for the Site. CivicSD requested that KMA conduct a peer review of the London analysis to determine:

(1) If the assumptions and conclusions used in the analyses are acceptable; and

(2) If any of the alternatives are economically feasible.

II. KEY FINDINGS

Development Alternatives

KMA analyzed three development alternatives for the Site as presented by the Developer and London.

- *Base Project* – Clear the Site of all existing improvements and develop a 44-unit permanent supportive housing development.
- *Alternative #1* – Retain both buildings and rehabilitate them into 13 permanent supportive housing units.
- *Alternative #2* – Retain only the front building and replace the rear building with a new four-story development for a total of 32 permanent supportive housing units on the Site.

KMA Pro Forma Modifications

For each alternative, KMA reviewed the London assumptions regarding product mix, construction cost estimates, net operating income, proposed funding sources, and estimated financing gap. KMA adjusted selected inputs and assumptions, as more fully discussed below. These KMA adjustments resulted in different conclusions from London with respect to the relative economic feasibility of each development alternative. Table II-1 below presents a comparison of the London vs. KMA conclusions in terms of the financing surplus/(deficit) for each alternative.

Table II-1 – Estimate of Financing Surplus/(Gap)– London vs. KMA Adjustments			
	Base Project	Alternative #1	Alternative #2
London			
Financing Surplus/(Gap)	$0	($7.6) M	($4.0) M
KMA Adjustments			
Financing Surplus/(Gap)	$501,000	($6.5) M	($3.8) M

The London analysis finds the Base Project to be the only development alternative without a financing gap. As indicated above, the KMA adjustments resulted in a potentially small financing surplus for the Base Project and substantial financing gaps for Alternatives #1 and #2.

<u>*Threshold Feasibility Questions*</u>

Based on the above financial analysis, KMA provides the following responses to CivicSD's questions for this assignment:

(1) Are the assumptions and conclusions used in the (London) analyses acceptable?

- KMA finds the development cost and operating expense assumptions used by London to be slightly overstated.

(2) Are any of the alternatives economically feasible?

- KMA finds only the Base Project to be potentially economically feasible. Alternatives #1 and #2 would require identification of additional funding sources to support development of the Project.

III. METHOD OF ANALYSIS

The KMA peer review of the London analysis involved using the KMA financial pro forma template to evaluate the development costs, net operating income, and proposed funding sources for the three development alternatives under study. As detailed below, KMA reviewed the inputs and assumptions used in the London analysis, as well as third party cost estimates prepared for the Developer. KMA further compared this information with recent KMA experience with comparable projects and industry standards. The Appendix presents the modified pro formas incorporating the

KMA adjustments. A detailed comparison of the London vs. KMA pro forma analyses is discussed below.

- *Table 1 – Project Description* provides the physical description of the Project. KMA relied on data provided by the site plans to determine the Project's gross building area, Floor Area Ratio, affordability mix, density, and parking count.

- *Table 2 – Estimated Development Costs* presents an estimate of the Project's total development costs. KMA reviewed the costs estimated by the Developer and the Developer's contractor, Allgire General Contractors, Inc. The Developer indicates that the Allgire estimate of construction costs was adjusted to include $250,000 for photovoltaic costs and a 5% multiplier as a boost to threshold cost limits imposed by the Low Income Housing Tax Credit program. For all three scenarios, KMA modified the Developer estimate of parking and shell construction costs to reflect the Allgire estimate and an additional $250,000 for photovoltaic costs.

  In the case of Alternative #1, KMA also adjusted the Developer's estimate of developer fee to a level more appropriate for a 13-unit development (maximum $45,000/unit). KMA also removed syndication costs ($70,000) from the Developer's cost estimate, as Alternative #1 did not include Low Income Housing Tax Credits as a funding source.

  All other costs in the Developer pro formas were found to be reasonable given the level of quality anticipated for the Project and the unique aspects of retaining and rehabilitating older buildings.

  Based on the foregoing, the KMA estimates of development costs were found to be slightly lower than the London Study.

Table III-1 – Estimate of Development Costs – London vs. KMA Adjustments

	Base Project	Alternative #1	Alternative #2
London			
Total Development Costs (1)	$19.4 M	$9.3 M	$15.0 M
KMA Adjustments			
Total Development Costs (1)	$18.9 M	$8.2 M	$14.7 M

(1) Excludes land costs. KMA understands that the Site was donated by Episcopal Community Services.

- *Table 3 – Stabilized Net Operating Income* presents an estimate of the Project's annual net operating income. The following discussion compares the London vs. KMA estimates of net operating income.
  - *Gross Scheduled Income* – The Project will be restricted to households at 30%, 45%, and 50% of Area Median Income. The Developer has also assumed that the Project will receive an annual operating subsidy from Project Based Vouchers for all units. KMA made no adjustments to the Developer's estimate of gross scheduled income.
  - *Operating Expenses* - KMA reviewed operating expense data for other urban affordable housing developments. Based on this review, KMA finds the London estimate of operating expenses and tenant services/amenities to be overstated for Alternatives #1 and #2. As shown in Table III-2, KMA reduced the Developer's estimate of operating expenses on a per-unit basis.

Table III-2 – Estimate of Development Costs – London vs. KMA Adjustments

	Base Project	Alternative #1	Alternative #2
London			
Operating Expenses	\$5,793/Unit	\$11,095/Unit	\$6,809/Unit
Services/Amenities	\$464/Unit	\$1,569/Unit	\$638/Unit
KMA Adjustments			
Operating Expenses	\$5,793/Unit	\$8,000/Unit	\$6,500/Unit
Services/Amenities	\$464/Unit	\$464/Unit	\$464/Unit

As shown in Table III-3, based on the above modifications, the KMA estimates of net operating income were higher than the London Study for both Alternatives #1 and #2.

Table III-3 –Stabilized Net Operating Income– London vs. KMA Adjustments

	Base Project	Alternative #1	Alternative #2
London			
Net Operating Income	\$162,000	(\$46,000)	\$74,000
KMA Adjustments			
Net Operating Income	\$162,000	\$9,000	\$89,000

- *Table 4 – Financing Surplus/(Gap)* presents the estimate of financing surplus or gap for each alternative, calculated as the difference between sources of funds available to the Project less development costs. KMA reviewed the funding sources proposed for the Base Project and Alternative #1 and found them to be reasonable.

  In the case of Alternative #2, KMA made adjustments to the Developer's estimate of Permanent Loan and Tax Credit Equity as follows:

  - *Permanent Loan* – KMA assumed the same loan terms proposed by the Developer for the Alternative #2 Permanent Loan. However, because KMA has assumed lower operating expenses then the Developer, and therefore higher net operating income, the KMA Alternative #2 Permanent Loan is higher than the Developer figure.

  - *Tax Credit Equity* - The Developer's estimate of Low Income Housing Tax Credits assumed a 7% boost to the Project's threshold basis limits for parking provided underneath the Alternative #2 Project. Since Alternative #2 does not include any parking, KMA adjusted the Developer's estimate of Low Income Housing Tax Credits to exclude the 7% basis boost.

  Tables III-4 and III-5, below, provide a summary of the Project's financing surplus/(gap) calculations by alternative for London and KMA, respectively.

Table III-4 – Financing Surplus / (Gap) – London

	Base Project	Alternative #1	Alternative #2
London			
Funding Sources:			
Permanent Loan	$1.9 M	$0	$0.5 M
Tax Credit Equity	$11.5 M	$0	$6.1 M
MHSA Funds	$2.9 M	$0.8 M	$2.1 M
SDHC Loan	$3.1 M	$0.9 M	$2.2 M
Total Sources of Funds	$19.4 M	$1.7 M	$11.0 M
(Less) Development Costs	($19.4) M	($9.3) M	($15.0) M
Financing Gap	**$0**	**($7.6) M**	**($4.0) M**

Table III-5 – Financing Surplus / (Gap) – KMA Adjustments			
	Base Project	Alternative #1	Alternative #2
KMA Adjustments			
Funding Sources:			
Permanent Loan	$1.9 M	$0	$0.7 M
Tax Credit Equity	$11.5 M	$0	$5.8 M
MHSA Funds	$2.9 M	$0.8 M	$2.1 M
SDHC Loan	$3.1 M	$0.9 M	$2.2 M
Total Sources of Funds	$19.4 M	$1.7 M	$10.8 M
(Less) Development Costs	($18.9) M	($8.2) M	($14.7) M
Financing Surplus/(Gap)	**$0.5 M**	**($6.5) M**	**($3.8) M**

IV. LIMITING CONDITIONS

1. KMA has made extensive efforts to confirm the accuracy and timeliness of the information contained in this study. Such information was compiled from a variety of sources deemed to be reliable including state and local government, planning agencies, and other third parties. Although KMA believes all information in this study is correct, it does not guarantee the accuracy of such and assumes no responsibility for inaccuracies in the information provided by third parties.

2. The findings are based on economic rather than political considerations. Therefore, they should be construed neither as a representation nor opinion that government approvals for development can be secured.

3. The analysis, opinions, recommendations, and conclusions of this study are KMA's informed judgment based on market and economic conditions as of the date of this report. Due to the volatility of market conditions and complex dynamics influencing the economic conditions of the building and development industry, conclusions and recommended actions contained herein should not be relied upon as sole input for final business decisions regarding current and future development and planning.

4. The analysis assumes that neither the local nor national economy will experience a major recession. If an unforeseen change occurs in the economy, the conclusions contained herein may no longer be valid.

5. Any estimates of development costs, interest rates, income and/or expense projections are based on the best available project-specific data as well as the experiences of similar projects. They are not intended to be projections of the future for the specific project. No warranty or representation is made that any of the estimates or projections will actually materialize.

attachments

APPENDIX

THE BEACON - 1425 AND 1431 C STREET
PEER REVIEW OF ECONOMIC ALTERNATIVE ANALYSIS

KMA Adjustments

TABLE 1

PROJECT DESCRIPTION
THE BEACON
CIVIC SAN DIEGO

KMA ADJUSTMENTS

	Base Project Demolish Existing Structures Develop 44 Affordable Units		Alternative 1 Retain and Rehabilitate Existing Buildings Develop 13 Affordable Units		Alternative 2 Retain Front Building / Replace Rear Building Develop 32 Affordable Units	
I. Site Area	8,278 SF	0.19 Acres	8,278 SF	0.19 Acres	8,278 SF	0.19 Acres
II. Gross Building Area (GBA) (1)						
A. New Construction						
Net Residential	23,510 SF	92.2%	---	---	8,400 SF	86.1%
Common Area/Circulation	1,987 SF	7.8%	---	---	1,352 SF	13.9%
Total GBA Before Parking	25,497 SF	100.0%	---	---	9,752 SF	100.0%
Parking (2)	5,610 SF		---	---	0 SF	
Total GBA After Parking - New Construction	31,107 SF		---	---	9,752 SF	
B. Rehabilitaton						
Net Residential	---	---	4,660 SF	69.5%	3,000 SF	57.9%
Common Area/Circulation	---	---	2,043 SF	30.5%	2,177 SF	42.1%
Total GBA - Rehabilitation	---	---	6,703 SF	100.0%	5,177 SF	100.0%
C. Total GBA	31,107 SF		6,703 SF		14,929 SF	
III. Approximate Floor Area Ratio (FAR)						
Total FAR	3.76 FAR (3)		0.81 FAR		1.18 FAR	
IV. Market-Rate Units	0 Units	0.0%	0 Units	0.0%	0 Units	0.0%
Affordable Units (2)	44 Units	100.0%	13 Units	100.0%	32 Units	100.0%
Number of Units	44 Units	100.0%	13 Units	100.0%	32 Units	100.0%
Average Unit Size	534 SF		358 SF		356 SF	
V. Density	231.5 Units/Acre		68.4 Units/Acre		168.4 Units/Acre	
VI. Number of Stories	5 Stories		3 Stories		4 Stories	
VII. Construction Type	Type V		Type V		Type V	
VIII. Parking						
Type	Podium					
Spaces	8 Spaces		0 Spaces		0 Spaces	
Ratio	0.18 Spaces/Unit		0.00 Spaces/Unit		0.00 Spaces/Unit	

(1) Base Project site plans dated June 20, 2016. Alternatve 1 and 2 site plans dated February 10, 2016. MW Steele Group, Inc.
(2) Includes parking, bike storage, mechanical, and refuse/storage.
(3) Above grade parking garage included in FAR calculation.

KMA ADJUSTMENTS

TABLE 2

ESTIMATED DEVELOPMENT COSTS
THE BEACON
CIVIC SAN DIEGO

	Base Case: Demolish Existing Structures, Develop 44 Affordable Units			Alternative 1: Retain and Rehabilitate Existing Buildings, Develop 13 Affordable Units			Alternative 2: Retain Front Building / Replace Rear Building, Develop 32 Affordable Units		
	Totals	Per Unit	Comments	Totals	Per Unit	Comments	Totals	Per Unit	Comments
I. Direct Costs (1)									
Sitework	$0	$0	$0 /SF Site Area	$0	$0	$0 /SF Site Area	$0	$0	$0 /SF Site Area
Parking	***$773,000***	***$17,600***	$138 /SF GBA - Parking (2)	$0	$0	No on-site parking	$0	$0	No on-site parking
Shell Construction - New Construction	***$8,747,000***	***$198,800***	$343 /SF GBA - New (3)	$0	$0	$0 /SF GBA - New	***$4,662,000***	***$145,700***	$478 /SF GBA - New
Shell Construction - Rehabilitation	$0	$0	$0 /SF GBA - Rehab.	***$3,399,000***	***$261,500***	$507 /SF GBA - Rehab.	***$1,900,000***	***$59,400***	$367 /SF GBA - Rehab.
FF&E / Amenities	$44,000	$1,000	Allowance	$13,000	$1,000	Allowance	$32,000	$1,000	Allowance
Subtotal	$9,564,000	$217,400	$375 /SF GBA (3)	$3,412,000	$262,500	$509 /SF GBA	$6,594,000	$206,100	$442 /SF GBA
Contingency	$818,000	$18,600	8.6% of Above Directs	$425,000	$32,700	12.5% of Above Directs	$820,000	$25,600	12.4% of Above Directs
Total Direct Costs	$10,382,000	$236,000	$407 /SF GBA (3)	$3,837,000	$295,200	$572 /SF GBA	$7,414,000	$231,700	$497 /SF GBA
II. Indirect Costs									
Indirect Costs	$2,798,000	$63,600	27.0% of Directs	$1,941,000	$149,300	50.6% of Directs	$2,537,000	$79,300	34.2% of Directs
Developer Fee	$1,400,000	$31,800	13.5% of Directs	$585,000	$45,000	15.2% of Directs	$1,400,000	$43,800	18.9% of Directs
Total Indirect Costs	$4,198,000	$95,400	40.4% of Directs	$2,526,000	$194,300	65.8% of Directs	$3,937,000	$123,000	53.1% of Directs
III. Financing Costs									
Financing Costs	$1,473,000	$33,500	14.2% of Directs	***$1,076,000***	***$82,800***	28.0% of Directs	$1,290,000	$40,300	17.4% of Directs
Services Reserve	$2,833,000	$64,400	27.3% of Directs	$810,000	$62,300	21.1% of Directs	$2,024,000	$63,300	27.3% of Directs
Total Financing Costs	$4,306,000	$97,900	41.5% of Directs	$1,886,000	$145,100	49.2% of Directs	$3,314,000	$103,600	44.7% of Directs
IV. Total Development Costs - excluding Land (4)	**$18,886,000**	**$429,200**	**$741 /SF GBA (3)**	**$8,249,000**	**$634,500**	**$1,231 /SF GBA**	**$14,665,000**	**$458,300**	**$982 /SF GBA**

(1) Includes the payment of prevailing wages.
(2) Includes parking, bike storage, mechanical, and refuse/storage.
(3) Per SF GBA excluding parking.
(4) KMA understands that the Site was donated by Episcopal Community Services.
KMA adjustments to Developer's pro forma appear in bold and italics.

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TABLE 3

STABILIZED NET OPERATING INCOME
THE BEACON
CIVIC SAN DIEGO

		Base Project: Demolish Existing Structures, Develop 44 Affordable Units				
		Average Unit Size	# of Units	$/Month	Section 8 Subsidy	Total Annual
I. Gross Scheduled Income						
Studio	@ 30% AMI	534 SF	22	$425	$517	$248,688
Studio	@ 45% AMI	534 SF	10	$637	$305	$113,040
Studio	@ 50% AMI	534 SF	11	$708	$234	$124,344
Subtotal		534 SF	43	$547	$395	$486,072
One Bedroom	Manager		1	$0	$0	$0
Total			44	$547	$395	$486,072
Add: Other Income			$10	/Unit/Month		$5,280
Total Gross Scheduled Income						$491,352
II. Effective Gross Income						
Vacancy			5.0% of GSI			($24,568)
Total Effective Gross Income						$466,784
III. Operating Expenses						
(Less) Operating Expenses			$5,793	/Unit/Year		($254,906)
(Less) Services/Amenities			$464	/Unit/Year		($20,400)
(Less) Replacement Reserves			$300	/Unit/Year		($13,200)
(Less) Property Taxes			$182	/Unit/Year		($8,000)
(Less) Monitoring Fee			$189	/Unit/Year		($8,300)
Total Expenses			$6,927	/Unit/Year		($304,806)
IV. Net Operating Income						$161,978

		Alternative 1: Retain and Rehabilitate Existing Buildings, Develop 13 Affordable Units				
		Average Unit Size	# of Units	$/Month	Section 8 Subsidy	Total Annual
I. Gross Scheduled Income						
Studio	@ 30% AMI	358 SF	6	$425	$517	$67,824
Studio	@ 45% AMI	358 SF	3	$637	$305	$33,912
Studio	@ 50% AMI	358 SF	3	$708	$234	$33,912
Subtotal		358 SF	12	$549	$393	$135,648
One Bedroom	Manager		1	$0	$0	$0
Total			13	$549	$393	$135,648
Add: Other Income			$10	/Unit/Month		$1,560
Total Gross Scheduled Income						$137,208
II. Effective Gross Income						
Vacancy			5.0% of GSI			($6,860)
Total Effective Gross Income						$130,348
III. Operating Expenses						
(Less) Operating Expenses			***$8,000***	/Unit/Year		($104,000)
(Less) Services/Amenities			***$464***	/Unit/Year		($6,000)
(Less) Replacement Reserves			$300	/Unit/Year		($3,900)
(Less) Property Taxes			$308	/Unit/Year		($4,000)
(Less) Monitoring Fee			$281	/Unit/Year		($3,650)
Total Expenses			$9,350	/Unit/Year		($121,550)
IV. Net Operating Income						$8,798

		Alternative 2: Retain Front Building / Replace Rear Building, Develop 32 Affordable Units				
		Average Unit Size	# of Units	$/Month	Section 8 Subsidy	Total Annual
I. Gross Scheduled Income						
Studio	@ 30% AMI	356 SF	16	$425	$517	$180,864
Studio	@ 45% AMI	356 SF	8	$637	$305	$90,432
Studio	@ 50% AMI	356 SF	7	$708	$234	$79,128
Subtotal		356 SF	31	$544	$398	$350,424
One Bedroom	Manager		1	$0	$0	$0
Total			32	$544	$398	$350,424
Add: Other Income			$10	/Unit/Month		$3,840
Total Gross Scheduled Income						$354,264
II. Effective Gross Income						
Vacancy			5.0% of GSI			($17,713)
Total Effective Gross Income						$336,551
III. Operating Expenses						
(Less) Operating Expenses			***$6,500***	/Unit/Year		($208,000)
(Less) Services/Amenities			***$464***	/Unit/Year		($15,000)
(Less) Replacement Reserves			$300	/Unit/Year		($9,600)
(Less) Property Taxes			$250	/Unit/Year		($8,000)
(Less) Monitoring Fee			$203	/Unit/Year		($6,500)
Total Expenses			$7,722	/Unit/Year		($247,100)
IV. Net Operating Income						$89,451

KMA adjustments to Developer's pro forma appear in bold and italics.

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TABLE 4

FINANCING SURPLUS/(GAP)
THE BEACON
CIVIC SAN DIEGO

	Base Project Demolish Existing Structures Develop 44 Affordable Units		Alternative 1 Retain and Rehabilitate Existing Buildings Develop 13 Affordable Units		Alternative 2 Retain Front Building / Replace Rear Building Develop 32 Affordable Units	
	Total	Per Unit	Total	Per Unit	Total	Per Unit
I. Sources of Funds						
Permanent Loan	$1,933,000	$44,000	$0	$0	***$656,000***	$21,000
Low Income Housing Tax Credit Equity	$11,479,000	$260,900	$0	$0	***$5,830,000***	$182,000
MHSA Funds	$2,895,000	$65,800	$790,000	$61,000	$2,105,000	$66,000
SDHC Loan	$3,080,000	$70,000	$910,000	$70,000	$2,240,000	$70,000
Total Sources of Funds	$19,387,000	$441,000	$1,700,000	$131,000	$10,831,000	$338,000
II. (Less) Development Costs (1)	($18,886,000)	($429,000)	($8,249,000)	($635,000)	($14,665,000)	($458,000)
III. Financing Gap	**$501,000**	**$12,000**	**($6,549,000)**	**($504,000)**	**($3,834,000)**	**($120,000)**

(1) Excludes land costs. KMA understands that the Site was donated by Episcopal Community Services.

KMA adjustments to Developer's pro forma appear in bold and Italics.

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