Inclusionary Housing Analysis of Divisadero and Fillmore Street Rezoning

CITY & COUNTY OF SAN FRANCISCO

Office of the Controller
City Planning Department

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Reason for This Report

- In August, 2017, Ordinance 158-17 went into effect, which created a new requirement to study if significant rezoning creates the potential to increase inclusionary housing requirements, without undermining financial feasibility.
- The Planning Department has determined that this study is required for the 2015 rezonings of Neighborhood Commercial Districts (NCDs) to Neighborhood Commercial Transit Districts (NCTs) on Fillmore and Divisadero Streets.
- This report was prepared to summarize the key assumptions and findings of an economic feasibility study for these areas. This study was designed to estimate, for illustrative purposes only, the maximum potential on-site inclusionary housing requirement that would be economically feasible for a prototypical development project in these zoning districts, under current economic conditions and assuming that the entire amount of any value increase effected by the re-zoning would be absorbed by the on-site inclusionary requirement.

Feasibility Studies and the Land Residual Method

- In 2016, the Controller's Office, other City staff, a team of consultants, and the Inclusionary Housing Technical Advisory Committee studied how the financial feasibility of prototypical housing projects in San Francisco would be affected by different city-wide inclusionary housing requirements.
- For this study, a third-party consultant worked with the same City departments to prepare the study and used the same general methodology as in 2016. Project prototypes that are representative of typical projects in these parts of the city were developed.
- Under prevailing housing prices, development costs (excluding land), inclusionary housing and other fees, and rate of return, the project's financial model generates a "residual land value": a maximum expenditure on land before a project is no longer feasible for the developer. If that amount meets or exceeds the value expectations of potential land sellers—then land may potentially transact for development of new housing.

Estimating the Maximum Inclusionary Housing

- Two prototypes were prepared first to estimate the land residual values under the old zoning.
- The prototype projects were then revised to reflect different potential development options, based on the increased development capacity of the new zoning. Holding all other factors constant, these new prototype projects, with increased unit counts, would be anticipated to result in higher estimated land residual values.
- Raising inclusionary housing requirements for the new prototype projects, however, would lower the estimated land residual values. For illustrative purposes only, the assumed inclusionary housing requirement for each new prototype project was increased until the estimated land residual value equaled the estimated residual land value under the old zoning.

The Prototypes

- Prototype A generally reflects a potential project typology in the Divisadero NCT, where the residential density limit was changed from a maximum of 1 unit per 800 square feet of lot area to no limit, and the most prevalent height district for potential development sites in the district is 65' feet.
- Prototype B generally reflects a potential project typology in the Fillmore NCT, where the residential density limit was changed from a maximum of 1 unit per 600 square feet of lot area to no limit, and the most prevalent height district for potential development sites in the district is 50' feet.
- Because the original density limitations were more restrictive and the prevalent height district is higher on Divisadero Street, the elimination of density controls has a greater potential impact on the estimated residual land value generated by development there than on Fillmore Street.

The Pro Forma Models

- For each of the two prototypes, four different scenarios were examined:
  1. a baseline case, under the old zoning, assuming the projects were to be developed as for-sale condominiums
  2. potential for-sale condominium development under the new zoning, allowing more housing units, with more inclusionary housing.
  3. potential for-rent apartment development under the new zoning, with more inclusionary housing, assuming constant rent over the next 2 years.
  4. potential for-rent apartment development under the new zoning, with more inclusionary housing, assuming growing rent over the next 2 years.

Construction Details

- Reflecting the greater impact of the re-zoning on Divisadero Street, residential gross square footage is projected to increase by approximately 100% for the Divisadero prototype, but only by approximately 30% for the Fillmore prototype.
- The number of units in the Divisadero prototype is projected to rise from 16 to 47 for a condominium project, and 53 for an apartment project. The Fillmore prototype is projected to grow from 21 units to 37 (condominiums) or 43 (apartments), under the new zoning. Actual project unit counts may vary in each NCT; in which case, the prototype analysis may not be applicable.
- The unit count grows by more than the residential square footage, because the units are expected to be smaller, on average.
- Because both projects would, under the old zoning, have fewer than 25 units, they would only have a 12% inclusionary housing requirement.
- Specific assumptions related to construction are shown on the next page.

Construction Details

	Prototype A: Divisadero	Prototype B: Fillmore
Old Zoning		
Height (feet)	35	35
Residential Square Footage	24,000	29,625
# of Units	16	21
New Zoning - Condos		
Height (feet)	65	50
Residential Square Footage	48,375	39,000
# of Units	47	37
New Zoning - Apartments		
Height (feet)	65	50
Residential Square Footage	48,375	39,000
# of Units	53	42

Financial Details

- Research was conducted to identify current (late 2017-early 2018) cost and revenue information for each prototype scenario. The findings are summarized on the next slide. In general, research showed a significant increase in costs, and only a limited increase, if any, in prices and rents, since 2016.
- Costs per net square foot (NSF), which are also reported on the next page, vary between the two prototypes due to project size and program differences.
- Rents at the time of completion are assumed to be approximately 2% higher in the growing-rent scenario, compared to current rents.

Financial Details

	Prototype A: Divisadero	Prototype B: Fillmore
Old Zoning – Condos:		
Weighted Price/Rent per unit, market-rate	$1,343,000	$1,311,000
Total Cost per NSF	$784	$811
New Zoning – Condos:		
Weighted Price/Rent per unit, market-rate	$973,000	$993,000
Total Cost per NSF	$758	$832
New Zoning – Apartment (Current Rent):		
Weighted Price/Rent per unit, market-rate	$3,650/month	$3,785/month
Total Cost per NSF	$748	$841
New Zoning – Apartment (Growing Rent)		
Weighted Price/Rent per unit, market-rate	$3,725/month	$3,850/month
Total Cost per NSF	$748	$840

Results

- The old-zoning prototypes used an inclusionary housing requirement of 12%, all at the low-income tier, because these projects would have less than 25 units.
- As discussed earlier, for illustrative purposes only, the inclusionary housing requirements for the four new zoning scenarios were set to equalize the residual land values to what they would be under the old zoning.
- The new-zoning prototypes assumed that, for condominiums, 50% of the inclusionary housing would go to low-income, 25% to moderate-income, and 25% to middle-income households and, for apartments, 56% of the inclusionary housing would go to low-income, 22% to moderate-income, and 22% to middle-income households.

Results

	Prototype A: Divisadero	Prototype B: Fillmore
Old Zoning – Condos:		
Inclusionary Requirement	12%	12%
Total Land Residual Value	$2.3 Million	$3.9 Million
New Zoning – Condos		
Maximum Inclusionary	23%	13%
Total Land Residual Value	$2.3 Million	$3.9 Million
New Zoning–Apartment (Current Rent)		
Maximum Inclusionary	20%	5%
Total Land Residual Value	$2.3 Million	$3.9 Million
New Zoning–Apartment (Growing Rent)		
Maximum Inclusionary	22%	10%
Total Land Residual Value	$2.3 Million	$3.9 Million

Conclusions

- The Divisadero prototype can support a maximum inclusionary housing requirement that is slightly higher than the current citywide inclusionary requirements adopted in 2017. This finding reflects the level of density increase established by the re-zoning in the Divisadero NCT, and an assumption – for the illustrative purposes of this analysis – that the residual land value of development sites would reflect land values under the previous density limit, with all additional value accruing to the development project.
- However, because the Fillmore Street rezoning resulted in a lower increase in residential development capacity, the Fillmore Street NCT prototype cannot support additional inclusionary housing requirements under current market conditions.
- In today's market, the Fillmore Street NCT prototype would not be feasible even with the current citywide inclusionary requirements for projects with more than 25 units.

Summary Table

NCT Feasibility Study - Fixed Land Value

CITY & COUNTY OF SAN FRANCISCO - NCT INCLUSIONARY HOUSING FEASIBILITY ANALYSIS

Inclusionary Scenario	Prototype A - Base Condominiums	Prototype B - Base Condominiums	Prototype A - Alternate Condominiums	Prototype B - Alternate Condominiums	Prototype A - Alternate Apartments - Current Rent	Prototype B - Alternate Apartments - Current Rent	Prototype A - Alternate Apartments - Growing Rent	Prototype B - Alternate Apartments - Growing Rent
Affordability Assumption	12% at 80% AMI	12% at 80% AMI	11.5% at 80% AMI 5.8% at 105% AMI 5.8% at 130% AMI	6.5% at 80% AMI 3.3% at 105% AMI 3.3% at 130% AMI	11.1% at 55% AMI 4.4% at 80% 4MI 4.4% at 110% AMI	2.8% at 55% AMI 1.1% at 80% AMI 1.1% at 110% AMI	12.2% at 55% AMI 4.9% at 80% 4MI 4.9% at 110% AMI	5.6% at 55% AMI 2.2% at 80% AMI 2.2% at 110% AMI
Total Inclusionary Percentage Assumption	12%	12%	23%	13%	20%	5%	22%	10%
Programmatic Summary:								
1.) Construction Typology	Type V	Type V	Type V	Type V	Type V	Type V	Type V	Type V
2.) Product Type	Condominiums	Condominiums	Condominiums	Condominiums	Apartments	Apartments	Apartments	Apartments
3.) Building Stories	3 Stories	3 Stories	6 Stories	5 Stories	6 Stories	5 Stories	6 Stories	5 Stories
4.) Building Height	35 Feet	35 Feet	65 Feet	50 Feet	65 Feet	50 Feet	65 Feet	50 Feet
5.) Efficiency Factor	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%	80.0%
6.) **Gross Square Feet:**								
7.) Residential	24,000	29,625	48,375	39,000	48,375	39,000	48,375	39,000
8.) Retail	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500
9.) Parking	3,500	5,375	5,375	5,375	5,375	5,375	5,375	5,375
10.) Total Gross Square Feet	30,000	37,500	56,250	46,875	56,250	46,875	56,250	46,875
11.) Unit Count	16	21	47	37	53	42	53	42
12.) Average Unit Size	1125 NSF	1071 NSF	798 NSF	811 NSF	708 NSF	714 NSF	708 NSF	714 NSF
13.) Parking Ratio	0.56:1	0.67:1	0.30:1	0.38:1	0.26:1	0.33:1	0.26:1	0.33:1
14.) Parking Stalls	9	14	14	14	14	14	14	14
15.) Parking Type	At Grade	At Grade	At Grade	At Grade	At Grade	At Grade	At Grade	At Grade
Project Budget (Total / Unit):								
16.) Land Cost	$2.3M / $145,000	$3.9M / $186,000	$2.3M / $50,000	$3.9M / $106,000	$2.3M / $44,000	$3.9M / $93,000	$2.3M / $44,000	$3.9M / $93,000
17.) Hard Cost	$9.9M / $616,000	$11.7M / $557,000	$20.7M / $440,000	$16.8M / $455,000	$21.5M / $405,000	$18.1M / $430,000	$21.5M / $405,000	$18.1M / $430,000
18.) City Required Impact & Other Fees	$0.9M / $55,000	$1.0M / $48,000	$1.4M / $31,000	$1.2M / $33,000	$1.5M / $28,000	$1.3M / $30,000	$1.5M / $28,000	$1.3M / $30,000
19.) Soft Cost Excl. City Fees	$2.8M / $175,000	$3.5M / $165,000	$5.7M / $120,000	$4.9M / $132,000	$4.5M / $84,000	$3.9M / $93,000	$4.5M / $84,000	$3.9M / $92,000
20.) Total Project Budget	$15.9M / $992,000	$20.1M / $956,000	$30.1M / $641,000	$26.8M / $725,000	$29.7M / $561,000	$27.1M / $645,000	$29.7M / $561,000	$27.1M / $645,000
21.) *Total Cost per NSF*	*$784*	*$811*	*$758*	*$832*	*$748*	*$841*	*$748*	*$840*
22.) *Total Cost per GSF*	*$529*	*$535*	*$535*	*$572*	*$529*	*$578*	*$529*	*$578*
Schedule Summary:								
23.) Construction Start	Nov-18	Nov-18	Jan-19	Jan-19	Jan-19	Jan-19	Jan-19	Jan-19
24.) Months of Construction	16 Months	18 Months	20 Months	20 Months	20 Months	18 Months	20 Months	18 Months
25.) Construction End	Mar-20	May-20	Sep-20	Sep-20	Sep-20	Jul-20	Sep-20	Jul-20
Market Rate Units:								
26.) Market Rate Units	14 Units	18 Units	36 Units	32 Units	42 Units	40 Units	41 Units	38 Units
27.) Wtd. Average Sales Price/Rent	$1,343,000 / $1,205	$1,311,000 / $1,208	$973,000 / $1,210	$993,000 / $1,214	$3,700 / $5.15	$3,800 / $5.30	$3,700 / $5.26	$3,900 / $5.39
Inclusionary Housing Units:								
28.) Inclusionary Units	2 Units	3 Units	11 Units	5 Units	11 Units	2 Units	12 Units	4 Units
29.) Wtd. Average Sales Price/Rent	$309,000 / $257	$296,000 / $300	$351,000 / $451	$350,000 / $458	$1,700 / $2.45	$1,300 / $1.57	$1,600 / $2.27	$1,400 / $1.97
30.) *% of Total Unit Count*	*12.5%*	*14.3%*	*23.4%*	*13.5%*	*20.8%*	*4.8%*	*22.6%*	*9.5%*
Project Economics:								
31.) Minimum Target Return	20.0%	20.0%	21.3%	20.1%	5.0%	5.0%	5.0%	5.0%
32.) Residential Land Price per Unit	$145,000	$186,000	$50,000	$106,000	$44,000	$93,000	$44,000	$93,000

**** All financial and programmatic estimates are preliminary in nature for illustrative purposes and subject to change. ****

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