CITY OF RIVERSIDE

City of Arts & Innovation

Finance Committee Memorandum

TO: FINANCE COMMITTEE **DATE: JULY 11, 2018**

FROM: FINANCE DEPARTMENT **WARDS: ALL**
COMMUNITY & ECONOMIC DEVELOPMENT DEPARTMENT

SUBJECT: MONETIZATION OF CITY ASSETS – LAND DEVELOPMENT

ISSUE:

Review and provide input on land development options for land owned by the City.

RECOMMENDATIONS:

That the Finance Committee review and provide input on land development options for land owned by the City.

LEGISLATIVE HISTORY:

The Charter of the City of Riverside, Article IV. City Council and Mayor, Section 418. Contracts-Restriction on Duration, states that, "The City Council shall not have the power to make or authorize any contract or lease or extension thereof for a longer period than shall be provided by the laws of the State of California with respect to general law cities unless said contract, lease or extension be approved by a majority of the qualified electors of the City voting on such question at any election. A contract, lease or extension for a longer period shall be valid without such approval if it provides for the right of acquisition by the City at the end of such period of the real or personal property leased or contracted for. This section shall not apply to airports or to any franchise granted pursuant to the provisions of this Charter or to any contract for the furnishing, or acquisition of the products, commodity or services of any public utility."

According to California Civil Code, Section 718, "….The property owned by, or that held by, or under the management and control of, any municipality, or any department or board thereof, may be leased for a period not to exceed 55 years."

BACKGROUND:

At the February 14, 2018 Finance Committee meeting, Chair Adams requested a report on the financial benefits of leasing or selling city owned property.

DISCUSSION:

The City is the owner of substantial real property, which is used for various municipal purposes. As public service needs change, the requirements for these properties may be revised and, on occasion, certain parcels may be in excess of the City's current need. This requires that each individual property be reviewed in terms of its potential for future public use, as well as its potential economic benefit to the City.

There are factors that need to be considered in determining whether a specific City-owned property should be sold, including whether the sale of the property will generate greater economic value than a ground lease, or if a ground lease is a better economic option. To demonstrate, staff has developed the following hypothetical and actual examples, to determine when a direct sale or when a ground lease is more economically advantageous for the City.

Hypothetical Example (Direct Sale of City Property): Lot 33 Development (Convention Center)

A portion of City-owned public parking Lot 33 is approximately 3.01 acres (as highlighted in red on the site map below) and the staff-estimated current fair market value for it is approximately $4.6 million (or $35 per square foot). Should Lot 33 be privately developed with a mixed-use hotel, retail space and residential units, in a total amount of $200,000,000, the City can expect to receive approximately $280,000 in annual property tax revenue (not including Transient Occupancy and Sales taxes). Conversely, staff estimates that a 55-year fair market ground lease could generate approximately $184,000 in annual lease revenue. However, based on staff's discussions with multiple developers, it is highly unlikely that a developer will consider a ground lease for residential/hotel development since it is extremely difficult to find lenders willing to loan money on this kind of ground lease. Staff has had some developers flat out reject a ground lease for residential projects and one developer has indicated that unless the lease term is 75 years or longer, which conflicts with the City's Charter which only allows up to 55 years for lease agreements, they would not consider development using a ground lease agreement.

Under this example, the sale of the property would be preferred, as the City would net more annually in property taxes than lease revenue. Over a 55-year period, the City would receive a total of $20 million from the sale of the land valued at $4.6 million plus property tax payments of $280,000 annually totaling $15.4 million, versus receiving approximately $10.12 million (exclusive of future rent increases) from annual ground lease payments of $184,000 over the 55-year term of the lease. Additionally, under a direct sale agreement, staff would not be responsible for administering a lease agreement and the City would not be financially responsible for property maintenance and other infrastructure requirements.

<u>Actual Example (Lease of City Property at San Bernardino Golf Course): GWS#4 Development, LLC (Hillwood)</u>

The former San Bernardino public golf club site, located in the City of San Bernardino, is owned by the City and controlled by Riverside Public Utilities, who has existing water wells on the site. On March 7, 2017, City Council approved a 55-year ground lease with GSW#4, Development, LLP, a Hillwood entity. As part of this transaction, J.G. Golfing, who operated the former San Bernardino Golff Course since 1979, assigned its lease over to Hillwood. Hillwood is required to relocate any existing water wells to accommodate its planned development of an approximately 1,065,000 square foot logistics warehouse distribution building. The site is approximately 62 acres and staff-estimates the current fair market value is $27 million (or $10 per square foot).

When the property is privately developed into a large industrial warehouse, in an estimated amount of $100,000,000, the City of San Bernardino would receive approximately $140,000 in annual property tax revenue (if the property were to be sold). However, the existing 55-year lease with GWS#4 Development, LLC (Hillwood) will generate revenue of $1,113,192 annually less an annual rent credit of $643,440 for the first 15 years to cover the prior lease buy-out and well relocation costs, and will result in total lease revenue of approximately $51.6 million (exclusive of future rent increases) for the City.

Under this example, the 55-year ground lease would be preferred, as the City would net more revenue since the ground lease payments far exceed the value of the property. Over a 55-year lease term, the City will receive approximately $51.6 million in ground lease payments (exclusive of future rent increases) versus receiving $27 million from the sale of the property and no property tax revenue, since the property is located in the city of San Bernardino and not Riverside. Furthermore, the land and all improvements will revert back to the City of Riverside upon expiration of the lease.

In summary, each property should be reviewed on a case-by-case basis to determine if an outright sale or long term ground lease will be more economically preferential to maximize value to the City.

FISCAL IMPACT:

There is no fiscal impact associated with the recommendations in this report.

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Attachment: Presentation