

Memorandum

To: Fahteen Khan and Corinna Sandmeier, City of Menlo Park

From: Chelsea Guerrero, Vice President
Stephanie Hagar, Principal

Date: August 30, 2024

Re: Evaluation of 3705 Haven Avenue Community Amenities Proposal

Purpose

This memorandum provides BAE's assessment of the value of the community amenities proposal for the proposed residential project at 3705 Haven Avenue in Menlo Park. The City-approved appraisal for the project site identified a required amenity value of \$2,100,000, and the project applicant has submitted a community amenities proposal that consists of three very low-income below-market-rate (BMR) units. The applicant has provided an assessment of the value of the community amenities proposal that estimates a total value of \$2,312,620. This memorandum does not assess whether the proposed amenity is appropriate, falls within the current amenity list adopted by City Council resolution, or whether the same amenity has already been provided by another applicant. This memorandum evaluates the methodology and key assumptions that the applicant used to determine the value of the proposed community amenity and provides BAE's determination of the value.

Key Findings

Table 2 below provides a summary of the value of the community amenities proposal that the project applicant has proposed as part of a request for bonus level development for a proposed project located at 3705 Haven Avenue in Menlo Park. As shown, BAE found that the value of the proposed community amenity is an estimated \$3,840,117, exceeding the minimum required \$2.1 million value.

Table 1: Summary of Community Amenity Proposal Valuation for Proposed 3705 Haven Avenue Project

	Dedication of Three Very Low-Income BMR Units	Shortfall (Compared to \$2.1 million Required)
Applicant Valuation	\$2,312,620 <i>Methodology: Incremental Total Construction Cost</i>	N/A
BAE Valuation	\$3,840,117 <i>Methodology: Adjusted Incremental Residential Construction Cost</i>	N/A

Project Description

The proposed project at 3705 Haven Avenue in Menlo Park consists of 112 multifamily rental units and a parking garage with 104 parking spaces. The project site is located within the Bayfront Area of Menlo Park and the project applicant is seeking entitlements to construct the project at the bonus level of development pursuant to the City's community amenities program for the Residential Mixed-Use Bonus (R-MU-B) zoning district. The R-MU-B zoning district allows a project to develop at a greater level of intensity with an increase in density, floor area ratio, and/or height in exchange for providing community amenities, which are intended to address identified community needs that result from the effect of the increased development intensity on the surrounding community. Community amenities also enable the surrounding community to benefit from the substantial increase in project value that is attributable to the increase in density, floor area, and/or height. Full project details are available on the City of Menlo Park website (<https://menlopark.gov/Government/Departments/Community-Development/Projects/Under-review/3705-Haven-Ave>).

Community Amenities Proposal

Because the project would be built at the bonus level of development, the project applicant is required to provide community amenities in exchange for the additional development potential that is allowable under the bonus level of development. In the case of the subject project, an appraisal commissioned by the City (available on the City website at the link shown above) determined that the value of the community amenity must equal a minimum of \$2,100,000.

The project applicant has provided a community amenities proposal that consists of three BMR units that would be affordable to very low-income households, including one one-bedroom unit and two two-bedroom units. In addition to the three very low-income BMR units that would count toward the applicant's community amenity contribution, the project would include an additional eleven BMR units, including seven very low-income units and four moderate-income units, which would not count toward the community amenity requirement for the project.

Valuation of Community Amenities Proposal

The project applicant has provided an assessment of the value of the community amenity proposal described above. This section describes the applicant's methodology for assigning a value to each component of the proposal, presents BAE's methodology for assigning a value to each component, and provides BAE's determination of the value of each component.

Valuation of BMR Units

The project applicant's community amenities valuation estimated the value of the three BMR units based on an incremental cost approach that assigned a value to each BMR unit based on the total estimated construction costs for the residential space, amenities, and the parking garage, divided by the number of units in the project. Although the City values community amenity proposals using an incremental cost approach, the overall approach and methodology that the applicant used for the valuation is not consistent with the City's approach due to the inclusion of additional costs that are not related to the increased costs of constructing the three BMR units. The applicant's incremental cost estimate for the BMR units includes costs that the developer would incur regardless of whether the three BMR units were included in the project, and therefore overestimates the incremental cost associated with providing these three units. Certain costs associated with developing the project, such as construction costs for tenant amenity space, would be incurred regardless and are not affected by the inclusion of the three additional BMR units, and therefore should not be part of the incremental cost associated with providing the three BMR units as a community amenity. In addition, prior community amenities proposal evaluations have used the incremental cost approach to estimate the value of providing low-income BMR rental units, consistent with the affordability levels required for BMR rental units under the City's BMR housing program, as community amenities in a project. Because the proposed community amenity includes very low-income BMR units that are more affordable than standard low-income BMR rental units, without any further adjustment to account for the larger rent subsidy, the incremental cost approach does not capture the higher value of the very low-income units as an amenity to the community as compared to BMR rental units affordable to low-income households. Therefore, an adjusted incremental valuation approach is appropriate to evaluate the benefit or value to the community that is anticipated in exchange for the effects of the increase in density, floor area, or height at the bonus level of development.

BAE's analysis also values each of the three proposed BMR units based on the incremental costs associated with constructing the units as separate components within the project; however, BAE's analysis properly factors out costs that the developer would incur regardless of whether the project included the three BMR units and includes an adjustment to account for the very low-income affordability levels of the proposed BMR units for consistency with prior community amenities proposal evaluations. This approach results in a more accurate valuation of the proposed BMR units.

Project Applicant Valuation of BMR Units. The applicant's valuation of the three BMR units is based on an estimate of the total hard construction costs for the proposed project, inclusive of all residential space, amenities, and the parking garage, with an additional soft cost allowance. The applicant then adjusted the total hard costs to remove a portion of the construction cost that would not be affected by the construction of the three BMR units. The applicant then divided the adjusted hard and soft construction cost for the building across all units in the project to provide an adjusted per-unit construction cost and applied that adjusted per-unit cost to the three BMR units to estimate the value of the proposed community amenities contribution. While this approach is generally consistent with the overall concept of the incremental construction cost approach, further adjustments are needed.

The applicant's hard cost estimate for the project totals approximately \$77.7 million, comprised of \$66.3 million in hard costs for the residential portion of the building plus approximately \$11.4 million in hard costs for the parking garage. To exclude costs that would not be included in the incremental hard costs associated with constructing the three BMR units, the applicant deducted seven percent of the project's total hard costs for the residential portion of the building (\$4.6 million) and 20 percent of the project's total hard costs for the parking garage (\$2.3 million). The applicant based the seven-percent deduction for the residential building and the 20-percent deduction for the parking garage on the share of total hard costs that were removed from the incremental hard construction cost in a prior community amenities proposal evaluation for a project at 111 Independence Drive. In the case of the community amenities proposal evaluation for the project at 111 Independence Drive, the seven-percent deduction for the residential portion of the project was applied to the portion of the construction budget that covered the residential units in the project and associated circulation, which had already been adjusted to remove construction costs associated with the construction of building amenities. In the case of the subject project, the estimated construction budget for the residential portion of the building covers the entire residential portion of the building, including amenity space. Therefore, further adjustments to the applicant's hard construction costs are needed to remove the cost of constructing building amenities.

The applicant's valuation includes soft costs equal to 20 percent of the total hard costs for the building (\$15.5 million, or 20 percent of \$77.7 million). The approach overstates the soft cost allowance attributable to the incremental construction costs of the three BMR units by applying the 20-percent allowance to the total estimated hard construction costs for the entire project, rather than to the incremental hard construction costs.

The project applicant's total valuation of the project equals \$86.3 million, or \$770,873 per unit (\$86,337,831 total estimated incremental hard costs and total project soft costs ÷ 112 units in project). Based on this estimate, the applicant's valuation assesses the value of the three BMR units at \$2.3 million (\$770,873 per unit x 3 BMR units). These calculations are shown in Table 2 below.

Table 2: Applicant Valuation of BMR Units Provided as a Community Amenity

Total Building Hard Costs (Residential & Amenities/Back of House)	\$66,344,591
Less: Costs not Included in Incremental BMR Unit Costs	(\$4,644,121)
Total Garage Hard Costs	\$11,368,443
Less: Costs not Included in Incremental BMR Unit Costs	(\$2,273,689)
Soft Costs	\$15,542,607
Total	\$86,337,831
<i>per Unit</i>	<i>\$770,873</i>
 Value of 3 BMR Units	 \$2,312,620

Assumptions

Total Units in Project	112
BMR Units Provided as Community Amenities	3
 % of Residential/Amenity Hard Costs not Included in Incremental BMR Unit Cost:	 7%
% of Total Garage Hard Costs not Included in Incremental BMR Unit Costs	20%
 Soft Costs as a % of Incremental BMR Unit Hard Construction Costs	 22%

Sources: 3705 Haven LLC; BAE, 2024.

BAE Valuation of BMR Units. As mentioned above, BAE's valuation of the proposed BMR units is based on the estimated incremental cost associated with providing the three BMR units as a community amenity, net of all costs that the project applicant would incur regardless of whether these units are included in the project, adjusted to account for the very low-income affordability levels of the proposed BMR units. Consistent with prior community amenities proposal evaluations, BAE's incremental cost estimate excludes the costs of constructing tenant amenity spaces since these costs would be incurred regardless and are not affected by the inclusion of the three additional BMR units.

To estimate residential hard construction costs for the project, this analysis evaluated the applicant's hard construction cost estimate for the building (\$66,344,591, or \$563.29 per square foot) but omitted the cost of tenant amenity space, the lobby, and back of house areas. This analysis assumes that the lobby, tenant amenities, and back-of-house areas would essentially be unchanged by the inclusion of the three BMR units, compared to a scenario in which the project has three fewer units. As shown in Table 3, the applicant's hard construction cost per square foot estimate for the building (\$563.29 per square foot) was applied to the total square footage of the lobby/amenity and back of house areas (7,334 square feet) to estimate the costs of the lobby/residential amenity areas and back of house/utilities/maintenance/IT areas. These costs were removed from the applicant's hard construction cost estimate for the building (\$66,344,591) to estimate residential hard construction costs for the project (\$62,213,439). BAE then adjusted the hard cost estimate for residential space to remove the portion of the total costs that would not be directly impacted by the construction of the three BMR units. Consistent with prior community

amenities proposal evaluations, this analysis assumes that costs for items such as demolition, sitework, landscaping, the foundation, and the roof would essentially be unchanged by the inclusion of the three additional BMR units. Like the applicant, BAE estimated the incremental residential costs for the project based on the share of estimated residential hard costs not included in incremental unit costs as identified in a prior community amenities proposal evaluation for a generally comparable project at 111 Independence Drive (7.2 percent). As shown in the table, these calculations result in estimated incremental residential hard costs totaling \$57,734,071, or \$522.73 per gross residential square foot.

Like the applicant, BAE adjusted the hard cost estimate for the parking garage to remove items that would not be directly impacted by the construction of the proposed BMR units based on the share of estimated parking garage hard costs not included in incremental unit costs as identified in a prior community amenities proposal evaluation for 111 Independence Drive (19.7 percent). As shown in the table, the estimated incremental parking garage hard construction costs total \$9,128,860 or \$81,508 per residential unit.

Table 3: Estimated Incremental Residential Hard Construction Costs

Estimated Incremental Residential Hard Costs		
	Gross Floor Area Included in FAR (Sq. Ft.)	Building Hard Construction Costs
Total Building Costs (excl. Parking Garage)	117,781	\$66,344,591
Less: Est. Costs for Lobby/Amenities & Back of House Areas (a)	(7,334)	(\$4,131,152)
Estimated Residential Hard Costs	110,447	\$62,213,439
Less: Residential Costs not Included in Incremental Costs (b)		(\$4,479,368)
Total Est. Incremental Residential Hard Construction Costs		\$57,734,071
<i>per Residential Unit</i>		\$515,483
<i>per Gross Residential Sq. Ft.</i>		\$522.73
Estimated Incremental Parking Hard Costs		
Total Parking Garage Hard Costs		\$11,368,443
Less: Parking Garage Costs not Included in Incremental Costs (b)		(\$2,239,583)
Total Est. Incremental Parking Garage Hard Construction Costs		\$9,128,860
<i>per Residential Unit</i>		\$81,508
Assumptions		
Total Project Sq. Ft. Included in Floor Area Ratio		117,781
Lobby/Amenity		4,610
Back of House/Utilities/Maintenance/IT		2,724
Gross Residential (including common area/circulation)		110,447
Share of Residential Hard Costs not Included in Incremental Unit Costs (b)		7.20%
Share of Parking Hard Costs not Included in Incremental Unit Costs (b)		19.70%
Total Units in Project		112
Total Parking Spaces in Project		104
Parking Spaces per Unit		0.93

Notes:

(a) Costs for the lobby, tenant amenities, and back of house/utilities/maintenance/IT areas would be incurred regardless of whether the project included the three proposed BMR units and are therefore excluded from the incremental costs of

constructing the proposed community amenities. The construction budget provided by the project applicant does not divide hard costs between the residential areas, tenant amenity areas, back of house areas, or the parking garage. BAE relied on the applicant's estimate of the total costs for the building (excluding the parking garage) and estimated the costs of the lobby/residential amenity areas and back of house/utilities/maintenance/IT areas on a cost per square foot basis.

(b) Estimated hard costs that are not directly attributable to the construction of the three proposed BMR units, such as demolition, site work, foundation, and landscaping and irrigation. Estimate is based on the share of residential and parking hard costs excluded from incremental BMR unit costs identified in a prior community amenities proposal evaluation for a project at 111 Independence Drive.

Source: BAE, 2024.

BAE applied the incremental residential hard construction cost per square foot shown above in Table 3 (\$522.73) to the gross square footages (inclusive of circulation and common areas) of the proposed BMR units to generate a total incremental residential hard construction cost estimate for each proposed BMR unit. Incremental parking hard construction costs were allocated to each proposed BMR unit based on the incremental cost per residential unit cited above (\$81,508 per unit). Consistent with the applicant's soft cost assumption cited above, BAE's analysis also incorporates a 20 percent soft cost assumption. However, BAE's valuation applies the 20-percent soft cost assumption to the incremental hard construction cost estimate rather than the total hard construction cost estimate. The resulting total incremental BMR unit hard and soft costs are shown in Table 4 and would represent the valuation of the BMR rental units based on the incremental construction cost methodology established in prior community amenities proposal evaluations. As mentioned previously, prior community amenities proposal evaluations have all used a similar incremental construction cost approach to estimate the value of including low-income BMR rental units, consistent with the affordability levels for rental BMR units under the City's BMR housing ordinance, as community amenities in projects.

Table 4: BAE Valuation of Proposed BMR Units Provided as Community Amenity

	<u>1-Bedroom</u>	<u>2-Bedroom</u>	<u>2-Bedroom</u>	<u>Total</u>
Baseline Valuation - Incremental BMR Unit Hard + Soft Construction Costs				
Number of Proposed BMR Units	1	1	1	3
Proposed BMR Unit Size (Net Residential Sq. Ft.)	769	815	957	2,541
Total BMR Unit Gross Residential Square Footage	928	983	1,154	3,065
Total Incremental BMR Unit Residential Hard Construction Costs	\$485,094	\$513,845	\$603,232	\$1,602,171
Total Incremental BMR Unit Parking Hard Construction Costs	\$81,508	\$81,508	\$81,508	\$244,523
Soft Costs	<u>\$113,320</u>	<u>\$119,070</u>	<u>\$136,948</u>	<u>\$369,339</u>
Incremental BMR Unit Hard + Soft Construction Costs	\$679,922	\$714,423	\$821,687	\$2,216,032
	<u>1-Bedroom</u>	<u>2-Bedroom</u>	<u>2-Bedroom</u>	<u>Total</u>
Adjustment for Very Low-Income Affordability				
% AMI Required to Afford Market-Rate Unit Rent (a)	109.8%	129.0%	129.0%	
% AMI Required to Afford Low-Income BMR Unit Rent	80.0%	80.0%	80.0%	
Difference in AMI Level: Low-Inc. vs. Market Rate (b)	29.8%	49.0%	49.0%	
% AMI Required to Afford Very Low-Income BMR Unit Rent	50.0%	50.0%	50.0%	
Diff. in AMI Level: Very Low-Income vs. Market Rate (c)	59.8%	79.0%	79.0%	
Value Adjustment for Providing Very Low-Income BMR Units Instead of Low-Income-BMR Units (d)	2.005	1.612	1.612	
Value of Proposed Very Low-Income BMR Units	\$1,363,354	\$1,151,907	\$1,324,856	\$3,840,117
Assumptions				
Total Project Net Residential Sq. Ft.				91,564
Common Area/Circulation Sq. Ft.				<u>18,883</u>
Total Gross Residential Sq. Ft.				110,447
<i>Net Residential Sq. Ft. as a % of Gross Residential Sq. Ft.</i>				82.9%
Total Estimated Incremental Hard Construction Cost per Sq. Ft. (e)				\$522.73
Total Estimated Incremental Hard Construction Cost per Unit (e)				\$81,508
Soft Costs as a % of Incremental BMR Unit Hard Construction Costs				20%

Notes:

(a) See Appendix Table 5.

(b) Equal to the difference between the AMI level needed to afford a low-income BMR unit and the AMI level needed to afford a market-rate unit.

(c) Equal to the difference between the AMI level needed to afford a very low-income unit and the AMI level needed to afford a market-rate unit.

(d) Equal to the ratio between the difference in AMI level for a very low-income unit vs. a market-rate unit and the difference in AMI level for a low-income unit vs. a market-rate unit.

(e) See Table 3.

Sources: City of Menlo Park; BAE, 2024.

As mentioned previously, this analysis applies a value adjustment factor to the baseline incremental BMR unit hard and soft construction cost estimates to account for the lower affordability levels of the BMR units in the project applicant's community amenities proposal as compared with community amenities approved in connection with other comparable residential projects. The value adjustment factor is defined based on the relative affordability

of the proposed BMR units and is equal to the ratio between the difference in AMI level for a very low-income unit vs. a market-rate unit and the difference in AMI level for a low-income unit vs. a market-rate unit. As summarized in Table 4, the AMI levels required to afford market-rate unit rents equate to 109.8 percent of AMI for a one-bedroom unit and 129.0 percent of AMI for a two-bedroom unit. These affordability calculations are provided in Appendix Table 5. The required AMI levels for BMR units are 80 percent of AMI for low-income units and 50 percent of AMI for very low-income units.

Table 4 shows the difference in AMI levels for very low-income and low-income BMR one-bedroom and two-bedroom units and the resulting value adjustments for each proposed BMR unit. As shown, the resulting value adjustments equal 2.005 for a one-bedroom unit and 1.612 for a two-bedroom unit. These factors were applied to the incremental BMR unit hard and soft construction costs shown for each proposed BMR unit to estimate the total value of the proposed community amenity. As shown, this analysis results in a total estimated value of \$3,840,117 for the three BMR units.

APPENDIX A: SUPPORTING AFFORDABILITY CALCULATIONS

Table 5: AMI Levels Required to Afford Market-Rate Unit Rents

Affordability of Market Rate Rents	Unit (Household) Size		
	Studio (1 Person)	1-Bedroom (2 Person)	2-Bedroom (3 Person)
Monthly Market-Rate Rent (a)	\$3,300	\$3,900	\$5,150
Monthly Utility Costs (b)	\$178	\$200	\$266
Total Monthly Housing Costs	\$3,478	\$4,100	\$5,416
Annual Housing Costs	\$41,736	\$49,200	\$64,992
HH Income Required to Afford Housing Costs	\$139,120	\$164,000	\$216,640
2024 Median Household Income (c)	\$130,600	\$149,300	\$167,950
HH Income (% AMI) Required to Afford Market-Rate Housing Costs	106.5%	109.8%	129.0%

Notes:

(a) Based on asking rents in new multifamily properties in the Bayfront area.

(b) Housing Authority of San Mateo County 2024 allowances for tenant-furnished utilities and other services for a multifamily unit that uses electricity for cooking, heating, and water heating, as well as electricity for lights and appliances. Figure assumes the tenant is charged for water services.

(c) Based on 2024 household income limits by assumed household size.

Sources: City of Menlo Park; Housing Authority of San Mateo County; BAE, 2024.