TO: Members of the Plan Commission
FROM: Hickory R. Hurie
SUBJECT: Analysis of IZ Waiver Request for Kennedy Point (Krupp Development)
DATE: November 17, 2005

CDBG
Community Development Block Grant Program

SUMMARY:

Krupp Development proposes a 43-unit condominium development at the corner of First Street and Winnebago on Madison's east side, a .614-acre site that currently includes several residential buildings. Krupp seeks a change in the zoning from its current R-3 to a PUD. The company proposes to demolish the existing buildings and construct the multi-family building with enclosed parking for 44 stalls and 14 tandem stalls. (Based on discussions with the Urban Design Commission, the proposed development, now includes **42 condos**, in order to accommodate an entrance at the corner of First and Winnebago.)

Krupp Development sought a full waiver of the inclusionary zoning requirements due to the tight site constraints and projections of unit costs.

This analysis for an inclusionary zoning waiver is based upon data furnished by the Krupp Development Company and by the Planning Unit during September through November 2005, with the latest budget from October 4, 2005. The analysis focuses solely on the proposal for the residential units, including constraints recommended by the Urban Design Commission and Traffic Engineering.

METHOD OF ANALYSIS:

The Council adopted a waiver provision as part of the inclusionary dwelling unit ordinance that requires an analysis of project financial feasibility. The method consists of running three or more scenarios, using data provided by the developer. The first run is based upon a scenario whereby the project, using current zoning levels, is set at market rate sales. If this version is financially feasible according to the standards adopted by the Common Council, the project is then run with the full 15% inclusionary dwelling units included in the project. If this full IZ scenario does not meet the Council standards for financial feasibility, a scenario is selected with attributes (a combination of a partial percentage of IZ units, with units off-site, or payment in lieu of units on-site or reduction of expected number of units) that will provide a sufficient return for financial feasibility.

MARKET RATE SCENARIO:

The IZ ordinance suggests that the market rate scenario should be run within the density of the current zoning classification for the parcel. The current zoning for this site (R-3) permits up to 10 dwelling units on the site. In circumstances where there is no current zoning, the City will consider using the adopted Neighborhood Plan. In this case, the adopted Plan suggests a range of 25 to 30 dwelling units/acre, and would permit 18 units on the site. The Krupp proposal requests a density of 70 dwelling units/acre, or 42 units on the site.

Current zoning and Neighborhood Plan Level: Running the full-market rate scenario at the current zoning density of R-3 yields a project with a gross profit margin of a negative 15%. Even running the full-market rate scenario at the density permitted under the adopted neighborhood plan (which presumes a change in zoning from the current density) yields a project with a gross profit margin of negative 4.7%. Neither scenario meets the standards adopted by the Council for feasibility, and would normally not qualify for a waiver. (See note on second page.)

IZ SCENARIO WITH ADDITIONAL DENSITY:

In spite of the above conclusions, we ran a third scenario with the same cost assumptions but with the density requested by the developer, and the inclusion of the affordable units. According to the Planning unit, the requested density of 70 dwelling units per acre is 536% greater than the current zoning permits, and over twice the density permitted under the neighborhood plan.

This third scenario, with the additional market rate units and the seven inclusionary units (15% of 42 rounded up) does not meet the feasibility standards adopted by the Council. It does suggest, however, a gross profit margin several times the rate of the full market rate project within the

6

adopted plan densities, or about a positive 1.4% (A fourth scenario, with parking prices deleted from the sales prices of the IZ units, changes this gross profit margin to 2.5%.)

Consideration of extraordinary Costs:

Following the November 9 discussion of the Plan Commission, we ran a fifth scenario at the Neighborhood Plan Level density that excluded the extraordinary costs of the street reconstruction, since these appear to be imposed by the City on the project in spite of alternatives. Under this scenario, the full market rate project does achieve a positive gross profit margin of 3.3%, in addition to the permitted 7.6% development fee.

If the Plan Commission were to use this scenario's gross profit margin as the benchmark for profitability, the Plan Commission could consider the street reconstruction costs as extraordinary costs inherent in the project, and qualify the proposed project for some sort of waiver of the full 15% on-site provision of seven IZ units.

Using this assumption, and the additional density raised to the 42-unit level requested by the developer, a project with a partial waiver based on 4 IZ dwelling units and a payment of $77,923 for the other three would meet that new project-specific feasibility standard. This scenario would achieve a slightly higher level of feasibility (3.7%) than the full market-rate project at the Neighborhood Plan level (excluding the extraordinary street reconstruction costs) (3.3%).

Staff discussed other options of providing the inclusionary units with the developer and both concluded that the provision of new off-site units was not likely, given the lack of available sites in the area and the recent developments constructed by the developer himself.

CONCLUSION:

According to the ordinance provisions, the project does not meet the initial standards of financial feasibility for a market rate project at the density levels permitted either under the current zoning or the neighborhood plan. **Hence if the Plan Commission were to find that the street reconstruction costs were extraordinary costs, and use the Neighborhood Plan level of density for the feasibility benchmark, then the project would meet that standard of feasibility with a waiver based on the provision of 4 IZ units and a payment in lieu of the remaining three.**

Cc: Alder J. Olson, Jeanne Hoffman, Brad Murphy, Pete Olson, Barb Constans

For your information, the project run at market rate and at the density requested by the developer, but <u>without</u> any IZ units, does make a gross profit market of 7.8%, which is also outside the Council adopted standards.

Note: Part of the logic inherent in the discussions leading up to the adoption of the IZ ordinance suggested that the City should not be helping an <u>infeasible project</u> at market rate become feasible by waiving one of the primary City public goals (affordable units within larger projects).)

Krupp Development
Kennedy Point Condos: 42 units, 4 IZ
For Sale Parameters for Determining Financial Infeasibility of Inclusionary Zoning
For the periods from January 01, 2006 through December 31, 2016

Issue	Reference range	Manual Calculation	Actuals
Financing			
Interest rate	Prime plus 0.5	Within standards	7.0%
Project costs			
Land/Building acquisition - per square foot raw land	$5 per square foot - raw land $50 - $55 per square foot, downtown - vacant land $90 - $125 per square foot, downtown - improved with building	Lower than standard fo downtown propoerty with biuldings	$29.83 $29.83 $29.83
Hard cost contingency	5% new, 8% rehab of AIA contract	Within standards	4.7%
Soft cost contingency	5% new/rehab of soft costs	Within standards	2.5%
Contractor profit	6% of AIA contract (net of profit, overhead and general requirements)	Within standards	5.9%
Contractor overhead	2% of AIA contract (net of profit, overhead and general requirements)	Within standards	2.0%
Contractor general requirements	4% of AIA contract (net of profit, overhead and general requirements)	Within standards	4.0%
Parking	$1,000 per stall - surface $15,000 per stall - first level underground $20,000 per stall for second level underground $27,000 per stall for three levels or more of underground		$87,000.00
Development fees	8% of total project costs, net of development fees and reserves	Within standards	7.6%
Square foot cost of construction, includes buildings including profit overhead and general requirements, site improvements and personal property	4 stories and under - $62.50 per square foot, 5 to 8 stories - $95, and 8 stories or higher $110 - $120	Falls outside adopted standards, but appears within acceptable practice in the industry	$151.51
Soft cost	10% of cost of construction	Three times adopted standard	21.7%
Inflation index factor on sales			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Inflation index factor on costs			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Range of market rate initial selling prices			
	MLS or assessors website comps for market rate IZ as indicated in the ordinance (City of Madison annual calculation based on AMI)	na	See schedule
Sale/transaction costs			
	6.5% of selling price	Within standards	$712,997.87
Internal rate of return			
	15% - 30% (assuming 80% leverage, 20% equity) depending upon product type	na	28.6%
Ratio of sales to inventory (absorption)			
	Submit similar comps for similar projects		1.0
Gross profit assumption			
	12.5 - 17.5 sales minus direct project costs (not costs of sale or transaction costs)	Falls outside adopted standards	3.7%
Association fees			
	Amount of fees		225 to 375/month

ASSUMPTIONS:
Assumes density of 42 units requested by developer.
This is more than the density permitted by the current zoning, or the neighborhood plan.

This scenario is based on the figures submitted by the developer on October 5, so that it does include $400,000 for street reconstruction costs.
It also includes an offfset of $5,000/IZ unit for differences in finish, and tracks seperately the revenue for 4 parking stalls not included nor required in the base price for the IZ units.

With this scenario of 42 units, with 4 of them as IZ and a payment in lieu of 3 other IZ units of $77,923, this scenario produces a gross profit margin of 3.7%, which is slightly more than the 3.3% gross profit margin for a project at the neighborhood plan level density of 18 full market units.

CONCLUSION:
This project at market rates with density based on the developer requested density of 42 units does NOT meet the normal standard for an IZ waiver, but due to the extraordinary costs of street reconstruction, the Plan Commission may wish to consider approving the project at the density of 42 units, with 4 IZ units, and a waiver fee of $77,923.

According to the terms of the IZ ordinance, a project at market rate that does fall outside the normal standards does NOT qualify for a waiver of IZ units, on the grounds that a waiver should not make an infeasible market rate project feasible unless it addresses some of the public goals for the program. However, the Plan Commission, with advice of counsel, could choose to identify the street costs as extraordinary costs, and use the developer gross profit margin of 3.3% in the current zoning level as the benchmark standard. for profitability. (Note: This scenario also includes a development fee of 8% as permitted by the ordinance.)

Krupp Development
Kennedy Point Condos: 42 units, No IZ
For Sale Parameters for Determining Financial Infeasibility of Inclusionary Zoning
For the periods from January 01, 2006 through December 31, 2016

Issue	Required range	Manual Calculation	Actual
Financing			
Interest rate	Prime plus 0.5	Within standards	7.0%
Project costs			
Land/Building acquisition - per square foot raw land	$5 per square foot - raw land $50 - $55 per square foot, downtown - vacant land $90 - $125 per square foot, downtown - improved with building	Lower than standard fo downtown propoerty with biuldings	$29.59 $29.59 $29.59
Hard cost contingency	5% new, 8% rehab of AIA contract	Within standards	4.7%
Soft cost contingency	5% new/rehab of soft costs	Within standards	2.6%
Contractor profit	6% of AIA contract (net of profit, overhead and general requirements)	Within standards	5.9%
Contractor overhead	2% of AIA contract (net of profit, overhead and general requirements)	Within standards	2.0%
Contractor general requirements	4% of AIA contract (net of profit, overhead and general requirements)	Within standards	3.9%
Parking	$1,000 per stall - surface $15,000 per stall - first level underground $20,000 per stall for second level underground $27,000 per stall for three levels or more of underground		$87,000.00
Development fees	8% of total project costs, net of development fees and reserves	Within standards	7.7%
Square foot cost of construction, includes buildings including profit overhead and general requirements, site improvements and personal property	4 stories and under - $62.50 per square foot, 5 to 8 stories - $95, and 8 stories or higher $110 - $120	Falls outside adopted standards, but appears within acceptable practice in the industry	$150.66
Soft cost	10% of cost of construction	Three times adopted standard	20.6%
Inflation index factor on sales			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Inflation index factor on costs			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Range of market rate initial selling prices			
	MLS or assessors website comps for market rate IZ as indicated in the ordinance (City of Madison annual calculation based on AMI)	na	See schedule
Sale/transaction costs			
	6.5% of selling price	Within standards	$740,070.24
Internal rate of return			
	15% - 30% (assuming 80% leverage, 20% equity) depending upon product type	na	28.6%
Ratio of sales to inventory (absorption)			
	Submit similar comps for similar projects		1.0
Gross profit assumption			
	12.5 - 17.5 sales minus direct project costs (not costs of sale or transaction costs)	Falls outside adopted standards	7.8%
Association fees			
	Amount of fees		225 to 375/month

ASSUMPTIONS:
Assumes density of 42 units requested by developer.

This is more than the density permitted by the current zoning, or the neighborhood plan.
This scenario is based on the figures submitted by the developer on October 5.

CONCLUSION:
This project at market rates with density based on the Neighborhood Plan zoning does NOT meet the standard for for gross profit (7.8% compared to adopted standard of 12.5 to 18.5%.)

According to the terms of the IZ ordinance, a project at market rate that does fall outside these standards does NOT qualify for a waiver of IZ units, on the grounds that a waiver should not make an infeasible market rate project feasible unless it addresses some of the public goals for the program.

Krupp Development
Kennedy Point Condos: Neighb zoning with 18 units, No Street costs
For Sale Parameters for Determining Financial Infeasibility of Inclusionary Zoning
For the periods from January 01, 2006 through December 31, 2016

Issue	Required range	Manual Calculation	Actual
Financing			
Interest rate	Prime plus 0.5	Within standards	7.0%
Project costs			
Land/Building acquisition - per square foot raw land	$5 per square foot - raw land $50 - $55 per square foot, downtown - vacant land $90 - $125 per square foot, downtown - improved with building	Lower than standard fo downtown propoerty with biuldings	$48.05 $48.05 $48.05
Hard cost contingency	5% new, 8% rehab of AIA contract	Within standards	4.7%
Soft cost contingency	5% new/rehab of soft costs	Within standards	2.6%
Contractor profit	6% of AIA contract (net of profit, overhead and general requirements)	Within standards	5.9%
Contractor overhead	2% of AIA contract (net of profit, overhead and general requirements)	Within standards	2.0%
Contractor general requirements	4% of AIA contract (net of profit, overhead and general requirements)	Within standards	3.9%
Parking	$1,000 per stall - surface $15,000 per stall - first level underground $20,000 per stall for second level underground $27,000 per stall for three levels or more of underground		$37,285.70
Development fees	8% of total project costs, net of development fees and reserves	Within standards	7.0%
Square foot cost of construction, includes buildings including profit overhead and general requirements, site improvements and personal property	4 stories and under - $62.50 per square foot, 5 to 8 stories - $95, and 8 stories or higher $110 - $120	Falls outside adopted standards, but appears within acceptable practice in the industry	$144.25
Soft cost	10% of cost of construction	Three times adopted standard	20.6%
Inflation index factor on sales			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Inflation index factor on costs			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Range of market rate initial selling prices			
	MLS or assessors website comps for market rate IZ as indicated in the ordinance (City of Madison annual calculation based on AMI)	na	See schedule
Sale/transaction costs			
	6.5% of selling price	Within standards	$331,164.47
Internal rate of return			
	15% - 30% (assuming 80% leverage, 20% equity) depending upon product type	na	28.6%
Ratio of sales to inventory (absorption)			
	Submit similar comps for similar projects		1.0
Gross profit assumption			
	12.5 - 17.5 sales minus direct project costs (not costs of sale or transaction costs)	Falls outside adopted standards	3.3%
Association fees			
	Amount of fees		225 to 375/month

ASSUMPTIONS:
Assumes density permitted under adopted Neighborhood Plan zoning.
This is less than the 42 to 43 Dwelling units proposed by the developer.
This is more than the density permitted by the current zoning.
This scenario assumes pro-rated costs per unit of 42-unit development submitted October 4,
but holds the costs of acquisition and demolition at the same level as the 42-unit proposal.
This scenario does not include the cost of street reconstruction, since these are extraordinary costs imposed by the City, and may not be needed in this smaller project.

CONCLUSION:
This project at market rates with density based on the Neighborhood Plan zoning does not meet the standard for for gross profit (postive 3.3% compared to adopted standard of 12.5 to 18.5%.)

According to the terms of the IZ ordinance, a project at market rate that falls outside these standards does not qualify for a waiver of IZ units.

Krupp Development
Kennedy Point Condos: Current zoning with 10 units, without street costs
For Sale Parameters for Determining Financial Infeasibility of Inclusionary Zoning
For the periods from January 01, 2006 through December 31, 2016

Issue	Required range	Manual Calculation	Actual
Financing			
Interest rate	Prime plus 0.5	Within standards	7.0%
Project costs			
Land/Building acquisition - per square foot raw land	$5 per square foot - raw land $50 - $55 per square foot, downtown - vacant land $90 - $125 per square foot, downtown - improved with building	At high end of adopted standard	$78.00 $78.00 $78.00
Hard cost contingency	5% new, 8% rehab of AIA contract	Within standards	4.7%
Soft cost contingency	5% new/rehab of soft costs	Within standards	2.6%
Contractor profit	6% of AIA contract (net of profit, overhead and general requirements)	Within standards	5.9%
Contractor overhead	2% of AIA contract (net of profit, overhead and general requirements)	Within standards	2.0%
Contractor general requirements	4% of AIA contract (net of profit, overhead and general requirements)	Within standards	3.9%
Parking	$1,000 per stall - surface $15,000 per stall - first level underground $20,000 per stall for second level underground $27,000 per stall for three levels or more of underground		$20,714.30
Development fees	8% of total project costs, net of development fees and reserves	Within standards	5.9%
Square foot cost of construction, includes buildings including profit overhead and general requirements, site improvements and personal property	4 stories and under - $62.50 per square foot, 5 to 8 stories - $95, and 8 stories or higher $110 - $120	Falls outside adopted standards, but appears within acceptable practice in the industry	$130.09
Soft cost	10% of cost of construction	Twice adopted standard	20.6%
Inflation index factor on sales			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Inflation index factor on costs			
	5 year average economic change factor for DOR website or 5 year average HUD AMI increase for IZ units	na	0.0%
Range of market rate initial selling prices			
	MLS or assessors website comps for market rate IZ as indicated in the ordinance (City of Madison annual calculation based on AMI)	na	See schedule
Sale/transaction costs			
	6.5% of selling price	Within standards	$203,919.30
Internal rate of return			
	15% - 30% (assuming 80% leverage, 20% equity) depending upon product type	na	0.0%
Ratio of sales to inventory (absorption)			
	Submit similar comps for similar projects		1.0
Gross profit assumption			
	12.5 - 17.5 sales minus direct project costs (not costs of sale or transaction costs)	Falls outside adopted standards	-2.3%
Association fees			
	Amount of fees		225 to 375/month

ASSUMPTIONS:

Assumes density permitted under current R-3 zoning.
This is less than the 42 to 43 Dwelling units proposed by the developer.
This is less than the density permitted by the adopted neighborhood plan.
This scenario assumes pro-rated costs per unit of 42-unit development submitted October 4, but holds the costs of acquisiton and demolition at the same level as the 42-unit proposal.
This scenario also deducts the extraordinary costs of the street reconstruction, it would probably not be needed for a smaller project.

CONCLUSION:

This project at market rates with density based on the current zoning does not meet the standard for for gross profit (negative 2.3.% compared to adopted standard of postive 12.5 to 18.5%.)

According to the terms of the IZ ordinance, a project at market rate that falls outside these standards does not qualify for a waiver of IZ units.

I am the fifth property northeast of the proposed project(15years), a past SASYNA board member, past member of the committee that gave input for the Schenk Atwood Neighborhood Business District Master Plan, and current member of the "Project Management Team" for the Schenk Atwood area. In general I am in favor of the project and do have some concerns about the size and IZ issues. I do not feel this project should be held hostage to those issues. Those are ongoing issues about all projects in Madison.

The height and mass is similar to:

Across Winnebago Street is Tininity Lutheran Church and classrooms, next to that is the partially constructed Nelson Bros. Project, on Atwood Ave is United Way, Kennedy Place, Schenks Point, St. Bernards Church. My house on Winnebago St. is 36 feet to the peak of the roof and it was built in 1900. These new buildings should serve us for the next 100 years and declaring 2-3 stories as maximum, next to the business district, seems a little short sighted. The higher density should help with money for the bus system, signals at train crossings, and many other things that are under the budget ax. The most vocal opponent of Schenks Point praised it's design after it was built. Criticism of Kennedy Place is more about materials and change in surfaces than about height and mass. I like Kennedy Place and would not want all buildings to be of a "classic brick architecture."

The IZ and TIF topics are related, evolving, and of a rather complex and elusive nature. Currently my biggest influence is the precedence the Monroe Commons (council vote 19-1) set. Krupp should be highly praised for his minimal demands on the city and taxpayers.

Please give the project a green lite so that you have more time to figure out IZ and TIF.

Fritz Hastreiter
1933 Winnebago St. #2
279-9549