



CITY AND COUNTY OF SAN FRANCISCO  
OFFICE OF THE CONTROLLER

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July 25, 2016

The Honorable Board of Supervisors  
City and County of San Francisco  
Room 244, City Hall

Angela Calvillo  
Clerk of the Board of Supervisors  
Room 244, City Hall

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BOARD OF SUPERVISORS  
SAN FRANCISCO  
2016 JUL 25 PM 2:41  
BY AK

**Re: Office of Economic Analysis Impact Report for File Number 160698**

Dear Madam Clerk and Members of the Board:

The Office of Economic Analysis is pleased to present you with its economic impact report on file number 160698, "Requiring Replacement Space: Economic Impact Report." If you have any questions about this report, please contact me at (415) 554-5268.

Best Regards,

Ted Egan  
Chief Economist



# Requiring Replacement Space: Economic Impact Report

Office of Economic Analysis

Item #160698

July 25<sup>th</sup>, 2016

## Introduction

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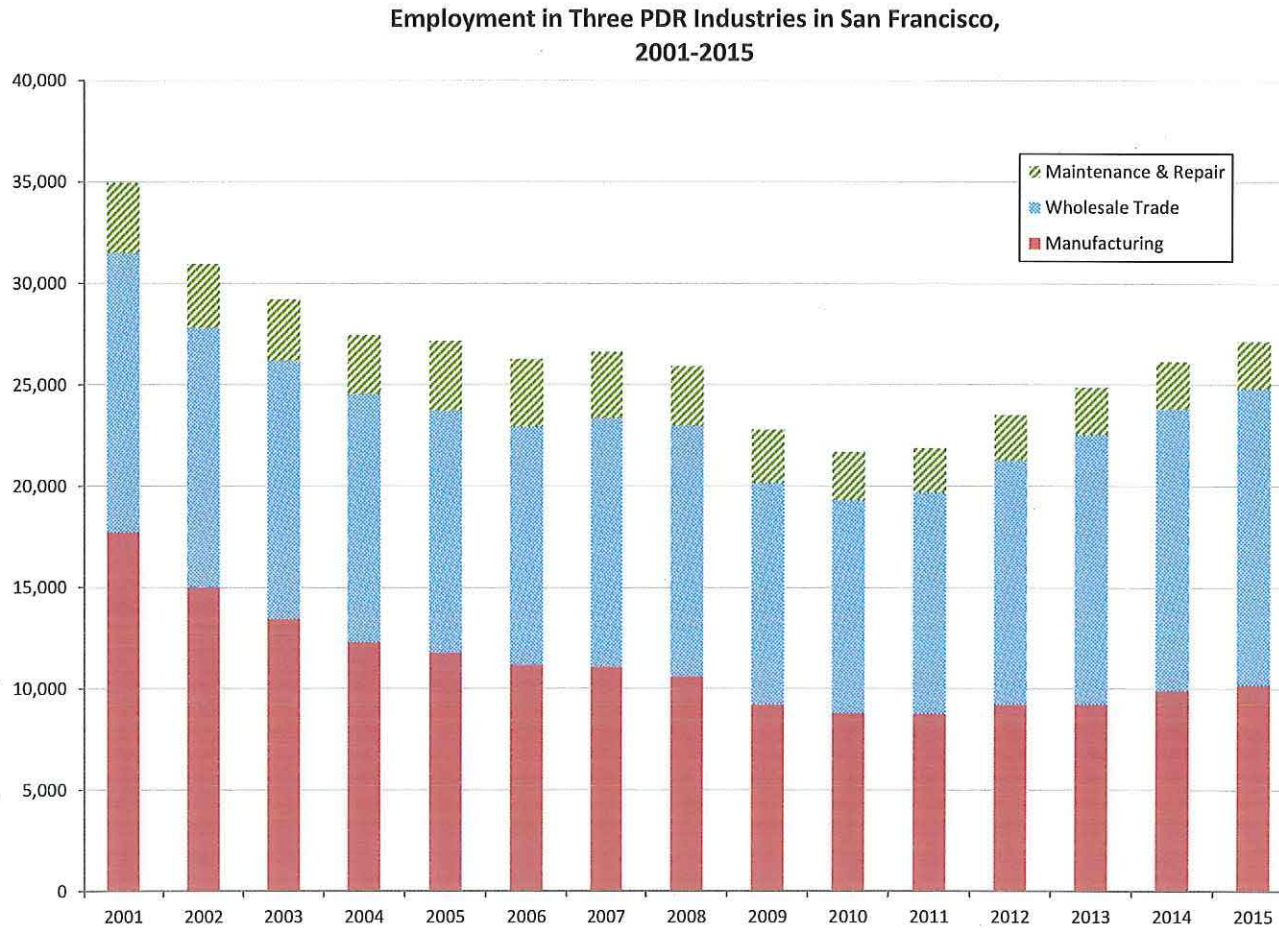
- The proposed legislation, which has been introduced as an initiative ordinance to be submitted to the voters for the November 2016 ballot, would create new restrictions on certain development projects within the Mission and South of Market neighborhoods of San Francisco.
- The legislation would require projects that seek to convert or demolish existing space used by production, distribution, repair (PDR), or institutional community uses, generally to build a greater amount of office space or housing, to obtain a conditional use authorization from the Planning Commission. These projects would also be required to provide a certain amount of new space to replace the PDR or community space that is converted or demolished.
- The provision of replacement space is likely to support employment in the PDR and community sectors of the city's economy, while reducing the City's property tax revenue and curtailing the development of new housing and office space.
- For these reasons, the Office of Economic Analysis has determined that the proposed legislation could have a material impact on the city's economy, and prepared this report.

## Applicability and Exemptions

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- The proposed replacement requirements apply to certain zoning districts within the Mission, East SoMa, Western SoMa plan areas. The requirements will also apply within the pending Central SoMa plan area, if and when that plan is adopted.
- Depending on the zoning where the project takes place, affected projects would have to replace 100%, 75%, or 50% of the space that was lost.
- Projects are exempt from the replacement requirements for the following reasons (among others):
  - they contain less than 5,000 square feet of PDR, 2,500 square feet of institutional community space, and have no arts activities.
  - they are controlled by the Port of San Francisco, the City's Recreation and Parks Department, or are located in a redevelopment area.
  - they have submitted an Environmental Evaluation Application to the Planning Department by June 14, 2016.

# Employment Trends in PDR Industries in San Francisco

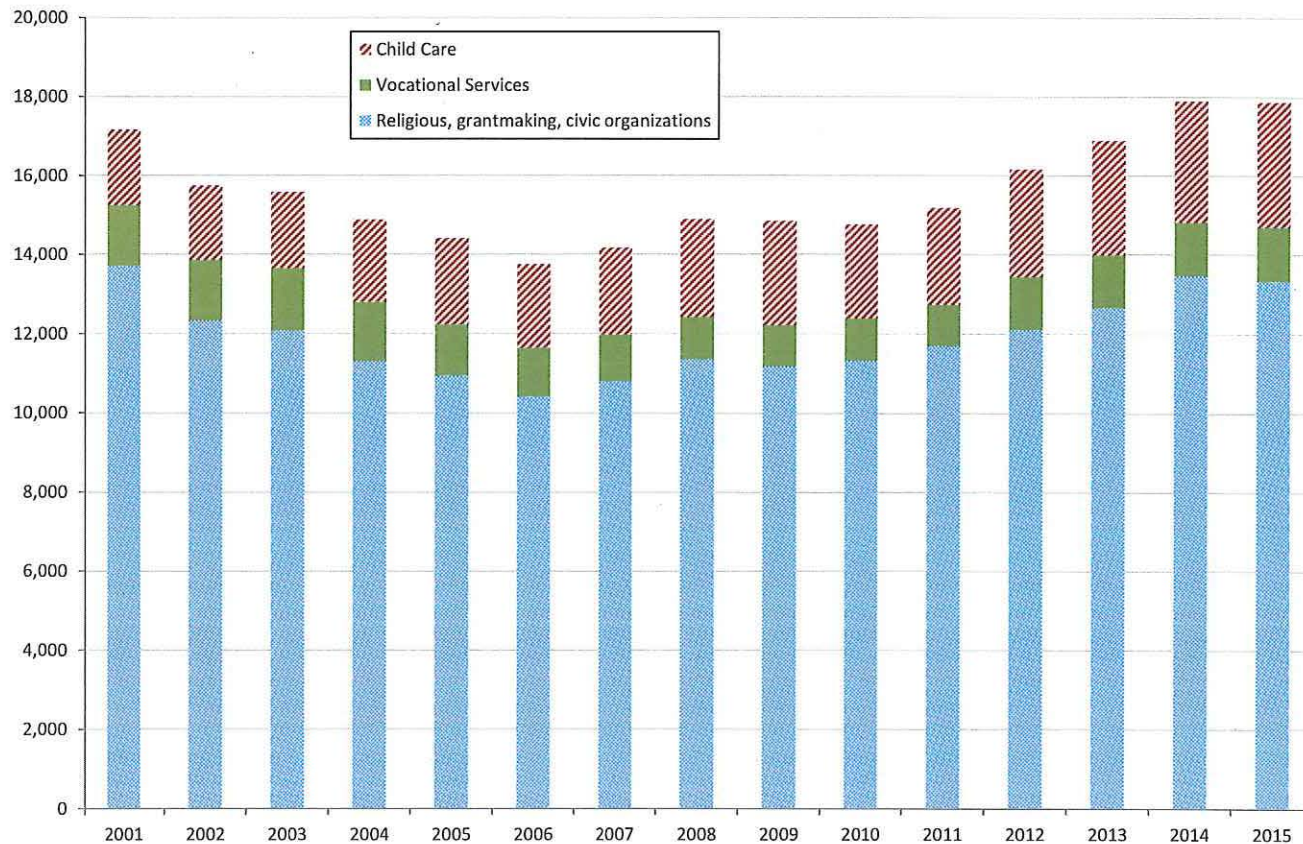


PDR includes industrial activities such as manufacturing, warehousing, wholesale trade, maintenance and repair services. It also includes arts activities, including motion picture, video, and sound production.

Employment trends in the three largest PDR industries are shown to the left. Long-term decline in manufacturing and wholesaling came to an end in 2010, and most segments of PDR have grown since then. Wholesale trade has grown 6.8%, faster than the overall city economy.

# Employment Trends in Community Industries in San Francisco

Employment in Three Community Industries in San Francisco, 2001-2015



Employment in Institutional Community sector in the city has been more cyclical than PDR employment, though the main industries in the sector lost far employment during the 2001-5 recession than in the Great Recession.

Since 2010, the sector has generally grown, but employment stayed flat between 2014 and 2015.

## Economic Impact Factors

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The proposed legislation would affect the economy in four primary ways:

1. First, mandating replacement of lost PDR and community space would increase the supply of that space in the city, putting downward pressure on the rents paid by these uses, and increasing their employment, relative to the status quo.
2. Second, because the legislation does not increase the total amount of space that can be built in the city, if more space has to be provided to replace PDR, arts, and community uses, less housing and office space can be built. Accordingly, the legislation would place upward pressure on housing prices and office rents.
3. Additionally, because the replacement space would a lower sales price than new residential or office space, the assessed value of the new property would be lower. This would reduce property tax revenues, and spending in the local economy by the City and other public agencies.
4. Finally, because the replacement requirement reduces the value of the completed project, it may make some projects financially infeasible. In such a case, the City would lose *all* of the project's property tax revenue, and the loss of residential and office space would be much greater than the amount of PDR/Arts space retained, unless prices rose to make the project feasible again.

## Economic Impact Assessment: PDR and Community Space

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- The Planning department estimates which land parcels in the city may be considered "soft sites" that are likely to experience redevelopment in the near future. This assessment is based on the size of the existing buildings on the site, and the size of potential buildings that could be built on the site, under the zoning rules in the Planning Code.
- PDR space on such soft sites is likely to be affected by this proposed legislation, since it otherwise would likely be converted or demolished to make way for larger residential and office buildings. However, PDR space on other sites which are not soft would not be affected by the legislation.
- The OEA analyzed the soft sites affected by the legislation, and determined that that approximately 315,000 square feet of PDR space on those sites could be preserved via replacement, representing slightly less than 1% of all the PDR space in San Francisco. Given the amount of space that a typical PDR job requires, preserving this much space is equivalent to protecting 350 to 400 PDR jobs.
- In addition, up to 90,000 square feet of community space could be replaced. At typical employment densities, this would maintain space for approximately 150 jobs in the social services sector.



## Economic Impact Assessment: Property Tax Revenue

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- As stated earlier, because the legislation does not permit new buildings to be built larger to accommodate the replacement space, creating new replacement space will necessarily lead to less housing and/or office space being built.
- The Property Tax revenue impact of this depends upon the relative prices of PDR and housing/office space, since property tax assessments are based on these sales prices. Recent broker reports suggest PDR space in San Francisco is currently selling for approximately \$420 per square foot\*, while new housing, for example, is selling at between \$1,000 and \$1,500 per square foot.
- Less is known about current sales prices for community space, but prices may also fall in the \$500 - \$750 per square foot range.
- These estimates are subject to considerably uncertainty, but if they are roughly correct, the City and other public agencies that receive Property Tax revenue could stand to lose between \$2.1 to \$4.3 million per year, once all of the soft sites in the affected areas are redeveloped.

## Economic Impact Assessment: Loss of of New Housing

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- The proposed legislation will also result in the loss of new housing and office space for two reasons:
  1. The replacement PDR space will consume allowable building space that otherwise would have gone to new housing and/or office space, as discussed on the previous page.
  2. The reduced value of the development may make the project financially infeasible, meaning all of the new supply is foregone.
- Given recent development trends, the OEA modeled the loss as if it would all be developed as housing, and none as office space. At a typical size of a new housing units, the replacement PDR and community space will lead the loss of between 400 to 500 new housing units.
- To estimate the impact of higher replacement requirements on feasibility and the probability of new housing and office being produced, the OEA used a development model originally created to model higher inclusionary housing requirements earlier in 2016. This model, which is subject to considerable uncertainty and is currently in the process of being improved, nevertheless suggests a very low annual loss in overall new development because of the replacement requirements.
- Together, these effects lead to an estimate of a 0.2% average annual increase of housing prices

## Economic Impact Assessment: Net Impact and REMI Simulation

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- Using our REMI model of the San Francisco economy, the OEA has modeled the net economic impact of the following effects we project will be caused by the legislation:
  - Net gain of 350-400 PDR jobs, and 150 jobs in social services.
  - Loss of between \$2.1 - \$4.3 million in property tax revenue annually.
  - 0.2% increase in Citywide housing prices.
- The simulation results in a net positive economic impact: a job gain of between 120 and 225 jobs, and a net expansion in the city's economy of between \$25 - \$50 million per year.
- The impact of job gains in the PDR and social service sectors was found to outweigh a slight loss of public sector jobs caused by reduced property tax revenue, and a slight citywide decline in jobs in every sector caused by higher housing prices.
- The positive net impact is particularly sensitive to estimates of housing price inflation, which is closely associated with the number of housing units that would not be built because the cost of the new requirement makes development infeasible. Since our modeling of this process is subject to considerable uncertainty, our confidence in these overall conclusions is limited.

## Staff Contacts

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Ted Egan, Ph.D., Chief Economist  
[ted.egan@sfgov.org](mailto:ted.egan@sfgov.org)