



A Public Agency

September 1, 2023

Mr. Gordon Tong
South Bayside Waste Management Authority (SBWMA) Technical Advisory Committee representative
County of San Mateo
455 County Center, 4th Floor
Redwood City, CA 94063

RE: Proposed Acquisition--1245 San Carlos Avenue, Suite E, San Carlos Property for SBWMA's Administrative Office necessary relocation on July 1, 2024.

Dear Gordon,

Thank you for your recent assistance in securing the Board of Supervisor's approval of Resolution 23-662 on August 1st, 2023 regarding the proposed purchase of the property noted above. We appreciate your efforts.

As you know from our recent conversation, we've discovered a mathematical error resulting in an inadvertent overstatement of the benefits of this acquisition. This calculation error is described below. We've taken immediate steps to responsibly bring this issue to light with the two SBWMA agencies that used the earlier calculation as a factor in their decision making on this issue. The County of San Mateo is one of these two agencies.

The good news is that, even with the adjusted calculation, the cost benefit to the ratepayers for purchasing this property is still substantial. This adjusted calc provides a net 25% compelling advantage in this analysis in favor of purchasing this property vs. leasing (vs. the 39% previously stated).

By way of background, all six SBWMA member agencies that have considered this item with the adjusted calcs have since unanimously voted to approve it. The remaining three SBWMA agency's governing bodies are scheduled to consider this issue by September 12th. Based on our review of this situation with our legal team, we recommend that you bring the modified staff report forward to include in the Board of Supervisor's next available meeting agenda to properly daylight this item—September 12th would be ideal. This item can be added to the consent calendar as simple information item. No further action by your Board is required. Our agency's General Counsel, Jean Savaree, is available for further clarification.

610 Elm Street, Suite 202 | P: 650-802-3500 | RethinkWaste.org
San Carlos, CA 94070 | F: 650-802-3501

MEMBER AGENCIES: City of Belmont • City of Burlingame • City of East Palo Alto • City of Foster City • Town of Hillsborough
City of Menlo Park • City of Redwood City • City of San Carlos • City of San Mateo • County of San Mateo • West Bay Sanitary District



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Timing:

Please note there is a strong time sensitivity to this process because our board will be considering the final components of this transaction at its September 28th meeting and all the approvals should be completed at this time.

Calculation explanation:

Through an additional peer review a calculation error was discovered in the Purchase vs. Lease Analysis related to the potential SBWMA purchase of property located at 1245 San Carlos Ave, Suite E, San Carlos, CA 94070. Due to this oversight the 30-year present value savings of purchasing vs. leasing is reduced from \$2,166,098 to \$1,416,098. See the updated Purchase vs. Lease Analysis in **Attachment A**.

Gordon, as I noted in our phone conversation, please accept my sincere apology to you and your colleagues for the hassle factor involved in this request. Our agency's team remains extremely proud to deliver an excellent standard of technical review and analysis for all of the work that we present and this is not representative of that standard. I commit that we will do better!

Thank you,

Joe La Mariana
Executive Director

CC:
Effie Verducci, Assistant Director, SMC Office of Sustainability
Paul Sheng, SMC County Counsel
Marci Dragun, SMC 4th Supervisorial District
John Mangini, SBWMA Sr. Finance Manager
Cyndi Urman, Clerk of the Board
Jean Savaree, SBWMA General Counsel

Attachment:

Purchase vs. Lease Analysis Report by HFH Consulting, adjusted

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Robert C. Hilton

MEMORANDUM

To: Joe La Mariana, Executive Director – South Bayside Waste Management Authority
From: Rick Simonson, Senior Vice President – HF&H Consultant
Date: August 15, 2023 (revises June 7, 2023 memo)
Subject: Cost Analysis of Office Purchase versus Lease

Background

The South Bayside Waste Management Authority's (SBWMA's) administrative office is currently located in the City of San Carlos Library. The office has been located in this space for over 16 years. Under the terms of the current lease, SBWMA occupies 2,429 square feet at a monthly rent of \$5,618 or \$2.31/sf. The current lease term ends on June 30, 2024 and the City has indicated that the term will not be extended because the space is needed to accommodate San Carlos staff and will no longer be available to the SBWMA.

Since receiving this notice, Executive Director La Mariana has been working with a commercial real estate broker to identify potential alternative spaces. The goal has been to identify an affordable space that will accommodate the current staff and agency/public guests, provide proper space for Board and TAC meetings, have easy access to parking for Board and Technical Advisory Committee (TAC) members, be located near public transit, and be in close/immediate proximity to the Shoreway Facility. With these factors in mind, the Executive Director La Mariana has researched and toured many local properties that are currently available for rent and one property that is currently for sale.

Executive Director La Mariana has toured a property, currently for sale, at 1245 San Carlos Avenue, Suite E, in San Carlos. In addition, working with a commercial real estate broker, Executive Director La Mariana has identified a number of properties available to lease that meet the some, but not all, of criteria above. The current lease rates have been estimated to be between \$4.50-\$6.50 per square foot in the general San Carlos area.

The following analysis compares the projected costs, over a 30-year period, of purchasing the available property versus leasing a property of the same size; the specific property is unknown at this time. An Excel model was developed to calculate the projected costs over time with a number of assumptions. The model has been constructed to allow multiple scenarios regarding costs and funding terms. This memorandum summarizes one such cost scenario. The model will be available to run additional scenarios at any upcoming meetings.

Cost Analysis of 1245 San Carlos Avenue Property

Executive Director La Mariana's discussions with the real estate broker has identified a commercial suite located at 1245 San Carlos Avenue, Suite E, which is 2,841 square feet with 20-foot ceilings which can

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accommodate adding a second floor and increase the usable space to 3,977 square feet. The expanded space will accommodate existing SBWMA staff workspaces, ADA-compliant restrooms, a kitchen, storage, and a large fully-wired video conference room available to host Board and TAC meetings.

The estimated cost to purchase and make the necessary interior improvements is \$2.3 million - \$2.5 million. For this analysis we have assumed the high of \$2.5 million.

Figure 1 summarizes the cost assumptions used to evaluate the cost-per-square foot procuring, improving, and maintaining the San Carlos Avenue property. **Figure 2** summarizes the first-year total cost of the property and the projected cost per square foot (\$4.11 per square foot), with additional detail describing the assumptions following **Figure 2**. **Attachment 1** includes a 30-year analysis of projected costs, including the calculation of the present value of the total annual costs of occupying the property over the next 30-years.

Figure 1 – Office Purchase Key Assumptions

Size (at purchase)	2,841	square feet
Estimated Size (at buildout)	3,977	square feet
Property Purchase Price	\$1,700,000	(est. \$1.5 - \$1.7 million)
Plus: Tenant Improvements	\$800,000	
Total Project Cost	\$2,500,000	
Downpayment	30%	
		(\$750,000)
Total Loan Amount	\$1,750,000	
Loan Term for Pymt Calc	30	years
Amortization	25	years
Balloon Payment	\$551,295	due @ Year 25
Interest Rate	6.19%	
Payments per Year	12	
Bank Fee	0.50%	of loan amount
Broker Fee	1.00%	of purchase price
Association Fees	\$0.14	per sq. ft. per month @ size at purchase
Association/Utilities Fee escalator	5.00%	per year
Reserves Return-on-Investments	2.00%	per year

Figure 2 – Year 1 Cost Summary

		FY 2023-24
Office Purchase Financial Analysis		
Loan Repayment		\$128,482
Bank Fee		\$8,750
Broker Fee		\$17,000
Balloon Payment Reserve		\$16,874
Association Fees		\$4,773
Utilities (excl. refuse)		\$6,000
Opportunity Cost ¹		\$14,485
	Total	\$196,364
	Build-out Square Footage	3,977.00
	\$ per sq. ft. per month	\$4.11

¹Lost investment income from use of reserves for downpayment and upfront bank/broker fees

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Loan Repayment, Fees, and Balloon Payment Reserve. One-time loan and broker fees are included in Year 1 only. The estimated annual loan repayment (at the terms included in Figure 1) is repaid over 25 years with a “balloon” payment due in Year 25. For this analysis, we have assumed the SBWMA would reserve 1/25 of the balloon payment each year so the cash is available when due. The calculated annual reserve contribution assumes earned interest on the funds at 2.0% per year. The loan payment terms include a fixed 6.19% interest rate for the first 10 years and adjusted thereafter based on 10-year Treasury plus 2.5%. Our analysis assumes the 6.19% throughout the 25-year term. Actual interest rates may be higher or lower.

Association Fees. Association fees are paid monthly by all property owners (i.e., City of San Carlos, Commercial Owners, and Residential Owners through a Joint Use Agreement). The fees cover common area maintenance, insurance, window washing, natural gas, water, sewer, and refuse. In addition, a portion of the fees are set aside in reserves for future capital repairs and maintenance (e.g., building exterior repair and paint, roofs). In total, the five commercial suites are allocated 4.84% of Joint Maintenance Costs. The \$0.14 per square foot is based on recent budgeted expenses and reserve contributions. The analysis assumes a 5% annual increase, which may vary from the actual annual changes. Unexpected capital needs may arise which shall be assessed to all property owners in excess of the current \$0.14 per square foot fee.

Utilities. The Association fees cover common area utilities, and the refuse needs for the commercial suites. The current understanding is the SBWMA will be responsible for their water, sewer, and electricity needs for their suite. These have been estimated at \$500 per month with a 5% annual escalator for this analysis.

Opportunity Costs. To purchase a property instead of leasing, requires upfront cash outlay for the downpayment and one-time bank/loan fees (\$775,750 in total). The SBWMA has reserves available to make these upfront payments. This analysis includes a “cost” component for the purchase option to recognize the loss of investment income that would otherwise be earned if the cash was continued to be held in reserves. For this analysis, we have assumed the cost of purchasing the property includes the annual loss of investment income at 2.0% per year on the \$775,750 withdrawal from reserves, based on recent historical return-on-investments experienced by the SBWMA.

Cost Analysis of Leasing a Property

Executive Director La Mariana, with assistance from a real estate broker researched and toured dozens of rental properties. Currently, for properties that fit the needs of the SBWMA in this targeted geographic area, leases range from \$4.50 to \$6.50 per square foot per month. Typically, the lease amounts are inclusive of the Common Area Maintenance (CAM) expenses (e.g., water, sewer, refuse, electricity), though the charges are reviewed annually and reconciled for any incremental differences that are passed along (or refunded) to the tenant. For comparison purposes, and to be conservative, we have assumed all CAM-related costs are included in the per square foot lease charge throughout the 30-year period.

Attachment 1 includes a 30-year analysis of projected costs, including the calculation of the present value of the total annual costs of leasing a property over the next 30-years. The analysis assumes the low end

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of \$4.50 per square foot per month, escalated 2.0% per year, which is equivalent to approximately \$0.10 per square foot each year.

Limitations

The analysis has been prepared with readily available projections and information provided by SBWMA staff, Beale Street Lending, Barc Architecture, and discussions with the 1245 San Carlos property builder, KB Homes. The projections contained herein may change. Additional costs not contemplated in this financial analysis to acquire the San Carlos property may be incurred.

Recommendation

Figure 3 summarizes the comparison of total estimated costs, and average cost per square foot per month, of the two options: 1) purchasing the San Carlos Avenue property and 2) continue leasing available commercial properties, based on the assumptions and projections described in this memo. Based on this financial analysis, the net present value (based on a present value discount rate of 3.0% annually) of the cost to purchase the San Carlos Avenue property is considerably less than leasing property at the low-end of current market rates with a conservation 2% annual increase to market rates. Assuming all costs of purchasing and maintaining the San Carlos Avenue property have been fairly represented, the purchase of the San Carlos Avenue property is recommended. Results may differ if the cost to purchase, finance the property, or other cost factors increase.

Figure 3 – Comparative Summary (detailed analysis provided in Attachment A)

	30-year Costs (in 2023\$)	Average Cost per Sq. Ft. per Month (in 2023\$)
Office Purchase	\$4,196,716	\$2.93
Office Lease	\$5,612,814	\$3.92

ATTACHMENT A

Key Assumptions - Office Purchase

Size (at purchase)	2,841 square feet
Estimated Size (at buildout)	3,977 square feet
Property Purchase Price	\$1,700,000 (est. \$1.5 - \$1.7 million)
Plus: Tenant Improvements	\$800,000
Total Project Cost	\$2,500,000
Downpayment	30% (\$750,000)
Total Loan Amount	\$1,750,000
Loan Term for Pymt Calc	30 years
Amortization	25 years
Balloon Payment	\$551,295 due @ Year 25
Interest Rate	6.19%
Payments per Year	12
Bank Fee	0.50% of loan amount
Broker Fee	1.00% of purchase price
Association Fees	\$0.14 per sq. ft. per month @ size at purchase
Association/Utilities Fee escalator	5.00% per year
Reserves Return-on-Investments	2.00% per year

Key Assumptions - Lease

Size (square feet)	3,977
Lease Amount	\$4.50 per sq. ft. per month (est. (\$4.50-\$6.50))
Annual Lease Amount	\$214,758
Common Area Maint (CAM)	incl. in lease
Lease Inflation Rate	2.00%

Key Assumptions - General

Present Value Discount Rate	3.0%
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water, sewer, electric, refuse, custodial, landscape, etc. (usually part of 1st yr lease amt (baseline), reconciled annually for incremental difference only)

WORKING AREA - Scenarios saved below

Office Purchase Financial Analysis	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28	FY 2028-29	FY 2029-30	FY 2030-31	FY 2031-32	FY 2032-33	FY 2033-34	FY 2034-35	FY 2035-36	FY 2036-37	FY 2037-38
Loan Repayment	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482
Bank Fee	\$8,750														
Broker Fee	\$17,000														
Balloon Payment Reserve	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874
Association Fees	\$4,773	\$5,012	\$5,262	\$5,525	\$5,801	\$6,092	\$6,396	\$6,716	\$7,052	\$7,404	\$7,775	\$8,163	\$8,571	\$9,000	\$9,450
Utilities (excl. refuse)	\$6,000	\$6,300	\$6,615	\$6,946	\$7,293	\$7,658	\$8,041	\$8,443	\$8,865	\$9,308	\$9,773	\$10,262	\$10,775	\$11,314	\$11,880
Opportunity Cost ¹	\$14,485	\$15,805	\$16,121	\$16,443	\$16,772	\$17,108	\$17,450	\$17,799	\$18,155	\$18,518	\$18,888	\$19,266	\$19,651	\$20,044	\$20,445
Down Payment	\$750,000														
Total	\$946,364	\$172,473	\$173,354	\$174,271	\$175,223	\$176,213	\$177,243	\$178,314	\$179,428	\$180,586	\$181,792	\$183,048	\$184,354	\$185,714	\$187,131
Build-out Square Footage	3,977.00														
\$ per sq. ft. per month	\$19.83	\$3.61	\$3.63	\$3.65	\$3.67	\$3.69	\$3.71	\$3.74	\$3.76	\$3.78	\$3.81	\$3.84	\$3.86	\$3.89	\$3.92
Present Value Discount Factor	1.0000	1.0300	1.0609	1.0927	1.1255	1.1593	1.1941	1.2299	1.2668	1.3048	1.3439	1.3842	1.4258	1.4685	1.5126
Present Value of Future Cost	\$946,364	\$167,449	\$163,403	\$159,482	\$155,683	\$152,003	\$148,438	\$144,985	\$141,642	\$138,404	\$135,271	\$132,237	\$129,302	\$126,463	\$123,716
30-year Costs (2023\$)	\$4,196,716														
Monthly NPV cost per square foot	\$2.93														

Office Purchase Financial Analysis	FY 2038-39	FY 2039-40	FY 2040-41	FY 2041-42	FY 2042-43	FY 2043-44	FY 2044-45	FY 2045-46	FY 2046-47	FY 2047-48	FY 2048-49	FY 2049-50	FY 2050-51	FY 2051-52	FY 2052-53	TOTAL
Loan Repayment	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482	\$128,482					\$3,212,056
Bank Fee	\$8,750															\$8,750
Broker Fee	\$17,000															\$17,000
Balloon Payment Reserve	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874	\$16,874					\$421,855
Association Fees	\$9,922	\$10,419	\$10,940	\$11,487	\$12,061	\$12,664	\$13,297	\$13,962	\$14,660	\$15,393	\$16,163	\$16,971	\$17,819	\$18,710	\$19,646	\$317,105
Utilities (excl. refuse)	\$12,474	\$13,097	\$13,752	\$14,440	\$15,162	\$15,920	\$16,716	\$17,552	\$18,429	\$19,351	\$20,318	\$21,334	\$22,401	\$23,521	\$24,697	\$398,633
Opportunity Cost ¹	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$20,854	\$579,758
Total	\$188,606	\$189,726	\$190,902	\$192,137	\$193,433	\$194,794	\$196,223	\$197,724	\$199,300	\$200,954	\$202,685	\$204,492	\$206,375	\$208,334	\$208,854	\$4,955,157
Build-out Square Footage																
\$ per sq. ft. per month	\$3.95	\$3.98	\$4.00	\$4.03	\$4.05	\$4.08	\$4.11	\$4.14	\$4.18	\$4.21	\$4.24	\$4.27	\$4.30	\$4.32	\$4.34	
Present Value Discount Factor	1.5580	1.6047	1.6528	1.7024	1.7535	1.8061	1.8603	1.9161	1.9736	2.0328	2.0938	2.1566	2.2213	2.2879	2.3566	
Present Value of Future Cost	\$121,059	\$118,231	\$115,499	\$112,860	\$110,312	\$107,853	\$105,480	\$103,191	\$100,983	\$98,856	\$96,805	\$94,827	\$92,920	\$91,084	\$89,317	

¹Lost investment income from use of reserves for downpayment and upfront bank/broker fees

Office Lease Financial Analysis	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28	FY 2028-29	FY 2029-30	FY 2030-31	FY 2031-32	FY 2032-33	FY 2033-34	FY 2034-35	FY 2035-36	FY 2036-37	FY 2037-38
Annual Lease	\$214,758	\$219,053	\$223,434	\$227,903	\$232,461	\$237,110	\$241,852	\$246,689	\$251,623	\$256,656	\$261,789	\$267,025	\$272,365	\$277,812	\$283,369
CAM Charges															
Other															
Total	\$214,758	\$219,053	\$223,434	\$227,903	\$232,461	\$237,110	\$241,852	\$246,689	\$251,623	\$256,656	\$261,789	\$267,025	\$272,365	\$277,812	\$283,369
\$ per sq. ft. per month	\$4.50	\$4.59	\$4.68	\$4.78	\$4.87	\$4.97	\$5.07	\$5.17	\$5.27	\$5.38	\$5.49	\$5.60	\$5.71	\$5.82	\$5.94
\$ change		\$0.09	\$0.09	\$0.09	\$0.10	\$0.10	\$0.10	\$0.10	\$0.10	\$0.11	\$0.11	\$0.11	\$0.11	\$0.11	\$0.12
Present Value Discount Factor	1.0000	1.0300	1.0609	1.0927	1.1255	1.1593	1.1941	1.2299	1.2668	1.3048	1.3439	1.3842	1.4258	1.4685	1.5126
Present Value of Future Cost	\$214,758	\$212,673	\$210,608	\$208,563	\$206,539	\$204,533	\$202,548	\$200,581	\$198,634	\$196,705	\$194,795	\$192,904	\$191,031	\$189,177	\$187,340
30-year Costs (2023\$)	\$5,612,814														
Monthly NPV cost per square foot	\$3.92														

Office Lease Financial Analysis	FY 2038-39	FY 2039-40	FY 2040-41	FY 2041-42	FY 2042-43	FY 2043-44	FY 2044-45	FY 2045-46	FY 2046-47	FY 2047-48	FY 2048-49	FY 2049-50	FY 2050-51	FY 2051-52	FY 2052-53	TOTAL
Annual Lease	\$289,036	\$294,817	\$300,713	\$306,727	\$312,862	\$319,119	\$325,501	\$332,012	\$338,652	\$345,425	\$352,333	\$359,380	\$366,568	\$373,899	\$381,377	\$8,712,320
CAM Charges																\$0
Other																\$0
Total	\$289,036	\$294,817	\$300,713	\$306,727	\$312,862	\$319,119	\$325,501	\$332,012	\$338,652	\$345,425	\$352,333	\$359,380	\$366,568	\$373,899	\$381,377	\$8,712,320
\$ per sq. ft. per month	\$6.06	\$6.18	\$6.30	\$6.43	\$6.56	\$6.69	\$6.82	\$6.96	\$7.10	\$7.24	\$7.38	\$7.53	\$7.68	\$7.83	\$7.99	
\$ change	\$0.12	\$0.12	\$0.12	\$0.13	\$0.13	\$0.13	\$0.13	\$0.14	\$0.14	\$0.14	\$0.14	\$0.15	\$0.15	\$0.15	\$0.16	
Present Value Discount Factor	1.5580	1.6047	1.6528	1.7024	1.7535	1.8061	1.8603	1.9161	1.9736	2.0328	2.0938	2.1566	2.2213	2.2879	2.3566	
Present Value of Future Cost	\$185,521	\$183,720	\$181,936	\$180,170	\$178,421	\$176,689	\$174,973	\$173,274	\$171,592	\$169,926	\$168,276	\$166,643	\$165,025	\$163,423	\$161,836	