



KEYSER MARSTON ASSOCIATES  
ADVISORS IN PUBLIC/PRIVATE REAL ESTATE DEVELOPMENT

**MEMORANDUM**

**To:** Eric Fonstein, Jennifer Ott, and Lori Taylor  
City of Alameda

**From:** Tim Kelly and Ernesto Vilchis

**Date:** September 13, 2012

**Subject:** Task 4: Adaptive Reuse Physical and Financial Analysis

This memorandum presents the analysis conducted by Field Paoli, Carson, Barbee & Gibson, Inc. (CBG) and Keyser Marston Associates, Inc. (KMA) for Task 4 of the Economic Development Strategy for Alameda Point.

Task 4 consisted of the following five (5) sub-tasks:

- 1) *Identifying five (5) existing buildings within Alameda Point that would be the most appropriate for consideration as prototypes for adaptive reuse.* The following five (5) buildings were selected by KMA and Field Paoli with extensive input from City staff:

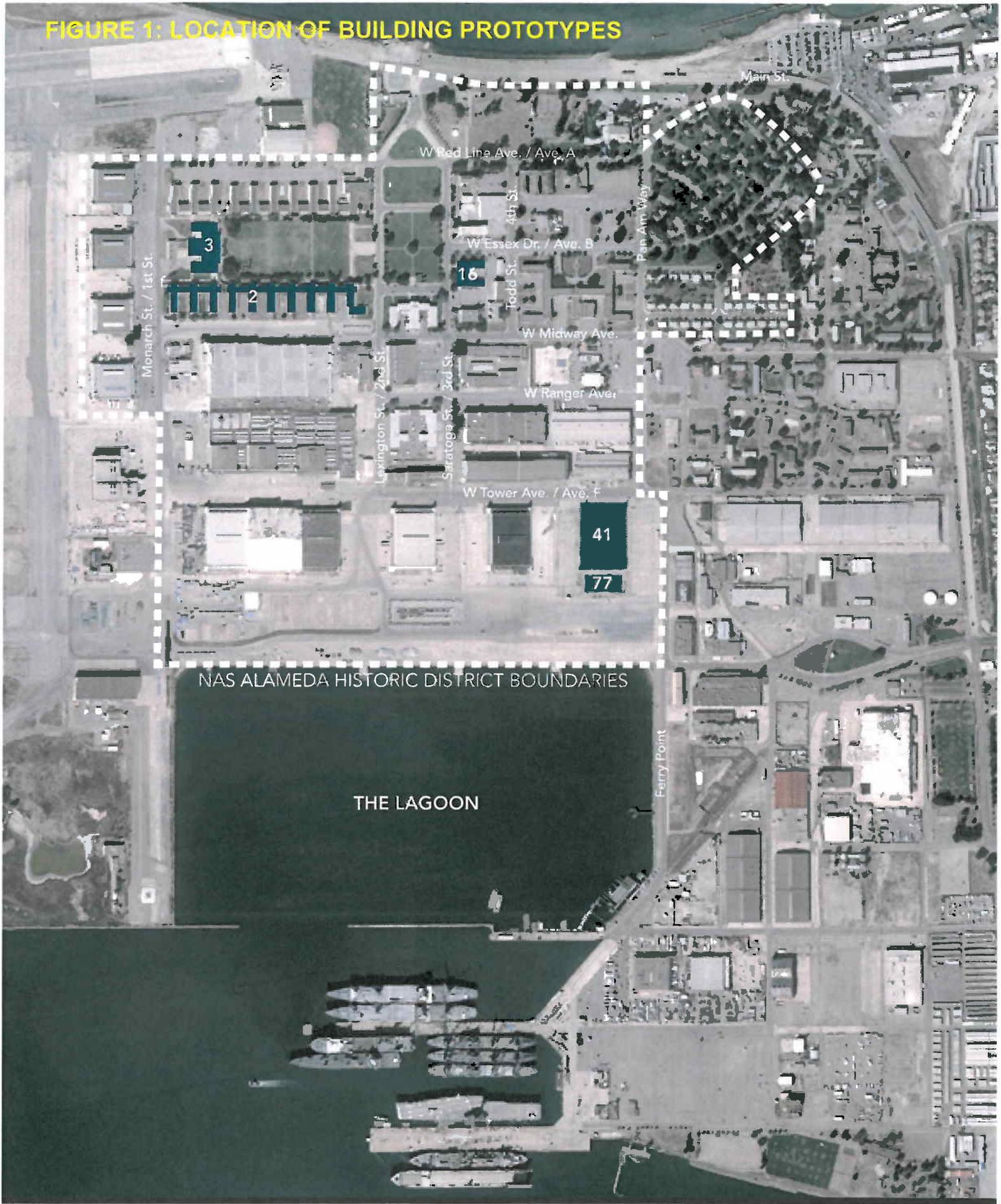
**Table 1 – Selected Prototypical Buildings**

Bldg. No.	Former Use	Building Area (Sq. Ft.)
2	Bachelor Enlisted Quarters	223,956
3	Mess Hall	51,965
16	Dispensing/Medical Clinic	38,322
41	Seaplane Hangar	115,656
77	Air Terminal	20,642

Source: KMA, Field Paoli. See Attachment 1 for building area.

As illustrated in Figure 1, all five (5) buildings are located within the NAS Alameda History District. Except for Building 77, which is currently home to the Alameda Naval Air Museum, all buildings selected are currently vacant.

**FIGURE 1: LOCATION OF BUILDING PROTOTYPES**



- 2) *Preparing information packages for each of the selected prototypes.* Field Paoli researched drawings, historical, structural, civil, code, cost and environmental reports to prepare two-page information documents for each building. Each information package includes a summary of building characteristics, floor plans and renderings of potential improvements to each building. These materials are presented in Attachment 1.
  
- 3) *Reviewing the existing condition and capacity of utility services to support the five (5) prototypical buildings sites.* CBG conducted an assessment to characterize the existing utility systems serving each of the existing prototypical buildings and to identify the required improvements to the existing utility services and surrounding surface improvements to support a new lessee. CBG’s analysis is presented in Attachment 2. The following table summarizes CBG’s findings:

**Table 2 – Summary of Engineer’s Preliminary Construction Cost Estimates for Basic Infrastructure Improvements**

	Bldg. 2	Bldg. 3	Bldg. 16	Bldg. 41	Bldg. 77
Basic Infrastructure Improvements - Hard Costs	\$166,500	\$336,500	\$22,500	\$101,500	\$45,000
40% Soft Costs (incl. contingency, Design, Etc.)	\$66,600	\$134,600	\$9,000	\$40,600	\$18,000
Total (rounded to the nearest \$1,000)	\$233,000	\$471,000	\$32,000	\$142,000	\$63,000

Source: CBG. See Attachment 2.

- 4) *Preparing a high-level financial feasibility analysis of each of the five (5) buildings.* KMA analyzed whether market rents can support an extensive renovation of the buildings so they can be competitive in the market and also to extend their useful life by 30 to 50 years. Tables 3 and 4 illustrate the level of investment (total development costs) that may be required to extensively renovate the five prototypical buildings. These estimates are based on cost estimates by Architectural Dimensions conducted in 2007 and 2010. Attachment 3 provides additional detail.

Per KMA’s analysis, office rents would have to range between \$2.00 and 2.20 per square foot per month (full service) to support extensive improvements to Buildings 2, 3, 16 and 77. Rents for industrial/warehousing space would have to be \$0.80 per square foot (triple net) to support extensive improvements to Building 41. These required rents are above market asking rates<sup>1</sup>, which currently average \$1.92 for office space in the City of Alameda, and approximately \$0.41 for industrial/warehouse space in the I-880 Corridor.

<sup>1</sup> Asking rents tend to be higher than actual rents.

Based on this analysis, KMA concludes that market rents would have to increase significantly before an extensive rehabilitation of the buildings is financially feasible.

**Table 3 – Analysis of Buildings 2, 3, 16, and 77**

<b>KMA Estimates</b>	
Total development costs of extensive renovations	\$198 - \$224 per square foot
Full service rents required to support extensive renovations; Assuming development costs are reduced with New Market Tax Credit Equity.	\$2.00 - \$2.20 per square foot
<b>Pricing Indicators</b>	
Harbor Bay average asking rents	\$1.58 per square foot
Marina Village average asking rents	\$1.92 per square foot
City of Alameda average asking rents	\$1.92 per square foot
Average asking price for office buildings in Oakland, Emeryville and Alameda	\$130 per square foot

Source: See Attachment 3 and Tables 6 and 7.

**Table 4 – Analysis of Building 41**

<b>KMA Estimates</b>	
Total development costs of extensive renovations	\$121 per square foot
Triple net rents required to support extensive renovations: Assuming development costs are reduced with New Market Tax Credit Equity.	\$0.80 per square foot
<b>Pricing Indicators</b>	
Average asking rents for large blocks (80,000 to 120,000sf) of industrial/warehouse space	\$0.41 per square foot
Average asking price for industrial/warehouse buildings in I-880 Corridor	\$67 per square foot

Source: See Attachment 3 and Tables 6 and 7.

KMA conducted an alternative financial analysis to determine the level of improvements that might be able to be financed under current market rents of \$1.80 per square foot of office space and \$0.40 per square foot of industrial/warehouse space.<sup>2</sup> These rents could hypothetically support

<sup>2</sup> As discussed above, current office *asking* rents in the City of Alameda are approximately \$1.92 per square foot. Current rental rates for office space in Alameda Point average \$1.68 per square foot. For modeling purposes we have selected the midpoint between average asking rates in the City and the average actual rent in Alameda Point. Meanwhile current *asking* rates for industrial space in the I-880 corridor average \$0.41 per square foot. Current rental rates for large industrial space at Alameda Point averages \$0.38 per square foot. Base on this, KMA assumes an average of \$0.40 per square foot for industrial/warehouse space.

approximately \$170 of improvements per square foot in Buildings 2, 3, 16, and 77 and approximately \$60 per square foot in Building 41. However, while in theory these numbers could finance substantial improvements in each of the buildings, market realities make the prospects challenging. In particular, the lack of demand for office/flex space and the availability of competitively priced office and industrial/warehouse space for lease and for-sale currently available in the market present significant challenges for Alameda Point. The buildings are additionally handicapped due to their size, particularly Buildings 2 and 3 which require significant investment amounts.

The existing Alameda market for both office space and industrial space creates a ceiling on rents and on the amount of new investment supported in buildings at Alameda Point. The effect is that the rent necessary to support major reinvestment in the selected prototypes at Alameda Point are above the current market. The investment required to substantially rehabilitate the buildings is higher than the cost to purchase existing buildings in the marketplace. Simply stated, unless the space at Alameda Point is unique and at an affordable rent, tenants have many choices in the market. Rents needed to support major investment at Alameda Point could occur after the overall market vacancy levels decline. The timing for such increases in rent and value is not known since demand for space, as measured by net new absorption, is weak and there is a large overhang of vacant space in established business parks, for example, there is approximately 385,000 square feet of vacant office space at Marina Village and Harbor Bay. An additional challenge at Alameda Point that hinders the investment environment for major renovation is the size of buildings, such as Buildings 2, 3 and 41. The conclusion of the financial analysis is that the current leasing practice of competitive rental rates and minimal improvements to the buildings will continue until market rents increase and the large supply of vacant space in the East Bay declines. The exception would be an end user that finds existing buildings and the Alameda location uniquely meet its space needs and are not available elsewhere in the marketplace.

- 5) *Identification of Potential Users.* The financial analysis presented in this memorandum assumes that Buildings 2, 3, 16, and 77 will be used primarily as office space and Building 41 will be used as industrial/warehousing space. In addition to these broad use categories, KMA also examined what types of industries the five prototype buildings may be suitable for, based on their size, location, access, and other such constraints. The following table presents a brief summary of the types of industries that the five prototypical buildings may be suitable for:

*Potential Flex Space Users – Category applies to all five prototypes*

- *Biotech and life-sciences*
- *Caterers/incubator kitchen/culinary school*
- *Clean tech – renewable resources*
- *Specialized manufacturing – artisans/artists/small urban manufacturing*
- *Specialty food production*

*Potential Office Space Users – Category applies to buildings 2, 3, 16, and 77*

- *Architecture/engineering firms*
- *Graphic design and other design firms*
- *Nonprofits*

*Potential Industrial/Warehouse Space Users – Category applies to building 41*

- *Entertainment and recreation*
- *Film/event producers and planners*
- *Logistics and distribution – point of sale distribution facility*
- *Marine-related services*

Each of these subtasks is described in more detail below. Supporting materials are presented in Attachments 1 - 4.

**1) Selection of five (5) prototypical buildings.**

KMA and Field Paoli worked with City staff to identify five (5) existing buildings at Alameda Point that are most appropriate to be considered as 'prototypes' for adaptive reuse. The goal was to identify buildings that best represent the range of opportunities within the existing building stock and buildings with the greatest potential interest to tenants, commercial and institutional developers.

The selection process began with an overview of all available information, including:

1. Maps available,
2. Studies completed to date,
3. City provided information, such as tenant roll, etc.,
4. Consultant team site and building tour, including photographs, and
5. Analyses conducted in previous task of the Economic Development Strategy including the market study, tenant forum, and approach to commercial and institutional groups.

Following the initial overview, KMA and Field Paoli selected a group of 12 buildings that based on their professional opinion, warranted consideration for examination as prototypical buildings. The criteria for a preliminary selection of buildings included:

1. Size and type of structures,
2. Possible uses that could be accommodated,
3. Current physical condition of the buildings, utilities & surroundings,
4. Potential costs to make the building usable,
5. Potential impact for the sub-region of Alameda Point,
6. Contribution to the overall future of Alameda Point,
7. Current occupancy and rent (if any), and
8. Environmental information.

Given the criteria for selection, the following twelve (12) buildings, or parts of buildings, were recommended to be on a preliminary list for further consideration and examination. The buildings are grouped into three categories by size, structure, and location:

*Large span structures*

Building 8 – Four-story concrete building; former Multi-purpose Administration Building

Building 12 – Two-story, concrete structure with metal frame; former Aircraft Maintenance Hangar

Building 41 – Two-story, concrete structure with metal frame; former Seaplane Hangar

Building 162 – Large, irregularly-shaped building of various heights; former Engine Accessory Overhaul Factory

*Poured concrete structures*

Building 2 – Two-story concrete structures with key-shape plan; former Bachelor Enlisted Quarters

Building 3 – Two-story, concrete building; former Mess Hall

Building 16 – Three-story, concrete building; former Dispensing/Medical Clinic

Building 17 – Two-story, concrete building; former Bachelor Officers Quarters

Building 77 – Four-story, concrete building; former Air Terminal

*Gateway and smaller buildings*

Building 18 at the northern entrance

Buildings 30/31 – Main Gatehouse and Sentry House – Northern entrance

Buildings 398 and 66 at the eastern entrance

KMA and Field Paoli worked with City staff to reduce the preliminary list to five (5) buildings. After numerous consultations, and further analyses based on the criteria described above, the following buildings selected as prototypes:

Building 2 – former Bachelor Enlisted Quarters

Building 3 – former Mess Hall

Building 16 – former Dispensing/Medical Clinic

Building 41 – former Seaplane Hangar

Building 77 – former Air Terminal

## **2) Preparation of Building Information Materials**

Field Paoli prepared graphic, photographic and statistical information about each of the five identified prototypical buildings at Alameda Point, Buildings 2, 3, 16, 41 and 77. Photographs were taken on three separate field investigations; drawing information and statistics were collected at various sites within Alameda Point. Based upon the information available to Field Paoli, plan drawings were produced using AutoCAD software and are found in Attachment 1. The photographs, plan drawings, statistics and a brief verbal description of each building were compiled into one two-sided and colored information sheet for each building (each sheet measures 8 ½" x 11"). The building information sheets are located in Attachment 1, are produced electronically, and are available in Adobe Acrobat Reader and Microsoft PowerPoint software formats.

The building information sheets explain the existing condition of the five buildings with the exception of the large photographic rendering on the front page of each sheet. The wall color in the photographic rendering for each building is shown to be rich tones of a cream tan, warmer and yellower in tone than the existing beige-white color. The trim elements of the five buildings are shown to be a greenish blue, which is darker and warmer than the light blue color on the existing buildings. In addition, the buildings are shown with landscape planting around them, in order to reduce the amount of pavement at the building sites, especially at Buildings 41 and 77. It is assumed, and depicted where applicable, that the building entrances, ramps, windows and roofs will be rehabilitated, replaced, or added as necessary.

## **3) Review the existing condition and capacity of utility services to support the five (5) prototypical buildings sites.**

CBG conducted an assessment to characterize the existing utility systems serving each of the existing prototypical buildings and to identify the required improvements to the existing utility services and surrounding surface improvements to support a new lessee. Table 5 summarizes CBG's findings regarding the costs associated with this level of utility improvements. Attachment 2 contains additional details on CBG's approach and findings.

For this analysis, the existing base-wide utility systems, which previously supported the Navy's demands, are assumed to have adequate capacity for the proposed demands associated with new lessees. The improvements to the existing utilities and surrounding surface improvements described in CBG's assessment are based upon the typical improvements that have been implemented for other existing building tenants within Alameda Point. The assessment assumes that improvements to the existing utility trunk

mains and distribution systems associated with future redevelopment of Alameda Point will be improved at a later date and are not required at the time of a new lease.

Table 5 only includes cost estimates for limited improvements for Building 77. CBG deems the utilities for that building to be in operable condition and no further improvements are necessary (except for minor landscaping improvements) for another lessee with similar utility needs.

**Table 5 - CBG's Preliminary Construction Cost Estimates for Basic Infrastructure Improvements**

Improvement Description	Bldg. 2	Bldg. 3	Bldg. 16	Bldg. 41	Bldg. 77
Sanitary Sewer Lateral Replacements	\$80,000	\$10,000	\$10,000	\$30,000	
Intall Submeter on Existing Potable Water Line <sup>1</sup>	\$2,500	\$2,500	\$2,500	\$2,500	
Install Backflow Preventer on Existing Potable Water	\$10,000	\$10,000	\$10,000	\$10,000	
Replace Electrical Transformer		\$20,000		\$20,000	
Demolish Existing Ancillary Structures		\$100,000			
Pavement		\$100,000			
Natural Gas Service Extension					
Parking Lot Striping and Signage				\$7,500	
ADA Parking Stall Striping and Signage	\$1,500	\$1,500		\$1,500	
ADA Path of Travel Improvements	\$5,000	\$5,000		\$5,000	
Landscaping and Surface Improvements at Entrance					
Landscaping and Irrigation		\$87,500			\$45,000
Landscaping - Turf Only	\$67,500			\$25,000	
<b>Subtotal</b>	<b>\$166,500</b>	<b>\$336,500</b>	<b>\$22,500</b>	<b>\$101,500</b>	<b>\$45,000</b>
<b>40% Soft Costs (incl. contingency, Design, Etc.)</b>	<b>\$66,600</b>	<b>\$134,600</b>	<b>\$9,000</b>	<b>\$40,600</b>	<b>\$18,000</b>
<b>Total (rounded to the nearest \$1,000)</b>	<b>\$233,000</b>	<b>\$471,000</b>	<b>\$32,000</b>	<b>\$142,000</b>	<b>\$63,000</b>

Source: CBG. See Attachment 2.

<sup>1</sup> Excludes all East Bay Municipal Utility District fees

**4) Prepare a high-level financial feasibility analysis of each of the five (5) buildings.**

Task 4 is a high level financial analysis and evaluates, on a broad assessment, the financial feasibility of 5 specific buildings. For Alameda Point to be successful, it will ultimately need to attract private investment. To attract private investment, the investment in the buildings will require a return to support the capital funding and the return needs to be commensurate with the investment risks. Fundamentally, value of the investment must exceed the cost of the investment to attract developers and their capital partners.

For all of Alameda Point, the City will want to develop an asset management strategy. Financial feasibility analyses of existing buildings and underdeveloped land are an important tool that will provide input to the asset management strategy for the overall base. Key issues can be addressed, such as, the necessary rent to support major reinvestment in the selected buildings and the relationship of the market rate rents to the necessary rent to support reinvestment and the appropriate form of property conveyance, such as, building lease, ground lease, or sale of parcel of land with an existing building. A realistic assessment of financial feasibility improves likelihood of successfully implementation related to individual buildings and underdeveloped land. The financial pro forma analysis also informs the planning process by evaluating the potential (amount and timing) for funding broader infrastructure costs for Alameda Point and other public benefits through the reinvestment and reuse of existing buildings and land.

In Task 4, the high level financial analysis focuses on vertical development costs related to the reinvestment in the selected buildings, including the site development costs as analyzed by CBG. The analysis assumes that entitlements are in place, there are limited costs related to remediation, and the broader infrastructure (sewer, water, dry utilities, telephone and internet access, roads, etc.) are adequate to serve individual buildings.

The financial test used to evaluate feasibility is referred to as the Return on Cost (ROC) analysis. The ROC is used by the development community to assess feasibility and measures the relationship between rents, income and total project development costs (before profit). It can be used to evaluate the sensitivity of changes among the various components.

Table 6 presents a summary of the feasibility analysis. Supporting tables are provided in Attachment 3. The following describes the assumptions of the analysis:

- 1) Rentable Building Area – The rentable building area is based on the total area for each building estimated by Architectural Dimensions. These estimates differ from the building area estimated by Field Paoli. However, since the costs estimates used in the analysis are based on Architectural Dimensions estimates, KMA relied on Architectural Dimension estimates for consistency purposes.
- 2) Use – It is assumed that Buildings 2, 3, 16, and 77 will be used primarily as office space with a single tenant leasing whole buildings or multiple tenants occupying large blocks (e.g., 10,000 square feet or more) of space in each building. Other uses could be envisioned for each of these buildings. For example, portions of buildings 3 or 77 could be used as restaurant space. Building 2, or a portion of it, could be used as a mix of flex and office space, as live/work space, or as space

for an academic institution. Building 16 could be used as a medical facility, or also as a mix of office and flex space. Different types of uses will require different types of upgrades and tenant improvements, and will also command rents higher or lower than the office market currently commands. Given the uncertainty of a particular use, these buildings are modeled as standard office space.

Building 41 is assumed to be used as industrial/warehousing space, similar to the other hangars currently leased at Alameda Point.

Sub-task 5 below examines the extent to which each of the prototypes offers some flexibility for accommodating specific types of uses (i.e., what types of industries the buildings may be suitable for.)

- 3) Vacancy – Vacancy rate for buildings 2, 3, 16, and 77 is assumed to be 15 percent based on the City of Alameda's historic (1997-2011) average vacancy rate of 14 percent for office space. However, it should be noted that currently Marina Village and Harbor Bay are experiencing vacancy rates of approximately 30 and 20 percent, respectively.

Building 41 is assumed to be leased to a single tenant; therefore vacancy is assumed to be zero (0) percent.

- 4) Operating expenses – KMA assumes annual operating expenses of \$6 per square foot for office space (Buildings 2, 3, 16, and 77) based on estimates by the Building Owners and Managers Association (BOMA) for the Oakland submarket.

The lease for Building 41 is assumed to be a triple net (NNN) lease where tenant or lessee agrees to pay all real estate taxes, building insurance, and maintenance. Therefore, operating expenses for Building 41 are assumed to be minimal.

- 5) Development costs – Development cost estimates are based on an assessment by Architectural Dimensions and Vanir Construction Management dating back to 2007 and 2010. Attachment 3 includes a detailed breakdown of the construction cost estimates. Those cost estimates reflect the level of investment needed to conduct a complete overhaul of the buildings to make the buildings competitive in the market and also to extend their useful life. The types of improvements assumed include, among other:

- Hazmat Cleanup
- Demolition
- Site Construction
- Utility Upgrades
- Conveying Systems
- Roof System
- Doors and Windows
- Interior Finishes
- Tenant Improvements
- Structural Solution – Seismic upgrades
- Electrical, Mechanical, and Plumbing
- Fire Sprinklers (Including Fire Alarm)

- 6) New Market Tax Credits (NMTC) – KMA assumes that the rehabilitation of the buildings would qualify for NMTC. The calculations of NMTC equity for each building are shown in Attachment 3. It should be noted, however, that the Census tract for Alameda Point currently does not qualify for NMTC. Furthermore, the future of the NMTC program is uncertain. In August 2012, the Senate Finance Committee recently recommended a two-year, \$3.5 billion per year extension. However, it is not clear if congress will adopt the bill and/or whether the NMTC credit program will exist beyond 2014.
- 7) Historic Preservation Tax Credits – KMA also considered including Historic Preservation Tax Credits as a funding source. Current tax incentives for preservation, established by the Tax Reform Act of 1986 include:
- a. 20% tax credit for the certified rehabilitation of *certified historic structures*<sup>3</sup>.
  - b. 10% tax credit for the rehabilitation of nonhistoric *buildings built before 1936*.

None of the prototypical buildings qualifies for either of the programs. Therefore, historic tax credits are not included in the analysis.

- 8) Return on Costs (ROC) – Returns required by developers depend upon a number of factors including the risk profile associated with developing the project, the costs of financing, capitalization rates (used to estimate value at completion, then compared to costs), and real estate market conditions in general. For this high level assessment, the pro forma ROC is projected to be 10%, that is, for each \$1 of net operating income (operating revenues less expenses before financing costs and depreciation), the private sector will invest \$10. The ROC is determined by dividing the net operating income by total project costs. The ROC on cost of 10% provides a 2% spread over the estimated capitalization rate

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<sup>3</sup> A *certified historic structure* is a building that is listed individually in the National Register of Historic Places or a building that is located in a *registered historic district* and certified by the National Park Service as contributing to the historic significance of that district.

**To:** Eric Fonstein, Jennifer Ott, and Lori Taylor

September 13, 2012

**Subject:** Task 4: Adaptive Reuse Physical and Financial Analysis

Page 14

(capitalization rates are used to determine value including profit) and we believe that this spread would be the minimum acceptable amount given the risks with potential increases in construction costs, interest rates, and capitalization rates. According to CoStar, warehouse building capitalization rates have been trending roughly in the range of 6 to 8 percent between 2008 and the end of 2011. During this period, office building capitalization rates have been trending in the 6 to 9 percent range. Properties at Alameda Point would be expected to be at the higher end of the range given the existing conditions of Alameda Point.

**Table 6**

**Stabilized Year Proformas - Rent levels needed to support 10% Return on Costs - Includes Tax Credit Equity  
Adaptive Reuse Physical and Financial Analysis  
Alameda Point Economic Development Strategy**

**Assumptions**

	<u>Bldg. 2</u>	<u>Bldg. 3</u>	<u>Bldg 16</u>	<u>Bldg. 41</u> <sup>1</sup>	<u>Bldg. 77</u> <sup>2</sup>
Rentable Building Area (SF) <sup>3</sup>	177,408	97,215	38,648	147,050	20,642
Use	Office	Office	Office	Industrial	Office
Stabilized Vacancy <sup>4</sup>	15%	15%	15%	0%	15%
Annual Operating Costs per Square Foot of Leased Space <sup>5</sup>	\$6.00	\$6.00	\$6.00	\$0.17	\$6.00

**Rent required to achieve 10% Return on Costs**

Monthly Rent per SF	\$2.10	\$2.00	\$2.20	\$0.80	\$2.05
Annual Rent per SF	\$25.20	\$24.00	\$26.40	\$9.60	\$24.60
Rent type	Full Service	Full Service	Full Service	NNN	Full Service

**Proforma (rounded to nearest \$10,000)****Stabilized Year Income**

Gross Annual Rents	\$4,470,000	\$2,330,000	\$1,020,000	\$1,410,000	\$510,000
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Vacancy	(\$670,500)	(\$349,500)	(\$153,000)	\$0	(\$76,500)
Operating Costs	(\$904,781)	(\$495,797)	(\$197,105)	(\$25,000)	(\$105,274)
<b>Net Operating Income</b>	<b>\$2,894,719</b>	<b>\$1,484,704</b>	<b>\$669,895</b>	<b>\$1,385,000</b>	<b>\$328,226</b>
<b>NOI - Rounded</b>	<b>\$2,890,000</b>	<b>\$1,480,000</b>	<b>\$670,000</b>	<b>\$1,390,000</b>	<b>\$330,000</b>

**Development Costs <sup>6</sup>**

Hard Costs	\$29,210,000	\$14,810,000	\$6,650,000	\$13,640,000	\$3,310,000
Soft Costs	\$8,760,000	\$4,440,000	\$2,000,000	\$4,090,000	\$993,000
<b>Total Development Costs</b>	<b>\$37,970,000</b>	<b>\$19,250,000</b>	<b>\$8,650,000</b>	<b>\$17,730,000</b>	<b>\$4,303,000</b>
<b>TDC per square foot</b>	<b>\$214</b>	<b>\$198</b>	<b>\$224</b>	<b>\$121</b>	<b>\$208</b>

&lt;Less&gt;

Net New Market Tax Credit Equity	(\$8,650,000)	(\$4,390,000)	(\$1,970,000)	(\$4,040,000)	(\$980,000)
<b>Adjusted Development Costs</b>	<b>\$29,320,000</b>	<b>\$14,860,000</b>	<b>\$6,680,000</b>	<b>\$13,690,000</b>	<b>\$3,323,000</b>
<b>Adjusted Development Costs PSF</b>	<b>\$165</b>	<b>\$153</b>	<b>\$173</b>	<b>\$93</b>	<b>\$161</b>

Return on (Adjusted) Costs	9.9%	10.0%	10.0%	10.2%	9.9%
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See Attachment 3 for sources.

<sup>1</sup> Development costs based on estimates for Building 39.<sup>2</sup> Development costs based on weighted average per square foot costs for Buildings 2, 3, and 16.<sup>3</sup> Square footage is based on Architectural Dimension estimates, except for Building 77 which is based on Field Paoli's estimates.<sup>4</sup> Based on historical vacancy in the City of Alameda<sup>5</sup> Operating expenses for Buildings 2, 3, 16, and 77 are based on estimates by the Building Owners and Managers Association (Average for Oakland Metro Area). Operating expenses for Building 41 are based on an allowance estimated by KMA.<sup>6</sup> See Tables A - 3.2 through A - 3.5.

Based on this analysis, KMA concludes that given the investment required to make the buildings competitive with other space currently available in the market, current market conditions do not support significant renovation of the buildings. This conclusion is reached even under relatively optimistic assumptions, such as average vacancy of 15 percent for office space and the assumption that New Market Tax Credits would be available to finance the rehabilitation.

Per our analysis, in order to support extensive capital improvements, rents would have to range between \$2.00 and 2.20 per square foot per month (full service) for office uses (i.e., Buildings 2, 3, 16 and 77) and approximately \$0.80 per square foot (triple net) for industrial/warehouse uses (i.e., Building 41).<sup>4</sup> These rents are above current market rates. As shown in Table 7, average *asking*<sup>5</sup> rates per square foot for office space in Alameda are approximately \$1.92 (full service). Meanwhile, rents for industrial/warehousing spaces larger than 80,000 square feet in the I-880 Corridor (from Berkeley to Hayward) were approximately \$0.41 per square foot on a triple net basis.

Additional factors that complicate the possibility of a developer or an end-user undertaking an extensive renovation of any of the five prototypical buildings include:

- 1) Large size of the buildings. The relatively large size of the buildings at Alameda Point represents a significant challenge. For example, as shown in Table 1, Buildings 2 and 3 are approximately 224,000 and 52,000 square feet, respectively. Figure 2 illustrates the limited demand for large commercial spaces in the East Bay, especially for office space. Less than 5 percent of office space tenants occupy spaces larger than 25,000 square feet.

Moreover, annual net absorption<sup>6</sup> of office space in the City of Alameda and the whole East Bay has been relatively anemic between 1997 and 2007. For example, average net absorption in the City of Alameda averaged approximately 38,000 square feet per year during this period (See Market Study). Assuming a similar rate of absorption, and assuming that Alameda Point were able to capture 100 percent of the historical net absorption, it would take approximately 9 years for the space in Buildings 2, 3, 16, and 77 to be absorbed.

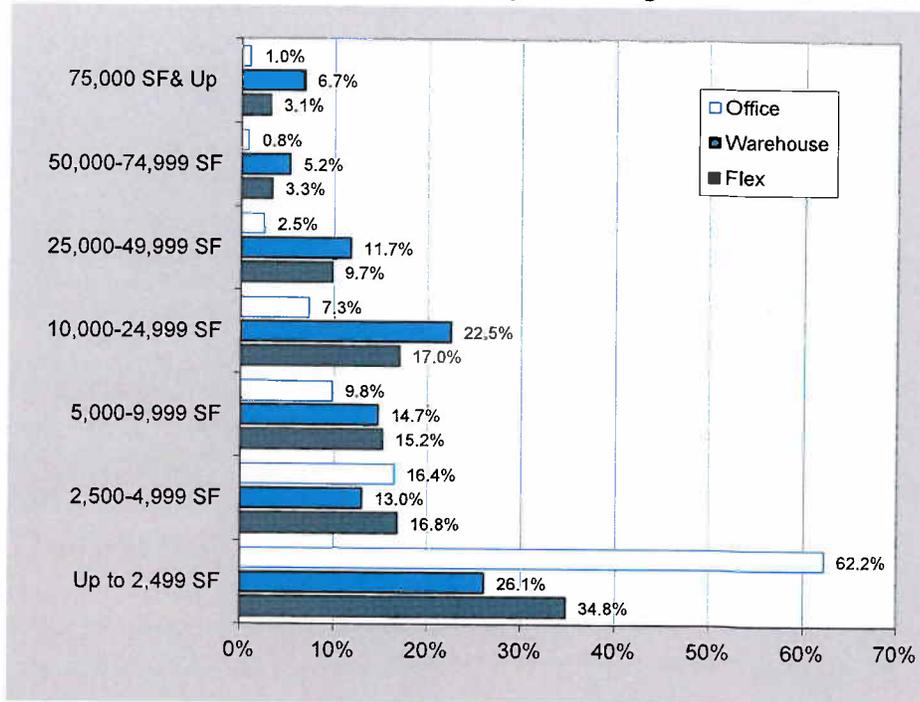
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<sup>4</sup> As shown in Attachment 3, if New Market Tax Credits are excluded from the analysis, the rents necessary to support extensive renovations would need to be \$2.45 to \$2.70 per square foot for Buildings 2, 3, 16, and 77 and \$1.00 for Building 41.

<sup>5</sup> Asking rates are typically higher than actual rents.

<sup>6</sup> Net absorption is a measure of change in total demand for real estate. It is equal to the amount occupied at the end of a period minus the amount occupied at the beginning of a period and takes into consideration space vacated during the period.

Figure 2 - East Bay Industrial Tenants by Size Range - Fourth Quarter 2011



Source: CoStar

- 2) Availability of large blocks of competitively priced office space available for lease. There are more than 600,000 square feet of vacant office space in the City of Alameda, including substantial space at Marina Village and Harbor Bay. Attachment 4 illustrates the wide range of spaces available to potential tenants in the Alameda submarket. A potential tenant could lease space for rental rates lower than what it would take to make the buildings at Alameda Point comparable in quality.
  
- 3) Availability of competitively priced office space available for sale. The total development costs for extensive renovations of Buildings 2, 3, 16, and 77 (which are assumed to be used as office space) range from \$198 to \$224 per square foot. From a purely financial perspective, it may make more sense for a potential user or investor to buy space that is more affordable and ready to be used, as opposed to undertaking a complex and costly renovation project. For example, according to Colliers International, the Waterfront in Harbor Bay, a 385,000 square foot office/flex complex with 85 percent occupancy was recently sold at over \$111 per square foot. That price is nearly half of what it may cost to extensively renovate existing buildings at Alameda Point. As shown in Table 7, average asking price for office space in Alameda, Emeryville, and Oakland is approximately \$130 per square foot.

The same is true for industrial/warehouse buildings. For example, total development costs for extensive renovations of Building 41 are estimated to be approximately \$121 per square foot. This is significantly higher than the average asking sales price for industrial/warehouse in the I-880 Corridor, which is approximately \$67 per square foot.

**Table 7 – Real Estate Market Statistics, August 2012**

<b>For Rent Statistics</b>	<b>Avg. Asking Rates per Sq. Ft.</b>	<b>Vacant Space Available (Sq. Ft.)</b>
Office Space		
Harbor Bay	\$1.58	232,646
Marina Village	\$1.92	152,505
City of Alameda	\$1.92	600,550
Industrial/Warehouse	\$0.41	4,505,951
<b>For Sale Statistics</b>		
Office Space	\$130	708,518
Industrial/Warehouse	\$67	371,426

Source: CoStar

Notes:

- Office rental statistics are for space available in the City of Alameda. Rents were reported on a full service basis.
- Office for-sale statistics are for space available for sale in Alameda, Emeryville, and Oakland.
- Harbor Bay includes Harbor Bay Business Park, Waterfront at Harbor Bay, Bay View Plaza, and Parkway Center.
- Industrial/warehouse statistics (for sale and for rent) are for large space (80,000 to 120,000 square feet) available in Emeryville, Oakland, Alameda, Hayward and San Leandro as of Q1 2012. Rents were reported on a triple net basis.

### *Alternative Scenario*

Given the challenges associated with an extensive renovation, which could not be supported with existing market rents, KMA analyzed what level of investments (in dollar terms) may be supported by existing market rents of \$1.80 for office and \$0.40 for industrial/warehouse space.<sup>7</sup>

As shown in Table 8, assuming the same factors for vacancy, operating expenses, NMTC, and return on costs, average current market rents could support approximately \$170 per square foot of total development costs in Buildings 2, 3, 16, and 77 and approximately \$60 per square foot in Building 41. These costs are significantly lower than the average cost of a comprehensive rehabilitation as assumed above. However, current market rents could still support substantial improvements to the prototypical buildings. For example, \$170 per square foot of improvements in building 16 could support approximately \$6.6 million dollars in improvements and \$60 per square foot could finance \$8.8 million of improvements in building 41.

However there are numerous reasons which make this alternative scenario improbable, including:

- 1) Demand for office space is relatively weak in Alameda Point, as illustrated by a vacancy rate of nearly 63 percent in Building 7 which is in a physical condition comparable to other Class C buildings in the area.<sup>8</sup> Also, wings 8, 9, and 10 of Building 2, which were renovated in 2001 and therefore may only need minimal investment to be occupied, have been vacant since 2007. Other business parks in Alameda face similarly high vacancy. Marina Village currently has vacancy of over 30 percent and Harbor Bay averages 20 percent. As a result, there are currently more than 600,000 square feet of available vacant office space in the City.

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<sup>7</sup> As discussed above, current office *asking* rents in the City of Alameda are approximately \$1.92 per square foot. Current rental rates for office space in Alameda Point average \$1.68 per square foot. For modeling purposes we have selected the midpoint between average asking rates in the City and the average actual rent in Alameda Point. Meanwhile current *asking* rates for industrial space in the I-880 corridor average \$0.41 per square foot. Current rental rates for large industrial space at Alameda Point averages \$0.38 per square foot. Base on this, KMA assumes an average of \$0.40 per square foot for industrial/warehouse space.

<sup>8</sup> Building 7 currently houses 5 biotech and high-tech companies in approximately 3,900 square feet of space. The building was rehabilitated in the late 1990s to accommodate a life sciences incubator. The incubator closed in 2005 but office and lab space continued to be leased to various life-sciences and high-tech companies.

**Table 8**

**Stabilized Year Proformas - Investment Supported by Current Market Rents - Alternative Scenario  
Adaptive Reuse Physical and Financial Analysis  
Alameda Point Economic Development Strategy**

**Assumptions**

	<u>Bldg. 2</u>	<u>Bldg. 3</u>	<u>Bldg. 16</u>	<u>Bldg. 41</u> <sup>1</sup>	<u>Bldg. 77</u> <sup>2</sup>
Rentable Building Area (SF) <sup>3</sup>	177,408	97,215	38,648	147,050	20,642
Use	Office	Office	Office	Industrial	Office
Stabilized Vacancy	15%	15%	15%	0%	15%
Annual Operating Costs per Square Foot of Leased Space <sup>4</sup>	\$6.00	\$6.00	\$6.00	\$0.17	\$6.00

**Current Market Rents<sup>5</sup>**

Monthly Rent per SF	\$1.80	\$1.80	\$1.80	\$0.40	\$1.80
Annual Rent per SF	\$21.60	\$21.60	\$21.60	\$4.80	\$21.60
Rent type	Full Service	Full Service	Full Service	NNN	Full Service

**Proforma (rounded to nearest \$10,000)**

**Stabilized Year Income**

Gross Annual Rents	\$3,830,000	\$2,100,000	\$830,000	\$710,000	\$450,000
<Less>					
Vacancy	(\$574,500)	(\$315,000)	(\$124,500)	\$0	(\$67,500)
Operating Costs	(\$904,781)	(\$495,797)	(\$197,105)	(\$25,000)	(\$105,274)
Net Operating Income (NOI)	\$2,350,719	\$1,289,204	\$508,395	\$685,000	\$277,226
NOI - Rounded	\$2,350,000	\$1,290,000	\$510,000	\$690,000	\$280,000

**Development Costs Supported by Current Market Rents**

Total Development Costs	\$30,160,000	\$16,530,000	\$6,570,000	\$8,820,000	\$3,510,000
TDC Per square foot	\$170	\$170	\$170	\$60	\$170
<Less>					
Net New Market Tax Credit Equity	(\$6,870,000)	(\$3,770,000)	(\$1,500,000)	(\$2,010,000)	(\$800,000)
Adjusted Development Costs	\$23,290,000	\$12,760,000	\$5,070,000	\$6,810,000	\$2,710,000
Adjusted Development Costs PSF	\$131	\$131	\$131	\$46	\$131

Return on (Adjusted) Costs	10.1%	10.1%	10.1%	10.1%	10.3%
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See Attachment 3 for sources.

<sup>1</sup> Development costs based on estimates for Building 39.

<sup>2</sup> Development costs based on weighted average per square foot costs for Buildings 2, 3, and 16.

<sup>3</sup>

Square footage is based on Architectural Dimension estimates, except for Building 77 which is based on Field Paoli's estimates.

<sup>4</sup> Operating expenses for Buildings 2, 3, 16, and 77 are based on estimates by the Building Owners and Managers Association (Average for Oakland Metro Area). Operating expenses for Building 41 are based on an allowance estimated by KMA.

<sup>5</sup> Current office asking rents in the City of Alameda are approximately \$1.92 per square foot. Current rental rates for office space in Alameda Point average \$1.68 per square foot. For modeling purposes KMA selected the midpoint between average asking rates in the City and the average actual rent in Alameda Point. Meanwhile current asking rates for industrial space in the I-880 corridor average \$0.41 per square foot. Current rental rates for large industrial space at Alameda Point averages \$0.38 per square foot. Base on this, KMA assumes an average of \$0.40 per square foot for industrial/warehouse space.

- 2) A larger user searching for a large block of space or an investor looking for an office building could purchase a building for a price lower than \$170 per square foot (the level of investment supported by market rents). For example, current asking prices for office buildings on the market average \$130 per square foot. A user searching for a large industrial/warehouse (80,000 to 120,000 sq. ft.) could also purchase a building for a price similar to the investment supported by market rents. Current average asking price for industrial/warehouse space is \$67 per square foot, excluding the vacant space at Alameda Point.
- 3) Given the large size of the buildings, the level of investment needed for improvements is quite significant making it very unlikely for a potential end-user or investor to undertake the projects.

**Table 9 – Total Development Costs by Building**

Bldg. No.	TDC
2	\$30,160,000
3	\$16,530,000
16	\$6,570,000
41	\$8,820,000
77	\$3,510,000

Source: See Table 8.

### 5) Identification of Potential Users

The five prototypical buildings selected were originally designed for very specific uses such as dormitory (Building 2), mess hall (Building 3), medical clinic (Building 16), airplane hangar (Building 41), and air terminal (Building 77). As noted above, adaptive reuse of these buildings will require significant investment to accommodate new users. Assuming that financial challenges are not a binding constraint, this section examines the extent to which each of the prototypes offer some flexibility for the accommodation of new uses (i.e., what types of industries the buildings may be suitable for), based on their size, shape, location, access and other such constraints.

The financial analysis presented in this memorandum assumes that Buildings 2, 3, 16, and 77 will be used primarily as office space and Building 41 will be used as industrial/warehousing space. However, the selected prototypes offer some flexibility for accommodating other uses. For example it is possible that these buildings could be configured as 'flex' space. Flex space is typically an office type use in a warehouse type of building, or it might be a warehouse type building with a mix of uses (storage, light

assembly, plus administrative offices). Flex space can also act as showroom space. Generally, flex space is a more affordable than office and more expensive than pure industrial/warehouse space.

Due to the flexibility of the buildings to be adapted to various uses, the list of potential users presented below is segmented into three categories:

- Flex: This use category applies to all five of the prototypes. As described below, except for specialty beverages or a culinary school, most of the businesses in these industries may require spaces smaller than 10,000 square feet. Therefore, a multi-tenant configuration conversion will be needed to accommodate these tenants in the existing buildings.
- Primarily Office Space: This use category applies to Buildings 2, 3, 16, and 77. Due to the size of these buildings and the limited space needs of these users, a multi-tenant conversion will be needed to accommodate these users.
- Primarily Industrial/Warehouse Space: This use category applies only to building 41. Businesses in this category may be able to lease whole buildings or very large portions of building 41. A potential opportunity would be a “point of sale” distribution center that generates annual sales tax revenue.

The existing buildings may be suitable for other uses not included in the list, such as an academic institution or a corporate campus for a high tech company or another type of corporation. However, it is difficult to predict what these industries may be and what the timeline may be. If unique opportunities such as these materialize, the City should actively pursue them. Tasks 6 will present potential strategies for how the City can increase the marketability of the site for when such opportunity arises.

**Table 10**  
**Potential Tenants for Adaptive Reuse Buildings**  
**Adaptive Reuse Physical and Financial Analysis**  
**Alameda Point Economic Development Strategy**

Industry	Additional Information	Relocation/ Expansion Potential <sup>1</sup>	Currently present in Alameda Point
<i>FLEX SPACE USERS</i>			
Biotech and life-sciences	Small biotech and life-science research companies, such as In-Touch Biosolutions and Volochem, which are currently located in Alameda Point in Building 7. These are likely to be small businesses leasing less than 2,000 sq. ft. of space. However, they may present an opportunity for growth.	Limited	Yes
Caterers/incubator kitchen/culinary school	<p>Building 3 and Building 77 present an opportunity to house food caterers similar to Pacific Fine Foods (currently leasing 3,000 sq. ft. in Building 42) or an incubator kitchen similar to the Artisan Kitchen in Richmond (2,000 sq. ft.) or La Cocina in San Francisco (4,400 sq. ft.)</p> <p>Some of the buildings may also be suitable for a culinary school, which may occupy anywhere between 40,000 and 89,000 sq. ft. of space for production and demonstration laboratories, dining room, classrooms, etc.</p>	Unknown	Yes
Clean tech - renewable resources	Companies engaged in the development of technology to extract energy from biofuels, wind, hydro, solar. Companies in these sub-sectors that are attracted to Alameda Point are likely to be start-ups looking for affordable, light industrial space that allows them to test product development, conduct production/assembly/construction, and some office space for operations. The suitability of existing buildings to businesses in this industry is illustrated by the presence of Makani Power and Natel Energy, which lease approximately 17,000 sq. ft. of flex space in Building 19 or Point Source Power which leases approximately 1,900 sq. ft. of office/lab space in Building 7.	Moderate	Yes
Specialized manufacturing - Artisan/Artists/small urban manufacturing	<p>Painting, sculpture, photography, print media, jewelers, carpentry and woodwork, furniture restoration, welding and metalwork, apparel manufacturing and design, etc. Demand for locally made products is on the rise resulting in an increase in the number of companies that manufacture products to serve primarily the regional market. These business typically need basic industrial buildings and need few tenant improvements to be able to operate. Alameda Point offers a central location that enables them to serve the Bay Area market.</p> <p>Buildings 14 and 29 demonstrate how large buildings can be segmented to accommodate multiple tenants in this industry.</p>	High	Yes
Specialty food production	<p>Bakeries, confectioneries, natural foods products, etc. Specialty food production has been on the rise in the East Bay. The City of Oakland, in particular, has been relatively successful at creating a specialty food production corridor along its waterfront. Existing buildings at Alameda Point could be adapted for this use and build on the success of Oakland. In fact, the City of Alameda is currently negotiating the lease of Building 119 (approx. 4,700 sq. ft.) to be used as commercial kitchen for food production and packaging for a small specialty food company.</p> <p>These tenants typically need small spaces, usually smaller than 5,000 sq. ft. According to professionals in this field, there is a big need for even smaller spaces of 1,000 to 3,000 sq. ft. A food incubator, as described above would be a good complement or even a catalyst for more of these businesses.</p>	High	Yes

**Table 10**  
**Potential Tenants for Adaptive Reuse Buildings**  
**Adaptive Reuse Physical and Financial Analysis**  
**Alameda Point Economic Development Strategy**

Industry	Additional Information	Relocation/Expansion Potential <sup>1</sup>	Currently present in Alameda Point
<b>PRIMARILY OFFICE SPACE USERS</b>			
Architecture/engineering	There may be an opportunity to attract design firms and nonprofits that find Alameda Point's unique setting and spaces within buildings attractive and that are seeking competitive rents.  It may be possible to intermix office users with flex and industrial space users. The American Industrial Center in San Francisco provides an example of how this can be done.	Unknown	No
Graphic design and other design firms		Unknown	No
Nonprofits		Unknown	Yes
<b>PRIMARILY INDUSTRIAL/WAREHOUSING SPACE USERS</b>			
Entertainment and Recreation	Mini-golf, ice hockey, indoor skate parks, indoor bike parks, swimming centers. The presence of Bladium (one of the largest entertainment and recreation venues in the East Bay) and Antiques/Auction by the Bay makes Alameda Point an attractive location for other entertainment and recreation businesses to locate there. In appendix C of Task 1, KMA noted that approximately 15 percent of the leasing inquiries received at Alameda Point are in this category. The City is also currently negotiating the lease of approximately 25,000 square feet of space for an indoor skate park at Alameda Point. This will further contribute to reinforce the image of Alameda Point as an entertainment and recreation destination.	Moderate to High	Yes
Film/event producers and planners	Businesses primarily engaged in the production of motion pictures, videos, television programs, or commercials, and/or promoting, organizing, and managing live performance art productions. Alameda Point is home to numerous businesses in these industries. These businesses tend to lease large industrial/warehousing buildings ranging from 4,000 to 40,000 square feet.	Moderate to High	Yes
Logistics and distribution - point of sale distribution facility	The I-880 Corridor is a preferred location for businesses in these industries and these businesses tend to lease some of the largest industrial/warehousing spaces in the East Bay including Alameda Point. The biggest challenge for Alameda Point is limited accessibility to I-880. Nevertheless, as demonstrated by the presence of Tran-Freight Express, which leases approximately 110,000 square feet of warehouse space, Alameda Point is a viable location for businesses in this industry.  A potential opportunity would be for a point-of-sale distribution center that generates annual sales tax revenue. Examples include Office Depot facility in Fremont and Southern Wines and Spirits in Union City.	Limited	Yes
Marine-related services	Ship building and repair, marine contractors and designers, sandblasting, subsea robotics and submersible systems. Marine-related companies currently account for the largest amount of leased buildings/land and generate the largest amount of rent revenues in Alameda Point. In general, it is difficult for companies in this industry to find suitable space (i.e., affordable large industrial spaces with deep water access) in the Bay Area. In the opinion of industry representatives, Alameda Point offers a "match made in heaven" for marine-related companies.	High	Yes

Source: Keyser Marston Associates, Inc.

<sup>1</sup> Relocation/expansion potential is based on findings of Task 3 of the Economic Development Strategy, in which KMA evaluated the prospects of twelve industries to locate and/or expand at Alameda Point. Industries were evaluated primarily based on the economic outlook for the industry, regional clustering patterns, and suitability of existing space at Alameda Point. For further details, please refer to "Approach to Commercial and Institutional Groups: Economic Development Strategy for Alameda Point", May 2012.