

**CITY AND COUNTY OF SAN FRANCISCO  
BOARD OF SUPERVISORS**

**BUDGET AND LEGISLATIVE ANALYST**

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**POLICY ANALYSIS REPORT**

To: Supervisor Mar  
From: Budget and Legislative Analyst  
Date: August 20, 2013  
Re: Preventing and Filling Commercial Vacancies in San Francisco



**Summary of Requested Action**

Your office requested that the Budget and Legislative Analyst draft a report on commercial vacancies in San Francisco including: (1) a determination of the current commercial property vacancy rate (by District and Citywide) including a historic perspective and an outlook for the next few years; (2) the factors that contribute to commercial vacancies and the role/impact of formula retail in creating vacancies; (3) the current City strategy for addressing commercial vacancies, a determination of which departments are responsible for implementing that strategy including the Office of Economic and Workforce Development (OEWD) and the Office of Small Business, and how well these agencies have performed or met goals; and, (4) how other municipalities prevent and address commercial vacancies. Pursuant to your request, the Budget and Legislative Analyst has contacted various City agencies; collected data on commercial vacancy rates in San Francisco; collected information on how other cities address commercial vacancies and the factors that contribute to such vacancies; and, assessed the potential role and impact of formula retail in creating vacancies through a review of the Budget and Legislative Analyst's previously conducted analysis on this topic.

**Executive Summary**

- While the City and County of San Francisco ("the City") does not track or prepare reports on commercial vacancies Citywide and does not issue reports on commercial vacancies by individual neighborhood commercial area, there are several City and private sector indices that provide partial information on commercial vacancy rates in certain neighborhoods and for certain segments of the commercial real estate market in San Francisco. While these indices cover only limited neighborhoods and sectors of the real estate market, such as office or retail space only, they all generally show a vacancy rate that peaked in 2010 and has been steadily decreasing through the present. However, based on data available, it is difficult to determine the geographic distribution of commercial vacancies in San Francisco.
- The Department of Building Inspection registry of vacant or abandoned buildings reflects only a limited subset of commercial vacancies as most vacancies registered are for buildings that are fully vacant. The registry shows that most of the 27 buildings classified for business occupants that registered as vacant or abandoned in 2012 were concentrated in the Tenderloin. The Department of Building Inspection registry of vacant or abandoned buildings likely understates all vacant commercial properties in the City because it relies primarily on owner self-reporting

rather than proactive efforts by City staff to identify all commercial vacancies and because it only counts fully vacant buildings rather than vacant commercial space in buildings that are otherwise occupied.

- OEWD reported a decline in the commercial vacancy rate in seven targeted commercial corridors from nine to seven percent between FY 2010-11 and 2011-12, but did not collect or report that information for other areas of the City.
- Vacancy rates for office and retail space downtown are tracked by the Controller's Office of Economic Analysis, a number of private companies and a realtors' association. All of these measures show decreases in vacancies over approximately the last year but none provides vacancy rates for all commercial real estate in the City or for neighborhoods other than downtown.
- Although it is not possible to determine the extent to which certain factors contribute to commercial vacancies in San Francisco, OEWD management reports that these factors include: (1) normal turnover; (2) buildings that are not leasable due to code violations or disability access issues; (3) the failure of building owners to effectively market their vacancy to potential tenants; (4) retail spaces that are held vacant because the owner is using it for a purpose that is not consistent with the planning or building code; (5) building owners that purposely keep their retail spaces vacant to avoid investment and/or speculate that rents will increase significantly in the near future; and, (6) absentee landlords who are less fervent about keeping their property occupied. In addition, the growth of large formula retail establishments has been shown to result in closure of nearby small non-formula establishments in other studies.
- Although the City does not have a comprehensive strategy for addressing commercial vacancies, there are various ordinances and programs administered by several City departments that aim to prevent or address commercial property vacancies and/or problems associated with vacant commercial properties such as graffiti and blight. These programs are concentrated in OEWD, but are also found in the Department of Building Inspection and, tangentially, in the Department of Public Works and the Office of Small Business. Most of the programs are either too new to have demonstrated their impact or the information and data on the programs' effectiveness in preventing and addressing commercial vacancies is limited and should be expanded.
- There are a number of alternative approaches to addressing commercial vacancies in effect in other municipalities, including a special property tax on vacant buildings in Washington, D.C.; the use of land banks in the State of Michigan and Dallas, Texas; vacant property registration, which is enforced more rigorously in the City of Chicago; and, receivership of nuisance properties in Baltimore, Maryland. Most of these approaches apply to fully vacant buildings or parcels that have resulted from a significant loss of population, which San Francisco did not experience to the same extent.

Nine policy options for consideration by the Board of Supervisors are presented at the end of this report.

## Background

Commercial property is property (an entire building or space within a building) that is intended to be used solely for business purposes and includes uses such as retail, office, hotels, medical centers, commercial garages, and offices, warehouses, and, by some definitions, multifamily residential and undeveloped land zoned for commercial purposes. In San Francisco, commercial property, often small retail spaces, are a critical piece of the economic and cultural health of the City's many neighborhood commercial corridors. While such properties become vacant from time to time due to normal business turnover, prolonged vacancies due to a depressed local economy, neglect, or other reason lead to negative effects such as blight. Such vacancies can also contribute to the loss of community serving small businesses and weaken the economy of neighborhood commercial corridors.

## Historic, Current, and Projected Vacancy Rates

While the City and County of San Francisco ("the City") does not maintain an index of all commercial vacancies Citywide, or for all neighborhood commercial areas, there are several City and private sector indices that provide partial commercial vacancy rates for the City, or for certain neighborhoods or certain segments of commercial real estate. These reported statistics include: (1) the Department of Building Inspection (DBI) registry of vacant or abandoned buildings; (2) the Office of Economic and Workforce Development's (OEWD) tracking of commercial vacancies in select commercial corridors, which is reported by the Controller's Office in the City Services Auditor's annual performance measure report; (3) the Controller's Office of Economic Analysis<sup>1</sup> Commercial Real Estate Economic Barometer; and, (4) other private-sector barometers of vacancy rates developed by firms and groups such as CBRE, Inc., and Colliers International. While each of these measures has strengths and weaknesses, none provide a comprehensive Citywide commercial vacancy rate or information on vacancies for individual San Francisco neighborhood commercial areas.

## DBI Vacant or Abandoned Buildings Registry

DBI maintains a list, or registry, of vacant or abandoned buildings in order to enforce Section 103A.4 of the San Francisco Building Code.<sup>2</sup> The Department maintains the list by: (1) owners self-reporting vacancies to DBI in compliance with the Vacant or Abandoned Building Registration Ordinance; (2) complaints from residents and other community members; and, (3) referrals from Police Department substations. For the most part, the DBI registry records buildings that are completely vacant or abandoned and therefore does not reflect vacant commercial spaces in buildings that are otherwise occupied, such as a multi-level mixed use building with occupied residential units and vacant ground floor commercial space. Further, the registry may undercount commercial vacancies due to the passive nature in which DBI maintains it. Conversely, the registry may also misreport the number of current vacancies as DBI staff report that the registry has not been updated regularly to remove addresses that are no longer vacant or abandoned.

According to the DBI registry, as updated in April 2013, there were 786 commercial and residential buildings listed as vacant or abandoned, which is 353, or 81.5 percent, more than the 433 vacant or

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<sup>1</sup> The Office of Economic Analysis is part of the Controller's Budget and Analysis Division and is staffed by two economists.

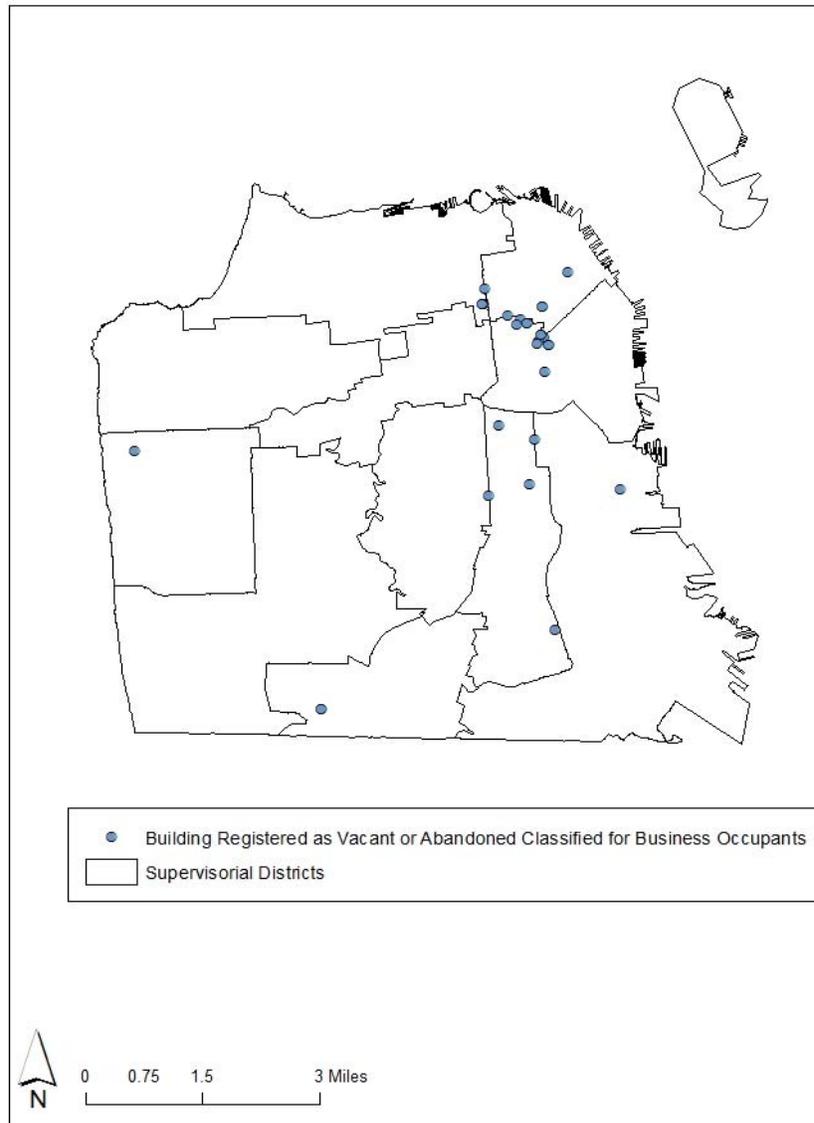
<sup>2</sup> This section of the Building Code, established by a 2009 ordinance, requires buildings that meet the definition of "vacant or abandoned" be registered as such with DBI within 30 days.

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abandoned buildings listed in May 2011 when the Budget and Legislative Analyst last reviewed the DBI registry. The increase in vacant or abandoned buildings registered with DBI may be due to: (1) additional time to implement registration requirements since the Vacant or Abandoned Building Ordinance was enacted in 2009, and (2) the lack of regular updating of the list by DBI staff (i.e. to remove buildings that are no longer considered vacant or abandoned). Of the 786 buildings listed as vacant or abandoned, 288, or approximately 37 percent, had owners that registered and paid the requisite fees in 2012 and 233, or only approximately 30 percent of the buildings listed on the registry, had owners that registered and paid the requisite fees in 2011. Of the 288 buildings on the registry in 2012, only 27, or 9.4 percent, were classified for business occupants with the remaining 261 buildings classified almost entirely as residential.

A map of the 27 buildings classified for business occupants whose owners paid the vacant and abandoned building registration fee in 2012 is shown in Exhibit 1 below, by Supervisorial District. As can be seen in Exhibit 1 the buildings listed as vacant or abandoned in 2012 that were classified for business occupants were highly concentrated in the Tenderloin areas of Supervisorial Districts 3 and 6 with a more dispersed set of buildings in the northern portion of Supervisorial District 9 (in the Mission). Note that this map does not capture partial vacancies and only reflects properties whose owners registered and paid the annual vacant and abandoned building fee in 2012 and whose properties were classified to allow for business occupants.

**Exhibit 1: Location of Buildings Classified for Business Use Registered as Vacant or Abandoned with the Department of Building Inspection in 2012**



**Office of Economic and Workforce Development Programs and Performance Measures**

OEWD annually collects data to calculate the retail vacancy rate in seven commercial corridors. This rate is reported by the Controller's Office in the City Services Auditor Annual Performance Measure Report. This vacancy rate, which was estimated to be 7 percent in FY 2011-12, measures retail vacancies only in the following commercial corridors: (1) Leland Avenue in Visitacion Valley; (2) San Bruno Avenue in Portola; (3) Third Street in the Bayview District; (4) Ocean Avenue in Oceanview/Merced/Ingleside; (5) Mission Street in the Excelsior; (6) Lower Polk Street; and, (7) Divisadero Street in the Western Addition.

OEWD reports it has recently expanded their vacancy rate tracking from seven commercial corridors by adding 19 additional commercial corridors and deleting Divisadero Street in the Western Addition from the calculation, which will result in a total of 25 tracked commercial corridors for the forthcoming FY 2012-13 City Services Auditor Annual Performance Measure Report. These additional neighborhoods and corridors include the following: (1) Geary Boulevard in the Richmond District; (2) Lombard Street in Cow Hollow; (3) Union Street in Cow Hollow; (4) Chinatown; (5) North Beach; (6) Middle Polk Street; (7) Noriega Street in the Sunset District; (8) Outer Irving Street in the Sunset District; (9) Taraval Street in the Sunset District; (10) Japantown; (11) Lower Fillmore Street in the Western Addition; (12) Larkin Street in the Tenderloin; (13) Central Market Street; (14) West Portal; (15) 24<sup>th</sup> Street in Noe Valley; (16) Upper Market and Castro Street in the Castro District; (17) Lower 24<sup>th</sup> Street in the Mission District; (18) Broad Street in Oceanview/Merced/Ingleside; and, (19) Mission Street between Cesar Chavez and Bosworth.

OEWD has used a variety of methods, including the use of nonprofit organizations and local college students to collect an inventory of retail parcels. According to Mr. Jordan Klein, Senior Project Manager of the Invest in Neighborhoods program with OEWD, the vacancy rate is now calculated using data collected by departmental staff.

Exhibit 2 below shows the estimated rate of commercial vacancies in the seven targeted commercial corridors for Fiscal Years 2007-08 through 2011-12, as reported by the Controller's Office in the City Services Auditor Annual Performance Measure Report. As mentioned above, the Budget and Legislative Analyst notes that the accuracy of the data presented and comparisons between years cannot be verified since OEWD has used different methods of varying reliability for calculating the commercial vacancy rate during the years shown.

<b>Exhibit 2: Average Retail Vacancy Rate in Seven Commercial Corridors in San Francisco <sup>1</sup></b>	
<b>Fiscal Year</b>	<b>Vacancy Rate</b>
2007-08	5%
2008-09	7%
2009-10	8%
2010-11	9%
2011-12	7%

Source: City Services Auditor Annual Year-End Performance Measure Report FY 2011-12

<sup>1</sup> Note: The seven commercial corridors are (1) Leland Avenue in Visitacion Valley; (2) San Bruno Avenue in Portola; (3) 3<sup>rd</sup> Street in the Bayview District; (4) Ocean Avenue in Oceanview/Merced/Ingleside; (5) Mission Street in the Excelsior; (6) Lower Polk Street; and, (7) Divisadero Street in the Western Addition

*Office of Economic Analysis Barometer*

The Office of Economic Analysis, a unit of the Controller's Budget and Analysis Division, maintains and publishes a Commercial Real Estate Economic Barometer that tracks the net absorption<sup>3</sup> rate and vacancy rate but only for office real estate in downtown San Francisco. This barometer is based on quarterly reports produced by Jones Lang LaSalle, a financial and professional services firm specializing in real estate, which focuses on office buildings in downtown commercial districts. Unlike the DBI registry of vacant and abandoned buildings, described above, the Office of Economic Analysis report captures vacant space in office buildings downtown that are partially occupied in addition to buildings that are entirely vacant.

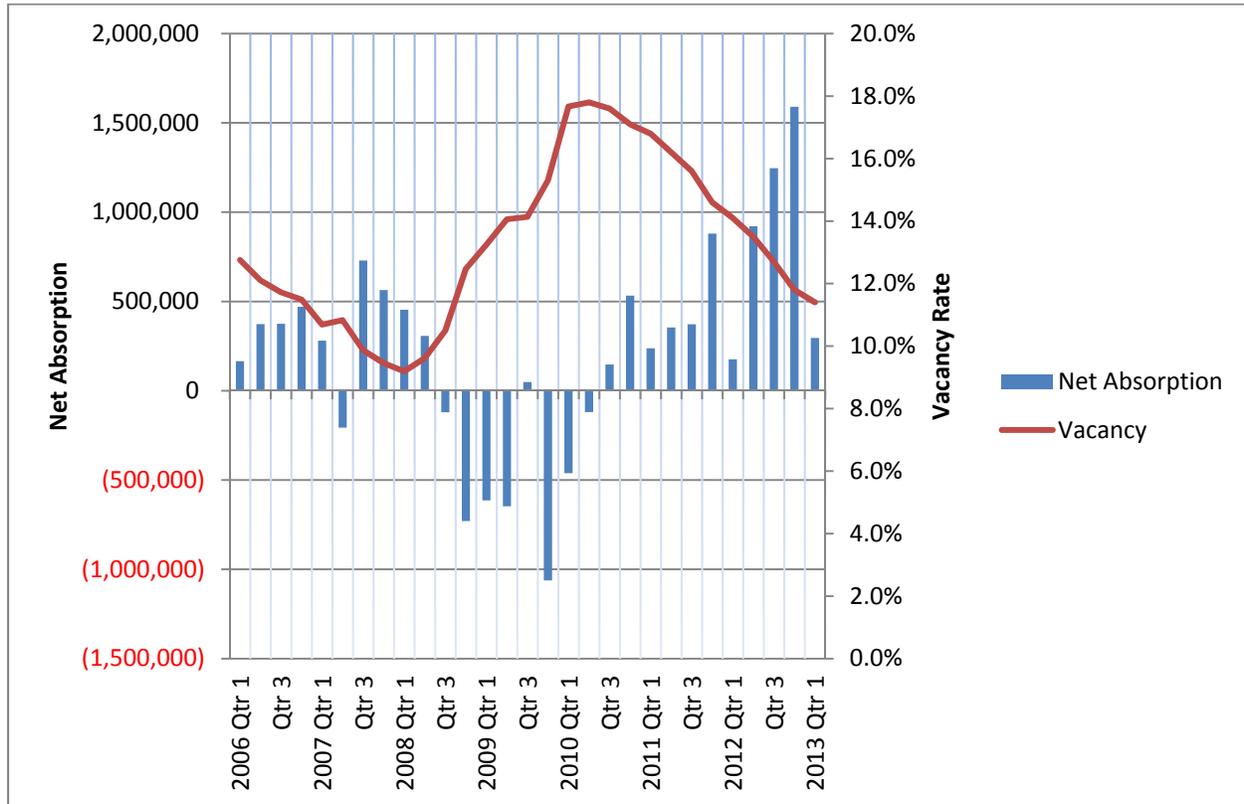
According to the April 2013 update to the Economic Barometer, the downtown office vacancy rate was 11.4 percent in the first quarter of 2013. At the same time, the net absorption rate was estimated to be approximately +295,000 square feet, meaning that 295,000 additional square feet were occupied compared to the quarter before. This data, shown in Exhibit 3 below, can't be broken down by Supervisorial District but primarily represents the downtown commercial areas of Supervisorial Districts 3 and 6.

As seen in Exhibit 3, the downtown office vacancy rate is well below its peak of nearly 18 percent in the first three quarters of 2010, but still above its previous seven-year low of 9.2 percent in the first quarter of 2008. The data also shows that the net absorption rate has been positive and generally increasing since the third quarter of 2010. According to the Jones Lang LaSalle report that contained the data, these trends have led to additional commercial construction and renovation activity to try to meet increased demand. Despite these efforts to increase supply, rents are reported to have increased 3.8 percent since the previous quarter and 15 percent since the first quarter of 2012.

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<sup>3</sup> Net absorption is the square feet leased in a specific geographic area over a fixed period of time after deducting space vacated in the same area during the same period.

**Exhibit 3: Graphical Profile of Historical Net Absorption and Vacancy Rates for Office Space in Downtown San Francisco**



Source: Jones Lang LaSalle as reported by the Controller’s Office of Economic Analysis

While the Office of Economic Analysis does not provide projections, Jones Lang LaSalle projects the downtown office vacancy rate to continue to drop while supply of, and demand for, downtown office space continues to increase. Specifically, the 2013 first quarter edition of Jones Lang LaSalle’s *Office Insight* states:

As the landscape of San Francisco continues to change and evolve with new developments and amenities, the pipeline of tenant demand going into 2013 is expected to remain steady. However, tenants continue to face heightened rental rates, which will continue to be a challenge for those tenants in industries that are still recovering [from the economic downturn].

**Other Indices**

In our efforts to obtain a comprehensive and accurate commercial vacancy rate for the City, the Budget and Legislative Analyst found several reports prepared by other real estate consulting firms, but none covered all commercial real estate segments for the entire City or provided information for all neighborhood commercial areas. The other indices reviewed were produced by (1) CBRE, Inc and (2) Colliers International. All of these additional reports provided information that was generally consistent with the trend data provided by the Office of Economic Analysis via Jones Lang LaSalle: a reduction in downtown commercial vacancy rates.

CBRE, Inc., a real estate services firm, prepares quarterly reports on vacant office space in buildings with at least 10,000 square feet in the downtown area only.<sup>4</sup> While CBRE, Inc. consistently estimates the vacancy rate to be about two percent lower than Jones Lang LaSalle's estimates, the two firms both show decreasing vacancy in recent months. The latest report prepared by CBRE, Inc. estimated that the downtown office vacancy rate was 8.7 percent in the first quarter of 2013, down 0.8 percent from their estimate of 9.5 percent for the fourth quarter of 2012. These figures and the vacancy rates published by the Office of Economic Analysis, for the fourth quarter of 2012 and the first quarter of 2013, are shown in Exhibit 4 below.

<b>Exhibit 4: San Francisco Office Vacancy Rate Estimates</b>		
<b>Firm/Agency</b>	<b>4<sup>th</sup> Qtr 2012</b>	<b>1<sup>st</sup> Qtr 2013</b>
Office of Economic Analysis/ Jones Lang LaSalle	11.8%	11.4%
CBRE, Inc.	9.5%	8.7%
<b>Average</b>	<b>10.65%</b>	<b>10.05%</b>

Source: Office of Economic Analysis and CBRE, Inc.

Citywide vacancy rates for 2011 and 2012 retail shopping centers only are shown in Exhibit 5, as compiled by Colliers International. As can be seen, the shopping center vacancy rate of 4.0 percent reported for the fourth quarter of 2011 dropped to 3.8 percent for the same period in 2012. While the Citywide shopping center vacancy rate is trending downward, the rate does not capture differences by neighborhood.

<b>Exhibit 5: San Francisco Retail Shopping Center Vacancy Rate Estimates</b>		
<b>Firm/Agency</b>	<b>4<sup>th</sup> Qtr 2011</b>	<b>4<sup>th</sup> Qtr 2012</b>
Colliers International	4.0%	3.8%

Source: Colliers International

### **Factors that Contribute to Commercial Vacancies**

According to Mr. Jordan Klein, Senior Project Manager of the Invest in Neighborhoods program at OEWD, there are six main factors that contribute to commercial vacancies in San Francisco. The factors include:

1. **Normal Turnover:** According to Mr. Klein, many properties in commercial corridors are vacant due to normal turnover of businesses. Typically these vacancies last 12 months or less.
2. **Non-Leasable Building:** Many buildings may not be legally leased to tenants due to building code issues such as compliance with the Americans with Disabilities Act or necessary electrical

<sup>4</sup> The downtown area covered by CBRE, Inc. includes the Financial District; South of Market (SOMA); Union Square; Mission Bay/China Basin; Potrero Hill; Jackson Square; North Waterfront (north of Columbus Avenue and Broadway); Civic Center; and, the Van Ness Avenue Corridor.

or plumbing repairs coupled with the building owner's inability or unwillingness to invest in necessary upgrades.

3. **Lack of Information:** Some buildings remain vacant due to an inability by the owner or manager to find appropriate tenants. According to Mr. Klein, this is largely due to buildings not being effectively marketed, particularly in outer neighborhoods that don't have commercial real estate broker services. In some instances, OEWD reports that owners lack sophistication around commercial real estate, lack the tools or resources to effectively market spaces and execute leases, and lack the financial capacity to hire brokers and lawyers to assist with lease negotiations.
4. **Non-Conforming Uses:** In some instances, retail spaces are held vacant because the owner is using it for a purpose that is not consistent with the Planning Code, such as for storage or for residential purposes.
5. **Speculation:** In some instances, building owners purposely keep their retail spaces vacant with the expectation that commercial rents or property values will increase significantly in the future.
6. **Absentee Landlords:** In some instances, building owners live or operate outside of the local area and are not motivated to fill the vacancy in a prompt timeframe.
7. **Neighborhood Conditions:** In some instances, property owners are unable to attract a viable tenant due to existing neighborhood conditions (e.g. public safety issues, poor physical conditions, negative sidewalk activity).

Through their Invest in Neighborhoods program, OEWD reports it has implemented a number of approaches to address these issues. As presented below, most of the programs are relatively new and, as a consequence, data is not available demonstrating the effectiveness of the programs.

### *Impact of Large Formula Retail*

In addition to the factors mentioned above, the growth of large formula retail establishments has been shown to result in the closure of nearby small non-formula establishments in other studies. According to a previous study conducted by the Budget and Legislative Analyst,<sup>5</sup> it was estimated that if a large formula retail store opened in a central location in San Francisco,<sup>6</sup> approximately 195 small non-formula retail food establishments, averaging 2,500 square feet each, would be closed after one year of the opening of the large formula establishment. The report further found that two years after the opening of a large formula retail food establishment, the cumulative impact would be the closure of an estimated 321 small non-formula retail food establishments of 2,500 square feet each. These estimates were based on the calculation of square footage reduction employed in two previous studies that analyzed the impact of Walmart stores in Chicago<sup>7</sup> and New York<sup>8</sup> and may therefore vary from the economic impact of a formula retail store other than Walmart. At this time, to the Budget and Legislative Analyst's knowledge, no analysis has been conducted showing the impact, if any, of the larger formula retail establishments that have opened in San Francisco on current commercial vacancy rates.

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<sup>5</sup> Possible Impacts of Formula Retail on Fresh Food Businesses, July 25, 2012 report to Supervisor Mar by the Budget and Legislative Analyst.

<sup>6</sup> For purposes of the 2012 analysis, the Budget and Legislative Analyst estimated the impact of the opening of an 80,000 square foot retail establishment that sells fresh food. This would be significantly larger than fresh food retail establishments currently in San Francisco.

<sup>7</sup> "The Impact of an Urban Wal-Mart Store on Area Businesses: An Evaluation of One Chicago Neighborhood's Experience" by Julie Davis, David Merriman, Lucia Samayoa, Brian Flanagan, Ron Baiman, and Joe Persky, December 2009.

<sup>8</sup> "Food for Thought: A Case Study of Walmart's Impact on Harlem's Healthy Food Retail Landscape," Office of the Manhattan Borough President, Scott M. Stringer, November 2011.

According to Mr. Klein, the Planning Department is currently undertaking a study of the impact of formula retail and formula retail controls on vacancies and neighborhood vitality, which will be completed later this year. This study may provide additional information as to the impact of large formula retail on neighborhood commercial vacancies.

### City Strategy for Addressing Commercial Vacancies

Although there is no comprehensive Citywide strategy for addressing commercial vacancies, there are various ordinances and programs throughout several City departments that aim to prevent or address the problems associated with extended commercial property vacancies. These programs are concentrated mostly in OEWD, but are also found in the Department of Building Inspection and, tangentially, in the Department of Public Works and the Office of Small Business. Information on each of these departments' role and performance is detailed below.

#### Office of Economic and Workforce Development

OEWD manages the most extensive programs in the City focused directly on preventing or reducing commercial vacancies under the Invest in Neighborhoods initiative. While the Department has programs that seemingly address most of the major causes of commercial vacancies, many of these programs are less than a year old, as can be seen in the detailed descriptions below, and therefore have had a limited impact, if any, thus far.

In fall 2012 OEWD launched Invest in Neighborhoods, an initiative to provide targeted assistance to select neighborhood commercial districts in the City through a variety of programs. Under this initiative, OEWD works with other City agencies to leverage existing resources that respond to the specific needs and opportunities in each commercial district. The program is being piloted in 25 neighborhood commercial districts around the City (corresponding to six of the seven neighborhood commercial corridors that OEWD previously included in its reported retail vacancy rate plus 19 new neighborhood commercial corridors that will be included in the vacancy rate for the first time later this year, for a total of 25 commercial districts, as listed on pages 5 and 6).

OEWD reports it has recently developed an agreement with the Planning Department to conduct assessments of each of the 25 commercial districts where the program is being piloted. During FY 2013-14, OEWD and its partner agencies and community based organizations will develop and deploy customized service plans for each neighborhood, informed by the results of these assessments. OEWD reports that interventions deployed through Invest in Neighborhoods – including public space activation, beautification projects, public safety campaigns, community capacity building, and other types of neighborhood improvement projects – improve the retail environment and may contribute indirectly to preventing commercial vacancies and filling existing vacancies.

Using the Invest in Neighborhoods framework, OEWD manages the following programs that aim to prevent commercial vacancies or address existing commercial vacancies:

#### OEWD Programs Aimed at Preventing Commercial Vacancies

- **Jobs Squad (initiated January 2013):** The Jobs Squad program assists small businesses by: (1) providing information on existing City resources and programs that directly benefit small

businesses; (2) providing technical assistance to help businesses navigate the City's permitting processes; and, (3) providing information on baseline services and customized services to small businesses in the 25 Invest in Neighborhoods commercial corridors.

- **ADA Outreach (initiated fall 2012):** In the fall of 2012 OEWD initiated a pilot outreach program in Supervisorial Districts 1, 3 and 4 to assist small businesses that may not be compliant with the Americans with Disabilities Act (ADA). The goals of the program are to increase ADA compliance and to reduce the risk of small businesses facing costly lawsuits over ADA access issues. The program consists of: (1) multilingual workshops, the first of which was held in the first quarter of 2013; (2) discounted or free ADA assessments; and, (3) grants for ADA-related design and construction costs for select businesses. So far 73 businesses throughout Supervisorial Districts 4, 1, and Chinatown in Supervisorial District 3 have been approved and assigned Certified Access Specialist inspectors for surveys with 21 businesses on the waiting list, which Department staff state will be funded. Additionally, four grants ranging in size from \$15,000 to \$20,000 have been provided to small businesses for ADA upgrades.<sup>9</sup>
- **Targeted Business Retention Program (to be initiated August 2013):** According to Mr. Klein, OEWD is preparing to launch a targeted business retention program in August 2013 to be implemented in six commercial districts in FY 2013-14: (1) Broad Street; (2) Castro / Upper Market; (3) Lower Fillmore; (4) Lower 24th Street; (5) Visitacion Valley; and, (6) 3<sup>rd</sup> Street. The aim of this program is to work with community leaders to identify key businesses that are at risk of displacement and offer 10 to 20 hours of focused one-on-one business assistance. OEWD is hoping to reach at least 10 businesses per commercial district. Department staff reports that the program should begin by the end of August.

#### **OEWD Programs Aimed at Existing Commercial Vacancies**

OEWD reports that, through its own staff and grantee organizations, it facilitates the leasing of vacant spaces through a variety of direct interventions. This includes outreach to property owners to enhance the marketing of their space; recruitment of existing business operators to expand to a new location; bundling of financing programs such as loans, tax credits, and grants; facilitation of lease negotiations; and, assistance with the permitting and licensing processes. These efforts are described in more detail below:

- **Storefront SF (initiated in "beta mode" in April 2013):** Storefront SF is an online database, which aims to connect property owners who have vacant retail space with potential tenants in 31<sup>10</sup> neighborhoods, in an effort to cover all commercial corridors in the City. Mr. Klein states that this program is unique in that the services are: (1) free to use for the property owners/managers and those searching for a space; (2) easy to access; (3) searchable and sortable by a variety of criteria; (4) could be linked to other incentives and programs; (5) could help OEWD to develop and maintain a dataset, which can be used for other purposes such as guiding policy and program development; and, (6) would enable OEWD to highlight particular

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<sup>9</sup> These grants have been provided to Cassava Bakery and Restaurant in the Richmond, Hamburger Haven in the Richmond, Grant Place in Chinatown, and Rolling Out Bakery in the Sunset.

<sup>10</sup> The neighborhoods covered by Storefront SF include: Bayview, Bernal Heights/Glen Park, Central Market/Tenderloin, Chinatown, Cole Valley/Twin Peaks, Divisadero, Embarcadero, Fillmore, Fisherman's Wharf, Haight/Hayes Valley, Japantown, Laurel Heights/Presidio, Mission, Mission Bay/Dogpatch, Nob Hill/Russian Hill, North Beach, Noe Valley, North Beach, Outer Mission/Excelsior, Pacific Heights/Marina, Polk Street, Portola, Potrero Hill, Oceanview/Ingleside, Richmond, SOMA, Sunset/Parkside, Union Square/Financial District, Upper Market/Castro, Visitacion Valley, and West Portal. Storefront SF also has a category for "other" listings that don't fall into the 31 neighborhoods listed.

commercial districts that are a focus of the Department. Mr. Klein notes the full launch of Storefront SF is slated for later in 2013 and that Storefront SF does not currently track the cause or reason for the vacancies listed, but that the Department is working on adding that functionality to their system. OEWD does not have data available yet on what impact this program has had to date, if any, on stemming commercial vacancies.

- **Small Business Revolving Loan Fund (initiated 2009):** OEWD contracts with TMC Working Solutions to administer a revolving loan fund that provides up to \$50,000 to start-up businesses and existing small businesses that are seeking capital to expand operations. As of April 2013 the small businesses revolving loan fund had 48 outstanding loans with \$1.3 million disbursed, or an average of \$27,083. The loans are funded through a combination of Community Development Block Grants, the General Fund, and other federal and private sources.
- **Emerging Business Loan Fund (initiated May 2013):** In May 2013 this program was launched with the aim of providing \$12 million in loans with amounts ranging from \$50,000 to \$1 million. The program was initiated to help address the drop in federal SBA lending in recent years. Seven loans have been executed from the fund with a total of \$1.1 million disbursed to date, or an average loan of \$157,143 per business. This program is funded through a variety of sources including Oakland Business Development Corporation's<sup>11</sup> banks and foundation partners, the federal Community Development Financial Institution fund administered by the U.S. Department of the Treasury, and the Section 108 loan guarantee program administered by the U.S. Department of Housing and Urban Development. Further, the City pays for the loan administrator's administrative and operating fees to market, manage and oversee the loan fund, and maintain a loan loss reserve of \$595,000 with General Fund monies.
- **SF Shines (initiated December 2009):** The SF Shines program provides grant funds to small businesses for investments in facade improvements in commercial corridors. The stated goals of the program are to increase economic vitality along the City's diverse commercial corridors, attract new businesses, and provide support to existing businesses. Since December 2009, SF Shines has provided approximately \$1.25 million to 42 businesses across the City, or an average loan of \$29,762 per business. Although funding for this program has varied and included federal Community Development Block Grant and Redevelopment Agency funds, the current source of funding for this program is an allocation from the City's General Fund.
- **Non-Retail Activation of Vacant Storefronts.** OEWD and its partners improve the conditions of vacant storefronts through cleaning services, 'Art in Storefronts', and temporary pop-up activities in order to generate interest and foot traffic and mitigate the negative impacts of retail vacancies on the surrounding commercial districts.

OEWD reports that the collective success of its programs to address commercial vacancies are measured by the Department and reported by the Controller's Office in the City Services Auditor's annual performance measure report. Specifically, relevant performance measures tracked by the Department include: (1) the rate of commercial vacancies in seven targeted commercial corridors (though the program is providing services to 25 targeted commercial corridors as previously noted); (2) number of businesses receiving one-on-one technical assistance; and (3) number of businesses that benefited from OEWD and Small Business Commission programs, as identified through business surveys. A summary of these performance measures is shown in Exhibit 6 below.

As seen in Exhibit 6, OEWD reports that it met its target for commercial vacancies and exceeded its target for the number of businesses receiving one-on-one technical assistance in FY 2011-12. However,

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<sup>11</sup> Oakland Business Development Corporation serves as the loan administrator for the Emerging Business Loan Fund.

it should be noted that none of the programs aimed at preventing and ending commercial vacancies were in place during FY 2011-12 other than the Small Business Revolving Loan Fund and SF Shines loan programs. Further, the measures shown in Exhibit 6 are for seven commercial corridors only whereas the Invest in Neighborhoods program covers 25 commercial corridors. The actual impacts of OEWD's other programs aimed at stemming commercial vacancies are not yet known. In addition, the number of businesses benefitting from OEWD programs is not known for FY 2011-12 as OEWD and the Small Business Commission did not measure their performance for FY 2011-12 as they did not issue a business survey. Department managers report that OEWD and the Office of Small Business were unable to issue a business survey in FY 2011-12 due to a lack of resources and because client servicing at the Office of Small Business increased dramatically during the year.

As previously noted, OEWD has calculated the commercial vacancy rate for certain neighborhoods using a variety of methods since FY 2009-10, including the use of nonprofit organizations and local college students who canvassed commercial neighborhoods and recorded vacancies, and therefore may not be a consistent measure of the effectiveness of the Department's programs aimed at addressing commercial vacancies. Further, the relationship between the OEWD programs and the decline in the commercial vacancy rate cannot be determined because: (1) commercial vacancies have been declining anyway, at least in the downtown area, without the benefit of OEWD programs due to changes in economic conditions; (2) most of the OEWD programs are relatively new, having only commenced in the last few months and thus have probably only had limited impact thus far; and, (3) results data for the longer standing OEWD programs are not broken out for the targeted commercial corridors. OEWD staff note that the Department is planning on working with the Controller's Office to develop a framework for a more rigorous evaluation of its neighborhood economic development programs than it has used to date.

<b>Exhibit 6: Office of Economic and Workforce Development Performance Measures Relating to Programs that Address Commercial Vacancies</b>						
<b>Measure</b>	<b>2009-10 Actual</b>	<b>2010-11 Actual</b>	<b>2011-12 Target</b>	<b>2011-12 Actual</b>	<b>2012-13 Target</b>	<b>2013-14 Target</b>
Commercial vacancy rate in seven targeted commercial corridors	8%	9%	7%	7%	6%	4%
Number of businesses receiving one-on-one technical assistance	1,160	955	840	1,234	780	980
Number of businesses that benefited from OEWD and Small Business Commission programs <sup>12</sup>	0	440	400	0	1,560	1,800

Source: City Services Auditor FY 2011-12 Annual Year-End Performance Measure Report

<sup>12</sup> As identified through business surveys.

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OEWD staff note that a longitudinal study released in January 2011 by Local Initiatives Support Corporation (LISC), a partner of OEWD, evaluated a program called the Neighborhood Market Initiative<sup>13</sup> (NMI), which was a precursor to the programs listed above. According to the study, vacancy rates dropped in each NMI corridor, averaging a drop from 20 percent in 2005 to 7 percent in 2008. Vacancy declines were most dramatic in Bayview (25 percent to 8 percent), Visitacion Valley (23 percent to 12 percent), and Excelsior (20 percent to 7 percent). The Budget and Legislative Analyst has not closely evaluated the integrity of the methods or findings of this study to confirm that reported outcomes were accurate, and if so, were a result of the efforts of the NMI program.

### *Office of Small Business*

The Office of Small Business (OSB) and its Small Business Assistance Center function as the City's central point of information and referral for entrepreneurs and small businesses. According to the Office's Executive Director, Ms. Regina Dick-Endrizzi, OSB doesn't have any programs that directly address commercial vacancies. However, OSB may indirectly reduce vacancies by providing services to small businesses including: (1) assistance with licensing and permitting and (2) referrals and liaison services to other City departments, including the various programs run by OEWD. The only measure of performance that is reported regarding OSB services to small businesses is included in the OEWD performance measures as noted in Exhibit 6 above.

### *Department of Building Inspection*

As previously mentioned, the Department of Building Inspection (DBI) administers the City's Vacant or Abandoned Building Registration Ordinance, which was adopted in 2009. The purpose of the ordinance is to discourage vacant and abandoned buildings.<sup>14</sup> The ordinance requires owners of residential and nonresidential buildings to complete an application and submit annual registration fees, currently \$765, to the Department of Building Inspection 30 days after their property becomes vacant or abandoned. Failure to comply with these and other requirements can initiate enforcement proceedings, which may result in the property owner being assessed a penalty of \$6,885, or nine times greater than the \$765 annual registration fee.

According to the vacant and abandoned building registry maintained by the Department, 288 commercial and residential properties were registered as vacant or abandoned in 2012, and 233 and 151 were similarly registered in 2011 and 2010, respectively. Of all the buildings that had been registered with a fee paid in 2012, only 27 were classified for business occupants. These amounts are

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<sup>13</sup> Under the Neighborhood Market Initiative, Bay Area LISC and OEWD partnered in 2005 to fund a corridor manager in five commercial districts (Oceanview/Mission/Ingleside; Visitacion Valley; Portola; Excelsior; and, Bayview) to staff local stakeholder committees, organize district-wide promotions, encourage and coordinate merchant participation, recruit and supervise volunteers, and advocate for district interests. The program also included direct investments such as streetscape improvements, transit projects, community policing, façade rehabilitation, graffiti removal and street-cleaning, festivals, district promotions, and other efforts.

<sup>14</sup> Ordinance 194-09 defines a building as vacant or abandoned if it (1) is unoccupied and unsecured; or (2) is unoccupied and secured by boarding or other similar means; or (3) is unoccupied and unsafe as defined in Section 102 of the Building Code; or (4) is unoccupied and has multiple code violations; or (5) has been unoccupied for over 30 days. A building which is partially unoccupied and has been cited for blight under Chapter 80 of the San Francisco Administrative Code shall also be deemed a vacant or abandoned building. The ordinance further states that a building shall not be considered vacant or abandoned if: (1) there is a valid building permit for repair, rehabilitation, or construction of a building on the parcel and the owner completes the repair, rehabilitation, or construction within one year from the date the initial permit was issued; or (2) the building complies with all codes, does not contribute to blight as defined by Chapter 80 of the San Francisco Administrative Code, is ready for occupancy, and is actively being offered for sale, lease, or rent.

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likely an understatement of the actual number of vacant or abandoned buildings in the City due to the passive approach the Department takes in enforcing the ordinance. DBI only adds buildings to its registry of vacant and abandoned buildings by: (1) owners self-reporting vacancies to DBI in compliance with the Vacant or Abandoned Building Registration Ordinance; (2) complaints from residents and other community members; and, (3) referrals from Police Department substations.

While there are no performance measures that track the Department's enforcement of the Vacant or Abandoned Building Registration Ordinance, a review of the vacant or abandoned building registry and interviews with staff found that improvements could be made in enforcement and administration of the ordinance. Specifically, the lack of a proactive effort to identify vacant or abandoned buildings likely results in an undercount of vacant buildings on the registry and a shortfall in fee and penalty revenues that could potentially be collected. Further, the Department does not proactively monitor buildings once they have registered. Of the 786 total buildings listed on the registry since 2010, only 18 have been deregistered, meaning that most buildings remain on the registry indefinitely even if they are no longer vacant or abandoned and regardless of whether or not their owners have paid the annual fee. Although Department staff could assume that buildings are no longer vacant if the owners stop paying the annual registration fee, there is no direct follow up by DBI or other City staff to confirm that the buildings are in fact occupied. Department staff has noted that they are making efforts to revise and update the registry to better track vacant properties, but it is unclear how quickly and how effectively this will be completed.

### *Department of Public Works*

The Department of Public Works (DPW) is responsible for implementing the Community Preservation and Blight Reduction Act,<sup>15</sup> which went into effect in 2009. The purpose of the ordinance is to reduce the number of blighted properties. Blight is often associated with vacant and neglected buildings though this DPW program is aimed at both vacant and occupied commercial and residential buildings.

According to Mr. Larry Stringer, Deputy Director of Operations at DPW, the vast majority of properties that are inspected for blight come to the attention of the Department through 311 calls. During an inspection, DPW staff review the building for signs of blight, including (1) properties with overgrown or decaying vegetation; (2) buildings or structures that are unpainted or have substantially worn paint; (3) buildings or structures with graffiti and/or significant amounts of defaced sections; (4) property where the outdoor area contains rubbish or debris not commonly stored outdoors; or, (5) property with conditions that present public safety risks. If an inspector finds that a building meets the program's definition of blight, the property owner is sent a notice to repair and/or improve the property within 15 days. If the property owner does not respond to the notice DPW can initiate repairs and bill the property owner.

There are currently no performance measures that track DPW's implementation of the Community Preservation and Blight Reduction Act. Mr. Stringer estimates that about 95 percent of the properties cited for blight are due to graffiti that is neglected. The remaining estimated 5 percent are due to other signs of blight such as chipped paint, overgrown weeds, and broken windows. Mr. Stringer does not have data available regarding how many of the cited buildings are commercial and how many are residential nor the amount that are vacant, though he states that most of the properties they work with are occupied.

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<sup>15</sup> The Community Preservation and Blight Reduction Act is codified in Chapter 80 of the City's Administrative Code.

A review of the Department's procedures manual found that there were no references to the Vacant or Abandoned Building Registration Ordinance administered by DBI. Revising the Department's procedures to require a referral to DBI when a DPW Inspector believes that a building may be vacant or abandoned would help the City's efforts to identify all commercial vacancies.

### **Peer City Approaches to Prevent/Address Commercial Vacancies**

The Budget and Legislative Analyst collected information about how other municipalities are attempting to prevent and address commercial vacancies. In addition, the Budget and Legislative Analyst reviewed research prepared by a Philadelphia-based coalition of non-profit groups and the Building Industry Association of Philadelphia, known as Fix It Philly, on best practices for addressing vacant real estate. It should be noted that a number of peer cities are facing significant effects from the loss of population in the second half of the 20<sup>th</sup> Century, which San Francisco did not experience to the same degree, and that most of these programs apply to fully vacant buildings or parcels.

#### **Washington, D.C.: Vacant Building Tax**

Washington, D.C. imposes a supplemental property tax on commercial and residential vacant buildings. The property tax rate for vacant non-blighted buildings in Washington, D.C. is five percent of assessed value and the rate for vacant blighted buildings is 10 percent of assessed values. Vacant properties are identified by the Department of Consumer and Regulatory Affairs by responding to complaints from citizens, the City Council, and other City agencies. The imposition of a vacant building tax would not be permissible under current California state law as the California Constitution defines the maximum ad valorem (based on value) tax on real property as one percent of assessed value, not including supplementary property taxes for any voter-approved bonded indebtedness.

#### **Michigan and Dallas: Land Banks**

The State of Michigan and the City of Dallas, Texas have created land banks, which are public authorities or non-profit entities created to efficiently acquire, hold, manage and develop vacant and abandoned properties. Most land banks fill their inventory with properties obtained through the tax foreclosure process and then sell or transfer the properties based upon locally developed priorities. As a result, laws that establish or authorize land banks typically also reform tax foreclosure sale laws to allow foreclosed properties to be transferred to the land bank rather than sold at a tax sale<sup>16</sup> to the highest bidder. Land banks are typically authorized to transfer properties without the need for extensive sign-offs from elected officials, such as a Treasurer or Tax Collector, in order to get properties quickly back on the market.

Creating a land bank would probably not have a strong impact on commercial vacancies in San Francisco. According to Mr. Greg Kato, Policy and Legislative Manager with the San Francisco Treasurer and Tax Collector's Office, nearly all of the properties that fall behind on their property taxes are able to pay all back taxes before they are put up for auction (the Treasurer and Tax Collector has the right under State law to sell properties that are delinquent on property taxes after five years). Further, Mr. Kato

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<sup>16</sup> A tax sale is the sale of property by a taxing authority after a period of nonpayment of taxes. In most states, including California, the defaulting party has a redemption period during which he/she may pay the unpaid taxes, interest, and court costs to redeem the property.

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notes that the foreclosure process is strictly governed by State law, which gives the City very little flexibility to experiment with the processing and disposition of tax delinquent properties.

### **Chicago and Milwaukee: Vacant Property Registration**

The cities of Chicago, Illinois and Milwaukee, Wisconsin are among other American cities, in addition to San Francisco, that have enacted vacant property registration laws. As previously described, vacant property registration laws such as San Francisco's require owners to register a property after it has been vacant for a certain number of days. The owner must also pay annual registration fees, which typically increase the longer the property is vacant, although this is not the case in San Francisco where a flat fee of \$765 is due every year the property is vacant.

According to the Fix It Philly Coalition, described above, some cities have experienced difficulty gaining vacant property owners' compliance with registration laws. According to the Milwaukee Journal Sentinel,<sup>17</sup> in the first year of the City of Milwaukee's enactment of a vacant property registration law only 15 percent of vacant property owners had registered. In an effort to improve compliance with vacant building registration requirements, the City of Chicago has instituted a fine of up to \$1,000 per day for unregistered vacant buildings beginning on the 31<sup>st</sup> day the building is vacant. According to the Milwaukee Journal Sentinel, as of May 2010, 7,831, or 65 percent, of the 12,000 estimated vacant buildings in Chicago were registered. As mentioned previously, San Francisco DBI may charge a fee of nine times the registration fee, or \$6,885, in instances when building owners are not compliant with the City's Vacant or Abandoned Building Registration Ordinance but Department staff was unable to provide an estimate of the percentage of vacant building owners that were compliant with the ordinance. According to the DBI vacant and abandoned building registry, the nine times fee of \$6,885 has been paid on 33 properties since 2010.

### **Baltimore: Receivership of Nuisance Properties**

The City of Baltimore, Maryland and nonprofit organizations in that city can bring an action against any vacant property with an outstanding building violation notice to put the property into receivership. Receivership gives the City and nonprofits the ability to rehabilitate properties that are significantly out of compliance with code requirements when the property owner refuses to do so. A legal action places the property under the control of a judicially appointed receiver who repairs the building so that it meets code requirements. Once a receiver is appointed, the receiver's expenses become a super-priority lien on the property. The receiver may foreclose on the lien before rehabilitation work has begun and sell the property to a qualified developer to conduct the rehabilitation. According to the National Community Revitalization Coalition, 85 percent of property owners in Baltimore made necessary repairs or sold their property when faced with the threat of receivership.

Like the use of land banks, San Francisco may have difficulty implementing a receivership ordinance for properties seriously out of compliance with building codes due to the strict State law that governs the foreclosure process. Implementation of such a program in San Francisco may require amendment to State law.

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<sup>17</sup> Willie L. Hines Jr., The burden of vacant buildings, Milwaukee Journal Sentinel (December 20, 2010).  
<http://www.jsonline.com/news/opinion/112212659.html>

### Policy Options for Consideration by the Board of Supervisors

There are several policy options available to the Board of Supervisors to improve the City's efforts at preventing and reducing the number of prolonged commercial vacancies. These include, but are not limited to, the following:

1. The Board of Supervisors could request the Director of the Department of Building Inspection to study and report back on cost-effective methods that the Department could use to more proactively administer and enforce the Vacant or Abandoned Buildings Ordinance so that the program could serve as more of a deterrent to prolonged commercial vacancies and the registry could provide a more accurate reflection of vacant and abandoned buildings throughout the City and by individual commercial area.
2. The Board of Supervisors could consider amending the Vacant or Abandoned Buildings Ordinance to include commercial space in buildings that are vacant for prolonged periods of time even though other commercial or residential space in the building may be occupied.
3. To ensure a comprehensive Citywide perspective and better link between OEWD's activities and its performance measures, the Board of Supervisors could request that the OEWD Director of Economic Development enhance the Department's performance measures by annually reporting to the City Services Auditor on the commercial vacancy rate by specific neighborhood commercial corridor instead of only the commercial vacancy rates for seven selected neighborhoods currently reported to the City Services Auditor as a performance measure.
4. The Board of Supervisors could consider enhancing existing small business loan programs currently in effect to the extent that OEWD can empirically demonstrate that these programs enable businesses to continue operating in San Francisco and therefore reduce commercial vacancies.
5. In conjunction with OEWD's current plans to expand its program performance measures, the Board of Supervisors could request the OEWD Director of Economic Development to monitor and report the performance of new services being provided, including outreach to small businesses on ADA issues and the creation of Storefront SF, an online database of commercial vacancies throughout the City. Performance measures on the ADA program could include number of businesses that received free access surveys, number of businesses that received grants to improve access to be compliant with the ADA, and/or number of businesses required to close due to non-compliance with the ADA. A performance measure for the Storefront SF commercial vacancy listing could include number of commercial vacancies filled as a result of the listing.
6. The Board of Supervisors could request the Directors of OEWD and the Office of Small Business to consistently monitor their performance in the number of businesses reached through their programs by conducting annual business surveys or through another method approved by the City Services Auditor.
7. The Board of Supervisors could request the DPW Deputy Director of Operations to revise departmental procedures to require a referral to DBI whenever a DPW inspector believes or

suspects that a building may be vacant or abandoned when administering the Community Preservation and Blight Reduction Act.

8. The Board of Supervisors could consider strengthening the penalty for non-compliance with the City's Vacant or Abandoned Building Ordinance to be consistent with the City of Chicago's penalty fee of up to \$1,000 per day for every day that the building owner fails to comply with registration enforcement proceedings.
9. The Board of Supervisors could consider legal and programmatic options for the City taking control and disposing of long-term vacant properties through a foreclosure-based process. Specifically, the Board of Supervisors could request that the Treasurer and Tax Collector conduct a study to determine the feasibility of this option as well as the specifics and feasibility of amending State law, if necessary.