



Introduction to Florida Land Development News

Welcome to the first issue of the Florida Land Development Newsletter. As my company is in the market looking at "broken" land development deals and notes for sale, I realized there are a lot of changes going on in the land development and entitlement processes. In a normal market, the development community would be reacting - either positively or negatively - to proposed regulation changes that will have significant affects on development in the years to come. Because of the decline in just about every segment of the business community, many new legislative and financial issues are slipping by, largely unnoticed. This newsletter's goal is to keep you informed on these important issues and my hope is that it will provide you or one of your clients with information you may not have previously considered (or been aware of) to aide you in your decision making process. I have asked seasoned professionals in the development business to provide some insight on topics they know well. Feel free to contact any one of the authors directly or you can send me an email with your question and I will get it to the right person. Enjoy!

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Compensatory Mitigation Rule by Lynn Zenczak



Lynn is Director of Sales & Marketing for Mitigation Marketing in Fort Myers.

In July 2008, a federal guidance known as the Compensatory Mitigation Rule was issued by the United States Army Corps of Engineers. Among other objectives, this new rule established a hierarchy among mitigation options which created equivalent standards for all types of mitigation. The new rule does not change *when* mitigation is required but rather *where* and *how* mitigation is required by the federal

permitting agencies.

The goal of the new rule is to reduce risk and uncertainty in mitigation and to establish a preference hierarchy when offsetting unavoidable wetland impacts. This new hierarchy establishes wetland mitigation banks as the most preferred option with in-lieu fees as the second most desirable option and permittee-responsible mitigation as the third option. The old ideal of on-site mitigation is replaced with the new hierarchy.

The most significant change of the new rule is that all three mitigation options will be held to the same standard of quality and results as dictated by the 12 fundamental components: objectives; site selection criteria; site protection instruments such as conservation easements; baseline information for the impact and the compensation sites; credit determination methodology; a mitigation work plan; a maintenance plan; ecological performance

standards; monitoring requirements; a long-term management plan; an adaptive management plan; and financial assurances. The new rule was established to create a "level playing field" among all forms of mitigation. In the hierarchy, wetland banks are deemed most desirable because of the increased emphasis on large scale, regional mitigation with a watershed context as opposed to the smaller, isolated mitigation efforts resulting from on-site mitigation. Mitigation banks have been required to utilize the 12 fundamental components since the origination of the bank concept. Because of this, in addition to the watershed context, there is less risk and uncertainty involved when purchasing credits. Credits only become available to the bank to sell *after* performance standards are met. Banks must be approved to provide for wetland impacts by both state and federal agencies.

Certain mitigation banks are approved to provide habitat mitigation along with wetland mitigation. For example, both the Big Cypress Mitigation Bank and the Corkscrew Regional Mitigation Bank are approved by the US Fish and Wildlife Service to provide both Panther and Wood Stork Mitigation along with the wetland credits. Additional Panther Mitigation required for the project may be purchased at a Panther Conservation Bank.

In this depressed real estate market, the cost of many types of mitigation credits have significantly decreased, some as much as 50%. This provides a wonderful temporary opportunity for the developer to acquire much needed credits at a steep discount.

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Developer's Reality by Andrew Zeck



In good times of sinking cap rates, the developer made HUGE profits in excess of what his initial pro-forma indicated. The party got even better when the small shops rented at much higher rates than anticipated and lower vacancy was used in underwriting deals. A deal that was expected to net \$2M in 2000 might have actually resulted in a \$8m profit when sold in 2007 after cap rates fell 2 points and rents increased 30% . In the "good 'ol days" cap rate declines, increasing rents and lower vacancy made millionaires out of those with the wisdom or dumb luck of perfect timing. Pretty soon the rich and jubilant development industry, spurred by greed, bid up land values and attracted more players until the fat windfalls became less, but retailer demand, low equity requirements and low interest rates kept the party going.

Optimistic about the future, developers hoped

that there was always potential for a repeat of windfall profits, but in the meantime they were still happy with multiple deals that netted \$2M each, (a typical profit for a grocery anchored shopping center.) Trust me when I tell you that this handsome profit is justifiable when one considers the myriad of risks and costs associated with running a development business. Add in the equity requirement and a typical 3 year cycle and it doesn't look that impressive any more. Furthermore, profits are generally governed by the anchor tenant that typically approves the pro-forma and structures its rent to ensure that the developer does not make an obscene profit that is only possible with the long term commitment of the anchor tenant.

Nonetheless, \$2M with hope of future windfall was good enough for many. Little did they know that they really needed to structure a deal with \$5.5M of projected profit to ensure against the horrible storm they are battling now.

But surely you are still in the money as a developer with a pipeline of "bread and butter" grocery anchored shopping center developments... right? Wrong. Even these venerable real estate investments are getting bludgeoned, albeit less than other retail product. Besides the increase in cap

rates there are 3 other important elements that are sharpening the opposite edge of the blade right now... lower rental rates, higher vacancy, and lower out parcel values.

Seemingly shallow cuts into the solid pro-formas for these shopping centers make their rock solid investment foundations seem like brittle chalk. The truth is that Johnny Economy slapped the erasers together and returns have vanished in a cloud of dust. Cuts like a 1 point move in cap rate, a 20% reduction in small shop rent, a 5% increase in vacancy, and a 35% decrease in out parcel values seem hurtful but not disastrous when considered individually, but taken together these demerits drastically change the developer's position. A typical grocery anchored shopping center might have required a total investment of \$15M equity of \$3M and generated a profit of +/- \$2M for the merchant developer. Today, the developer that engaged in this project has lost all of his anticipated profit (\$2M) and all of the cash equity (\$3M). To pour salt in the wounds, he needs to bring about half a million dollars of his own money to the closing.

Developer's Investment Summary

Time Spent: **3 years**

Soccer Games Missed: **18**

Grey hair increase: **20%**

Profit from hard work: **\$0**

Money Lost : **\$3,500,000**



Andrew is a consulting partner with Keystone Development Advisors and is located in Vero Beach.

My Conclusion: The older I get, the more willing I am to seek advice. Not because I am falling behind the peloton of practitioners, but because I can learn so much from their mad paced pedaling.

Staying at the head of the pack means I can hear the real wisdom in the breath of a figure ahead of me wearing the yellow jersey. Never assume you have earned the yellow jersey because then you have fallen to the rear of the pack.

The real estate development and investment industry is very precarious right now. Losses are terrifying but discounts are enticing. You may be stuck in the race and pedaling faster than ever or maybe you are conserving strength for the next stage.

Regardless, I encourage you to ask for advice and listen carefully.

Do you have an idea that should be featured? Would you like to be a guest author? Email: news@keystonellc.net

Florida Water Quality by David H. Farmer, PE, AICP

In July 2010 the State of Florida will be adopting new rules regulating the quality of water discharged into the state's waterways. The new rule requirements will be based on quantifiable and measurable numeric values. Presently, Florida's water quality standards are in narrative form versus a numeric form. Florida Administrative Code (FAC) states that "in no case shall nutrient concentrations of body of water be altered so as to cause an imbalance in natural populations of flora or fauna." The narrative criteria also states that (for all waters of the state) "the discharge of nutrients shall continue to be limited as needed to prevent violations of other standards contained in this chapter [Chapter 62-302, FAC]. The purpose of the new rules is to provide "better means to protect state waters from the adverse effects of nutrient over enrichment" according to FDEP's website.



On one hand, water quality rules and criteria are nothing new to Florida. In fact, Florida's original stormwater rule was adopted in 1981 and went into effect in February 1982. On the other hand, new rules presently being drafted will have a much wider impact in terms of cost to new development, redevelopment and municipalities than existing standards. To be fair, the FDEP is not looking for ways to make life more difficult; rather, the department is reacting to a mandate by the EPA to adopt or enforce higher standards for water quality throughout the state (or else!).

Water quality is measured in terms of nutrient loading. The most common substances of concern are nitrogen and phosphorous. Limiting and reducing nutrient loads is important for the sustainability of the environment. High nitrogen and phosphorus concentrations in stormwater runoff impact wildlife and human health. Nitrates may be toxic and can cause liver damage and cancer. Phosphorus may trigger toxic algal blooms and excessive aquatic weeds in fresh water bodies as well as endanger the source of drinking waters. Other common pollutants of concern include ammonia, nitrite, orthophosphate and total dissolved phosphorus. Nitrogen, particularly nitrate, easily moves from the land into surface and groundwater, including lakes, streams, rivers, and estuaries. Florida aquifers are particularly vulnerable to impacts related to runoff from land development activities in high recharge areas where the ground water (aquifer) is not confined by a layer of clay or cap-rock. Nitrate concentrations have been steadily increasing in aquifer springs since the 1950s.

In March 2009, the state set the stormwater rule standard level of treatment as 80% nutrient load reduction (95% for

discharges to OFWs i.e. most property in SWF) OR post-development nutrient load not exceeding predevelopment nutrient load (where predevelopment is native vegetative).

What does this rule change mean to you? The answer is complicated but one very important variable is the depth from the ground surface to the water table. If the depth to the water table is more than 2', the impact will be minor. If the depth to the water table is less than 2' the impact could be quite significant. Typical residential and commercial projects in Southwest Florida permitted after July 2010 may require an additional 30% of water management area to meet the new rule requirements. In round numbers, new developments may lose 4% or more of precious developable (buildable) property.

What will the impact be to the bottom line? A 10 acre commercial site could lose over 17,000 square feet of buildable land. In South Florida that means about \$300,000 in permanently lost revenue. The same 10 acre site developed as residential could lose 2-3 lots due to the new rules resulting in a \$50,000-\$300,000 revenue reduction. Neither case above is going to bring an end to development, but added to existing government regulations there will be an increase in risk with a decrease in profit.

What can be done for your clients? After the new rule has been formally adopted, all new development projects will be required to meet the new standards. Now is the time to start planning and determining how this will affect a given project. In a recent meeting with Water Management District representatives, we were notified that if a permit has not been issued by the time the rule is adopted the project will have to be redesigned to comply with the new rule.

To summarize, the state's existing water quality rules will be updated and enforced with numeric standards in July 2010. The new water quality rule will impact all new development and municipal sewer discharges in the State of Florida. Now is the time to get informed and make your voice heard by attending a public workshop on July 22, 2009 at the Marco Island Marriott Beach Resort in the Coconut Meeting Room from 8:30 am until noon.



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Growth Management Legislation by Noah

Florida is home to great opportunities and has fostered people of vision to match historical challenges. Leaders have emerged and shaped our state when difficult times arose. Our current economic situation is generating a multitude of proposed solutions that may impact the ability of our state to continue growing its quality of life. Many individuals are involved in the debate, but the discussion has yet to yield a silver bullet.

One such solution are the amendments to Senate Bill 360, the growth management legislation that directs and guides the development of Florida's communities, recently signed by Governor Crist. It does many things to curb regulation in favor of more local control. For instance it relaxes transportation concurrency laws that will allow development to proceed without being tied to road capacity. Further, local governments can repeal or lower impact fees. This will certainly incentivizes development projects to move forward but may have effects for years to come in the

form of a backlog of infrastructure projects.

Government offices across the state are seeing a substantial decrease in staff and revenue. This has affected the timeline of project approvals and entitlements thereby increasing cost to developers. Planning departments have seen workloads drop, but staff resources have dropped even further. Due to requirements of the state and federal government such as Evaluation and Appraisal Reports (EAR) based comprehensive plan amendments, Census, and county commission redistricting, to name a few, plan amendments have been protracted up to a year. This not only adds to clog in the system and inefficient use of resources, but an additional cost for landowners and developers because of timeline increases.

The Department of Community Affairs, flush with volumes of plan amendments from previous years and reduced staff and budget, has slowed the rush on rural development in much of the state. The Rural Lands Stewardship Statute is undergoing a third iteration of rule development, a testament to a challenging public process. An alternative planning tool is sector planning or even large scale plan amendments that Secretary Pelham seems to in favor. As a planner, I prefer large coordinated planning initiatives, but the coordination of such efforts gets immensely complex and can undermine the goal of the successful design of a long range vision.

Practically speaking, expect delays in future planning amendments, and infrastructure improvements both at the local and state levels. Be prepared for a public backlash when roads are clogged and you are seeking development approvals. With politics being what they are, if a project cannot be denied for concurrency reasons then it may be found "incompatible" or "too intrusive" environmentally.

The relaxing of growth management in Senate Bill 360 may lead to a situation private landowners, developers and government planning agencies dread - the passing of the Hometown Democracy referendum. When this reaches the ballot in 2010 and is subsequently approved, all land designation changes at the comprehensive planning level will need to be passed by popular vote. The effect being that good and not so good changes to our land use patterns will be stalled. Forward momentum will be lost and any progress will be very slow in coming. If any landowners are on the fence deciding whether or not to proceed with a land-use change, it would be a good idea to act before 2010 on moving their vision and projects forward.

In Conclusion...

As you can see there are quite a bit of changes in the land development industry. The good news is mitigation credits for project impacts to wetlands and wildlife habitats are less expensive than they have been in the last 5-7 years. As Lynn wrote in her article, mitigation banks are now the preferred choice by permitting agencies to offset our project impacts. The bad news is cheap credit is not coming back anytime soon and large commercial projects will experience reduced returns and increased expenses. Andrew's article paints a picture of commercial development that is less than pleasant, however realistic. With cap rates and interest rates on the rise it will be interesting to see what the next 2-3 years brings. Water quality is the next frontier in development permitting. I think the new permitting requirements on the horizon will pale in comparison to what will be required 5 years from now. Senate Bill 360 will have a far and reaching impact. The question is will it be for the better or not. Noah got it right when he wrote we have an opportunity to make a better future. The question is will we have the courage and political will to do the hard work today that will pay dividends tomorrow.

Thank you for reading the first South Florida Land Development Newsletter.