Centre City
Development
Corporation

REPORT NO. CCDC-10-05
CCDC-10-02

DATE ISSUED:	February 17, 2010
ATTENTION:	Honorable Chair and Members of the Redevelopment Agency Council President and City Council Docket of February 23, 2010
ORIGINATING DEPT.:	Centre City Development Corporation
SUBJECT:	Hotel Sandford (1301 Fifth Avenue) – Owner Participation Agreement between the Redevelopment Agency of the City of San Diego and San Diego Housing Commission and Relocation Plan – Cortez Redevelopment District of the Expansion Sub Area of the Centre City Redevelopment Project – COMPANION TO HOUSING AUTHORITY ITEM
COUNCIL DISTRICT:	2
REFERENCE:	None
STAFF CONTACT:	John W. Collum, Senior Project Manager, 619-533-7124

<u>REQUESTED ACTION:</u> That the City Council of the City of San Diego ("Council") adopts a resolution approving the Relocation Plan for the acquisition and rehabilitation of the Hotel Sandford property ("Property").

And, that the Redevelopment Agency of the City of San Diego ("Agency") adopts a resolution:

- Approving the Owner Participation Agreement (OPA) between the Agency and the San Diego Housing Commission ("Commission") for the acquisition and rehabilitation of the Hotel Sandford property ("Property"), including an Agency loan from its low and moderate-income housing funds in the not-to-exceed amount of $6,095,000;

- Making certain determinations relating to the Relocation Plan in accordance with Title 25, Code of California Regulations Section 6010 and adopting and approving the Relocation Plan; and

- Authorizing the Agency's Executive Director, or designee, to execute the OPA and sign all documents necessary to carry out and implement the OPA.

STAFF RECOMMENDATION: That that Council adopts a resolution approving the Relocation Plan; and that the Agency approves the OPA between the Agency and the Commission for the acquisition and rehabilitation of the Property, including an Agency loan from its low and moderate-income housing funds in the not-to-exceed amount of $6,095,000; makes certain determinations relating to the Relocation Plan in accordance with Title 25, Code of California Regulations Section 6010 and adopts and approves the Relocation Plan; and authorizes the Agency's Executive Director, or designee, to execute the OPA and sign all documents necessary to carry out and implement the OPA.

SUMMARY: Hotel Sandford is a 130-unit Single Room Occupancy (SRO) residential hotel that provides affordable housing for low-income seniors. It is located on a 15,000-square-foot site at the northeast corner of Fifth Avenue and A Street within the Cortez neighborhood in downtown San Diego. The four-story building also includes first floor (7,663 square feet) and basement commercial space (3,267 square feet). The building was constructed in 1914, and designated by the San Diego Historical Resources Board as a local historical resource (HRB #215). The building was last renovated in 1989. The land is currently owned by the Downtown Senior Center Corporation, a California 501(c)(3) nonprofit corporation, while the building is owned by Senior Fifth Avenue Associates – Sandford, a California Limited Partnership. The Commission is interested in purchasing the Property from the current owners with financial assistance from the Agency. If purchased by the Commission with Agency assistance, the Property would continue to provide housing for low-income residents and be subject to long-term affordability covenants.

Centre City Development Corporation ("Corporation") staff, on behalf of the Agency, has negotiated a proposed OPA with the Commission that includes Agency financial assistance in the form of a loan in the not-to-exceed amount of $6,095,000 to cover costs to acquire the SRO residential portion of the building and rehabilitate a portion of it. The Commission would fund the remaining portions of the Property, including acquisition of the land and the building's commercial space, as well as the commercial space rehabilitation and the balance of the SRO residential rehabilitation. The term of the loan would be 55 years, and affordability covenants would be placed on the Property for 99 years. Other OPA and loan terms and conditions are outlined in this report.

FISCAL CONSIDERATIONS: Funds in the amount of $6,095,000 are available in the Agency's Fiscal Year 2010 Low and Moderate Income Housing Budget ("FY2010 Budget") to expend on costs associated with the proposed Agency loan to acquire and rehabilitate the SRO residential portion of the Property. The Property is included within the Corporation's adopted Affordable Housing Guidelines and Project Priorities regarding Expenditures of the Centre City and Horton Low and Moderate Income Housing Funds (Affordable Housing Guidelines) as one of several acquisition and/or rehabilitation projects under consideration.

These project expenditures were included in the FY2010 Budget, were taken into account when determining the subject project area's ability to fund its estimated portion of the State's Educational Revenue Augmentation Fund (ERAF) Take, and will not impact the Agency's ability to make the FY 2010 ERAF Payment at such time it becomes legally obligated to do so.

CENTRE CITY DEVELOPMENT CORPORATION RECOMMENDATION: On January 27, 2010, the Corporation Board voted unanimously to recommend that the Agency approves the OPA between the Agency and the Commission for the acquisition and rehabilitation of the Property, including an Agency loan from its low and moderate-income housing funds in the not-to-exceed amount of $6,095,000, and adopts and approves the Relocation Plan for the Property.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS: On January 20, 2010, the Centre City Advisory Committee and the Project Area Committee voted to recommend that the Corporation Board recommends that the Agency approves the terms and conditions of an OPA between the Agency and the Commission for the acquisition and rehabilitation of the Property and adoption of a Relocation Plan for the Property.

KEY STAKEHOLDERS AND PROJECT IMPACTS:

On December 18, 2009, the Commission Board voted to authorize its Chief Executive Officer (CEO) to execute all documents related to the acquisition, rehabilitation and management of the Property, as well as the proposed OPA. The Commission Board also approved a nonrefundable option payment by the Commission to the Property's current owners in the approximate total amount of $175,000, which would be applicable to the purchase price.

At its meeting on February 23, 2010, the San Diego Housing Authority ("Housing Authority") will consider:

- approving the acquisition and rehabilitation of the Property authorizing the President and CEO of the Commission to execute a purchase and sale agreement and other necessary documents to purchase the Property;

- authorizing the President and CEO of the Commission to execute the OPA and related agreements and documents with the Agency under the terms discussed in this report; and,

- proceeding with the process of procuring the necessary professional services to complete the rehabilitation work and for the permanent management of the Property after acquisition.

DEVELOPMENT TEAM

ROLE	FIRM/CONTACT	OWNERSHIP
Developer/Owner	San Diego Housing Commission/ Roger Green, Real Estate Manager	Public Agency
Architect/Contractor	To be determined	

BACKGROUND:

This proposed project advances the Visions and Goals of the Downtown Community Plan and the Objectives of the Centre City Redevelopment Project by:

- Continuing to promote the production of affordable housing in all of downtown's neighborhoods and districts, thereby promoting geographic distribution;
- Identifying the need to preserve the supply of SRO and living units;
- Encouraging preservation and construction of SRO and living units by funding renovation of older buildings and securing rent restrictions; and
- Protecting historic resources to communicate downtown's heritage and encouraging the rehabilitation of designated historic properties.

In spring 2009, a representative of the Property owners contacted the Corporation and Commission to inquire about interest in acquiring the Property, in an effort to preserve it as affordable housing. Commission and Corporation staff met with the Property's current owners in August 2009 to discuss a purchase based on an appraised determination of value. The parties agreed in principle on the terms of a purchase and sale agreement, based on a negotiated purchase price of $6,800,000, which is supported by an appraisal. On September 16, 2009, the Corporation Board directed staff to proceed with acquisition of or investment in the Property on behalf of the Agency through a joint agreement with the Commission under a structure to be determined prior to closing.

Shortly after the September 2009 Board meeting, Corporation and Commission representatives determined that the most viable option for the Property's acquisition and rehabilitation would be for the Commission to acquire the entire property with Agency financial assistance. The Commission requested funding to cover acquisition and rehabilitation costs for the building. Because the Agency's source of funding would be Low and Moderate Income Housing Budget funds, the funding request was further defined to be limited to the SRO residential portion of the building. The Commission would provide the balance of the funding needed to acquire the remainder of the Property (land and commercial space) and rehabilitate the commercial space and balance of the SRO residential.

Corporation and Commission staff negotiated specific deal terms that set forth the steps needed to move forward with the acquisition and rehabilitation, as well as the terms and conditions of an OPA including an Agency loan. The Corporation and Commission boards have approved the proposed OPA, and now Corporation staff is bringing it forward for final approval by the Agency.

DISCUSSION:

Project Description – The Property consists of a 15,000-square-foot site on which sits an approximately 82,000-square-foot, four-story building with a basement. The basement contains a television lounge, commercial-grade kitchen, large community dining room, laundry room and storage for the benefit of the 130 SRO units located on floors two through four. The basement also contains approximately 3,300 square feet (SF) of vacant commercial space and the building's electrical and mechanical rooms. The ground floor contains five tenant spaces comprising approximately 7,700 SF of commercial space, as well as main and secondary SRO lobbies/entrances and two lounges for the SRO units. The second floor contains an outdoor roof terrace. Each SRO unit includes a private bath, a small closet and sleeping room, but no kitchen facilities. The units range in size from 86 to 150 SF. One of the units measures 396 SF in size and serves as the manager's apartment. The building contains two passenger elevators that serve all five floors. The building's last renovation occurred in 1989 and included the addition of fire sprinklers, upgraded mechanical systems and plumbing, and a new roof. The Property has no on-site parking.

The building's first floor commercial space currently is partially leased, and its tenants include a barber college and a delicatessen. The leases are under month-to-month terms. The commercial leases would transfer to the Commission as part of its purchase of the Property.

After acquisition of the Property, the Commission plans to rehabilitate the entire building based on a set of upgrades and improvements recommended by consultants that conducted an assessment of the building. As SRO units are rehabilitated, the Commission plans to phase in rent increases from the existing 33 percent of area median income (AMI) levels to 45 percent AMI by Year 4. This would be accomplished through a combination of 70 percent of the units at 45 percent AMI and the remaining 30 percent of the units at 45 percent AMI combined with U.S. Department of Housing and Urban Development (HUD) Project-Based Section 8 vouchers for an initial 15-year period, if the Commission is successful in securing the vouchers.

The 45 percent AMI level, which equates to a maximum monthly rent of $590 in 2009, was derived via a comparison of rents for similar downtown properties, consideration of the Property's unit sizes and common amenities, and recognition that the Property's existing rents are currently well below comparable affordable rents. The below-comparable rents have contributed to the Property's history of annual operating shortfalls. The proposed OPA would allow the Commission to increase rents to up to 60 percent AMI during the term of affordability restrictions, but any increases would be limited to ensure the Property always includes at least 40 percent very-low-income units (or 50 percent AMI and below), consistent with the Corporation's Affordable Housing Guidelines. Targeted rents will be set at a level for maximum affordability while funding projected annual operating costs and prudent reserves.

Due Diligence – Corporation and Commission staff coordinated several due diligence items that have been used to evaluate the Property, including:

a. *Appraisal* – An appraisal of the Property, prepared on August 4, 2009, determined the "as is" value of the fee simple interest in the Property and supports the negotiated purchase price of $6,800,000.

b. *Building Condition Assessment Report (BCAR)* – A multidisciplinary team conducted an assessment of the Property's current physical condition and submitted a report. A construction management/licensed contractor firm provided a peer review of the report, supplemental information on the Property, and construction phasing plan options for the rehabilitation project. The report summarizes the existing conditions of the building and provides a preliminary scope of work and opinion of probable direct construction costs for upgrades and improvements if the Property is rehabilitated. Overall, the condition of the Property was determined to be good, but in need of certain upgrades and improvements to cure existing code and life-safety issues, as well as other repairs/replacements to shore up and improve the overall condition of the Property.

   The BCAR and peer review results became the basis of an overall development budget of $5,111,000 including direct, indirect and other costs related to the rehabilitation. As the Property's rehabilitation planning moves forward, the Commission is committed to utilizing value engineering to reduce the overall development budget if possible.

c. *Phase I Environmental Site Assessment* – A Phase I Environmental Site Assessment ("Phase I") of the Property was conducted that included limited sampling/testing to determine the presence of asbestos and lead paint. Some asbestos was found in roof materials and flooring tiles, while lead was found in paint on stucco, metal and wood finishes located in the roof penthouse. Hazardous material abatement is recommended, and costs were determined and included in the upgrades and improvements estimates noted above.

d. *Phase II Environmental Report* – The Phase I report recommends that a more comprehensive asbestos- and lead-based materials survey be conducted in accordance with relevant government guidelines prior to any building renovation activities. The survey is being conducted by the firm that provided the Phase I work and will be completed prior to closing on the Property.

e. *ALTA Survey* – Prior to closing on the Property, an ALTA survey is required. Commission staff has hired a civil engineer that is currently preparing the survey.

Housing Impact/Relocation Plan – California Health and Safety Code Section 33411 (Section 33411) requires that a feasible method or plan for relocation be prepared for families and persons to be temporarily or permanently displaced from housing facilities in a redevelopment project area. Commission staff hired the consulting firm of Overland Pacific and Cutler, Inc. (OPC) to prepare a Relocation Plan (Attachment D) for the Property's rehabilitation in accordance with Section 33411 and Title 25, California Code of Regulations Section 6038 (Section 6038). OPC evaluated temporary and permanent relocation of residents, and evaluated the 12-unit rehabilitation phasing plan to determine if this option triggers any temporary relocation of residents during the construction process.

OPC determined that no off-site relocation will be required during the rehabilitation work and that 12 residents at a time will be temporarily displaced for only approximately 10 days in another vacant room in the hotel. The total budgeted amount to relocate each resident (within 129 rooms) during the nine-month rehabilitation work is approximately $27,000. In addition, OPC determined that one other resident may be permanently displaced. This resident currently occupies the manager's unit and may need to be relocated so a future on-site manager can occupy the unit and manage the property. The approximate cost to permanently relocate this resident is estimated at $22,000. Additional consultant costs will be incurred to oversee the process to relocate residents during the rehabilitation work. All of these costs are included in the development budget.

The President and CEO of the Commission/Executive Director of the Housing Authority has reviewed and approved the Relocation Plan in accordance with Section 6038. Also in accordance with Section 6038, the Relocation Plan was provided to the Property's residents 30 days prior to consideration and approval of the Relocation Plan as part of the actions requested through this report. Corporation staff recommends that the Council and Agency approve the Relocation Plan.

Project Budget and Financing – The Commission proposes that the costs to acquire and rehabilitate the Property be equally shared between the Commission and the Agency (through a proposed loan), with the understanding that the Agency's funds would be utilized only to acquire and rehabilitate the SRO residential portion of the Property and that due diligence, closing and residential relocation costs would be equally shared between the parties.

The Commission's funding source will be funds received from the recently refinanced existing public housing stock, allowing the Commission to take advantage of the federal Build America Bonds interest rebate of 35 percent on portions of the debt related to housing since the Property will be entirely owned by the Commission. Other sources of funds available to the Commission may be substituted after acquisition, including the Build America Bonds financing being acquired by the Commission.

The Agency's funding source for its proposed loan would be from its 2010 Low and Moderate Income Housing Budget. The following table provides a breakdown of the proposed funding sources for the Property's acquisition and rehabilitation costs:

Entity	Property Portion	Funding Amount	Cost per SRO Unit
Commission	Acquisition		
	Land	$3,300,000	
	Building (Ground Floor & Basement Commercial)	$500,000	
	Other (Due Diligence, Closing, Relocation)	$140,000	
	Rehabilitation (Directs, Indirects, Lease-up Reserves)	$2,155,000	
	Commission Subtotal	**$6,095,000**	**$46,885**
Agency	Acquisition		
	Land	$0	
	Building (SRO Residential)	$3,000,000	
	Other (Due Diligence, Closing, Relocation)	$139,000	
	Rehabilitation (Directs, Indirects, Lease-up Reserves)	$2,956,000	
	Agency Subtotal	**$6,095,000**	**$46,885**
TOTALS		**$12,190,000**	**$93,770**

<u>Pro forma</u> – On behalf of the Commission, Keyser Marston Associates, Inc. (KMA) developed a project pro forma dated January 20, 2010 (OPA Attachment No. 7, Project Budget), based on the proposed funding sources, project acquisition and rehabilitation (development) costs, allocation of development costs, targeted affordability rents, commercial rental revenues, likely operating expenses, and other financial assumptions. The pro forma determined the Property's net operating income (NOI) under Commission ownership, and includes results of a 55-year cash flow analysis. All pro forma assumptions have been reviewed by both Commission and Corporation staff.

The pro forma indicates a total investment of $12,190,000, of which $6,800,000 is for the acquisition of the land and building, $279,000 is for acquisition-related costs (due diligence, closing and relocation), and $5,111,000 is for the rehabilitation (directs, indirects and operating/ lease-up reserves).

The 55-year cash flow analysis indicates that the Property is projected to provide positive NOI for Years 1 through 39 with the exception of Years 1, 25, 30, 35 and 36. During each of these five years are projected expenses relating to the turnover of retail tenants and associated expenses for tenant improvements and broker leasing commissions. Except for Year 1, which would be covered by the SRO residential and commercial operating/lease-up reserves included within the development budget, the negative NOI in these years is proposed to be covered by proceeds from an operating reserve fund that is described in detail below and on pro forma Table 7. From Years 40 through 55, the Property's NOI is also projected to be negative and is proposed to be covered by this reserve fund.

The following outlines some of the cash flow assumptions for the Property:

a. Residential Revenue – Based on State of California Housing and Community Development Income Limits for San Diego County, the rent level for the property will be based on a 45 percent AMI, which equates to a maximum monthly rent of $590. This rent level was derived from a comparison of rents for similar downtown properties and consideration of the Property's unit sizes and common amenities. Residential rent escalation is assumed to be 2.5 percent each year. The vacancy rate is assumed to be 15 percent in Year 1. The vacancy rate will be reduced by 2.5 percent each year until Year 4. At Year 4, the vacancy rate is assumed to be 5 percent and will be remain as 5 percent through Year 55. The 15 percent Year 1 vacancy rate equates to 19 units, which will be used for temporary relocation of SRO tenants within the building as construction is completed. These details are shown in pro forma Table 5.

b. Retail Revenue – Baseline retail revenue for 2010 is estimated at $41,500. This amount is based on rent from the existing barber college and delicatessen. The barber college and delicatessen rents are less than comparable market rents. In consideration of the soft economy, rents for these occupied spaces will be increased to market rates over a four-year period. Beginning in Year 5, the rents will escalate at 2.5 percent per year. For the vacant 3,000 SF ground floor space, at a highly visible corner location at Fifth Avenue and A Street, it is assumed that a tenant will be recruited to lease the space at market rate in Years 2-6. In Years 7-11, rent will escalate by 9 percent over the original rate, and beginning in Year 12, rent will escalate at 2.5 percent per year. The retail vacancy rate is assumed to be 10 percent during the 55-year pro forma period. These details are shown on pro forma Table 5.

c. Operating Expenses – Baseline operating expenses for 2010 are estimated at approximately $723,000 ($5,562/SRO unit/year), which includes administration fees, utilities, operating and maintenance, taxes and insurance, and payroll. In addition, social services, replacement reserves, resident room furniture replacement reserves, mattress replacement and a Commission monitoring fee are also included in the baseline expenses. The pro forma assumes an annual 3.5 percent operating expense escalation over the 55-year pro forma period. The assumed escalation rate is higher when compared to rates for other Agency-funded properties over the past ten years, whose rates are closer to a 3 percent escalation. The operating expense details are shown in pro forma Table 4.

d. Operating Reserve Fund – To ensure that operating expenses can be covered throughout the 55-year period, the Commission requested that an operating reserve fund be established, utilizing the Property's NOI. The NOI revenues would typically be paid out to the Commission and Agency as residual receipts. The pro forma assumes the reserve fund will earn 2 percent interest annually. Under the assumptions utilized in the cash flow analysis, it is estimated that from Years 2 through 17 (partial year), NOI revenues would be deposited into the reserve fund. In Years 17 (partial year) through 39 (with the exception of Years 25, 30, 35 and 36), NOI revenues would be distributed equally between the Commission and Agency, as the reserve fund would have adequate funds to cover possible future negative operating expenses. In Years 25, 30, 35, 36 and 40 through 55, NOI is negative and deficits would be paid from the reserve fund. Should any funds remain in the reserve fund at the end of the 55-year loan term, they would be distributed equally between the Commission and Agency.

   It is important to note that the need for and size of the proposed reserve fund is sensitive to assumptions made about annual operating expenses, residential/retail rent levels and the fund's interest rate. For example, if operating expenses could be lowered, residential/retail rent levels could be increased, and/or a higher interest rate could be earned on the fund's balance, the number of years during which the reserve would need to be funded with NOI revenues would change from the scenario set forth in the pro forma. Under the proposed structure of the reserve fund, the Commission would review the Property's performance after the first five years and every two years thereafter, and adjust timelines for anticipated deposits into the reserve fund as required to assure that it is not unnecessarily overfunded.

<u>Participation by Agency</u> – The Agency would enter into an OPA with the Commission to provide financial assistance for the Commission's acquisition and rehabilitation of the Property. The Commission would own and oversee the long-term management of the Property. Corporation and Commission staffs have negotiated specific deal terms for the acquisition/rehabilitation that would serve as the terms and conditions of the OPA, including an Agency loan.

The proposed essential terms and conditions of the OPA are as follows:

- Agency Assistance: The Agency subsidy will be provided in the form of a loan to be secured by a first priority deed of trust. The loan amount shall not exceed $6,095,000, which is linked to the pro forma (OPA Attachment No. 7, Project Budget). The Commission will make reasonable best efforts to procure additional financing sources which, if successful, will allow both the Agency and Commission to reduce their respective funding obligations on a pro rata basis. Corporation staff will work cooperatively with Commission staff to explore additional financing sources, including tax credits, federal stimulus, grants, and other state and federal affordable housing programs. Due to the need to close the Property's acquisition by March 2010, it is not anticipated that additional financing would be explored or obtained prior to closing. If additional financing is not feasible, however, the Agency and Commission funding commitments will remain in place. The Commission shall not encumber the Property with additional debt at any time during the Agency loan period without the Agency's written approval.

- Agency Loan Terms: The Agency loan is proposed as a loan with a term of 55 years and an interest rate of 1 percent (simple interest). At the end of the 55-year loan term, provided that the SRO residential units have been affordable at the agreed-upon levels and assuming no Commission default of the loan, any outstanding balance (including principal and all accrued but unpaid interest) of the loan shall be forgiven by the Agency.

- Residual Receipts/Operating Reserve Fund: The loan is proposed as a residual receipts loan with residual receipts being paid equally to the Agency and the Commission (in concert with the proposed equal sharing of funding costs). However, no residual receipts would be paid to either the Agency or Commission until an Operating Reserve Fund has accumulated sufficient capital, plus a 10 percent contingency, to cover possible negative NOI anticipated in the middle and latter years of the loan term (starting in Year 25). The reserves would be retained by the Commission and placed into an interest-bearing account with the highest secured yield available in accordance with all HUD regulations, which the Commission is obligated to follow.

  The amount of the necessary operating reserves would be analyzed and re-evaluated after five years of operation of the Property and again every two years thereafter. To the extent it is determined that reserves are in excess of amounts necessary to fund the anticipated negative NOI, any excess amounts would be distributed to the Agency and Commission on an equal basis. The Commission will make reasonable best efforts to seek operating subsidies for a portion of the SRO units to improve the long-term cash flow of the Property.

- Affordability Covenants: The Property would be encumbered by affordability covenants of 99 years in length, with at least 40 percent of the units being affordable at or below 50 percent of AMI and the remainder being affordable at or below 60 percent of AMI, and required to be operated as affordable housing for low-income residents. The Property would be subject to a regulatory agreement in favor of the Agency, to allow the Agency to count these units to meet California Community Redevelopment Law affordable housing production and expenditure requirements. Acquisition of the Property satisfies the HUD requirements that land and building ownership by the Commission meets the definition of "acquisition and/or production," and these units will count toward the Commission's goals of providing affordable housing within the City. The 130 units will count toward the 350 unit minimum that HUD has required the Commission to acquire and/or produce.

  At any time after the expiration of the initial 55 years of affordability, the Commission may request the Housing Authority to modify, release or rescind the balance of the 99-year covenant period if any of the following conditions occur:

  - The Property has a projected unfunded negative operating income of six (6) consecutive months or more, which projection shall be based upon six (6) consecutive months of actual income, expenses, and losses;

  - The Property requires substantial rehabilitation for which there is no dedicated and available source of funds; and/or

  - Any other factors which, in the opinion of the Housing Authority, justify the release of the covenants.

In the event that the Housing Authority releases the covenant within 10 years of the expiration of 55 years of affordability, and upon the Commission's transfer or sale of the Property or any part thereof, the Commission and Agency would share equally the net proceeds of any disposition of the Property up to point that the Agency receives an amount equal to its forgivable loan amount plus accrued interest through the loan maturity date. Any balance of disposition proceeds in excess of the above scenario would be allocated entirely to the Commission. The Commission would be prohibited from transferring ownership of the Property during the first 55 years of the covenant period without the Agency's written consent.

- Other proposed terms related to the Agency loan include:

  a. The Agency loan would cover only the costs of acquiring the SRO residential portion of the building and a portion of its rehabilitation costs, including contingency and indirect costs, subject to the not to exceed amount authorized by the Agency.

  b. The Commission would be responsible for the costs of acquiring all of the land and the commercial portion of the building, costs of all of the commercial rehabilitation and remaining portion of the SRO residential rehabilitation, and cost overruns during the rehabilitation that exceed the approved budget.

  c. In the event the Commission subdivides the commercial portion of the Property and sells it or any part thereof, the Commission would share the net proceeds on a pro rata basis with the Agency. The Agency's share would be deposited into the Agency's Low and Moderate Income Housing budget.

- <u>Close of Escrow</u>: Close of escrow for the Property would not be later than March 15, 2010, subject to three 30-day extensions.

- <u>Disbursement of Loan</u>: The building acquisition costs shall be disbursed through escrow at closing. All other monies shall be disbursed as construction proceeds, based on draw requests from the Commission, based on the percentage of completion as determined by the Commission architect and verified by Corporation staff or consultant. The Agency shall deposit the necessary funds for acquisition into escrow prior to the closing; all other Agency loan funds shall be disbursed through Corporation oversight outside of escrow.

- <u>Assigned Responsibilities</u>: Specific responsibilities placed on the Commission or Agency through the OPA include:

  a. The Commission shall manage the building's rehabilitation, utilizing a portion of the Agency loan for the SRO residential portion and its own funds for the commercial portion, including obtaining bids; selecting a licensed contractor(s); obtaining all necessary approvals, permits, and insurances; overseeing work of contractors; ensuring compliance with environmental requirements and the payment of prevailing wages; and paying all invoices for the work, materials and supplies.

  b. The Commission shall use commercially reasonable efforts to incorporate energy efficient and sustainable components that are likely to reduce operating costs, as referenced in the pro forma, and strive to meet guidelines and methods from Leadership in Energy and Environmental Design-Existing Buildings (LEED-EB) or an equivalent green building rating system to provide an environmentally sustainable rehabilitation.

c. Subject to the Agency's reasonable approval, the Commission or an operator chosen by Commission with experience in operating SRO hotels shall operate the Property as decent, safe and sanitary senior housing for the term of the loan and for the longer term of the regulatory agreement.

d. The Commission shall procure a relocation consultant and assume primary responsibility for compliance with relocation requirements under federal and state law, as applicable. The Agency and Commission shall share equally in the cost of any and all relocation benefits required under applicable law, with the Agency's share to be included as a cost to be covered by the proposed Agency loan.

e. The Commission, as the Property's new owner, will determine a management plan for the building's operations to cover a transition period following the Property closing and implementation of a long-term approach.

f. Both parties will mutually cooperate regarding the future use of the building basement's noncommercial space. The majority of the basement space is designated for residential ancillary uses, which would be acquired and rehabilitated using Agency loan funds. The OPA would include a mutual cooperation provision regarding efficient future uses of the basement space (e.g., conversion from residential common areas to office or retail), including, provisions for a rebate of a portion of the Agency's subsidy based on square footage, due to conversion from residential to commercial uses, and consideration for using the basement space for use by nonprofit health/social service organizations.

- Equal Opportunity: The Commission shall comply with the City's Equal Opportunity Contracting (San Diego Ordinance No. 18173, Section 22.2701 through 22.2708) and Non-Discrimination in Contracting Ordinance (San Diego Municipal Code Sections 22.3501 through 22.3517).

Evaluation of Deal Terms – Corporation staff has evaluated the proposed deal terms and believes that they are appropriate for the proposed transaction. The acquisition/rehabilitation of the Property is an opportunity for both the Agency and Commission to preserve important affordable housing units in downtown San Diego and improve the overall condition of a locally designated historic resource. It is also an opportunity for both public entities to fully collaborate and pool resources to provide affordable housing in the midst of a housing market that is lacking other sources of project financing (both public and private). Since the Agency and Commission are both public agencies which are engaged in the provision of affordable housing within the City of

San Diego, the two organizations are jointly managing the transaction for the ultimate benefit of the City and downtown San Diego in particular. For these reasons, typical transaction terms may not be warranted in this case.

The Commission has requested that the Property's NOI be utilized to fund an operating reserve fund sufficient to ensure the operation of the Property for the entire 55-year loan term. The request is part of the Commission's overall concept in which both parties (the Commission and Agency) share equally in the acquisition/rehabilitation as well as any potential operating deficits. As the parties have been negotiating the deal terms over the past several months, the Commission increased its originally proposed funding contribution from 30 percent to 50 percent, thereby lowering the potential Agency loan by approximately $1,600,000.

While the Commission is likely to explore options typical of developers which partner with the Agency during negative NOI years, such as funding from other sources to meet operational needs, lowering operating costs and increasing rental rates, the safety net provided by the reserve fund to the Commission as a public agency seems appropriate. The Commission's pro forma utilizes a very conservative underwriting approach. Corporation staff was agreeable to the reserve fund concept only if a systematic look-back was included as an OPA term to ensure that the reserve fund is not unnecessarily over funded.

The Commission also requested that the Agency forgive the balance of the loan at the end of the 55-year loan term. The pro forma indicates that the estimated amount of the outstanding Agency loan at Year 55 (including principal and all accrued but unpaid interest) to be approximately $7,386,000. Some past transactions have designated Agency loans as forgivable. Further, the OPA includes a provision that may provide the Agency with an opportunity to have all or a portion of its loan repaid in the event the Housing Authority releases the affordability covenant within 10 years of the expiration of 55 years of affordability (see "Affordability Covenants" section above). The actual amount of loan balance at Year 55 would be impacted by the actual need and size of the proposed operating reserve fund, which would be funded with Agency residual receipts that would otherwise be used to repay the Agency loan principal and interest. As noted previously, the need for and size of the proposed operating reserve fund is sensitive to assumptions made about annual operating expenses, residential/retail rent levels and the fund's interest rate. Should the actual levels of these items be more favorable than the pro forma's assumptions, the forgivable balance of the Agency loan would be lower.

<u>Level of Agency Subsidy</u> – The Commission requests that the Agency provide a subsidy in a not-to-exceed amount of $6,095,000, which would cover the cost of acquiring the SRO residential portion of the building and its rehabilitation. At a total cost of $6,095,000, and considering only the 130-unit SRO component of the building, the Agency cost per unit would be approximately $46,885. This per-unit cost is below the funding subsidy required on most

other Agency-funded affordable housing projects for recent newly constructed SROs, living units or studios, as demonstrated in the following table.

Project Name	# of SRO, Living or Studio Units	Subsidy per Bedroom	# of Total Units	Agency Subsidy per Unit	Year Completed
Parkside	28	$121,053	77	$181,579	2010
Ten Fifty B	68	$ 83,000	229	$148,000	Under construction
City Heights Square*	71	$ 61,000	150	$ 61,000	2007
Studio 15	273	$ 60,432	275	$ 60,432	2009
15^{th} & Commercial	64	$ 52,518	65	$ 52,518	Pending construction
Hotel Sandford	130	$46,885	130	$46,885	------------------------

*Senior apartments consisting of studios and one-bedroom units located outside of the downtown project areas.

Purchase and Sale Agreement – The Commission is currently negotiating a purchase and sale agreement (PSA) with the Property's current owners. The anticipated terms expected to be included in the PSA are:

- Purchase price ($6,800,000);
- Assignment of commercial tenant leases to the Commission;
- Option payment provision to cover temporary operating expenses to ensure there is no lapse in operating expenses between now and the Property closing (approximate amount of $175,000); and
- Project schedule (close of escrow by March 15, 2010).

According to a preliminary title report dated August 20, 2009, there is approximately $4,247,535 of outstanding debt on the Property. In addition, Downtown Senior Center Corporation (part of the current ownership group) has a line of credit with Bank of America in the amount of $3,200,000, which has been utilized and has been called due by Bank of America, putting the owners in a position of taking immediate action to avoid default. The line of credit is not secured by the Property. The acquisition of the Property by the Commission will allow Downtown Senior Center Corporation to repay some of the debt due on the property and repay the line of credit with Bank of America. Bank of America is cooperating with the owners by providing payment extensions during the period that the Corporation and Commission have been negotiating the proposed OPA and are processing the Property acquisition/rehabilitation and OPA approvals.

The deed of trust currently encumbering the property will be fully reconveyed upon acquisition of the Property by the Commission. Because the negotiated purchase price is less than the outstanding debt on the Property, the PSA would require that all liens and deeds of trust be released from the Property at closing so that the Commission takes title to the Property free and clear of all monetary encumbrances and debts owed to others.

Proposed Schedule of Performance – A Schedule of Performance is included as OPA Attachment No. 5. As part of the OPA negotiations, the Corporation and Commission staff have established the following schedule that includes approval of the OPA by the Agency in February 2010.

Action	Anticipated Completion
Agency and Housing Authority Meetings	February 23, 2010
Property Closing	March 2010
Construction Drawings Completed	August 2010
Building Permit Availability	October 2010
Construction Start Date	November 2010
Construction Completion Date	July 2011

PROJECT DESCRIPTION

The following is a summary of the Property:

Site Area	15,000 (SF) (quarter block)
Maximum Floor Area Ratio (FAR) Permitted Minimum FAR Required Existing FAR	8.0 – 12.0 5.0 4.2
FAR Bonuses Proposed	NA
Stories	4 stories with basement
Amount of Retail Space	10,930 SF (below grade = 3,267 SF; above grade = 7,663 SF
Amount of Office Space	NA
Type of Housing	Single Room Occupancy (SRO) units
Total Number of Units / Total Residential Square Feet	130 / 71,027 SF (below grade = 15,008 SF; above grade = 56,019 SF)
Types of Units (sizes)	129 studios (86 – 150 SF) 1 1-br (396 SF) (manager's apartment)

Existing Rental Rates - SROs	$330 – $438 per month
Number of Units Demolished	NA
Inclusionary Housing Ordinance Compliance/ Number of Affordable Units	Provision of 130 affordable apartments with placement of long-term affordability covenants
Parking Required Proposed	 0 spaces 0 spaces residential 0 spaces retail (or office) 0 total
Assessor's Parcel Nos.	533-453-03

Environmental Impact – This activity is categorically exempt from the California Environmental Quality Act (CEQA) pursuant to State CEQA Guidelines Section 15331 (entitled "Historical Resource Restoration/Rehabilitation") in that the project will involve the rehabilitation and restoration of a designated historic resource in a manner consistent with the Secretary of the Interior's standards for the treatment of historic properties. The activity does not fall within any of the classes of projects for which a categorical exemption may not be applied (Pub. Resources Code Section 21084). Moreover, the activity triggers none of the exceptions to the application of a categorical exemption set forth in CEQA Guidelines Section 15300.2. Therefore, the application of the categorical exemption(s) set forth under CEQA Guidelines Sections 15326 and 15331 is appropriate for this activity.

Because of the utilization of Build America Bonds financing (a federal government funding source) by the Commission to acquire the Property, the building's rehabilitation must be reviewed for compliance with the National Environmental Policy Act (NEPA), which is the federal counterpart to CEQA. The proposed activity is categorically excluded under NEPA pursuant to 24 CFR Part 58.35(a) (3) (ii).

CONCLUSION

The acquisition and rehabilitation of Hotel Sandford represents a unique opportunity for the Agency and Commission to assist with preventing homelessness by placing affordability covenants on the Property's SRO residential units at a favorable per-unit cost. The opportunity will permit two public agencies to leverage funds to preserve 130 affordable housing units in the downtown housing stock, while meeting each agency's affordable housing guidelines and production goals. Further, the rehabilitation of the building would preserve and improve a locally designated historic resource.

Staff recommends that the Council adopts a resolution approving the Relocation Plan, and that the Agency approves the OPA between the Agency and the Commission for the acquisition and rehabilitation of the Property, including an Agency loan from its low and moderate-income housing funds in the not-to-exceed amount of $6,095,000; makes certain determinations relating to the Relocation Plan in accordance with Title 25, Code of California Regulations Section 6010 and adopts and approves the Relocation Plan; and authorizes the Agency's Executive Director, or designee, to execute the OPA and sign all documents necessary to carry out and implement the OPA.

Respectfully submitted,

John W. Collum, AICP
Senior Project Manager

Concurred by:

Frank J. Alessi
Executive Vice President & Chief Financial Officer

Attachments: A – Site Map
B – Property Photos
C – Owner Participation Agreement
D – Relocation Plan