Agenda Report

January 27, 2014

TO: Honorable Mayor and City Council

THROUGH: Finance Committee

FROM: Housing and Career Services Department

SUBJECT: APPROPRIATE FUNDS IN THE AMOUNT OF $167,000 FROM GENERAL FUND UNAPPROPRIATED RESERVE TO THE HOUSING AND CAREER SERVICES DEPARTMENT'S FISCAL YEAR 2014 OPERATING BUDGET TO COVER DUE DILIGENCE AND LOAN REPAYMENT COSTS RELATED TO THE ACQUISITION OF THE PASADENA ENTERPRISE CENTER PROPERTY LOCATED AT 1015 N. LAKE AVENUE

RECOMMENDATION:

It is recommended that the City Council appropriate $167,000 from the General Fund unappropriated reserve to the Housing and Career Services Department's Fiscal Year 2014 Operating Budget to cover due diligence costs related to the City's acquisition of real property located at 1015 N. Lake Avenue and the repayment of a County of Los Angeles Community Development Commission ("County CDC") loan.

BACKGROUND:

The subject property, owned by the nonprofit Pasadena Enterprise Center (PEC), has a site area of 30,440 sq. ft. and is improved with a two-story commercial structure with a building area of 14,650 sq. ft. The property is encumbered with debt including a loan made by the County of Los Angeles ("County") with a current outstanding balance in the amount of approximately $593,000 and a loan made by the County CDC with a current outstanding balance in the approximate of amount of $97,000. Furthermore, there are outstanding obligations totaling over $1.146 million on Community Development Block Grant (CDBG) program loans that the City made to the Pasadena Development Corporation (PDC) over the years. PDC in turn re-loaned these CDBG funds to PEC of which $504,883 were used by PEC to acquire the subject property in March 1992. PDC was a nonprofit which provided technical assistance and credit to small businesses.

PDC operated from the subject property but had only limited success in incubating and retaining small business at the site. PDC is no longer in operation, having been absorbed by the Valley Economic Development Corporation last year. PEC has been unable to keep current on the County loans and is in the process of being desolved. With these untenable financial circumstances, the City is exploring the possibility of acquiring the property at a substantially below-market price and operating it in such manner to provide a public benefit. Under a proposed agreement with the County, the City would pay off the $97,000 County loan on behalf of PEC; PEC would deed the property over to the City; the County would forgive the $593,000 loan; and the City would forgive the $1.146 million in CDBG loans.

The Housing and Career Services Department in coordination with the City's Real Property Manager will manage the transaction, which will include due diligence activities (e.g., title review, site survey, environmental studies, seismic study, real estate appraisal, geotechnical study, structural analysis, and a general building inspection). Pending the outcome of the due diligence investigations, the City can decide to proceed with acquisition or not.

The recommended appropriation of funds will be applied towards due diligence activities and, if the City decides to proceed with acquisition, to repay the $97,000 County CDC loan. In consideration of its forgiveness of the $593,000 loan to PEC, the County will require that the property be restricted for use by nonprofits and government/quasi-government agencies (however, existing for-profit tenants will be grandfathered in). Accordingly, after acquisition, the City would master-lease the property to a nonprofit organization which will operate and manage the building as office space for nonprofits. The building would function to foster collaboration between nonprofits, but not as a business incubator.

The nonprofit master lessee would be selected through a Request for Proposal process. Among other City conditions, the master lessee would be required to partner with an experienced property management company and to have capacity to manage any capital improvement projects that it determines necessary for the property, such as renovations, upgrades to the building systems, and seismic reinforcement. The associated capital costs would be the responsibility of the master lessee; a potential funding source is the City's Community Development Block Grant program under which annual applications may be submitted.

Currently, PEC receives approximately $8,500 in monthly property rent revenues. Property operating costs total approximately $8,200 per month, with no payments being made on the two County and County CDC trust deed loans. As indicated above, the County loan would be forgiven and the County CDC loan would be repaid. Both trust deeds would be reconveyed prior to the City taking title and any residual cash flow from the operation of the property (lease revenues minus operating costs including property management, insurance, utilities, and replacement reserve) would be applied towards the Pasadena Assistance Fund. Based on market rate rent of $1.50 per square foot (full service gross basis), if the building were fully occupied with rent paying tenants (net a 7.50% vacancy rate) the monthly income would be over $13,000. Utilizing a preliminary figure of $6,600 for monthly operating costs and capital reserve, the property under City ownership could generate an estimated residual cash flow of nearly $67,000 in the first year of operation, as shown in the attached operating pro forma summary.

COUNCIL POLICY CONSIDERATION:

The proposed action supports the City Council strategic objective to maintain fiscal responsibility and stability through the exercise of due diligence to ensure that the potential acquisition of real property with City funds is a sound and prudent investment. Furthermore, the intended use of the property as office space for nonprofit organizations will facilitate collaborative efforts between the nonprofits, thereby supporting the City Council strategic objective to support and promote the quality of life and the local economy.

FISCAL IMPACT:

The General Fund unappropriated reserve was increased at the end of FY2013 due to one-time revenues from the debt service reserve release relating to a 2006 debt issuance in the amount of $753,000 of which approximately $521,000 remains uncommitted. This action will result in a reduction in the amount of $167,000 in the General Fund unappropriated reserve (a transfer out from account #8757-101-955100) and an increase of $167,000 in both revenues (account #6807-238-955100) and appropriations (account #8166 -238-684120-51701-55) in the Fiscal Year 2014 Housing and Career Services Department operating budget. It is anticipated that $167,000 of the revenues and $167,000 of the cost will be received and spent during the current fiscal year. The estimated indirect cost of staffing to manage the due diligence activities described in this agenda report will be $3,640 over a period of approximately four months. The related indirect costs of $3,640 can be absorbed within the currently authorized FY 2014 Housing and Career Services Department budget.

Respectfully submitted,

for WILLIAM K. HUANG, Director
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for

MICHAEL J. BECK
City Manager

1015 N. LAKE AVENUE -- 30-YEAR OPERATING PRO FORMA SUMMARY

YEAR	1	2	3	4	5	6	7	8	9	10
Commercial Rent (2%/yr)	$158,000	$161,160	$164,383	$167,671	$171,024	$174,445	$177,934	$181,492	$185,122	$188,825
Commercial Vacancy (7.50%)	11,850	12,087	12,329	12,575	12,827	13,083	13,345	13,612	13,884	14,162
Effective Gross Income	$146,150	$149,073	$152,054	$155,096	$158,197	$161,361	$164,589	$167,880	$171,238	$174,663
Operating Expenses & Reserves (3%/yr)	79,200	81,576	84,023	86,544	89,140	91,815	94,569	97,406	100,328	103,338
CASH FLOW	**$66,950**	**$67,497**	**$68,031**	**$68,552**	**$69,057**	**$69,547**	**$70,020**	**$70,474**	**$70,910**	**$71,325**

YEAR	11	12	13	14	15	16	17	18	19	20
Commercial Rent (2%/yr)	$192,601	$196,453	$200,382	$204,390	$208,478	$212,647	$216,900	$221,238	$225,663	$230,176
Commercial Vacancy (10%)	14,445	14,734	15,029	15,329	15,636	15,949	16,268	16,593	16,925	17,263
Effective Gross Income	$178,156	$181,719	$185,354	$189,061	$192,842	$196,699	$200,633	$204,645	$208,738	$212,913
Operating Expenses & Reserves (3%/yr)	106,438	109,631	112,920	116,308	119,797	123,391	127,093	130,906	134,833	138,878
CASH FLOW	**$71,718**	**$72,088**	**$72,433**	**$72,753**	**$73,045**	**$73,308**	**$73,540**	**$73,740**	**$73,905**	**$74,035**

YEAR	21	22	23	24	25	26	27	28	29	30
Commercial Rent (2%/yr)	$234,780	$239,475	$244,265	$249,150	$254,133	$259,216	$264,400	$269,688	$275,082	$280,583
Commercial Vacancy (10%)	17,608	17,961	18,320	18,686	19,060	19,441	19,830	20,227	20,631	21,044
Effective Gross Income	$217,171	$221,515	$225,945	$230,464	$235,073	$239,775	$244,570	$249,461	$254,451	$259,540
Operating Expenses & Reserves (3%/yr)	143,044	147,335	151,755	156,308	160,997	165,827	170,802	175,926	181,204	186,640
CASH FLOW	**$74,127**	**$74,179**	**$74,190**	**$74,156**	**$74,076**	**$73,947**	**$73,768**	**$73,535**	**$73,247**	**$72,900**