



# Agenda Report

May 15, 2017

**TO:** Honorable Mayor and City Council

**FROM:** Housing and Career Services Department

**SUBJECT: APPROVAL OF MODIFICATIONS TO GROUND LEASE AGREEMENT WITH HERITAGE SQUARE HOUSING PARTNERS, LP FOR A CAPITALIZED GROUND LEASE PAYMENT TO THE CITY IN THE AMOUNT OF \$437,000**

**RECOMMENDATION:**

It is recommended that the City Council take the following actions:

- 1) Find that the recommended action is exempt from the California Environmental Quality Act ("CEQA") pursuant to State CEQA Guidelines per Section 15061 (b)(3), the "General Rule" that CEQA only applies to projects that may have an effect on the environment;
- 2) Approve certain modifications to the Ground Lease Agreement with Heritage Square Housing Partners, LP (Agreement No. 20,998-2) as described in this agenda report, in connection with the proposed capitalized ground lease payment to the City in the amount of \$437,000; and
- 3) Authorize the City Manager to execute, and the City Clerk to attest, the modified Ground Lease Agreement, and any and all documents in connection with the proposed capitalized ground lease payment to the City.

**BACKGROUND:**

Construction of the Heritage Square senior apartments at 762 N. Fair Oaks Avenue was successfully completed in October 2016. The project met or exceeded all three of the City's local benefits requirements (hiring, subcontracting, purchasing), and is currently in service, providing 70 affordable rental units to very low income senior citizens. The City owns the project site and leases it to the project sponsor, Heritage Square Housing Partners, LP ("Tenant"), pursuant to Ground Lease Agreement No. 20,998-2 which has an initial term of 55 years. Tenant is currently in the process of converting the project's Wells Fargo construction loan to a permanent mortgage with nonprofit lender California

Community Reinvestment Corporation. In connection with this, Tenant is seeking to make a capitalized ground lease payment to the City in the amount of \$437,000. According to Tenant, the City's below-market value ground lease poses potential tax consequences for the Low Income Housing Tax Credit financed project and its investors. A capitalized ground lease payment to the City in the amount of \$437,000 would address this issue and enable the proposed permanent loan conversion to close.

However, the terms of the Heritage Square project transaction that were approved by City Council at its regular meeting of April 23, 2012 did not provide for a capitalized ground lease payment by the Tenant. To address this, it is recommended that the terms of the Ground Lease Agreement be modified to include the following provisions: a) require Tenant to make a capitalized ground lease payment to the City in the amount of \$437,000; b) such payment shall be made before or on the date of the permanent financing conversion; and c) any other related modifications as may be deemed necessary.

#### **COUNCIL POLICY CONSIDERATION:**

This proposed action supports the City Council Strategic Planning Three-Year Goals in the area of maintaining fiscal responsibility and stability.

#### **ENVIRONMENTAL ANALYSIS:**

The action proposed herein is exempt from the California Environmental Quality Act (CEQA), pursuant to State CEQA Guidelines Section 15061 (b)(3), the "General Rule" provision of CEQA which applies to projects which may have the potential for causing a significant effect on the environment. Where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment, the activity is not subject to CEQA. The recommended action, approval of modifications to the Ground Lease Agreement for the Heritage Square project, does not fall within the definition of "project" pursuant to State CEQA Guidelines Section 15378(b)(4). Accordingly, no further CEQA review is required for this action.

**FISCAL IMPACT:**

Approval of the staff recommendation will enable the City to receive a one-time capitalized ground lease payment in the amount of \$437,000 from Heritage Square Housing Partners, LP.

Respectfully submitted,

  
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Housing and Career Services

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