

Agenda Report

May 11, 2020

TO: Honorable Mayor and City Council

THROUGH: Economic Development and Technology Committee (May 7, 2020)

FROM: Department of Housing

SUBJECT: **APPROVAL OF THE KEY BUSINESS TERMS OF A DEVELOPMENT, LOAN AND LEASE AGREEMENT WITH BRIDGE HOUSING, INC. AND A BUDGET AMENDMENT FOR FUNDING IN AN AMOUNT NOT TO EXCEED \$4,992,683 FOR THE DEVELOPMENT OF THE MIXED-USE HERITAGE SQUARE SOUTH PERMANENT SUPPORTIVE HOUSING AND COMMERCIAL PROJECT AT 710-738 NORTH FAIR OAKS AVENUE AND 19-35 EAST ORANGE GROVE BOULEVARD**

RECOMMENDATION:

It is recommended that the City Council:

- 1) Find that the proposed development of the mixed-use Heritage Square South permanent supportive housing and commercial project at 710-738 N. Fair Oaks Ave. and 19-35 E. Orange Grove Blvd. (the "Heritage Square South" project) is categorically exempt from environmental review pursuant to the California Environmental Quality Act (CEQA) Public Resources Code §21080(b)(9); and California Code of Regulation, Title 14, Division 6, Chapter 3, State CEQA Guidelines §15332, Class 32, In-Fill Development Projects, and that there are no features that distinguish this project from others in the exempt class and, therefore, there are no unusual circumstances; and
- 2) Approve a budget amendment appropriating \$3,468,834 in expenditures from the Housing Successor Low Income Housing Asset Fund unappropriated fund balance and \$1,523,849 from the Inclusionary Housing Trust Fund unappropriated fund balance to fund the proposed City loan in the total amount of \$4,992,683 through the Department's FY 2020 Operating Budget for the Heritage Square South project; and

- 3) Approve the key business terms of a Development, Loan and Lease Agreement with BRIDGE Housing, Inc. for the development of the Heritage Square South project, as described in this agenda report; and
- 4) Authorize the City Manager to execute, and the City Clerk to attest, any and all documents necessary to effectuate the staff recommendation.

EXECUTIVE SUMMARY

The subject recommendation includes key business terms with developer BRIDGE Housing, Inc. for the construction of a proposed mixed-use complex located on the City-owned Heritage Square South site. The development includes 7,500 sq. ft. of commercial space and a 70-unit permanent supportive housing (PSH) project for homeless seniors. Financing for the housing component includes 4% tax credit equity, County of Los Angeles funding, and City loan assistance in the amount of \$4,992,683 (\$72,358 per affordable unit). The local benefits requirements for the project consists of 15% local hiring, 20% local contracting, and 30% local purchasing. BRIDGE Housing will develop and operate the project under a 99-year ground lease with the City.

BACKGROUND:

On January 28, 2019, City Council approved the development concept for the City-owned site located at 710-738 N. Fair Oaks Ave. and 19-35 E. Orange Grove Blvd., totaling approximately 54,500 square feet, commonly referred to as "Heritage Square South", and directed staff to negotiate with developer BRIDGE Housing, Inc. ("BRIDGE") on the terms for the development of the site. Accordingly, the City and BRIDGE entered into that certain Exclusive Negotiation Agreement, dated July 24, 2019, Agreement No. 23,101. The original staff-recommended development concept, as approved by City Council, consisted of two components: a) commercial use with 10,000 square feet to 15,000 square feet and; b) permanent supportive housing (PSH) with up to 70 units to serve homeless seniors.

Following the City Council action, staff formed and consulted with a working group of community members comprised of Jim Morris, Luke Walker, Cindy Schneulle, Daniel Pinzon, and Rogelio Ramirez. In addition, staff and BRIDGE conducted community outreach and hosted community meetings with businesses, residents and resident associations, faith-based congregations, and schools. Constructive dialog took place in the community meetings and within the community working group. The vast majority of participants were supportive of the PSH project. Concerns were raised and discussed. Key concerns pertained to security, local benefits, and the desire for the new retail tenants to positively impact the neighborhood by bringing goods and services not currently available to the community.

Analysis of Development Scenarios

BRIDGE evaluated a number of development scenarios. These options varied by amount of retail space and parking (surface parking, at-grade structured podium parking and subterranean parking podium). Parking for this development is driven by the retail requirement (3 spaces per 1,000 sf of retail = 34 spaces). BRIDGE found the following cost impacts associated with the three parking types: 1) Surface parking has a negligible cost impact; 2) At-grade podium parking is approximately \$25,000/parking space; 3) Subterranean parking costs can run \$60,000/parking space depending on soil conditions, layback conditions and temporary shoring. The financing gaps that resulted from the development scenarios ranged from \$4.9 million (7,500 sf retail space) to \$10.3 million (15,000 sf retail space) as summarized below:

Scenarios	PSH Units	PSH Parking	Retail SF	Retail Parking	Parking Type	City Loan
#1 Recommended	69 plus 1 mgr	20 spaces (0.25/unit)	7,500	24 spaces (3/1000 sf)	Surface	\$4,992,683
#2 Not Recommended	69 plus 1 mgr	20 spaces (0.25/unit)	10,000	30 spaces (3/1000 sf)	At-Grade Podium	\$8,267,086
#3 Not Recommended	69 plus 1 mgr	20 spaces (0.25/unit)	15,000	45 spaces (3/1000 sf)	Subterranean	\$10,352,600

In early February 2020, BRIDGE consulted with a regional retail developer/owner that has a track record in Southern California in markets similar to the area within which Heritage Square South is located to gauge market demand for 10,000 sf of retail space for this location. Based on the scale of retail and location, demand was considered weak at best. Since then, COVID-19 pandemic impacts have negatively impacted retail market risk and demand. With businesses across the region and country shuttering doors, it is anticipated there will be more significant retail vacancies. Uncertain of how soon the economy will resume with demand for dining and retail, BRIDGE believes that it is prudent to avoid a large retail frontage that may be vacant for some years to come.

Accordingly, BRIDGE utilized conservative financial underwriting assumptions for the retail component of this project, resulting in a low retail revenue stream which supports conventional permanent financing in the amount of \$2.9M at best. Increasing the retail component greater than 7,500 sf will increase the financing gap, requiring additional City non-affordable housing funds to subsidize the gap. Most of the proposed \$39 million in total financing for the proposed project are required to be used exclusively for affordable housing (tax credits, state and County funds, City Inclusionary funds, and a portion of the City land contribution and Housing Successor funds). This leaves only approximately \$7 million of remaining financing sources available to support the retail development cost (conventional loan, deferred developer fee, and a portion of the City land contribution and Housing Successor funds).

Hence, given the constraints of the available funding sources and appropriately conservative underwriting, the project would not be financially feasible with a retail component in excess of 7,500 sf. As previously noted, financing sources required to be used exclusively for the development of affordable housing cannot be used to develop and operate retail space and associated parking. Any significant increase in the size of the retail space and associated parking will require additional City non-affordable housing subsidy.

Under state redevelopment dissolution law, the City, as Housing Successor, is required to encumber a certain amount from the Low Income Housing Asset Fund annually by June 30. The amount is determined by an annual audit of the fund. The minimum required amount to be encumbered by June 30, 2020 is \$2,539,446. The use of \$3,468,834 of these funds for the proposed project will enable the City to exceed the encumbrance requirement, leaving a non-programmed fund balance of \$1,102,781. In addition, \$1,523,849 in City Inclusionary Housing funds are proposed to be used for the project, leaving a non-programmed fund balance of \$1,602,018.

Based on the analysis of development scenarios, the most financially feasible development program is a three-story non-podium project that includes 7,500 sf of retail space, a PSH residential project with 70 units, and surface parking. This project has a financing gap in the amount of \$4,992,683 (\$72,358 per affordable unit) which would be filled by a direct funding subsidy from the City. The proposed project would be developed, owned and operated by BRIDGE. The PSH component would consist of 69 one-bedroom units for homeless seniors plus one (1) unit for a resident manager. Adjacent to the north of the project site is the 70-unit Heritage Square Senior Apartments that BRIDGE developed in 2016 which provides affordable rental housing for very low income seniors. Operating on the City-owned Heritage Square South site is a commercial tenant, Church's Chicken restaurant at 710 N. Fair Oaks Avenue, which BRIDGE will be responsible for relocating. The City-owned Heritage Square South project site would be leased to BRIDGE under a 99-year ground lease.

BRIDGE Experience, Supportive Services, Operations, Property Management

BRIDGE has over 16 years of experience with mixed-use and supportive housing developments. Since 2002, BRIDGE has successfully completed 11 supportive housing projects (682 total units) and 30 mixed-use projects (4,034 total units) in current operations. Of the mixed-used projects, five include tax credit financed supportive housing components.

For the proposed Heritage Square South PSH project, an array of supportive services would be available to the residents including case management, food, health care, employment and job training, and education. These services would be provided directly by or coordinated through Union Station Homeless Services under a resident supportive services contract with BRIDGE.

BRIDGE will implement a "good neighbor" policy in which community concerns are anticipated and preempted. Close proximity to BRIDGE's Heritage Square Senior

Apartments will allow for efficiencies of management, and contribute to close oversight and responsiveness to neighborhood concerns.

Measures to be in place to avoid negative impacts on the community include the following:

- The PSH component will be managed by an experienced property management firm that specializes in special needs housing.
- The availability of on-site supportive services will address the comprehensive needs of PSH residents, with ample social & recreational activity indoors as positive alternatives to passing time in the neighborhood.
- PSH residents will sign leases specifying house rules and behaviors allowed by law to be grounds for sanction or eviction if not complied with.
- Property management will take needed action to enforce lease provisions

The Developer will engage an appropriately experienced property management firm to screen residents, execute leases, collect rent, and resolve tenancy issues with residents of the PSH, as well as to oversee the maintenance of the property and compliance with development financing requirements and reporting, and to perform other functions of a property management firm in supportive housing projects. Although a property management firm has not yet been selected, BRIDGE uses The John Stewart Company (JSCo) at Heritage Square Senior Apartments, and BRIDGE will confer with JSCo during pre-development of the Heritage Square South project.

Project Cost and Financing

The estimated total development cost of the Project is approximately \$39.03 million of which \$32.13 million is attributed to the PSH component and \$6.9 million to the commercial component (see Project Budget, Attachment "A"). The City's direct funding assistance in the amount of \$4,992,683 for the development of the project would be in the form of a deed of trust loan to BRIDGE, to be repaid from the project's annual residual receipts which are not guaranteed. Use of the City loan funds would be restricted for predevelopment and construction costs related to the PSH component; City funds may not be used to develop the commercial component. As proposed, the PSH component would be developed as a 4% tax credit project, with the following permanent financing sources:

\$ 7,538,047	Equity from 4% Low Income Housing Tax Credits
\$11,000,000	State of California Multifamily Housing Program loan
\$ 6,390,000	County of Los Angeles NOFA loan and FHLB AHP grant
\$ 5,310,000	City of Pasadena land contribution (subject to 99-year ground lease)
\$ 4,992,683	City of Pasadena loan
\$ 2,916,036	Conventional permanent loan
\$ 888,556	Deferred developer fee and General Partner equity
\$39,035,322	TOTAL

All 69 income-restricted units are proposed to be rent-subsidized under the City's Section 8 Project-Based Vouchers (PBVs) program. BRIDGE intends to apply for an allocation of PBVs from the City through a competitive Request for Proposals (RFP), which is anticipated to be issued by the end of May, 2020.

KEY BUSINESS TERMS OF DEVELOPMENT, LOAN AND LEASE AGREEMENT:

The proposed Development, Loan and Lease Agreement includes the following key terms:

- 1) Property: The project site is owned by the City, located at 710-730 N. Fair Oaks Ave. and 19-35 E. Orange Grove Blvd., Pasadena, commonly referred to as "Heritage Square South." Existing improvements consist of the Church's Chicken restaurant building which will be demolished.
- 2) Project – Scope of Development: Construction of a three-story mixed-use development (the "Project") consisting: a) a permanent supportive housing complex on the second and third floors servicing homeless senior persons with 69 restricted affordable units, one (1) unrestricted resident manager unit, and amenities; b) a commercial component on the first floor of at least 7,500 sq. ft.; and c) at-grade parking for the residential and retail uses.
- 3) Developer: The project will be developed by BRIDGE Housing, Inc., a non-profit California corporation ("Developer")
- 4) Assignment: Initially, the parties to the Development, Loan and Lease Agreement (the "DLLA") will be the City and the Developer. It is anticipated that in connection with the Low Income Housing Tax Credit ("LIHTC") financing, the Developer will form a new limited partnership (the "LP") of which the Developer will be the General Managing Partner. In this event, the City, Developer, and LP will enter into an agreement pursuant to which the Developer's obligations under the DLLA will be assigned to and assumed by the LP.
- 5) Ground Lease: City will ground lease the Project site to Developer/LP for a 99-year term with rent at one dollar (\$1.00) per year or a capitalized lease payment prior to the project being placed in service
- 6) Relocation: Relocation of the commercial tenant, Church's Chicken restaurant, will be the responsibility of the Developer/LP.
- 7) Section 8 Project-Based Vouchers: The Project will require an allocation from the City of Section 8 Project-Based Vouchers for 69 units to be awarded through a competitive Request for Proposals process.

- 8) Project Cost: The Project's estimated total development cost is estimated at \$39.03 million consisting of land (\$5.31 million), hard costs (\$22.06 million), soft costs (\$8.14 million) and syndication costs and developer fee (\$3.52 million).
- 9) Project Financing: City Loan, 4% LIHTC equity, LA Community Development Authority NOFA loan, State Multifamily Housing Program loan, conventional construction loan, FHLB Affordable Housing Program grant, general partner capital contribution, deferred developer fee, conventional permanent loan.
- 10) City Loan: The City Loan will not exceed \$4,992,683, bearing interest at a fixed rate of 3.00% per annum with a term of two years for the construction period and 55 years upon conversion to a permanent loan. The City Loan will be drawn from Housing Successor and Inclusionary funds
- 11) Use of City Loan Funds: The City Loan will be used by Developer/LP to pay for City-approved predevelopment and construction costs related to the Project. City Loan funds for predevelopment soft costs may not exceed \$750,000 of which total an amount not to exceed \$500,000 may be drawn prior to award of tax credits, and an additional amount not to exceed \$250,000 may be drawn after tax credit award and prior to construction closing. The remaining amount of City Loan funds after the predevelopment draws (not to exceed \$750,000) may not be disbursed to the Developer/LP until construction closing. The City Loan funds will be disbursed on a cost-incurred reimbursement basis.
- 12) City Loan Payment: During the initial two-year construction period term, interest on the City Loan will accrue but periodic payments will not be required as long as Developer/LP is not in default of the DLA. Upon conversion to a permanent loan, the accrued interest will be added to the principal balance of the City Loan, annual payments on the City Loan will be made from the Project's net cash flow on a residual receipts basis.
- 13) City Loan Security: The City Loan will be secured with a deed of trust recorded against the Property, in a lien position subordinate only to the conventional construction loan and the CTCAC regulatory agreement.
- 14) Basic Services Offset Payment: The Project will be underwritten with a Basic Services Offset Payment to the City in the amount of \$25,000 per year.
- 15) Schedule of Performance: The DLLA will contain a schedule of performance which sets forth certain milestones and completion timeframes for the development of the Project, beginning with the execution of the DLLA and ending with the closing of permanent financing sources. If Developer is not successful in obtaining a 4% tax credit award with its application to the State, Developer will be allowed under the DLLA to re-submit 4% tax credit applications for up to two (2) additional attempts in the following tax credit cycles.

- 16) Local Benefits: The following Local Benefits requirements shall apply to the Project: a) 15% local hire; b) 20% local contracting; c) 30% local purchasing. Pursuant to the City's First Source Ordinance, the City's direct subsidy to the Project (\$4,992,683) shall be subject to recapture if the 15% local hiring requirement is not met. Furthermore, Developer shall pay to City a local benefits fee in an amount up to \$125,000 from the developer fee if the 20% local contracting and/or the 30% local purchasing requirements are not met. The amount of this fee will be calculated on sliding scale based on the percentage shortfall in meeting the local contracting/purchasing requirements.
- 17) Property Management Plan: Developer/LP shall submit to the City for approval a Property Management Plan to screen residents, resolve tenancy issues, oversee property maintenance, comply with regulatory requirements, and to perform other functions in permanent supportive housing projects. Developer/LP shall submit to the City for monitoring purposes an annual report to document compliance with property management plan requirements, identify any related issues that should be addressed, and provide status on the resolution of previously identified issues. Property Management Plan to screen residents, resolve tenancy issues, oversee property maintenance, comply with regulatory requirements, and to perform other functions in permanent supportive housing projects. Developer/LP shall submit to the City for monitoring purposes an annual report to document compliance with property management plan requirements, identify any related issues that should be addressed, and provide status on the resolution of previously identified issues.
- 18) Regulatory Agreement: Developer/LP will comply with affordable rental housing deed restrictions in favor of the City ("City Regulatory Agreement") for a term of 99 years, which will be recorded against the Property. In compliance with state law Article 34, City Regulatory Agreement will restrict no more than 49% (34 units) of the Project's 69 affordable units at Extremely Low income (35% AMI) and 51% (35 units) of the affordable units at Lower income (60% AMI). However, all 69 affordable units will be restricted at the Extremely Low income level by the California Tax Credit Allocation Committee (CTCAC) for 55 years. The City Regulatory Agreement will be subordinate only to the conventional construction loan and the CTCAC regulatory agreement. The affordable units shall be restricted to seniors who are 55 years of age or older.
- 19) City Policies: Developer/LP shall comply with all applicable City ordinances Regulations and policies including but not limited to City Minimum Wage standards, "First Source" local hiring requirements, and insurance and indemnification requirements.
- 20) Prevailing Wage: It is anticipated that the Project will be determined by the State to be subject to prevailing wage. Developer/LP will be solely responsible for complying with the State prevailing wage law on this Project and

Developer/LP agrees to indemnify the City from any prevailing wage claim that may be brought against the City.

- 21) Services Provider: Developer/LP will contract with Union Station Homeless Services to provide supportive services for the residents.

Project Schedule - Key Milestones

May 2020	Submission of application to City for Section 8 PBV allocation
Aug. 2020	Submission of Preliminary Plan Review application to City
Sept. 2020	Submission of application for State MHP funding
Nov. 2020	Submission of application for LACDA NOFA funding
Nov. 2021	Submission of 4% tax credit/bond financing application to CTCAC
Jan. 2022	CTCAC announces tax credit award
July. 2022	Start of construction
Jan 2024	Completion of construction, project placed in service

COUNCIL POLICY CONSIDERATION:

The proposed action is consistent with the City's General Plan - Housing Element and the Five-Year Consolidated Plan. The proposed action supports and promotes the quality of life and the local economy, a goal of the City Council's strategic plan.

ENVIRONMENTAL ANALYSIS:

The State California Environmental Quality Act (CEQA) Guidelines require the preparation of environmental documents to assess and report the environmental impacts of certain types of projects that could result in adverse effects on the environment. Pursuant to CEQA Section 21084, the CEQA Guidelines (Section 15300 et seq.) also define classes of projects that are found by the Secretary of the California Natural Resources Agency to not have a significant effect on the environment and thus are declared to be categorically exempt from the requirement for the preparation of environmental documents. These types of projects are exempt from CEQA, provided that none of the exceptions to the use of categorical exemptions apply (CEQA Guidelines Section 15300.2).

Among the list of categorically exempt classes of projects is Class 32 In-Fill Development Projects, as defined in CEQA Guidelines Section 15332. Class 32 projects consist of those characterized as infill development meeting the following conditions identified in Section 15332:

- (a) the project is consistent with the applicable general plan designation and all applicable general plan policies as well as with applicable zoning designation and regulations;

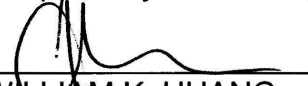
- (b) the proposed development occurs within city limits on a project site of no more than five acres substantially surrounded by urban uses;
- (c) the project site has no habitat for endangered, rare, or threatened species;
- (d) approval of the project would not result in any significant effects relating to traffic, noise, air quality, or water quality; and
- (e) the site can be adequately served by all required utilities and public services.

The proposed development of the Heritage Square South project at 710-738 N. Fair Oaks Avenue and 19-35 E. Orange Grove Blvd (the "Project") meets the requirements of Class 32 exemption, as it meets the definition of infill development; would be consistent with the applicable General Plan designation and all applicable General Plan policies as well as with the applicable zoning designation and regulations; occurs within City limits on a Project Site of no more than 5 acres substantially surrounded by urban uses; would be located on a site that has no habitat for endangered, rare, or threatened species; would not result in any significant effects relating to traffic, noise, air quality, or water quality; and could be adequately served by all required utilities and public services. Further, none of the exceptions to the use of a categorical exemption apply to the Project. Therefore, the proposed Project does not have a significant effect on the environment and has been determined to be categorically exempt under Class 32 (In-Fill Development Projects), Section 15332 of the CEQA Guidelines.

FISCAL IMPACT:

Approval of the subject recommendation will increase the Department's FY 2020 Operating Budget by an amount not to exceed \$4,992,683 by transferring \$3,468,834 from the Housing Successor Low Income Housing Asset Fund unappropriated fund balance and \$1,523,849 from the Inclusionary Housing Trust Fund unappropriated fund balance to the Heritage Square South Project (Account No. 23716003-816700-51036). Approval of this action will leave non-programmed balances of \$1,102,781 in the Housing Successor fund and \$1,602,018 in the Inclusionary fund. The City funding for the Project will be in the form of a loan secured by a trust deed. The scheduled annual debt service on the City loan would be paid from the Project's annual residual receipts which are not guaranteed.

Respectfully submitted,


for WILLIAM K. HUANG
Director of Housing

Prepared by:


James Wong
Senior Project Manager

Approved by:


STEVE MERMELL
City Manager

Attachment: Project Budget