

# Agenda Report

March 14, 2022

**TO:** Honorable Mayor and City Council

**THROUGH:** Finance Committee

**FROM:** Department of Housing

**SUBJECT:** **APPROVAL OF BUSINESS TERMS OF THE SECOND AMENDMENT TO DEVELOPMENT, LOAN AND LEASE AGREEMENT NO. 23,370 WITH BRIDGE HOUSING INC. INCLUDING ADDITIONAL CITY FUNDING IN AN AMOUNT NOT TO EXCEED \$2,000,000 FOR THE DEVELOPMENT OF THE HERITAGE SQUARE SOUTH PERMANENT SUPPORTIVE HOUSING PROJECT FOR CHRONICALLY HOMELESS SENIORS AT 710 N. FAIR OAKS AVENUE**

## **RECOMMENDATION:**

It is recommended that the City Council:

- 1) Affirm the May 11, 2020, finding of the City Council that the project discussed herein is 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, that there were no features that distinguish this project from others in the exempt class and, therefore, there were no unusual circumstances, and affirm that there is no new information or changed circumstances that would require further environmental review;
- 2) Approve a budget amendment appropriating \$2,000,000 from the Low and Moderate Income Housing Asset Fund, unappropriated fund balance, to fund the proposed City loan through the Housing Department's FY 2022 Operating Budget for the Heritage Square South Project;
- 3) Approve the business terms of a Second Amendment to 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.

**BACKGROUND:**

At its regular meeting of May 11, 2020, the City Council approved the key business terms of that certain Development, Loan and Lease Agreement No. 23,370 (the "Agreement") with BRIDGE Housing Inc. (the "Developer") to develop the Heritage Square South project (the "Project"), a 70-unit permanent supportive housing complex for chronically homeless seniors that is located at 710 N. Fair Oaks Avenue. The Agreement provided for, among other things, City loan funding in the amount of \$4,992,683 to assist the development of the Project. The Agreement was administratively amended pursuant to that certain First Amendment to Development, Loan and Lease Agreement, dated September 10, 2020, which made certain modifications to the Agreement to, among other things, comport with State affordable housing requirements.

Under the Agreement, the total development cost of the Project was approximately \$39M. In November 2021, the Developer was successful in obtaining a 9% Low Income Housing Tax Credit ("LIHTC") award in a highly competitive application environment and, more recently, the Developer received a lender's commitment for a conventional permanent loan.

However, as the Developer successfully moved the Project through the City's entitlement process, a number of construction industry-wide factors have impacted the financial feasibility of the Project, resulting in the need to increase the amount of the City loan. These factors include a general contractor / sub-contractor market that is in very high demand coupled with labor shortages resulting in much higher construction costs across all trades; and increases in materials prices by approximately 15% over the past nine months due to excessive demand and supply chain constraints. This environment has caused the total development cost of the Project to increase by approximately \$10M (from \$39M to \$49M). In response, the Developer took measures to reduce the funding gap including value engineering of the development; rebidding of the Project to general contractors; and renegotiating equity pricing and loan terms with the tax credit investor and conventional lender.

In doing so, the Developer reduced the funding gap by approximately \$8M, with a remaining gap of \$2M. Consequently, on February 14, 2022, the Developer submitted a request to the City for additional loan assistance in the amount of \$2,000,000 to solve the remaining funding gap. Staff evaluated the Developer's request and determined that the proposed City direct financing subsidy of the Project at the increased amount of \$6,992,683 (\$101,343 per restricted unit) remains a feasible and cost-effective way to address the City's critical affordable housing shortage. The staff recommendation was also reviewed on March 10, 2022, by the Internal Housing Loan Committee, which

serves the Housing Department and is comprised of staff in the City Manager, Housing, Human Services, Public Works, and Finance departments.

**BUSINESS TERMS OF THE SECOND AMENDMENT TO DEVELOPMENT, LOAN AND LEASE AGREEMENT:**

The proposed business terms of the Second Amendment to Disposition, Development and Loan Agreement for the Heritage Square South Project (the "Project") consist of the following:

- 1) Project Development Cost and Budget: The total development cost of the Project shall be increased to \$49,667,617 (see Attachment A "Project Budget").
- 2) City Loan: Funding of the City's residual receipts trust deed loan ("City Loan") for the Project shall be increased by an amount not to exceed \$2,000,000 for a total loan amount not to exceed \$6,992,683.
- 3) Equity and Other Permanent Financing: The equity and (non-City) permanent financing sources for the Project shall be revised to reflect \$25,010,099 in 9% LIHTC equity, and \$8,993,000 in conventional permanent financing.
- 4) Schedule of Performance: The existing Schedule of Performance for the Project shall be modified to reflect: a) a construction closing date that is no later than May 16, 2022; and b) a construction start date of May 17, 2022.

**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:**


At the regular meeting on May 11, 2020, the City Council made a finding that the proposed development of the 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 the Project from others in the exempt class and, therefore, there are no unusual circumstances.

The proposed actions under the subject recommendations to approve the business terms of a Second Amendment to the Development, Loan and Lease Agreement with BRIDGE Housing Corporation, and to appropriate additional City funding do not constitute new information or changed circumstances such that additional environmental review would be required at this time.

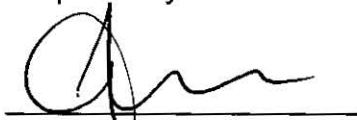
**FISCAL IMPACT:**

Approval of the recommended actions will increase the Housing Department's FY 2022 Operating Budget by an amount not to exceed \$2,000,000 (Account No. 23716003-816700-51036) by transferring \$2,000,000 from the Low and Moderate Income Housing Asset Fund unappropriated fund balance to the Heritage Square South Project. Approval of this action will leave an unappropriated balance of approximately \$660,000. The City funding for the Project will be in the form of a loan secured by a trust deed. The debt service on the City loan would be paid from the Project's annual residual receipts which are not guaranteed.


Respectfully submitted,

  
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Attachment A: Project Budget