



DATE: April 13, 2021

CATEGORY: Consent

DEPT.: Community Development

TITLE: **Lot 12 – Appropriation of Predevelopment Funding**

RECOMMENDATION

Staff recommends the City Council appropriate the following funds:

1. Appropriate \$1,000,000 in the Community Development Department Below-Market-Rate Housing Fund for predevelopment costs for the development of Lot 12, and authorize the City Manager to enter into an agreement with the selected joint developer team of Related and Alta Housing for the use of the predevelopment funds. (Five votes required)
2. Appropriate an additional \$300,000 in the Community Development Department, Below-Market-Rate Housing Fund for staff time, environmental, parking, and other special studies necessary to complete the entitlement review of this project. (Five votes required)

BACKGROUND

In 2019, the City initiated a two-step process for the redevelopment of the 1.4-acre Lot 12 site, currently a City-owned, 160-space public parking lot one block north of City Hall, into a residential mixed-use project. The first step began with a Request for Qualifications (RFQ), with a response period from May 15, 2019 to August 1, 2019, followed by a Request for Proposals (RFP) process, with a response period from December 16, 2019 to March 2, 2020.

The RFQ/RFP process concluded on May 19, 2020, when the City Council selected the joint developer team of Related and Alta Housing as the preferred developer (Developer). Note that the Developer submitted in the Developer's RFP an overall City subsidy request of approximately \$4.3 million. Of that total, approximately \$2.6 million would be for the affordable housing portion of the project, and \$1.7 million would be for the nonresidential portion of the project. Staff noted in the Council report that if Related and

Alta Housing were selected as the Developer, staff would need to better understand their project financing and the feasibility of the subsidy request, which was seen as relatively low.

Additionally, at that May 2020 meeting, Council identified remaining development priorities that needed further discussion, including whether the 160 public parking spaces should be replaced on-site or off-site within the downtown area, the potential use of County Measure A funds, and tenant selection preferences.

On October 13, 2020, Council held a Study Session to discuss these remaining priorities and provided direction that: (1) all 160 public parking spaces must be replaced off-site within the downtown area; and (2) Measure A funds for rapid rehousing units would be supported. Staff noted in the Council report that, due to COVID-19 impacts on the housing market, increasing development costs, and uncertainty in funding sources, the funding gap for the project was expected to be higher than what was estimated as part of the Developer's RFP application and that it was possible that the City would be asked to consider a higher subsidy amount to keep the project viable. It is staff's understanding that the issue of increasing subsidy gaps due to COVID-19 impacts, increasing construction costs, and funding uncertainty is a widespread problem impacting most, if not all, affordable housing projects in the region.

ANALYSIS

Since the October 2020 City Council meeting, the City team has worked with the Developer to execute an Exclusive Right to Negotiate Agreement (ERNA) and commenced the negotiation process for development of Lot 12. Additionally, staff has provided an informal project review regarding design, architecture, and other aspects based on information the Developer has provided to staff. The Developer has not yet submitted a formal planning application as will be required for the project. Submittal of a formal application (see Next Steps below) would officially start the project review and approval process with certain timelines that would need to be met. The ERNA has been executed, and negotiation of the proposed predevelopment loan agreement is nearly complete. The City and Developer continue to work on negotiating the Development and Disposition Agreement (DDA) along with the Ground Lease. The DDA negotiations will include the Developer's overall subsidy request, including for the affordable housing, nonresidential/retail, and parking subsidy.

As noted in the Background section of this report, the Developer's RFP submittal included a total subsidy request of \$4.3 million. The \$1.3 million in predevelopment funding that is the subject of this Council item is part of (i.e., not in addition to) the \$4.3 million total request. Eligible uses of the \$1 million in predevelopment funding by

the Developer include up-front work related to architectural, engineering, and other professional services necessary for securing the development entitlements, application fees for external funding sources, and permit fees/costs. The remaining \$300,000 of the predevelopment funding request would be used by the City to pay for Planning staff time along with consultant agreements necessary for the entitlement review.

Based on recent Developer cost estimates and as noted in the Background section, the overall subsidy request is likely to increase based on continued cost escalations, market fluctuations, and uncertainty regarding financing sources, such as tax credit pricing. Regardless of the ultimate City subsidy amount that will be determined through the DDA negotiation process, the \$1.3 million predevelopment loan amount will not change and will be included in the total subsidy amount.

Staff recommends approval of the predevelopment funding and authorization to complete negotiation and execution of the predevelopment loan agreement in order to continue to move the development process forward. Such predevelopment loans have been standard on recent affordable housing projects.

NEXT STEPS

If Council approves staff's recommendation, the predevelopment loan agreement will be finalized and executed as part of the next steps. Additionally, staff will continue to work with the Developer on the DDA, architecture/design, and overall project components. It is anticipated that a Closed Session will be held to discuss the DDA before the end of Fiscal Year 2021-22. This would be followed by a New Business item in fall 2022 for Council to approve the DDA and design and to authorize the developer to submit a formal planning entitlement application to begin the project approval process. The timing of these future Council meetings is dependent on the duration of the DDA negotiation. If the negotiations take longer than anticipated, then the timing of the Council meetings would need to be extended.

FISCAL IMPACT

There is no fiscal impact to the General Operating Fund for the predevelopment loan request. The City Council is being asked to appropriate \$1.3 million in Below-Market-Rate Housing Funds for predevelopment expenses for the eligible activities/costs noted above. The funding would be provided in the form of a predevelopment loan, and there would be no interest on this loan. It is anticipated that the predevelopment loan will be converted into a construction/predevelopment loan representing the total City subsidy amount, and interest will begin to accrue at the closing of the construction loan at 3 percent simple interest.

ALTERNATIVES

1. Choose not to appropriate predevelopment funding for this proposal.
2. Provide other direction.

PUBLIC NOTICING

The meeting agenda and Council report have been posted on the City's website and announced on Channel 26 cable television.

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