



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Leslye Krutko

**SUBJECT:** SEE BELOW

**DATE:** July 26, 2006

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7/28/06

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**COUNCIL DISTRICT:** 3  
**SNI AREA:** University

**SUBJECT: PUBLIC HEARING TO APPROVE A DISPOSITION AND DEVELOPMENT AGREEMENT FOR THE SALE AND CONVEYANCE OF CITY-OWNED PROPERTY, EXECUTION OF A NEW OPTION AGREEMENT, AND A FUNDING COMMITMENT TO A PROPOSED PARTNERSHIP BETWEEN FIRST COMMUNITY HOUSING AND JOHN STEWART COMPANY, OR ITS DESIGNATED AFFILIATE (SPONSOR), FOR THE DEVELOPMENT OF THE NEW CASA FELIZ, A 60-UNIT THREE- AND FOUR-STORY AFFORDABLE HOUSING PROJECT LOCATED AT 525 SOUTH NINTH STREET**

## RECOMMENDATIONS

After conducting a public hearing, it is recommended that the City Council adopt resolutions as follows:

1. Accepting the summary of costs and findings of the Summary 33433 Report pursuant to Health and Safety Code Section 33433 for the sale and disposition of the property located at 525 South Ninth Street under the terms and conditions of the proposed Disposition and Development Agreement ("DDA").
2. Approving a DDA between the City of San José and the proposed partnership between First Community Housing ("FCH") and the John Stewart Company ("JSCo") (collectively "Sponsor"), or their designated affiliate, for the development of the New Casa Feliz, a 60-unit three- and four-story affordable housing project and authorizing the City Manager or his designee to negotiate, execute and record all documents reasonably necessary to convey the property as provided in the DDA.

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3. Approving an Amendment to the Option Agreement for the subject property with Sponsor and authorizing the City Manager or his designee to negotiate and execute the amendment to the Option Agreement.
4. Approving a funding commitment of up to \$1,000,000 to the Sponsor for development costs of the project.

### **OUTCOME**

Approval of the recommended actions will result in the development of the New Casa Feliz, a project located at 525 South Ninth Street. The project will contain 60 studio units, 52 of which are to be restricted to Extremely Low-Income Households, seven units of which are to be restricted to Very Low-Income Households, and one of which will be a manager's unit available to a Lower Income Household. The Sponsor will also make available 21 of the units that are targeted to residents at or below 20% of Area Median Income ("AMI") for developmentally disabled persons.

### **EXECUTIVE SUMMARY**

The purpose of this memorandum is to seek (1) Acceptance of the 33433 report as required by California Health and Safety Code, (2) Approval of a Disposition and Development Agreement between the City of San José, First Community Housing, and The John Stewart Company to allow the City to transfer land and the existing Casa Feliz building at 525 South Ninth Street to FCH and JSCo and to construct a New Casa Feliz on the same site, (3) Approval to amend the Option Agreement for the property, and (4) Approval for a funding commitment for new construction/permanent loan to the project Sponsor, or its legal affiliate, in an amount not to exceed \$1 million to assist with rebuilding.

### **BACKGROUND**

The property, located at 525 South Ninth Street ("Casa Feliz"), was originally built in 1960 and served as a student boarding house. Housing for Independent People ("HIP") acquired the property in July 1989, changing the use to a special needs housing facility serving the mentally ill. Until September 2005, Casa Feliz operated as a 64-unit, SRO facility with shared bathrooms, social services space, a below-grade commercial kitchen and dining area, and 11 onsite parking spaces.

HIP acquired Casa Feliz with a first trust deed loan from the California Department of Housing and Community Development ("HCD") and a second trust deed loan from the City in the amount of \$590,000.

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Due to financial difficulties, HIP filed for bankruptcy in 1996. The bankruptcy court order allowed HIP to abandon Casa Feliz in 1997 and the City of San José became “creditor-in-possession” of the facility. As creditor-in-possession, the City acted as owner from 1997 to the present, allowing continued operation of the facility until September 2005. The City became the formal owner of record on September 8, 2004, after acquiring the property through a foreclosure sale on its Deed of Trust.

At that time, the City began to work with JSCo, the property management company, on a plan to redevelop the property. On February 15, 2005, the City Council approved an Option Agreement for the sale of Casa Feliz for to the proposed partnership of FCH and JSCo, or its designated affiliate, for the purpose of redeveloping the property (“New Casa Feliz”).

On March 1, 2005, the City entered into an Option Agreement with FCH and JSCo to sell Casa Feliz, subject to the HCD loan, and take back a promissory note for the difference between the purchase price and the HCD loan. The Option Agreement had an expiration date of February 15, 2006. On February 15, 2006, the Option Agreement was extended to August 15, 2006 to allow sufficient time to complete and close the construction financing for the project.

New Casa Feliz received its PD zoning approval on September 20, 2005 with a condition to the recommended project to increase the on-site parking requirement from 19 to 22 spaces.

On February 28, 2006, the City Council approved the transfer of five restricted units of Casa Feliz to the Hester Apartments project located at 1759 Hester Avenue in order to meet State Redevelopment Law requirements for transfer of existing affordability restrictions recorded in conjunction with the expenditure of 20% Housing Funds. Restrictions for one unit more than was needed were transferred, as the New Casa Feliz manager unit was originally anticipated to be unrestricted. Hester Apartments, an existing building that is exempt from Inclusionary requirements, has comparable affordability and size of units, and no 20% Funds will be used in that project; therefore, all State requirements regarding transfer of restricted units have been met.

### **Tenant Relocation**

On February 15, 2005, in conformance with State relocation law, the City Council accepted and approved implementation of the Relocation Plan for the then-current residents in an amount not to exceed \$1,020,000. There were 68 residents and former residents involved in the relocation, including 16 individuals 55 years of age or older.

During the relocation process, most of the residents elected to have their benefits paid out on a monthly basis through JSCo, the property manager, rather than receiving a lump-sum payment. All residents were successfully relocated by September 1, 2005 and the property was vacated, closed, and secured; many of the former residents continue to receive relocation payments.

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**ANALYSIS**

**33433 Analysis**

The attached Summary Report, pursuant to Section 33433 of the California Health and Safety Code, was prepared by Keyser Marston Associates, Inc. in July 2006. This report, along with a copy of the proposed DDA, will be made available for inspection as required by California Redevelopment Law on July 31, 2006. The Summary 33433 Report summarizes the key terms of the proposed DDA, the cost of the agreement to the City, the fair reuse value, and conformance with the City of San José's Redevelopment Agency Implementation Plan. Based on the analysis provided in the Summary Report, the consideration that the City will receive is not less than the fair market value at its highest and best use.

**Project Description**

The Sponsor (JSCo and FCH) is proposing to demolish the existing three-story facility and redevelop the site with a four-story building housing 59 studio rental units and one studio manager's unit. The project offers 22 below-grade parking spaces and 2 permitted parking spaces on the street, as well as 10 motorcycle spaces and 16 bicycle spaces. In addition, the Sponsor will provide each tenant with free yearly "Eco-Passes" to encourage the use of public transportation. It is anticipated that 21 (35%) of the units will be set aside for developmentally disabled persons with the remaining units available to the general public meeting the units' income restrictions. Of the total 59 rental units, 52 units will be available to households earning no more than 30% of Area Median Income (Extremely Low-Income) and 7 units will be available to households earning no more than 35% of AMI. The proposed unit mix, affordability levels and rents are as follows:

21 units @ 20% AMI	rent: \$347 per month
31 units @ 30% AMI	rent: \$533 per month
7 units @ 35% AMI	rent: \$533 per month
<u>1 unit @ 60% AMI</u>	<u>rent: \$750 per month (Manager's unit)</u>
60 units total	

The Sponsor, through The John Stewart Company ("JSCo"), will be responsible for the day-to-day property management of the facility and will contract with Housing Choices Coalition and other service providers to assist the developmentally disabled tenants.

**Summary of the Proposed Transaction:**

FCH and JSCo will form a partnership for the purpose of redeveloping 60 affordable housing units at Casa Feliz. To do so, they intend to request a bond allocation from the California Debt Limit Allocation Committee and request that the City of San José issue tax-exempt bonds for this project. They will apply also to the following sources for funding in order to demolish and rebuild Casa Feliz: the State's Multifamily Housing Program ("MHP"); the County of Santa

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Clara's Office of Affordable Housing; and, the Federal Home Loan Bank's Affordable Housing Program.

The existing property's sales price was determined according to the project's latest appraisal which valued the property at \$1.26 million. In return for conveying the property, the City will also convey to the Sponsor the existing California's Department of Housing and Community Development ("HCD") debt that the City assumed when it acquired the property in 2004. Assuming a closing date of June 1, 2007, the existing HCD debt and interest accrued is expected to be approximately \$1,156,354. The City will receive the difference between appraised value and HCD debt, approximately \$103,646, at the time of construction closing, and will place 55-year affordability restrictions on the property.

In addition, City staff is recommending that the City Council approve a loan commitment of up to \$1 million if the sponsor's application for funding from the County Office of Affordable Housing is unsuccessful or falls short of \$1 million. Assuming the project obtains a loan from MHP, which would be in second lien position ahead of a potential City loan, current MHP guidelines dictate that the City's share of net cash flow would be less than 50%, and may be as low as 11%.

These amended business terms, necessary in order to make the project financially feasible while minimizing additional outlay of the City's funds, will be reflected in the amended Option Agreement.

### **Anticipated Timeline**

Submitted funding application to State Multifamily Housing Program	May 10, 2006
Anticipated City Council approval of DDA and funding commitment	August 15, 2006
Submit funding application to County Office of Affordable Housing	Fall 2006
Submit funding application to Federal Home Loan Bank	October 2006
Apply to California Debt Limit Allocation Committee for bond allocation	January 2007
Hold TEFRA hearing	January 2007
Apply to State Tax Credit Allocation Committee for tax credits	April 2007
Convey land to developer	May 2007
Anticipated City Council approval to issue tax-exempt multifamily bonds	June 2007
Issue bonds, close construction loan and begin construction	June/July 2007
Complete construction	December 2008

### **Inclusionary Housing Policy**

The Project is in the University Strong Neighborhood Initiative area. The project is exempt from the Inclusionary Housing Requirement because the Disposition and Development Agreement

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requires 100% restricted units and exceeds the depth of affordability otherwise required in the redevelopment area.

## **POLICY ALTERNATIVES**

To arrive at this proposal, staff considered the following options:

***Alternative #1: Delay hearing for the DDA, amended Option Agreement, and City funding commitment until Sponsor has obtained other funding commitments.***

**Pros:** Allows additional time for refining the project's financial budget and pro forma prior to the City committing to the terms and conditions of the proposed DDA.

**Cons:** The existing Option Agreement expires on August 15, 2006 and a lapse in the Sponsor's site control would disqualify its application already submitted for State MHP funding and likely delay the project's construction start and increase construction costs.

**Reason for not recommending:** The City's control over the project and likelihood of prompt, on-budget project delivery is maximized by not delaying approval of the DDA and loan commitment at this time.

***Alternative #2: Approve the DDA and amended Option Agreement, but delay approval of the City funding commitment until need is defined.***

**Pros:** Allows additional time for refining the project's financial budget and pro forma prior to the City commitment. Allows continued site control for the Sponsor.

**Cons:** Delaying the loan commitment could necessitate amendment and re-posting of the DDA as it is now drafted. If the County's funding round is delayed or if the project is unsuccessful in seeking the full \$1 million needed and then must apply to the City Council for City funding, the project's construction start could be delayed, likely escalating construction costs. The project's funding gap is likely to increase rather than decrease over time, and delaying approval of this loan risks a higher City loan amount being requested.

**Reason for not recommending:** Delaying City approval of the loan commitment may result in delayed project timing, higher project costs, and will require another request to City Council later this Fall.

The recommended alternative is to approve the DDA, negotiation of an amended Option Agreement, and funding commitment of up to \$1 million at this time.

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Adopting the DDA allows the City to obtain a firm commitment on the part of the Sponsor to develop the new facility based on the stated terms and conditions, and transfer the property shortly before the start of construction. The Sponsor must complete the development based on the stated terms or be in default of the DDA and risk termination of the agreement and the loss of already expended predevelopment costs.

One risk that exists with this alternative is that staff may need to amend or re-notice and return to the City Council if the developer cannot live up to the terms of the DDA. This risk is inherent to execution of the DDA relatively early in the development process; however, delaying approval at this time would guarantee that the project would need to be reconsidered by the City Council and Redevelopment Agency Board.

Further, staff recommends that the City Council approve the request to enter into a new Option Agreement at this time to keep the Sponsor's pending MHP application in good standing and to avoid almost certain increases in costs from delays. Because MHP funds are limited, any delays could result in rejection of the Sponsor's application due to insufficient funds. This would result in a \$7 million gap in the budget.

In addition, the recommended alternative is to approve a City construction/permanent loan of up to \$1 million if the County's funding does not materialize by early 2007. Approving this loan commitment now—contingent upon the Sponsor actively seeking additional subordinate funding and subject to the City's usual underwriting guidelines and determination of need for subsidy—will prevent potential costly project delays given that the County has not yet determined timing for its Notice of Funding Availability for its Fall 2006 round.

In summary, approving all the actions at this time will maximize the City's degree of control over the project, minimize potential project delays and cost increases and maximize the likelihood of obtaining outside funding.

### **PUBLIC OUTREACH/INTEREST**

- √ **Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- **Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- **Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

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This item meets Criteria 1: Requires Council action on the use of public funds equal to \$1 million or greater. This Memorandum will be posted to the City's website for the August 15, 2006, Council Agenda.

Casa Feliz was acquired with Redevelopment Agency tax-increment funds dedicated to affordable housing. Pursuant to Section 33433 of the California Health & Safety Code, public noticing is required when an agency proposes disposition of property acquired by redevelopment agency tax increment funds. A Notice of Public Hearing will be published on July 31, 2006, for the City Council meeting to be held on August 15, 2006, which conforms to the legal noticing requirements. A Summary Report and the analysis of this DDA pursuant to Section 33433 were completed by Keyser Marston and Associates, Inc. The results of the analysis are on file with the City Clerk and have been incorporated into this report.

Representatives of FCH and JSCo presented information concerning the project to the University Neighborhoods Coalition Board and the South University Neighborhood Board on January 11, 2005. A general community meeting was held on July 19, 2005. A Planning Commission public hearing for PD zoning was held on August 24, 2005. A City Council public hearing for PD zoning approval was held on September 20, 2005.

### **COORDINATION**

This report has been coordinated with the Office of the City Attorney and the Department of Planning, Building and Code Enforcement.

### **FISCAL/POLICY ALIGNMENT**

This expenditure is consistent with the Housing Department's goal of targeting resources to Strong Neighborhood Initiative areas per the Strong Neighborhood Initiative Redevelopment Plan, adopted June 25, 2002.

### **COST SUMMARY/IMPLICATIONS**

#### **1. COST OF PROJECT:**

Currently, the construction budget for New Casa Feliz is as follows:

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<u>Construction Uses</u>	<u>Amount</u>
Land Acquisition	1,260,000
Demo / Site Work and Construction	11,130,000
Hard Cost Contingency	661,299
Soft Costs	2,076,770
Soft Cost Contingency	100,000
Developer Fee	885,000
Capitalized Operating Reserve	73,850
<b>Total Project Uses</b>	<b>\$16,186,919</b>

2. **COST ELEMENTS OF CITY LOAN AMOUNT, IF NEEDED:**

<u>Uses</u>	<u>Amount</u>
Land acquisition	103,646
Architecture & Engineering Design	525,000
Permit fees	48,079
<u>Bond issuance costs</u>	<u>323,275</u>
<b>TOTAL</b>	<b>\$1,000,000</b>

In addition, the City has incurred costs since acquiring the property through foreclosure on September 8, 2004. The anticipated cost of relocation is \$1,020,000, of which \$601,941 has been expended as of July 13, 2006. The ongoing property management expenses incurred during the period of ownership by the City were \$193,534 as of July 13, 2006. Funds expended for relocation and property management are being considered a grant to the project.

3. **SOURCE OF FUNDING:** Fund 443—Low- and Moderate-Income Housing Fund

4. **FISCAL IMPACT:** No ongoing fiscal impact for new loan. On-going relocation expenses were fully budgeted in Fund 443 in FY 06-07.

CEQA

CEQA: Exempt, File No. PDC05-020.

  
 LESLYE KRUTKO  
 Director of Housing

For questions, please contact Mike Meyer, Assistant Director of Housing at 408-535-3855.

Attachment



**SUMMARY REPORT PURSUANT TO  
SECTION 33433  
OF THE  
CALIFORNIA COMMUNITY REDEVELOPMENT LAW  
ON  
THE DISPOSITION AND DEVELOPMENT AGREEMENT BY AND BETWEEN  
THE CITY OF SAN JOSE  
AND  
CASA FELIZ, LP**

**I. INTRODUCTION**

The California Health and Safety Code, Section 33433, requires that if a redevelopment agency wishes to sell or lease property to which it holds title and if that property was acquired in whole or in part with property tax increment funds, the agency must first secure approval of the proposed sale or lease agreement from its local legislative body after a public hearing. A copy of the proposed sale or lease agreement and a summary report that describes and contains specific financing elements of the proposed transaction shall be available for public inspection prior to the public hearing. As contained in the Code, the following information shall be included in the summary report:

1. The cost of the agreement to the redevelopment agency, including land acquisition costs, the costs of any improvements to be provided by the agency, plus the expected interest on any loans or bonds to finance the agreement;
2. The estimated value of the interest to be conveyed or leased, determined at the highest and best use permitted under the redevelopment plan;
3. The estimated value of the interest to be conveyed in accordance with the uses, covenants, and development costs required under the proposed agreement with the Agency, i.e., the reuse value of the site;
4. An explanation of why the sale or lease of the property will assist in the elimination of blight, as required by Section 33433; and
5. The purchase price or sum of the lease payments which the lessor will be required to make during the term of the lease. If the sale price or total rental amount is less than the fair market value of the interest to be conveyed or leased, determined at the highest and best use consistent with the redevelopment plan, then the agency shall provide as part of the summary an explanation of the reasons for the difference.

This report outlines the salient parts of the Disposition and Development Agreement (“DDA”) to be entered into by and between the City of San Jose (“City”) and Casa Feliz, LP, a partnership of First Community Housing and the John Stewart Company (“Developer”).

Under this Agreement, the Developer or its affiliate will purchase the subject property from the City, demolish the existing improvements and build a new 60-unit studio apartment complex. The purpose of this analysis is to determine the net cost of the Agreement to the City.

This report is based upon information in the proposed Agreement and is organized into the following five sections:

1. **Summary of the Proposed Agreement** - This section includes a description of the site, the proposed development and the major responsibilities of the City and the Developer.
2. **Cost of the Agreement to the City of San Jose** - This section outlines the cost of the Agreement to the City for costs that have been funded with Redevelopment Agency tax increment funds. It presents the terms of the land conveyance and the loan to the Developer by the City, and sets forth the net cost of the Agreement of the City.
3. **Estimated Value of the Interest to be Conveyed** - This section summarizes the value of the property to be sold to the Developer.
4. **Consideration Received and Reasons Therefor** - This section describes the value of the land payments to be paid by the Developer to the City. It also contains a comparison of the purchase price and the fair market value at the highest and best use consistent with the redevelopment plan for the interests conveyed.
5. **Provision of Low or Moderate Income Housing**- This section demonstrates how the sale of the property will provide housing for low- or moderate-income persons.
6. **Conformance with Five-Year Implementation Plan** - This section describes how the Agreement is in conformance with the Agency's Five-Year Implementation Plan.

## **II. SUMMARY OF THE PROPOSED AGREEMENT**

### **A. *Description of the Site and the Proposed Development***

#### **Property**

The subject Property is located on an approximately 0.34-acre site at 525 South Ninth Street in San Jose. The Property is improved with a 64-room, 3-story residential building, which was originally constructed in 1960 as a student boarding house, with shared bathrooms and a below-grade commercial kitchen and dining area. It has several major capital repair needs and is functionally obsolete.

The Property was acquired by Housing for Independent People (HIP) in 1989 using a \$768,000 loan from the California Department of Housing and Community Development (HCD) and a \$590,000 loan from the City of San Jose. HIP changed the use from student housing to a special needs housing facility serving the mentally ill. In exchange for its loan, the City required a 30-year affordability covenant, restricting all units to very low-income households.

Due to financial difficulties, HIP filed for bankruptcy in 1996 and the City became creditor-in-possession of the facility in 1997. The City eventually became the formal owner of record through a foreclosure sale in 2004 and subsequently relocated all the remaining tenants of the building in preparation for the new development.

The Developer proposes to acquire the Property from the City of San Jose, demolish the existing building, and construct a new 60-unit apartment building in its place.

#### **Developer**

The Developer is a partnership of First Community Housing and the John Stewart Company.

#### **Project Description**

Under the DDA, the Developer or its affiliate will purchase the Property from the Agency, demolish the existing building, and construct a new 60-unit studio apartment complex. The housing units will be deed restricted for 55 years. The rents for the affordable units will be based on the area median income for Santa Clara County (adjusted for household size), as follows: 21 units based on 20% of area median income (AMI), 31 units based on 30% of AMI, 7 units based on 35% AMI, and one resident manager's unit based on 60% of AMI. All units except the manager's unit will be studios and all units will contain a kitchen and bathroom. The units will range in size from 254 to 283 square feet. The Project will include 22 partially below-grade parking spaces as well as 10 motorcycle spaces and 16 bicycle spaces.

**B. City Responsibilities**

The City's responsibilities are as follows:

- The City will sell the Property to the Developer for a sum of \$1,260,000, which is the appraised value of the Property. The \$1,260,000 sale price is comprised of the assumption of the HCD loan, the current balance of which is estimated at \$1,156,000<sup>1</sup>, and \$104,000 in cash.
- The City will provide a loan to the Developer of up to \$1,000,000, should funds from Santa Clara County not materialize.

**C. Developer Responsibilities**

The Developer is responsible for developing the Project in accordance with the terms of the DDA as follows:

- Obtain approval of design development and construction drawings and related documents consistent with the Scope of Development by the City of San Jose;
- No later than the date shown in the Schedule of Performance, submit to the City a construction budget and evidence of financing and other project commitments sufficient to finance the Project;
- Purchase the Property from the Agency for the amount of \$1,260,000 including the assumption of existing HCD debt;
- Commence and complete construction in the manner and within the times specified in the DDA;
- Rent or make available for rent, 21 units at 20% of area median income (AMI), 31 units at 30% AMI, 7 units at 35% AMI, and one resident manager's unit at 60% AMI as required by the DDA and any and all applicable state and local laws and regulations.
- Agree to record affordability restrictions on 100% of the units, which will remain in effect for 55 years.
- While not a requirement of the DDA, if the development is successful in securing MHP funds for Supportive Housing, then the project will be required to include units for developmentally disabled persons.

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<sup>1</sup> The original \$768,000 HCD loan accrues interest at 3% simple interest per year (\$23,000/year).

**III. COST OF THE AGREEMENT TO THE AGENCY**

This section presents the total potential cost of the DDA to the City. The "net cost" of the Project after consideration of the project revenues that will accrue to the City is also evaluated. The net cost can be either an actual cost, when expenditures exceed receipts, or a net gain, when revenues created by implementation of the DDA exceed expenditures.

**A. Estimated Cost to the City**

The costs to the City resulting from this transaction relate to funding include the following:

- The City acquired the Property through a foreclosure sale in 2004 for approximately \$600,000 in cash as well as the assumption of the debt owed to HCD. The current balance of the HCD loan is approximately \$1,156,000. Therefore, the total cost of the acquisition to the City, including assumption of debt, is approximately \$1,756,000.
- To date the City has expended \$601,941 to relocate the previous tenants of the building in order to prepare the property for new construction. Total relocation expenses are estimated at \$1,020,000.
- The City will provide a loan to the Developer in the maximum amount of \$1,000,000 should funds from Santa Clara County not materialize.
- The City does not anticipate that it will use any debt to fund the obligations under the DDA. Therefore, the City is not anticipated to incur an interest cost related to the transaction.

As shown below, the total cost to the City will range from \$2.78 million to \$3.78 million depending on the City's loan to the developer.

	Assuming City Provides \$1,000,000 Loan		Assuming City Does Not Provide \$1,000,000 Loan	
	Total Nominal Costs	Total Net Present Value of Costs (discounted at 6%)	Total Nominal Costs	Total Net Present Value of Costs (discounted at 6%)
Acquisition Cost	\$1,756,000	\$1,756,000	\$1,756,000	\$1,756,000
Relocation Cost	\$1,020,000	\$1,020,000	\$1,020,000	\$1,020,000
City Loan to Developer	\$1,000,000	\$1,000,000	\$0	\$0
<b>Total City Cost</b>	<b>\$3,776,000</b>	<b>\$3,776,000</b>	<b>\$2,776,000</b>	<b>\$2,776,000</b>

**B. Revenues to the City**

The Developer will purchase the Property from the City for its appraised value, \$1,260,000. This purchase price includes assumption of the existing HCD debt.

Should it be needed, the City's maximum \$1,000,000 loan will be for a term of 55 years and will accrue simple interest at 3% per year during the construction phase and 4% per year during operations. However, due to the Project's thin operating margins, it is not projected that the City will receive any repayment of this loan during the 55-year loan term. The loan balance at the end of the 55-year loan term, including accrued interest, is \$3.23 million. The net present value of this future payment is approximately \$120,000.

As shown below, the City's revenues from the transaction are anticipated to range from \$1.26 million to \$4.49 million in nominal terms or \$1.26 million to \$1.38 million in net present value terms.

	Assuming City Provides \$1,000,000 Loan		Assuming City Does Not Provide \$1,000,000 Loan	
	Total Nominal Revenues	Total Net Present Value of Revenues (discounted at 6%)	Total Nominal Revenues	Total Net Present Value of Revenues (discounted at 6%)
Sale of Property	\$1,260,000	\$1,260,000	\$1,260,000	\$1,260,000
City Loan Repayment	\$3,230,000	\$120,000	\$0	\$0
Total Revenues	\$4,490,000	\$1,380,000	\$1,260,000	\$1,260,000

**C. Net Cost to the City**

The net cost to the City resulting from this transaction is the difference between the City's costs and the City revenues. In nominal dollars, the transaction is actually anticipated to generate a net positive value stream to the Agency totaling \$714,000 if the City provides a \$1,000,000 loan. This positive value reflects the non-discounted future value of the repayment of the City's maximum \$1,000,000 loan in Year 55. In net present value terms, the net cost to the City is \$2,396,000 with the \$1,000,000 City loan or \$1,516,000 without the \$1,000,000 City loan.

	Assuming City Provides \$1,000,000 Loan		Assuming City Does Not Provide \$1,000,000 Loan	
	Total Nominal	Total Net Present Value (discounted at 6%)	Total Nominal	Total Net Present Value (discounted at 6%)
City Costs	\$3,776,000	\$3,776,000	\$2,776,000	\$2,776,000
(Less) City Revenues	(\$4,490,000)	(\$1,380,000)	(\$1,260,000)	(\$1,260,000)
Total Net City Cost/(Revenue)	(\$714,000)	\$2,396,000	\$1,516,000	\$1,516,000

#### IV. VALUE OF THE INTEREST TO BE CONVEYED

##### *Reuse Value*

The reuse value of the site is directly a function of the development economics specific to the proposed Project. The units in the Project will be restricted to extremely low-income households. The income restrictions are critical to the Property's reuse value.

Given the income restrictions, it is estimated that the Project's average rent will be \$470 per month. Based on operating cash flow projections, it is projected that the rental stream will be sufficient to cover operating expenses for 25 to 30 years. However, after that time it is projected that operating expense could exceed revenues. Because of the project's deep affordability levels and marginal cash flow, the Project does not generate sufficient cash flow to support debt service payments beyond the minimum payments required under the MHP loan. The Developer's financing plan is therefore relying entirely upon a mix of subsidies and below market loans as shown below:

<b>Permanent Sources of Funds</b>	<b>Financing Plan</b>
Low Income Housing Tax Credits	\$6,531,000
MHP Loan	\$7,000,000
AHP Loan	\$472,000
Santa Clara County	\$1,000,000
CA HCD (existing debt)	\$1,156,000
Total Sources	\$16,159,000

Given the Project's rental restrictions, operating expenses, and the availability of subsidy sources specified above, it is KMA's opinion that the fair reuse value of the site is \$1,260,000, which is consistent with the agreed upon purchase price and the appraised value. However, without the availability of the subsidy sources specified above the fair reuse value of the site would be nominal.

##### *Estimated Value at Highest and Best Use*

The Property was appraised by the Fillmore Group in September 2005. The appraisal determined that the highest and best use for the Property was development of a residential project which satisfies the deed restriction requiring "SRO units available to low income residents fulfilled with tax credits and/or below market financing". As of September 2005, the fair market value of the property was \$1,260,000.

## **V. CONSIDERATION RECEIVED AND REASONS THEREFOR**

Under the terms of the DDA, the Developer will purchase the Property from the City for approximately \$104,000 in cash and the assumption of approximately \$1,156,000 in existing HCD debt, for a total of \$1,260,000. This amount is equal to the Property's appraised value. The Developer's ability to pay the \$1.26 million purchase price is entirely driven by the availability of \$16.1 million of financial subsidies from various federal, state, and local agencies. Without these subsidies, the property's fair reuse value and the developer's ability to purchase the site would be nominal. Should \$1,000,000 of funding from Santa Clara County not materialize, the City has committed to providing a loan to the Developer in the maximum amount of \$1,000,000. It is anticipated that the City's loan will be repaid only upon the expiration of the affordability covenants at the end of the 55-year loan term.

The income restrictions that will be placed on the property greatly reduce the market value of the Project. Under the terms of the DDA, 59 of the Project's units will be restricted to households earning 20% to 35% of AMI for a period of 55 years. The resident manager's unit will be restricted at 60% AMI.

## **VI. PROVISION OF LOW OR MODERATE INCOME HOUSING**

The Project will provide 59 housing units restricted to households earning 20% to 35% of AMI for a 55-year period. There will be one resident manager's unit, which will be restricted at 60% AMI.

## **VII. CONFORMANCE WITH FIVE-YEAR IMPLEMENTATION PLAN**

The subject Project is consistent with the City of San Jose Redevelopment Agency's Implementation Plan because it helps achieve the goal of the Redevelopment Project Area to eliminate the conditions of blight existing in the Project Area and to prevent the recurrence of blighting conditions in the Project Area. This Project also meets the goal of increasing the number of affordable housing units and closing the affordable housing gap by increasing the number of affordable units.

In its Regional Housing Needs Determination, the Association of Bay Area Governments (ABAG) has made a determination of the number of housing units needed at each affordability level in the City of San Jose. According to ABAG, approximately 20% of the City's projected housing need is for very low-income units (50% and less of AMI) and approximately 9% of the City's projected housing need is for low-income units (60% AMI). The subject Project will restrict 59 of its units to households earning 20%-35% of AMI and one unit at 60% AMI. Therefore, the Project's distribution of affordability exceeds ABAG's affordable housing needs for the City of San Jose.