

# Memorandum

**TO:** HONORABLE MAYOR  
AND CITY COUNCIL

**FROM:** Kim Welsh

**SUBJECT: SALE OF CITY-OWNED PROPERTY AT 500 SOUTH FIRST STREET**      **DATE:** November 13, 2012

Approved



Date

11/16/12

## RECOMMENDATION

Adopt a resolution:

- (a) Declaring the property located at 500 South First Street, comprised of a 33,284 square foot building on an approximately 19,023 square foot parcel, surplus to the needs of the City;
- (b) Approving an agreement between the City and Movimiento de Arte y Cultura Latino Americano (MACLA) for the sale of the property in the amount of \$1,400,000, \$650,000 to be paid in cash over a three-year period and \$750,000 to be paid in in-kind services over 20-year period; and
- (c) Authorizing the City Manager or her designee to execute the sale agreement, the deed, and all other documents necessary to complete the transaction.

## OUTCOME

Movimiento de Arte y Cultura Latino Americano (MACLA) was founded in 1989 and has been a tenant at the property for 20 years. MACLA is an anchor institution in the City's South of First Area (SoFA) District. The purchase of the 500 South First Street property will accomplish multiple City goals including securing General Fund revenues, eliminating maintenance costs and strengthening Downtown San José as the creative and cultural center of Silicon Valley. MACLA intends to improve the facility, enhance the organization's program offerings, and facilitate private and foundation support for creative entrepreneurs. The purchase of the property will strengthen MACLA's ability to generate private and foundation funds.

## BACKGROUND

### About MACLA

MACLA is a contemporary arts organization that was founded in 1989 by a group of community leaders committed to supporting multicultural arts and artists. Programs offered by MACLA

include visual arts, performing arts, as well as literary arts programs. Its contemporary arts programs are grounded in Chicano/Latino experience and aimed to engage people across cultures in civic dialogue and community transformation. The connecting of Latino and non-Latino audiences has been a distinctive feature of MACLA since its inception. A large portion of its programs are geared towards creating opportunities for interaction between cultures, experiences, audiences, new art forms, and emerging artists. MACLA works extensively with at-risk youth, providing art training opportunities, such as its notable Peapod Academy, which is a partnership between the Black Eyed Peas Foundation and Adobe Youth Voice. Annually, MACLA reaches approximately 30,000 San José residents.

As an outgrowth of its arts and cultural objectives, MACLA has collaborated closely with the community in the William-Reed Corridor, University, and Market-Almaden neighborhoods and beyond. This collaboration has resulted in a broad range of additional community development work.

#### 500 South First Street

In 1998, the San José Redevelopment Agency (RDA) purchased the property at 500 South First Street from the Center for Employment Training (CET). Through this purchase a pre-existing lease with MACLA was conveyed to the RDA. The property consists of an approximately 38,300 square foot building on an approximately 19,000 square foot parcel. The building requires replacement of the roof and significant upgrade to building systems including electrical, mechanical, and plumbing systems. The second floor of the building can only be used for limited storage purposes; therefore the effective lease capacity of the building is restricted to the ground level.

In June 2011, the property was conveyed from the RDA to the City of San José. MACLA has remained a tenant of the building and pays an annual rent of \$1 under the City's below market rental policy. The Redevelopment Agency transferred the property to the City of San José in June of 2011. For several years, MACLA's Board had been discussing purchase of the building in order to invest in the facility and provide stability for MACLA's future. MACLA has been in many conversations with local and national foundations, and with City staff, in an effort to craft a possible purchase of the property. Section 4.20.080 of the City's Municipal Code allows the City to sell surplus property at a private negotiated sale to any non-profit corporation engaged in programs or projects that provide a direct benefit to the residents of the City of San José.

Beginning in 2007, due to the ongoing budget shortfall, the City Council directed staff to actively pursue the sale of surplus properties in order to generate revenues for the City. The direction for this strategy can be found in the 2007-2008 Mayor's March Budget Message and was incorporated into the General Fund Structural Deficit Elimination Plan that was released in November 2008. It was the City Council's direction to generate revenue to support City services as well as minimize the City's maintenance and liability costs through the sale of surplus City property.

## ANALYSIS

An As-Is appraisal of the property was completed by Carneghi-Blum & Partners, Inc. (Carneghi) in March 2012. The appraisal identified the As-Is fee simple Fair Market Value for the property as \$1,400,000. Carneghi arrived at the value of \$1,400,000 using both a sales comparison approach of fee simple land if the building was demolished and the property was eventually developed for housing and an income approach based on market rate rents. Only the first floor of the building was included in determining value for the income approach since the second floor can only be used for limited storage without significant improvement.

Staff has determined that there are no other municipal purposes now or in the foreseeable future for which the property could be used and therefore there is no reason for the City to own and maintain the property. On October 29, 2012, in accordance with California Government Code Section 54222(d), staff prepared and distributed a notification to those local agencies of the availability of the 500 South First Street property for the following uses: development of housing for persons and families of low or moderate income; park, recreation, and open space; public school and/or enterprise zone purposes. Staff did not receive any offers in response to the notification letters.

Section 4.20.080 of the City's Municipal Code allows the City to sell surplus property to any non-profit corporation engaged in programs or projects which provide a direct benefit to the residents of the City of San José. MACLA has become a highly respected cultural organization providing innovative programming for residents of San José and Silicon Valley. MACLA contributes greatly to the fabric of the SoFA District, the adjacent William-Reed Corridor, and to the broader San José and Silicon Valley arts community.

MACLA is a financially sound non-profit 501c3 organization. According to MACLA'S most recently audited financial statements, its 2010-2011 Operating Budget was \$544,528. MACLA'S revenue streams are diversified between grants, donations, and earned income. The organization has generated an operating surplus over the past five years. MACLA has built a strong reputation among public and private funders for both its artistic programming and operational effectiveness and successfully leverages outside grant funding from national foundations such as the Ford Foundation, Packard Foundation, and Knight Foundation, among others.

### MACLA'S Proposed Expansion

Building on MACLA'S commitment to artists, community members, and the growing vitality of Downtown San José, the project embodies the principles of creative placemaking. Through this property acquisition and renovation - led by artist/architect Teddy Cruz - MACLA aspires to provide local multicultural artists of color with a permanent place to create and showcase their art, enhance the experience of audience members and program participants, and bolster SoFA'S burgeoning reputation as an arts destination.

MACLA's vision for the property includes an expanded and updated ground floor space for exhibitions, a more efficient and aesthetically designed black box theater, administrative offices, classrooms, and commercial space such as a café, restaurant, or retail business related to the arts. The proposal also includes a reconfigured second floor consisting of a "Creative Entrepreneur Incubator" where multidisciplinary artists and arts-based businesses can create their work in a vibrant space.

MACLA is currently conducting a market feasibility study to determine the needs of small businesses, as well as developing a mixed-used model that will generate earned income and a financially stable operations model. Through its expansion, MACLA aims to serve the space and small business needs of the local creative sector, with a focus on creative entrepreneurs of color. Anticipated outcomes include an increase in small business activity and cultural vibrancy in the SoFA District.

#### Proposed Sale Achieves Multiple City Goals

The sale of the 500 South First Street property to MACLA achieves multiple City goals. The General Fund Structural Deficit Elimination Plan approved by the City Council in 2008 directed staff to sell surplus City property to generate revenue that could be used to pay for City services and eliminate costs for maintenance and liability. The City's Economic Strategy calls for the development of a distinctive set of sports, arts, and entertainment offerings aligned with the City's diverse, growing population; continuing to position Downtown as Silicon Valley's city center; nurturing the successes of local small businesses; and creating more walkable, vibrant, mixed-use environments to spur interaction and attract talent.

The sale of the surplus property to MACLA to expand its artist and creative entrepreneur services supports the vision and goals outlined in *Cultural Connection: San José's Cultural Plan for 2011-2020*, adopted by the City Council on February 1, 2011. The plan's strategic goals include: support the availability of diverse cultural spaces and places throughout the community; strengthen downtown San José as the creative cultural center of Silicon Valley; and enhance support for creative entrepreneurs and the commercial creative sector. MACLA's proposed project specifically addresses these goals by providing needed space for creative entrepreneurs and artists of multiple disciplines who are sole proprietors or small business owners. The needs of San José's artists and arts-based businesses can be well served by MACLA who has served this community, specifically Latino Artists for decades. Furthermore, Latino artists represent a growing segment of our creative economy. MACLA's project will enable access to resources specific to their needs, supporting cultural equity, and economic prosperity.

The City's partnership with MACLA will demonstrate to national and private foundations the City's continuing commitment to creatively assisting diverse cultural arts and creative placemaking. In turn, MACLA will be better positioned to leverage the City's investment for the external grants and donations needed to build-out MACLA's vision for the property.

### Summary of Purchase and Sale Terms

The terms of the proposed sale are based on the \$1,400,000 fair market value established for the property in the March 2012 Carneghi appraisal. At closing, MACLA will provide a promissory Note to the City and the Note will be secured by a deed of trust on the property. MACLA will pay \$650,000 in cash payments as outlined in paragraph three of the "Summary of Terms" below. MACLA's obligation to pay the remaining \$750,000 will be offset through the provision of in-kind services over a twenty year Note period. For each year in the 20 year period, MACLA will receive \$37,500 in credit toward paying off this \$750,000 obligation under the Promissory Note, provided it has met its obligations to provide in-kind non-profit services at the site. Through this agreement San José will secure the services to the community of an anchor arts and cultural institution in SOFA for 20 years.

Such services will be delivered pursuant to a minimum annual operating budget of \$400,000 and must include substantial on-site cultural production amenities. The initial services categories will include visual arts, literary arts, and youth services. MACLA's programming will be reviewed annually by the Office of Cultural Affairs through reports obtained through its annual operating grant program. Beyond the broad parameters described above, the areas, categories, and minimum levels of in-kind services to be delivered shall be subject to annual approval of the City Manager or their designee.

The terms of the sale do not allow pre-payment of the \$750,000 amount to be paid by MACLA in the form of services. Further, if for whatever reason during the 20 year repayment term MACLA does not continue operation at the South First Street location, MACLA may only assign their in-kind repayment obligation to another non-profit to be approved by the City. If MACLA defaults on its repayment obligations, either the cash or in-kind services portions, the property can be sold under the City's Deed of Trust. If the property were purchased at foreclosure, the remaining value owed to the City will be paid in cash from available sale proceeds. In this way, the City secures both a permanent home for MACLA and 20 years of cultural arts programming in the SoFA District.

Currently the State Controller is conducting a review of properties transferred to the City from the RDA for the purposes of possibly ordering the return of certain properties to the RDA's successor agency. The return of the 500 South First Street property has not been noted as of interest to the state in the Controller's draft report. Closure of this issue to the satisfaction of both the City and MACLA will be a condition to closing the sale; it is expected this will occur when the State Controller issues its final report which is anticipated before the end of the year.

#### A Summary of Terms:

1. Price: \$1,400,000;
2. "As-Is" purchase, with 30-day period during which MACLA shall satisfy itself as to property condition; no obligations from the City to the purchaser concerning condition of the property;

3. Cash Payments in three installments totaling \$650,000 as follows:
  - a. \$20,000 deposit payable at closing,
  - b. \$315,000 payment due 12 months after closing, and
  - c. \$315,000 payment due 36 months after closing.
4. Remaining In-Kind Payments over a 20 year period totaling \$750,000.
  - a. Promissory Note in the amount of \$750,000 for 20 years; each year MACLA provides specified services \$37,500 is credited against the portion of remaining \$750,000 due under the Promissory Note.
  - b. A Deed of Trust secures the Promissory Note. MACLA cannot pre-pay this portion of the Promissory Note and the City secures 20 years of service from an anchor institution in SoFA. MACLA can only assign its in-kind repayment obligation to another non-profit and the selected non-profit must be approved by the City.
  - c. If MACLA defaults, the City remedy would be to foreclose under its Deed of Trust; sale proceeds would be paid to the City up to the amount of the outstanding amount on the Promissory Note at the time of the sale.

### **EVALUATION AND FOLLOW-UP**

The terms of the proposed sale of the 500 South First property call for annual review of MACLA's budget. The annual review will provide the City with an audited account of MACLA's budget and a review of the programs and services delivered by the organization. The terms of the proposed agreement allow, if necessary or desired by MACLA, assignment to another non-profit if to be approved by the City.

### **POLICY ALTERNATIVES**

#### ***Alternative #1 City retain ownership of the building and potentially sell in the future***

**Pros:** If the City were to retain ownership of the building, it could in the future potentially sell the property for residential purposes, which may generate additional revenue.

**Cons:** The City would not accomplish the goals set out in *Cultural Connection: San José's Cultural Plan for 2011-2020*, adopted by City Council on February 1, 2011.

**Reason for not recommending:** The SoFA district has become the City's arts and cultural center Downtown. Should the property be sold for residential purposes, it is unclear if this would continue to be the case. The property is unlikely to be attractive for residential purposes in the short term as the site is small for residential development.

### **PUBLIC OUTREACH/INTEREST**

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criterion 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)**
- Criterion 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)**

This item meets Criteria 1; the memorandum will be posted on the City's website for the November 27, 2012 City Council meeting.

### **COORDINATION**

This memo has been coordinated with the City Attorney's Office and the City Manager's Budget Office.

### **FISCAL/POLICY ALIGNMENT**

The City's Economic Strategy calls for the development of a distinctive set of sports, arts, and entertainment offerings aligned with the City's diverse, growing population; continuing to position Downtown as Silicon Valley's city center; nurture the successes of local small businesses; and create more walkable, vibrant, mixed used environments to spur interaction and attract talent.

The sale of the surplus property to MACLA to expand its artist and creative entrepreneur services supports the vision and goals outlined in *Cultural Connection: San José's Cultural Plan for 2011-2020*, adopted by City Council on February 1, 2011.

### **COST SUMMARY/IMPLICATIONS**

Under the proposed sale agreement, the City would receive cash payments of \$650,000 over a three-year period that would be recognized in the General Fund. The first installment of \$20,000 is anticipated to be received in 2012-2013. The sale proceeds would be used to help meet the revenue estimate from the sale of surplus property that is incorporated into the annual operating budget.

HONORABLE MAYOR AND CITY COUNCIL

November 13, 2012

**Subject: Sale of 500 South First Street**

Page 8

**CEQA**

File No. PP12-099, Exemption

/s/

**KIM WALESH**

Director of Economic Development

Chief Strategist

For questions please contact Nanci Klein, Deputy Director, at (408) 535-8184.