

**CITY AND COUNTY OF SAN FRANCISCO**  
**BOARD OF SUPERVISORS**  
**BUDGET AND LEGISLATIVE ANALYST**

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**TO:** Budget and Finance Sub-Committee

**FROM:** Budget and Legislative Analyst



**SUBJECT:** May 18, 2017 Budget and Finance Sub-Committee Meeting

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| <b>Item 1</b><br><b>File 17-0470</b>   | <b>Department:</b><br>San Francisco Public Utilities Commission (SFPUC) |
| <b>EXECUTIVE SUMMARY</b>   |   |
| <p><b>Legislative Objectives</b></p> <ul style="list-style-type: none"> <li>• Resolution authorizing an increase of Wastewater Enterprise Commercial Paper from a principal amount not-to-exceed \$500,000,000 to a not-to-exceed \$750,000,000, to be issued from time to time by the San Francisco Public Utilities Commission (SFPUC) to finance on an interim basis various capital projects benefiting the Wastewater Enterprise pursuant to amendments to the City’s Charter enacted by voters on November 5, 2002 as Proposition E and ratifying previous actions taken in connection therewith.</li> </ul> <p><b>Key Points</b></p> <ul style="list-style-type: none"> <li>• The SFPUC Wastewater Enterprise operates a combined storm water and sewer system.</li> <li>• The SFPUC Sewer System Improvement Program (SSIP) began in 2004 and is estimated to cost \$6.976 billion over approximately 20 years. To date, the Board of Supervisors has appropriated \$1.2 billion for SSIP capital improvement projects.</li> <li>• In October 2006, the Board of Supervisors authorized the SFPUC to issue Wastewater Enterprise Commercial Paper for a not to exceed \$150,000,000. In 2012 and 2014, the Board of Supervisors approved two subsequent resolutions to increase this authorization to the current \$500,000,000 authorization for commercial paper.</li> </ul> <p><b>Fiscal Impact</b></p> <ul style="list-style-type: none"> <li>• The SFPUC is requesting the increased authorization of \$250,000,000, from \$500,000,000 to \$750,000,000 to provide immediate funding for projects in FY 2016-17 and FY 2017-18 and for future fiscal year funding of projects. To date, the SFPUC has expended, encumbered and allocated \$492 million against the existing \$500 million authorization for Wastewater Enterprise Commercial Paper, leaving a remaining authorized balance of approximately \$8 million.</li> <li>• Commercial paper interest rates and fees at approximately 1%-1.4% annually are significantly lower than long-term revenue bond interest rates and fees, which are currently approximately 4% annually. Increasing the SFPUC commercial paper program will provide flexibility for the SFPUC to more efficiently finance its capital projects, by reducing the period of paying capitalized interest and allowing the SFPUC to issue bonds at a later date and less often, thereby lowering the SFPUC’s debt and debt service costs. Reducing SFPUC debt service costs should result in lower cost increases to Wastewater rate payers.</li> <li>• SFPUC estimates the additional \$250 million commercial paper authorization would result in approximately \$8.7 million of savings over the next two years.</li> </ul> <p><b>Recommendation</b></p> <ul style="list-style-type: none"> <li>• Approve the proposed resolution.</li> </ul> |   |

## MANDATE STATEMENT

City Charter Section 8B.124 states that the San Francisco Public Utilities Commission (SFPUC) may issue revenue bonds, including notes, commercial paper or other forms of indebtedness in order to reconstruct, replace, expand, repair or improve SFPUC water facilities or clean water facilities and that such debt issuances are subject to two-thirds approval by ordinance by the Board of Supervisors.

The Board of Supervisors authority under Charter Section 8B.124 is subject to receipt of a certification from (1) an independent engineer that (i) the projects to be financed by such debt meet utility standards and (ii) estimated net revenue will be sufficient to meet operating, maintenance, debt service coverage and other indenture or resolution requirements and (2) the San Francisco Planning Department that facilities financed with such debt will comply with applicable requirements of the California Environmental Quality Act (CEQA).

## BACKGROUND

### **SFPUC Sewer System Improvement Program (SSIP)**

The SFPUC Wastewater Enterprise currently operates a combined storm water and sewer system. Master planning for the SFPUC Sewer System Improvement Program (SSIP) began in 2004 with the goal of bringing the City's aging sewer system to a state of good repair and ensuring continued regulatory compliance and system reliability.

The SSIP is anticipated to be completed in three phases at a total cost of \$6.976 billion over approximately 20 years. In August 2012, the SFPUC approved Phase 1 of the SSIP for approximately \$2.9 billion. Of the \$2.9 billion for Phase 1, to date, the Board of Supervisors has appropriated \$1.2 billion for SSIP capital improvement projects.

### **Commercial Paper and Revenue Bonds**

The SFPUC can issue commercial paper in advance of an anticipated longer-term revenue bond sale in order to provide short-term funding (no more than 270 days) to finance capital projects. Proceeds from the sale of revenue bonds are then used to pay off the shorter-term commercial paper. Ultimately, the SFPUC redeems any revenue bonds, including notes, commercial paper or other forms of indebtedness from revenues collected from sewer service fees charged to San Francisco residents and businesses.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would (a) authorize an increase of \$250,000,000 in the principal amount of the SFPUC's Wastewater Enterprise Commercial Paper Program from the current not-to-exceed principal amount of \$500,000,000 to a principal amount not-to-exceed \$750,000,000, (b) authorize such commercial paper to be issued from time to time by the SFPUC to finance on an interim basis various capital projects benefitting the Wastewater Enterprise pursuant to amendments to the City Charter enacted by San Francisco voters on November 5, 2002 as Proposition E, (c) authorize and direct the SFPUC General Manager,

Controller, Director of the Office of Public Finance, Treasurer, City Attorney and other authorized staff and agents to take actions necessary to execute, issue and deliver the authorized commercial paper, and (d) ratify previous actions taken in connection therewith.

**Authorizations for SFPUC Commercial Paper**

Proposition E, approved by San Francisco voters on November 5, 2002, authorized the SFPUC to issue indebtedness including revenue bonds, notes, or commercial paper, when authorized by ordinance approved by a two-thirds vote of the Board of Supervisors to reconstruct, replace, expand, repair or improve the SFPUC’s wastewater facilities, and in compliance with City Charter Section 8B.124. In October 2006, the Board of Supervisors approved an ordinance to authorize the SFPUC to issue Wastewater Enterprise Commercial Paper in the aggregate principal amount not-to-exceed \$150,000,000 (File 06-1298). Table 1 below shows this initial authorization, two increased authorizations for a not-to-exceed authorized amount of \$500,000,000 previously approved by the Board of Supervisors and the current request for increased authorization of \$250,000,000 under the proposed resolution.

**Table 1: SFPUC Commercial Paper Authorizations**

| <b>File Number</b> | <b>Date Approved</b> | <b>Not to Exceed Amount Authorized</b> | <b>Increased Amount</b> |
|--------------------|----------------------|--|-------------------------|
| 06-1298            | October, 2006        | \$150,000,000                          |                         |
| 12-0354            | May, 2012            | 300,000,000                            | \$150,000,000           |
| 14-0955            | October, 2014        | 500,000,000                            | 200,000,000             |
| 17-0470            | May, 2017            | 750,000,000                            | 250,000,000*            |

\*Subject of the proposed resolution.

**Certification by Independent Engineer**

As noted above, the Board of Supervisors authority under Charter Section 8B.124 is subject to receipt of a certification from an independent engineer that the (i) projects to be financed by such debt meet utility standards and (ii) estimated net revenue will be sufficient to meet operating, maintenance, debt service coverage and other indenture or resolution requirements. AECOM Technical Services, Inc. (AECOM), a private engineering firm was retained by SFPUC to provide this certification. Based on a review of SFPUC’s documents, including SFPUC’s Wastewater Enterprise Financial Projections produced by Bartle Wells Associates on May 31, 2016, and discussions with SFPUC staff, AECOM certified on October 24, 2016 that

- (a) SFPUC’s wastewater projects, including prioritization, cost estimates and scheduling, meet generally accepted utility standards.
- (b) Estimated net revenue after payment of operating and maintenance expenses will be sufficient to meet debt service coverage and other indenture or resolution requirements, including debt service on the bonds to be issued and estimated repair and replacement costs.
- (c) All projects being funded by notes or bonds are scheduled for completion by 2026.
- (d) Cost estimates contained in the SFPUC documents, including budgeted costs for each project, appear reasonable.

(e) The methodology is reasonable, provided the methodology is consistently applied to all projects.

### **Certification by Planning Department**

Charter Section 8B.124 also requires the San Francisco Planning Department certify that the facilities financed with such debt will comply with applicable requirements of the California Environmental Quality Act (CEQA). On May 17, 2016, the Planning Department certified that the SFPUC projects to be funded with the proceeds from this indebtedness (a) comply with applicable requirements of CEQA, or (b) are not considered to be projects under CEQA at this time and will comply with CEQA if and when they are defined. In addition, Planning reports that pursuant to the provisions of Chapter 31 of the City's Administrative Code, any additional project to be financed will comply with the applicable requirements prior to any draw on any revenue indebtedness process to finance the acquisition of construction of such facilities.

### **Authorization by Public Utilities Commission**

On April 25, 2017, the SFPUC approved Resolution No. 17-0086, to authorize an increase of an additional \$250,000,000 from the existing authorization of not to exceed \$500,000,000 for a total not-to-exceed authorization of \$750,000,000 of aggregate principal Wastewater Enterprise Commercial Paper and authorize the SFPUC General Manager to issue the Commercial Paper in accordance with the specified terms.

## **FISCAL IMPACT**

The SFPUC is requesting the increased authorization of \$250,000,000, from a not-to-exceed \$500,000,000 to a total authorization not-to-exceed amount of \$750,000,000, in order to provide immediate short-term funding for projects for FY 2016-17, FY 2017-18 and FY 2018-19. On June 24, 2016, the Board of Supervisors approved Ordinance 111-16 which authorized the issuance of \$1.1 billion in SFPUC Wastewater Revenue Bonds, State Revolving Fund Loans and other forms of indebtedness including commercial paper for projects budgeted in FY 2016-17 and FY 2017-18. Without the requested \$250,000,000 increase in the commercial paper program, the SFPUC would issue SFPUC revenue bonds for these capital projects in 2017. However, if the proposed resolution is approved, Mr. Michael Brown, SFPUC Capital Finance advises that the SFPUC would issue commercial paper to fund these capital project costs in 2017 and then delay the issuance of revenue bonds until 2018.

According to Mr. Brown, the SFPUC primarily uses the commercial paper program to encumber and certify contracts. To date, the SFPUC has expended, encumbered and allocated \$492 million against the existing not-to-exceed \$500 million authorization for Wastewater Enterprise Commercial Paper. This leaves a current remaining authorized commercial paper balance of approximately \$8 million.

As shown in Table 2 below, the SFPUC is planning to use the \$8 million balance of previously authorized and available Wastewater Enterprise Commercial Paper, the requested \$250,000,000 additional authorization for Wastewater Enterprise Commercial paper,

\$94,651,953 of State Revolving Fund Loans<sup>1</sup> plus \$1,892,214,727 of proceeds from the issuance of Wastewater Enterprise Revenue Bonds to fund a total estimated \$2,244,866,680 of Wastewater Enterprise capital project needs.

**Table 2: Summary of Projects to Be Funded With Commercial Paper, State Revolving Funds and Wastewater Enterprise Revenue Bonds**

| <b>Sources of Funds</b>              |                        |
|--------------------------------------|------------------------|
| Existing Commercial Paper Authority  | \$8,000,000            |
| Requested Commercial Paper Authority | 250,000,000            |
| State Revolving Fund Loans           | 94,651,953             |
| Revenue Bonds                        | 1,892,214,727          |
| <b>Total Sources</b>                 | <b>\$2,244,866,680</b> |
| <b>Uses of Funds</b>                 |                        |
| <u>SSIP Project Costs</u>            |                        |
| Phase 1 Treatment Facilities         | \$1,374,173,789        |
| Phase 1 Collection System            | 83,967,457             |
| Storm Water Management               | 14,167,405             |
| Flood Resilience Projects            | 18,611,000             |
| Land Reuse                           | 33,846,569             |
| Phase 1 Program Management           | 20,000,000             |
| Phase 2 Treatment Facilities         | 9,844,735              |
| Phase 2 Collection System            | 690,255,725            |
| <b>Total Uses</b>                    | <b>\$2,244,866,680</b> |

Once these SFPUC capital projects are completed and long-term revenue bond debt is issued, the commercial paper will be repaid and then reissued to fund other projects. All fund proceeds received by the proposed increased debt borrowing from commercial paper are subject to appropriation approval by the Board of Supervisors for each of the subject capital projects.

### **Commercial Paper Interest Rates**

In accordance with the proposed resolution, the interest rate on the commercial paper will not exceed 12% annually. However, according to Mr. Brown, the actual interest rate on commercial paper is currently approximately 1% annually based on 60-day maturities, the typical length of SFPUC commercial paper. In addition to the commercial paper interest rate of 1%, there are bank credit facility fees and dealer fees, which generally result in an additional 0.5% cost or total costs of approximately 1.5% annually for the subject commercial paper under current market conditions. Rates for commercial paper may increase or decrease as the benchmark federal fund rates vary.

<sup>1</sup> State Revolving Fund Loans, which come from the State Water Resources Control Board, would be provided to the SFPUC at one-half of the State's General Obligation Bond rate, or approximately 1.7%, with 30-year amortization in today's market, with payments starting after the project is completed.

Table 3 below shows the estimated interest and fee expenses that would be incurred totaling \$3,604,890 or approximately 1.4% of the additional \$250,000,000 authorization of Wastewater Enterprise Commercial Paper.

**Table 3: Summary of Principal and Annual Interest and Fees Costs<sup>2</sup>**

|  |                      |
|--|----------------------|
| Principal Amount Available for Projects                                  | \$250,000,000        |
| Bank of America Fees (0.34% on \$150 Million Annually) <sup>3</sup>      | 555,271              |
| Sumitomo Mitsui Bank Fees (0.39% on \$100 Million Annually) <sup>3</sup> | 424,619              |
| Dealer Fees (0.005% Annually)  | 125,000              |
| Interest Payments (1.0% Annually in today's market)                      | 2,500,000            |
| <b>Total Costs</b>   | <b>\$253,604,890</b> |

**Commercial Paper vs Revenue Bonds**

Mr. Brown notes that commercial paper interest rates and fees at approximately 1%-1.4% annually are significantly lower than long-term revenue bond interest rates and fees, which are currently approximately 4% annually. Mr. Brown advises that increasing the SFPUC commercial paper authorization will provide the SFPUC the flexibility to more efficiently finance its capital projects, by reducing the period of paying capitalized interest and allowing the SFPUC to issue bonds at a later date, thereby lowering the SFPUC's debt and debt service costs. Reducing SFPUC debt service costs should result in lower cost increases to water and sewer rate payers.

As shown in Table 4 below, based on the Wastewater Enterprises contract and encumbrance project requirements over the next two years, SFPUC conservatively estimates the additional \$250 million commercial paper authorization would result in approximately \$8.7 million of net debt service savings from issuing a combination of commercial paper and revenue bonds.

**Table 4: Projected Net Debt Service Requirements over Next Two Years**

| Cumulative Net Debt Service Expenses Based on Current \$500 Million Commercial Paper Authorization and Bonding Requirements | Cumulative Net Debt Service Expenses Based on Proposed \$750 Million Commercial Paper Authorization and Bonding Requirements | Cumulative Net Debt Service Savings Based on Increase of \$250 Million Commercial Paper Authorization and Bonding Requirements |
|---|--|--|
| \$11,519,344,000  | \$11,510,644,000   | \$8,700,000  |

Similar savings would likely be realized by the SFPUC in subsequent years, varying with the amount of debt issued and the variance in the interest rates between commercial paper and longer-term revenue bonds.

<sup>2</sup> The actual amount of fees will vary depending on when the SFPUC issues commercial paper; interest and dealer fees accrue only when commercial paper is outstanding.

<sup>3</sup> Calculated based on the stated amount in the letter of credit which includes interest.



**RECOMMENDATION**

Approve the proposed resolution.

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| <p><b>Item 2</b><br/><b>File 17-0445</b></p>   | <p><b>Department:</b><br/>Recreation and Parks Department (RPD)</p> |
| <p><b>EXECUTIVE SUMMARY</b></p>  |   |
| <p style="text-align: center;"><b>Legislative Objectives</b></p>   |   |
| <ul style="list-style-type: none"> <li>• In accordance with Administrative Code Section 6.60, the proposed resolution would approve the Recreation and Park Department General Manager’s Declaration of an Emergency based on catastrophic tree mortality at Camp Mather due to a public safety hazard requiring the removal of approximately 1,500 trees due to bark beetle infestation at Camp Mather.</li> </ul>  |   |
| <p style="text-align: center;"><b>Key Points</b></p>   |   |
| <ul style="list-style-type: none"> <li>• Camp Mather is a 350-acre family summer camp located in the Sierra Nevada Mountains and operated by the Recreation and Park Department.</li> <li>• Between November 2016 and January 2017, the Recreation and Park Department’s certified arborist and Chief Urban Forester inspected the trees at Camp Mather and inventoried approximately 1,500 dead trees that pose an extreme public safety hazard and must be removed by summer 2017 when Camp Mathers opens.</li> <li>• In order to have the trees safely removed in time for the beginning of camp, the Recreation and Park Department reached out to contractors for informal bids, and received three bids in February 2017.</li> <li>• The Recreation and Park Department selected Crook Logging, Inc. since Crook Logging, Inc. was the only contractor that had the capacity to perform the tree removal work by the stated deadline of May 1, 2017, in accordance with the mandated requirements of the California Department of Forestry and Fire Protection.</li> </ul> |   |
| <p style="text-align: center;"><b>Fiscal Impact</b></p>  |   |
| <ul style="list-style-type: none"> <li>• Recreation and Park staff determined that removal, regulatory compliance, and disposal of the 1,500 trees would cost approximately \$1,600,000, based on the average per tree removal cost and the estimated costs to comply with State requirements.</li> <li>• Of the \$1,600,000, \$666,744 is from the Urban Forestry Program 2012 General Obligation Bonds, and \$933,256 is from the Recreation and Park Department General Fund Capital Budget yearly allocation for tree contracts as appropriated by the Board of Supervisors.</li> </ul>  |   |
| <p style="text-align: center;"><b>Recommendation</b></p>   |   |
| <ul style="list-style-type: none"> <li>• Approve the proposed resolution.</li> </ul>   |   |

## MANDATE STATEMENT

Administrative Code Section 6.60(D) states that contracts entered into for emergency work that are more than \$250,000 are subject to Board of Supervisors approval. Prior to the commencement of emergency work above the \$250,000 threshold, the Department must also secure approval in writing from the Mayor, the President of the Board, or the Commission. The proposed resolution approving the emergency determination must be submitted to the Board of Supervisors 60 days after the Department Head's emergency declaration.

## BACKGROUND

The four-year period between 2011 and 2015 was the driest weather in California since record keeping began in 1895. As a result of the drought and subsequent wildfires, various species of bark beetle infested and killed a significant amount of conifer trees through the Sierra Nevada region, leading the Governor of California to declare a State of Emergency in October 2015.

Camp Mather is a 350-acre family summer camp located in the Sierra Nevada Mountains close to the border of Yosemite National Park and operated by the Recreation and Park Department. Every year, approximately 7,000 San Franciscans secure a one-week reservation through the annual Camp Mather lottery to stay on site. Camp Mather is comprised primarily of large conifer trees that have been infected and killed by the bark beetles. According to Mr. Dennis Kern, Recreation and Park Department Director of Operations, the Department's Chief Urban Forester visited Camp Mather in April 2016 to track the presence of the bark beetle in the camp trees. The Department's tree crew and a contractor, Sierra Mountain Construction, removed over 350 trees in April and May of 2016 due to the infestation. Subsequently, between November 2016 and January 2017, the Recreation and Park Department's certified arborist and Chief Urban Forester inspected the trees at Camp Mather and inventoried approximately 1,500 dead trees that pose an extreme public safety hazard and must be removed by summer 2017 when Camp Mathers opens.

The Recreation and Park Department General Manager declared a state of emergency in a letter to the Board of Supervisors on February 27, 2017. The Department submitted the resolution, declaring a state of emergency, to the Board of Supervisors on April 18, 2017.

## DETAILS OF PROPOSED LEGISLATION

In accordance with Administrative Code Section 6.60, the proposed resolution would approve the Recreation and Park Department General Manager's Declaration of an Emergency based on catastrophic tree mortality at Camp Mather due to a public safety hazard requiring the removal of approximately 1,500 trees due to bark beetle infestation at Camp Mathers.

Recreation and Park staff analyzed the bark beetle infestation, inventory of dead trees, State of California regulatory requirements for timber removal, and disposal options for all removed tree wood. The staff determined that removal, regulatory compliance, and disposal of the 1,500 trees would cost approximately \$1,600,000. The \$1,600,000 estimate was based on the average per tree removal cost, calculated from Sierra Mountain Construction's work in the summer of

2016, and the estimated costs to comply with the requirements of the California Department of Forestry and Fire Protection and the California Department of Fish and Wildlife.

Because removal of the trees was considered an extreme public safety hazard and after obtaining three bids, the Recreation and Park Department entered into a contract for tree removal with Crook Logging, Inc., on a sole source basis, as permitted under Administrative Code Section 6.60. The scope of the work includes tree felling, removal, and project closeout from the period of March 14, 2017 to May 1, 2017.

According to Mr. Kern, the normal open-bidding process usually takes approximately three to four months. The spring work crew for Camp Mather is scheduled to arrive on May 8, 2017, and the first day of camp season for the public is May 28, 2017. In order to have the trees safely removed in time for the beginning of camp, the Recreation and Park Department reached out to contractors for informal bids beginning in November 2016, before the full count of trees was known. The Department counted 1,500 trees by January, and received three bids in February 2017: Sierra Mountain Construction, Kevin Kalkowski, and Crook Logging, Inc. According to Mr. Kern, contractors delayed submitting bids as the tough winter conditions in the mountains made work extremely difficult. The Recreation and Park Department selected Crook Logging, Inc. since Crook Logging, Inc. was the only contractor that had the capacity to perform the tree removal work by the stated deadline of May 1, 2017, in accordance with the mandated requirements of the California Department of Forestry and Fire Protection. According to Mr. Kern, the California Department of Forestry and Fire Protection has approved the emergency tree removals. Crook Logging began work on the tree felling and removal in March 2017, which was completed on May 1, 2017. The project clean-up is expected to end on May 8, 2017.

## FISCAL IMPACT

The budget for tree removal at Camp Mather is \$1,600,000, as shown in Table 1 below.

**Table 1: Budget for Tree Removal at Camp Mather**

| <b>Purpose</b>                       | <b>Estimate Cost</b> |
|--------------------------------------|----------------------|
| Tree felling                         | \$500,000            |
| Tree removal                         | <u>800,000</u>       |
| Subtotal                             | 1,300,000            |
| Contractual obligations <sup>a</sup> | 250,000              |
| Project closeout <sup>b</sup>        | 50,000               |
| <b>Total Cost Estimate</b>           | <b>\$1,600,000</b>   |

<sup>a</sup> Contractual obligations include costs associated with permitting, payment of fees, licenses, and yield tax.

<sup>b</sup> Project closeout includes costs for clean-up, final approvals, and inspections by CAL FIRE

Of the \$1,600,000, \$666,744 is from the Urban Forestry Program 2012 General Obligation Bonds, and \$933,256 is from the Recreation and Park Department General Fund Capital Budget yearly allocation for tree contracts as appropriated by the Board of Supervisors.

## RECOMMENDATION

Approve the proposed resolution.

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| <p><b>Item 3</b><br/><b>File 17-0322</b></p>  | <p><b>Department:</b><br/>San Francisco International Airport (Airport)</p> |
| <p><b>EXECUTIVE SUMMARY</b></p>   |   |
| <p style="text-align: center;"><b>Legislative Objectives</b></p>  |   |
| <ul style="list-style-type: none"> <li>The proposed resolution would retroactively approve the first modification to the license and service agreement between the Airport and Airport Research and Development Foundation (ARDF), a nonprofit agency, to monitor transportation network companies (Uber, Lyft, Wingz, and Sitbaq) pick up and drop off trips at the Airport and collect the trip fees on behalf of the Airport. The first modification would (i) exercise all three one-year options to extend the agreement term for the period of March 13, 2017 through March 12, 2020, and (ii) cap the Administrative Services Fee paid by the Airport to ARDF at \$250,000 annually for the period of March 13, 2017 through March 12, 2020.</li> </ul>  |   |
| <p style="text-align: center;"><b>Key Points</b></p>  |   |
| <ul style="list-style-type: none"> <li>The Airport began issuing permits to transportation network companies in October 2014. These permits allowed transportation network companies to pick up and drop off passengers at the Airport for a fixed fee payable to the Airport of \$3.80 per trip. Airport staff developed an application-based commercial ground transportation (ABCT) system in-house, which can monitor transportation network companies' trips to the Airport and collect the appropriate fees. The Airport's ABCT system can be licensed to other airports that charge trip fees to transportation network companies.</li> <li>In March 2015, the Board of Supervisors approved the license and service agreement on a sole source basis between the Airport and a non-profit, Airport Research and Development Foundation (ARDF), in which the Airport would license the application-based commercial ground transportation, or ABCT, system to ARDF (File 15-0152). The license and service agreement has an initial two-year term from March 13, 2015 through March 12, 2017, with three optional one year extensions through March 12, 2020.</li> </ul> |   |
| <p style="text-align: center;"><b>Fiscal Impact</b></p>   |   |
| <ul style="list-style-type: none"> <li>The Airport has paid \$500,000 in Administrative Services Fees to ARDF from March 2016 through February 2017. ARDF has paid the Airport \$126,672 in Service Development Fees (\$125,000 or 25 percent of Administrative Services Fee revenues from the Airport and \$1,672 from other participating airports). As a result of transportation network companies being authorized to pick up and drop off passengers at the Airport, the Airport has realized net revenues of \$39,593,777.</li> <li>Three transportation network companies with ABCT permits - Uber, Lyft, and Wingz - currently account for over 68 percent of all paid commercial ground transportation trips at the Airport, generating approximately \$2 million per month in trip fee revenue which exceeds original projections. The high level of ABCT trip activity was unanticipated when the agreement began in March 2015 when transportation network companies with ABCT permits represented less than 37 percent of commercial ground transportation trips.</li> </ul>  |   |
| <p style="text-align: center;"><b>Recommendation</b></p>  |   |
| <ul style="list-style-type: none"> <li>Approve the proposed resolution.</li> </ul>  |   |

**MANDATE STATEMENT**

City Charter Section 9.118(a) states that contracts entered into by a department, board, or commission that (i) have anticipated revenues of \$1 million or more, or (ii) have anticipated revenues of \$1 million or more and require modifications, are subject to Board of Supervisors approval.

**BACKGROUND**

The Airport began issuing permits to transportation network companies in October 2014. These permits allowed transportation network companies to pick up and drop off passengers at the Airport for a fixed fee payable to the Airport of \$3.80 per trip. Four transportation network companies currently have annual permits to pick up and drop off passengers at the Airport: Uber, Lyft, Wingz, and Sitbaq.<sup>1</sup> Airport staff developed an application-based commercial ground transportation (ABCT) system in-house, which can monitor transportation network companies' trips to the Airport and collect the appropriate fees. The ABCT system is technically compatible with the transportation network companies that have permits to pick up and drop off Airport passengers.

The ABCT system defines a perimeter around the Airport using geographic coordinates. Transportation network companies are required by the terms of their permit to send data to the Airport's ABCT system any time that one of their respective vehicles enters, leaves, picks-up or drops-off passengers within the perimeter. The ABCT system stores this trip data for future auditing and passes this trip data to the Airport's financial systems for invoicing.

The Airport's ABCT system can be licensed to other airports that charge trip fees to transportation network companies.

In March 2015, the Board of Supervisors approved the license and service agreement on a sole source basis<sup>2</sup> between the Airport and a non-profit, Airport Research and Development Foundation (ARDF), in which the Airport would license the application-based commercial ground transportation, or ABCT, system to ARDF (File 15-0152). The license and service agreement has an initial two-year term from March 13, 2015 through March 12, 2017, with three optional one year extensions through March 12, 2020, which are at the discretion of the Airport.

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<sup>1</sup> The Airport originally issued permits to Uber and Lyft in October 2014, to Wingz in November 2015, and to Sitbaq in March 2017.

<sup>2</sup> According to Ms. Cathy Widener, Airport Government Affairs Manager, the Airport investigated companies that could serve as its licensee and determined that a not-for-profit trade organization representing the interests of the airport industry was the only option because such an organization could use the ABCT system to provide services to other airports at reasonable rates. Of the not-for-profit trade organizations representing the interests of the airport industry, the Airport determined that ARDF is the only such organization with the technical expertise and clearinghouse capabilities to adequately provide the desired services.

**DETAILS OF PROPOSED LEGISLATION**

The proposed resolution would retroactively<sup>3</sup> approve the first modification to the license and service agreement between the Airport and Airport Research and Development Foundation (ARDF), a nonprofit agency, to monitor transportation network companies (Uber, Lyft, Wingz, and Sitbaq) pick up and drop off trips at the Airport and collect the trip fees on behalf of the Airport. The first modification would (i) exercise all three one-year options to extend the agreement term for the period of March 13, 2017 through March 12, 2020, and (ii) cap the Administrative Services Fee paid by the Airport to ARDF at \$250,000 annually for the period of March 13, 2017 through March 12, 2020.

Under the license and service agreement, ARDF monitors transportation network companies' trips, and collects trip fees on behalf of the Airport. The Airport pays ARDF an Administrative Services Fee of 5 percent of total trip fee revenues, and ARDF pays the Airport a Service Development Fee equal to 25 percent of ARDF's Administrative Services Fee revenues. The Service Development Fee is intended to partially reimburse the Airport for its costs to develop the ABCT system.

The license and service agreement capped the Administrative Services Fee paid by the Airport to ARDF at \$500,000 for the two-year period from March 2015 to March 2017. The proposed first modification to the license and service agreement caps the Administrative Service Fee paid by the Airport to ARDF at \$250,000 per year, totaling \$750,000 for the proposed three-year option period from March 2017 to March 2020.

**Licensing the ABCT System to Other Airports**

Under the license and service agreement, the ABCT system remains the exclusive property of the City. ARDF may enter into service agreements with other airports to implement and operate the ABCT system, including (1) collecting Administrative Services Fees from participating airports; and (2) paying to the San Francisco International Airport the Service Development Fee, equal to 25 percent of total Administrative Services Fee revenues received by ARDF from the participating airports.

According to Mr. Angus Davol, Airport Senior Transportation Planner, there are currently eight airports that have entered into agreements with ARDF to use the ABCT system. These airports include Hartsfield Jackson Atlanta International Airport (ATL), Wilkes-Barre/Scranton International Airport (AVP), City of Colorado Springs Municipal Airport (COS), Fresno Yosemite International Airport (FAT), Spokane International Airport (GEG), Jacksonville International Airport (JAX), Norfolk International Airport (ORF), and McGhee Tyson Airport in Knoxville (TYS).

**FISCAL IMPACT**

Based on \$3.80 per trip, the Airport has collected \$39,967,105 in trip fees from the four transportation network companies (Uber, Lyft, Wingz, and Sitbaq) between October 2014,

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<sup>3</sup> According to the Airport, the resolution is retroactive due to the negotiation process with the Airport Research and Development Foundation.

when the Airport first issued permits to the transportation network companies, and February 2017, as shown in Table 1 below. ARDF began collecting trip fees from transportation network companies on behalf of the Airport in March 2015. During the first year of the license and service agreement from March 2015 to March 2016, both the Administrative Services Fee paid by the Airport to ARDF, and the Service Development Fee paid by ARDF to the Airport, were waived to allow ARDF sufficient time to develop a derivative of the Airport's ABCT system for the purpose of providing trip monitoring and fee collection services to other airports.

The Airport has paid \$500,000 in Administrative Services Fees to ARDF from March 2016 through February 2017.<sup>4</sup> ARDF has paid the Airport \$126,672 in Service Development Fees (\$125,000 or 25 percent of Administrative Services Fee revenues from the Airport and \$1,672 from other participating airports<sup>5</sup>). As shown in Table 1 below, as a result of transportation network companies being authorized to pick up and drop off passengers at the Airport, the Airport has realized net revenues of \$39,593,777.

**Table 1: Fee Collection from Transportation Network Companies and ABCT System**

| <b>Fees</b>  | <b>FY 2014-15</b><br>(Oct 2014 to<br>June 2015) | <b>FY 2015-16</b>   | <b>FY 2016-17</b><br>(July 2016<br>through Feb<br>2017) | <b>Total</b>        |
|--|---|---------------------|---|---------------------|
| Transportation Network Companies Trip Fee Revenues Paid to the Airport | \$6,574,554                                     | \$16,870,980        | \$16,521,571  | \$39,967,105        |
| Administrative Services Fee Paid by Airport to ARDF                    | 0   | (306,498)           | (193,502)   | (500,000)           |
| Service Development Fee paid by ARDF to the Airport                    | 0   | 0                   | 126,672   | 126,672             |
| <b>Net Revenue to the Airport</b>                                      | <b>\$6,574,554</b>                              | <b>\$16,564,482</b> | <b>\$16,454,741</b>                                     | <b>\$39,593,777</b> |

According to Mr. Davol, three transportation network companies with ABCT permits - Uber, Lyft, and Wingz - currently account for over 68 percent of all paid commercial ground transportation trips at the Airport, generating approximately \$2 million per month in trip fee revenue which exceeds original projections. The high level of ABCT trip activity was unanticipated when the agreement began in March 2015 when transportation network companies with ABCT permits represented less than 37 percent of commercial ground transportation trips.

<sup>4</sup> According to Mr. Davol, the Airport began paying Administrative Services Fees to ARDF on March 13, 2016. From March 13, 2016 through June 30, 2016, the fee amount totaled \$306,498. For FY 2016-17, the Airport met the \$500,000 Administrative Services Fee cap in September 2016, so the remaining fee amount collected was \$193,502.

<sup>5</sup> According to Mr. Davol, the Airport has not yet received revenue from all participating airports using the ABCT system, as some of them only recently signed up. However, the Airport should receive revenue from all participating airports in the upcoming fiscal year.



Mr. Davol states that because of the many variables related to trip volumes at airports, demand for transportation network companies' services, and new airports that enroll with ARDF and use the ABCT system, the Airport cannot project Service Development Fees for the remaining three options years of the services term.

**RECOMMENDATION**

Approve the proposed resolution.

|  |   |
|--|---|
| <p><b>Item 5</b><br/><b>File 17-0473</b></p>   | <p><b>Department:</b><br/>Mayor’s Office of Housing and Community Development (MOHCD)</p> |
| <p><b>EXECUTIVE SUMMARY</b></p>  |   |
| <p style="text-align: center;"><b>Legislative Objectives</b></p> <p>The proposed resolution approves: (1) the purchase and sale agreement between the Mayor’s Office of Housing and Community Development (MOHCD) and Eddy &amp; Taylor Associates, L.P., established by the non-profit organization, Tenderloin Neighborhood Development Corporation (TNDC), for the purchase of the land consisting of 22,343 square feet at 210 Taylor Street for a purchase price of \$10,600,000; and (2) a ground lease between the City and Eddy &amp; Taylor Associates, L.P. for 210 Taylor Street for a term of 87 years and one 12-year extension, totaling 99 years.</p> <p style="text-align: center;"><b>Key Points</b></p> <ul style="list-style-type: none"> <li>• Eddy &amp; Taylor Associates, L.P. purchased 210 Taylor Street in 2007 for \$9,300,000 as a site for affordable housing development, using MOHCD acquisition and private loans. Eddy &amp; Taylor Associates, L.P. was not able to develop affordable housing on the site due to the recession and inability to obtain funding. The site has been used as a parking lot and billboard site.</li> <li>• MOHCD now proposes to purchase the site for \$10,600,000, based on the appraised value of the site, and enter into a ground lease with Eddy &amp; Taylor Associates, L.P. to construct a 113-unit affordable housing project. Project costs of \$74.4 million will be financed by a combination of MOHCD gap loans, other State of California grants and loans, and private financing. Construction is scheduled to begin in June 2017.</li> </ul> <p style="text-align: center;"><b>Fiscal Impact</b></p> <ul style="list-style-type: none"> <li>• MOHCD would purchase 210 Taylor Street for \$10,600,000. Funds to purchase the site include forgiveness of \$7,250,108 in principal and interest on the loan originally made to Eddy &amp; Taylor Associates, L.P. and \$3,349, 892 in cash.</li> <li>• Eddy &amp; Taylor Associates, L.P. would enter into a ground lease for up to 99 years, paying base rent of \$15,000 per year and residual rent (based on the availability of funds after expenses are paid) equal to 10 percent of the appraised value.</li> </ul> <p style="text-align: center;"><b>Policy Consideration</b></p> <ul style="list-style-type: none"> <li>• MOHCD adopted a policy in 2011 to acquire sites to develop affordable housing, and ground lease these sites to affordable housing developers.</li> <li>• Since 2011 MOHCD has provided acquisition financing to affordable housing developers with the understanding that the principal and interest would be considered paid upon the conveyance of the land to the City.</li> </ul> <p style="text-align: center;"><b>Recommendation</b></p> <ul style="list-style-type: none"> <li>• Approve the proposed resolution.</li> </ul> |   |

## MANDATE STATEMENT

City Administrative Code Section 23.1 requires the Director of Real Estate to recommend approval of real property transactions prior to approval by the Board of Supervisors. Administrative Code Section 23.3 requires an appraisal prior to the property purchase, and an appraisal review for the purchase of property exceeding \$200,000 in appraised value.

## BACKGROUND

In 2006, the Mayor's Office of Housing—now the Mayor's Office of Housing and Community Development (MOHCD)—issued a Notice of Funding Availability (NOFA) to provide \$9,000,000 in financing for the development of affordable rental housing for low income families. MOHCD selected the non-profit organization, Tenderloin Neighborhood Development Corporation (TNDC), which established Eddy & Taylor Associates, L.P. to develop 113 units of housing affordable to low-income families at 210 Taylor Street.<sup>1</sup>

Eddy & Taylor Associates, L.P. purchased 210 Taylor Street in 2007 for \$9,300,000, using a \$5,950,108 acquisition loan<sup>2</sup> from MOHCD and a \$6,000,000 acquisition and predevelopment loan from Bank of America.<sup>3</sup> In 2011, Eddy & Taylor Associates, L.P. refinanced the Bank of America loan, using a \$7,055,000 loan from the Low Income Investment Fund (LIIF)<sup>4</sup>. The 22,343 square foot lot currently contains a billboard and a parking lot.<sup>5</sup> The Project experienced delays due to the Great Recession during the years 2007 to 2009 and project plans have changed in the interim to make the project feasible.<sup>6</sup>

### 210 Taylor Street Project Details

At completion, the 210 Taylor Street Project will include 113 housing units, including: 35 units affordable to households earning up to 15 percent of the Area Median Income (AMI)<sup>7</sup>, 77 units

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<sup>1</sup> TNDC selected the site at 210 Taylor Street and included the site (as part of their proposal) in their response to MOHCD's NOFA.

<sup>2</sup> A low-interest loan (3 percent) from MOHCD payable back to the City from residual rent receipts (i.e. funds that remain once all other expenses and debt are paid) over 55 years. To date, this loan has accrued \$1,690,157 in interest.

<sup>3</sup> The combined loan amounts of \$11,950,108 exceeded the \$9,300,000 purchase price by \$2,650,108. These funds of \$2,650,108 were used for pre-development expenses, including architecture and engineering, environmental work, and fees associated with entitlements and CEQA approval.

<sup>4</sup> LIIF is a non-profit community development financial institution that provides capital for projects that serve low-income communities.

<sup>5</sup> CBS Outdoor (the billboard operator) and Execupark (the parking lot operator) will receive relocation benefits in accordance with the Federal Uniform Relocation Action and the California Relocation Assistance Act. Relocation benefits will be funded by the Project and were previously approved by MOHCD.

<sup>6</sup> The project was downsized from 153 units to 113 units due to financial feasibility based on low income housing financing sources. The property is zoned for 153 units and entitled for construction of the 113 units.

<sup>7</sup> 15 percent of the AMI in 2017 for a family of four is \$19,740, calculated as 100 percent of AMI for a family of four as published by the California Tax Credit Allocation Committee (\$131,600) multiplied by 15 percent.

affordable to households earning up to 50 percent of AMI<sup>8</sup>, and one two-bedroom unit for the property manager. The 112 affordable units (excluding one unit for the property manager) will be comprised of a mix of studio, one-bedroom, two-bedroom, and three-bedroom units, as shown in Table 1 below. The project will include a total of 108,711 square feet of residential space, 5,677 square feet of retail commercial space, and 2,238 square feet for non-residential space, including offices, a lounge, and a community room.

**Table 1: 210 Taylor Street Project Affordable Units**

| Unit Type     | Affordability Level |           | Total      |
|---------------|---------------------|-----------|------------|
|               | 15% AMI             | 50% AMI   |            |
| Studio        | 2                   | 14        | 16         |
| One-bedroom   | 7                   | 7         | 14         |
| Two-bedroom   | 20                  | 47        | 67         |
| Three-bedroom | 6                   | 9         | 15         |
| <b>Total</b>  | <b>35</b>           | <b>77</b> | <b>112</b> |

Source: MOHCD

The 35 units affordable to families earning up to 15 percent of AMI will receive rent subsidies from the City's Local Operating Subsidy Program (LOSP)<sup>9</sup> and California's Section 811 Project Rental Assistance Demonstration program.<sup>10</sup> Five of the units will be set aside for adults with developmental disabilities and subsidized by Section 811 funds, and the remaining 30 units will be set aside for homeless families and subsidized by LOSP.<sup>11</sup> LOSP subsidies are estimated to equal \$73,772 in FY 2018-19<sup>12</sup>, \$225,767 in FY 2019-20 and will increase by 4 percent per year through FY 2032-33.

### Project Financing

Construction of the Project is scheduled to begin in June 2017 and is expected to be completed by June 2019. Total estimated costs for development of 113 housing units (not including land acquisition costs) are \$74,406,813, or \$658,467 per unit, including \$44,387,314 in public financing and \$30,019,499 in private financing, as shown in Table 2 below.<sup>13</sup> MOHCD previously committed \$19,600,000 in gap loan financing and the Citywide Affordable Housing Loan

<sup>8</sup> 50 percent of the AMI in 2017 for a family of four is \$57,650 as published by MOHCD.

<sup>9</sup> The Local Operating Subsidy Program is funded by the City's General Fund, subject to annual appropriation by the Board of Supervisors in the Department of Homelessness and Supportive Housing's budget. A future agreement between the project sponsor and the City to allocate LOSP funds to the 210 Taylor Street project will be subject to Board of Supervisors approval.

<sup>10</sup> Funded by the U.S. Department of Housing and Urban Development (HUD) and administered by the California Housing Finance Agency (CalFHA)

<sup>11</sup> Section 811 operating funds are committed for 20 years, and LOSP funds are committed for 15 years. According to the MOHCD gap loan terms for the Project, if the subsidies are lost for any of these units, the affordability threshold may be raised from 15 percent of AMI to 50 percent of AMI.

<sup>12</sup> LOSP subsidies for FY 2018-19 would be for four months.

<sup>13</sup> Including land acquisition costs, total estimated costs for development are \$85,396,970, or \$755,725 per unit.

Committee approved an additional \$3,452,146 in gap loan financing on May 5, 2017 for a total of \$23,052,146. All financing for the Project has been finalized.

**Table 2: Sources of Funds for Project**

| <b>Source</b>  | <b>Amount</b>       |
|--|---------------------|
| <b>Public Sources</b>  |                     |
| MOHCD Gap Loan <sup>14</sup>   | \$23,052,146        |
| Accrued Interest on MOHCD Loan   | 175,192             |
| Subtotal, MOHCD Sources  | 23,227,338          |
| Affordable Housing Program <sup>15</sup>                                       | 1,875,000           |
| California Department of Housing and Community Development (HCD) <sup>16</sup> | 19,284,976          |
| <b>Subtotal, Public Sources</b>  | <b>44,387,314</b>   |
| <b>Private Sources</b>   |                     |
| Deferred Developer Fee   | 851,048             |
| Private Investor Contributions <sup>17</sup>                                   | 29,168,451          |
| <b>Subtotal, Private Sources</b>   | <b>30,019,499</b>   |
| <b>Total Sources</b>   | <b>\$74,406,813</b> |

Source: MOHCD

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution approves:

(1) the purchase and sale agreement between the City and Eddy & Taylor Associates, L.P., established by the non-profit organization, Tenderloin Neighborhood Development Corporation (TNDC), for the purchase of the land consisting of 22,343 square feet at 210 Taylor Street for a purchase price of \$10,600,000, and

(2) a ground lease between the City and Eddy & Taylor Associates, L.P. for 210 Taylor Street for a term of 87 years and one 12-year extension, totaling 99 years.

The proposed resolution also finds that the property purchase and ground lease are consistent with the California Environmental Quality Act (CEQA); and authorizes the Director of Real Estate and Director of the Mayor's Office of Housing and Community Development to execute

<sup>14</sup> MOHCD Gap Loan includes (a) 19,600,000 previously committed in 2015 plus (b) \$3,452,146 approved by the Citywide Affordable Housing Loan Committee on May 5, 2017. Sources for the gap loan include: (a) the Affordable Housing Trust Fund, (b) the City's Inclusionary Housing Program, and (c) HUD grant funds through the HOME Investments Partnerships Program.

<sup>15</sup> An Affordable Housing Program (AHP) grant from the Federal Home Loan Bank of San Francisco.

<sup>16</sup> HCD funding includes (a) \$7,000,000 from the Multifamily Housing Program (MHP) plus (b) 12,284,976 from the Affordable Housing and Sustainable Communities Program.

<sup>17</sup> Private Investor Contributions include (a) \$1,148,952 in cash investment plus (b) \$28,019,499 in proceeds from the sale of Federal Low Income Housing Tax Credits for affordable housing projects.

documents, make certain modifications, and take certain actions in furtherance of the property purchase and ground lease.

The property would be used for the construction of 112 affordable housing units and one property manager unit. According to Ms. Sarah Nusser, Senior Project Manager at MOHCD, MOHCD adopted a policy of owning land for affordable housing developments and ground leasing the land to developers in 2011 to ensure the long-term affordability and viability of publicly funded housing (see Policy Consideration Section Below).<sup>18</sup> Under the ground lease, the City would own and control the use of the land, and Eddy & Taylor Associates, L.P. would own any improvements on the land. In the event that the developer falls into default, the City would have the right to “cure the default” or pay the money owed, replace the developer, and ensure the property is still used for affordable housing.

## FISCAL IMPACT

### Land Acquisition Costs

A valuation analysis conducted by Joseph J. Blake and Associates, Inc. for TNDC in September 2016 valued the land parcel at 210 Taylor Street at \$10,600,000.<sup>19</sup> CBRE, Inc. reviewed the appraisal for the City and found the appraisal to be reasonable.

According to the purchase agreement, MOHCD would forgive a \$5,950,108 acquisition loan<sup>20</sup> that it issued in 2007 and \$1,300,000 of the \$1,690,157 in accrued and unpaid interest on that loan (see Policy Consideration Section below) and also provide \$3,349,892 in cash<sup>21</sup>, for a total purchase price of \$10,600,000.

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<sup>18</sup> According to Ms. Nusser, this policy was adopted based on the success of the former Redevelopment Agency in using this model.

<sup>19</sup> The valuation was based on the assumption that the parcel would be used for a 153-unit market rate housing development. The valuation assumes 153 units and not 113 units because the property is zoned for 153 units. As mentioned previously, the project was downsized from 153 units to 113 units due to financial feasibility based on low income housing financing sources, which would not impact market rate financing. The valuation was calculated as the estimated number of units (153) multiplied by the estimated value per unit (\$69,500), based on the unit sale prices of comparable properties.

<sup>20</sup> The source of funds for the \$5,950,108 acquisition loan was a supplemental appropriation ordinance, which appropriated money from the City’s General Fund to MOHCD for affordable housing (Ordinance 71-06). Any loan repayments (including interest payments) would be re-appropriated for affordable housing through MOHCD’s annual budget process.

<sup>21</sup> Cash payment would cover the value of the land financed by the LIIF loan.

**Table 3: MOHCD land acquisition costs**

| <b>Description</b>  | <b>Amount</b>       |
|---|---------------------|
| Outstanding balance of 2007 acquisition loan (forgiven)         | \$5,950,108         |
| Accrued and unpaid interest on 2007 acquisition loan (forgiven) | <u>1,300,000</u>    |
| Subtotal, loan and interest                                     | 7,250,108           |
| Cash (to be provided by MOHCD)                                  | 3,349,892           |
| <b>Total</b>  | <b>\$10,600,000</b> |

Source: MOHCD

Eddy & Taylor Associates, L.P. would pay the City's one-time transfer tax estimated to be \$291,500.<sup>22</sup> The cash amount of \$3,349,892 to be paid to Eddy & Taylor Associates, L.P. would come from the Inclusionary Affordable Housing Program.<sup>23</sup> According to Mr. Benjamin McCloskey, Deputy Director of Finance and Administration at MOHCD, the unencumbered balance of the Inclusionary Affordable Housing Program is \$130 million (as of April 30, 2017). Mr. McCloskey also states that a cash payment for the purchase of 210 Taylor Street would not impact the affordable housing pipeline, as the payment is already assumed in the affordable housing pipeline as part of the Project's total financing.

### **Annual Rent Receipts**

According to the ground lease terms, Eddy & Taylor Associates, L.P. would pay rent to the City on an annual basis. Annual rent would be equal to 10 percent of the appraised value of the site. Annual rent would be comprised of \$15,000 in base rent (i.e. rent paid each year regardless of rent receipts) and the remaining annual rent balance in residual rent.<sup>24</sup> As discussed above, the appraised value of the site is \$10,600,000. Thus, rent for the first year would equal \$1,060,000, including \$15,000 in base rent and \$1,045,000 in residual rent. Annual rent receipts would be re-appropriated for Inclusionary-eligible uses<sup>25</sup> through MOHCD's annual budget process.

## **POLICY CONSIDERATION**

### **MOHCD Policy to Acquire Sites for Affordable Housing Development**

MOHCD adopted a policy in 2011 to acquire sites to develop affordable housing, and ground lease these sites to affordable housing developers. As noted in the attached memorandum from Mr. Olson Lee, MOHCD Director, MOHCD adopted this model to ensure the long-term affordability and viability of publicly-funded housing.

MOHCD's underwriting guidelines to provide loans to non-profit organizations to develop affordable housing provide for loans with terms of 40 years to 75 years (typically 55 years), at

<sup>22</sup> Equal to the transfer tax rate of 2.75 percent times the purchase price of \$10,600,000.

<sup>23</sup> The Inclusionary Affordable Housing Program—established by Section 415 of the City's Planning Code—requires residential developments with at least ten units to either: (a) pay an Affordable Housing Fee; or (b) provide a certain percentage of their units as affordable to low- to moderate-income households.

<sup>24</sup> Residual rent would be paid out of funds that remain once all other expenses and debt are paid.

<sup>25</sup> "Inclusionary-eligible" uses include new multi-family affordable housing projects.

interest rates ranging from 0 percent to 3 percent simple interest. According to the underwriting guidelines, unpaid principal and interest on the loans is deferred during the term of the loan and payable at the end of the term.

Based on MOHCD's 2011 site acquisition policy, MOHCD now proposes to purchase 210 Taylor Street and enter into a ground lease with Eddy & Taylor Associates, L.P. MOHCD will forgive \$7,250,108 in loan principal and interest (see Table 3 above) as a source of payment toward the \$10,600,000 purchase price for 210 Taylor Street. According to Mr. Olson, since 2011 MOHCD has provided acquisition financing to affordable housing developers with the understanding that the principal and interest would be considered paid upon the conveyance of the land to the City.

### **RECOMMENDATION**

Approve the proposed resolution



Mayor's Office of Housing and Community Development  
City and County of San Francisco

Attachment



**Edwin M. Lee**  
Mayor

**Olson Lee**  
Director

To: Severin Campbell, Director, Budget & Legislative Analyst's Office

From: Olson Lee, Director, Mayor's Office of Housing and Community Development *OL*

Re: MOHCD Acquisition Loan Policy

Date: May 11, 2017

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In the past, MOHCD did not have a policy of owning land and ground leasing it to affordable housing developers for the development and ownership of affordable housing projects.

Starting in 2011, based on the success of the former Redevelopment Agency, MOHCD adopted this model to ensure the long-term affordability and viability of publicly funded housing. Ground leases allow the City to restrict the use of the land for a term up to 99 years.

Since 2011, MOHCD has provided acquisition financing to affordable housing developers with the understanding that the principal and accrued interest would be considered paid upon the conveyance of the land to the City.

A recent example of this approach can be found in the transfer of land at 1036 Mission (an affordable housing development currently under construction) to the City in 2016. Acquisition financing for the 1036 Mission land parcel was made to the developer from the Redevelopment Agency in 2007. Because the Agency had a ground leasing policy, the repayment terms of that acquisition loan were as such:

3.5 Repayment of Principal and Interest. The outstanding principal balance of the <sup>Attachment</sup> Loan, together with all accrued and unpaid interest will be due and payable on the Maturity Date according to the terms set forth in full in the Note. Upon the latest to occur of the following events, the Funding Amount shall be reduced by the principal balance of the Loan equal to the Acquisition Funds, together with the interest accrued on that portion of the Loan:

a. The City's approval of the conveyance documents evidencing the conveyance of Borrower's fee interest in the Site to the Agency, less the improvements;

b. The City's approval of the ground lease and ancillary documents between the Agency and the City evidencing Borrower's ground lease of the Site (the " Agency's Ground Lease"):

c. The execution and recordation of a new deed of trust approved by the City encumbering the Borrower's leasehold interest in the Site and its fee interest in the improvements; and

d. The execution and if requested by the City, the recordation, of any other document reasonably required by the City to evidence Borrower's obligation to repay the reduced Funding Amount.

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| <b>Item 6</b><br><b>File 17-0474</b>  | <b>Department:</b> Mayor's Office of Housing and Community Development (MOHCD) |
| <b>EXECUTIVE SUMMARY</b>  |  |
| <b>Legislative Objectives</b>   |  |
| <p>The proposed resolution would authorize the Mayor's Office of Housing and Community Development (MOHCD) to submit an application to the U.S. Department of Health and Human Services (HHS) Federal Property Assistance Program (FPAP) to acquire the property located at 1064 and 1068 Mission Street for use in constructing permanent supportive housing for formerly homeless San Franciscans.</p>  |  |
| <b>Key Points</b>   |  |
| <ul style="list-style-type: none"> <li>• 1064 and 1068 Mission Street are owned by the U.S. Department of Health and Human Services. If MOHCD's FPAP application is approved, MOHCD will purchase the property for \$1.00.</li> <li>• The City would use the site to develop up to 250 units of permanent supportive housing for homeless persons in two buildings. Building A would offer 150 units for formerly homeless single adults, and Building B would offer 100 units for formerly homeless seniors.</li> <li>• MOHCD expects that the development team would (1) complete design development by May 2018, (2) 50 percent construction documents by August 2018, (3) procure construction management services by November 2018, and (4) complete construction documents by January 2019. MOHCD anticipates that entitlements and environmental review would be completed by the end of 2019. Construction is expected to commence in mid-2020 and be completed by mid-2022.</li> </ul>   |  |
| <b>Fiscal Impact</b>  |  |
| <ul style="list-style-type: none"> <li>• If MOHCD is unable to place the property into use within three years of the deed transferring (or approximately 2020), then the City will owe the U.S. Department of Health and Human Services 1/360<sup>th</sup> of the then market value of the property for each month of non-use.</li> <li>• Since the estimated current market value of the property is approximately \$35,000,000, the City would owe HHS an estimated \$2,333,333 if the property is put into use after five years (approximately 2022, the anticipated construction completion date), or estimated \$4,666,667 if there are unanticipated delays of two years resulting in a development process of seven years to 2024. The source of funds for the acquisition cost would be dedicated affordable housing funds, such as Inclusionary Housing fee revenue.</li> <li>• Development of Buildings A and B is estimated to cost \$76,843,004 and \$50,181,559, respectively. The source of funds would be a combination of capital sources, none of which would require Board of Supervisors appropriation approval. However, the issuance of tax-exempt bonds by the City for construction financing would require approval by the Board of Supervisors.</li> </ul> |  |
| <b>Recommendation</b>   |  |
| <ul style="list-style-type: none"> <li>• Approve the proposed resolution.</li> </ul>  |  |

## MANDATE STATEMENT

City Administrative Code Section 10.170(b) states that, for grants of \$5,000,000 or more, the department head shall submit a resolution articulating the grant application to the Board of Supervisors at least 60 days prior to the grant deadline for review and approval.

## BACKGROUND

The Federal Property Assistance Program (FPAP) transfers surplus federal property to eligible local governments and non-profit organizations for various public benefit purposes. The McKinney-Vento Homeless Assistance Act uses the FPAP structure to prioritize the conveyance of surplus federal properties to providers of homeless assistance services.

In January 2017, the U.S. General Services Administration issued a Notice of Determination of Homeless Suitability and a Notice of Surplus Determination for the property at 1064 and 1068 Mission Street, which is under the jurisdiction of the U.S. Department of Health and Human Services (HHS). 1064 Mission Street contains a 1.1-acre parking lot currently leased to City Park for public parking. The lease is set to expire in September 2017. 1068 Mission Street contains 0.049 acres of land and a vacant three-story building with 6,310 gross square feet of space.

Because the U.S. Department of Housing and Urban Development (HUD) determined that the property is suitable for use as a facility to assist the homeless, homeless-serving interests have priority over other uses.

Applications to acquire the property are due to HHS by June 1, 2017. HHS evaluates applications based on (a) the extent of homeless services offered; (b) demand for homeless services in the community; (c) the amount of time necessary for the program to become operational; (d) demonstrated prior success in operating similar programs; and (e) financial ability to operate the program. Although the date of the award is not certain, HHS has 30 days to complete their review of applications and make a recommendation. Following the recommendation by HHS, the U.S. General Services Administration would negotiate the sale transaction with the selected applicant.

The City has not previously applied for property through FPAP. Based on the 2015 Point-in-Time Homeless Count, there are an estimated 6,700 homeless individuals in San Francisco of whom approximately 1,700 are chronically homeless.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would authorize the Mayor's Office of Housing and Community Development (MOHCD) to submit an application to the U.S. Department of Health and Human Services Federal Property Assistance Program to acquire the property located at 1064 and 1068 Mission Street for use in constructing permanent supportive housing for formerly homeless San Franciscans.

If MOHCD is awarded the property and unable to place it into use as supportive housing for formerly homeless people within three years of the deed transferring the property to the City,

then the City will pay HHS 1/360<sup>th</sup> of the then market value of the property for each month of non-use. Under the proposed resolution, further Board of Supervisors approval for MOHCD to accept 1064 and 1068 Mission Street from HHS is not required. However, MOHCD would need to obtain Board of Supervisors approval prior to accepting the property if there are extraordinary conditions of liability or additional unforeseen costs imposed by the federal government.

### **Project Description**

If awarded the property, the City would use the site to develop up to 250 units of permanent supportive housing for homeless persons. The development would be comprised of two buildings. Building A would face Mission Street and offer 150 units of permanently supportive housing for formerly homeless single adults, with no parking, in a mid-rise structure of no more than 85 feet in height. The ground floor would offer resident-serving spaces, including a community room with kitchen, and offices for the staff providing property management and resident services. Studio apartments of approximately 350 square feet would populate the upper floors. Building B would face Stevenson Alley and be similar in function to Building A, with some design features added to further support aging in place for formerly homeless residents who would be age 62 or older. Similarly, this building would have no parking and offer resident serving amenities on the ground floor, with studio apartments on the upper floors. Building B would offer 100 units and be up to 65 feet in height. Design concerns related to the adjacency to the Federal Appellate Court, related to security, may need to be incorporated and could require a reduction in the number of units.

### **Project Timeline**

If the City is awarded the property, MOHCD would issue a request for proposals (RFP) for a development team to develop the permanent supportive housing project for formerly homeless persons. According to Ms. Mara Blitzer, Director of Housing Development at MOHCD, MOHCD expects that the development team would (1) complete design development by May 2018, (2) 50 percent construction documents by August 2018, (3) procure construction management services by November 2018, and (4) complete construction documents by January 2019. MOHCD anticipates that entitlements and environmental review would be completed by the end of 2019. Construction is expected to commence in mid-2020 and be completed by mid-2022.

## **FISCAL IMPACT**

### **Property Acquisition**

According to Mr. Benjamin McCloskey, Deputy Director of Finance and Administration at MOHCD, MOHCD anticipates that the property would transfer to the City for \$1 if HHS awards rights to the property to the City. However, as noted above, if MOHCD is unable to place the property into use within three years of the deed transferring from HHS to the City, then the City will owe HHS 1/360<sup>th</sup> of the then market value of the property for each month of non-use. According to Mr. McCloskey, the estimated current market value of the property is

approximately \$35,000,000, and MOHCD estimates that it will take five years from the date of transfer to put the property into use. Therefore, assuming the City is able to put the property into use after five years and the property value is approximately \$35,000,000, the City would owe HHS approximately \$2,333,333.<sup>1</sup> Estimating conservatively, with unanticipated delays of two years resulting in a development process of seven years, the payment to HHS would be approximately \$4,666,667.<sup>2</sup>

According to Mr. McCloskey, the source of funds for the acquisition cost (the amount that the City would owe HHS for putting the property into use after three years, as noted above) would be dedicated affordable housing funds, such as Inclusionary Housing fee revenue. Additionally, if the City retains the existing parking function on the site prior to construction, MOHCD anticipates covering holding costs and potentially generating additional revenue to offset acquisition/predevelopment costs of the project.

### Development Costs

Development of Building A is estimated to cost \$76,843,004 and would be funded by a combination of capital sources as shown in Table 1 below.

**Table 1: Financing Plan for Building A – Single Adults – 150 Units**

| Source   | Value               | Interest Rate | Term     | Per Unit         |
|--|---------------------|---------------|----------|------------------|
| Inclusionary Housing Fee   | \$30,358,618        | 3.0%          | 55 years | \$202,391        |
| No Place Like Home   | 15,000,000          | 3.0%          | 0 year   | 100,000          |
| Affordable Housing Program from the Federal Home Loan Bank of SF | 1,924,000           | 0.0%          | 30 years | 12,827           |
| Deferred Developer Fee   | 1,014,000           | --            | --       | 6,760            |
| Developer Capital Contribution                                   | 500,000             | --            | --       | 3,333            |
| Limited Partner Equity   | 28,046,386          | --            | --       | 186,976          |
| <b>Total</b>   | <b>\$76,843,004</b> |               |          | <b>\$512,287</b> |

Development of Building B is estimated to cost \$50,181,559 and would be funded by a combination of capital sources as shown in Table 2 below.

**Table 2: Financing Plan for Building B – Seniors – 100 Units**

| Source   | Value               | Interest Rate | Term     | Per Unit         |
|--|---------------------|---------------|----------|------------------|
| Inclusionary Housing Fee   | \$20,100,009        | 3.0%          | 55 years | \$201,000        |
| No Place Like Home   | 4,000,000           | 3.0%          | 0 year   | 40,000           |
| Affordable Housing Program from the Federal Home Loan Bank of SF | 1,584,000           | 0.0%          | 30 years | 15,840           |
| Limited Partner Equity   | 24,497,550          | --            | --       | 244,976          |
| <b>Total</b>   | <b>\$50,181,559</b> |               |          | <b>\$501,816</b> |

The Inclusionary Housing Program is administered by MOHCD and use of Inclusionary Housing Fee revenue for development of permanent supportive housing is not subject to Board of

<sup>1</sup> 24 months \* 1/360 \* \$35,000,000 = \$2,333,333

<sup>2</sup> 48 months \* 1/360 \* \$35,000,000 = \$4,666,667

Supervisors appropriation approval. Therefore, funding for the proposed project would not be subject to future Board of Supervisors approval. However, if the City were to enter into a ground lease with the developer, the ground lease would be subject to Board of Supervisors approval. According to Ms. Blitzer, the City would act as the issuer of tax-exempt bonds, which would be used for construction financing, and the bond issuance would require approval by the Board of Supervisors.

**RECOMMENDATION**

Approve the proposed resolution.

|  |   |
|--|---|
| <b>Item 7</b><br><b>File 17-0522</b>   | <b>Department: Real Estate Division</b><br><b>Mayor's Office of Housing and Community Development</b> |
| <b>EXECUTIVE SUMMARY</b>   |   |
| <p style="text-align: center;"><b>Legislative Objectives</b></p> <ul style="list-style-type: none"> <li>• The proposed resolution would authorize the Real Estate Division, on behalf of the Mayor's Office of Housing and Community Development (MOHCD), to acquire real property located at 772 Pacific Avenue from Shew Yick Trust One (Trustees Robert Yick and Andy Ting), Robert Yick Trust Two (Trustee Joseph Yick) and Robert Yick Non-Exempt Assets Trust (Trustee Mark Shustoff), for the purchase at below fair market value of \$5,000,000 to develop affordable housing.</li> </ul> <p style="text-align: center;"><b>Key Points</b></p> <ul style="list-style-type: none"> <li>• The City was approached by the current owners of the property who offered to sell it at below market rate. MOHCD evaluated the property and found that it was suitable for affordable housing. MOHCD is anticipating the property would be developed for approximately 60 permanently affordable housing units. Housing construction is anticipated to begin in early 2022.</li> <li>• Prior to development of the affordable housing, the property will continue to be used for a restaurant, which will remain in operation until the end of the restaurant lease on December 31, 2021.</li> <li>• The City will take the property "as-is." A 1,000-gallon gasoline underground storage tank remains on the site. No testing of the tank or soils has occurred to determine whether it has leaked. When construction begins in 2022, the City will be taking on the potential for any future remediation related to the tank and its removal.</li> </ul> <p style="text-align: center;"><b>Fiscal Impact</b></p> <ul style="list-style-type: none"> <li>• The appraisal reports a fair market value of \$5,400,000. The appraisal notes that this value assumes that there is no soil remediation required and that the cost of removal of the tank is fairly nominal as part of the demolition of the larger improvements on the site.</li> <li>• The City will receive monthly rent of \$22,500 from the on-site restaurant, which will total \$1,237,500 over the remainder of the lease.</li> </ul> <p style="text-align: center;"><b>Policy Consideration</b></p> <ul style="list-style-type: none"> <li>• Remediation costs for a potential leak in the underground storage tank vary widely depending on the extent of the contamination but could add \$150,000 or more (including the cost of removal and disposal of the storage tank) to the construction costs. Assuming remediation costs of \$150,000, the total cost to the City for this acquisition, including purchase costs, is \$5,170,000 which is \$230,000 below the appraised market rate of \$5,400,000.</li> </ul> <p style="text-align: center;"><b>Recommendation</b></p> <ul style="list-style-type: none"> <li>• Approve the proposed resolution.</li> </ul> |   |



## MANDATE STATEMENT

City Administrative Code Section 23.3 states that before the Board of Supervisors approves any acquisition of real property, the Director of Real Estate shall determine the fair market value of such real property based on a review of available and relevant data. If the fair market value exceeds \$10,000, the Director of Real Estate shall obtain an appraisal of the subject property. If the appraisal determines the fair market value of the real property exceeds \$200,000, the Director of Real Estate shall obtain an appraisal review for such appraisal. Both the appraisal and appraisal review shall have effective dates not earlier than nine months before the legislation to acquire the subject property is submitted to the Board of Supervisors.

## BACKGROUND

The property at 772 Pacific Avenue, owned by Shew Yick Trust One (Trustees Robert Yick and Andy Ting), Robert Yick Trust Two (Trustee Joseph Yick) and Robert Yick Non-Exempt Assets Trust (Trustee Mark Shustoff), is located on the north side of Pacific Avenue between Stockton Street and Grant Avenue in the Chinatown neighborhood of San Francisco. The property consists of a single parcel of land totaling 9,219 square feet. The property was formerly used to house an auto garage and a stainless steel fabrication shop. The property currently consists of a one-story plus mezzanine building which was built in 1919, and is now the site of the New Asia restaurant. The property is zoned Chinatown Residential - Neighborhood Commercial District and it sits on a block with both residential and commercial uses.

According to Ms. Sandi Levine, Project Manager in the City's Real Estate Division, the property came to the City's attention for possible purchase when the owners approached City officials and offered to sell it at below market rate. The property is located across the street from two other affordable housing projects which are currently managed by Chinatown Community Development Corp.

According to Ms. Mara Blitzer, Director of Housing Development for the Mayor's Office of Housing and Community Development (MOHCD), an evaluation was made of the property, its zoning and prior land use as well as the financing needs of the proposed project. The analysis found that the property would be suitable for affordable housing. MOHCD is anticipating the property would be developed for approximately 60 permanently affordable housing units at the location. The New Asia restaurant has a lease with the property owner through December 31, 2021 and will be allowed to continue operations until that time.

Construction on the affordable housing project is scheduled to occur in early 2022 shortly after the restaurant lease ends. Ms. Blitzer notes that in order to secure a property in a location where MOHCD would like to make an investment but for which no funds are available to begin construction right away, MOHCD is willing to "land bank" sites until such construction funds become available. Ms. Blitzer added that the terms of the existing lease with the New Asia restaurant and the estimates of availability of future funds aligned well in the case of this property.

According to Ms. Blitzer, the future housing construction assumes a building eight stories in height with residential uses on the 2nd through 8th floors and ground floor commercial. This also assumes a granting of the affordable housing density bonus. Housing is estimated to be a mix of 60 percent studio and 40 percent 1-bedroom units with their own bathroom and kitchen. The building would house approximately 150 people depending on the individual housing mix and assuming a maximum household size of 2 persons in a studio and 3 persons in a 1-bedroom. There will be on-site open space on the roof and a second floor terrace. There will be no parking.

The San Francisco Planning Department found this project, on balance, to be in conformity with the City General Plan.

### **DETAILS OF PROPOSED LEGISLATION**

The proposed resolution would authorize the Real Estate Division, on behalf of the Mayor's Office of Housing and Community Development, to acquire 772 Pacific Avenue from Shew Yick Trust One (Trustees Robert Yick and Andy Ting), Robert Yick Trust Two (Trustee Joseph Yick) and Robert Yick Non-Exempt Assets Trust (Trustee Mark Shustoff), for the purchase price of \$5,000,000 for use in constructing affordable housing for San Franciscans.

The New Asia restaurant currently on site will remain in operation until the end of its lease on December 31, 2021.

#### **Property Appraisal**

In a report dated April 19, 2017, R. Blum + Associates (retained by the San Francisco Real Estate Division) appraised the fair market value of the property at \$5,400,000, or \$400,000 more than the property purchase price of \$5,000,000. The appraised value was established by sales comparisons with six properties across an area bounded by Franklin Street to the West, Filbert Street to the North, Columbus Avenue and Kearny Street to the East and Market Street to the South. The appraisal concludes that the purchase price of \$5,000,000 would be slightly under the estimated market value of \$5,400,000.

Mateo Advisors, LLC (retained by the San Francisco Real Estate Division), performed an appraisal review dated May 9, 2017. The review concluded that the appraisal value is reasonable and supported based on the analysis performed. It also found that the appraisal conformed to the Uniform Standards of Professional Appraisal Practice of the Appraisal Foundation.

## FISCAL IMPACT

Total estimated costs to the City to purchase the property are \$5,020,000 as shown below. According to Mr. Benjamin McCloskey, Deputy Director of Finance and Administration of MOHCD, the source of the funds for purchase and any closing costs is inclusionary housing fees.

|  |                    |
|--|--------------------|
| <b>Source of Funds</b>                             |                    |
| Inclusionary Housing Fees                          | \$5,020,000        |
| <b>Use of Funds</b>                                |                    |
| Property Purchase                                  | \$5,000,000        |
| Title Insurance, Escrow Fees & Other Miscellaneous | <u>20,000</u>      |
| <b>Total</b>                                       | <b>\$5,020,000</b> |

### Restaurant Income

The New Asia restaurant is to pay monthly rent to the City over the remainder of its lease through December 31, 2021. The current monthly rent is \$22,500, amounting to a total income to the City of \$1,237,500 over the 55 months remaining in the lease period. There are no contractual provisions for the rent rate to be increased during the remaining lease period.

### Real Property Transfer Taxes and Property Taxes

According to the appraisal, the 2016-2017 taxes for the property are \$35,853. According to Mr. John Updike, Director of Real Estate, the restaurant will owe City Possessory Interest Taxes post-acquisition.

The seller will pay the Real Property Transfer Tax, estimated to be \$112,500.

## POLICY CONSIDERATION

### Possible Site Contamination from Underground Storage Tank

The appraisal report by R. Blum + Associates notes in its “Extraordinary Assumption” section that the subject property is impacted by an underground storage tank (UST). According to the Phase I environmental assessment of the site prepared by EBI Consulting on November 21, 2016, San Francisco Fire Department records indicate that a 1,000-gallon gasoline UST was installed in 1953 and permitted for continued operation in 1965. There were no records of its removal.<sup>1</sup> A site assessment dated March 15, 2017 by TR&A, Inc. (a construction and claim consultant retained by one of the current property owners) found a hinged fuel tank fill under the sidewalk in front of the property suggesting that the UST was abandoned in place (the tank, itself, was not seen). The appraisal notes that no testing of the tank or soils has occurred to determine whether it has leaked. The estimated market value of \$5,400,000 stated in the

<sup>1</sup> p.24.

appraisal report assumes that there is no soil remediation required and that the cost of removal of the tank is fairly nominal as part of the demolition of the larger improvements on the site.

The property is being sold to the City in “as is” condition. When construction on the affordable housing begins in 2022, the City will be responsible for any future remediation costs related to the tank and its removal.

According to Mr. Stanley DeSouza, Division Manager for the Site Assessment and Remediation Division of the Department of Public Works, there is a likelihood that there is some sort of leakage considering the age of the UST and the fact that it would have been single-walled. The extent of any leaks would determine the need for remediation and monitoring measures which would affect the overall cost. Mr. DeSouza said that UST extractions and disposals, by themselves, can cost anywhere from \$30,000 to \$80,000. The cost of additional site remediation needs due to a leak from a UST can vary widely but have the potential to bring costs up to around \$150,000 or more (including the cost of UST removal and disposal), depending on the extent of the contamination.<sup>2</sup>

If the eventual remediation cost were \$150,000, the total cost to the City for this acquisition, including purchase costs, is \$5,170,000, \$230,000 less than the appraised value of \$5,400,000.

## RECOMMENDATION

Approve the proposed resolution.

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<sup>2</sup> These are generalized estimates to aid in consideration of the possible fiscal impacts of the presence of the UST in this proposal. They are in no way specific to the conditions and circumstances of the property at 772 Pacific Avenue, which have not been fully evaluated. The estimates also do not consider other possible sources of contamination.

|  |  |
|--|--|
| <p><b>Items 12, 13 and 14</b><br/> <b>Files 17-0468, 17-0464 and 17-0471</b></p> | <p><b>Departments:</b><br/>                 Controller, Office of Public Finance<br/>                 Real Estate Division<br/>                 Public Works</p> |
|--|--|

**EXECUTIVE SUMMARY**

**Legislative Objectives**

- **File 17-0468:** The proposed ordinance would authorize the execution and delivery of Certificates of Participation (COPs) on a tax-exempt or taxable basis for a not to exceed \$321,765,000 to fund a portion of the development costs, including construction, improvement and related furniture, fixture and equipment (FF&E), technology and moving costs for the 1500 Mission Street office building; authorize issuance of commercial paper notes in advance of the delivery of the COPs; authorize selection of Trustee by Director of Public Finance; approve the form and execution of all required documents including the Trust Agreement, Property Lease, Lease Agreement, Purchase Contract, Official Notice of Sale and Notice of Intention to Sell COPs, Preliminary Official Statement, Official Statement and Continuing Disclosure Certificate; approve and ratify actions and modifications by City officials to sell the COPs; and declare City’s intent to reimburse expenditures.
- **File 17-0464:** Supplemental appropriation ordinance for \$321,765,000 of proceeds from COPs to fund the development costs of the 1500 Mission Street office building and related furniture, fixture or other equipment, technology and moving costs and placing the total \$321,765,000 of proceeds on Controller’s Reserve pending the sale of the COPs.
- **File 17-0471:** Resolution ratifying the Conditional Purchase Agreement for the City’s Acquisition of an office project at 1500 Mission Street and authorizing the Director of Property and City staff to proceed with the proposed office project; confirming the City’s authorization to issue commercial paper and/or certificates of participation to pay for the land acquisition and complete the proposed office project; adopting environmental findings under the California Environmental Quality Act (CEQA); and making findings of consistency with the General Plan and with the eight priority policies of Planning Code Section 101.1.

**Key Points**

- On December 9, 2014, the Board of Supervisors approved a Conditional Land Disposition and Acquisition Agreement with Related to develop a City-owned office building at 1500 Mission Street, subject to environmental approval. The City intended to sell three City-owned buildings and finance the balance of the costs to construct the new City office building with commercial paper and Certificates of Participation (COPs).
- On March 21, 2017, the Board of Supervisors approved the sale of three City-owned properties at (a) 1660 and 1680 Mission Street for \$52,000,000 and (b) 30 Van Ness for \$70,000,000 for total sales proceeds of \$122,000,000. Escrow has now closed on these properties. As the costs were lower than projected the City actually received net proceeds of \$97,069,836 from these sales, instead of \$93,935,000, an increase of \$3,134,836.

- On March 23, 2017, the Planning Commission approved actions, which are subject to Board of Supervisors final approval for a new City office building at 1500 Mission Street.

#### **Fiscal Impact**

- The City would pay Related, the developer, \$56,180,772 under the previously approved Conditional Purchase and Sale Agreement, for the land acquisition and predevelopment costs. The comparable current market value of this acquisition is \$74,000,000 based on an appraisal completed in April 2017 by R. Blum+ Associates for the Real Estate Division, such that the City's cost is 76% of the current market value. The Construction Management Agreement is estimated at \$270,510,181. The total maximum costs for land acquisition, design and construction of the new City office building is \$326,690,953.
- Office of Public Finance is requesting authorization to issue a total not to exceed \$321,765,000 of COPs, including an estimated par amount of \$314,131,000.

#### **Policy Consideration**

- The requested \$29,397,433 for FF&E, technology and moving expenses is \$17,099,033 or 139% more than previously estimated, with no details or bids provided.
- The proposed new office building will create an estimated net increase of 154,760 square feet of new space. With such significant increases in space, the amount of leased space and lease costs in the Civic Center should be reduced, resulting in the termination of existing City leases, as the Board of Supervisors were advised in 2014 when the 1500 Mission Street office building was approved.

#### **Recommendations**

- Amend the proposed ordinance (File 17-0464) to reflect the recommended savings shown in Table 3, based on the proceeds from the sale of the three City buildings resulting in an additional \$3,134,836 for the Project Fund.
- Amend the proposed ordinance (File 17-0464) to place \$28,397,433 of the requested \$29,397,433 on Budget and Finance Committee Reserve for FF&E, technology and moving to allow \$1,000,000 to be released now. The \$28,397,433 on reserve should not be released, pending a report that identifies (a) number of employees and amount of space currently used by each City department, (b) number of employees and amount of space proposed to be used by each City department in the new City building, and (c) existing City leases that will be terminated, existing City leases that will be backfilled or reused, including square footage of leases, rent savings and any additional costs. The City should maximize the leases terminated and City departments and employees relocated into the new City office building, as originally proposed to the Board of Supervisors when this project was approved. To request release of the \$28,397,433 being placed on reserve, Public Works should maximize the City's existing furniture for reuse and moved into the new building and minimize additional City expenses. Details should be provided and bids obtained prior to requesting the release of a reduced amount of funding for this purpose.
- Approve the proposed ordinance (File 17-0464), as amended.
- Approve the proposed ordinance (File 17-0468) and resolution (File 17-0471).

## MANDATE STATEMENT

City Charter Section 9.118(b) states that any contract entered into by a department, board or commission that (1) has a term of more than ten years, (2) requires expenditures of \$10 million or more, or (3) requires a modification of more than \$500,000 is subject to Board of Supervisors approval.

City Administrative Code Section 10.62(b) states that the Board of Supervisors may authorize the issuance of Certificates of Participation (COPs) and other lease financing debt to fund capital projects provided the annual debt service cost of such outstanding indebtedness does not exceed 3.25% of discretionary revenue as determined by the Controller and Director of Public Finance. Administrative Code Section 10.62(c) states that the Director of Public Finance may issue tax-exempt and taxable commercial paper notes to provide interim funds to finance the acquisition, construction and rehabilitation of capital improvements and capital equipment, subject to the project's and financing plan's approval by the Board of Supervisors and Mayor.

City Charter Section 9.105 states that amendments to the Annual Appropriation Ordinance are subject to Board of Supervisors approval by ordinance after the Controller certifies the availability of funds.

## BACKGROUND

### Development of City Office Building at 1500 Mission Street

On December 9, 2014, the Board of Supervisors approved a Conditional Land Disposition and Acquisition Agreement (Agreement) with Related California Urban Housing, LLC (Related)<sup>1</sup> to develop a new City-owned office building at 1500 Mission Street, subject to environmental review and approval based on total estimated project costs of \$338,989,353. Related plans to develop this site to include (a) an approximately 463,300 gross square foot 16-story City-owned office building along 11<sup>th</sup> Street and (b) a 39-story, 550 residential unit development with ground floor retail, at Mission Street and South Van Ness Avenue (Ordinance 254-14). To fund the City's new office building project, the City intends to use the proceeds from the sale of three other City-owned buildings and finance the balance with commercial paper and Certificates of Participation (COPs).

On March 21, 2017, the Board of Supervisors approved the sale of three City-owned properties at (a) 1660 and 1680 Mission Street for \$52,000,000 (File 17-0213) and (b) 30 Van Ness for \$70,000,000 (File 17-0214) for total sales proceeds of \$122,000,000. On May 2, 2017, the Board of Supervisors approved a supplemental appropriation of \$122,000,000 from the sale of these three City buildings, as summarized in Table 1 below (File 17-0201; Ordinance No. 094-17).

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<sup>1</sup> Related California Urban Housing LLC created a subsidiary, Goodwill SF Urban Development LLC, to acquire and develop this site.

**Table 1: Previously Approved Supplemental Appropriation**

| <b>Sources and Uses</b>  | <b>Total</b>         |
|--|----------------------|
| <b>Sources</b>   |                      |
| Sales proceeds from 30 Van Ness and 1660 and 1680 Mission Street             | \$122,000,000        |
| <b>Total Sources</b>   | <b>\$122,000,000</b> |
| <b>Uses</b>  |                      |
| Sales Commissions and Expenses   | 1,000,000            |
| Defeasance of Series 2001A and 2007A COPs                                    | 27,065,000           |
| Balance to Controller's Capital Project Fund Account for new Office Building | 93,935,000           |
| <b>Total Uses</b>  | <b>\$122,000,000</b> |

According to Mr. John Updike, Director of Real Estate, escrow closed on the two properties at 1660 and 1680 Mission Street on May 1, 2017 and on 30 Van Ness on May 5, 2017. As the sales commissions and defeasance costs were slightly lower than projected, the City actually received net proceeds of \$97,069,836 from these sales, instead of \$93,935,000, an increase of \$3,134,836.

As part of these sale transactions, the City entered into leases for these three properties which expire on April 30, 2020, with options to extend for two additional one-year terms. The initial termination date of these leases coincides with the anticipated completion of a new City office building at 1500 Mission Street, at which time the employees in these three buildings will relocate to the new City office building at 1500 Mission Street. If the Board of Supervisors does not approve the proposed resolution to develop a new City office building at 1500 Mission Street, the City employees located in these three office buildings will need to be relocated at the end of these leases.

Construction of the 1500 Mission Street City office building is anticipated to begin in October 2017 and extend for two years. The development is anticipated to be substantially complete by November 2019. City staff would then move into this building through the spring of 2020.

### **Approval of Planning and Environmental Authorizations**

On March 23, 2017, the Planning Commission

(a) Certified the Final Environmental Impact Report (FEIR) and adopted California Environmental Quality Act (CEQA) findings for the 1500 Mission Street projects;

(b) Recommended a General Plan Amendment to revise the height and bulk limits, allow for additional office use parking and permit office uses above the fourth floor for non-City occupancy for this project;

(c) Recommended a Planning Code Amendment to create the 1500 Mission Street Special Use District to modify the height and bulk limits and related office enhancements while requiring the developer to provide 20% affordable housing units, instead of the required 13.5%;

(d) Adopted Shadow Findings that would not adversely affect public open space; and

(e) Approved a Downtown Project Authorization, which approves the office and residential development projects as proposed, subject to a lengthy list of conditions of approval and the



Board of Supervisors approval of the General Plan Amendment and the Planning Code Amendment.

On May 9, 2017, the Board of Supervisors approved the first reading on two ordinances (Files 17-0408 and 17-0348) to approve the above-noted General Plan Amendments and the Planning Code Amendments, incorporating the CEQA findings, as required for the 1500 Mission Street project.

### **Certificates of Participation**

Certificates of Participation (COPs) are a form of long-term debt which are sold to investors for a portion of the lease revenues from a specific City-owned property, such that the investors “participate” in receiving lease revenues in the form of debt service payments. Although COPs generally have higher interest rates and are therefore more expensive than general obligation bonds, general obligation bonds require San Francisco voters’ approval whereas COPs can be approved by the Board of Supervisors and Mayor. Under the COP structure, the City leases a City-owned property to a trustee in consideration for a one-time lease payment from the trustee to the City that is equal to the proceeds from the issuance of the COPs. The trustee subsequently subleases the same City-owned property back to the City in return for semi-annual rent payments equal to the debt service (including principal and interest) due on the COPs. This lease-sublease structure is known as an asset transfer model. Under this asset transfer model, the City-owned property leased to the trustee serves as collateral to the trustee on the issued COPs. After the COPs are fully repaid by the City, the City-owned property, previously leased to the trustee, reverts back to the City.

## **DETAILS OF PROPOSED LEGISLATION**

**File 17-0468:** The proposed ordinance would

- Authorize the execution and delivery of Certificates of Participation (COPs) on a tax-exempt or taxable basis for a not to exceed \$321,765,000 to fund a portion of the development costs, including construction, improvement and related furniture, fixture and equipment (FF&E), technology infrastructure and moving costs for the 1500 Mission Street office building;
- Authorize the issuance of commercial paper<sup>2</sup> notes in advance of the delivery of the COPs;
- Approve the form of Trust Agreement between the City and County of San Francisco (City) and the Trustee (including certain indemnities contained therein);
- Authorize the selection of the Trustee by Director of Public Finance;

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<sup>2</sup> The City’s maximum authorization for commercial paper is \$250 million. Ms. Nadia Sesay, the Director of the Office of Public Finance advises that as of April 2017, \$218 million of the \$250 million is outstanding. However, the pending issuances of COPs for the Moscone Expansion and HopeSF will free up commercial paper capacity.

- Approve the respective forms of a Property Lease and a Lease Agreement, each between the City and the Trustee for the lease and lease back of 1500 Mission Street City property and facilities;
- Approve the forms of Purchase Contract, Official Notice of Sale and Notice of Intention to Sell COPs;
- Direct the publication of the Notice of Intention to Sell COPs;
- Approve the form of the Preliminary Official Statement and the form and execution of the Official Statement relating to the sale of the COPs;
- Approve the form of the Continuing Disclosure Certificate;
- Grant general authority to City officials to take necessary actions in connection with the authorization, execution, sale and delivery of the COPs;
- Approve modifications to documents and agreements;
- Declare the City's intent to reimburse certain expenditures; and
- Ratify previous actions taken in connection therewith.

**File 17-0464:** The proposed ordinance would appropriate \$321,765,000 of proceeds from COPs to fund the development costs of the 1500 Mission Street office building and related furniture, fixture and equipment, technology and moving costs and place the total \$321,765,000 on Controller's Reserve pending the sale of the COPs.

**File 17-0471:** The proposed resolution would

- Ratify the Conditional Purchase Agreement for the City's acquisition of an office project at 1500 Mission Street and authorize the Director of Property and City staff to proceed with the proposed office project.
- Confirm the City's authorization to issue commercial paper and/or Certificates of Participation to pay for the land acquisition and complete the proposed office project.
- Adopt environmental findings under the California Environmental Quality Act (CEQA).
- Make findings of consistency with the City's General Plan and the eight priority policies of Planning Code Section 101.1.

As noted above, on December 9, 2014, the Board of Supervisors approved a Conditional Land Disposition and Acquisition Agreement with Related to develop a new City-owned office building at 1500 Mission Street, subject to final environmental review and final approval by the Board of Supervisors. As discussed above, on May 9, 2017<sup>3</sup>, the Board of Supervisors approved the first readings on Files 17-0408 and 17-0348, related to the General Plan, Planning Code and environmental requirements for the subject project. As provided in the previous Conditional Land Disposition and Acquisition Agreement, the Board of Supervisors must now either

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<sup>3</sup> The second and final approval of these ordinances is scheduled for the May 16, 2017 Board of Supervisors meeting.

(a) Ratify the Conditional Purchase Agreement and proceed with the City’s acquisition of the office parcel and developer’s completion of the proposed office project for the City, or

(b) Reject the Conditional Purchase Agreement and not proceed with the City’s acquisition of the office parcel solely on the basis of the environmental impacts of the proposed office project disclosed in the environmental review documents that have not been adequately mitigated or overridden under CEQA.

The proposed resolution would ratify the Conditional Purchase Agreement and authorize the Director of Property and City staff to proceed with the City’s acquisition of 1500 Mission Street and complete the proposed office project in accordance with the terms of the Conditional Purchase Agreement.

Under the proposed Conditional Purchase Agreement, Related would sell the City the fully-entitled post-CEQA approved property at 1500 Mission Street at a cost of \$32,332,524, including real estate commissions and fees. If the proposed resolution is approved, it is anticipated that the City would acquire this property on approximately July 1, 2017. Concurrent with the acquisition of the property, the City would also be authorized to enter into a Construction Management Agreement with Related to manage and complete the construction of a new City office building on this site.

As shown in Table 2 below, the City would pay Related an estimated \$56,180,772 under the previously approved Conditional Purchase and Sale Agreement, for the land acquisition and predevelopment costs, including environmental documents and approvals. The comparable current market value of this acquisition is \$74,000,000 based on an appraisal completed in April 2017 by R. Blum+ Associates for the Real Estate Division, such that the City’s cost is 76% of the current market value. The estimated costs of the Construction Management Agreement is \$270,510,181, with total maximum costs for the land acquisition, design, development and construction of the new City office building at 1500 Mission Street of \$326,690,953.

**Table 2: Total Cost of 1500 Mission Street Project**

|   |                      |
|---|----------------------|
| Conditional Purchase and Sale Agreement | \$56,180,772         |
| Construction Management Agreement       | <u>270,510,181</u>   |
| <b>Total Project Cost</b>               | <b>\$326,690,953</b> |

When the City acquires the land and enters into the Construction Management Agreement for \$270,510,181 with Related, Related will enter into a general construction contract, which is structured as a Guaranteed Maximum Price (GMP). Related, as the developer and construction manager, has contracted with Skidmore, Owings and Merrill as the architect and will enter into a GMP with a general contractor when the City acquires the land. If at any point, Related believes the total project cost will exceed \$326,690,953, Related must notify the City to discuss alternatives to design, square footage, finishes or other changes to be made so as not to exceed the \$326,690,953. Under these agreements, Related has no authority to increase the budget beyond \$326,690,953. Construction is anticipated to commence in the fall of 2017 and extend for approximately 26 months or through the end of 2019.

The proposed resolution would also adopt the CEQA findings and General Plan and Planning Code Section 101.1 findings from the General Plan amendment legislation and incorporate such findings in this resolution.

**FISCAL IMPACT**

In 2014, the Board of Supervisors approved nonrefundable payments to Related of \$1,000,000 for land acquisition and \$250,000 for schematic design. If the proposed resolution is approved, the \$1,250,000 will be credited to the City’s development costs. If the proposed resolution is not approved, the \$1,250,000 will not be refunded by Related.

In 2014, the Board of Supervisors also appropriated \$8,072,300 which was set aside to potentially reimburse Related for architecture, engineering, environmental and professional fees and permits costs. In accordance with the agreements, if the Board of Supervisors does not authorize the issuance of the subject COPs or does not approve the Conditional Purchase Agreement with Related, the City would be responsible for up to \$7,072,300 of costs from the \$8,072,300 appropriated funds to Related for reimbursement of their predevelopment and entitlement costs incurred on this project.

**COPs and Supplemental Appropriation of Funds**

Table 3 below identifies the sources and uses for the current supplemental appropriation (File 17-0464) and the proceeds from the sale of the COPs and recommended amendments. These amendments are recommended because as shown beneath Table 1 above, the proceeds from the sale of the three City buildings resulted in an additional \$3,134,836 for the Project Fund. These additional proceeds reduce the required Project Fund Costs as detailed in Table 4 and shown in Table 3 below from \$231,505,953 to \$228,371,117, a savings of \$3,134,836.

**Table 3: Sources and Uses for COPs**

| Sources and Uses   | Current              | Recommended          |
|--|----------------------|----------------------|
| <b>Sources</b>   |                      |                      |
| COP Par Amount   | \$317,265,000        | \$314,131,000        |
| COP Reserve for Market Uncertainty                         | 4,500,000            | 7,634,000            |
| <b>Total Sources</b>                                       | <b>\$321,765,000</b> | <b>\$321,765,000</b> |
| <b>Uses</b>  |                      |                      |
| - Project Fund Costs                                       | \$231,505,953        | \$228,371,117        |
| - FF&E, Technology Equipment and Moving Costs              | 29,397,433           | 29,397,433           |
| - Controller’s Internal Audit Fund (0.2% of project costs) | <u>653,382</u>       | <u>653,382</u>       |
| <b>Total Project Fund Deposits</b>                         | <b>\$261,556,768</b> | <b>\$257,768,550</b> |
| - Bond Reserve   | 21,832,100           | 21,832,100           |
| - Capitalized Interest and Fees                            | 31,051,471           | 31,051,471           |
| - Bond Issuance Costs                                      | 603,807              | 604,643              |
| - Underwriter’s Discount Fee                               | <u>2,220,854</u>     | <u>2,220,854</u>     |
| <b>Total COP Delivery Expenses</b>                         | <b>\$55,708,232</b>  | <b>\$55,709,068</b>  |
| - Reserve for Market Uncertainty                           | 4,500,000            | 7,634,000            |
| <b>Total Uses</b>  | <b>\$321,765,000</b> | <b>\$321,765,000</b> |

The proposed supplemental appropriation ordinance (File 17-0464) should therefore be amended to reflect the recommended amounts shown in Table 3 above.

### **Sources of Funds**

#### **COP Par Amount**

As shown in Table 3 above, the Office of Public Finance is requesting authorization to issue a total not to exceed \$321,765,000 of COPs, including an estimated par amount of \$314,131,000. To date, the underwriter has not yet been selected. The ordinance (File 17-0468) authorizes the Office of Public Finance to conduct this transaction on a competitive or negotiated basis. The Office of Public Finance anticipates issuing this transaction on a competitive basis. However, Ms. Nadia Sesay, Director of the Office of Public Finance advises that a negotiated sale could occur, if the City's credit rating significantly deteriorates or future market disruptions occur.

According to Ms. Sesay, the City's plan is to finance the initial acquisition and development of the 1500 Mission Street building's expenses from the net sales proceeds from 30 Van Ness and 1660 and 1680 Mission Street, and then to issue commercial paper as interim funding for up to two years, while the project is being constructed, before issuing the COPs. The proposed ordinance (File 17-0468) also authorizes the Office of Public Finance to issue commercial paper to fund the development costs prior to the issuance of the COPs.

Ms. Jamie Querubin in the Controller's Office of Public Finance advises that one issuance of the COPs are anticipated to be sold no earlier than summer 2018 and no later than fall 2019, depending on available commercial paper capacity at a par amount of \$314,131,000. Assuming a 30-year term and an estimated interest rate of 5.5%, the total estimated debt service to the City will be \$660,705,075<sup>4</sup>, which includes \$314,131,000 principal and \$346,574,075 of interest expense. The estimated average annual debt service on the COPs is \$21,044,000, which would be repaid by the City over the 30-year term, subject to Board of Supervisors annual appropriation approval.

To pay the annual debt service, the tenants that occupy the new City office building would be charged commensurate rental fees. Ms. Querubin estimates the cost per square foot will be approximately \$64 in year one, increasing to \$78 per square foot in the last year of the 30-year term, which includes debt service costs plus operating expenses. Although the composition of all the City tenants to occupy the new 1500 Mission Street building has not been determined, most of the City departments that will occupy 1500 Mission Street do not currently receive General Fund support.

Mr. John Updike, Director of Real Estate advises that new Civic Center leases currently range from approximately \$60 to \$65 per year.<sup>5</sup> Mr. Updike further advises that if the City was to lease office space beginning in 2019, the rate would be at least \$60 per square foot per year

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<sup>4</sup> The \$660,705,075 reflects total gross debt service, including capitalized interest, reserve fund for the final debt service payment and ongoing annual costs of administration (i.e., insurance, trustee fees).

<sup>5</sup> Based on CRBE 2016 fourth quarter data reported by Mr. Updike.

and under a conservative annual escalation of 1% per year, the rate per square foot per year after 30 years would be \$80 per square foot. After 30 years, assuming no major tenant improvements, the cost per square foot for the City-owned 1500 Mission Street would decrease after completing all debt service payments.

### **COP Reserve for Market Uncertainty**

As noted above, the Office of Public Finance anticipates one issuance of the estimated par amount of \$314,131,000 of COPs no earlier than summer 2018 and no later than fall 2019, depending on available commercial paper capacity or in approximately 2.5 years. Given that the interest rates at the time of issuance are not currently known, the Office of Public Finance included \$7,634,000 as a COP Reserve due to market uncertainty. Ms. Sesay advises that the typical range for such a COP Reserve is between 1% and 3% of the par amount of the COPs. The \$7,634,000 represents 2.4% of the estimated par amount of \$314,131,000. If a portion of this COP Reserve for Market Uncertainty is not required, these funds will not be expended.

### **Uses of Funds**

#### **Project Fund Costs**

Based on Public Works' total project development costs of \$326,690,953 and Board of Supervisors previous approvals, as shown in Table 4 below, the net Project Fund cost is \$228,371,117 to be financed with the subject COPs.

**Table 4: Net Project Development Costs**

|   |                       |
|---|-----------------------|
| Land Acquisition Costs  | \$32,332,524          |
| Financing Costs during Predevelopment   | 8,904,313             |
| Architectural and Engineering, Professional Fees and Insurance                              | 15,906,196            |
| Construction Costs/ Fees, Permits & Taxes/ Development Management Fees and Return on Equity | 269,547,920           |
| <b>Total Project Development Costs</b>  | <b>\$326,690,953</b>  |
| FY 2014-15 funds appropriated for land acquisition and design <sup>6</sup>                  | (\$1,250,000)         |
| <b>Total Appropriation Funds for Project Development</b>                                    | <b>\$325,440,953</b>  |
| <b>Net proceeds from the recent sale of 3 properties</b>                                    | <b>(\$97,069,836)</b> |
| <b>Net Project Development Costs</b>  | <b>\$228,371,117</b>  |

Source: Samuel Chui, Public Works and Joshua Keene, Real Estate.

### **FF&E, Technology Equipment and Moving Costs**

In December 2014, when the Board of Supervisors approved the Conditional Land Disposition and Acquisition Agreement with Related to develop a new City office building at 1500 Mission Street, the total estimated cost for furniture, fixtures and equipment (FF&E), technology and moving expenses was \$12,298,400. However, as shown in Table 3 above, the requested

<sup>6</sup> In accordance with the original agreement between the City and Related in 2014, the City, through the Department of Building Inspection, paid Related non-reimbursable \$1,000,000 toward acquisition of the property at 1500 Mission Street and \$250,000 for schematic design.

supplemental appropriation would fund \$29,397,433 for FF&E, technology and moving costs, an increase of \$17,099,033 or 139%. Table 5 below compares the earlier \$12,298,400 estimate with the current \$29,397,433 request for FF&E, technology equipment and moving costs, an increase of \$17,099,033 or 139%.

**Table 5: Comparison of Costs for FF&E, Technology and Moving Expenses**

| Description and Assumptions          | 2014 Costs          | Current Estimated Costs | Increase/(Decrease) Over 2014 Costs |
|--------------------------------------|---------------------|-------------------------|-------------------------------------|
| Workstation Furniture                | \$4,500,000*        | \$6,750,000**           | \$2,250,000                         |
| Ancillary Furniture***               | 0                   | 5,170,140               | 5,170,140                           |
| Moving                               | 5,000,000           | 4,481,168               | (518,832)                           |
| Department of Technology/IT Expenses | 2,798,400           | 10,771,125              | 7,972,725                           |
| City staff and consultant services   | 0                   | 2,225,000               | 2,225,000                           |
| <b>Total</b>                         | <b>\$12,298,400</b> | <b>\$29,397,433</b>     | <b>\$17,099,033</b>                 |

Source: Josh Keene of Real Estate Division and Samuel Chui of Public Works

\* Assumes \$3,000 per FTE @ 1,500 FTEs.

\*\* Assumes \$4,500 per FTE @ 1,500 FTEs.

\*\*\* Assumes \$12 per square feet of net rentable area of 430,845 square feet.

According to Mr. Samuel Chui, Project Manager at Public Works, Public Works began formally managing this project in 2016 and has incurred DPW staff and other costs associated with this project since then. Mr. Chui further advises that the Real Estate Division's earlier estimate is comparable to the costs of moving into an existing office building and does not reflect the realities of new construction, which requires furniture and equipment that is not part of tenant improvements, furniture and equipment for a new permit center, common areas and building support, building connection to the City's fiber infrastructure in the streets, application of Voice over Internet Protocol (VoIP) for the telephony system, network equipment and infrastructure for building systems and City business needs. In addition, the requested \$29,397,433 is not based on actual bids.

Based on DPW's cost proposal provided to the City Administrator in September 2016, DPW will incur approximately \$1,000,000 of expenses for consultant peer review, two DPW project managers and City Attorney legal fees through FY 2017-18. Therefore, \$1,000,000 should be released at this time and the remaining \$28,416,265 placed on reserve pending details and reductions provided.

### Controller's Internal Audit Fund

The Controller's City Services Auditor would receive \$653,382 from the subject COPs to provide internal audit functions. In accordance with Appendix F of the City's Charter, this amount is based on 0.2% of City project development costs of \$326,690,953.

### Total COP Delivery Expenses

The COP fees and expenses include the bond reserve, capitalized interest and fees, bond issuance costs, underwriter's discount, and a reserve for market uncertainty. According to Ms. Querubin, the bond reserve amount of \$21,832,100 (Table 3 above) is calculated at 100% of the maximum annual debt service for the COPs over the 30-year term and is required to be set

aside. The capitalized interest and fees amount of \$31,051,471 (Table 3 above) assumes estimated accrued interest and fees for the potential use of commercial paper for up to two years prior to the issuance of the COPs and the capitalized interest for up to one year from the date of bond issuance. Bond issuance costs of \$604,643 (Table 3 above) include legal fees, financial advisory fees, rating agency fees, printing, bond insurance and other issuance expenses. Underwriter's discount of \$2,220,855 (Table 3 above) is the fee paid to the underwriter of the COPs for dissemination of the bonds. The reserve for market uncertainty of \$7,634,000 (Table 3 above) represents the additional amount included in the supplemental to allow for fluctuations in market interest rates from the date of authorization by the Board of Supervisors until the time of the sale of the COPs.

## **POLICY CONSIDERATION**

### **Relocation of City Departments and Use of Space at 1500 Mission Street**

In July 2014, the Board of Supervisors approved Resolution No. 312-14 authorizing the City to enter into an Exclusive Negotiation Agreement and Letter of Intent with Related to develop a new City-owned office building. Resolution No. 312-14 also authorized the Director of Property to provide a report detailing City office space requirements, the specified projected uses and staffing for the new City office building and the overall plan for Civic Center office space. In response, working with Real Estate, the Controller's Office provided a report to the Board of Supervisors in the fall 2014 that projected potential City staff and square feet requirements for a new office building for FY 2018-19.

This 2014 report projected consolidating office space for five City departments, including (a) Public Works, (b) Department of Building Inspection, (c) City Planning, (d) Retirement and (e) Health Services System, currently in City-owned space or leasing office space in the Civic Center. At the time, the Board of Supervisors was advised that this new City office building was anticipated to add approximately 100,000 square feet of new City-owned office space and reduce the amount of leased space in the Civic Center. According to Mr. Updike, the net increase in square feet of City office space is now estimated at 154,760 square feet. With the information contained in the report, the Board of Supervisors on December 9, 2014 approved the Conditional Land Disposition and Development Agreement with Related for the City office building at 1500 Mission Street.

Table 6 below compares the square feet requirements specified in this 2014 report<sup>7</sup> projected to FY 2018-19 to what Public Works and Real Estate are now reporting are City department requirements for the new City office building.

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<sup>7</sup> The square footage amounts in the 2014 report were based on 463,300 gross square feet, which has been converted to rentable square feet in Table 6 below to provide a comparison with the rentable square feet for 2017.



**Table 6: Comparison of Square Footage Use of 1500 Mission Street**

| Departments                        | 2014<br>Rentable<br>Square<br>Feet | 2017<br>Rentable<br>Square<br>Feet | Increase/(Decrease)<br>Square Feet |
|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
| Public Works                       | 181,018                            | 194,588                            | 13,570                             |
| Building Inspection                | 63,086                             | 56,819                             | (6,267)                            |
| Planning                           | 49,574                             | 59,910                             | 10,336                             |
| Health Service System <sup>8</sup> | 18,682                             | -                                  | (18,682)                           |
| Retirement <sup>9</sup>            | 35,360                             | -                                  | (35,360)                           |
| Other Tenants (TBD)                | 5,405                              | 25,102                             | 25,102                             |
| Permit Center <sup>10</sup>        | 28,791                             | 38,960                             | 10,169                             |
| Common Areas and Building Support  | 52,043                             | 55,466                             | 3,423                              |
| <b>TOTAL</b>                       | <b>433,959</b>                     | <b>430,845</b>                     | <b>(3,114)</b>                     |

As shown in Table 6 above, the square feet allocated to Public Works, Planning and DBI are proposed to increase significantly. Regarding the differences in square footage for the various City departments, Mr. Chui advises that DBI's 6,267 square foot reduction in space is more than offset by the estimated 22,000 square feet of space that DBI will occupy in the new one-stop permit center, in which Building Inspection will be the anchor tenant, along with at least 11 other City departments. Mr. Chui also notes that the 10,336 square foot increase in Planning's space may enable another tenant to occupy a portion of this space. The Common Areas and Building Support include the lobby, conference center, childcare facilities, potential wellness center and other building support functions. According to Mr. Updike, the square footage requirements for the common areas and building support increased by 3,423 square feet because the entire first floor will now be common areas, with additional conference and training rooms and facilities.

However, the most notable change in the proposed plans is the elimination of Health Service System for 18,682 square feet and Retirement System for 35,360 square feet or a total of 54,042 square feet from the new City office building. Currently, both of these City departments rent space at 1145 Market Street at an annual rental cost of approximately \$2,314,000, with leases that expire in 2023 and 2024 respectively. In addition, the previous plan provided for an additional 5,405 square feet for other potential tenants or 59,447 square feet total for other City tenants. Instead, the current proposal only allows for 25,102 square feet for other City

<sup>8</sup> Health Service System currently occupies 19,500 square feet of leased office space at 1145 Market Street, a ten-year lease, which commenced in 2013 and terminates in 2023, at a current rental rate of approximately \$42 per square foot, or total annual costs of \$826,000 in FY 2017-18, with 3% annual rent increases.

<sup>9</sup> San Francisco Employees Retirement System currently occupies 35,579 square feet of leased office space at 1145 Market Street under a ten-year lease commencing in 2014 and terminating in 2024 at a current rent of approximately \$42 per square foot, or total annual rental costs of \$1,488,000 in FY 2017-18, with 3% annual rent increases.

<sup>10</sup> Of the 38,960 square feet proposed, approximately 22,000 square feet, or 56% will be used by DBI.

departments to potentially relocate to 1500 Mission Street, a reduction of 34,345 square feet of space or 58%.

Based on information provided by Real Estate, Table 7 below shows the number of rentable square feet currently occupied by the three main City departments (Public Works, Building Inspection (DBI) and Planning) that are proposed to occupy the new City office building at 1500 Mission Street. As shown in Table 7 below, all three City departments would increase their amount of rentable space in the new City office building by a combined total of 27,667 square feet. At the same time, two City departments, notably Health Service System and Retirement System, will not relocate into this new City office building.

**Table 7: Current and Proposed Square Footage for 3 City Departments**

| Location               | Public Works   | DBI           | Planning      | Total          |
|------------------------|----------------|---------------|---------------|----------------|
| 30 Van Ness            | 101,144        |               |               | 101,144        |
| 1650 Mission           |                | 4,280         | 48,704        | 52,984         |
| 1660 Mission           | 748            | 68,821        | 543           | 70,112         |
| 1680 Mission           | 36,753         |               |               | 36,753         |
| City Hall              | 5,426          |               |               | 5,426          |
| 1155 Market            | 38,922         |               |               | 38,922         |
| <b>Total</b>           | <b>182,993</b> | <b>73,101</b> | <b>49,247</b> | <b>305,341</b> |
| <b>Proposed</b>        | <b>194,279</b> | <b>78,819</b> | <b>59,910</b> | <b>333,008</b> |
| <b>Increased Space</b> | <b>11,286</b>  | <b>5,718</b>  | <b>10,663</b> | <b>27,667</b>  |

The current proposed square footage use and City departments that would occupy the new 1500 Mission Street office building is not consistent with the information the Real Estate Division and the Controller’s Office provided to the Board of Supervisors in 2014, when the Board of Supervisors approved this project. Most notably, the proposed use significantly expands the amount of space for three City departments, Public Works, Planning and Building Inspection and excludes Health Service System and Retirement System or significant space for other City departments. As previously noted, the proposed new office building will create an estimated net increase of 154,760 square feet of new space. With such significant increases in space, the amount of leased space and lease costs in the Civic Center should be reduced, resulting in the termination of existing City leases, as the Board of Supervisors were advised in 2014 when the 1500 Mission Street office building was approved.

In response, over the last several weeks, the Real Estate Division has identified seven leases containing a total of 93,970 square feet of space in the Civic Center that could potentially be terminated with the addition of the new 1500 Mission Street building and/or through backfilling space at 1650 Mission Street once the Planning Department vacates and moves into the new 1500 Mission Street building. Under these seven leases, the City currently spends approximately \$4.1 million annually. At this time, other than the approximately 25,000 square feet that is shown in Table 6 above in the current plan for Other Tenants to be determined (TBD), the Real Estate Division cannot commit to moving additional City employees into specific additional space in the new 1500 Mission Street building.

**Need for Reduction in City FF&E, Technology and Moving Expenses**

Given the requested increase of \$17,099,033 or 139% for furniture, fixtures, equipment, technology and moving expenses and the lack of any detailed information, the Board of Supervisors should approve the entire \$29,397,433, but only release \$1,000,000 at this time to fund City staff, legal and consultant expenses through FY 2017-18 and place the remaining \$28,397,433 on Budget and Finance Committee Reserve.

Before the Board of Supervisors approves the release of the remaining funds, Real Estate should provide a report to the Board of Supervisors that clearly identifies the (a) number of employees and amount of space that are currently used by each City department, (b) number of employees and amount of space that are proposed to be used by each City department in the new City building, and (c) existing City leases that will be terminated and the existing City leases that will be backfilled or otherwise reused, including the square footage of such leases, the amount of rent savings and any additional costs assumed. The City should maximize the number of leases being terminated and the number of City departments and employees relocated into the new City office building, as was originally proposed to the Board of Supervisors when this project was approved.

As part of the report identifying which City departments would be relocated to 1500 Mission Street, Public Works should rework the remaining \$28,397,433 for FF&E, technology and moving expenses request to maximize the amount of existing furniture that is reused and moved into the new building and minimize the additional City expenses. Details should be provided and bids obtained prior to requesting the release of a reduced amount of funding for this purpose.

**RECOMMENDATIONS**

1. Amend the proposed ordinance (File 17-0464) to reflect the recommended savings shown in Table 3 above, based on the proceeds from the sale of the three City buildings resulting in an additional \$3,134,836 for the Project Fund.
2. Amend the proposed ordinance (File 17-0464) to place \$28,397,433 of the requested \$29,397,433 on Budget and Finance Committee Reserve for FF&E, technology and moving to allow \$1,000,000 to be released now. The \$28,397,433 on reserve should not be released, pending a report that identifies (a) number of employees and amount of space currently used by each City department, (b) number of employees and amount of space proposed to be used by each City department in the new City building, and (c) existing City leases that will be terminated, existing City leases that will be backfilled or reused, including square footage of leases, rent savings and any additional costs. The City should maximize the leases terminated and City departments and employees relocated into the new City office building, as originally proposed to the Board of Supervisors when this project was approved. To request release of the \$28,397,433 being placed on reserve, Public Works should maximize the City's existing furniture for reuse and moved into the new building and minimize additional City expenses. Details should be provided and bids obtained prior to requesting the release of a reduced amount of funding for this purpose.

3. Approve the proposed ordinance (File 17-0464), as amended.
4. Approve the proposed ordinance (File 17-0468) and resolution (File 17-0471).