CITY AND COUNTY OF SAN FRANCISCO

BOARD OF SUPERVISORS

BUDGET AND LEGISLATIVE ANALYST

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TO: Budget and Finance Committee

FROM: Budget and Legislative Analyst

SUBJECT: April 19, 2023 Budget and Finance Committee Meeting

TABLE OF CONTENTS

Item	File		Page
2	23-0257	Appropriation - Ambulance Service Revenue - Fire Department - $4,236,098 - De-Appropriation and Appropriation - Various Departments - $63,701,785 - FY2022-2023	1
4	23-0207	Contract Agreement - Retroactive - Michelin North America, Inc. - SFMTA Tire Lease and Associated Services - Not to Exceed $18,900,000	13
5	23-0337	Contract Amendment - Bay Cities Produce Co, Inc. - Purchase of Fresh and Frozen Produce for ZSFGH and LHH - Not to Exceed $12,067,569	19
9 & 10	23-0204 23-0342	Airline and Airport 2023 Lease and Use Agreement Airline and Airport 2023 Lease and Use Agreement - Various Airlines	23
12	23-0377	Loan Agreement - Sunnydale Block 3A Housing Partners, L.P. - Sunnydale HOPE SF Block 3A - 100% Affordable Housing - Loan Amount Not to Exceed $27,272,065	33
15	23-0380	Loan Agreement - HV Partners 3, LP - Hunters View HOPE SF Vertical Phase III - 100% Affordable Housing - Not to Exceed $50,495,000	45
16	23-0319	Loan Amendment - Turk 500 Associates, L.P. - 100% Affordable Housing - 555 Larkin Street - Not to Exceed $23,805,311	53
17	23-0318	Loan Amendment - 4840 Mission Associates, L.P. - 100% Affordable Housing - 4840 Mission Street - Not to Exceed $37,728,757	60

Item 2 **File 23-0257**	**Departments:** Emergency Management, Fire, Public Health, Public Works, Public Utilities Commission, and Sheriff

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed ordinance (a) appropriates $4,236,098 in Ambulance Service Revenue in the Fire Department; (b) de-appropriates $59,465,687 from permanent salaries and mandatory fringe benefits and appropriates $62,547,210 to overtime in the Department of Emergency Management, Department of Public Health, Department of Public Works, Fire Department, San Francisco Public Utilities Commission, and the Sheriff's Department; and (c) appropriates $1,154,574 to Materials and Supplies in the Fire Department. Approval of the proposed ordinance requires a two-thirds vote of all members of the Board of Supervisors pursuant to Charter Section 9.113(c).

Fiscal Impact

- The Department of Public Health has (a) $29.2 million surplus in salaries due to an increase in budgeted positions, vacant positions, and hiring challenges; and (b) projected excess overtime expenditures of $29.2 million due to back-filling vacancies and increased staffing to meet a higher-than-budgeted patient census at Zuckerberg San Francisco General Hospital.
- The Fire Department has (a) $4.2 million surplus in ambulance service revenue due to increases in ambulance call volume; (b) surplus of $17.0 million in salaries and benefits due to vacant positions; (c) projected excess overtime expenditures of $20.1 million largely due to backfilling vacant positions to meet minimum staffing levels for fire suppression as well as increased EMS staffing to manage the increased calls; and (d) projected excess materials and supplies expenditures of $1.2 million for general supplies to run and maintain ambulances due to the increase in call volume.
- The Sheriff's Department has (a) $9.3 million in surplus salaries due to vacant positions; and (b) $9.3 million in projected excess overtime expenditures due to backfilling vacant positions to meet minimum staffing levels in the jails and other security posts.
- The Department of Emergency Management has (a) $2.3 million in surplus salaries due to vacant positions and hiring challenges, particularly for Public Safety Communications Dispatchers; and (b) $2.3 million in projected excess overtime expenditures due to backfilling vacant positions to meet minimum staffing levels in the 911 call center.
- The San Francisco Public Utilities Commission has (a) $1.4 million in surplus salaries due to vacant positions; and (b) $1.4 million in projected excess overtime expenditures due to increased workload from damage caused by winter storms.
- The Department of Public Works has (a) $267,591 in surplus salaries due to vacant positions in the Bureau of Street Environmental Services; and (b) $267,591 in projected excess overtime expenditures due to increased workload from damage caused by winter storms.

Recommendation

- Approve the proposed ordinance.

MANDATE STATEMENT

Charter Section 9.105 provides that amendments to the Annual Appropriation Ordinance be subject to Board of Supervisors approval by ordinance, after the Controller certifies the availability of funds.

Administrative Code Section 3.17 states that the Airport; Department of Emergency Management; Fire Department; Police Department; Department of Public Health; Public Utilities Commission; Department of Public Works; Recreation and Park Department; and Sheriff must obtain a supplemental appropriation to exceed the overtime budgets in their annual operating funds.

Charter Section 9.113(c) states that, in the event the Mayor or a member of the Board of Supervisors recommends a supplemental appropriation ordinance after the adoption of the budget and prior to the end to the budget year that contains any item rejected by the Mayor or the Board of Supervisors in the original budget appropriation, the supplemental appropriation can only be approved by a two-thirds vote of the Board of Supervisors.

BACKGROUND

Six departments are requesting a supplemental appropriation to increase their overtime budgets in annual operating funds, as per Administrative Code Section 3.17. The need for additional overtime funds is similar across departments, with many reporting that vacancies combined with minimum staffing levels required for some departments to maintain services are contributing to the need for staff to work overtime. In addition, the Department of Public Works and the San Francisco Public Utilities Commission report that they have seen increased workloads from the winter storms, resulting in a need for additional overtime.

As of the FY 2022-23 Six-Month Budget Status Report, the Department of Public Health had exceeded its overtime budget across its annual operating funds, as of December 31, 2022. The Fire Department and the Department of Emergency Management have exceeded their overtime budgets at the end of March, after the proposed ordinance was introduced. As of the writing of this report, the Department of Public Works, the Sheriff's Department, and the San Francisco Public Utilities Commission had not yet exceeded their overtime budget across annual operating funds.

DETAILS OF PROPOSED LEGISLATION

The proposed ordinance (a) appropriates $4,236,098 in Ambulance Service Revenue in the Fire Department; (b) de-appropriates $59,465,687 from permanent salaries and mandatory fringe benefits and appropriates $62,547,210 to overtime in the Department of Emergency Management, Department of Public Health, Department of Public Works, Fire Department, San Francisco Public Utilities Commission (SFPUC), and the Sheriff's Department; and (c) appropriates $1,154,574 to Materials and Supplies in the Fire Department. The appropriation totals

$63,701,784. Approval of the proposed ordinance requires a two-thirds vote of all members of the Board of Supervisors pursuant to Charter Section 9.113(c).

Exhibit 1 below summarizes the proposed appropriation of $63,701,784 by department.

Exhibit 1: Appropriation of $63,701,784 by Department

	Fire	Emergency Management	Public Health	Public Works	Public Utilities	Sheriff	Total
Sources							
Appropriation							
Ambulance Service Revenue	$4,236,098						$4,236,098
De-appropriation							
Permanent Salaries/Benefits	17,003,186	$2,294,910	$29,200,000	$267,591	$1,400,000	$9,300,000	59,465,687
Total Sources	$21,239,284	$2,294,910	$29,200,000	$267,591	$1,400,000	$9,300,000	**$63,701,785**
Uses							
Appropriation							
Overtime	20,084,709	2,294,910	29,200,000	267,591	1,400,000	9,300,000	62,547,210
Materials & Supplies	1,154,575						1,154,575
Total Uses	**$21,239,284**	**$2,294,910**	**$29,200,000**	**$267,591**	**$1,400,000**	**$9,300,000**	**$63,701,785**

Source: Proposed Ordinance

FISCAL IMPACT

Proposed Increases in Overtime

The proposed percent increases in overtime for the six departments range from 25.5 percent for SFPUC up to 113.8 percent for Public Health. If the proposed increases are approved, three departments would exceed their FY 2021-22 overtime budgets by more than five percent (Emergency Management, Public Health, and SFPUC). Exhibit 2 summarizes the FY 2022-23 approved overtime budget for each department, the resulting increase from the proposed ordinance, and FY 2021-22 actual expenditures.

Exhibit 2: FY 2022-23 Overtime Budget and Proposed Increase, Annual Operating Funds*

	Fire	Emergency Management	Public Health	Public Works	Public Utilities	Sheriff
FY 2022-23 Overtime Budget	$57,394,339	$5,402,307	$25,660,412	$1,511,371	$5,875,471	$17,007,640
Proposed Increase in Legislation	20,084,709	2,294,910	29,200,000	267,591	1,400,000	9,300,000
Proposed Increase (Dept. request)				232,409	100,000	
Total Increase	20,084,709	2,294,910	29,200,000	500,000	1,500,000	9,300,000
New Overtime Budget	$77,479,048	$7,697,217	$54,860,412	$2,011,371	$7,375,471	$26,307,640
Percent Increase	35.0%	42.5%	113.8%	33.1%	25.5%	54.7%
FY 2021-22 Actual Overtime Expenditures	$83,073,039	$6,128,537	$44,321,283	$2,253,363	$6,239,234	$25,608,252
New Overtime Budget, Percent of FY 2021-22 Actual Expenditures	93.3%	125.6%	123.8%	89.3%	118.2%	102.7%

Source: FY 2022-23 department overtime budgets for funds considered in this ordinance; Proposed Ordinance
*Excludes work order funds

The following sections provide additional detail on the proposed increases in overtime for each of the six departments and the proposed increase in materials and supplies for the Fire Department.

Department of Public Health: $29,200,000

The proposed ordinance de-appropriates $29,200,000 in surplus salaries in the Department of Public Health's (DPH) FY 2022-23 budget to pay for additional overtime. This funding will be appropriated across Zuckerberg San Francisco General Hospital (ZSFGH)[1], Laguna Honda Hospital (LHH), and multiple other divisions across DPH, including Jail Health, Primary Care, Behavioral Health, Administration, Health Network Services, and Public Health. Exhibit 3 below summarizes the de-appropriation and appropriation of funds. As of the FY 2022-23 Six-Month Budget Status Report, DPH had exceeded their overtime budget across its annual operating funds, expending 103 percent of its overall budget. As of the pay period ending March 3, 2023, DPH had spent 182 percent of budgeted overtime at ZSFGH, 86 percent of budgeted overtime at Laguna Honda, and 172 percent of budgeted overtime in divisions outside of ZSFGH and Laguna Honda.

[1] The appropriation of overtime at ZSFGH will go toward addressing overtime needs across the hospital, including the pharmacy, engineering and maintenance, the Family Health Center, maternal and child health, emergency ambulator care, intensive care, medical-surgical, environmental services, and patient accounting.

Exhibit 3: DPH Appropriation

Sources	Amount
De-appropriation	
ZSFGH Permanent Salaries	$22,000,000
Laguna Honda Permanent Salaries	4,000,000
Other DPH Permanent Salaries (Non-ZSGFH or Laguna Honda)	3,200,000
Total Sources	**$29,200,000**

Uses	Amount
Appropriation	
ZSFGH Overtime	$22,000,000
Laguna Honda Overtime	4,000,000
Other DPH Overtime (Non-ZSGFH or Laguna Honda)	3,200,000
Total Uses	**$29,200,000**

Source: Proposed Ordinance, File 23-0257 and BLA consolidation

DPH's surplus budget in salaries is primarily driven by vacant positions that affect ZSFGH, Laguna Honda, and other divisions within DPH. A Department vacancy report shows 1,408 vacancies in permanent positions, or a vacancy rate of 17.9 percent of authorized positions. In FY 2022-23 DPH added 391 FTEs across all divisions, increasing the Department's FTE count by five percent, from 7,466 FTEs in FY 2021-22 to 7,857 FTEs in FY 2022-23. In the Department's February 28, 2023 memo to the Health Commission, staff report that the surplus in budgeted salaries is a result of the increase in budgeted FTEs, combined with the number of vacant positions and challenges with the City's hiring process. DPH reports it has increased its human resources staff[2] and is working to increase the efficiency of their hiring processes.

DPH's Budget Manager, James Alexander, and Deputy Financial Officer, Emily Gibbs, report that the overtime needs are driven by high vacancies across several job classifications as well as a higher-than-average patient census at ZSFGH, which requires additional staffing to maintain staff-patient ratios.[3] In addition, there have been increases in non-productive time over the last two years across job classifications because of additional hours of COVID sick leave, resulting in the need to cover missed shifts with overtime according to Deputy Financial Officer Gibbs.

As of March 15, 2023, DPH reports vacancies in key classifications contributing to overtime spending. Exhibit 4 below shows a summary of the 15 job classifications with the highest overspending and corresponding vacancy rate. This is across DPH, including ZSFGH and Laguna Honda. As shown in this exhibit, patient-facing staff have some of the highest vacancies and overtime spending rates (Registered nurses, Patient Care Assistances, Nurse Practitioners, and Nurse Managers). Porters and food service workers also have high overtime spending despite

[2] The FY 2022-23 budget increased number of Human Resource Analyst FTE from 25.50 FTE in FY 2021-22 to 33.30 FTE in FY 2022-23.

[3] According to Deputy Financial Officer Gibbs, the average daily census for FY 2022-23 year to date is 325, which is 18 over budgeted levels. In FY 2022-23, the average daily census was 298, which was five over budgeted levels.

relatively lower vacancy rates in March 2023 because workload for these positions is impacted by the high patient census. In addition, vacancy rates are point in time figures and year-to-date overtime expenditures are impacted by vacancy rates that have changed throughout the year.

Exhibit 4: DPH Classifications with Largest Overtime Expenditures and Vacancies

Classification	Authorized Positions	Vacancies (As of 3/15/23)	Percent Vacant (As of 3/15/23)	Year to Date Overtime Expenditures (3/3/23)
2320 Registered Nurse	1,481	232	16%	$11,735,745
2303 Patient Care Assistant	550	53	10%	4,034,519
P103 Special Nurse*	n/a	n/a	n/a	3,072,301
2736 Porter	335	17	5%	3,030,013
2312 Licensed Vocational Nurse	184	34	19%	1,577,774
2604 Food Service Worker	122	8	7%	1,165,753
2328 Nurse Practitioner	162	19	12%	1,160,017
2322 Nurse Manager	103	14	14%	909,214
2430 Medical Evaluations Assistant	253	33	13%	872,397
2903 Hospital Eligibility Worker	224	45	20%	656,242
7334 Stationary Engineer	46	15	32%	640,549
2471 Radiologic Tech I, II, III	79	3	3%	601,085
2302 Nursing Assistant	107	18	17%	531,406
2409 Pharmacy Technician	89	10	11%	524,915
2583 Home Health Aide	61	18	30%	335,571
Total	**3,807**	**519**	**14%**	**$30,847,501**

Source: Department of Public Health
*All P103 position appointments are as needed to backfill paid time off, 2320 vacancies, and to staff for increased census. Therefore, there are no P103 vacancies.

Fire Department: $21,239,284

The proposed ordinance appropriates $4,236,098 in additional ambulance service revenue and de-appropriates $17,003,186 in surplus salaries and benefits in the Fire Department's FY 2022-23 budget to pay for $20,084,709 additional overtime and $1,154,575 additional materials and supplies. Exhibit 5 below summarizes the de-appropriation and appropriation of funds. Mark Corso, the Fire Department's Deputy Director for Finance and Planning, reports that the Fire Department exceeded the current budget in the pay period ending March 31, 2022.

Exhibit 5: Fire Department Appropriation

Sources	Amount
Appropriation	
Ambulance Billings	$4,236,098
De-appropriation	
Fire Salaries	15,503,186
Retirement Fringe	1,500,000
Total Sources	**$21,239,284**

Uses	Amount
Appropriation	
Fire Overtime	$20,084,709
Fire Materials and Supplies	1,154,575
Total Uses	**$21,239,284**

Source: Proposed Ordinance

The $4,236,098 in additional ambulance billing revenues is a result of an increase in the volume of ambulance calls as well as the Fire Department taking on a larger share of the calls relative to the private ambulance providers. This has increased revenues from ambulance billings. From July 1, 2022 through February 2023, call volume has averaged 5,379 per month, which is 10 percent higher than the previous fiscal year, which averaged 4,911 per month in FY 2021-22.

The surplus salary budget is a result of the Department being unable to hold a third academy to enter the field in the FY 2022-23 budget. The Fire Department's Deputy Director for Finance and Planning reports that the Department was unable to accommodate the third class[4] due to an insufficient number of instructors and because the Department wanted to stagger the number of probationary firefighters in the field. In addition, the Department reports that they will often have trainees in the academies who come from EMS, which requires backfilling these positions. To meet mandatory minimum staffing levels, the Fire Department uses overtime when there are not a sufficient number of full-time staff. The $1,500,000 in de-appropriation from retirement is an estimate of the fringe benefit savings associated with vacant positions.

Of the $20,084,709 in overtime, $19,769,270 will support Fire Department operations (including $17,963,255 for fire suppression, $1,367,313 for EMS, and $438,703 for other Department operations), and a small portion of the appropriation will also support Fire operations with the Port ($58,551) and the Airport ($256,888), which have experienced staffing shortages. The overtime appropriation will increase the Fire Department's annual operating overtime budget (including Airport operations) by 35 percent from $57,394,339 to $77,479,048. The increase in call volume described above has also required overtime from EMS staff to manage the increased

[4] The Fire Department reports that each academy has 50 to 55 trainees with low attrition rates, estimating that of 54 in an academy, approximately 48 will complete it. The Department reports that a new fire training facility will expand the size of academies.

calls. The FY 2022-23 budget increased ambulance staffing by 60 FTEs to help respond to calls, but the Department reports that while additional staffing has helped, the call volume has required additional overtime.

The materials and supplies appropriation of $1,154,575 will go toward general supplies needs to run and maintain ambulances (fuel, medical supplies, pharmaceuticals) that the Department also attributes to the increase in call volume. The FY 2022-23 annual operating materials and supplies budget is $4,989,299, of which the Department has spent $4,583,169 (91.9 percent). If approved, this supplemental appropriation will increase their materials and supplies budget to $6,143,874, an increase of 23.1 percent.

Sheriff's Department: $9,300,000

The proposed ordinance de-appropriates $9,300,000 in permanent salaries in the Sheriff's Department FY 2022-23 budget to pay for $9,300,000 in overtime expenditures.

According to Kevin Fisher-Paulson, Chief Deputy Sheriff, the permanent salaries surplus and overtime needs are largely due to vacancies, mostly in the 8504 Deputy Sheriff classification.[5] The Sheriff's Department projects that FY 2022-23 General Fund permanent salaries will total approximately $69.3 million compared to the budgeted amount of $113.7 million, resulting in a projected surplus of $44.3 million, which is offset by sick pay, other paid time off, and projected use of overtime. The Sheriff's Department projects total overtime expenditures of approximately $25.8 million compared to the budgeted amount of $17.2 million, resulting in a projected deficit of $8.6 million. The Sheriff's Department is requesting a $9.3 million appropriation to provide a buffer in case overtime expenditures increase in the final three months of the fiscal year. The Sheriff's Department reports that the Department exceeded their overtime budget, excluding work orders, in the pay period ending March 3, 2023, but the Department had not exceeded their total overtime budget including work orders.

According to Chief Deputy Sheriff Fisher-Paulson, the Sheriff's Department has 146 vacancies within the 8504 Deputy Sheriff classification out of 746 FTE positions, a 20 percent vacancy rate. Additionally, the Sheriff's Department has 29 vacancies within the 8300 Sheriff's Cadet classification and 28 vacancies within the sworn supervisor classifications (8306 Senior Deputy Sheriff, 8308 Sheriff's Sergeant, and 8310 Sheriff's Lieutenant). Overtime has been used to backfill vacancies to meet minimum staffing requirements in the jails and other security posts (such as City Hall) for these classifications.

According to Chief Deputy Sheriff Fisher-Paulson, the Sheriff's Department plans to hire 21 Deputy Sheriff recruits to begin an academy class in July 2023, although it would take approximately eight months before these new hires would be able to reduce overtime utilization. Additionally, the Sheriff's Department plans to hire five Cadets in April 2023, as well as promote

[5] The Sheriff's Department uses the 8304 classification for Deputy Sheriffs who were hired before the change in retirement plans and remain within the California Public Employees' Retirement System (CalPERS), while the 8504 classification is used for more recent hires who are within the City's San Francisco Employees' Retirement System (SFERS). Functionally, the two classifications are interchangeable.

internally and recruit lateral transfers to fill supervisory roles. The Sheriff's Department has worked with the Department of Human Resources to produce a promotional examination for sworn supervisor positions. Internal promotions would help to fill supervisory positions but would create new vacancies within the Deputy Sheriff classification.

Department of Emergency Management: $2,294,910

The proposed ordinance de-appropriates $2,294,910 in permanent salaries in the Department of Emergency Management's (DEM) FY 2022-23 budget to pay for $2,294,910 in overtime expenditures, as shown in Exhibit 1 above.

According to Thomas Chen, DEM Budget Manager, the permanent salaries surplus and overtime needs are largely due to vacancies in the 8238 Public Safety Communications Dispatcher classification. DEM projects that FY 2022-23 General Fund permanent salaries will total approximately $30.5 million compared to the budgeted amount of $35.1 million, resulting in a projected surplus of $4.6 million. However, DEM projects total overtime expenditures of approximately $6.9 million compared to the budgeted amount of $5.4 million, resulting in a projected deficit of $1.5 million. DEM is requesting the $2.3 million appropriation to provide a buffer in case overtime expenditures increase in the coming months. DEM exceeded its overtime budget in the pay period ending March 31, 2023.

According to Budget Manger Chen, DEM has approximately 18 vacancies within the 8238 Public Safety Communications Dispatcher classification, which translates into a 11 percent vacancy rate.[6] DEM had anticipated holding three training classes in FY 2022-23 with 12 trainees in each class, but due to recruitment difficulties, the second class only had nine candidates and the third class will likely be canceled due to a low number of applicants. DEM has hired a 1250 Recruiter position to assist with hiring, and DEM has received 724 applicants for the 8238 Public Safety Communications Dispatcher position in the two-month period after the Recruiter started. DEM plans to have three training classes in FY 2023-24 with 12 trainees in each class.

Due to the high level of vacancies, DEM has been using overtime to meet minimum staffing levels in the 911 call center. DEM's service standard is to answer at least 90 percent of calls within 10 seconds, and performance has ranged from 73 to 79 percent each month over the current fiscal year, despite high overtime utilization. Budget Manager Chen reports that without the requested overtime appropriation, DEM's performance compared to this service standard would be worse.

Public Utilities Commission: $1,400,000

The proposed ordinance de-appropriates $1,400,000 in permanent salaries in the San Francisco Public Utilities Commission's (SFPUC) FY 2022-23 budget to pay for $1,400,000 in overtime expenditures. However, due to damage caused by recent storms, SFPUC plans to request the

[6] DEM has 189 full-time equivalent (FTE) 8238 Public Safety Communication Dispatcher positions in the FY 2022-23 budget. However, due to attrition savings within the 911 call center, there are effectively 156.7 FTE funded positions, which translates into in an eleven percent vacancy rate.

ordinance be amended to increase the overtime appropriation to $1,500,000, as shown in Exhibit 6 below.

Exhibit 6: SFPUC Proposed Overtime Appropriation

Sources	Amount (Original)	Amount (Amended)
De-Appropriation		
Permanent Salaries (Wastewater Enterprise)	$745,000	$800,000
Permanent Salaries (Hetch Hetchy Water & Power)	180,000	250,000
Permanent Salaries (Water Enterprise)	475,000	450,000
Total Sources	**$1,400,000**	**$1,500,000**

Uses	Amount (Original)	Amount (Amended)
Appropriation		
Overtime (Wastewater Enterprise)	$745,000	$800,000
Overtime (Hetch Hetchy Water & Power)	180,000	250,000
Overtime (Water Enterprise)	475,000	450,000
Total Uses	**$1,400,000**	**$1,500,000**

Source: Proposed Ordinance, SFPUC

According to Laura Busch, SFPUC Budget Director, SFPUC's increased overtime usage in FY 2022-23 is largely due to the severe storm events that have persisted since December 2022. Between the Wastewater, Water, and Hetch Hetchy Water and Power Enterprises, SFPUC projects that FY 2022-23 overtime expenditures will total approximately $7.2 million, exceeding the budgeted amount of $5.7 million by $1.5 million. Overtime has been utilized as follows:

- Wastewater Enterprise: The primary overtime drivers include installation of flood barriers during heavy rains, deployment of Collections Systems wet weather field crews, and staffing the North Point Wet Weather Facility. SFPUC projects total overtime expenditures of $3,245,585, exceeding the budgeted amount of $2,445,585 by $800,000. SFPUC estimates that the Wastewater Enterprise will exceed its overtime budget in the pay period ending March 31, 2023.
- Water Enterprise: The primary overtime drivers include response to urgent requests at water treatment facilities for critical repairs and power outages, repairing damage to watershed infrastructure, and wet weather water testing. SFPUC projects total overtime expenditures of $2,737,544, exceeding the budgeted amount of $2,287,544 by $450,000. SFPUC estimates that the Water Enterprise will exceed its overtime budget in the pay period ending May 12, 2023.
- Hetch Hetchy Water and Power: The primary overtime drivers include emergency work to restore electrical and streetlighting infrastructure, roadway failures impairing access to facilities, wildfire mitigation, and staffing shortages. SFPUC projects total overtime expenditures of $1,265,002, exceeding the budgeted amount of $1,015,002 by $250,000. SFPUC estimates that the Hetch Hetchy Enterprise will exceed its overtime budget in the pay period ending April 28, 2023.

The job classifications driving the largest overtime usage to date are shown in Exhibit 7 below.

Exhibit 7: SFPUC Classifications with Largest Overtime Expenditures

Classification	Enterprise	Overtime Expenditures (As of 3/3/2023)
7372 Stationary Engineer, Sewage Plant	Wastewater	$824,367
7388 Utility Plumber	Water	665,805
7449 Sewer Service Worker	Wastewater	421,089
7250 Utility Plumber Supervisor 1	Water	394,316
7373 Sr. Stationary Engineer, Sewage Plant	Wastewater	383,850
7482 Power Generation Technician 2	Hetch Hetchy Power	206,070

Source: SFPUC

The proposed de-appropriation of $1,400,000 from permanent salaries is due to projected salary savings in the enterprise budgets. SFPUC projects that permanent salary expenditures in the enterprises will total approximately $104.1 million, compared to the budgeted amount of $156.2 million, resulting in projected savings of $52.1 million. Between the Water, Wastewater, and Hetch Hetchy Water and Power Enterprises, SFPUC has approximately 303 FTE vacant budgeted positions out of 1,273 budgeted positions, a 24 percent vacancy rate.[7] According to Budget Director Busch, SFPUC is working with the Department of Human Resources to reduce the vacancy rate as part of the Citywide Government Operations Recovery Initiative.

Department of Public Works: $267,591

The proposed ordinance de-appropriates $267,591 in surplus permanent salaries in the Department of Public Works (DPW) FY 2022-23 budget to pay for additional overtime. However, DPW reports that they anticipate amending the request to increase the overtime supplemental amount to $500,000, as shown previously in Exhibit 2.

According to DPW's Finance Manager Jennifer Marquez, additional overtime funding is needed to cover the labor costs associated with responding to the winter storms. Response work includes clearing fallen trees and other debris as well as sandbag distribution, patching potholes, repair of damaged City buildings, and clearing City gutters. Positions supporting the storm response efforts include, but are not limited to, communications dispatchers, urban forestry inspectors, arborist technicians, and engineering staff.

The funding being de-appropriated in permanent salaries comes from the Bureau of Street Environmental Services, which is in the process of hiring 135 vacant positions. According to Public Works' Hiring and Vacancy Update to the Public Works Commission on March 1, 2023, Public Works had a functional vacancy rate of 20.8 percent, after adjusting for positions that are about to be filled and positions that are expected to be deleted due to the passage of Proposition B in November 2022, which eliminated the Department of Sanitation and Streets and transferred its duties back to DPW. Public Works' FY 2022-23 budget included funding for a new Human

[7] SFPUC has 495 vacant budgeted positions. However, due to attrition savings totaling 192.16 FTE positions, only 302.84 FTE vacant positions may be filled within budget.

Resources section, and the Human Resources section has a goal to fill 250 positions department-wide by the end of the fiscal year.

DPW's current FY 2022-23 annual operating fund overtime budget of $1,511,371 will increase by 17.7 percent with the proposed $267,591 appropriation. An increase of $500,000 would increase DPW's overtime budget to $2,011,8371, or 33.1 percent. As of the FY 2022-23 Six-Month Budget Status Report, DPW had expended 96 percent of its annual operating overtime budget, which does not include overtime for General Fund work orders. DPW staff reports that the Department exceeded their overtime budget, excluding work orders, in the pay period ending January 6, 2023, but the Department has not exceeded its total overtime budget including work orders.

RECOMMENDATION

Approve the proposed ordinance.

Item 4 **File 23-0207** *(Continued from 4/12/23 meeting)*	**Departments:** Office of Contract Administration (OCA) Municipal Transportation Authority (MTA)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve a new agreement with Michelin North America, Inc. (Michelin) to lease tires for MTA buses and associated services. The initial contract amount is for $13,500,000 for a five-year term from April 1, 2023 through March 31, 2028, with the option to extend the contract for an additional two years and $5,400,000, for a potential total not to exceed amount of $18,900,000 and total seven year term, ending on March 31, 2030.

Key Points

- Michelin currently provides tire lease and associated services for MTA under a contract that ends on September 30, 2023. According to the Office of Contract Administration (OCA), the current contract end date included a buffer period to allow the City to procure a new tire lease agreement. Actual spending on the existing $9,995,000 contract was $9,640,000 as of March 2023.
- In September 2022, OCA issued a competitive solicitation for tire leasing. Michelin North America, Inc. was the only vendor to submit a bid, but it was deemed non-responsive because they failed to provide the required minimum qualifications documentation. OCA determined that the lack of responsive offers was not due to the solicitation content, and, in accordance with City Administrative Code Section 21.6, OCA selected Michelin to continue providing services under the proposed new agreement. OCA has since determined that Michelin meets the minimum qualifications of the solicitation.
- The proposed agreement includes a $151,042 monthly fee to pay for Michelin staff at six MTA bus yards and $0.00577-$0.0075 per mile for each bus tire leased by MTA, amounting to approximately $70,000 per month.

Fiscal Impact

- The cost of staff and tire leasing both increase by 5.5 percent between the current and proposed contract. Contract costs are funded by the MTA operating budget.

Policy Consideration

- MTA reports Michelin has been performing satisfactorily against contract requirements but does not document satisfactory/compliant performance.
- We reviewed summary mileage reports provided by MTA that showed the department was tracking the mileage for each of its buses, but the record did not contain information specific to each tire, which is tracked by Michelin. As of this writing, MTA is compiling additional information to demonstrate contractor performance.

Recommendation

- Approve the proposed resolution.

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.

BACKGROUND

Since at least 2009, San Francisco Municipal Transportation Authority (MTA) has contracted for rubber tire leasing, maintenance, and disposal for its transit fleet of 860 buses, each of which has six to eight tires.

Previous Vendors

The contract for tire lease and associated services for MTA buses has previously been provided by the following vendors:

- Bridgestone Americas Tire Operations LLC: April 1, 2009 – March 31, 2014
- Michelin North America, Inc.: October 1, 2014 – September 30, 2018
- Michelin North America, Inc.: October 1, 2018 – September 30, 2023

The ongoing contract between the City and Michelin North America, Inc. (Michelin) provides for the lease by MTA from Michelin of an unlimited number of tires over the contract period with payment determined by the number of new tires, number of miles driven per tire, and maintenance on each tire. Each tire has a serial number and is tracked.

In addition, MTA pays a monthly fee of $143,125 to Michelin to provide personnel and equipment at six separate MTA bus yards to support tire operations: Flynn, Islais Creek, Kirkland, Potrero, Presidio, and Woods. Michelin handles the entire lifecycle of the tire, including recycling and disposal.

MTA reports that leasing tires rather than purchasing from Michelin is beneficial because leasing reduces costs related to the disposal of the tires, reduces liability related to product quality, and provides for Michelin tire experts in six of the MTA bus yards. According to an April 2022 Personal Services Contract approval request from MTA to the Civil Service Commission, it is common practice for transit agencies to lease tires and contract for support services.

The current contract with Michelin has been modified twice. The first modification increased the contract's not-to-exceed amount by $1.8 million, extended the contract term by one year, added a new tire size to the contract, but did not increase the existing tire lease costs or labor costs. The second modification extended the contract term by one additional year for a total five-year term and increased the not to exceed amount by $195,000. The new contract amount totaled $9,995,000, which is below the $10 million threshold triggering Board of Supervisors approval.

Exhibit 1. Tire Lease and Associated Services Contract History (Contract No. 1000012572)

	Contract Term	Not to Exceed Amount
Original Contract	Oct. 1, 2018-Sept. 30, 2021	$8,000,000
Modification No. 1	Oct. 1, 2018-Sept. 30, 2022	$9,800,000
Modification No. 2	Oct. 1, 2018-Sept. 30, 2023	$9,995,000

Source: OCA

The existing contract term ends September 30, 2023, but because MTA has nearly exhausted the $9,995,000 contract authority, the Office of Contract Administration is recommending a new contract with a start date in April 2023.

New Solicitation for Bids

On September 15, 2022, the Office of Contract Administration (OCA) issued a competitive solicitation for bids for tire lease and associated services for San Francisco Municipal Transportation Agency. Eight suppliers were invited to the public pre-solicitation meeting including: SF Tire & SVC Ctrl Inc DBA Bid O Tires, Michelin North America, Inc., McCoy Tire & Auto Service, KA-PA Tire & Auto Service, Inland Industrial Tire, East Bay Tire Co, Doherty Tire of Sonora, and Bridgestone Americas Tire Operations, LLC. None attended. OCA extended the bid due date by one week to October 11, 2022, but there were still no responsive bidders to the solicitation. Michelin North America, Inc. was the only vendor to submit a bid, but it was deemed non-responsive because they failed to provide the required minimum qualifications documentation. OCA has since determined that Michelin meets the minimum qualifications of the solicitation.[1]

City Administrative Code Section 21.6 states that when OCA issues a solicitation for goods or services and no responsive offers are received, OCA shall first review the solicitation to determine whether it could be altered and reissued in a manner that would be likely to attract a responsive offer. If OCA determines that the lack of responsive offers is not due to the content of the solicitation, OCA may purchase the goods or services from any source. OCA reports that it determined that the vendor requirements could not be changed to attempt to solicit additional bids. Therefore, in accordance with Section 21.6, OCA selected Michelin North America, Inc. to continue providing the contracted services under the proposed new agreement. OCA reports that it only uses Section 21.6 on rare occasions. OCA indicates it has used Section 21.6 six times since 2021, when OCA first started tracking use of this purchasing authority in the City's Financial and Procurement system.

[1] Michelin did not initially submit the required documentation to demonstrate they met Minimum Qualifications (MQ) No. 3 or No. 6. However, post-solicitation, Michelin has submitted documentation demonstrating that the company does, in fact, meet these qualifications. MQ No. 3 requires the bidder to submit ten purchase orders or contracts issued within the last three years to the bidder by other entities of similar size and nature as the City and County of San Francisco. MQ No. 6. requires bidders to submit one representative form or document, as an example, demonstrating Bidder's ability to individually track tires.

Maximized Current Contract Not to Exceed Amount

The contract is arriving before the Board of Supervisors for consideration at this time, six months before the expiration of the current five-year contract end date on September 30, 2023 because, according to OCA, the vendor has almost exceeded its not-to-exceed contract amount of $9,995,000. Actual spending as of early March 2023 is $9,640,000. According to OCA, the existing contract term had a buffer built in to allow for the procurement of a replacement contract.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a new agreement with Michelin North America, Inc. to lease tires for MTA buses and associated services. The initial contract amount is for $13,500,000 for a five-year term from April 1, 2023 through March 31, 2028, with the option to extend the contract for an additional two years and $5,400,000, for a potential total not to exceed amount of $18,900,000 and total seven-year term, ending on March 31, 2030. Exercising the options to extend would not require Board of Supervisors' approval.

Scope of Services

MTA has a fleet of 860 rubber-tire revenue vehicles (buses), stationed across six City bus yards. Each bus needs six to ten tires per vehicle, not including spares. The contractor will lease, service and dispose of all tires used by MTA on its buses. The contractor is responsible for the manufacturing, procuring, and transporting a sufficient supply of tires as required to guarantee the continuity of services to transport the public. The contractor must mount and dismount tires, balance tires, maintain proper tire pressure, recap rear tires, provide emergency road-side service 24 hours/7days per week (required to arrive within 60 minutes of notification), conduct monthly maintenance checks on all tires, and track tires through all stages including proper tire disposal. Michelin is to provide at minimum 16 staff to support its tire services including a Manager, six shop Supervisors, and drivers (of buses to and from the tire areas).

Michelin is to maintain a detailed monthly report for MTA which depicts the tire mileage for each tire (by serial number) on every vehicle.

Contract Terms

As shown below in Exhibit 2, the tire leasing cost and monthly tire service cost would increase under the proposed contract. The resolution's not to exceed amount is based on the projected full seven-year term of the contract, using recent spending as a guide.

Michelin is responsible for recycling tires. The contract states that the Fresno-based business Jack's Tire and Oil will be used for tire recycling, and that as of March 2023, the recycling cost per tire is $1.75.

Exhibit 2. Michelin Tire Lease and Service Contract Terms, current vs proposed

	Current Contract *(10/1/2018-9/30/2023)*	Proposed Contract *(4/1/2023-3/31/2028)*
Tire Leasing Cost[a]	$0.00547-$0.00711 per mile	$0.00577-$0.0075 per mile
Est. Lease Cost per Month[b]	$70,000	$70,000
Tire Service per Month	$143,125	$151,042
Est. Monthly Recycling Fee[c]	$0	$595
Total Annual Cost	**$2,557,500**	**$2,659,644**

Source: MTA

Notes: a) Leasing cost varies across the four different bus tire sizes; b) Lease cost estimate provided by OCA based on historical miles traveled per month. c) MTA estimates that 4,080 tires are scrapped annually, at a cost of $1.75 per tire. Under the current contract, there is no fee recycling fee.

Under the proposed agreement, Michelin North America, Inc. would invoice the City on a monthly basis of $151,042 for tire services, or approximately $113,281 per FTE. This includes providing 24/7 roadside assistance. According to MTA, in FY 2021-22 Michelin provided a total of 1,793 roadside calls, varying from 110 to 184 calls per month. The proposed monthly tire service rate would increase by $7,917 per month (approximately 5.5 percent) from the current agreement. Similarly, the cost of leasing tires would increase by 5.5 percent.

The current and proposed contracts allow for the vendor to request one annual price adjustment to reflect increases to the US Department of Labor's Producer Price Index (PPI) for Truck and Bus Pneumatic Tires and regional Consumer Price Index (CPI). Between 2021—the most recent date when contract prices were adjusted via Contract Modification No. 1 – and September 2022, there has been a 29.5 percent increase in the PPI for commodities[2] and an approximately 7.8 percent increase in the CPI for the services in San Francisco-Oakland-Hayward, which are both more than the proposed 5.5 percent increase for labor and materials.

Reporting Requirements

The proposed contract requires Michelin to submit an annual usage report detailing the total quantity and dollar value of services ordered, by month, during the preceding calendar year. Additionally, the proposed contract introduces the requirement for Michelin to provide to MTA monthly reports detailing the average tire mileage for each size tire and a summary report of all damaged or destroyed tires.

[2] Bureau of Labor Statistics Commodities Series ID WPU07120105 - Rubber and plastic products - Truck and bus including off-the-highway pneumatic tires.

FISCAL IMPACT

Under the proposed contract, Michelin would invoice the city for the cost of tire leasing. This monthly cost varies depending on actual usage and the wear and tear on tires. According to MTA, in January 2023, the total number of tire miles traveled across all buses was 12,958,085 miles. All buses have a mileage counter, and when they reach a certain mileage milestone, Michelin checks the rubber for wear and makes repairs/replacement accordingly. Under the agreement, MTA would pay Michelin between approximately $0.005 and $0.007 per tire per mile.

According to MTA, funding for this contract comes from the MTA operating budget, subject to appropriation approval of the Board of Supervisors.

POLICY CONSIDERATION

Performance Management

MTA reports Michelin has been performing satisfactorily but does not document satisfactory/compliant performance against contract requirements. We recommend OCA and MTA consider annual performance monitoring on future contracts.

The current and proposed contract do require that Michelin maintain monthly reports of an inventory of all tires, showing location (Bus Number), date installed and/or removed and "other pertinent data." We reviewed summary mileage reports provided by MTA that showed the department was tracking the mileage for each of its buses, but the record did not contain information specific to each tire, which is tracked by Michelin.

As of this writing, MTA is compiling additional information to demonstrate contractor performance.

Single Bidder

As noted above, although eight suppliers were invited to bid, the solicitation for this contract resulted in one bidder, Michelin, that was deemed non-responsive due to a failure to submit its documentation of minimum qualifications. As we noted in our report on the Granite Rock asphalt products (File 23-0039), this could be an indication that the City's procurement policies and procedures could be revised to increase competition. At the February 8, 2023 Budget & Finance meeting, at the recommendation of the Budget & Legislative Analyst, the Committee Chair requested the Purchaser and City Administrator to provide a report that: (1) assesses existing procurement strategies and municipal code requirements, (2) evaluates the feasibility of partnering with other governments to increase the number of joint procurements that the City participates in, and (3) provides recommendations to increase the number of bidders for goods, commodities, and services; by June 2023.

RECOMENDATION

Approve the proposed resolution.

Item 5 **File 23-0337**	**Department:** Office of Contract Administration (OCA), Department of Public Health (DPH)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve Modification No. 2 to the produce purchasing contract between the Office of Contract Administration (OCA) and Bay Cities Produce Co., Inc., extending the term by two years through September 2026, and increasing the not-to-exceed amount by $6,049,854, for a total not to exceed $12,067,569.

Key Points

- In 2019, OCA issued a Request for Proposals (RFP) to award a fresh and frozen produce purchasing contract for San Francisco General Hospital and Laguna Honda Hospital on behalf of the Department of Public Health (DPH). Bay Cities Produce was the highest scoring proposer and was awarded a contract. In September 2019, OCA executed a contract with Bay Cities Produce for a term of three years, from October 2019 through September 2022, and an amount not to exceed $4,017,715. In April 2022, OCA executed Modification No. 1 to the contract, extending the term by two years through September 2024, and increasing the not-to-exceed amount by $2,000,000, for a total not to exceed $6,017,715.
- Under the contract, Bay Cities Produce provides fresh and frozen produce to San Francisco General Hospital and Laguna Honda Hospital at prices calculated as a percent markup over cost. Prices are marked up by five to 10 percent (depending on the product) over Bay Cities' wholesale costs, which are subject to change based on market conditions. According to OCA, DPH has not made any complaints to OCA regarding contractor performance, and therefore OCA deems that Bay Cities Produce is meeting its contractual obligations. As of this writing, DPH is compiling documentation of satisfactory produce deliveries to demonstrate the vendor's performance.

Fiscal Impact

- The proposed Modification No. 2 would increase the not-to-exceed amount of the Bay Cities Produce contract by $6,049,854, for a total not to exceed $12,067,569. Using actual expenditures to date, OCA projects average future contract expenditures of $121,729 per month. Based on actual and projected contract expenditures, the Budget and Legislative Analyst recommends reducing the not-to-exceed amount of the contract by $967,569, for a total not to exceed $11,100,000.

Recommendations

- Amend the proposed resolution to reduce the not-to-exceed amount of the contract by $967,569, for a total not to exceed $11,100,000.
- Approve the resolution, as amended.

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.

BACKGROUND

In July 2019, the Office of Contract Administration (OCA) issued a Request for Proposals (RFP) to award a fresh and frozen produce purchasing contract for San Francisco General Hospital and Laguna Honda Hospital on behalf of the Department of Public Health (DPH). OCA received three proposals and an evaluation panel scored them, as shown in Exhibit 1 below.[1]

Exhibit 1: Proposals and Scores from RFP

Proposer	Score (Maximum 300 Points)
Bay Cities Produce	240
Daylight Foods	205
VegiWorks	174

Source: OCA

Bay Cities Produce was deemed the highest scoring responsive and responsible proposer and was awarded a contract. In September 2019, OCA executed a contract with Bay Cities Produce for a term of three years, from October 2019 through September 2022, and an amount not to exceed $4,017,715. In April 2022, OCA executed Modification No. 1 to the contract, extending the term by two years through September 2024, and increasing the not-to-exceed amount by $2,000,000, for a total not to exceed $6,017,715.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve Modification No. 2 to the produce purchasing contract between OCA and Bay Cities Produce, extending the term by two years through September 2026, and increasing the not-to-exceed amount by $6,049,854, for a total not to exceed $12,067,569. The total contract term of seven years would be the maximum term allowed by the RFP.

Under the contract, Bay Cities Produce delivers fresh and frozen produce to San Francisco General Hospital and Laguna Honda Hospital at prices calculated as a percent markup over cost. Prices are marked up five to 10 percent (depending on the product) over Bay Cities' wholesale costs, which are subject to change based on market conditions.[2] According to data provided by OCA, prices for fresh and frozen food have increased by 26 percent and 28 percent respectively

[1] The evaluation panel consisted of a DPH Food and Nutrition Director, a DPH Chef Manager, and a DPH Food Service Director.

[2] The original contract contains a provision stating that the percentage markup may be adjusted 24 months after contract commencement and every 12 months thereafter. According to Assistant Director Moayed, this provision is an error and would be removed in the final Modification No. 2 after Board of Supervisors approval.

since August 2019 (the bid due date). OCA may audit Bay Cities' accounting records to ensure that reported prices are accurate.

Performance

The contract allows DPH to: (a) monitor and document contractor's performance and provide documentation to OCA; (b) inspect goods received from contractor immediately upon delivery and reject or return incorrect or damaged goods; (c) establish quality control measures and provide documentation of any product defects to OCA; and (d) provide OCA with documentation of unsatisfactory contractor performance. According to Taraneh Moayed, OCA Assistant Director, DPH has not made any complaints to OCA regarding contractor performance, and therefore OCA deems that Bay Cities Produce is meeting its contractual obligations. DPH provided our office with documentation of the vendor's food safety certifications and timely produce deliveries for General Hospital. As of this writing, DPH is compiling performance documentation for the vendor's deliveries to Laguna Honda.

FISCAL IMPACT

The proposed Modification No. 2 would increase the not-to-exceed amount of the Bay Cities Produce contract by $6,049,854, for a total not to exceed $12,067,569. Using actual expenditures to date, OCA projects average future contract expenditures of $121,729 per month. Actual and projected expenditures are shown in Exhibit 2 below.

Exhibit 2: Actual and Projected Contract Expenditures

Actual Expenditures (Oct 2019 through Feb 2023)	$4,938,136
Average Monthly Spend	121,729
Remaining Months (Mar 2023 through Sep 2026)	44
Projected Expenditures	$5,356,071
Contingency (15%)	803,411
Total Actual & Projected Expenditures	**$11,097,618**

Source: OCA, BLA Analysis

OCA has revised its calculations to show that there are 44 remaining months in the contract term, rather than 54 months, which was used to calculate the proposed not-to-exceed amount of $12,067,569. That amount also included a contingency of $1,574,031, which is 15 percent of all actual and projected expenditures. However, since actual expenditures have already been expended, the Budget and Legislative Analyst recommends reducing the contingency to $803,411, which is 15 percent of projected expenditures for the remaining term. Based on actual and projected contract expenditures, the Budget and Legislative Analyst recommends reducing the not-to-exceed amount of the contract by $967,569, for a total not to exceed $11,100,000.

The contract is funded by the annual operating budgets for San Francisco General Hospital and Laguna Honda Hospital, which are supported by Medi-Cal and the City's General Fund.

RECOMMENDATIONS

1. Amend the proposed resolution to reduce the contract not-to-exceed amount by $967,569, for a total not to exceed $11,100,000.
2. Approve the resolution as amended.

Items 9 & 10 **Files 23-0204 & 23-0342**	**Department:** Airport

EXECUTIVE SUMMARY

Legislative Objectives

- **File 23-0204** is a resolution that would approve the 2023 Lease and Use agreement between the City and 29 airlines to conduct flight operations at the Airport for a 10-year term from July 1, 2023 through June 30, 2033.
- **File 23-0342** is a resolution that would approve the 2023 Lease and Use agreement between the City and an additional 11 airlines to conduct flight operations at the Airport for a 10-year term from July 1, 2023 through June 30, 2033.

Key Points

- According to Airport staff, there are currently 60 airlines operating at the Airport. Of the 60 airlines, 40 signatory airlines are under the Airport's 2011 Lease and Use Agreement and 20 are "non-signatory airlines" operating under month-to-month Airline Operating Permits and Terminal Space and Use Permits. Non-signatory airlines pay a 25 percent premium on landing fees and a higher security deposit compared to signatory airlines.
- The original term of the 2011 Lease was July 1, 2011 through June 30, 2021. Airport staff and signatory airlines suspended negotiations of a new lease due to the impact of the COVID-19 pandemic on airport operations, and the Board of Supervisors approved a two-year extension of the term for the 2011 Lease to a new expiration date of June 30, 2023.
- Rental rates, landing fees, and related fees are adjusted annually according to the Airport's "residual rate setting methodology (breakeven policy)" such that the total amount of airline revenues received by the Airport together with non-airline revenues received by the Airport, including concession and parking revenues, is equal to total Airport costs, including debt service and operating costs.
- The proposed lease creates a new Operating Revenue and Capital Improvement Fund (ORCIF) totaling $800 million over the 10-year term and increases annually to account for inflation, among other changes. According to the proposed lease, ORCIF funds "may be used for any lawful purpose for which Airport Revenues may be used."

Fiscal Impact

- The proposed new lease and use agreement with the 40 signatory airlines are estimated by Airport staff to provide approximately $6.1 billion in revenues to the Airport, over the 10-year lease term, including $3.4 billion in airline rents and $2.6 billion in landing fees.

Recommendation

- Approve the proposed resolutions.

MANDATE STATEMENT

Section 2A.173 of the City's Administrative Code authorizes the Airport to negotiate and execute leases of Airport lands and space in Airport buildings without undergoing a competitive bid process, as long as the original term of the lease does not exceed 50 years.

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

2011 Airport Lease & Use Agreement

According to Airport staff, there are currently 60 airlines operating at the Airport. Of the 60 airlines, 40 signatory airlines are under the Airport's 2011 Lease and Use Agreement and 20 are "non-signatory airlines" operating under month-to-month Airline Operating Permits and Terminal Space and Use Permits. The airline lease and use agreement set the rate making methodology, legal and business terms for the operation of airlines at the airport, and gate allocation and operating procedures. Non-signatory airlines pay a 25 percent premium on landing fees and a higher security deposit compared to signatory airlines.

The original term of the 2011 Lease was July 1, 2011 through June 30, 2021. According to a February 7, 2023 memorandum from the Airport Director to the Airport Commission on the award of the 2023 Lease and Use Agreement (2023 Airport Lease Award Memo), airport staff and signatory airlines suspended negotiations of a new lease due to the impact of the COVID-19 pandemic on airport operations, and the Airport Commission approved a two-year extension of the term for the 2011 Lease for a new expiration date of June 30, 2023, which was approved by the Board of Supervisors in May 2021 (File 21-0335). The Airport and signatory airlines later resumed negotiations of a new lease and have agreed to the terms of the 2023 proposed lease.

Residual Rate Setting Methodology

The rent and landing fees, which are charged by the Airport to the airlines, are determined by the Airport's "residual rate setting methodology (breakeven policy)" set forth in the 2011 Lease. Under such methodology, the rental rates, landing fees, and related fees are adjusted annually such that the total amount of airline revenues received by the Airport together with non-airline revenues received by the Airport, including concession and parking revenues, is equal to total Airport costs, including debt service and operating costs.

According to Exhibit O of the 2023 proposed lease, each airline's terminal area rentals are calculated by multiplying the terminal area rental rate by the airline's leased terminal space (in square feet). Terminal area rental rates are based on net terminal area expenses and gross terminal space and vary according to five categories of terminal space (i.e., the rental rates for check-in counters are different than the rental rates for baggage claim lobbies). Landing fees are

calculated by multiplying net airfield area expenses by the airline's projected share of total landed weight (in thousands of pounds). In addition, each airline pays a surcharge (which is applied to both terminal area rentals and landing fees) to cover the expenses of public space in the terminal. The Pro Forma for FY 2023-24 from Exhibit O of the 2023 proposed lease showing the calculation of terminal area rentals, rental rate structure, and calculation of landing fees is provided in Attachment 1.

Airport Economic Recovery

According to traffic and non-airline revenue performance data presented to the Airport Commission on January 17, 2023, the number of enplaned passengers for both domestic and international air travel was 82 percent of 2019 levels in November 2022, and non-airline revenues were 104 percent of 2019 levels due to strong parking, ground transportation, and car rental revenues according to the meeting minutes. Although air traffic has not fully recovered, Airport staff report that airline revenues continue to be sufficient together with non-airline revenues to cover the Airport's costs due to the breakeven policy.

DETAILS OF PROPOSED LEGISLATION

File 23-0204 is a resolution that would approve the 2023 Lease and Use agreement between the City and 29 airlines to conduct flight operations at the Airport for a 10-year term from July 1, 2023 through June 30, 2033.

File 23-0342 is a resolution that would approve the 2023 Lease and Use agreement between the City and an additional 11 airlines to conduct flight operations at the Airport for a 10-year term from July 1, 2023 through June 30, 2033.

The proposed resolutions would also affirm the Planning Department's determination under the California Environmental Quality Act and authorize the Airport Director to enter into immaterial modifications to the lease.

Signatory Airlines

All signatory airlines execute the same form of the lease with slight differences reflecting the specific airline's allocation of space. To date, the Airport Commission has awarded the proposed 2023 lease to 40 airlines. The Airport Commission awarded the proposed 2023 lease to the following 29 signatory airlines on February 7, 2023:

1. ABX Air, Inc.
2. Aerovias de Mexico S.A. de C.V. dba Aeromexico
3. Air China Limited
4. Air India Limited
5. Air New Zealand Limited
6. Air Transport International, Inc.
7. Alaska Airlines, Inc.
8. All Nippon Airways Co, Limited
9. Asiana Airlines Inc.
10. China Eastern Airlines Co. Ltd
11. Condor Flugdienst GMBH
12. Delta Air Lines, Inc.
13. Deutsche Lufthansa AG dba Lufthansa German Airlines
14. Emirates
15. EVA Airways Corporation
16. Federal Express Corporation
17. Japan Airlines Co., Ltd.
18. Kalitta Air LLC
19. Koninklijke Luchtvaart Maatschappij N. V. dba KLM Royal Dutch Airlines
20. Korean Air Lines Co., Ltd
21. Nippon Cargo Airlines, Inc.
22. Scandinavian Airlines of North America Inc dba Scandinavian Airlines SAS
23. Singapore Airlines Limited
24. Societe Air France dba Air France
25. Southwest Airlines Co.
26. Sun Country, Inc.
27. Turk Hava Yollaria A.O. dba Turkish Airlines
28. United Airlines, Inc.
29. Virgin Atlantic Airways Limited

In addition, the Airport Commission awarded the proposed 2023 lease to the following 11 airlines on March 21, 2023:

30. Air Canada
31. American Airlines, Inc.
32. British Airways, PLC
33. Cathay Pacific Airways, Ltd.
34. China Airlines, Ltd.
35. China Southern Airlines Company Limited
36. Frontier Airlines, Inc.
37. Philippine Airlines, Inc.
38. Swiss International Air Lines, Ltd.
39. TACA International Airlines, S.A. (TACA dba Avianca)
40. WestJet

File 23-0204 would approve leases between the City and airlines one through 29 above, and File 23-0342 would approve leases between the City and airlines 30 through 40. According to the 2023 Airport Lease Award Memo, the proposed 2023 lease has been offered to all airlines operating at the Airport and will continue to be offered to all other airlines, including new entrants, through the remainder of its term.[1]

Key Lease Terms

Key lease terms are summarized in Exhibit 1 below, based on the 2023 Airport Lease Award Memo.

[1] According to Airport staff, there were fewer signatory airlines initially under the proposed lease (29) compared to the existing lease (40) because some airlines could not get the necessary corporate approval within the timeframe or may elect not to sign the 2023 lease.

Exhibit 1: Proposed 2023 Airport Lease and Use Agreement Terms

Term	July 1, 2023 through June 30, 2033 (10 years)
Rate-Making Methodology	Existing residual rate setting methodology (described above) is maintained. Signatory airlines pay terminal area rentals, landing fees, and other usage fees, which are adjusted annually by the Commission to ensure that total airline and non-airline revenues are equal to total airport costs, including debt service.
Annual Service Payment	Existing Airport Annual Service Payment to the City's General Fund is maintained at the greater of $5 million or 15% of Airport concession revenues.
Operating Reserve and Capital Improvement Fund	Establishes an operating reserve and capital improvement fund totaling $800 million over the 10-year term and adjusted annually for inflation.
Shared Use Equipment	Expands rights of the Airport Commission to install shared use equipment throughout the Airport, including in exclusive use spaces of airlines, to enhance operational efficiency.
Preferential Use Gate Allocation	Expands review period of airline seat capacity to allocate preferential use gates to encourage consistent use of preferential use gates throughout the year.
Gate Accommodations	Enhances rights of the City to accommodate flights at preferential use gates of signatory airlines to maximize the use of a gate and capacity and efficiency of the Airport.
Sustainable Aviation Fuel Working Group	Establishes a Sustainable Aviation Fuel Working Group of Airport staff and signatory airlines that would determine how the parties can cooperate to increase the uptake of sustainable aviation fuel at the Airport. The working group will be chaired by the Airport Director.
Ground Service Equipment Electrification	Establishes a mutual goal to achieve 100% electric-powered ground service equipment at the Airport.
Airline Relocation Costs	Clarifies financial liability for airline relocations. If an airline initiates its relocation within the Airport, that airline is financially responsible for the move and for any required secondary relocations of other airlines. If the Airport initiates relocation of an airline, the Airport is financially responsible, subject to rate recovery under the lease.
Digital Information Working Group	Establishes a Digital Information Working Group chaired by the Airport Director and consisting of Airport staff and signatory airlines that will identify data on airport infrastructure and airline operations that could be exchanged to enhance Airport operations and improve the experience of Airport guests.
Commercialization of Digital Assets	Acknowledgement that the Airport has the sole and exclusive right to control, manage, and utilize all Airport Proprietary Content.

Source: 2023 Airport Lease Award Memo

Operating Revenue and Capital Improvement Fund

As shown in Exhibit 1 above, the proposed lease creates a new Operating Revenue and Capital Improvement Fund (ORCIF) totaling $800 million over the 10-year term and increases annually to account for inflation. According to the proposed lease, ORCIF funds "may be used for any lawful purpose for which Airport Revenues may be used." Expenditures on capital improvements from the fund are subject to the lease's review process for capital improvements. The proposed lease establishes a minimum and a maximum annual ORCIF deposit for each year and states that no deposit shall be made to the fund in any year when the unencumbered and unallocated balance of the fund exceeds $650 million. Deposits to the fund will be funded by airline revenues.

FISCAL IMPACT

As shown in Exhibit 2 below, the proposed new lease and use agreement with the 40 signatory airlines are estimated by the Airport to provide approximately $6.1 billion in revenues to the Airport, over the 10-year lease term.[2] In FY 2023-24, total airline rents are budgeted at $371.5 million, of which $283.1 million is provided by the Lease and Use Agreement for the 40 airlines, with the remaining $88.4 million in rental revenues coming from non-signatory airlines. Total landing fees are budgeted at $300.4 million in FY 2023-24, of which $217.4 million is provided by the Lease and Use Agreement, with the remaining $83.0 million in landing fees coming from non-signatory airlines.

Exhibit 2: Estimated Total Annual Lease Revenues

Fiscal Year	Terminal Area Rental Revenue	Landing Fees	Total Lease Revenue	Annual Percent Change
FY 2023-24	$283,070,971	$217,443,856	$500,514,827	
FY 2024-25	297,856,096	230,664,442	528,520,538	6%
FY 2025-26	312,526,623	242,336,064	554,862,687	5%
FY 2026-27	327,807,755	252,126,441	579,934,196	5%
FY 2027-28	339,703,578	262,312,349	602,015,927	4%
FY 2028-29	349,946,602	270,234,181	620,180,784	3%
FY 2029-30	360,455,258	278,395,254	638,850,513	3%
FY 2030-31	371,279,173	286,802,790	658,081,963	3%
FY 2031-32	382,427,805	295,464,235	677,892,040	3%
FY 2032-33	393,910,897	304,387,256	698,298,154	3%
Total	**$3,418,984,758**	**$2,640,166,870**	**$6,059,151,628**	

Source: Airport

[2] File 23-0204 would generate an estimated $5.1 billion in revenues over the 10-year term from 29 signatory airlines, and File 23-0342 would generate an estimated $1.0 billion in revenues over the 10-year term from 11 additional signatory airlines.

The estimated revenue is based on: (a) projected terminal use and landed weight of the 40 airlines through FY 2027-28; (b) proforma terminal area rental rates from the proposed lease, increased annually by three percent per year; and (c) proforma landing fee rates from the proposed lease, increased annually by two percent per year.

As discussed above, the revenues generated by the proposed leases are calculated by the Airport's residual rate setting methodology (breakeven policy), such that the proposed new leases would continue to result in the Airport's budget being fully balanced by the revenues paid by the airlines to the Airport after considering the Airport's budgeted expenditures and all non-airline revenues. Changes to Airport expenses, including debt service, and non-airline revenues will result in changes in airline revenues.

RECOMMENDATION

Approve the proposed resolutions.

Attachment 1: FY 2023-24 Pro Forma for Terminal Rentals and Landing Fees from Exhibit O of Proposed ABX Air, Inc. Lease

Attachment 3

CALCULATION OF TERMINAL AREA RENTALS AND RENTAL SURCHARGE
(BASIC RENTAL ADJUSTMENT)
SAN FRANCISCO INTERNATIONAL AIRPORT
Fiscal Year 2023/24
(dollars in thousands, except for rates)

		Pro Forma 2024
Terminal Area Expenses		
Operation and Maintenance Expenses		$ 390,267
Debt Service		453,436
Small Capital Outlays		2,699
Equipment		1,185
Annual Service Payment		45,773
Annual ORCIF Deposit		196,844
Deferred Aviation Revenue		(196,844)
		$ 893,360
÷ 'Gross Terminal Space (square feet)		5,916
= Basic Rate		$151.02
x Airline Leased Space (square feet)		1,742
= Basic Rentals	[A]	$ 263,048
Rental Surcharge (Basic Rental Adjustment)		
Basic Rate		$151.02
x Public Space		4,174
= Cost of Public Space		$630,312
- Non-airline revenues		(175,077)
- PFCs Classified as Revenues		(150,000)
+ Net Expense - GT and Parking Area		-
Rental Surcharge		$ 305,236
Allocation of Rental Surcharge (Basic Rental Adjustment)		
Terminal Area Rental Surcharge	[B]	$ 152,618
Landing Fee Surcharge		152,618
		305,236
Terminal Area Rentals		
Basic Rentals	[A]	$ 263,048
Terminal Area Rental Surcharge	[B]	152,618
		$ 415,666
Effective Average Rental Rate		
Basic Rate		$151.02
Rental Surcharge Rate		87.62
		$238.63

Note: Amounts may not add due to rounding.

2023-2033 Lease and Use Agreement
ABX Air, Inc.

Exhibit O, Page 12

Attachment 4

DERIVATION OF REQUIRED AIRLINE RENTAL RATE STRUCTURE

SAN FRANCISCO INTERNATIONAL AIRPORT

Fiscal Year 2023/24

(dollars in thousands, except for rates)

Airline Leased Space (square feet)		Pro Forma 2024
Category I		321
Category II		552
Category III		195
Category IV		633
Category V		40
		1,742

Equivalent Category I (square feet)	Relative value	
Category I	1.00	321
Category II	0.75	414
Category III	0.50	98
Category IV	0.25	158
Category V	0.10	4
		995

Required Category I	
Terminal Area Rentals	$ 415,666
Divided by Equivalent Category I space (square feet)	995
Required Category I Rate (per square foot)	$417.58

Terminal Rental Rates	Relative value	
Category I	1.00	$417.58
Category II	0.75	313.19
Category III	0.50	208.79
Category IV	0.25	104.40
Category V	0.10	41.76

Note: Amounts may not add due to rounding.

2023-2033 Lease and Use Agreement
ABX Air, Inc.

Exhibit O, Page 13

Attachment 5

CALCULATION OF LANDING FEES AND LANDING FEE RATE

SAN FRANCISCO INTERNATIONAL AIRPORT

Fiscal Year 2023/24

(dollars in thousands, except for rates)

	Pro Forma 2024
BASIC LANDING FEES	
Operation and Maintenance Expenses	$105,388
Debt Service	43,403
Small Capital Outlays	460
Equipment	671
Annual ORCIF Deposit	53,156
	$203,077
Non-airline revenues	(4,616)
PFCs Classified as Revenues	(1,000)
Deferred Aviation Revenue deficit (surplus)	(53,156)
Net expense (revenue) - Other Leased Areas	3,115
Net expense (revenue) - West of Bayshore Area	2,471
Airfield Area Net Expense	$149,891
÷ Composite landed weight forecast (in 1,000 lbs units)	36,050
= Basic Rate (per 1,000 lbs.)	$4.16
LANDING FEE SURCHARGE	
Landing Fee Surcharge	$ 152,618
Net revenue - GT and Parking Area	(52,048)
	$ 100,570
÷ Composite landed weight forecast (in 1,000 lbs units)	36,050
= Landing Fee Surcharge Rate (per 1,000 lbs.)	$2.79

Landing Fees	
Basic Landing Fees	$ 149,891
Landing Fee Surcharge	100,570
	$ 250,461
Landing Fee Rate	
Basic Rate	$4.16
Surcharge Rate	2.79
	$6.95

Note: Amounts may not add due to rounding.

2023-2033 Lease and Use Agreement
ABX Air, Inc.

Exhibit O, Page 14

Item 12 **File 23-0377**	**Department:** Mayor's Office of Housing and Community Development

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve (1) a $14.8 million amended and restated loan agreement with Sunnydale Black 3A Housing Partners, L.P. to develop 80 affordable housing units and (2) a $12.4 million amended and restated loan agreement with Sunnydale Commercial LLC to develop commercial space within the Sunnydale Block 3A development area.

Key Points

- Sunnydale Block 3A will include 60 replacement units for current Sunnydale public housing residents, 19 additional affordable units, and one manager's unit.
- The proposed commercial loan is funding the development of 20,028 square feet of retail and neighborhood services space, including an early childhood education center, a Department of Public Health (DPH) operated health and wellness center, Mercy Housing's customer service center serving the entire Sunnydale project, and two retail spaces. City funding includes tenant improvements for the DPH health center and the Mercy office.

Fiscal Impact

- The total development cost per residential unit for Sunnydale Block 3A is $1,235,676, of which the City is funding $340,901 per unit.
- The City loan is funded by 2019 general obligation bond proceeds, HOME Investment Partnership Program funds provided by HUD, and Low and Moderate Income Housing Asset Fund monies.

Recommendation

- Approve the proposed resolution.

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.

BACKGROUND

Sunnydale HOPE SF History

In 2007, the San Francisco Housing Authority, in partnership with the Mayor's Office of Housing and Community Development (MOHCD), launched the HOPE SF initiative to revitalize the City's most distressed public housing sites into mixed-income communities comprised of affordable housing, including replacement units for existing public housing and new affordable units, and production of market rate housing. Sunnydale is the largest of the four HOPE SF sites undergoing revitalization as part of the HOPE SF initiative. Sunnydale is located in the Visitacion Valley Neighborhood and was comprised of 775 units of public housing across 50 acres.

In 2007, the San Francisco Housing Authority and HOPE SF released a request for qualifications to develop the four large-scale target sites. The San Francisco Housing Authority selected Mercy Housing California (Mercy) and The Related Companies of California (Related), as co-developers for the Sunnydale development. Mercy and Related established a separate entity named Sunnydale Development Co., LLC (Developer) to plan and develop the project.

Development Agreement and Master Development Agreement

In January 2017, the Board of Supervisors approved a development agreement (File 16-1164) and a master development agreement (File 16-1356) between the City, the San Francisco Housing Authority, and Sunnydale Development Co., LLC, to facilitate the development of the project. The development agreement included the phasing plan and master infrastructure plan for the master development. The proposed Sunnydale development will provide 1,705 units of housing by replacing the 775 units of public housing on the site, adding approximately 200 affordable residential units (up to 60 percent area median income), and developing up to 730 market rate units. The master plan also includes developing new street and utility infrastructure, 3.6 acres of new open spaces, and an estimated 60,000 square feet of new neighborhood space.

The Sunnydale HOPE SF project is being developed across three main phases for over 25 years. According to MOHCD staff, the affordable parcels are expected to be completed in 2033, subject to financing availability, compared to estimated completion in 2030 under the original schedule. To date the City has provided $9.8 million for master planning and $92.0 million for vertical and horizontal development. Sunnydale Block 3A will be the fourth Sunnydale affordable housing

project and is set to begin construction in May 2023.[1] Phase 1A3 infrastructure, which includes Blocks 3A and 3B and Community Building Block 1, began construction in May 2022 and is anticipated to reach substantial completion in summer 2023. In February 2023, the Board of Supervisors approved a permanent gap loan for Block 3B for a not to exceed amount of $31,506,016 (File 23-0062), and MOHCD is now requesting approval for permanent financing for Block 3A.

Sunnydale Block 3A

Sunnydale Block 3A is a proposed 80-unit affordable housing development within Phase 1A3, located at 1545 Sunnydale Avenue. The 80 units include 60 replacement units for current Sunnydale public housing residents, 19 additional affordable units, and one manager's unit. The units include four studios, 24 one-bedrooms, 28 two-bedrooms, 16 three-bedrooms, and eight four-bedrooms.

The project will also include approximately 20,028 square feet of retail and neighborhood services space, including an early childhood education center, a Department of Public Health (DPH) operated health and wellness center to replace the existing center in the Sunnydale administration building, Mercy's customer service center serving the entire Sunnydale project, and two retail spaces. Block 3A will share an underground parking garage with Block 3B which will be located in Block 3B.

Construction for Block 3A is scheduled to start in May 2023 and to be completed in November 2024. Construction for neighboring Block 3B began in April 2023. Sunnydale Blocks 3A and 3B are shown within Phase 1A3 as "Block 3" in Exhibit 1 below. Exhibit 2 shows Blocks 3A and 3B in greater detail.

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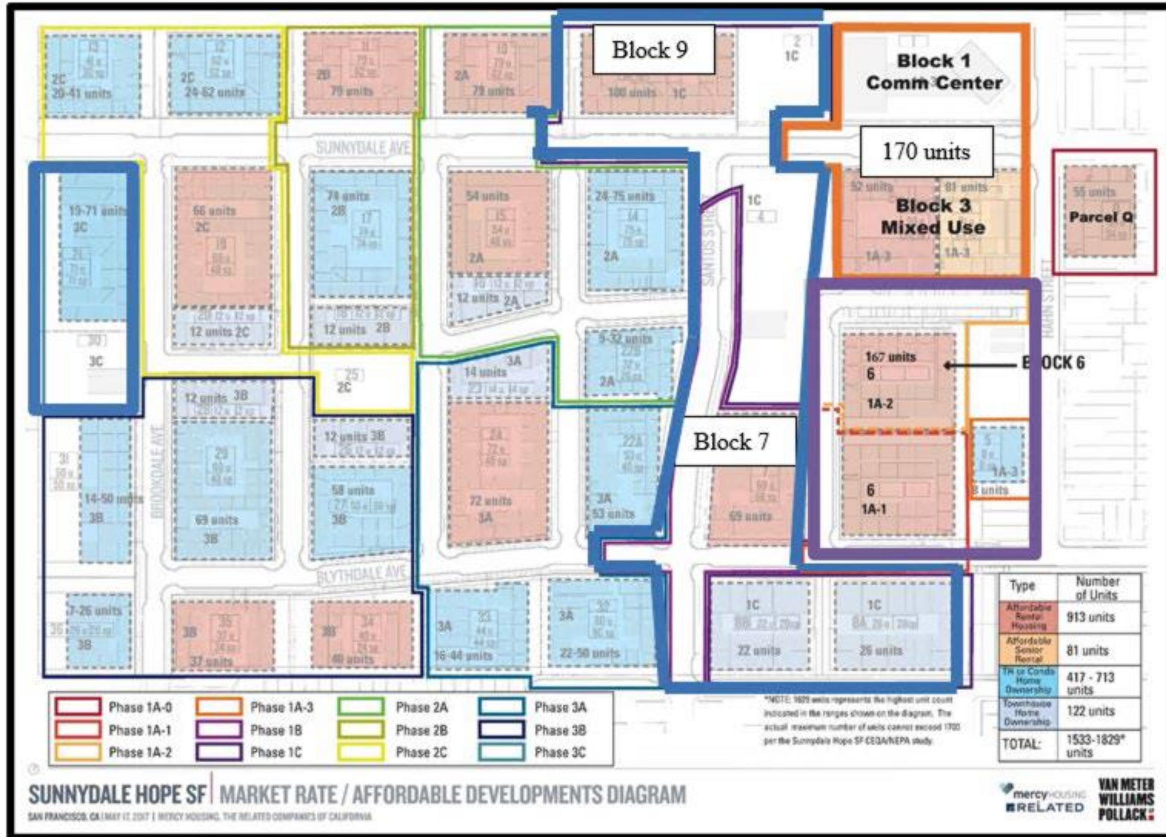
[1] The first Sunnydale Hope SF development was Parcel Q, also known as Casala, and the second development was Block 6, also known as 290 Malosi.

Exhibit 1: Sunnydale HOPE SF Project Phases



Source: MOHCD

Exhibit 2: Sunnydale HOPE SF Blocks 3A and 3B

Source: MOHCD

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would:

1) approve a not-to-exceed $14,862,818 amended and restated loan agreement for a term of 57 years between the City and Sunnydale Block 3A Housing Partners, L.P.[2] to construct Sunnydale Block 3A, an 80-unit affordable housing project;

[2] The Developer established Sunnydale Block 3A Housing Partners, L.P., a separate entity, to develop Block 3A.

2) approve a not-to-exceed $12,409,247 amended and restated loan agreement for a term of 57 years between the City and Sunnydale Commercial LLC[3] to construct the community-serving commercial project located on the ground floor of Block 3A;
3) find that the loan agreement is consistent with the Mitigation Monitoring and reporting Program under the California Environmental Quality Act, as well as the City's General Plan and policy priorities in the Planning Code; and
4) authorize the Director of MOHCD to amend the Loan Agreement, provided amendments do not increase the obligations or liabilities to the City.

Loan Agreements

Residential Loan

The original loan agreement provided by MOHCD in 2020 was for $1,850,000 for predevelopment costs. In 2022, the Affordable Housing Loan Committee approved another $4,727,660 predevelopment loan to cover costs associated with Block 3A's portion of the parking garage located in Block 3B for a total predevelopment loan of $6,577,660. MOHCD proposes to amend the loan agreement to increase the loan amount by $8,285,158 to complete development and construction, including permanent financing. Under the proposed amended loan agreement, the total loan amount to Sunnydale Block 3A Housing Partners, L.P. would increase to a not-to-exceed $14,862,818.

The proposed residential loan agreement includes affordability restrictions to preserve the affordability of the housing units in the proposed development. The agreement specifies the affordability levels for each unit and requires the non-profit housing operator to maintain these for the duration of the agreements unless agreed to by the City. Of the 79 affordable units (excluding the manager's unit), the 60 public housing replacement units are reserved for tenants holding U.S. Department of Housing and Urban Development (HUD) Section 8 vouchers and are limited to households earning up to 50 percent MOHCD defined area median income (AMI). The remaining 19 affordable units are limited to households earning up to 80 percent MOHCD AMI.

Commercial Loan

Under the proposed loan agreement, the total loan amount to Sunnydale Commercial LLC would not exceed $12,409,247. The loan would cover costs associated with building the cold and warm shell[4] for the community-serving commercial spaces located on the ground floor of Block 3A as well as tenant improvements for Mercy's customer service center and the DPH wellness center. According to MOHCD staff, the $12,409,247 loan includes a $2 million bridge loan for the DPH wellness center, which DPH will repay with Mental Health Services Act funds when funds become

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[3] The Developer established Sunnydale Commercial LLC, a separate entity, to develop the Sunnydale Block 3A commercial project.

[4] A cold shell is a building without heating and plumbing. A warm shell is a building that contains those elements.

available according to terms in a forthcoming memorandum of understanding between DPH and MOHCD.

A declaration of restrictions will require all commercial spaces to be community-serving to benefit residents of Block 3A and the larger Sunnydale site.

Loan Repayment

Under both loan agreements, loan repayments are based on residual receipts for the residential and commercial project. The borrowers must repay the loans by the later of: (a) the 57th anniversary date of the recordation of the deed of trust or (b) the 55th anniversary of the date on which construction financing is converted into permanent financing. Simple interest will accrue to the loan principal balances at a rate of three percent per year.

Sponsor Performance

According to MOHCD, Mercy, the lead service provider for Block 3A, has no outstanding performance issues.

FISCAL IMPACT

Total Development Costs

The total development cost for the 80 units of housing is $98.9 million, as shown in Exhibit 3 below. Of the approximate $98.9 million in costs, $28.3 million (28.7%) are supported by City funds (including $1.1 million in accrued deferred interest), $10.9 million (11.0%) are supported by State funds, and $59.7 million (60.4%) are supported by private funds.

Exhibit 3: Total Development Sources and Uses of Funds

	Residential	Commercial	Total
Sources			
City			
MOHCD Loans	$14,862,818	$12,409,247	$27,272,065
MOHCD Deferred Interest	1,054,476		1,054,476
Subtotal, City	*15,917,294*	*12,409,247*	28,326,541
State			
HCD AHSC Loan	10,850,000		10,850,000
Private			
Permanent Loan	16,964,430		16,964,430
Tax Credit Equity	39,813,002		39,813,002
General Partner Equity	100		100
Deferred Developer Fees	2,900,000		2,900,000
Subtotal, Private	*59,677,532*		*59,677,532*
Total Sources	**$86,444,826**	**$12,409,247**	**$98,854,073**
Uses			
Acquisition	7,976	2,026	10,002
Hard Costs	63,628,332	9,569,016	73,197,348
Soft Costs	17,083,646	1,905,493	18,989,139
Reserves	624,773	382,712	1,007,485
Developer Fees	5,100,100	550,000	5,650,100
Total Uses	**$86,444,826**	**$12,409,247**	**$98,854,073**

Source: MOHCD

A companion resolution subject to Board of Supervisors' approval would allow MOHCD to execute a standard agreement with the California Department of Housing and Community Development (HCD) for an Affordable Housing and Sustainable Communities (AHSC) Program loan totaling $10,850,000 for the construction of Sunnydale Block 3A (File 23-0378), as shown in Exhibit 3 above.[5]

Funding Sources for City Loans

Sources of funds for the proposed amended and restated residential loan of $14,862,818 include:

- $9,203,177 in 2019 General Obligation Bond funds;[6]
- $2,362,641 in Low and Moderate Income Housing Asset Fund funds;[7]

[5] The proposed resolution would also allow MOHCD to execute a standard agreement with HCD for a AHSC grant totaling $10,355,299 for public transportation improvements near Block 3A (which are not included in the total development costs shown in Exhibit 1), for a total award of $21,205,299, including the loan and grant.

[6] In November 2019, San Francisco voters approved Proposition A, which provided for the issuance of up to $600 million in general obligation funds to finance the acquisition, rehabilitation, and construction of affordable housing.

[7] Upon dissolution of state redevelopment agencies, Office of Community Investment and Infrastructure (as the Successor Housing Agency) created the Low and Moderate Income Housing Asset Fund to collect proceeds from former redevelopment agency housing assets transferred to the City.

- $1,447,000 in HOME Investment Partnership Program funds provided by HUD to increase the housing stock for low- and very low-income persons;
- $1,800,000 in 2015 General Obligation Bond Funds for predevelopment costs;[8] and
- $50,000 in 75 Howard Gift Fund funds for predevelopment costs.[9]

Sources of funds for the proposed commercial loan of $12,409,247 include:

- $10 million in 2019 General Obligation Bond funds;
- $1,659,247 in Low and Moderate Income Housing Asset Fund funds; and
- $750,000 in HOME Program funds.

The City's Subsidy per Housing Unit

Total development costs for construction of Block 3A are $98.9 million or approximately $1.2 million per unit. The City's total subsidy for the housing development costs is $27.3 million, or $340,901 per unit, as shown in Exhibit 4 below. Total City funding shown below also includes $12.4 million in funding for development of the commercial space (discussed below).

Exhibit 4: City Subsidy for Affordable Housing Units

Number of Units	80	
Total residential area (sq. ft.)	91,700	
	Total Costs	*Residential Costs Only*
Development Cost	$98,854,074	$86,444,826
Total City subsidy	$27,272,065	$14,862,818
Development cost per unit	$1,235,676	$1,080,560
Development Cost per sq. ft.	$1,078	$943
City Subsidy per unit	$340,901	$185,785
City Subsidy per sq. ft.	$297	$162

Source: MOHCD

Cost Comparison to Similar Projects

According to a cost comparison of new affordable multifamily housing projects in the MOHCD loan evaluation of the proposed gap loan, the total development cost per unit is 40 percent above average compared to similar projects, and 23 percent above average excluding the commercial costs. The total development cost per unit for Sunnydale Block 3A is $1,235,676 compared to $879,884 for similar projects. Projects included in the comparison are similar projects in size, unit

[8] In November 2015, San Francisco voters approved Proposition A, which provided for the issuance of up to $310 million in general obligation funds to finance the acquisition, rehabilitation, and construction of affordable housing.

[9] In 2017, the Board of Supervisors authorized MOHCD to accept and expend a gift of $6,010,047 from RDF 75 Howard LP, the developer of a residential project located at 75 Howard Street, to the Citywide Affordable Housing Fund (File 16-1073).

count, target population, and construction type. Comparison projects also include other HOPE SF projects.

According to the MOHCD loan evaluation, Sunnydale Block 3A's construction costs are above average due to:

- Higher quality of exterior skin material compared to other projects because Block 3A is in a prominent location and a more complex structural design due to the slope of the site and elevated terraced landscapes.
- Fewer units compared to other HOPE SF projects and inclusion of a large commercial space (20,028 square feet) being built out to warm shell conditions, which adds $1.2 million in costs and is consistent with MOHCD's Underwriting Guidelines for community serving spaces.
- A higher parking ratio (0.75 parking spaces per unit) compared to other projects (0.5 parking spaces per unit on average). Block 3B houses parking for both Block 3A and Block 3B, and Block 3A's total development costs include $4.7 million for Block 3B's portion of the parking garage.
- HOPE SF projects have a higher bedroom count compared to non-HOPE SF projects and are required to provide In-unit laundry hookups for three- and four-bedroom units, which is not a requirement for most other affordable housing projects.
- Cost estimates are higher than previously anticipated due to inflation and construction escalation. Since March 2020, hard costs have increased by 33 percent due to inflation according to MOHCD.
- Anticipated delays to Block 3A construction from relocating power poles along Block 3A on Hahn Street.
- Higher general conditions costs from potential delays in Block 3A's construction, which would limit efficiencies in sharing general conditions cost with neighboring Block 3B due to staff and resources not overlapping as planned.
- The cost of temporary generators to provide power to the project during construction activities, as the project may not be able to acquire temporary power from PG&E in time.

Residential Operating Revenues and Expenses

According to the 20-year cash flow analysis for Sunnydale Block 3A, the residential project will have sufficient revenues to cover operating expenses, operating reserves, construction loan payments, and management fees. Project revenues consist of tenant rents and HUD Project Based Section 8 rental subsidies for 60 units. Total operating expenses for the project include ground lease base rent payments to the San Francisco Housing Authority. A portion of net income after operating expenses (residual receipts) will be used to repay the proposed MOHCD residential loan, and the remaining portion will be used to repay the HCD loan.

Commercial Space

The proposed loan will fund construction of warm and cold shell for 20,028 square feet of commercial space, as well as tenant improvements and replacement and operating reserves for a total estimated cost of $12.4 million. The commercial space will be divided as follows:

- 8,070 square feet for the Felton Institute Early Childhood Education Center ($3.6 million in project costs);
- 4,775 square feet for the Mercy customer service office, available to all Sunnydale residents ($3.7 million in project costs);
- 2,662 square feet for the DPH health and wellness center ($2.4 million in project costs);
- 2,926 square feet of retail space, currently planned for a grocer or food-related business ($1.9 million in project costs); and
- 1,204 square feet of retail space, currently planned for a food hall or food-related business ($0.8 million in project costs).

According to the residential pro-forma provided by MOHCD, the commercial space is not expected to contribute revenue to the residential operating budget. According to Section 7.2 of the proposed commercial loan, leases of commercial space may be for for-profit, at market rate, or community serving purposes, at below market rate. Surplus cash generated from market-rate leases will accrue to MOHCD per the Residual Receipts policy and be used for the public benefit.

Two Retail Spaces

MOHCD is working with OEWD to identify tenants for the food-related spaces through a Request for Qualifications process in late 2023. According to the MOHCD loan evaluation, the Sponsor may need to seek larger, less local tenants if the Sponsor cannot identify suitable local tenants. The San Francisco Housing Authority will master lease the commercial space to Mercy, and Mercy will sublease the spaces to individual commercial tenants. The pro-forma prepared by MOHCD for the commercial spaces shows that only community-serving tenants would generate a positive cash flow for the project (in the first 10 years only), since they have a lower property tax rate.

Health Center

The commercial loan includes $2.4 million for the DPH health and wellness center and $3.6 million for the Felton Institute Early Childhood Education Center. DPH will provide $2 million to cover an estimated $1.0 million in tenant improvements for the wellness center, with the remaining $1.0 million covering a portion of MOHCD costs including permit fees and warm and cold shell costs for the wellness center.

Early Childhood Education Center

MOHCD will provide funding for cold and warm shell costs for the Felton Institute Early Childhood Education Center. Tenant improvements will be paid for by the Felton Institute according to the terms of a 2019 memorandum of understanding between the Sponsor and the Felton Institute.

Mercy Customer Service Center

The proposed commercial loan includes approximately $3.7 million for the Mercy Customer Service Center, including $1.3 million for tenant improvements, subject to MOHCD approval. The customer service center was originally planned to be a centralized office for Sunnydale property management and services staff to reduce costs. However, the center is not expected to lead to

cost efficiencies as originally planned since the Sponsor prefers that each building include property management and services staff. The Sponsor plans to reduce the sizes of property management and services offices in future Sunnydale buildings to accommodate additional affordable units.

The service center will provide office space for 14 Mercy staff and eight staff from two community-based organizations currently working at Sunnydale, Visitacion Valley Strong Families, and the YMCA. The center will be a centralized resource for Sunnydale residents and will also provide space for Mercy staff to gather for collaboration.

Commercial Space Funding Level

MOHCD typically does not fund tenant improvements. According to Ryan Vanzuylen, MOHCD project manager, the scale of the City's funding for the commercial spaces (including the warm shells for five commercial spaces and the tenant improvements for DPH health center and the office for Mercy Housing) is part of a larger strategy to enhance economic activity within the development area.

RECOMMENDATION

Approve the proposed resolution.

Item 15 **File 23-0380**	**Department:** Mayor's Office of Housing and Community Development

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve a $50,495,000 amended and restated loan agreement for a term of 57 years between the City and HV Partners 3, L.P. to construct Hunters View Phase III, an affordable housing project.

Key Points

- Hunters View Phase III includes 118 public housing and affordable housing units over two buildings, new infrastructure, community-serving ground-floor spaces, and a neighborhood park. In 2021, the Board approved a $33.9 million loan for infrastructure improvements, which are ongoing and expected to be complete in 2025, simultaneous with the proposed residential construction.
- Unit costs are 40 percent higher than comparable MOHCD projects due to parking requirements, family-sized units (three to five bedrooms), and laundry hookups.
- The proposed loan includes $1.3 million to construct a cold shell for 3,848 square feet of commercial space between the two buildings. MOHCD, the project sponsor, and the Hunters View Resident Council intend to finalize plans for the two commercial spaces by January 2024.

Fiscal Impact

- Excluding infrastructure costs, the total development cost for the 118 residential units is $140.7 million, or $1.2 million per unit. The City's subsidy for the housing development costs is $50.5 million, or $427,924 per unit.
- The City loan is funded by 2019 general obligation bond proceeds, HOME Investment Partnership Program funds provided by HUD, and Low and Moderate Income Housing Asset Fund monies.

Recommendation

- Approve the proposed resolution.

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.

BACKGROUND

In 2007, the San Francisco Housing Authority (SFHA) in partnership with the Mayor's Office of Housing and Community Development (MOHCD) launched the HOPE SF initiative to revitalize the City's most distressed public housing sites into mixed-income communities comprised of affordable housing, including replacement units for existing public housing and new affordable units, and production of market-rate housing. Hunters View is one of the four sites undergoing revitalization as part of the HOPE SF initiative, which also includes Potrero Terrace, Alice Griffith, and Sunnydale. Hunters View is located in the Bayview Hunters Point neighborhood and was originally comprised of 267 public housing units on approximately 21 acres of land.

Development Agreements

In 2007, SFHA released a Request for Qualifications (RFQ) for developers to develop the Hunters View site. SFHA selected The John Stewart Company, in collaboration with Ridge Point Nonprofit Housing Corporation and Devine and Gong, Inc., to develop the master development plan for the Hunters View site. The three developers established a separate entity named Hunters View Associates, L.P. to plan and develop the Hunters View project.

The Hunters View development will provide up to 800 residential units by replacing the 267 units of public housing on the site, adding 137 affordable rental units (for households earning up to 50 percent of the Area Median Income, or AMI), and developing approximately 396 market-rate for-sale units. The master plan also includes developing new street and utility infrastructure, parks, and space for community-based organizations.

The Hunters View HOPE SF project is being developed over three phases, as shown below in Exhibit 1. Phase I, completed in 2013, includes 107 public housing and affordable housing units across three new buildings, as well as new infrastructure, offices, and Promontory Park. Phase II, completed in 2018, includes 179 public housing and affordable housing units over three new buildings, as well as new infrastructure, Ironwood Park, and a community hub with a childcare center, wellness center, and additional services offices. Approximately 64 market rate units are awaiting Planning Department approval. SFHA and Hunters View Associates L.P. executed a master development agreement in 2009, and disposition and development agreements (DDA) for Phases I and II in 2010 and 2013. SFHA and Hunters View Associates L.P. entered into a disposition and development agreement (DDA) for Phase III in January 2021. All DDAs are approved by the U.S. Department of Housing and Urban Development (HUD).

Phase III includes 118 public housing and affordable housing units over two buildings located on two lots, new infrastructure, community-serving ground-floor spaces, and a neighborhood park. Demolition of the former Phase III public housing buildings to their foundation is complete and tenants have been relocated to new housing units in Phases I and II. The public housing replacement and affordable housing unit mix consists of 52 one bedrooms, 11 two bedrooms, 16 three bedrooms, 34 four bedrooms, and 5 five bedrooms.

The Phase III DDA provides for horizontal infrastructure work to begin by November 30, 2022 and be completed by October 31, 2023. However, infrastructure improvements are underway and expected to be complete in 2025 and simultaneous with the vertical construction.[1] The delay in starting infrastructure improvements and the consequent extension of the completion date is due to longer than expected permitting timelines for the infrastructure work and due to the time needed to secure vertical financing. Construction of Phase III housing units is planned to start May 2023 and units are expected to be fully occupied in August 2025.

Exhibit 1: Hunters View Development Plan

Source: MOHCD Loan Evaluation for Hunters View Phase III
Note: Public & Affordable Housing is on Blocks 4, 5, 6 7, 10, 14, & 17

[1] In September 2021, the Board of Supervisors approved a $33.9 million loan to Hunters View Associates, L.P. to fund horizontal infrastructure improvements (File 21-0812). Horizontal infrastructure work consists of new streets (including to-be-named Streets 1 and 2, shown in Exhibit 1 above), utilities lines and conduits, sewer and other site work and improvements. MOHCD intends to forgive the previously approved infrastructure loan when infrastructure improvements are accepted by the City, subject to future Board of Supervisors approval.

Up to 332 market-rate ownership units are planned for Phase III after the completion of the public housing replacement and affordable housing units. Hunters View L.P. will solicit developers for market rate housing units, which will be evaluated by MOHCD and SFHA. SFHA will ground lease the parcels intended for market rate development to Hunters View L.P. during construction and then sell the land to the selected market rate developer. Under a separate agreement between MOHCD and SFHA, proceeds from land sales of market rate parcels are transferred to MOHCD to be used for HOPE SF projects.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would:

1) approve a not-to-exceed $50,495,000 amended and restated loan agreement for a term of 57 years between the City and HV Partners 3, L.P.[2] to construct Hunters View Phase III, a 118-unit affordable housing project;
2) find that the loan agreement is consistent with the Mitigation Monitoring and reporting Program under the California Environmental Quality Act, as well as the City's General Plan and policy priorities in the Planning Code;
3) authorize the Director of MOHCD to amend the Loan Agreement, provided amendments do not increase the obligations or liabilities to the City.

Loan Agreement

The original loan agreement provided by MOHCD in 2017 was for $6,192,595 for predevelopment costs, funded by Certificates of Participation (Files 19-1011 & 19-1014). MOHCD proposes to amend the loan agreement to increase the loan amount by $44,302,405 to complete development and construction, including permanent financing. Under the proposed amended loan agreement, the total loan amount to HV Partners 3, L.P. would increase to a not-to-exceed $50,495,000.

HV Partners 3, L.P. must repay the loan by the latter of: (a) the 57th anniversary date of the recordation of the deed of trust or (b) the 55th anniversary of the date on which construction financing is converted into permanent financing. Simple interest will accrue to the loan principal balance at a rate of 0.25 percent per year.

Affordability Restrictions

The proposed loan agreement includes affordability restrictions to preserve the affordability of the housing units in the proposed development. The agreement specifies the affordability levels for each unit and requires the limited partnership to maintain these for the duration of the agreement unless agreed to by the City. Of the 118 units, the 53 public housing replacement units are supported by project-based U.S. Department of Housing and Urban Development (HUD)

[2] HV Partners 3, L.P. is a limited partnership among affiliates of Devine & Gong, Inc., John Stewart Company, and Ridge Point.

Section 8 vouchers. The remaining 65 units will be limited to households with incomes ranging from 55 to 75 percent of area median income.

Sponsor Performance

According to MOHCD, none of the Hunters View development partners have performance issues.

FISCAL IMPACT

Total Development Costs

The total development cost for the 118 units of housing is $140.7 million, as shown in Exhibit 2 below. Of the approximate $140.7 million in costs, $50.5 million (35.9%) are supported by City funds and the remaining costs are funded by private funds.

Exhibit 2: Total Development Sources and Uses of Funds

Sources	
MOHCD Loan	$50,495,000
Private Mortgage	24,700,000
Apple Loan	2,200,000
Tax Credit Equity	61,999,922
Developer Equity	100
Deferred Developer Fee	1,300,000
Total Sources	**$140,695,022**
Uses	
Acquisition	$0
Construction	113,587,541
Soft Costs	23,427,381
Developer Fee	3,680,100
Total Uses	**$140,695,022**

Source: MOHCD

The City's $50.5 million includes $355,000 in case the Apple Loan funding source is not included in the final project financing sources. The project was awarded $2.2 million from Apple Inc., which has set aside loan funding for affordable housing, administered by the Housing Trust of Silicon Valley (HTSV). However, the project sponsor and HTSV are still negotiating the lien position of the Apple Loan relative to the private mortgage and MOHCD loan. If an agreement cannot be reached, the Apple Loan will be repaid by the project and backfilled with additional private mortgage debt and City funding.

The City loan also includes $1,480,000 as an interest rate contingency to allow for an increase in construction loan or permanent loan interest rates of up to 0.5 percent from the time of the Citywide Affordable Housing Loan Committee recommendation up to the construction loan closing, which is currently scheduled to occur the week ending May 19, 2023.

Funding Sources for City Loan

Sources of funds for the $44,302,405 in new City funding includes:

- $32,234,933 in 2019 General Obligation Bond Funds;[3]
- $5,000,000 in HOME Investment Partnership Program funds provided by HUD to increase the housing stock for low- and very low-income persons;
- $7,067,472 in Low and Moderate Income Housing Asset Fund monies;[4]

The City's Subsidy per Housing Unit

Excluding the $33.9 million in infrastructure costs, which MOHCD intends to forgive when infrastructure improvements are accepted by the City, subject to future Board of Supervisors approval of public right of way areas, total development costs are $140.7 million or approximately $1.2 million per unit. The City's total subsidy for the housing development costs is $50.5 million, or $427,924 per unit, as shown in Exhibit 3 below. The City funding shown below also includes $1.3 million in funding for development of commercial space shells in two buildings (discussed below).

Exhibit 3: City Subsidy for Affordable Housing Units

Number of Units	118
Total residential area (sq. ft.)	141,290
Development Cost (excluding infrastructure)	$140,695,022
Total City subsidy	$50,495,000
Development cost per unit	$1,192,331
City Subsidy per unit	$427,924
City Subsidy per sq. ft.	$357

Source: MOHCD

Cost Comparison to Similar Projects

According to a cost comparison of new affordable multifamily housing projects in the MOHCD loan evaluation of the proposed gap loan, the total development cost per unit is 40 percent above average compared to similar projects. The total development cost per unit for Hunters View Phase III is $1,192,331 compared to $851,822 for similar projects. Projects included in the comparison are similar projects in size, unit count, target population, and construction type. Comparison projects also include other HOPE SF projects.

[3] In November 2019, San Francisco voters approved Proposition A, which provided for the issuance of up to $600 million in general obligation funds to finance the acquisition, rehabilitation, and construction of affordable housing.

[4] Upon dissolution of state redevelopment agencies, MOHCD (as the Successor Housing Agency) created the Low and Moderate Income Housing Asset Fund to collect proceeds from former redevelopment agency housing assets transferred to the City.

According to the MOHCD loan evaluation, Hunters View Phase III construction costs in particular are above average due to:

- Costs related to the sloped site, which requires grading as part of the site preparation.
- A higher parking ratio (0.75 parking spaces per unit) compared to other projects (other affordable housing projects have 0.5 parking spaces per unit on average).
- HOPE SF projects are required to provide In-unit laundry hookups for three- and four-bedroom units, which is not a requirement for most other affordable housing projects.
- 45% of the units are three bedrooms or larger, whereas other affordable housing projects typically include many more one/two bedrooms.

Operating Revenues and Expenses

According to the 20-year cash flow analysis for Hunters View Phase III, the project will have sufficient revenues to cover operating expenses, operating reserves, private mortgage and Apple Loan payments, management fees, and deferred developer payments. Project revenues consist of tenant rents and HUD Project Based Section 8 rental subsidies. Total operating expenses for the project include ground lease base rent payments to the San Francisco Housing Authority. A portion of net income after operating expenses (residual receipts) will be used to repay the proposed MOHCD loan.

Commercial Space

The proposed loan includes $1.3 million to construct a cold shell[5] for 3,848 square feet of commercial space in the two buildings. Block 14 may include a "learning area" that includes a San Francisco Library book vending machine. Block 17 could include a commercial kitchen and café space, though a solicitation from late 2022 did not receive any responses. MOHCD, the project sponsor, and the Hunters View Resident Council intend to finalize plans for the two commercial spaces by January 2024.

MOHCD's Underwriting Guidelines allow for City funding to develop a warm shell for commercial spaces for public benefit uses. The Department estimates that remaining development costs for the warm shell and tenant improvements for the commercial spaces total $2,766,460. MOHCD reports that it does not normally provide funding for tenant improvements for commercial spaces.

According to the commercial pro-forma provided by MOHCD, the commercial space is expected to contribute approximately $30,000 per year to the residential operating budget. According to Section 7.8 of the proposed loan, leases of commercial space may be for for-profit, at market rate, or community serving purposes, at below market rate. Surplus cash generated from market-rate leases will accrue to MOHCD per the Residual Receipts policy and be used for the public benefit.

[5] Per MOHCD's Commercial Space Underwriting Guidelines, a cold shell includes exterior walls, basic electrical service, stubs for plumbing and heat, and unfinished flooring. A warm shell includes interior walls and doors, finished flooring, restroom accessories, HVAC, plumbing, and electrical outlets.

RECOMMENDATION

Approve the proposed resolution.

Item 16 File 23-0319	Department: Mayor's Office of Housing & Community Development (MOHCD)

EXECUTIVE SUMMARY

Legislative Objectives

- This proposed resolution would approve an amended and restated loan agreement between the Mayor's Office of Housing and Community Development (MOHCD) and Turk 500 Associates, L.P. in an amount not-to-exceed $23,805,311, an increase of $4,226,311.

Key Points

- 500 Turk Street (also known as 555 Larkin) is an affordable housing development, consisting of 108 affordable housing units and commercial space. The Board previously authorized up to $20.15 million for project development. Of the $20.15 million, $1.25 million was intended to be short-term gap financing for an Affordable Housing Program (AHP) award. While $20.15 million was previously authorized by the Board, the project ultimately required only $19.6 million in financing from the City.
- MOHCD is requesting additional gap financing due to a) project development delays and cost overruns caused by PG&E delays and b) the project was deemed not competitive for an Affordable Housing Program award.

Fiscal Impact

- The proposed $4.2 million loan increase would be funded from the Housing Trust Fund.

Policy Consideration

- As the gap lender for affordable housing projects, a significant amount of project risk is borne by the City. While the City is a partner in these projects, the developer is ultimately responsible for a project's success. Before the Board approves increased gap funding for any reason, it should evaluate the larger context of how project risks are managed and establish criteria for who absorbs that risk.
- Increased costs resulting from PG&E delays and excess requirements are the subject of litigation in cases before the Federal Energy Regulatory Commission. It is unclear when or if those costs will be recovered from PG&E. There is limited opportunity to pay for interconnection and related project costs from the PUC given State law regulating utility revenues, industry-practice, the City's Charter, and PUC rules and regulations. The City is investigating opportunities for recovery of these costs.
- The City could consider negotiating cost-sharing with Tenderloin Neighborhood Development Corporation (TNDC) and other affordable housing developers impacted by utility connection delays. In this case, TNDC generates project income through developer fees as well as operating revenues with annual management and asset management fees.

Recommendation

- Approval of the proposed resolution is a policy matter for the Board.

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.

BACKGROUND

Low-Income Housing at 500 Turk Street

In January 2020, the Board of Supervisors approved agreements to purchase the site at 500 Turk/555 Larkin Street and increase gap financing by $11.9 million to $32.4 million to partially fund the development of an affordable housing project co-located with commercial space (File 19-1265). The site, which is owned by the City, was developed by the Tenderloin Neighborhood Development Corporation (TNDC), which was selected through a competitive process. The development is a mixed-use eight-story building, with 107 units of 1-3 bedrooms of income-restricted housing, one resident manager unit, and commercial space. Unit income limits range from 30 to 80 percent of area median income and 27 units receive vouchers from the San Francisco Housing Authority (SFHA) and set aside for tenants relocating from HOPE SF projects.

Construction was originally expected to occur from February 2020 to December 2021. Actual construction occurred from February 2020 to October 2022. Currently, the project is at 63 percent lease-up (occupancy) and the commercial space will be leased to a nonprofit senior center with occupancy anticipated in September 2023.

PG&E Project Delays

San Francisco's Power Enterprise includes Hetch Hetchy Power, which generates and provides power to City facilities, and CleanPowerSF, a community choice aggregate program that purchases clean electricity for its retail customers in San Francisco. Both rely on PG&E transmission and distribution infrastructure within San Francisco to deliver power. Chapter 99 of the City's Administrative Code requires the San Francisco Public Utilities Commission (PUC) to study the feasibility of providing public power to City facilities and states that all City departments, including those not in City-owned facilities, should receive power from PUC wherever feasible.

The City obtains electric distribution service from PG&E via a federally regulated agreement. Due to ongoing litigation pertaining to PG&E's requirements, the City must negotiate each interconnection application. Retail and wholesale PG&E customers must pay for new interconnections, though retail customers may be reimbursed for some costs. According to PUC Power Enterprise Deputy Assistant General Manager Catherine Spaulding, PUC has similar reimbursement policies for its retail customers. In December 2021, the Board of Supervisors approved a 10-year agreement between SFPUC and PG&E to streamline interconnections at

certain affordable housing sites (File 21-1053), but the list attached to the agreement did not include 500 Turk because the project was already under construction.

According to media reports, PG&E has significant interconnection delays for new housing projects throughout its service area, not just in San Francisco.[1] According to a MOHCD March 3, 2023 staff memo to the Citywide Affordable Housing Loan Committee regarding this project and a similarly impacted project at 4840 Mission Street, PG&E recently announced a moratorium on interconnection work for retail and wholesale customers, citing staffing constraints. In addition, the City and PG&E are presently involved in litigation and negotiation before the Federal Energy Regulatory Commission regarding PG&E's interconnection terms, which the City believes are more costly and time-consuming than interconnection for PG&E retail customers.[2]

MOHCD reports that PG&E's process for approving electricity service at 500 Turk Street has caused the construction delays experienced at 500 Turk Street. The building was energized in September 2022, nine months later than the original project schedule of late 2021. These delays have resulted in both increased project costs as well as increased financing costs, especially due to the rising interest rates over the construction period.

According to MOHCD, because of delays in energizing the building, conversion of the construction loan to a permanent loan has been delayed 10 months, resulting in additional $2.8 million interest costs for the construction loan, which has risen from 2.5 percent to 6.0 percent. Further, given the increase in interest rates over the construction period, the permanent loan will now incur an estimated interest rate of approximately 5.73 percent instead of 3.67 percent originally anticipated and result in a short loan term of 25 years rather than 35 years. Limited partner tax credit equity financing has also decreased because the project has not been able to meet the expected Occupancy Place in Service date required by the California Tax Credit Allocation Committee. These increased costs are resulting in an additional gap in project financing.

In addition to the financing impacts, the project has incurred hard costs associated with the delay, including retaining the general contractor, consultants, and security for an additional 10 months, as well as additional utility-related costs such as for a generator to be located on site and costs associated with change orders related to permanent power design. These additional costs total approximately $1.4 million.

Federal Home Loan Bank of San Francisco: Affordable Housing Program

Original project financing included a bridge loan from the City of $1.25 million in anticipation of TNDC applying for and receiving an Affordable Housing Program (AHP) award from the Federal Home Loan Bank of San Francisco. AHP awards are competitive grants wherein applicants are

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[1] Dustin Gardiner, Julie Johnson. "Big hold for new Northern California Housing? PGE," *San Francisco Chronicle,* March 10, 2023. https://tinyurl.com/26vbtaum.

[2] The City also offered to purchase PG&E transmission and distribution assets in and around San Francisco for $2.5 billion in 2019 and in 2020, but PG&E denied the offers, stating that they were below market value. In 2021, City filed a petition with the California Public Utilities Commission to establish a fair value for these PG&E assets.

scored on a variety of project characteristics, such as population served and project financing. According to MOHCD, AHP awards prioritize serving formerly homeless households. While TNDC did apply in 2020, the project did not sufficiently meet the award criteria for funding. TNDC did not re-apply in subsequent years because TNDC determined that the project would again not score high enough to receive an award.

Pursuant to the original Amended and Restated Loan Agreement from 2020, if TNDC applied for the AHP award in 2020 and 2021, failure to receive the AHP award does not result in default of the loan. While TNDC did not apply for the award on 2021, their analysis demonstrating non-competitiveness was shared and discussed with MOHCD.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would:

- Approve an amended and restated loan agreement between the City and 500 Turk Associates in an amount not-to-exceed $23,805,311, an increase of $4,226,311 to be funded from the Housing Trust Fund;
- Authorize the Mayor and the Director of MOHCD, or their designee, to execute any amendments or modifications to the First Amendment to the Amended and Restated Loan Agreement and other documents and instruments, including the Third Amended and Restated Promissory Note and the First Amendment to Deed of Trust, necessary in furtherance of this resolution;
- Authorize the Mayor and the Director of MOHCD, or their designee, to take any actions necessary to protect the City's financial interest in the property and to enforce affordable housing restrictions; and
- Confirm the project is consistent with the City's General Plan.

Amended and Restated Loan Agreement

The current loan agreement between MOHCD and Turk 500 Associates is for $19,579,000.[3] Under the proposed third amendment and restated loan agreement, the loan amount to Turk 500 Associates would increase by $4,226,311 to $23,805,311 as shown in Table 1 below.

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[3] File 19-1265 included approval of the original amended and restated loan agreement totaling up to $32,400,000. This figure included $12,250,000 as purchase credit against the City's prior loans of $20,474,731 in exchange for acquiring the property and $11,925,269 in new financing, resulting in total gap financing of $20,150,000. The City's actual outstanding loan of $19,579,000 is $571,000 less than the maximum loan amount previously approved by the Board of Supervisors because of changes to total project costs and permanent financing sources.

Table 1: Updated Sources and Uses for 500 Turk Project

Sources	Original Amount	Proposed Amount	Change Amount	Change Percent
MOHCD	$18,329,000	$23,805,311	$5,476,311	30%
MOHCD – AHP Gap Financing	1,250,000		-1,250,000	-100%
Subtotal MOHCD	**19,579,000**	**23,805,311**	**4,226,311**	**22%**
Limited Partner Equity	30,803,465	29,787,566	-1,015,899	-3%
General Partner Equity	500,000	500,000		
Permanent Debt	10,953,000	8,652,000	-2,301,000	-21%
Affordable Housing Sustainable Comm.	13,700,000	13,700,000		
Deferred Developer Fee	6,548,937	6,548,937		
Interim Income	329,901	329,901		
Total Sources	**$82,414,303**	**$83,323715**	**$909,412**	**1%**
Uses				
Acquisition	$770,061	$725,666	-$44,395	-6%
Hard Costs	54,962,213	55,764,900	802,687	1%
Soft Costs	14,815,905	16,186,655	1,370,750	9%
Reserves	2,287,186	1,067,557	-1,219,629	-53%
Developer Fee	9,578,937	9,578,937		
Total Uses	**$82,414,302**	**$83,323,715**	**$909,413**	**1%**

Source: MOHCD

As described above, development costs are increasing by $2.1 million due to PG&E delays, offset by a $1.2 million decrease in project reserves. According to MOHCD staff, reserves can be reduced due to new regulation changes in State financing that allow for the reduction, as well as overall project savings. Total City funding is increasing by $4.2 million to pay for these additional costs ($0.9 million) and backfill a $3.3 million decrease in non-City funding sources, also described above.

FISCAL IMPACT

The proposed increased loan amount of $4.2 million would be funded from the Housing Trust Fund. MOHCD staff report that the current fund balance allocated to new housing development within the Housing Trust Fund is $58.4 million.

According to the terms of the loan, Turk 500 Associates must repay the loan by the 57th anniversary date of the deed of trust, but no later than December 31, 2077. No interest will be charged on the loan.

The loan balance will be reduced upon receipt by the City of residual receipts generated annually by project operations. In TNDC's application for the additional loan of funds, TNDC projects these receipts to total $930,910 over the first 20 years of operations, an average of $46,545 per year. According to Sara Amaral, MOHCD Director of Housing Development, there is no intention to forgive any balance remaining on this loan at the end of the term.

Project financing requirements are dependent on TNDC estimates. MOHCD reports these estimates have been reviewed, deemed reasonable, and are consistent with MOHCD's underwriting guidelines. Pursuant to the Amended and Restated Loan Agreement, MOHCD will monitor the rate of lease-up (occupancy) and interest rates. Any resulting cost savings will reduce the loan provided to 500 Turk Associates. Further, 500 Turk Associates will provide a report of updated operating expenses within three months of the conversion date, holding constant or reducing operating costs.

Revised Pro-Forma Operating Income and Expenses

MOHCD staff updated the projected income and expenses for the project in the first year of occupancy. Tenant rents remain virtually unchanged because the income bands for the units have not changed, but tenant assistance payments have increased from $560,000 to $833,000 due to an increase in the value of SFHA housing vouchers. No rent is assumed for the commercial space, a decrease of $80,000 per year in project income.

Annual operating costs have increased by approximately $280,000 due to higher property management staff costs, utility costs (not including the PG&E interconnection costs), and insurance costs, which MOHCD staff report is consistent with other affordable housing projects in process. The project is still projected to generate sufficient net income to make residual receipt payments on the MOHCD loan as described above.

The City's Subsidy per Housing Unit

The total per unit City subsidy is $220,420, excluding site acquisition costs of $12.5 million. The total development cost for the 108 units plus commercial space is $83,323,715, or $771,516 per unit.

POLICY CONSIDERATION

As the gap lender for affordable housing projects, a significant amount of project risk is borne by the City. While the City is a partner in these projects, the developer is ultimately responsible for a project's success. That success depends upon many variables and financing is complex. Risks associated with affordable housing projects are anticipated, evaluated, and mitigated throughout the pre-development and development process. Before the Board approves increased gap funding for any reason, it should evaluate the larger context of how project risks are managed and establish criteria for who absorbs that risk.

Recovery of Costs Resulting from PG&E Delays

Pursuant to Board Resolution 227-18, the PUC is required to provide the Board with a quarterly report of City projects with applications for electric service and the associated cost impacts of PG&E – related delays and requirements. Because 500 Turk was energized in September 2022, the project was not included in the January 2023 report. However, the October 2022 quarterly report identified a total of $174,000 in additional project costs related to utilities for the 500 Turk project. According to Grace Tang, Utility Specialist at PUC, the PUC relies on individual departments to report these costs.

According to City's Attorney's Office staff, utility enterprises, including Hetchy Hetchy Power, are subject to State laws regulating the use of utility ratepayer revenues, which restrict charging utility rate payers for costs not related to serving them. Catherine Spaulding, PUC Power Enterprise Deputy Assistant General Manager, reports that PUC policy is for customers to pay for their own connection costs, which is consistent with not only industry-practice, but also State law. Accordingly, there is no available mechanism by which to recover interconnection and other power utility costs from the PUC.

The costs reported in PUC's quarterly report do not include the impact of PG&E delays on project financing or other hard and soft costs not associated with the provision of power services. Sheila Nickolopoulos, Director of Policy and Legislative Affairs for MOHCD, reports these increased costs are currently estimated to total $40.0 million across 11 MOHCD projects. Because of the complexity and the breadth of PG&E issues, MOHCD-specific cost impacts may not be addressed through the City's filings with the Federal Energy Regulatory Commission (FERC), which pertain to infrastructure requirements. The City is investigating other opportunities for remedy.

Shared Project Risk

While MOHCD staff report that the $4.2 million in additional loan financing for the 500 Turk Street project is due to PG&E delays, there are other project financing variables that have increased the need for additional funding. If interest rates had not increased to the extent they have, financing cost increases would be substantially lower. If TNDC was granted the AHP award that was previously determined to be obtainable, the City's subsidy would be less. The City cannot take one of these variables in isolation because project financing is the sum total of all of its parts. Accordingly, MOCHD and the City should consider negotiating cost-sharing with TNDC, which generates project income through developer fees as well as operating revenues with annual management and asset management fees.

RECOMMENDATION

Approval of the proposed resolution is a policy matter for the Board.

Item 17 **File 23-0318**	**Department:** Mayor's Office of Housing & Community Development (MOHCD)

EXECUTIVE SUMMARY

Legislative Objectives

- This proposed resolution would approve an amended and restated loan agreement between the Mayor's Office of Housing and Community Development (MOHCD) and 4840 Mission Associates, L.P. in an amount not-to-exceed $37,728,757, an increase of $8,977,307. The proposed resolution would also grant two utility easements on the City-owned land that were not previously identified by PG&E in the pre-development stage.

Key Points

- 4840 Mission Street is an affordable housing development, consisting of 137 affordable housing units, commercial space, and a health clinic. The Board previously authorized $28,751,450 in loan financing to 4840 Mission Associates, a limited partnership of BRIDGE Housing Corporation (BRIDGE), for project development. MOHCD is requesting additional gap financing due to unbudgeted PG&E infrastructure requirements and increased project costs due to delays in obtaining PG&E infrastructure approvals.

Fiscal Impact

- The proposed $9.0 million loan increase would be funded from the Housing Trust Fund ($6.8 million) and 2019 general obligation bonds ($2.2 million).

Policy Consideration

- As the gap lender for affordable housing projects, a significant amount of project risk is borne by the City. While the City is a partner in these projects, the developer is ultimately responsible for a project's success. Before the Board approves increased gap funding for any reason, it should evaluate the larger context of how project risks are managed and establish criteria for who absorbs that risk.
- Increased costs resulting from PG&E delays and excess requirements are the subject of litigation in cases before the Federal Energy Regulatory Commission. It is unclear when or if those costs will be recovered from PG&E. There is limited opportunity to pay for interconnection and related project costs from the PUC given State law regulating utility revenues, industry-practice, the City's Charter, and PUC rules and regulations. The City is investigating opportunities for recovery of these costs.
- The City could consider negotiating cost-sharing with BRIDGE and other affordable housing developers impacted by utility connection delays. In this case, BRIDGE generates project income through developer fees as well as operating revenues with annual management and asset management fees.

Recommendation

- Approval of the proposed resolution is a policy matter for the Board.

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.

BACKGROUND

Low-Income Housing at 4840 Mission Street

The City is partially funding the development of affordable housing at 4840 Mission Street (also known as Islais Place), which is co-located with a health clinic. The site, which is owned by the City, is being developed by the BRIDGE Housing Corporation (BRIDGE), which was selected through a competitive process. The development is a mixed-use five-story building, with 135 units of income-restricted housing, two resident manager units, property management staff office space, residential parking, commercial space, and a health clinic. The maximum income for the units ranges from 30 to 105 percent of area median income and the project includes 35 units set aside for households voluntarily relocating from the HOPE SF Potrero development.

The Board of Supervisors has approved two loans for the 4840 Mission Street project: (1) a $18.6 million loan in 2019 for acquisition and predevelopment costs (File 19-0934) and (2) a $28.8 million gap loan in 2021 to pay for development costs (File 21-0383).

Construction was originally expected to occur from June 2021 to June 2023. While construction began in June 2021 and is anticipated to be substantially complete by June 2023, the project is awaiting PG&E approval for permanent power, which is expected to be obtained in May 2023. Therefore, MOHCD expects that construction will not be entirely completed and a Certificate of Occupancy obtained by December 2023, six months after construction is complete.

PG&E Project Infrastructure Requirements and Approval Delays

San Francisco's Power Enterprise includes Hetch Hetchy Power, which generates and provides power to City facilities, and CleanPowerSF, a community choice aggregate program that purchases clean electricity for its retail customers in San Francisco. Both rely on PG&E transmission and distribution infrastructure within San Francisco to deliver power. Chapter 99 of the City's Administrative Code requires the San Francisco Public Utilities Commission (PUC) to study the feasibility of providing public power to City facilities and states that all City departments, including those not in City-owned facilities, should receive power from PUC wherever feasible.

The City obtains electric distribution service from PG&E via a federally regulated agreement. Due to ongoing litigation pertaining to PG&E's requirements, the City must negotiate each interconnection application. Retail and wholesale PG&E customers pay for new interconnections, though retail customers may be reimbursed for some costs. According to PUC Deputy Manager Catherine Spaulding, PUC has similar reimbursement policies for its retail customers. In

December 2021, the Board of Supervisors approved a 10-year agreement between PUC and PG&E to streamline interconnections at certain affordable housing sites. The list attached to the agreement includes 4840 Mission Street (File 21-1053).

According to media reports, PG&E has significant interconnection delays for new housing projects throughout its service area, not just in San Francisco.[1] According to a MOHCD March 3, 2023 staff memo to the Citywide Affordable Housing Loan Committee regarding this project and a similarly impacted project at 500 Turk Street, PG&E recently announced a moratorium on interconnection work for retail and wholesale customers, citing staffing constraints. In addition, the City and PG&E are presently involved in litigation and negotiation before the Federal Energy Regulatory Commission regarding PG&E's interconnection terms, which the City believes are more costly and time-consuming than interconnection for PG&E retail customers.[2]

MOHCD reports that PG&E has caused construction delays at 4840 Mission Street due to an extended review process for an application to connect the site to PG&E distribution infrastructure that has lasted almost three years. Further, PG&E has assigned a tie-in location for power 1,770 feet farther than what the project originally assumed for the project using PG&E maps, resulting in additional costs for trenching, PG&E installation charges and taxes, and consultant and contractor change orders, which together are estimated to cost $5.04 million.

Additionally, these delays have resulted in increased financing costs due to the rising interest rates over the construction period. The construction loan interest rate has increased from 3.25 to 4.96 percent, which is expected to increase total construction loan interest by up to $5.9 million.

Federal Home Loan Bank of San Francisco: Affordable Housing Program

The 2021 $28.8 million gap loan from the City included $1.25 million of bridge financing in anticipation of BRIDGE applying for and receiving an Affordable Housing Program (AHP) award from the Federal Home Loan Bank of San Francisco. AHP awards are competitive grants wherein applicants are scored on a variety of project characteristics, such as population served and project financing. According to MOHCD, AHP awards prioritize serving formerly homeless households.

BRIDGE did not apply for the award in 2022 believing that the project was not competitive. However, BRIDGE did apply for the award in March 2023 and recipients will be notified this summer. If not awarded, MOHCD is expecting BRIDGE to apply for AHP awards in subsequent funding cycles until construction has been completed and to seek alternative financing sources.

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[1] Dustin Gardiner, Julie Johnson. "Big hold for new Northern California Housing? PGE," *San Francisco Chronicle,* March 10, 2023. https://tinyurl.com/26vbtaum.

[2] The City also offered to purchase PG&E transmission and distribution assets in and around San Francisco for $2.5 billion in 2019 and in 2020, but PG&E denied the offers, stating that they were below market value. In 2021, City filed a petition with the California Public Utilities Commission to establish a fair value for these PG&E assets.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would:

- Approve an amended and restated loan agreement between the City and 4840 Mission Associates L.P. in an amount not-to-exceed $37,728,757, an increase of $8,977,307 to be funded from the Housing Trust Fund and 2019 general obligation bonds;
- Authorize the Mayor and the Director of MOHCD, or their designee, to execute any amendments or modifications to the First Amendment to Loan Agreement and other documents and instruments, including the Amended and Restated Promissory Note and the First Amendment to Deed of Trust, necessary in furtherance of this resolution without increasing liabilities of the City;
- Grant two utility easements to PG&E on the City-owned land; and
- Authorize the Mayor and the Director of MOHCD, or their designee, to take any actions necessary to protect the City's financial interest in the property and to enforce affordable housing restrictions.

Amended and Restated Loan Agreement

The current loan agreement between MOHCD and 4840 Mission Housing Associates is $28,751,450. Under the proposed amendment and restated loan agreement, the loan amount to 4840 Mission Housing Associates would increase by $8,977,307 to $37,728,757 as shown in Table 1 below.

Table 1: Updated Sources and Uses for 4840 Mission Project

Sources	Original Amount	Proposed Amount	Change Amount	Change Percent
MOHCD – Residential Note	$24,501,450	$33,478,757	$8,977,307	37%
MOHCD – Clinic Note	3,000,000	3,000,000		
MOHCD – AHP Gap Financing	1,250,000	1,250,000		
Subtotal MOHCD	28,751,450	37,728,757	8,977,307	31%
Limited Partner Equity (Tax Credit Investor)	50,416,989	50,416,989		
General Partner Equity	100	100		
Permanent Debt	24,550,000	24,550,000		
Deferred Developer Fee	2,118,779	2,118,779		
Total Sources	**$105,837,318**	**$114,814,625**	**$8,977,307**	**8%**
Uses				
Acquisition	$825,000	$825,000		
Hard Costs	85,366,484	89,404,211	4,037,727	5%
Soft Costs	13,821,096	18,760,676	4,939,580	36%
Reserves	835,859	835,859		
Developer Fee	4,988,879	4,988,879		
Total Uses	**$105,837,318**	**$114,814,625**	**$8,977,307**	**8%**

Source: MOHCD

As shown above, City funding is increasing by $8.98 million cover an estimated $4.1 million in construction costs and $4.9 million in soft costs.

Loan Disbursement Conditions

Section 4.9 of the proposed loan agreement states that MOHCD will only disburse the proposed additional funding to pay for construction, to prevent liens against the project, pay construction loan interest, and pay for soft costs, which together are estimated to total $5,005,000. The remaining funds, if needed, would be applied as a permanent financing source. BRIDGE must also provide updated occupancy and verify all development costs and sources of funding prior to disbursing the remaining portion of the City loan and releasing the $1.4 million At Risk Developer Fee (a portion of the $4.99 million developer noted in Table 1 above assigned to project close-out).

In addition, as noted above, BRIDGE would be required to apply an award of AHP funds against the City loan and to seek out other non-City funding sources.

FISCAL IMPACT

The proposed increased loan amount of $8,977,307 would be funded as follows:

- $6,791,357 from the Housing Trust Fund, and
- $2,185,950 from 2019 general obligation bond proceeds.

MOHCD reports that the current fund balance allocated to new housing development within the Housing Trust Fund is $58.4 million.

According to the terms of the loan, 4840 Mission Housing Associates must repay the loan by the 57th anniversary date of the deed of trust or the 55th anniversary of the conversion date, whichever is later. Given an estimated construction completion date of December 2023, the loan would not be due until 2080 or later. No interest will be charged on the loan.

The loan balance will be reduced upon receipt by the City of residual receipts generated annually by project operations. In the project's pro-forma of project income and expenses from 2021, BRIDGE projected these receipts to total $3.9 million over the first 20 years of operations, an average of $195,000 per year. According to Sara Amaral, MOHCD Director of Housing Development, there is no intention to forgive any balance remaining on the loan at the end of the term.

Project financing requirements presented for this proposed loan increase are dependent on 4840 Mission Housing Associates estimates. MOHCD staff report these estimates have been reviewed and deemed reasonable. Although the project pro-forma of project income and expenses from 2021 has not been updated to reflect new revenue estimates (including project-based voucher revenues), operating costs, or occupancy and lease-up timelines, MOHCD staff believe these estimates continue to be consistent with the MOHCD's underwriting guidelines and in-line with other affordable housing projects in process.

Cost per Housing Unit

The total development cost for the 137 units, office and commercial space, and the health clinic is $114,814,625 or $838,063 per unit, which is an increase from the $772,535 per unit originally budgeted.

POLICY CONSIDERATION

As the gap lender for affordable housing projects, a significant amount of project risk is borne by the City. While the City is a partner in these projects, the developer is ultimately responsible for a project's success. That success depends upon many variables and financing is complex. Risks associated with affordable housing projects are anticipated, evaluated, and mitigated throughout the pre-development and development process. Before the Board approves increased gap funding for any reason, it should evaluate the larger context of how project risks are managed and establish criteria for who absorbs that risk.

Recovery of Costs Resulting from PG&E Delays and Requirements

Pursuant to Board Resolution 227-18, the PUC is required to provide the Board with a quarterly report of City projects with applications for electric service and the associated cost impacts of PG&E-related delays and requirements. The January 2023 quarterly report identified a total of $47,000 in additional project costs related to utility changes at 4840 Mission but did not list the additional trenching requirements identified in this proposed resolution. According to Grace Tang, Utility Specialist at PUC, the PUC relies on individual departments to report these costs.

According to City Attorney's Office staff, utility enterprises, including Hetchy Hetchy Power, are subject to State laws regulating the use of utility ratepayer revenues, which restrict charging utility ratepayers for costs not related to serving them. Catherine Spaulding, Power Enterprise Deputy Assistant General Manager, reports that PUC policy is for customers to pay for their own connection costs, which is consistent with not only industry-practice, but also State law. Accordingly, there is limited opportunity to recover interconnection and related project cost increases from the PUC.

The costs reported in PUC's quarterly report do not include the impact of PG&E delays on project financing or other hard and soft costs not associated with the provision of power services. Sheila Nickolopoulos, Director of Policy and Legislative Affairs for MOHCD, reports these increased costs are currently estimated to total $40.0 million across 11 MOHCD projects. Because of the complexity and the breadth of PG&E issues, MOHCD-specific cost impacts may not be addressed through the City's filings with the Federal Energy Regulatory Commission (FERC), which pertain to infrastructure requirements. The City is investigating other opportunities for remedy.

Shared Project Risk

While MOHCD reports that the $9.0 million in additional loan financing for the 4840 Mission Street project is due to PG&E delays and excessive requirements, there are other project variables that have increased the need for additional financing. If interest rates had not increased to the extent they have, financing cost increases would be substantially lower. Further, there is uncertainty in whether the project will be granted the AHP award that was previously determined to be obtainable. If not received, the City's subsidy will increase. The City cannot take one of these variables in isolation because project financing is the sum total of all of its parts. Accordingly, MOHCD and the City should consider negotiating cost-sharing with BRIDGE, which generates project income through developer fees as well as operating revenues with annual management and asset management fees.

RECOMMENDATION

Approval of the proposed resolution is a policy matter for the Board.