

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

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March 31, 2016

TO: Budget and Finance Sub-Committee

FROM: Budget and Legislative Analyst



SUBJECT: April 6, 2016 Budget and Finance Sub-Committee Meeting

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<p>Item 1 File: 15-1225</p>	<p>Departments: Mayor’s Office of Housing and Community Development (MOHCD) Controller’s Office of Public Finance</p>
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EXECUTIVE SUMMARY

Legislative Objectives

- Ordinance authorizing the execution and delivery of Certificates of Participation (COPs) in an aggregate principal amount not to exceed \$95,000,000 to provide funds to assist in the development, acquisition, construction or rehabilitation of affordable rental housing projects; approving the form of a Supplemental Trust Agreement; approving the form of a Supplemental Property Lease; approving the form of a Supplemental Project Lease; approving the form of an Official Notice of Sale and Notice of Intention to Sell the COPs or authorizing certain actions relating to the COPs; approving the form of an official statement in preliminary and final form; approving the form of a Continuing Disclosure Certificate; granting general authority to City officials to take necessary actions in connection with the authorization, issuance, sale and delivery of the COPs; approving modifications to documents; and ratifying previous actions taken in connection therewith.

Key Points

- In November 2012, San Francisco voters approved the City’s Housing Trust Fund for the creation of additional affordable housing. \$20 million was appropriated to the Fund in FY 2013-14, increasing \$2.8 million annually, for a total of \$128 million through FY 2017-18.
- MOHCD’s budgets for FY2014-15 and FY2015-16 included an additional \$25 million each year of Certificate of Participation (COP) revenue and MOHCD’s FY 2016-17 budget includes another \$25 million for a total of \$75 million of additional COP revenue.

Fiscal Impact

- Affordable housing project development costs are estimated at \$1.7 billion, including these COP proceeds of \$75 million to renovate and/or construct 3,147 housing units.
- The requested not to exceed \$95,000,000 COPs would be issued for a term of 30 years. Assuming \$83,440,000 issuance and a conservative 7.528% annual interest rate results in total costs of approximately \$213,235,199 over the 30-year term, including \$129,795,199 of interest, and average annual debt service payments of approximately \$7,088,151.

Recommendation

- Approve the proposed ordinance.

MANDATE STATEMENT

City Charter Section 16.110 provides that the Housing Trust Fund will support the creation, acquisition and rehabilitation of affordable housing and promote affordable home ownership programs in the City. In accordance with Section 16.110(c), \$20 million of General Fund revenues would be appropriated to the Housing Trust Fund in FY 2013-14, an amount which would be increased by \$2.8 million each year thereafter from FY 2014-15 through FY 2024-25. After FY 2024-25 through FY 2042-43, General Fund revenues would be appropriated to the Housing Trust Fund equal to prior year appropriations, adjusted by annual percentage increases or decreases in the General Fund discretionary revenues budgeted.

Charter Section 16.110(f) authorizes issuance of debt to be repaid with future Housing Trust Fund allocations. In addition, the City may disburse monies from the Housing Trust Fund through loans, grants or other types of payments, on terms determined by the Mayor's Office of Housing and Community Development (MOHCD) in its sole discretion, with all repayments or interest returned to the Housing Trust Fund. Allowable uses of the Housing Trust Fund include multifamily housing development, including acquisition and rehabilitation of existing housing, down payment assistance for first-time homebuyers, housing stabilization programs to help owners and tenants stay in their existing homes, infrastructure grants for public-serving projects in areas of increased residential development and program administration. All expenditures from the Housing Trust Fund are subject to the Board of Supervisors appropriation approval.

BACKGROUND

In November 2012, San Francisco voters approved a Charter amendment which created the City's Housing Trust Fund, now codified in Charter Section 16.110. As shown in Table 1 below, in accordance with Charter Section 16.110(c), \$20 million was appropriated to the Housing Trust Fund in FY 2013-14, an amount which has increased by \$2.8 million annually, such that a total of \$128 million will be appropriated over the five year period through FY 2017-18.

As also shown in Table 1 below, the Mayor's Office of Housing and Community Development (MOHCD) approved budgets for FY 2014-15, FY 2015-16 and FY 2016-17 included an additional \$25 million appropriation each year of Certificates of Participation (COP) revenue, for a total of \$75 million for affordable housing projects. The anticipated debt service to repay the COPs with Housing Trust Fund revenues projected for FY 2016-17 and FY 2017-18 is \$11,349,156. Overall, Housing Trust Fund expenditures would total \$203 million over the five year period from FY 2013-14 through FY 2017-18, as summarized in Table 1 below.

Table 1: Housing Trust Fund Five Year Plan from FY 2013-14 Through FY 2017-18

Program	2013-14	2014-15	2015-16	Proposed 2016-17	Proposed 2017-18	Total
Down payment Loan	\$2,000,000	\$3,000,000	\$3,000,000	\$3,000,000	\$4,000,000	\$15,000,000
Housing Stabilization	2,825,000	3,600,000	4,250,000	4,100,000	4,100,000	18,875,000
Neighborhood Infrast	200,000	500,000	1,000,000	1,500,000	1,500,000	4,700,000
Afford Housing Devel	13,821,000	14,500,063	15,269,091	13,953,988	13,116,150	70,660,292
Program Delivery	<u>1,154,000</u>	<u>1,199,937</u>	<u>2,080,909</u>	1,420,706	1,560,000	7,415,552
Debt Service	-	-	-	<u>4,425,306</u>	<u>6,923,850</u>	<u>11,349,156</u>
Total Base HTF	20,000,000	22,800,000	25,600,000	28,400,000	31,200,000	128,000,000
Add Afford Housing	-	25,000,000	25,000,000	25,000,000	-	75,000,000
TOTAL	20,000,000	47,800,000	50,600,000	53,400,000	31,200,000	\$203,000,000

On November 16, 2015, the Capital Planning Committee recommended the proposed ordinance.

DETAILS OF PROPOSED LEGISLATION

The proposed ordinance would

- authorize the execution and delivery of Certificates of Participation (COPs) in an aggregate principal amount not to exceed \$95,000,000 to provide funds to assist in the development, acquisition, construction or rehabilitation of affordable rental housing projects;
- approve the form of a Supplemental Trust Agreement between the City and County of San Francisco and the Trustee, including certain indemnities;
- approve the form of a Supplemental Property Lease between the City, as lessor, and the Trustee, as lessee;
- approve the form of a Supplemental Project Lease between the Trustee, as lessor and the City, as lessee;
- approve the form of an Official Notice of Sale and Notice of Intention to Sell the COPs, if sold by competitive sale, which identifies the date and time of the bond sale, including the terms of the sale, form of the bids and delivery and closing procedures and documents.
- authorize certain actions relating to the COPs, if sold by negotiated sale, including approving the form of a Purchase Contract between the City and the underwriter(s) selected in accordance with City policies;
- approve the form of an Official Statement in preliminary and final form;

- approve the form of a Continuing Disclosure Certificate which describes the nature of the financial information and operating data contained in the City's Annual Report; and
- grant general authority to City officials to take necessary actions in connection with the authorization, issuance, sale and delivery of the COPs, approve modifications to the documents and ratify previous actions taken.

Trust Agreement

The proposed Supplemental Trust Agreement would be the third supplement to the original Trust Agreement between the City and U.S. Bank National Association (US Bank). This Trust Agreement provides the terms of the COPs, prepayment provisions, default and remedy provisions, and other related administrative provisions. The third party trustee holds the proceeds from the sale of the COPs and acts on behalf of the Certificate of Participation holders by administering and disbursing all payments and enforcing the covenants under the Agreement.

The proposed ordinance states that the selection of the third party trustee is delegated to the Director of Public Finance based on the lowest fees and other considerations via a competitive RFP process. Ms. Nadia Sesay, Director of the Office of Public Finance advises that US Bank has already been selected, based on a prior RFP process, under the original transaction. US Bank will continue as the Trustee under the proposed new Supplemental Trust Agreement, as authorized in the Original Trust Agreement, First Supplemental Trust Agreement and the Second Supplemental Trust Agreement.

Property Lease and Project Lease

Under the proposed Supplemental Property Lease, the City would lease City-owned properties that have a market value at or above the par value of the COPs, to the third party trustee. In accordance with the Supplemental Project Lease, the City would then lease back the same City-owned properties, from the third party trustee, by making annual base rental payments in amounts required to repay the COPs. When the COPs are fully repaid, the Property Lease and Project Lease between the City and the third party trustee will terminate.

The City-owned Pavilion Building and the North Residence Building within the Department of Public Health's Laguna Honda Hospital complex are the designated City-owned properties that will secure the subject COPs under the proposed Supplemental Property Lease and Supplemental Project Lease. These Laguna Honda Hospital properties have an estimated asset valuation of \$575,000,000, as determined by the Director of Real Estate. These same Laguna Honda Hospital buildings also serve as the leased asset for outstanding COP Series 2009A, Series 2009B and Series 2012A for other City capital improvements. As shown in Table 2 below, these prior COPs secured a total of \$244,055,000, leaving an available capacity of \$330,945,000 (\$575,000,000 less \$244,055,000) remaining in the Laguna Honda properties that can be secured by other COPs. As noted above, the proposed ordinance would authorize a not to exceed \$95,000,000 COPs for affordable housing projects.

Table 2: Original and Supplemental Trust Agreements, Property Leases and Project Leases Secured by Laguna Honda Hospital Properties

Legislation	COP Series	Date Issued	Trust Agreement, Property and Project Leases	Amount Secured
Resolution 351-08	2009A	May 1, 2009	Original	\$163,335,000
Ordinance 74-09	2009B	September 1, 2009	First Supplement	37,885,000
Ordinance 264-10	2012A	June 1, 2012	Second Supplement	42,835,000
Total				\$244,055,000

Competitive vs Negotiated Sale

The proposed ordinance authorizes the Director of Public Finance to sell the COPs by either a competitive or negotiated sale, pursuant to a purchase contract. If sold by competitive bid, the Controller is authorized to award the Certificates to the bidder whose bid represents the lowest true interest cost to the City. The advantage of a competitive sale is that it typically results in a lower interest rate and therefore less cost to the City, barring any major market disruption. The advantage of a negotiated sale is that the interest rate is pre-negotiated with a known underwriter and therefore predictable on the date of the sale. Given the City's strong credit rating and extensive market experience, Ms. Sesay advises that she anticipates this sale will be competitive.

Affordable Housing Projects

As summarized in Table 3 below, total affordable housing project development costs are estimated at \$1,686,377,688, of which the Housing Trust Fund will contribute \$179,598,383 including \$75,000,000 from these COP proceeds to renovate and/or construct an estimated total of 3,156 housing units. The balance of non-City Housing Trust Fund sources include developer fees, Federal low-income tax credits, State and other grants, private equity and traditional commercial debt secured by developers of these affordable housing projects. Mr. McCloskey advises that all of the City Housing Trust Fund contributions are structured as loan agreements, which provide a legal mechanism to ensure that each project maintains the affordability requirements and restrictions. The dates shown in the parenthesis in Table 3 are the estimated dates that MOHCD will need the initial disbursement of the subject funds.

Parcel O is the largest remaining Central Freeway/Octavia Boulevard property, comprised of 108 housing units specifically for low-income families, ground floor retail, central courtyard and community garden. Based on a Request for Proposal (RFP) process in 2014, the development team of Mercy Housing and San Francisco Housing Development Corporation were selected and are anticipated to commence construction in early 2017. As shown in Table 3 below, this project will require \$30,400,000 of Housing Trust Fund revenues or 49% of the total estimated

project cost of \$61,741,174, including \$3,527,709 of the requested COPs. This project is anticipated to be completed in the Fall of 2018.

The Rental Assistance Demonstration (RAD) funding, as shown in Table 3 below, would contribute to the rehabilitation of 796 existing housing units in nine public housing projects at a total estimated project cost of \$381,736,514 under RAD Phase I, including a total of \$21,472,291 from the requested COPs. In addition, the rehabilitation of 1,932 existing housing units in ten public housing projects at a total estimated project cost of \$1,060,000,000 would be under RAD Phase II, including a total of \$30,000,000 from these COPs. According to Mr. Benjamin McCloskey, Deputy Director of Finance and Administration for MOHCD, RAD changes the formula for how the Federal government subsidizes public housing and also moves the ownership and property management of the properties to community based non-profit affordable housing developers for the rehabilitation of such public housing units. Disbursements of the subject funds would occur in lump sums to each project when rehabilitation of each project is completed and converted to permanent financing. According to Mr. McCloskey, construction of the RAD Phase I projects began in November 2015 and are anticipated to be completed by July 2017. The RAD Phase II projects will start construction by the end of 2016 and are anticipated to be completed by December 2018. Mr. McCloskey advises that the total project costs for RAD Phase I have been secured and total project costs for RAD Phase II are currently being finalized. Non-City funding for these RAD projects include tax credit investors and commercial lenders.

As shown in Table 3 below, development and construction costs for 311 additional new affordable housing units on the following three sites are estimated at \$182,350,000, of which \$78,450,000 would come from Housing Trust Fund revenues, including \$20 million from these COP proceeds.

Treasure Island Parcel C3.2 is part of Phase I development to replace existing housing serving the homeless on Treasure Island and create new affordable housing. This project will include 101 new transitional and permanent housing units for veterans. Swords to Plowshares, a nonprofit member of the Treasure Island Homeless Development Initiative, together with a development partner to be determined, will develop this site. This parcel will be available for development in 2018, with the units completed no earlier than 2020-21. As shown in Table 3 below, funding would not be needed until FY 2019-20, using \$3,000,000 of the requested COPs to fund the gap in permanent financing for this project.

801 Brannan Street is a vacant parcel that will be deeded to the City at the end of 2017 under the City's Inclusionary Program's land dedication alternative option for developers. Feasibility studies indicate this parcel can accommodate up to 150 new units of family housing. Predevelopment will begin in early 2017 with estimated completion by early 2020. As shown in Table 3 below, this project would use \$4,000,000 of the requested COPs to fund the gap in permanent financing for this project.

HOPE SF Sunnydale Block 7 would be a new 69-unit multi-family apartment building to provide replacement housing for the overall Sunnydale relocation efforts, targeted to households with

incomes up to 50% of the Area Median Income. Block 7 is anticipated to be completed in late 2020. As shown in Table 3 below, of the total \$44,850,000 project cost, \$13,000,000 would come from the requested COPs.

Table 3: Projects to be Funded with the Requested COPs

Project and Location	Number of Housing Units	Total Estimated Project Cost	Total Housing Trust Revenues	Total Housing Trust Fund COP Allocation
Parcel O (January 2017)	108	\$61,741,174	\$30,400,000	\$3,527,709
<u>RAD Phase I (March 2017)</u>				
227 Bay Street	51	\$24,847,635	\$3,728,290	\$2,781,173
990 Pacific	92	66,645,645	11,040,821	2,540,821
939-951 Eddy	60	23,315,505	2,911,448	1,768,432
666 Ellis	100	39,153,004	3,238,369	1,941,615
430-440 Turk	89	37,670,083	2,699,043	1,354,444
25 Sanchez	90	44,398,975	1,177,891	33,684
462 Duboce	42	30,863,408	9,410,236	8,385,005
Robert B. Pitts	203	83,017,327	1,622,886	1,622,886
345 Arguello	<u>69</u>	<u>31,824,932</u>	<u>2,045,142</u>	<u>1,044,231</u>
Subtotal	796	\$381,736,514	\$37,874,126	\$21,472,291
<u>RAD Phase II (September 2018)</u>				
Ping Yuen	234	115,000,000	2,000,000	2,000,000
Ping Yuen North	200	105,000,000	2,151,298	2,151,298
Westside Courts	136	75,000,000	2,267,425	2,002,869
1750 McAllister	97	45,000,000	4,049,733	4,049,733
320 & 330 Clementina	276	100,000,000	3,076,940	3,076,940
350 Ellis	100	55,000,000	6,980,184	6,980,184
Alemany	158	110,000,000	5,079,131	7,078,131
Mission Dolores	92	45,000,000	1,401,816	331,000
1760 Bush	108	45,000,000	1,080,000	1,080,000
Westbrook Apts.	<u>226</u>	<u>130,000,000</u>	<u>2,530,819</u>	<u>1,249,845</u>
Subtotal	1,932	\$1,060,000,000	\$32,974,257	\$30,000,000
<u>Development Sites (FY 2019-20)</u>				
Treasure Island C3.2	101	55,550,000	25,250,000	3,000,000
801 Brannan Street	150	82,500,000	37,500,000	4,000,000
HOPE SF-Sunnydale Block 7	<u>69</u>	<u>44,850,000</u>	<u>15,600,000</u>	<u>13,000,000</u>
Subtotal	320	\$182,900,000	\$78,350,000	\$20,000,000
Total	3,156	\$1,686,377,688	\$179,598,383	\$75,000,000

FISCAL IMPACT

The proposed ordinance would authorize a not-to-exceed amount of \$95 million of COPs. As discussed above, \$75 million of the COPS would be used to fund affordable housing project costs. The balance of up to \$20 million will fund the Controller’s Office audit fees, debt service reserve account, issuance expense, underwriter’s discount and allow for sufficient flexibility for conservative assumptions of market conditions for the COPs, as shown in Table 4 below.

Table 4: Estimated Uses for the \$95 Million COPs

Project Funds	\$75,000,000
Controller’s Audit Fee (2%)	150,000
Debt Service Reserve Fund	7,169,836
Cost of Issuance	700,000
Underwriters Discount	420,164
Subtotal	\$83,400,000
Market Conditions Flexibility	11,600,000
Total	\$95,000,000

Ms. Sesay advises that the \$11,600,000 for market conditions flexibility will also allow for potential capitalized interest expense between the time of issuance and the use of the funds. These COPs are anticipated to be sold in the spring of 2017. However, Ms. Sesay notes the Office of Public Finance may issue commercial paper prior to the COP issuance and that one or more issuances of the COPs may occur, depending on the timing for the need for housing project funds. Approval is being requested now to allow MOHCD and the Office of Public Finance the ability to move quickly to respond to changing market conditions as the affordable housing projects proceed and utilize commercial paper as an interim funding source prior to the COP issuance. Ms. Sesay further advises that the Office of Public Finance will only issue what is necessary to fund the \$75 million of specified affordable housing project expense.

According to Ms. Sesay, the requested not to exceed \$95,000,000 COPs would be issued for a term of 30 years. Assuming one \$83,440,000 issuance and a conservative 7.528 annual interest rate will result in total estimated costs of \$213,235,199 over a 30-year term. This \$213,235,199 total includes \$129,795,199 of interest and \$83,440,000 of principal, based on estimated average annual debt service payments of \$7,088,151. Repayment of the not to exceed \$95 million of COPs will solely be from future Housing Trust Fund allocations.

As shown in Table 1 above, to date \$50 million of the COPs were appropriated in the FY 2013-14 and FY 2014-15 budgets. Mr. McCloskey advises that the remaining \$25 million of COP funds and debt service payments would be requested to be appropriated in the FY 2016-17 budget, subject to appropriation approval by the Board of Supervisors.

RECOMMENDATION

Approve the proposed ordinance.

<p>Items 6 and 7 Files 16-0282 and 16-0283</p>	<p>Departments: Adult Probation Department Real Estate Division</p>
<p>EXECUTIVE SUMMARY</p>	
<p style="text-align: center;">Legislative Objectives</p>	
<p>File 16-0282 approves fifth amendment to the contract between the Adult Probation Department and LCA to operate the Community Assessment and Services Center (CASC).</p>	
<p>File 16-0283 approves a ten-year lease between the City, as tenant, and Presidio Bay Ventures (PBV) II, LLC, as landlord for office space located at 564 6th Street for use as the CASC.</p>	
<p style="text-align: center;">Key Points</p>	
<ul style="list-style-type: none"> • The Adult Probation Department entered into a contract in June 2012 with the Leaders in Community Alternatives, Inc. (LCA) to operate the CASC. In addition, LCA leases space at 564 6th Street for the CASC. The proposed fifth amendment to the contract between the Adult Probation Department and LCA would exercise the final one-year contract extension option from July 1, 2016 to June 30, 2017. • The proposed lease between the City and PBV II, LLC replaces the existing lease between LCA and PBV II, LLC for 564 6th Street. The proposed lease is for ten years from July 1, 2016 through June 30, 2026 with four 5-year options to extend through June 30, 2046. 	
<p style="text-align: center;">Fiscal Impact</p>	
<ul style="list-style-type: none"> • The proposed fifth amendment to the contract increases the not-to-exceed amount by \$2,276,196, from \$9,213,957 to \$11,490,153. Rent to be paid by the City to PBV II, LLC for 564 6th Street over the initial ten-year lease term is \$9,723,548. 	
<p style="text-align: center;">Policy Consideration</p>	
<ul style="list-style-type: none"> • Based on the inquiry of the Budget and Legislative Analyst, PBV II, LLC, owner of 564 6th Street, will agree to revise the proposed lease to provide the City the right to terminate the lease with one year’s notice in order to give the Capital Planning Committee the opportunity to evaluate and recommend alternatives to the Adult Probation Department’s long-term lease for 564 6th Street. 	
<p style="text-align: center;">Recommendations</p>	
<ul style="list-style-type: none"> • Approve the proposed resolution approving the fifth amendment to the contract between the Adult Probation Department and Leaders in Community Alternatives, Inc. (File 16-0282). • Amend the proposed resolution (File 16-0283), approving the lease between the City and PBV II, LLC for 564 6th Street, to (a) request the Capital Planning Committee to evaluate alternatives to the Adult Probation Department’s long-term lease for 564 6th Street as part of the evaluation of the Sheriff’s Department’s and Adult Probation Department’s space needs, and incorporate these alternatives into the City’s capital plan; and (b) state that the City’s Real Estate Division and PBV II, LLC have agreed to add a clause to the proposed lease providing the City the right to terminate the lease with one year’s notice. This right to terminate the lease would expire in two years on June 30, 2018. • Approve the proposed resolution (File 16-0283) as amended. 	

MANDATE STATEMENT

City Charter Section 9.118(b) requires Board of Supervisors approval for contracts that have a term of more than ten years or expenditures of \$10 million or more.

City Administrative Code 23.27 states that any lease with a term of one year or longer or with rent of \$5,000 or more and where the City is the tenant is subject to Board of Supervisors approval.

BACKGROUND

The Adult Probation Department's Community Assessment and Services Center (CASC) is a one-stop service center to coordinate services, such as behavioral health and job training, to individuals under the jurisdiction of the Adult Probation Department. These individuals include offenders sentenced to probation supervision by the Adult Probation Department, and offenders released from State prison to post release community supervision by the Adult Probation Department (rather than State parole) under Assembly Bill (AB) 109.¹

The Adult Probation Department entered into a contract in June 2012 with the Leaders in Community Alternatives, Inc. (LCA), a non-profit organization, through a competitive Request for Proposals (RFP) process, to operate the CASC. Under the contract, LCA assesses individuals under Adult Probation Department supervision to identify appropriate treatments and services, provides direct services, and refers individuals to other services, such as housing referrals. In addition, LCA leases space at 564 6th Street for the CASC.

The original contract was for one year from June 1, 2012 through June 30, 2013, with four one-year options to extend through June 30, 2017. The original contract not-to-exceed amount was \$2,258,879. The contract has been amended four times to extend the contract through June 30, 2016 and increase the not-to-exceed amount to \$9,213,957.

DETAILS OF PROPOSED LEGISLATION

File 16-0282 is a resolution approving the fifth amendment to the contract between the Adult Probation Department and LCA to operate the CASC. The fifth amendment authorizes the fourth option to extend the contract by one year to June 30, 2017 and increases the not-to-exceed amount by \$2,276,196, from \$9,213,957 to \$11,490,153.

File 16-0283 is a resolution approving a ten-year lease between the City, as tenant, and Presidio Bay Ventures (PBV) II, LLC, as landlord for office space located at 564 6th Street for use as the Community Assessment and Services Center. LCA initially entered into a lease with PBV II, LLC for 564 6th Street in September 2012 for use as the CASC. LCA's lease for 564 6th Street was for

¹ In 2011, the State Legislature adopted AB 109, which shifted responsibility for certain offenders from the State to the County. AB 109 revised the State Penal Code to create a new category of non-serious, non-violent and non-sex crimes for offenders without serious prior convictions that would be prosecuted by the County rather than the State. These offenders are now sentenced to County jail time (rather than State prison time) or a combination of jail time and mandatory supervision by the Adult Probation Department. Also, under AB 109, inmates exiting from state prison on or after October 2011, who were serving sentences for lower level felonies, were released to post release community supervision by the Adult Probation Department (rather than State parole).

approximately four years and 10 months from September 7, 2012 through June 30, 2017. The proposed lease between the City and PBV II, LLC for 564 6th Street would replace the lease between LCA and PBV II, LLC.

File 16-0283: Proposed Lease for 564 6th Street

The proposed lease terms are shown in Table 1 below.

Table 1: Proposed Lease Terms for 564 6th Street

Premises	17,500 square feet of office space on the first and second floors of 564 6 th Street
Lease Term	10 years from July 1, 2016 through June 30, 2026
Options to Extend	Four five-year options to extend, totaling 20 years, through June 30, 2046
Initial Rent	Approximately \$48.47 per square foot per year for 17,500 square feet \$848,190 annual rent in first year
Annual Rent Increase	3 percent per year
Rent Adjustment on Exercise of Options	95 percent of fair market rate based on properties of comparable size and location. If the City and landlord do not agree to the prevailing market rate, then the fair market rate will be determined by an independent appraisal.
Property Taxes	City pays increase in property taxes over 2016/2017 base year property tax
Operating Expenses	City pays gas, electricity, water, sewer, trash removal, pest control, janitorial, security

According to information provided by the Real Estate Division to the Budget and Legislative Analyst's Office, rents for comparable properties in the neighborhood range from \$60 per square foot to \$73 per square foot, which is \$11.53 to \$24.53 per square foot more than the proposed rent for 564 6th Street of \$48.47 per square foot.

Sublease between the City, as sub-landlord, and LCA, as sub-tenant

The proposed resolution would also approve a one-year sublease between the City, as sub-landlord, and LCA, as sub-tenant for LCA to use the space at 546 6th Street to operate the CASC. The sublease would continue through June 30, 2017, when the contract between the Adult Probation Department and LCA will terminate. The sublease may be extended beyond June 30, 2017 if LCA is awarded a new contract to operate the CASC following a new competitive RFP process.

Under the sublease, LCA would occupy approximately 4,923 square feet, including 2,085 exclusive use space and 2,838 shared space including common areas. The sublease states that LCA would pay to the City initial rent of \$238,596 in the first year, which is LCA's proportional

share of the City’s rent for 564 6th Street, ² and a proportional share of utilities, property tax, and other charges. However, LCA will not pay rent, utilities and other charges to the City during the term of the contract between the City and LCA for LCA to operate the CASC which expires on June 30, 2017.

Current and Proposed Use of Space

Of the 17,500 square feet of space at 564 6th Street:

- 5,326 square feet are occupied by the Adult Probation Department;³
- 2,085 square feet are occupied by LCA;⁴ and
- 10,089 square feet are shared program space.

Change in Rent Arrangement under Proposed Lease

Currently, LCA has the lease with PBV II, LLC, for 564 6th Street, which terminates on June 30, 2017. Under the contract between LCA and the Adult Probation Department, LCA pays rent and operating expenses to PBV II, LLC and is reimbursed the full amount by the Adult Probation Department. In addition the City pays a lease administration fee to PBV II, LLC, as shown in Table 2 below.

Under the proposed lease, the City pays rent directly to PBV II, LLC. As shown in Table 2 below, the City’s rent payments to PBV II, LLC under the proposed lease are 8.7 percent less than the City’s reimbursements to LCA and lease administration fees under the current lease.

Table 2: Comparison of City Costs under Current and Proposed Lease

	Current Lease Between LCA and PBV II, LLC			Proposed Lease Between City and PBV II, LLC	Decrease in Rent Under Proposed Lease	
	LCA Rent Paid to Landlord and Reimbursed by City	City Lease Administration Fee	Total Current Lease	City Rent Paid to Landlord	Amount	Percent
Annual	\$807,792	\$121,169	\$928,961	\$848,190	(\$80,771)	-8.7%
Per Square Foot ^a	\$46.16	\$6.92	\$53.08	\$48.47	(\$4.62)	-8.7%

Source: Real Estate Division

^a Amounts may differ by \$.01 due to rounding

² 4,923 square feet equals 28.1 percent of 17,500 total square feet, and rent of \$238,597 equals approximately 28.1 percent of the City’s total rent of \$848,190.

³ 31 Adult Probation Department staff, and four Department of Public Health staff, totaling 35 staff, are assigned to the CASC at 564 6th Street (resulting in approximately 152 square feet per staff member). The Adult Probation Department staff consist of probation officers providing probation supervision services, and civilian staff providing contract administration, record keeping, probation support and other services.

⁴ 25 LCA staff are assigned to 564 6th Street (resulting in approximately 83 square feet per staff member).

File 16-0282: Proposed Fifth Amendment to the Contract between the Adult Probation Department and LCA

The proposed fifth amendment to the contract between the Adult Probation Department and LCA for LCA to operate the CASC would exercise the final one-year contract extension option from July 1, 2016 to June 30, 2017. The Adult Probation Department will issue a new competitive RFP to select a contractor to operate the CASC prior to June 30, 2017.

The proposed fifth amendment includes the following provisions:

- Continues LCA's scope of work as part of the operation of the CASC, including: (1) staff training in the National Institute of Correction's evidence-based principles for effective community corrections interventions; (2) assessment of individuals under community intervention, and planning for appropriate services; (3) oversight of service provision, including case management; and (4) providing rehabilitative programs, such as anger management and substance abuse counseling.

According to Ms. Diane Lim, Adult Probation Department Director of Finance and Administrative Services, eligibility for these services will be extended to any San Francisco resident who is currently involved in the criminal justice system or who has a criminal history.

- Continues LCA's role in maintaining the CASC facility at 564 6th Street, including onsite security and other facility maintenance. However, while LCA currently holds the lease for 564 6th Street and is compensated by the City for the rent, under File 16-0283, the City would enter directly into a ten-year lease with PBV II, LLC, for 564 6th Street and pay the rent directly to PBV II, LLC.

FISCAL IMPACT**File 16-0282: Proposed Fifth Amendment**

The proposed fifth amendment increases the contract not-to-exceed amount by \$2,276,196, from \$9,213,957 to \$11,490,153, as shown in Table 3 below.

Table 3: Contract Budget Compared to Actual and Projected Contract Expenditures

	Start Date	End Date	Budget	Actual and Projected	Over/ (Under) Budget
Original Contract/ First Amendment	6/1/12	6/30/13	\$3,075,795	\$2,048,465	(\$1,027,330)
2nd Amendment	7/1/13	6/30/14	2,360,603	2,822,023	461,420
3rd Amendment	7/1/14	6/30/15	2,361,603	2,384,773	23,170
4th Amendment	7/1/15	6/30/16	1,415,956		(1,415,956)
5th Amendment	7/1/15	6/30/16		2,556,286	2,556,286
5th Amendment	7/1/16	6/30/17		1,678,606	1,678,606
Total			\$9,213,957	\$11,490,153	\$2,276,196

Source: Adult Probation Department and Contract Amendments

The FY 2015-16 and FY 2016-17 budgets for the CASC contract are shown in Table 4 below.

Table 4: FY 2015-16 and FY 2016-17 CASC Budget

	FY 2015-16 Revised Budget	FY 2016-17 Budget
LCA Staff Salaries and Benefits	\$807,774	\$894,968
Program and Operating Expenses	559,289	539,522
Subtotal, Staff and Operating	1,367,063	1,434,490
Rent for 564 6th Street	807,792	0
Utilities and Other Charges	48,002	48,002
Subtotal, Facilities	855,794	48,002
Indirect Expenses	333,429	196,114
Total	\$2,556,286	\$1,678,606

Source: Contract Fifth Amendment

Sources of funds to pay for the contract are State Public Safety Realignment funds, authorized under AB 109, subject to appropriation approval by the Board of Supervisors.

File 16-0283: Proposed Lease for 564 6th Street

Rent to be paid by the City to PBV II, LLC for 564 6th Street over the initial ten-year lease term is \$9,723,548, as shown in Table 4 below. In addition, the City's Real Estate Division estimates \$1,219,471 in operating costs, including utilities, security, and other costs over ten years, for total estimated lease and operating costs of \$10,943,019.

Table 4: Rent to be Paid by the City to PBV II, LLC for 564 6th Street

Lease Year	Month Rent	Annual Rent
FY 2016-17	\$70,683	\$848,190
FY 2017-18	72,803	873,636
FY 2018-19	74,987	899,845
FY 2019-20	77,237	926,840
FY 2020-21	79,554	954,645
FY 2021-22	81,940	983,285
FY 2022-23	84,399	1,012,783
FY 2023-24	86,931	1,043,167
FY 2024-25	89,538	1,074,462
FY 2025-26	92,225	1,106,696
Total		\$9,723,548

Source: Proposed Lease

The lease costs are City General Fund costs. Funds to pay the lease costs will be requested in the Department's annual budget submission, subject to appropriation approval by the Board of Supervisors.

POLICY CONSIDERATION

The City needs to develop a space plan for re-entry programs to avoid duplication of programs and related lease costs

According to the March 11, 2016 memorandum from the Chief Adult Probation Officer to the Board of Supervisors, the Adult Probation Department seeks to retain 564 6th Street as the dedicated CASC facility due to (a) the proximity to the Adult Probation Department offices in the Hall of Justice, (b) the usefulness of the facility as a one-stop service center for re-entry services for people in the criminal justice system, and (c) continued use of \$1.6 million in tenant improvements paid by the City in 2013 when LCA entered into the original lease with PBV II, LLC for 564 6th Street.

The Budget and Legislative Analyst previously noted in the report to the April 30, 2014 Budget and Finance Committee that the Adult Probation Department provides programs at the CASC at 564 6th Street which are similar to the programs provided by the Sheriff's Department at the leased space at 70 Oak Grove Street (File 14-0249). Based on the Budget and Legislative Analyst's recommendation, the Board of Supervisors amended File 14-0249 to state that "re-entry programs provided by community justice departments of the City be analyzed for opportunities of consolidation where feasible to effect reductions in leasing expenses".

The City needs to develop a longer-range plan to consolidate space for re-entry programs provided by the Adult Probation Department and the Sheriff's Department to avoid duplication

of leased space and high costs to the City.⁵ According to Mr. Brian Strong, Director, Capital Planning Program, the Sheriff's Department is currently evaluating a facility master plan that will consider the space needs for the Sheriff's Department, including re-entry programs. Further, the Capital Planning Committee is evaluating (1) the alternatives to constructing a jail to replace County Jails No. 3 and 4, (2) the alternatives to the Sheriff's Department's use of 70 Oak Grove Street for re-entry programs, and (3) the relocation of the Adult Probation Department from the Hall of Justice. The Capital Planning Committee should evaluate alternatives to the Adult Probation Department's long-term lease for 564 6th Street as part of the evaluation of the Sheriff's Department's and Adult Probation Department's space needs, and incorporate these alternatives into the City's capital plan.

Based on the inquiry of the Budget and Legislative Analyst and in order to give the Capital Planning Committee the opportunity to evaluate and recommend alternatives to the Adult Probation Department's long-term lease for 564 6th Street, according to Mr. Charlie Dunn, Real Estate Division, Senior Real Property Officer, PBV II, LLC, owner of 564 6th Street, will agree to revise the proposed lease to provide the City the right to terminate the lease with one year's notice. This right to terminate the lease would expire in two years on June 30, 2018.

RECOMMENDATIONS

1. Approve the proposed resolution approving the fifth amendment to the contract between the Adult Probation Department and Leaders in Community Alternatives, Inc. (File 16-0282).
2. Amend the proposed resolution (File 16-0283), approving the lease between the City and PBV II, LLC for 564 6th Street, to (a) request the Capital Planning Committee to evaluate alternatives to the Adult Probation Department's long-term lease for 564 6th Street as part of the evaluation of the Sheriff's Department's and Adult Probation Department's space needs, and incorporate these alternatives into the City's capital plan; and (b) state that the City's Real Estate Division and PBV II, LLC have agreed to add a clause to the proposed lease providing the City with the right to terminate the lease with one year's notice. This right to terminate the lease would expire in two years on June 30, 2018.
3. Approve the proposed resolution (File 16-0283) as amended.

⁵ The estimated costs to the City to lease 564 6th Street would be \$40.3 million over 30 years, based on annual rent increases of 3 percent per year, if the City were to exercise the four 5-year options to extend the lease for 546 6th Street for up to 30 years. The annual rent increases during the initial 10-year term by 3 percent per year; the rent adjusts to 95 percent of fair market value for each of the four 5-year options to extend the lease.