



CITY OF MILPITAS AGENDA REPORT (AR)

ATTACHMENT 2

Item Title:	Receive a report on the proposed project proposal for low and moderate income housing at Turing Apartments through a California Statewide Communities Development Authority program and provide direction to staff on next steps, if any.
Category:	Community Development
Meeting Date:	11/1/2021
Staff Contact:	Ashwini Kantak, Assistant City Manager, 408-586-3053 Sharon Goei, Building Safety and Housing Director, 408-586-3260
Recommendations:	<ol style="list-style-type: none">1. Receive follow-up information on the proposed project proposal for low and moderate income housing at Turing Apartments through a California Statewide Communities Development Authority program.2. If Council wishes to pursue the proposed project, staff recommends Council (a) require project team to provide needed funding for additional staff, City Attorney, and consultant resources; (b) direct staff to bring back a framework and goals for this type of a moderate income housing program for Council consideration based on staff recommendations and Council input; and (c) direct staff to work with the project team on an agreement that is consistent with the approved framework and goals for a moderate income housing program.

Background:

In May 2021, Council directed staff to analyze a proposal to join the Community Improvement Authority (Authority), an affiliate of the California Statewide Communities Development Authority (CSCDA), and to support the purchase of the Turing Apartments for the purpose of converting the 371-unit market rate project to moderate income housing. In response to the many questions that have been asked about this project, staff has prepared a Frequently Asked Questions (FAQ) document (Attachment 1).

On September 21, the City Council received a presentation, including findings and preliminary recommendations, on the project proposal. Here is the link to the [September 21 Staff Report](#) and it is also included as Attachment 2.

Council directed the CSCDA team to return to the City Council in October with a revised proposal that would address staff recommendations including deepening affordability levels, increasing capital investment and improving numbers across the board. Some Councilmembers also noted their desire for community outreach. The project proposal was on the agenda for the October 19 City Council meeting. The City Council postponed the item to a future date.

Analysis:

The CSCDA team submitted a preliminary revised proposal on October 8, however some additional clarification was requested by staff, which was provided on October 13 (See Attachment 3). The project team also submitted a revised proposal on October 15 (See Attachment 5). Staff has not completed its in-depth analysis of these revised proposals; however, the consultant did provide a brief analysis of the October 13 proposal (See Attachment 4).

If Council directs staff to continue work on this proposal, additional funding for consultant and City Attorney services will be required from the project team.

Additionally, staff continues to spend a significant amount of time on this proposed project and if additional staff work is required, the work will not be able to continue on an accelerated timeline since there are many other Council priority projects, including those with federal and state mandated deadlines, that need to be completed.

Key Areas that were recommended by staff and deemed important by Council are:

1. Affordability

- a. Rents higher than market rate apartments in Milpitas
- b. Different income eligibility for California Department of Housing and Community Development (HCD) and CSCDA
- c. Units do not count towards City's Regional Housing Needs Allocation (RHNA) numbers, no new housing stock added

2. Financial Assumptions

- a. Assumptions are too optimistic; more conservative assumptions could result in significantly decreased Return on Investment (ROI). A 3% rent increase assumption is not realistic, based on historical data in Milpitas and rent increase restrictions related to the Area Median Income. This is important since City will be foregoing property taxes and may not reap the benefits as projected.

3. Level of Capital Investment

- a. Capital investment was initially based on a 12-year condition report, not on life of project/bond term; this has since been updated.

4. Transparency and Oversight

- a. City does not control rental rates, implementation of affordability covenants, timing of re-financing, if any, and appropriate maintenance of asset.

A few additional items of note are as follows:

- 1. The current agreements do not include any performance metrics or enforcement mechanisms in favor of the City.
- 2. Cash flow projections and proforma are based on assumptions regarding tenant turnover, however, since existing tenants are not asked to leave and the rents are higher than market-rate, the likelihood of a turnover to low and moderate income households within a three year timeframe appears highly unlikely. In fact, once rents are reduced one would expect less tenant turnover as with other rent controlled projects.
- 3. Also, the process of tenant selection when a unit becomes vacant is not clearly defined. It could take several years for the project to serve the tenant population that is at the 60-80% AMI and the 80-100% AMI.
- 4. There are no enforceable metrics associated with the level of affordability. Thus, it is important for the City to negotiate terms that will provide true affordability in exchange for foregoing property taxes and vehicle license fees so as to ensure that the project does not inadvertently just provide rent control for luxury apartments at the expense of City property tax revenues.

Information about how the revised proposal as received on October 13 and 15 addresses the preliminary recommendations discussed by Council on September 21 is noted below. An updated brief analysis by the consultant is included as Attachment 4.

1. The rent reductions should be set at levels that are below market rate levels in Milpitas so that the Project truly delivers enhanced affordability. The proposed rent levels exceed average market rate rental rates, which largely nullifies the argument that the Project will meaningfully enhance the affordability of apartments in Milpitas.
The revised proposal does not address this recommendation.
2. Rent and income restrictions contained in the Regulatory Agreement should conform to the California Department of Housing and Community Development (HCD) income limits. As proposed, the rent and income formulas are not consistent with the HCD formulas and result in significantly higher rents than what would be permitted by HCD.
The revised proposal does not address this recommendation. The revised proposal does reduce the allowable maximum rents based on 30% of income versus 35% of income but it still does not align with HCD formulas.
3. The Property Condition Report should address the Project's needs for a 34-year term and the Project's financing plan provide funding to cover the anticipated capital improvement costs over the 34-year term. The draft property condition report only addresses 12 years of needs. The proposed annual contributions for capital improvements appears to be inadequate.
The revised proposal includes an updated Property Condition Report based on the 35 year term and the capital investment has been increased from \$7.6 million to \$11.8 million in 2021 dollars. However, this increase is made possible by making cash flow projections more favorable in two primary ways – increased current rent assumptions and decreased vacancy rate projections in the first three years of the project. Staff has already noted concerns about previously proposed cash flow projections including its underlying assumptions and these changes appear to further exacerbate these concerns.
4. Any refinancing of Project debt should be subject to the City's approval.
The project team is amenable to this recommendation in concept; however, this will require staff and City Attorney coordination with CSCDA. Staff is recommending that performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.
5. The Project should be required to submit proposed rent increases to the City's approval to ensure that the affordability restrictions are enforced.
The revised proposal does not address this recommendation. The project team has noted concerns with this recommendation.
6. The Project should be required to submit an annual report to the City demonstrating that the affordability covenants are being properly implemented and enforced and meeting the identified affordability goals.
The project team is amenable to this recommendation in concept; however, this will require staff and City Attorney coordination with CSCDA. Staff is recommending that performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.
7. The Administrator should be obligated to certify that the affordability covenants are being properly implemented and enforced to meet the agreed upon affordability goals.

The project team is amenable to this recommendation in concept; however, this will require staff and City Attorney coordination with CSCDA. Staff is recommending that performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.

8. The Project's cash flow projection should be based on more conservative assumptions to reduce the level of risk and provide greater assurance for long-term viability.
The revised proposal does not address this recommendation rather, the assumptions are increasing risk as noted in Item #3.
9. The bond underwriting assumptions should be reviewed by an underwriter retained by the City and the City's Financial Advisor to ensure that the financial structure is sound and consistent with industry standards for multifamily revenue bonds and is appropriate for the City's participation, as well as review the City purchase option price and evaluate if the project can recoup the substantial lost property tax revenue.
The project team has advised that the City should rely on the underwriter retained by them; this does not address the recommendation of review by an underwriter hired by the City.
10. Greystar (Manager) should be required to submit its tenant selection plan, maintenance plan, staffing plan and marketing plan for the City's review and approval.
The project team is amenable to this recommendation in concept; however, this will require staff and City Attorney coordination with CSCDA on specific agreement terms. Staff is recommending that in order to ensure the project meets the City's affordability goals, performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.
11. Greystar (Manager) should be required to submit annual reports on the Project's operations, including the Project's rent roll, that clearly track the annual increase in rental rates, operating expenses, capital improvements, vacancy rates, bond interest and redemption payments, and all bond specific payments.
The project team is amenable to this recommendation in concept; however, this will require staff and City Attorney coordination with CSCDA. Staff is recommending that performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.
12. In addition to the preliminary recommendations developed by the consultant, the City should consider entering into an agreement with the project team so as to clearly capture the roles of the project team and the City through the term of the bond and describe process for enforcement.
The project team has indicated that the Public Benefit Agreement could be amended to address this recommendation; however, this will require staff and City Attorney coordination with CSCDA. Staff is recommending that performance metrics, remedies and consequences of not meeting those metrics be included in the agreement.

In addition to the responses noted above, the project team has proposed local preference guidelines so as to enable a preference to households which include one or more persons who are employed by a public school district or public higher education institution within the City of Milpitas. **This will require further analysis by the City Attorney to evaluate risk of implementation and compliance with State and federal fair housing laws.**

The revised proposal submitted on October 15 includes additional items that will need further financial and legal review as noted below:

- Term of Regulatory Agreement - potentially change to a 55-year term; will require legal and financial review.
- Affordable Housing Monitoring Fee - \$37,100; since agreement terms have not been negotiated and actual costs of monitoring are yet to be determined.
- Mandated Rental Savings in Regulatory Agreement – designated 8 units to be market rate, with minimum discounts for different income groups; any changes to proforma have not been submitted to and evaluated by the City.
- Partial Property Tax Backfill - \$100,000 per year for five years; will require legal review.

The project team conducted community outreach at the Milpitas Chamber of Commerce and at Turing Apartments. Information about the community input received will be presented by the project team at the Council meeting.

If Council wishes to pursue this proposed project, there are several actions that will need to be undertaken prior to approval of the project. Also, some of these actions will be applicable for any similar types of projects that may be brought to the Council for consideration.

1. Authorization of funding for additional staff, Attorney, and consultant resources

As noted in the September 21 staff report, staff resources are already fully committed to delivering existing services and programs as well as several new programs and initiatives added because of increased federal funding and other Council funded priorities. If Council provides direction for staff to continue to work on this project as well as other similar projects, staff will need to bring back a discussion to Council on the need for additional resources and prioritization of other workplan items. It is important to note that staff may not be able to pause work on many of the work plan items since there are state and federal requirements and deadlines associated with those work plan items.

Additionally, based on the recommendations, the services of the City Attorney and a third-party financial advisor will also be needed. To date the project team has paid for consultant services provided by KMA but has not paid for staff or City Attorney time. If Council provides direction to move forward with additional work on the proposed project, additional funding will have to be provided by the project team.

2. Develop City goals and framework for this type of program and bring back for Council consideration

Since the proposed project will be providing a substantial City subsidy with the foregoing of approximately \$15.4 million in property tax and property tax in-lieu of vehicle license fee revenues over 30 years, staff recommends developing specific goals and a framework for decision making for this type of project. A framework with goals could include the following:

- a. Percentage of low and moderate income units for each project with a timeline for meeting that percentage
- b. Alignment with City's Housing goals, including RHNA numbers
- c. Condition of asset and proposed improvements
- d. Number of years that bonds need to be paid off by
- e. Amount of lost City revenue and total public subsidy
- f. Types of performance metrics and consequences of not meeting those metrics
- g. Level of oversight and enforcement and remedies
- h. Establishment of associated fees to be paid for by the project to provide oversight and enforcement

3. Work with the project team to develop an agreement that meets the Council approved goals

The proposed Public Benefit Agreement submitted by the project team only addresses the purchase of the asset by the City. Staff and the City Attorney will need to work with the project team on agreement terms that align with approved City goals and framework for this type of program.

Policy Alternative:

Not Applicable

Fiscal Impact:

Although the consultant costs to date have been paid for by the Owner, staff has spent a substantial amount of time working with the consultant and project team. Any additional work on this project will require additional funding for staff and City Attorney time as well as for a financial consultant.

If the City moves forward with this proposed project, over a 30-year period, it is estimated that the City would forego a total of \$15.4 million (or approximately \$9.7 million in 2021 dollars) of property tax revenue, comprised of \$12.4 million of ad valorem property tax revenue and \$3.0 million of property tax in-lieu of vehicle license fee revenues from the state that are linked to taxable assessed property values.

Including all taxing agencies, foregone tax revenues would approximate \$92.9 million over a 30-year period.

Property tax is the City's General Fund top revenue source, representing 37% of total revenues. Property taxes are therefore used to provide vital City services. Any agreement to reduce City property tax revenue for 30+ years will have City service level ramifications.

At the end of the bond term, the project team has suggested that the City may be able to recoup this lost revenue. However, project performance assumptions appear optimistic, which causes the risk of overstating the net return to the City. This proposed agreement does not guarantee the City would recover the \$15.4 million of property tax foregone.

California Environmental Quality Act:

This item is not a Project under CEQA in accordance with CEQA Guidelines Section 15061(b)(3) (Common Sense Exemption) as it can be seen with certainty that a general discussion of funding priorities by the City Council will not have a significant effect on the environment. Further, the item is also not a Project pursuant to CEQA Guidelines Section 15378(b)(4) as it is a government fiscal activity that does not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment.

Recommendations

1. Receive follow-up information on the proposed project proposal for low and moderate income housing at Turing Apartments through a California Statewide Communities Development Authority program.
2. If Council wishes to pursue the proposed project, staff recommends Council (a) require project team to provide needed funding for additional staff, City Attorney, and consultant resources, (b) direct staff to bring back a framework and goals for this type of a moderate income housing program for Council consideration based on staff recommendations and Council input, and (c) direct staff to work with the project team on an agreement that is consistent with the approved framework and goals for a moderate income housing program.

Attachments:

Attachment [1](#) – FAQs

Attachment [2](#) – September 21 Agenda Report

Attachment [3](#) – Response letter from CSCDA and Waterford

Attachment [4](#) – Consultant (KMA) analysis of revised project proposal

Attachment [5](#) – Revised proposal from CSCDA and Waterford (dated October 15)