

Agrihood Q & A Addendum

(January 2019)

Transaction

Q1: What is the appraised land value for the project?

- A. The appraisal valued the market rate parcels at roughly \$6.5 million per acre (approximately \$20 million for 3.04 acres). However, when the market rate parcels are blended together with the buildout of the Agrihood parcel (cost of \$4 to \$6 million), the value of the overall site (including all restrictions) was \$15,260,000.

Q2: Why didn't the valuation include any of the affordable housing land?

- A. The affordable housing land is not being sold to the Developer; rather the City will retain ownership through a ground lease. Given the significant amount of subsidy required and proposed income level restrictions, the affordable housing site component was not factored into the appraised value. Typically, affordable housing projects (especially those projects with similar income levels such as the Agrihood project) do not produce an appreciable residual land value. The amount of income generated by an affordable project over time is limited not only by the amount of starting rent but pro-formas also assume annual rent increases of 2% with expenses increasing at a 3% annual rate.

Q3: Why is the market-rate rental building being built on land that is "sold" and not a "ground lease" like the affordable building?

- A. The project selected by the City through the City's Request for Proposals (RFP) process did not propose a ground lease for any portion of the project. The RFP requested that developers propose a transaction that would reduce or eliminate any further City subsidy. All proposals contemplated the use of proceeds from the market rate components of the project for the benefit of the required affordable component. At the time CORE was selected, an additional City cash contribution in the range of \$4 to \$6 million was contemplated.

As the City's financing plan for the affordable portion of the project evolved, the project was able to secure a significant contribution from the Santa Clara County Office of Supportive Housing utilizing Measure A Funding. Use of Measure A funding requires that the project be retained in public ownership and so the ground lease became an element of the financing for the affordable housing portion of the project. If the City were to require a ground lease on the market rate parcel, this requirement would ultimately devalue the property and create the need for additional offsetting subsidy in the affordable project. Under the proposed financing structure, there is no additional City contribution necessary for the affordable project.

Q4: Core (the developer) plans to purchase the land under the market-rate apartment building and the townhomes for approximately \$15,700,000, which the City will immediately loan back to Core to help pay for the affordable building. Why couldn't that money be directly invested into the affordable building by Core?

- A. While this is mechanically possible, it would be disadvantageous to the City. The proposed loan structure allows the City to receive a 3% annual return as well as payment back of the loan principle amount. These funds then become available to invest in other affordable housing projects. Most importantly, under the proposed transaction structure, the City retains ownership of the land.

Q5: Could there be a mechanism in the affordable housing ground lease that recoups future “windfall profits” of the entire project to be shared with the City for this project site, similar to “performance rent” in a structured commercial lease?

A. Such a provision has been included in the proposed Disposition and Development Agreement (DDA). The DDA states that in the event Borrower (Core) demonstrates to City’s reasonable satisfaction upon completion of construction that there have been material savings from the Construction Budget, Borrower shall be permitted to reduce general partner equity in an amount equal to fifty percent (50%) of such cost savings, and the remaining fifty percent (50%) shall be used to make payment of principal and interest on the City Loan. Extension of this concept to the ongoing operation of the project is inconsistent with established practices and the developer would likely require additional City subsidy to offset the resulting decrease in project performance. The entire project requires nearly \$50 million of private equity investment. Given the inherent risk of the market rate assumptions, that level of investment would not be possible if the City capped profits.

Q6: If there are any costs to adding a retail component to the project, couldn’t the City provide financial support and use some of the income generated by the Valley Fair parking lease (over \$250,000) and overall project savings to invest in public spaces or retail spaces.

A. There are three separate but related challenges to adding retail: cost, financing, and time. There is a cost associated with the addition of retail into the current plan as there is not currently significant flex or un-programmed space available to add a significant retail component. The costs of building the space and code-required parking would need to be funded by the City’s General Fund. All of the revenue generated through interim use of the property is deposited into the City’s Affordable Housing Fund. The Affordable Housing Fund must support affordable housing development and programs. To provide financial support for retail within the Agrihood project, the City would need to use General Fund dollars to subsidize retail on the site.

The inclusion of incremental retail onsite would cause a redesign of the project to accommodate appropriate space appropriate for retail (e.g., higher ceiling heights, service areas, utilities) and a CEQA re-evaluation to determine the potential impacts (e.g., traffic). Even if an additional subsidy were available, the project faces numerous time constraints from the State of California that would limit the ability for project redesign. As currently proposed, the project would significantly advance the City’s objective of developing affordable housing on the property, while also providing a significant amount of publicly accessible open space and place-making opportunities.

Q7: Understanding that affordable units require public subsidy (because projects have a negative value in terms of the profitability) what is the actual opportunity cost to produce an affordable housing unit?

A. The opportunity cost for an affordable housing unit is the current market value for each unit minus the affordable rent. The affordable rent is based on the level of area median income. For the affordable senior housing units in the Agrihood project, the projected rent is approximately \$1,500 below market rent, which translates to a \$360,000 cost per unit (based on a 30 year revenue model), or a total cost of \$60,000,000 for the 165 unit project.

The average AMI for the Senior Project is roughly 50% AMI. 2018 affordable rents are listed below. The opportunity cost is the assumed market value for each unit type minus the affordable rent.

	50%
Studios	1,163
1 Bd	1,330
2 Bd	1,496
3 Bd	1,662
4 Bd	1,796

Based on actual construction costs and depreciation of units, the cash flows are very tight, making it difficult to attract investment funding, and the project will likely have a negative cash flow at around 20 years. Public subsidy is required to offset these financial conditions.

The cost to build new units is coming in around \$550,000 to \$650,000 per unit.

- Q8: In most development discussions, the cost of land is one of the biggest factors (construction costs being the largest). Since the developer is paying nothing for the land (\$0), how does this play into the cost analysis?
- A. The developer is not paying \$0 for the land. The developer is paying \$15,700,000 for the two market rate parcels and the agrihood parcel. This amount will be lent back to the Senior Affordable Project so that there will be a return of principal + interest (3% per annum) to the City based on residual cash flow receipts. In total, the city will receive \$15,700,000 plus interest, the full build-out and operations of the Agrihood open space, 165 affordable units with supportive services, and retain long-term ownership of the affordable parcel.
- Q9: What actions did the City take to review the financial impact of this development? What determined the affordability levels and housing types provided?
- A. The City has reviewed the pro-formas with the Developer in great depth as highlighted by some of the responses noted above. The City and Developer examined a variety of housing types. The Affordable Project is composed of mostly smaller units borrowing from the micro-unit concept. In the end, costs and feasibility challenges led to a partnership with the County that ultimately determined the proposed AMIs. The County has also reviewed the project design and financial structure in making their determination to support the project.

Planning

- Q10: Please describe how the City sees the current proposal responding to the Project for Public Places (PPS) suggestions, and how it satisfies the place-making goals and activated ground levels.
- A. The active open space area was moved to the Winchester Blvd. frontage to provide an engaging entry to the project site. The project now includes multiple publicly accessible amenities (agricultural area, performance area, café/community buildings, community kitchen) in accordance with the PPS Power of 10 philosophy and consistent with the PPS recommendations for the site.

Q11: How has the request for 20,000 square feet of additional retail been addressed in the project?

- A. The project now includes multiple publicly accessible amenities (agricultural area, performance area, café/community buildings, community kitchen) in accordance with PPS' Power of 10 philosophy and consistent with the PPS recommendations for the site. The project was redesigned to incorporate "place-making" elements based on the recommendations of the City's consultant, Project for Public Spaces (PPS). Changes made to the project to support "place-making" activities include:
- Addition of a community kitchen
 - Addition of a café
 - Addition of electrical and hose bibs to allow adaptability for future uses in outdoor areas
 - Addition of a performance area within the open space

The City has worked with the Developer to ensure that the open space design incorporates the necessary fixtures to allow for adaptability of future uses in the outdoor areas. Specifically, the open space paseo that connects the site from Winchester Boulevard to Worthington Circle is envisioned as an area that can be curated as an active corridor for special events such as farmer's markets and pop-up retail, which are in line with the PPS recommendations for place-making. Full activation of this open space corridor would result in approximately 20,000 square feet of retail.

The current project design cannot realistically accommodate the traditional 20,000 square feet of "brick and mortar" retail without significant redesign, which would have detrimental cost and time impacts. The project faces significant cost and time constraints such that a significant redesign to address retail at this point in the process would potentially jeopardize the housing units. Direction to increase the amount of ground floor retail would increase construction costs so that the project require additional subsidy from the City. To be viable, the retail space would need to be designed to commercial standards (e.g., higher ceilings; service areas; utilities) and additional parking would also be needed necessitating additional changes to the project design and increases in construction costs.

While the addition of a small amount of retail would likely not require recirculation of the project's Environmental Impact Report (EIR), project redesign and financial restructuring would result in time delays to the project's implementation. The Developer would have to resubmit their County funding approval, which could take up to 6 months and jeopardize competitive housing vouchers. Time delays would also eliminate the possibility to meet the fall tax credit deadline and complicate the time constraints associated with the State reverter. The retail and amenity components of the project are intended primarily to serve the population that would already be on the site. Adding retail that would draw additional people to the site would trigger the need for further evaluation of potential traffic impacts. Ultimately, redesign would postpone the delivery of desperately needed affordable housing to a community in the midst of an affordable housing crisis.

Q12: Why did the City create the NOP in April 2017 with the parameters it had, specifically the 584 units and the 25,000 sq. ft. of commercial?

- A. Staff and CORE discussed the pending submittal and worked together to create a project description that would provide flexibility for the project design as the PPS process was just beginning. Ultimately, the CEQA analysis was based on what the Developer deemed feasible at the site.

Q13: Why didn't the City study the defined NOP parameters (584 units and the 25,000 sq. ft. of commercial) and study only the proposal?

- A. The City has been conducting the review of the project land use entitlements through the City's standard process and in accordance with the requirements of CEQA. CEQA requires that the EIR include an analysis of the project as proposed by the project proponent, which in this case is the developer.

Q14: How did the City inform the public about its decisions regarding the NOP measures?

- A. Information about the project design was maintained up to date on the City's website. Plans for the final design were posted on the City's website immediately after they were submitted to the City in early January 2018. Multiple email notifications were sent to the community, the developer conducted several stakeholder meetings prior to the circulation of the EIR. The City conducted a community meeting during circulation of the EIR at which community members expressed support for the project as programmed. The NOP as issued indicated a range of up to a potential maximum amount of density that could be studied in the EIR and the project analyzed in the EIR fell within the scope of what was disclosed within the NOP. Alternatively, if the scope had increased, a new NOP would have been issued.