TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER DEPARTMENT: PLANNING AND COMMUNITY ENVIRONMENT

DATE: JULY 19, 2004 CMR: 332:04

SUBJECT: OPPORTUNITY CENTER OF THE MID-PENINSULA PROJECT AT 33 ENCINA AVENUE: 1) APPROVAL OF LOAN AND REGULATORY AGREEMENTS BETWEEN THE CITY OF PALO ALTO AND THE OPPORTUNITY CENTER ASSOCIATES L. P. TO PROVIDE A LOAN OF $750,000 IN PERMANENT CITY FUNDING FOR THE APARTMENTS DEVELOPMENT; 2) APPROVAL OF A LOAN AND REGULATORY AGREEMENT BETWEEN THE CITY OF PALO AND THE COMMUNITY WORKING GROUP, INC. TO PROVIDE A LOAN OF $1,280,000 FOR THE SERVICE CENTER PART OF THE PROJECT; 3) APPROVAL OF A NEW ACTIVITY IN THE FY 2004-05 COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG) ANNUAL ACTION PLAN ALLOCATING OF UP TO $81,000 IN CDBG FUNDS FOR THE CITY’S COSTS OF RELOCATING HIGH VOLTAGE ELECTRIC LINES FROM THE PROJECT’S FRONTAGE

RECOMMENDATION
Staff recommends that the City Council:

1. Approve the attached loan and regulatory agreements between the City of Palo Alto and Opportunity Center Associates L. P., which provides a $750,000 loan from the Residential Housing Fund for housing construction and restricts the use and occupancy of the residential units.

2. Approve the attached loan and regulatory agreement between the City and the Community Working Group, Inc. (CWG), which provides a $1,280,000 loan of Community Development Block Grant (CDBG) Funds for Service Center development and restricts the use of the Service Center portion of the project.

3. Approve the attached forms of promissory notes and deeds of trust for each City loan.
4. Authorize the Mayor to execute the attached loan and regulatory agreements in substantially similar form as approved by the City Attorney.

5. Authorize the City Manager to consent to the modification of the City’s existing deed of trust securing the $1,280,000 interim City predevelopment funding agreement and loan to the Housing Authority of Santa Clara County and CWG, and to authorize the close of escrow for the funding of the City’s construction and permanent loans to Opportunity Center Associates L.P. and CWG, upon satisfaction of all City conditions to funding.

6. Authorize the City Manager, after approval as to form by the City Attorney, to review, approve and execute subordination agreements of the City’s deeds of trust securing each loan to the construction and permanent funding and to subordinate the City’s regulatory agreement on the apartments to the requirements of other lenders and funding entities as described herein.

7. Direct the City Manager to execute any other documents such as estoppel statements, escrow instructions and assignment agreements as required to close the escrows for both the construction and permanent project financing and to secure the City’s interests in the project.

8. Approve the addition of a new CDBG-funded project in the Annual Action Plan for FY 2004-05 providing up to $81,000 in funding, to be transferred from the CDBG Housing Fund, which was previously set aside for the Opportunity Center and other housing developments, for the costs of relocating high voltage electric lines from the Opportunity Center project site frontage.

**BACKGROUND**

The Opportunity Center of the Mid-Peninsula, to be constructed at 33 Encina Avenue, will provide 89 units of housing over a 6,700 square foot day use and service center serving homeless adults and families and other very low-income households who need affordable rents. Council approved Planned Community (PC) Ordinance 4782 in March 2003 permitting development of the project. All necessary financing for the $22 million development budget has now been secured. The project has broad support from public and private organizations with over $6 million raised by CWG from local foundations, businesses and individual donors. Of the private contributions raised by CWG, about $1.6 million will be used for development costs, about $2 million for interim funding for housing rent subsidies and about $2.5 to $3 million for an endowment for Service Center operating costs. Plans have recently been announced to continue the fundraising campaign with the goal of adding another $1 million to the Service Center endowment fund.

A ceremonial groundbreaking was held on May 5th; however the actual start of construction is planned for early August. Council approval of the attached final City loan
and regulatory agreements is a prerequisite to the start of construction. Council has previously committed $2,030,000 in funding to the Opportunity Center. $1,280,000 of City CDBG funds were loaned to the project sponsors for site acquisition and predevelopment costs under an interim funding and loan agreement approved by Council on July 22, 2002, with repayment due at the end of 2004, if construction is not underway under permanent City agreements. An additional $750,000 in Residential Housing Funds was committed to the project in March 2003 with Council adoption of Budget Amendment Ordinance Number 4780. The attached loan agreements would replace the interim agreement and provide a total of $2,030,000 in construction period and permanent City funding for the project, with the $1,280,000 in CDBG Funds allocated to CWG for the Services Center’s development costs and secured by the Service Center, and the $750,000 provided to the Opportunity Center Associates L. P. to be used for development of, and secured by, the 89-housing units.

**DISCUSSION**

**Occupancy and Rents for the Housing Units**: Rent levels, income limits and tenant household types will be controlled by the rules of the major government funding programs that are being used for development costs and by the project’s PC District zoning regulations. The sponsors secured an award of $7.5 million in State funding under the Supportive Housing component of the Multifamily Housing Program (MHP). The MHP program places the most stringent controls on the rent and occupancy of the housing, with all 88 affordable units required to be restricted to occupancy by very low-income households (one unit will be occupied by a resident manager and is not income restricted). 35 of the units will be available at rents affordable by persons on public assistance or earning very low wages. Section 8 rental assistance will be tied to 22 of the units under a 10-year contract from the Housing Authority. Due to federal rules for the Section 8 program, residents moving into these units must come from the Housing Authority’s waiting list. InnVision (the Service Center operator under contract to CWG) intends to work with its current shelter and drop-in center clients to assist its clients in getting on the Section 8 waiting list and in improving their qualifications for housing. Up to 50 percent of the units may be used for a transitional housing program under the City’s regulatory agreement. Transitional housing typically offers homeless households housing at almost no charge together with intensive services. CWG intends to seek funding for this type of program from HUD and from private sources. However, until sufficient funding is obtained, all 88 units will be operated as permanent housing. Table 1 below describes the different types of housing units, the eligibility restrictions and the maximum initial rents as required under the State’s rules for the MHP program and the City’s regulatory agreement.
## Table 1
**Opportunity Center Apartments – Unit Mix & Occupancy Restrictions**

**Initial Rents & Income Limits for 2004**

<table>
<thead>
<tr>
<th>Rent Formula&lt;sup&gt;1&lt;/sup&gt;</th>
<th>Tenant Restrictions</th>
<th>SRO</th>
<th>1 Bedroom</th>
<th>2 Bedrooms</th>
<th>Total Units &amp; (Total SH Units)&lt;sup&gt;4&lt;/sup&gt;</th>
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</thead>
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<tr>
<td>20% of AMI</td>
<td>Extremely low income</td>
<td>16 at $369</td>
<td>3 at $395</td>
<td>1 at $475</td>
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<td>$14,860 for 1</td>
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<tr>
<td>25% of AMI</td>
<td>[See Note 4 for the 32 SH Units]</td>
<td>11 at $461</td>
<td>3 at $494</td>
<td>1 at $593</td>
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<tr>
<td></td>
<td></td>
<td>$18,575 for 1</td>
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<tr>
<td>35% of AMI</td>
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<td>24 at $646</td>
<td>5 at $692</td>
<td>2 at $831</td>
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<tr>
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<td></td>
<td>$26,005 for 1</td>
<td>$29,715 for 2</td>
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<tr>
<td>Section 8 or 45% of AMI&lt;sup&gt;1&lt;/sup&gt;</td>
<td>Very low income</td>
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<td>$33,435 for 1</td>
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<td>---</td>
<td>1</td>
<td>----</td>
<td>1</td>
</tr>
</tbody>
</table>

**Total Units** | 70 | 13 | 6 | 89

**Table 1 Notes:**

1) AMI means the Area Median Income for Santa Clara County, which currently equals $105,500, as published in February 2004. Initial rents and income limits are as published by State HCD for 2004.

2) The SRO units will be limited to one-person occupancy. The income limits shown assume a two-person family in a one-bedroom unit and a three-person household in a two-bedroom unit.

3) The 22 very low-income units will rent for the HUD approved Section 8 Fair Market Rent (FMR) or, if Section 8 becomes unavailable, at rents based on 45% of AMI (the Section 8 rent is expected to be higher and is shown in the table). Section 8 tenants will pay only 30% of their income for rent. Section 8 tenants are likely to have extremely low incomes, but the maximum income under the Section 8 program is 50% of AMI.

4) SH Units are the 32 Restricted Units in the apartments designated in the MHP Regulatory Agreement as “Supportive Housing Units” which requires that these units be occupied by households that were homeless or at-risk of homelessness, and with at least one household member with a disability prior to occupying the unit. Supportive services are required to be provided to these tenants by the State’s MHP funding.
Regulatory Agreement Provisions on the Apartments and Subordination of City’s Agreement: At the construction loan closing, the City will be required to subordinate its regulatory agreement for the apartments to the tax exempt bond financing regulatory agreement and its related restrictions. Even after the bond-financed construction loan is paid off, these regulatory provisions will continue in effect for 55 years. The bond financing affordability restrictions are less restrictive than the rent and occupancy restrictions shown above that the State and the City will be placing on the project. The bond financing affordability restrictions require that 66 units (75 percent) be rented at affordable rents to very low-income households with incomes below 50 percent of median income and 22 units be affordable to low-income households with incomes below 60 percent of median. Additionally, for a 10-year period, the bond financing also requires the provision of training classes and emergency supportive services to the tenants of all 88 rent restricted units.

With the close of the permanent funding, the MHP and tax credit regulatory agreements will be recorded and the City will also be required to subordinate to those agreements and to the $7.5 million MHP deed of trust. The MHP regulatory agreement is the most restrictive; it will cover all of the units for 55-years, restrict rents and occupancy as summarized in Table 1, and require the provision of supportive services to tenants in 32 of the units. The City is requiring a 55-year regulatory agreement (the maximum term compatible with the provisions of the tax credit program rules), similar in content to the MHP restrictions, which will function as additional, back-up restrictions. In a side letter, both CWG and the Housing Authority will commit to extended 89-year affordability in the event either entity exercises its option to acquire limited partner’s ownership interest at the end of the 15-year tax credit compliance period. The City will also hold a back-up purchase option in the event that neither CWG nor the Housing Authority decides to take over the ownership. In addition, the site’s PC zone restricts all 88 units for occupancy by low and very low-income households at affordable rents. There will also be a 55 year regulatory agreement under the Low Income Housing Tax Credit program. This document is the least restrictive as it requires that just 40% of the units (36) be occupied by low-income households with incomes up to 60 percent of the median income at affordable rents. The HOME funds provided by both San Mateo and Santa Clara Counties place regulatory controls on 11 units for 55 years. As a practical matter, unless the project goes into a financial or regulatory default and foreclosure, the owners will be maintaining compliance with the most restrictive State MHP affordability requirements, together with any provisions of the other agreements that supplement the MHP provisions.
Ownership and Management: The CWG and the Housing Authority of Santa Clara County are the project’s joint sponsors and developers. However, the project will be owned by a limited partnership, named the Opportunity Center Associates L. P. (Partnership), that has been formed to facilitate the funding contributions of the tax credit limited partner. The limited partner investor is an affiliate of MMA Financial, LLC a major investor in tax credit housing projects. An estimated figure of approximately $7.3 million in tax credit equity is being used in the current budget projections.

Parcel Map for Lot Merger and Condominium Plan Recording: The site was assembled from three separate legal parcels known as 33, 39 and 45 Encina Avenue. The Director of Planning and Community Environment approved an application on February 5, 2004 to merge the three parcels into one single parcel to be known as 33 Encina Avenue. The project developers intend to record the parcel map and the condominium plan prior to the closing of the bond loan and the City’s new loans. Completing the parcel map process in advance will facilitate the very complex bond and construction loan closing. The City will be agreeing to modify its existing $1.28 million deed of trust, which is presently recorded against the 33 and 39 Encina Avenue parcels, to allow the lot merger and recording of the condominium plan to occur. The security for the modified City deed of trust will be the new, single parcel encompassing the entire site. The City Manager will need to execute escrow instructions and other legal instruments to authorize these transactions.

The buildings and improvements will be divided into three condominium units. The Partnership will own a unit consisting of the building shell, the four floors of housing, the two levels of underground parking, the front courtyard and portions of the ground floor that will be used for access to the housing and for housing-related services. Easements will be recorded to provide for use of the parking by the Service Center staff and visitors. CWG will own two units of the condominium, which will be composed of the single adult and family service centers located on the ground floor. Common areas will be owned in undivided fractional interests by the Partnership and CWG; recorded CC & R’s will address the maintenance responsibilities of the two owners.

Opportunity Center HDC, Inc. (HDC Inc.), the non-profit general partner of the Partnership, will control and manage the housing portion of the project. HDC Inc. has a five member board of directors composed of three members appointed by the Housing Authority, one member representing CWG and the fifth member appointed by InnVision. CWG, through its own Board of Directors, will have control and overall responsibility for the management of the Service Center. InnVision will operate the Service Center space under a contract with the Partnership and CWG. That agreement will obligate InnVision to provide and contract with other service providers to offer on-site a broad array of
social services to meet the needs of both the area’s homeless and the residents of the Opportunity Center apartments. A half-time service coordinator, funded by the housing portion of the project but employed by InnVision, will be assigned to working with the formerly homeless residents of the 32 supportive housing units. InnVision’s service programs will also assist mid-peninsula households that are threatened with loss of their housing due to financial problems or other emergencies.

**Service Center Programs:** Services will be provided in two separate physical areas of the ground floor. All of the services presently provided at the InnVision / Urban Ministry drop-in center located behind the Red Cross will be moved to the Opportunity Center and expanded into a full day program. The new day center, focusing on single adults, will be open to the public on a drop-in basis; it will offer personal hygiene facilities, lockers, a message center, hot breakfasts, snacks, a clothes closet, and information and referral. More intensive services such as case management, job skills training, screening and referral for medical, mental health and substance abuse problems and money management will also be available to those seeking to stabilize their lives and move into housing. The Elsa Segovia Center, now located at the Clara Mateo shelter at the Menlo Park Veteran’s Administration hospital, will relocate and operate a family and children’s center in a separate wing of the ground floor. Services for families will be similar to those offered for single adults, but will emphasize the special needs of homeless women and children.

Both service programs will offer guidance and counseling to currently homeless clients who are serious about securing housing to help these clients improve their chances of being able to meet a rental property owner’s application and screening requirements, including the requirements for residency in the Opportunity Center’s apartments. Clients will be offered assistance in documenting income, resolving credit problems and guidance through the rental housing application process. There will also be assistance in accessing the Section 8 program waiting list, so that clients have an opportunity to move into the 22 Section 8 assisted units in the project.

The State and federal funding programs being used for a major portion of the development costs require that the Partnership develop and implement a written affirmative marketing program to rent the apartments in the project. This affirmative marketing program must be reviewed and approved by both the State and HUD and follow their guidelines and standards. Together with the extensive funding from the two counties, this means that there will not be any specific allocations or preference for occupancy of the 89 housing units for Palo Alto residents, employees or homeless clients of agencies providing services in Palo Alto or at the center. However, the marketing
program will include extensive outreach to the local homeless population and to clients of local service agencies.

**Funding for Relocation of High Voltage Electric Lines:** During the final plan check reviews, it was determined that there are high voltage electrical lines located above the standard low voltage lines on the poles in the public right of way along the Encina frontage of the site. The City had required as a standard project condition that electrical lines be placed underground and the developer had included funds in the construction budget for that work. However, it is unsafe to underground high voltage lines and, if left in their present location, they will be a serious safety hazard during construction and occupancy. The tall construction equipment needed to build the structures would be hazardous to use near the lines and, once the project is completed, the Fire Department must be able to use its hook and ladder trucks to access the upper floors in an emergency. City Utilities staff analyzed several options and related costs and concluded that relocating both the high voltage and distribution lines to the southern side of Encina is the most cost-effective solution with an estimated budget of about $200,000. Requiring the developer to bear the entire cost of this work would be a significant impact on the project’s budget because the budget includes only a total of $100,000 for all electrical utility and joint trench work. Therefore, staff proposes that the costs be shared, with some new funding from an additional allocation of CDBG funds, some from the Electric Fund and the remainder from the developer.

Staff requests Council approval at this time for a new project within the previously adopted CDBG program for FY 2004-2005 to cover most of the costs of the high voltage electrical work through a transfer of up to $81,000 (about 40 percent of the $200,000 total costs) from the FY 2004-05 CDBG Housing Fund to the Electric Fund. This additional CDBG funding will not be provided to the Partnership or CWG and is not included in the City’s loans for the project; these funds will be expended directly by the City and will not be repaid by the developer. The Electric Fund will pay twenty-five percent of total costs (estimated at $45,000 to $50,000) from its capital improvement budget for FY 2004-05, similar to normal contributions made by the City for undergrounding programs. City utility workers will carry out the electrical work for the high voltage line relocation and an outside contractor will complete the rest of the work. The developer will reimburse the City for the remaining costs (estimated at $70,000) from the project’s construction budget. The developer will still be responsible for the installation cost of underground electrical distribution lines across Encina to the project site and for the typical joint trench work and utility service connections on-site. The Electrical Engineering section of the Utility Department is preparing the plans and will manage the construction work. Work needs to proceed immediately to avoid delays in the Opportunity Center’s construction schedule.
RESOURCE IMPACT
The Opportunity Center will be financed with a complex mix of public and private sources from federal, State and local levels. Securing the development and operating funding for the Opportunity Center was an extremely difficult challenge for the Housing Authority and CWG. Due to the very low rents, the project will not be able to make payments on a permanent, long-term mortgage, so all funding, other than the bond-financed construction loan, had to be in the form of donations, grants, or long-term, deferred loans with flexible interest and payment terms. $22 million in permanent development funds had to be raised, plus funds for an operating reserve for the housing and an endowment for the Service Center. In addition, almost $11 million in loans are necessary for the construction period. Ten different entities are participating in funding the Opportunity Center together with numerous individual, business and faith-based donors. The major sources of permanent funding include the State’s Supportive Housing component of its Multifamily Housing Program (MHP) at $7.5 million; over $7.3 million from the sale of the four percent Low Income Housing Tax Credits to a private investor; $2.5 million from the Santa Clara County Office of Affordable Housing; and the City’s $2.03 million. Other key funding contributors include the Housing Authority for $9.75 million in construction financing and 22 units of project-based Section 8 assistance; Union Bank as the bond purchaser and trustee (see below); $3.6 million in private foundation grants and individual donations raised by CWG for capital costs including a $2 million operating reserve fund for the housing; and an additional $1.35 million from the Housing Trust of Santa Clara County, HUD and the County of San Mateo.

Summary of Construction Period Financing: The principal source of construction period financing will be a $9.975 million construction loan funded by tax-exempt, variable interest rate bonds issued by the Housing Authority and privately placed with Union Bank. This structure provides a very cost effective source of construction debt with the estimated interest rate at three and one-half percent over the 24-month construction and rent-up period and bond issuance costs at about $200,000. The City does not assume any financial obligation or risk in connection with the bond issuance. The Housing Authority, in its role as the bond issuer, will bear all such risks and a default by the borrower would not affect the City’s credit or bond rating.

The $9.1 million in remaining funds needed to complete construction is composed of $5.88 million in public funding from the two counties, the City, HUD and from the County Housing Trust, plus about $2.66 million in loans and $500,000 in equity from CWG, as shown in the table below. During the construction period, a first lien deed of trust for $9.975 million will be recorded against the property in favor of the Union Bank as the bond trustee. The City must subordinate its $2.03 million in loans to this
construction loan. All the local public lenders funding (including the City’s) and the 
CWG funds are at-risk should there be a default or serious problems during construction 
and rent-up. The $7.5 million permanent loan from State HCD and most of the $7.3 
million from the tax credit investor come into the project after construction is complete 
and full, stabilized occupancy of the housing units has been achieved and verified by 
audit to be in full compliance with the State and the tax credit program rules.

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<th>Source</th>
<th>Housing</th>
<th>Service Center</th>
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<td>- HOME Funds</td>
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<td>TOTAL ALL SOURCES</td>
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<td>$19,133,422</td>
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Permanent Financing Summary: After completion and full occupancy, the State’s $7.5 
million loan and about five million dollars of the tax credit investor’s funds will close 
escrow, pay off the smaller ($713,494) CWG construction loan, the $9.975 million bond-
financed construction loan and fund the developer fee. The permanent financing, for 
both the housing and Service Center components, is shown in Attachment E, with the 
order of priority of each party’s deeds of trust. The City’s $750,000 housing loan, and 
the other government loans, will remain in place after the permanent funding comes in, 
but will be subordinated to the new first deed of trust that secures the State MHP funding.

Description of City Funding for the Project: The Opportunity Center’s financing has been 
restructured due to welcome, but unanticipated, successes in winning higher funding than
was previously estimated last July when Council approved the interim City loan agreement. The major changes are substantial increases in the State HCD award and the tax credit investor’s contribution, and a $2 million award from the County of Santa Clara’s Affordable Housing Program. In addition, due to CWG’s successful capital and endowment campaigns, there is now sufficient private funding to fully finish the interior of the Service Center, establish a well-capitalized operating reserve fund for the housing and setup a $2.5 to $3 million endowment for the operating costs of the Service Center. The principal objective of restructuring some of the local public funding was to transfer some of CWG’s private funding that had previously been allocated to Service Center development costs to the housing side of the project to fully fund the establishment of an operating rent reserve fund for the apartments. To accomplish this objective, over $2 million had to be identified in funding that was eligible for use for Service Center development costs. The solution suggested by the developer, and concurred in by City and County staff, was to utilize a combination of $1 million of the Santa Clara County funds together with the City’s $1.28 million of CDBG funds to replace some of CWG funds previously allocated to the Service Center.

Although the City’s $1.28 million interim loan has already been expended for land acquisition and predevelopment, these funds will now be allocated in the final project development budget for Service Center development costs as shown in Attachment E-2. Staff supported this revision because development of a homeless service center is an eligible use under the CDBG regulations and the City’s CDBG funds will still indirectly assist the 89 housing units by freeing some of the private CWG funds to establish the housing’s operating reserve fund, a use that would be ineligible under CDBG regulations.

**City Loan for the Housing:** Palo Alto’s commitment of $750,000 in Residential Housing Funds will continue to be used as originally intended for housing unit construction costs. While the $750,000 for the housing is being provided as an interest-bearing loan, repayment over the 55 years that the project is under the MHP program’s restrictions is expected to be minimal. This is due to the extremely low rents and the high operating costs of service-enriched housing serving primarily persons that have experienced homelessness, have disabilities or extremely low incomes. Also, any residual receipts available for loan repayments must be split proportionately between the City and the two counties that also are providing loans. The provisions of the City’s loan are described below:

The terms of the City’s $750,000 housing loan are:

- 55-year loan term
- Outstanding balance due at the end of the 55-year term
- Maximum annual interest of three percent, not compounded

City Loan for the Housing: Palo Alto’s commitment of $750,000 in Residential Housing Funds will continue to be used as originally intended for housing unit construction costs. While the $750,000 for the housing is being provided as an interest-bearing loan, repayment over the 55 years that the project is under the MHP program’s restrictions is expected to be minimal. This is due to the extremely low rents and the high operating costs of service-enriched housing serving primarily persons that have experienced homelessness, have disabilities or extremely low incomes. Also, any residual receipts available for loan repayments must be split proportionately between the City and the two counties that also are providing loans. The provisions of the City’s loan are described below:

The terms of the City’s $750,000 housing loan are:

- 55-year loan term
- Outstanding balance due at the end of the 55-year term
- Maximum annual interest of three percent, not compounded
- Actual interest rate will be calculated annually ranging from zero to three percent based on the audited surplus cash flow from operations that is available to pay interest
- Unpaid interest does not accumulate from year to year
- Annual payments required only to the extent of residual receipts
- Residual receipts for the payment of interest and principal, if any are available, are divided among the lenders proportionately to each lender’s share of the total project debt
- City’s loan will be recorded in fourth position behind a total of $9 million in State and Santa Clara County loans.

City Funding for the Service Center: The City’s $1.28 million in CDBG funding for the Service Center will be secured with a deed of trust that will enforce an 89 year City regulatory agreement on the future use of the Center. The City deed of trust will be recorded against CWG’s condominium ownership interest in the project, but will be subordinated to Santa Clara County’s deed of trust securing its $1 million in Center funding because the County is providing more total funding for the entire project ($2.50 million), than the City ($2.03 million). No repayment of the City’s $1.28 million will be required, provided that compliance with the City’s regulatory agreement is maintained. After 89 years of compliance with the regulatory agreement, the City’s loan would convert to a grant and its deed of trust would be reconveyed.

The City’s regulatory agreement requires that the Service Center space be used as a facility for the delivery of services for homeless adults and families with children as eligible under the CDBG program and as described in the site’s PC zoning ordinance. Should the use be discontinued completely, substantially modified, or CWG’s ownership interest sold or transferred without the prior consent of the City, then the City’s funding would be subject to repayment, unless Council acted to waive the payment or amend the agreement. Council consent to a sale or transfer, or an amendment of the agreement to allow a change in use, would need to be consistent with the then-current CDBG regulations and the PC zoning for the site, which restricts the use of the ground floor to the provision of services such as counseling, training, childcare, and personal hygiene, primarily for lower income persons.

The formula for calculating the repayment amount of the City’s CDBG loan is prescribed in the CDBG regulations on the funding of real property. The repayment amount would be the then-current fair market value of CWG’s combined ownership interests in the Service Center structure, the land and easement rights for access and parking, times the proportionate share that the City’s CDBG funds represent of the total original funding for CWG’s ownership interest. Based on the current project budget and planned CWG
contribution to the Center’s costs, the City’s CDBG funding represents 45.8% of the total $2,793,707 in funding. The final percentage shares for each funding source for the Center will be calculated after completion of a post-construction cost audit.

**Capitalized Operating Reserve Fund for Housing:** The larger $1.9 million CWG construction loan will initially capitalize an operating reserve for the housing project. Over the first five years of the housing project’s operations, the final payments from the tax credit investor will gradually replace CWG funds and repay its loan, then freeing up these CWG funds to supplement the Service Center endowment. Under the City’s regulatory agreements with CWG and the Partnership each entity has formally committed to funding the operating reserve with the full $1.9 million and to utilizing the reserve on an ongoing basis to fund any operating deficits of the apartments. Establishing this reserve is a condition of the State MHP permanent loan, the tax credit investor’s funds and the City because the project is likely to operate at a deficit without these subsidies. The Operating Reserve will be held in a separate, dedicated account, under CWG name and administered by the Partnership. The earnings, and principal if needed, will be used only for the purpose of supplementing the annual rental revenue from the 89 housing units to the level necessary to meet all regular operating costs plus the salary of the part-time services coordinator, the required payments on the State loan and the annual deposits to replacement reserves and to pay the general partner a partnership management fee.

The cash flow projections for the project indicate that it will require regular annual payments from the Operating Reserve, beginning with about $45,000 for the first year after completion and continuing to increase as time goes on. These projections are somewhat conservative and are based on assumptions that rents increase more slowly than operating costs, that overall vacancy and collection losses run about five percent of rents, and that rent revenues fully fund the housing service coordinator staff position. To augment the CWG Operating Reserve fund, any development cost savings (such as unused contingency funds), up to $500,000, will be deposited into a companion Operating Reserve fund held by the Partnership, to be drawn upon before the CWG-held reserve funds are utilized.

**Operating Costs of the Service Center and CWG Endowment Funds:** CWG preliminary estimates of basic operating costs range from $40,000 to $75,000 per year for utilities, insurance, custodial, repairs and landscaping. By covering these regular ongoing operating costs from the endowment’s earnings, CWG expects to offer service providers space within the Center without the providers having to pay rent. Presently, CWG has raised sufficient funding for an initial endowment fund of $2.5 to $3 million, depending upon the final costs for equipment and furnishing of the interior. At this size, the
endowment will generate about $100,000 to $120,000 annually in investment earnings. A campaign for a final one million addition to the fund is underway.

CWG’s priorities for the endowment’s earnings, with the most emphasis on the first two priorities, are: 1) operating expenses of the Center, 2) rent subsidies for persons with little or no income, 3) start-up costs for special program support services, and 4) other discretionary Service Center costs. CWG does not envision becoming an ongoing source of financial support for the operating budgets of the service providers utilizing space within the Center; these agencies will be expected to have sufficient resources of their own to run their programs. However, CWG would partner with these agencies, when appropriate, to assist them in accessing funding to implement or expand their programs.

**POLICY IMPLICATIONS**
The actions recommended in this report implement previous Council actions supporting the project, appropriating the housing funding and furthering the Council’s “Top Five” priority for the development of affordable housing. These actions also implement the priorities of the City’s HUD Consolidated Plan for 2000 – 2005 for projects serving the needs of homeless and extremely low income households.

**TIMELINE**
Below is an updated list of key past and future milestones in the project schedule.

- Project conceived & CWG founded \(1998-99\)
- 33 & 39 Encina purchased with foundation grants \(1999\)
- Project expanded to include housing over a Service Center \(2000\)
- Housing Authority joins the development team \(2001\)
- Plans revised to include 45 Encina and provide 89-units \(2002\)
- Council approves $1.28 million in interim CDBG loan \(July 2002\)
- Control of entire site including 45 Encina achieved \(August 2002\)
- Planned Community zone adopted by Council and $750,000 in additional City housing funds approved \(March 3, 2003\)
- State approves $7.5 million in MHP funding \(December 2003\)
- State approves tax-exempt bond allocation and tax credits \(March – April 2004\)
- City Council action on final financing agreements \(July 19, 2004\)
- Building permit ready to issue \(Late July 2004\)
- Planned closing of construction funding and bond issuance \(July 22, 2004\)
- Legal deadline to issue bonds \(August 9, 2004\)
- Project under construction – 18 months \(August 2004 – January 2005\)
- Complete Rent-up; Occupancy of Service Center \(March 2006\)
- Finalize permanent loans; Pay-off construction loans \(April 2006\)
ENVIRONMENTAL REVIEW
A federal environmental review under the National Environmental Policy Act (NEPA) covering the use of CDBG funds for the project was completed and approved by HUD on July 22, 2002. On March 3, 2003, the Council certified the Final Environmental Impact Report (FEIR) pursuant to the California Environmental Quality Act (CEQA) and approved the Planned Community zone change on the project. The Budget Amendment Ordinance appropriating the City’s $750,000 in Residential Housing Funds was also adopted on that date.

ATTACHMENTS
A) Loan Agreement For Opportunity Center Apartments with attached form of Note and Deed of Trust
B) Regulatory Agreement and Declaration of Restrictive Covenants for Opportunity Center Apartments
C) Loan and Regulatory Agreement and Declaration of Restrictive Covenants for Opportunity Center of the Mid-peninsula – A Service Center with attached form of Note and Deed of Trust
D) Summary Development Budget
E) Permanent Funding Sources & Terms for Residential & Service Center Portions of Project

PREPARED BY: ________________________________
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Assistant City Manager

cc: Community Working Group, Inc.
    Housing Authority of the County of Santa Clara