



City of Palo Alto

City Council Staff Report

(ID # 10928)

Report Type: Consent Calendar

Meeting Date: 1/13/2020

Summary Title: Approve Additional City Funds for Wilton Court

Title: Authorize and Approve an Additional \$10.5 Million Loan From the Housing In Lieu and Impact Fee Funds for a Total City Contribution of \$20.5 Million for the Development of the 100 Percent Affordable Housing Project at 3705 El Camino Real (Wilton Court); and Approve Budget Amendments in the Residential Housing In-Lieu Fund, the Commercial Housing Fund, and the Residential Impact Fee Funds

From: City Manager

Lead Department: Planning and Development Services

Recommendation

Staff recommends that the City Council approve an additional \$10,518,971 million loan to Palo Alto Housing Corporation for the development of an 100% affordable housing project at 3705 El Camino Real (Wilton Court), for a total contribution from the City of \$20.5 million. Staff recommends realizing the contribution by:

- 1) Reallocating existing funding reserved for the Potential Teacher Housing Project at 231 Grant Ave in the amount of \$2,638,993 and replenishing this amount with additional fee revenues as they become available.
- 2) Establishing the Residential Impact Fund (Fund 293) for the collection and accounting of residential impact fees established in FY2017.
- 3) Amending the Fiscal Year 2020 Budget Appropriation Ordinance for:
 - a. The Residential Housing In-Lieu Fund by:
 - i. Increasing Grants and Subsidies in the amount of \$7,249,601; and
 - ii. Decreasing the Ending Fund Balance in the amount of \$7,249,601;
 - b. The Commercial Housing In-Lieu Fund by:
 - i. Increasing Grants and Subsidies in the amount of \$2,669,330; and
 - ii. Decreasing the Ending Fund Balance in the amount of \$2,669,330;
 - c. The Residential Housing Impact Fund by:
 - i. Increasing Residential Housing Impact Fees in the amount of \$600,040
 - ii. Increasing Grants and Subsidies in the amount of \$600,040

- 4) Authorizing the City Manager or designee to negotiate and execute a Loan Agreement, Regulatory Agreement, and related documents necessary to implement Council direction.

Executive Summary

On January 14, 2019, the City Council unanimously approved Palo Alto Housing (PAH) proposal to construct 59 units of affordable rental housing units, of which one unit would be exempt for an on-site manager's unit ([CMR 9917](#)).¹ Rents for the 58 restricted units would be affordable to those with incomes between 30% and 60% of Area Median Income (AMI). As of May 2019, for a family of two earning 60% AMI, the household's income cannot exceed \$70,260. Of the total 59 units, 21 of the units are reserved for adults with developmental disabilities. Given the deep affordability of the project, PAH is requesting financial assistance from local, State, and Federal governments. Local contributions to date include \$10 million from the City of Palo Alto's Residential Housing and Commercial In-Lieu funds, which was unanimously approved by Council on June 3, 2019 ([CMR 10143](#)).² The City also agreed to allow PAH to use \$2.6 million in reserve funds that were no longer needed for Section 8 housing at the Sheridan apartments to apply toward the Wilton Court project.

Palo Alto Housing applied for Intellectual and Developmental Disabilities Housing Funds for the 21 units reserved for adults with developmental disabilities in the amount of \$4 million. Since then, the County awarded the project \$2.8 million, short by \$1.2 million of what the project expected. In addition, a \$10 million contribution that was projected from a State competitive grant was also unsuccessful.

The cost to develop the Wilton Court project was previously estimated to be \$46,127,456. Development costs have increased by \$168,971 for a total projected cost of \$46,296,427. To close this funding gap, Palo Alto Housing is requesting an additional \$10.5 million in City funds to construct the 100% affordable housing project. This City's contribution at this time will narrow the gap and allow Palo Alto Housing to apply for additional state grants.

Background

In April 2018, the City Council created the Affordable Housing Combining District (AHCD) ([CMR 8966](#)) which enabled 100% affordable, multi-family housing projects located within half-mile of major transit stops or quarter-mile from a transit corridor to utilize the relaxed development standards.³ On January 14, 2019, the City Council approved PAH's application to combine parcels, 3703-3705 and 3703-3709 El Camino Real, zone changes to apply the Affordable Housing Combining District to the site, and a waiver from the retail preservation requirement ([CMR 9917](#)).

¹ <https://www.cityofpaloalto.org/civicax/filebank/documents/68435>

² <https://www.cityofpaloalto.org/civicax/filebank/documents/71434>

³ <https://www.cityofpaloalto.org/civicax/filebank/documents/64347>

The maximum rent for each household will be based on 30% of the household’s income, not to exceed 60% AMI of California Tax Credit Allocation Committee’s income limits. For a household of two in a 1-bedroom unit at 60% AMI, the maximum household income as of May 2019, would be \$70,260. Given the project will be subject to tax credit rent limits, the rent will not exceed 30% of income or \$1,647. PAH proposed rents comply with affordability requirements as shown below in Table 1 and in detail in Attachment A. The mix of unit types and expected rents is shown in Table 1 below. Given the mission of PAH to provide affordable housing rentals, the project relies entirely on public funds to be developed. One major funding source that will help the construction of the project is the federal Low-Income Housing Tax Credit (LIHTC) administered by the California Tax Credit Allocation Committee (CTCAC).

Table 1: Unit Mix and Rent for Wilton Court Apartments

| Affordability | Household Size | Number of Units | Type | Rental Amount with Utility Allowance |
|----------------------|-----------------------|------------------------|-------------|---|
| 30% AMI | 1 | 14 | Studio | \$659 |
| 50% AMI | 1 | 19 | Studio | \$1,124 |
| 60% AMI | 1 | 23 | Studio | \$1,357 |
| 60% AMI | 2 | 2 | 1 bedroom | \$1,442 |
| Exempt | 2 | 1 | 1 bedroom | Exempt |
| Total | | 59 | | |

On June 3, 2019, the City Council approved a \$10 million contribution from the City’s Affordable Housing Funds in the form of an affordable housing loan for development and construction of the project ([CMR 10143](#)).

Discussion

PAH is seeking an additional \$10.5 million funding from the City, for a total contribution of \$20.5 million, to bridge the funding gap resulting from the unsuccessful bid for a competitive state housing grant and unanticipated increases in construction costs.

According to the applicant’s most recent estimates, the project will cost approximately \$46,296,427 to be developed. Attachment B is the project’s development proposed financing, which lays out the updated uses, sources, and the total gap financing needed for the project. The table below assumes that \$16,646,642 in tax credits will be awarded to the project.

Permanent Sources of Funds for Construction

| | | |
|--|----|------------|
| City of Palo Alto | \$ | 20,518,971 |
| Low Income Housing Tax Credits | \$ | 16,646,642 |
| County of Santa Clara – Developmental Disabled Funding | \$ | 2,800,000 |
| Permanent Construction Loan | \$ | 2,480,814 |

| | | |
|---|-----------|-------------------|
| Sheridan Affordability Reserve Account ⁴ | \$ | 2,350,000 |
| State of California Enhanced Tax Credit | \$ | 1,500,000 |
| TOTAL PROJECT FUNDING | \$ | 46,296,427 |
| TOTAL COST PER UNIT: | \$ | 784,685 |
| <u>City's Contribution</u> | | |
| Commercial and Residential Funds (Commercial \$11.7M) (Residential In-lieu \$7.7M*) (Residential Impact \$0.6M) | \$ | 20,518,971 |
| <small>*\$2.6M of \$7.7M is allocated from money presently reserved for a Potential Teacher Housing Project. The Teacher Housing Project reserve is expected to be restored by the end of the first quarter 2020 due to an anticipated contribution to the housing fund from the Maybell Project.</small> | | |
| TOTAL CITY FUNDING PER UNIT | \$ | 347,779 |

The following is a revised estimate of the project's funding timeline:

| | |
|---------------------------|------------------|
| City's Funding Commitment | January 2020 |
| Apply for State Funds | Fall/Winter |
| Start Construction | Summer 2020 |
| Completion of project | Winter 2021/2022 |

Loan Agreement and related documentation

The City's contribution will take the form of an affordable housing loan, which will be supported by a Promissory Note and Deed of Trust secured by the property. In addition, the parties will execute a Regulatory Agreement ensuring the continued affordability of the rental units once they are developed. The parties were in the midst of negotiating the terms of these documents when the need for additional funding arose and have delayed finalizing these documents pending the City Council's decision. Consistent with prior affordable housing loans, staff anticipates that the Note will bear simple interest at 3% per annum and payments will be made from any residual receipts beyond the project's net operating income expenses. Payments will be divided among funding agencies with the City receiving its proportionate share based on its funding to total development costs. No interest will accrue, and no payments will be required until after the project is constructed and occupied.

⁴ Council passed CMR 8105 that amended the Promissory Note Amendment No. 1, to Amendment No. 2, which revised the use of the Affordability Reserve Account (ARA). The revision enabled PAHC to use ARA funds on new construction or rehabilitation of affordable housing by 2030. Details of the Sheridan ARA are included in the [Informational Report dated June 3, 2019](#)

Additionally, the loan agreement will include language that will reduce the City's loan contribution if PAH finds additional funding sources to help fund the project.

Policy Implications

The actions recommended in this report implements the City's adopted 2015-2023 Housing Element policies and programs supporting the development of low-income housing, which are set forth in detail in CMR 10143.

Resource Impact

The City has approximately \$4.6 million in the Residential Housing In-Lieu Fund; approximately \$2.7 million in the Commercial Housing Fund (\$1.7M of which is permitted by the Stanford University Medical Center Development Agreement); and approximately \$0.6 million in the Residential Housing Impact Fund once Fund 293 is established for the collection and accounting of residential impact fees established in FY2017. If the loan is approved by City Council, staff will amend the budget to allocate \$4.6 million from the Residential Fund, \$2.7 million from the Commercial Fund, \$0.6 million from the Residential Housing Impact Fees Fund. Additionally, staff will reallocate existing funds in the amount of \$2.6M from the \$3.0M set aside for the Potential Teacher Housing Project at 231 Grant Avenue ([CMR 9371](#)) to fund the 3705 El Camino Real (Wilton Court) Project; this amount will be replenished with fee revenues as they become available. One potential source of the additional fee revenues is the \$4.7 million the City is expecting from the 567 Maybell project (Resolution 9794). The recommended budget amendments with the appropriation of the \$10.5 million in additional funding requires an supermajority, or 2/3 vote approval by the City Council in accordance with the City's Charter and Municipal Code.

If approved, the project will receive \$20.5 million from the City. Sources of the funds include the City's Commercial Housing Fund (\$11.7 million), Residential Housing In- Lieu Fund (\$8.2 million) and Residential Housing Impact Fees Fund (\$0.6M). The remaining balances of the Commercial Housing Fund, Residential In-Lieu Fund and the Residential Impact Fees Fund will be \$0.

Timeline

Staff will work with PAH to execute loan documents and release funds, if approved by City Council.

Environmental Review

Review and submittal of the attached report and the approval of the loan and related financing regulatory documents are exempt from the California Environmental Quality Act (CEQA). The affordable housing project itself is exempt from the CEQA per CEQA Guidelines Section 15194 (Affordable Housing).

Attachments:

- Attachment A: December 2019 Update on Wilton Court
- Attachment B: Sources and Uses of Funds for Wilton Court Update

December 2019 Update on Wilton Court

We are requesting the City's assistance with our current funding gap for Wilton Court, a 59 unit 100% affordable housing project. After receiving County funds and identifying State funding that is available and for which we will be competitive, our gap remains \$10,350,000. Since the project was entitled in January 2019, we have been investigating/exploring various State funding programs to help close this gap. Due to the housing shortage and the strong demand for more affordable housing, these funding sources are oversubscribed by two and three times. So, in order to even be considered, each proposed affordable housing development project must meet a hundred percent of the criteria within the applicable notices of funding.

Earlier this year, our original strategy was to apply for State funding through the Housing and Community Development Department's MHP program for \$10 million. MHP program funding was replenished in the 2018 election after being dormant for seven years. However, based on the projected results from MHP's first round of funding this fall, the number of competitively scoring projects significantly outstripped the available funding. Unfortunately, a Wilton Court would not likely receive enough of a competitive score under the MHP program so this is no longer considered a viable source of funding.

We have also investigated applying for a State IIG (Infill Infrastructure Grant) which could potentially be eligible for use to pay for approximately half of Wilton Court's \$4.5 million, 41 space, underground parking garage. However, primarily due to the building's lack of proximity to public transit with enough service frequency, Wilton Court will not be competitive for the grant.

In 2016, Santa Clara County set aside \$10 million of Measure A funding to help underwrite affordable housing for adults with developmental disabilities. We applied for the maximum allowed eligible amount of \$4 million which could underwrite the 21 units that will set aside for this population. The County approved Wilton Court for \$2.8 million.

With a commitment from the City to fill the projected gap, we have identified one State funding source that Wilton Court could potentially be competitive to receive, thereby leveraging the City's additional gap funding commitment. In January 2020, we intend to apply to TCAC for "enhanced" tax credits which could bring in an additional \$1.5 million. Enhanced tax credits are a new funding source from the State to help fund "shovel ready" projects (projects that will be able to break ground in 180 days).

Along with the challenges of being a competitive financing source, the requirement to break ground within 180 days of funding approval (for a successful Wilton Court application, this would be September 2020) is challenging. However, our architect's construction drawings will be submitted for building permits in Spring 2020. We will also receive a concurrent confirmation of construction cost estimates pricing as an update to the estimates we have received in 2019. Thus, with the City's financial assistance and efficient building permit approval process after our building, we believe that Wilton Court could be under construction in Fall 2020.

Finally, as we have discussed with City staff, PAHC remains committed to following through on other leads for potential funding sources, including Silicon Valley corporate philanthropy, a loan from the Federal Home Loan Bank, and other viable sources. While these sources of funding would not be available in time in order to leverage the enhanced tax credits, all future successful financing received by Wilton Court that is not needed to pay for development project costs would be used to directly pay-down the City's additional gap loan committed to Wilton Court.

DEVELOPMENT COSTS

| | |
|--------------------------------|-------------------|
| ACQUISITION | |
| Total Acquisition Costs | 4,450,689 |
| HARD COSTS | |
| Total Hard Costs | 33,131,108 |
| SOFT COSTS | |
| Total Soft Costs | 8,714,630 |
| TOTAL DEVELOPMENT COSTS | 46,296,427 |

PERMANENT FUNDING SOURCES

| | |
|---|-------------------|
| Permanent Loan - A Tranche | 2,480,814 |
| Tax Credit Investor Proceeds | 16,646,642 |
| State of CA Enhanced Tax Credits - to be secured Spring 2020 | 1,500,000 |
| City of Palo Alto - secured Spring 2019 | 10,000,000 |
| City of Palo Alto - Sheridan Funds Repurposing | 2,350,000 |
| County 2019 Funding for Developmentally Disabled | 2,800,000 |
| Gap Sources - City of Palo Alto Additional Funds/Grant Funding | 10,518,971 |
| TOTAL DEVELOPMENT SOURCES | 46,296,427 |

DEVELOPMENT SCHEDULE

2019

- April Submit Application for City of Palo Alto funding
- Summer Submit Application for Santa Clara County
- Summer Design Development Drawings
- Winter Construction Drawings

NOTE: All below steps/dates are contingent upon securing CA State Tax Credits funding and filling entire remaining funding gap.

2020

- January Submit Applications for TCAC and CDLAC
- Spring Submit for Building Permits
- Summer/Fall Obtain Building Permit
- September Close all Construction Financing
- September Commence Construction

- Summer 2022** Complete Construction/Tenants Move-in