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REPORT TO COUNCIL/SUCCESSOR AGENCY

SUBJECT

Direction on Article 6 of the 2010 Amended Disposition and Development and Owner Participation Agreement (ADDOPA) for Transfer of the Sunnyvale Town Center Property

BACKGROUND

In August 2015, Wells Fargo Bank (REDUS SVTC, LLC), the current property owner of the Town Center property, solicited proposals for sale or transfer of the property (Attachment 1). The Town Center property consists of an approximately 20-acre area bounded by Mathilda, Washington, Sunnyvale and Iowa Avenues. The property excludes the public parking parcels that are owned by the City/Successor Agency and the parcels occupied by the Target and Macy's stores which are under separate ownership. On November 18, 2015, Wells Fargo Bank submitted a "Notice of Intent to Transfer" (Attachment 2) to sell the Town Center property to a to-be-formed joint venture comprised of affiliates of (a) Sares Regis Group of Northern California, (b) Hunter Properties, Inc., and (c) an institutional investor advised by J.P. Morgan Asset Management (hereinafter referred to as Transferee).

Under the 2010 Amended Disposition and Development and Owner Participation Agreement (ADDOPA), Article 6, the City Council acting as the Successor Agency to the Sunnyvale Redevelopment Agency (Agency), is able to review specified criteria related to the proposed Transferee's business qualifications (Attachment 3). Article 6 does not provide Agency authority to select or approve the proposed Transferee, but provides an opportunity for the Agency to assess the capabilities of the Transferee before the property transfer occurs. Certain exemptions to Agency review are stated in Article 6, including transfer of those portions of the project that have already been completed. While much of the Town Center project is pending completion, two existing office buildings (Buildings A and C) on Block 2 (see Attachment 4) have been completed and are currently occupied by Nokia and Apple. Thus, most of the proposed transfer is subject to Article 6 review, with the exception of the parcels with the completed office buildings.

ENVIRONMENTAL REVIEW

Article 6 review is not subject to the California Environmental Quality Act since it does not approve or alter the approved project or land use entitlements and only pertains to the transfer of private property.

DISCUSSION

The purpose of the special Agency meeting is to provide an assessment of the proposed Transferee under the provisions of Article 6 of the ADDOPA. The following discussion reviews the Article 6 criteria and review process and summarizes the findings of staff and consultants regarding the financial and professional experience of the proposed Transferee.

Article 6 Criteria

Article 6 defines four criteria for review of proposed Transferees qualifications that are subject to Agency review (see Attachment 3):

- i. Has experience in and has completed major mixed-use commercial, retail, residential projects of similar size, scope and nature involving a mix of national, regional and local tenants;
- ii. Has adequate financial capacity, including the references of at least two lending institutions with substantial lending experience in California mixed use real estate, to timely commence and complete the construction thereof;
- iii. Possesses a good business character and reputation; and
- iv. Has prior development projects and an operating presence in California.

In order for the Agency to conduct its Article 6 review, Wells Fargo Bank is required to provide reasonable evidence to the Agency demonstrating that the proposed Transferee satisfies the four criteria. Under the terms of Article 6, the Agency has 20 business days to review the evidence and to “acknowledge or challenge” whether the proposed Transferee meets the criteria. The purpose of the review period is to allow the Agency and Bank to request and exchange additional information. Based on the notification date of November 18, the Agency must provide a response to Wells Fargo Bank by December 18, 2015. If the Agency fails to respond to the Bank within the 20-day period, the transfer is deemed permitted. Attachment 5 details the time schedule for the Article 6 review process.

Under Article 6, an acknowledgement indicates that sufficient evidence has been provided for the Agency to reach a conclusion that the proposed Transferee satisfies the criteria. If the Agency acknowledges that the proposed Transferee satisfies the four criteria, then the Article 6 review process is complete and the parties may proceed with their transaction.

Alternatively, if the Agency, exercising “commercially reasonable discretion,” challenges the proposed Transferee’s ability to satisfy one or more of the criteria, the Agency must provide detailed evidence for reaching this conclusion. On December 10, it may be premature to take this action since the 20-day review period (December 18) has not concluded. If necessary, the Agency could request additional information specific to any of the Article 6 criteria for its further review, which could be scheduled for the December 15 meeting. If the Agency provides evidence to the Bank by December 18 challenging the proposed Transferee’s ability to meet one or more of the criteria, Article 6 provides a process for the parties to exchange more information during the following 15 days, and if the Agency ultimately continues to dispute the proposed Transferee’s ability to satisfy the criteria, the dispute would then be resolved by “expedited arbitration.”

The Article 6 criteria pertain to the financial capability, development experience and business reputation and character of the proposed Transferee to acquire and complete the Town Center project. While evaluating the past projects completed by the proposed development partners is germane to the Article 6 review, requesting specifics regarding the Transferee’s plans for completing the Town Center project are outside of this review process and not a basis for assessing the criteria. No proposals have been put forth by the Transferee for amending the ADDOPA, land use entitlements or other agreements. Any deliberations on these items are premature until the Article 6 review is concluded. The Article 6 review functions as a sort of threshold review; if the proposed Transferee is cleared to move forward, specific proposals about how to proceed or modify any existing documents and entitlements would be negotiated and processed between the parties in the following months.

Article 6 Review Support

Completion of the Article 6 review process is a key milestone for the project and the City used two highly-qualified consultants to complete this ADDOPA requirement. The short time allowed for Article 6 review requires a fast turnaround by the Agency with limited staff and during a peak workload. Additionally, while in-house staff has considerable development review experience, the assistance of finance and real estate experts is required to supplement staff's experience and to ensure a thorough evaluation of the proposed Transferee. For these reasons, the services of two highly-qualified finance and real estate consultants were obtained to conduct a comprehensive investigation of the three entities involved in the proposed property transfer and to also understand the financial structure and development capabilities of the to-be-formed joint venture.

The lead consultant that prepared the Article 6 report is Macias Gini & O'Connell LLP (MGO), a statewide certified public accounting and business management firm with eight offices throughout the state. Scott P. Johnson, CPA, CGMA, partner with MGO, is overseeing the Article 6 evaluation. MGO serves a wide variety of industries, and is nationally recognized for its professional leadership from both the profession and industry regulators. The firm offers a diverse array of audit assurance, tax, advisory, and business management services to clients ranging from startup companies to middle-market public and private companies, the world's largest public pension system, and California's largest local governments. MGO's State and Local Government Practice is one of the largest in the country and offers unmatched resources in serving this complex sector, including serving the City of Sunnyvale as the City's Independent Certified Public Accountants for external financial reporting requirements in accordance with professional accounting standards. The City has a longstanding relationship with MGO; it has conducted our annual external audits for the past three years and is familiar with our team and organization.

Keyser Marston Associates, Inc. (KMA) has also been retained to provide peer review of the Article 6 report, as well as contribute added expertise in real estate development and finance. Tim Kelly, president of KMA, is the principal in charge of this assignment. KMA has advised many California cities and major public entities throughout the state with respect to public policy and implementation to achieve the desired public benefits using innovative approaches to land use planning and specific real estate projects. KMA has advised public clients in the Bay Area and Santa Clara Valley for over 30 years on a wide range of land use and public policy matters. The firm's local knowledge of real estate, market and economic conditions, combined with the firm's broad perspective of regional, statewide and national trends, provides valuable expertise for evaluating the financial feasibility of large developments such as the Town Center project. KMA has particular knowledge about downtown Sunnyvale, having prepared a past analysis for the Town Center project; they also prepared the recently completed market analysis that will be presented in today's study session.

Article 6 Data Request

Wells Fargo Bank indicated to the City Manager in late October that it was negotiating the sale of the Town Center property, with the intent of submitting to the City in mid-November the names of the proposed Transferee. In anticipation of this submittal, staff worked with MGO and KMA to develop a data request for conducting the City's Article 6 review. This request was submitted to Wells Fargo Bank on November 9 (Attachment 6). At the time the request was prepared, the City had no information about the identity or nature of the proposed Transferee, so the data request and related questions were broad for cautionary purposes, to some degree extending beyond the scope of the Article 6 criteria. While this broader information is helpful for providing a fuller understanding of the capabilities of the Transferee, the focus of the data request is on the core information that is needed to reach a conclusion on the four Article 6 criteria.

On November 18, Wells Fargo Bank submitted a "Notice of Intent to Transfer" (Notice) to sell the Town Center property to the proposed Transferee (Attachment 2). The Notice acknowledges that the anticipated sale of the two completed office buildings on Block 2 (Buildings A and C) as part of the transfer is not subject to Article 6 review per Section 6.01(c). However, the Notice recognizes that the remainder of the property is subject to Article 6 review per Section 6.01(b). After an initial review of the Notice and attachments, MGO and KMA concluded that additional information would be beneficial to verify and acknowledge that the proposed Transferee satisfies the Article 6 criteria.

Following submittal of the Notice and during the past week in particular, staff and consultants have actively engaged with the Transferee to request additional information to complete the Article 6 analysis. Much of the information was deemed by the Transferee to be confidential or proprietary in nature, so the consultants met directly with the development partners

to share and discuss their companies' financial and real estate development data. Additionally, corporate background checks, including individual background checks of the principals, were conducted by a third party firm and these reports were provided to MGO and are deemed confidential.

Article 6 Conclusions

After a thorough review of the data shared by the Transferee, MGO and KMA have concluded that the proposed entities in the to-be-formed joint venture satisfy the four Article 6 criteria, and an acknowledgement of this finding is appropriate by the Successor Agency to conclude the review process. Attachment 7 is the primary report prepared by MGO, and Attachment 8 is the peer review memorandum prepared by KMA.

The Article 6 review was conducted with the representation that J.P. Morgan Asset Management (JPM, more specifically the JPMCB Strategic Property Fund) will be the sole equity owner of the two office building lots. For the remainder of the retail, residential and undeveloped portions of the property (subject of Article 6 review), JPM is represented as the majority property owner (95 percent equity interest or greater). A to-be-formed limited liability joint venture is proposed for ownership of the property that will consist of JPM, Sares Regis Group of Northern California (SRGNC as the residential developer), and Hunter Properties, Inc. (Hunter as the retail and office developer). While SRGNC and Hunter will actively oversee their respective residential and commercial components, JPM will have the decision-making authority.

Criteria (i), (iii) and (iv):

With regard to the experience, business reputation and California presence of the development partners, MGO/KMA found that the strengths of SRGNC and Hunter complement each other well, along with the financial backing of the significant equity investment/ownership with JPM. Overall, MGO/KMA found that collectively, SRGNC and Hunter have considerable experience completing major mixed-use commercial, retail and residential projects involving primarily national, and, to a lesser extent, regional and local tenants. MGO/KMA found that while SRGNC's and Hunter's various projects are not analogous to the Sunnyvale Town Center project, these projects demonstrate their experience with mixed use development.

In comparison to Sunnyvale Town Center, MGO/KMA found that SRGNC's mixed-use residential/commercial developments have a significantly larger residential component, whereas Hunter Properties' mixed-use office/commercial projects have a significantly larger office component. SRGNC was reported to excel in upfront planning and in their ability to communicate and negotiate with those outside of their immediate development team (e.g., other owners, their agents, the community, various levels of government). Hunter Properties demonstrated particular strengths in constructing commercial retail and office buildings. Additionally, MGO/KMA found that both developers have substantial experience operating in California, with a particular development presence in San Mateo and Santa Clara Counties for over 20 years. They have maintained strong reputational standing within the real estate industry and in the communities where they have built projects. Both are longstanding members of real estate professional organizations, such as the Urban Land Institute (ULI) and International Council of Shopping Centers (ICSC).

Staff Comments: The Town Center is a unique mixed use development in a downtown setting located at a premier location in Silicon Valley. It is not surprising that the property generated intense interest among the development community when the property was marketed by Wells Fargo Bank. Given the uniqueness of the project, it is expected that each developer would not have similar projects in their portfolio. Individually, each member of the to-be-formed joint venture brings considerable expertise to development team in addition to financial capabilities. Collectively, the team brings together an impressive combination of mixed use, residential and commercial development experience as well as asset management experience, which is critical for implementing and sustaining a large complex mixed use project. When evaluated together, the complementary and overlapping expertise of the three development partners are a good indication that the development team will be able to deliver the Town Center project. The to-be-formed joint venture represents a new business relationship for the parties. Staff expects that the details regarding the operating structure will be further defined once the property transfer is finalized.

Criterion (ii):

With regard to the financial capacity of the development partners, MGO took the lead in analyzing this criterion. JPM was examined in greater depth since they are the major equity investor. In examining their financial records, MGO found more than sufficient assets to fund the project. As of June 30, 2015, the fund had net assets of \$27.6 billion dollars. Based on the current proposed financing structure, MGO reviewed the financial condition rather than capacity of SRGNA and Hunter, and determined that both development partners exhibit strong fiscal strength. MGO's review of financial indicators shows both companies have sufficient financial capacity to meet their obligations throughout the development.

Staff Comments: JPM clearly has the financial capacity to be the prime equity partner for the proposed joint venture. They provide a solid financial foundation for delivering the Town Center project. Additionally, JPM already has a strong presence in downtown Sunnyvale as the owner of two office buildings at 150 and 190 Mathilda Place where Broadcom is the major tenant. As an institutional investor, JPM brings substantial equity to the project and they will be making the primary investment decisions. It is expected however that SRGNC and Hunter, as the development partners, will actively lead the construction and management of the residential and commercial components of the project. As the project moves forward, the factors affecting the decision-making process within the joint venture and how these factors will determine the path forward for the project (e.g. construction schedule, tenant mix, and project modifications) are of considerable interest to staff. While this is key consideration, it is not within the scope of the Article 6 review criteria, but would be addressed in future discussions with the three parties.

FISCAL IMPACT

Article 6 review does not have a fiscal impact on the City. Any amendments to the ADDOPA or other agreements that could have fiscal implications on the City are not being considered at this time.

PUBLIC CONTACT

Public contact was made by posting the Council agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's website.

ALTERNATIVES

1. Acknowledge that the proposed Transferee satisfies the four Article 6 criteria in the ADDOPA for transfer of the Sunnyvale Town Center property.
2. Request that the City Manager request additional data to further evaluate if the Transferee satisfies the Article 6 criteria in the ADDOPA for transfer of the property and hold a follow-up special City Council/Successor Agency meeting on December 15.

STAFF RECOMMENDATION

Alternative 1: Acknowledge that the proposed Transferee satisfies the four Article 6 criteria in the ADDOPA for transfer of the Sunnyvale Town Center property.

Per the report submitted by MGO with peer review by KMA, the Transferee has shared sufficient data to reach a positive conclusion that the proposed development partners and to-be-formed joint venture are considerably well financed to complete the Town Center project with JPM providing the vast majority of the equity for the project. The individual partners in the to-be-formed joint venture have

strong development backgrounds; as a combined team, they will provide considerable investment funds and complementary expertise to execute a complex mixed use development. Both SRGNC and Hunter have substantial experience in mixed use, residential and commercial development, respectively. In particular, both developers have a strong presence in the Bay Area with a large portfolio of successful projects in multiple communities.

If the Agency cannot reach a conclusion that acknowledges that the proposed Transferee satisfies the Article 6 criteria, then additional information should be requested for further review on December 15. Any information requested must be specific and germane to determining if the proposed Transferee satisfies the four Article 6 criteria. The Agency has until December 18 to respond to the Notice of Intent to Transfer.

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Approved by: Deanna J. Santana, City Manager

ATTACHMENTS

1. Eastdil Secured Marketing Notice
2. Notice of Intent to Transfer, November 18, 2015
3. Article 6 (excerpt of 2010 Amended Disposition and Development and Owner Participation Agreement)
4. Town Center Site Plan
5. ADDOPA Article 6 Review Schedule
6. Article 6 Developer Review Data Request, prepared by MGO, November 9, 2015
7. Independent Evaluation Report on Article 6 Criteria: Developer Experience and Reputational Review, and Assessment of Developer Financial Capacity, prepared by MGO, December 9, 2015
8. KMA Memorandum, December 9, 2015