



City of Sunnyvale

Agenda Item-No Attachments (PDF)

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REPORT TO COUNCIL

SUBJECT

Authorize the City Manager to Execute the First Amendment to the 1178 Sonora Court Disposition and Development Agreement Between the City of Sunnyvale and Mid-Peninsula Baker Park, Inc. to Extend the Close of Escrow Date and Incorporate the Ability to Enter into a Short-Term Lease with MP Sonora Court Associates, L.P. for the City-Owned Property at 1178 Sonora Court into the Disposition and Development Agreement

BACKGROUND

On February 25, 2020 (RTC No. 20-0115), City Council approved a \$14 million Housing Mitigation Fund conditional funding award to MidPen Housing ("MidPen") for the construction of a new 176-unit affordable housing development located at 1178 Sonora Court (the "Property"). At the request of Council, the City and MidPen entered into negotiations for the City to purchase the Property from MidPen and enter into a Disposition and Development Agreement ("DDA") for the project. On May 19, 2020 (RTC No. 20-0500), City Council approved a Disposition and Development Agreement and Purchase and Sale Agreement ("PSA") with Mid-Peninsula Baker Park, Inc., a subsidiary of MidPen, for the affordable housing project.

Pursuant to the DDA and PSA, the City provided a predevelopment loan of \$450,000 and purchased the Property from MidPen for \$13.55 million. The DDA requires that the City lease the Property to MidPen through a 65-year long-term ground lease for the duration of the project. Pursuant to the DDA, the long-term ground lease is required to begin at close of escrow, which shall occur no later than June 30, 2021. This date was chosen to coincide with the lease termination of the former industrial tenant on the property, Prototek, who had preexisting plans to relocate their office.

In early June of 2021, MidPen contacted City staff with concerns about unexpectedly high possessory interest (PI) taxes applicable to long-term leases that would not be applied to short-term leases. Based on conversations with the Office of the Santa Clara County Assessor, MidPen calculated that a short-term lease would reduce PI taxes by approximately \$340,000 per year, which would significantly reduce holding costs during the predevelopment phase of the project which could last two to three years. City staff reviewed these calculations and recommended entering into a short-term lease for the Property until construction financing for the project could be secured to reduce financial burden on the future development.

Although Sunnyvale Municipal Code Section 2.07.050 authorizes the City Manager to enter into revenue generating short-term leases under 55 years, the DDA requires an amendment to permit a short-term lease to occur prior to close of escrow. On June 22, 2021, MidPen submitted a written request to the City for an amendment to the DDA that would allow the City to enter into a short-term lease. Due to the quick nature of the former tenant vacating the existing facility and the looming tax issue, on June 30, 2021, the City Manager and MidPen executed the Short-Term Ground Lease

(Attachment 3) for the Property for a term of two years (with an optional extension up to two additional years) with rent of \$1,000 per month. The First Amendment will incorporate the ability to enter into a short-term lease with MP Sonora Court Associates, L.P.

EXISTING POLICY

Council Policy 5.1G.2: Provide incentives, such as co-location privileges or rent subsidies, to attract private agencies to provide needed health and social services.

General Plan, Housing Element

Goal HE 1: Assist in the provision of adequate housing to meet the diverse needs of Sunnyvale's households of all income levels.

Goal HE 5: Promote equal housing opportunities for all residents, including Sunnyvale's special needs populations, so that residents can reside in the housing of their choice.

ENVIRONMENTAL REVIEW

On November 8, 2021, the Planning Commission approved a Special Development Permit for the construction of the 1178 Sonora Court Project (Report No. 21-1027). As part of that approval, the Planning Commission made findings under the California Environmental Quality Act (CEQA) Guidelines Section 15168 that the Project is within the scope of the previously adopted Environmental Impact Report (EIR) for the Lawrence Station Area Plan, and no further environmental review is required. Approval of the amendment to the DDA is merely a fiscal action that implements the construction of the Project. No additional environmental review is required. (CEQA Guidelines, Sections 15162.)

DISCUSSION

This First Amendment to the DDA would accomplish two main objectives during the predevelopment phase of the project that will help the project secure construction financing. These objectives include (1) authorizing the Short-Term Lease to occur before close of escrow therefore extending the close of escrow date for the new long-term ground lease to be executed until start of construction, and (2) providing additional flexibility in project financing commitments and deadlines. Per the DDA, the close of escrow includes the commencement of the long-term ground lease and the closing of both the construction loan and the City's \$450,000 predevelopment loan. This Amendment would be retroactive to authorize the existing two-year short-term lease of the Property to occur prior to the close of escrow. Per the Amendment, the Short-Term Lease shall expire on June 30, 2023 (unless mutually extended by both parties for up to two years) and includes monthly rent of \$1,000.

1. Currently the DDA requires that the close of escrow and signing of a long-term ground lease must occur by June 30, 2021. However, due to reasons explained in the background section of this report, the City entered into a short-term lease with MidPen starting July 1, 2021. This amendment also extends the close of escrow date so a long-term ground lease begins no later than the expiration of the current Short-Term Lease. This change will allow time for a short-term lease during predevelopment and keep the close of escrow aligned with the construction loan closing date and commencement of a long-term ground lease as already outlined in the DDA.
2. The DDA also requires the project to secure an award of Affordable Housing and Sustainable

Communities (AHSC) financing prior to applying for tax credit financing and for tax credit financing to be awarded by May 19, 2023. Since the DDA was executed in May 2020, MidPen has diligently pursued all required Planning entitlements in November 2021; however, with the state changing deadlines and eligibility requirements for various grant opportunities, MidPen plans to apply for tax credit financing in late 2023 or early 2024. The Amendment would buffer in the additional time needed for financing previously unseen due to a recent change by the state. This Amendment would also give MidPen the option to pursue other forms of financing if the project does not receive an AHSC award and allows ample financing flexibility in a time when tax credit financing is reaching its highest levels of competitiveness. MidPen will pursue additional sources of project financing in order to start construction in late 2024.

The First Amendment will benefit the City by allowing the Short-Term Lease, which would ensure that the City-owned property at 1178 Sonora Court remains maintained and secure throughout the predevelopment phase of the project. This will also benefit the City as reduced costs for MidPen translate into less of a financing gap as the project nears construction. MidPen will supply all required liability insurance, pay taxes, and perform any necessary maintenance on the Property. Additionally, the First Amendment would benefit the project by ensuring that MidPen has site control of the Property, which is necessary to apply for tax credit financing, while minimizing holding costs during predevelopment. Lastly, adding flexibility to the DDA now ensures the DDA will meet the needs of both the development and of MidPen without having to return to Council for future amendments prior to construction.

FISCAL IMPACT

There is no impact to the General Fund. There is minimal, but positive, fiscal impact to the Housing Mitigation Fund (these funds were used for the City to purchase the parcel) associated with the Amendment to the DDA. The Short-Term Lease will increase the monthly rent payable to the City's Housing Fund from \$0 to \$1,000 for the duration of the Short-Term Lease.

PUBLIC CONTACT

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

RECOMMENDATION

Authorize the City Manager to Execute the First Amendment to the 1178 Sonora Court Disposition and Development Agreement Between the City of Sunnyvale and Mid-Peninsula Baker Park, Inc., to Extend the Close of Escrow Date and Incorporate the Ability to Enter into a Short-Term Lease with MP Sonora Court Associates, L.P. for the City-Owned Property at 1178 Sonora Court into the Disposition and Development Agreement.

Due to the importance of this affordable housing development, the First Amendment to the DDA would allow the City-owned Property at 1178 Sonora Court to remain secure, maintained, well scheduled for future funding applications, allow for lower holding costs, and ensure MidPen can continue to move forward with the development of this much-needed affordable housing project.

Prepared by: Ryan Dyson, Housing Specialist
Reviewed by: Sherine Nafie, City Property Administrator

Reviewed by: Trudi Ryan, Director, Community Development
Reviewed by: Jaqui Guzman, Deputy City Manager
Approved by: Kent Steffens, City Manager

ATTACHMENTS

1. Request Letter from MidPen
2. First Amendment to the 1178 Sonora Court DDA
3. Final Copy of Executed Short-Term Lease