CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Jacky Morales-Ferrand

SUBJECT: SEE BELOW

DATE: February 27, 2020

Approved D. DSyL

Date 2/28/2020

COUNCIL DISTRICT: 7

SUBJECT: TEFRA HEARING FOR CALIFORNIA STATEWIDE COMMUNITIES DEVELOPMENT AUTHORITY'S ISSUANCE OF TAX-EXEMPT MULTIFAMILY REVENUE BONDS TO ACQUIRE AND REHABILITATE THE VALLEY PALMS APARTMENTS

RECOMMENDATION

(a) Hold a Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") public hearing for the issuance not to exceed $120,000,000 in tax-exempt private-activity bonds by the California Statewide Community Development Authority to finance issue private-activity bonds for the acquisition by Valley Palms 2018 LP (the "Borrower") and rehabilitation of the Valley Palms Apartments, a 354-unit apartment complex located at 2155 and 2245 Lanai Avenue in San José (the "Development") and to pay certain expenses incurred in connection with the issuance of the bonds.

(b) Adopt a resolution approving the issuance of Tax-Exempt Revenue Bonds by CSCDA in a principal amount not to exceed $120,000,000 to be used to finance the Development and to pay certain expenses incurred in connection with the issuance of the tax-exempt private activity bonds.

OUTCOME

Hold a second TEFRA public hearing for the issuance of the $120,000,000 tax exempt bond for the development and rehabilitation of the Valley Palms Apartments Development. This tax exempt bond will finance acquisition and rehabilitation of the Development. Due to the expiration of the February 5, 2019 TEFRA approval, the Borrower has requested that the City Council hold a second public TEFRA hearing and adopt a resolution approving the issuance of bonds by California Statewide Community Development Authority ("CSCDA") for the Valley Palms Development prior to the expiration of the Development's bond allocation in April, 2020. Approval of the recommended action will authorize the CSCDA to issue tax-exempt bonds for the acquisition and rehabilitation of the Development and will allow the Development to close its financing prior to the expiration of its CDLAC allocation in April 2020.

EXECUTIVE SUMMARY

The City Council is holding a second TEFRA for the Development to allow the Borrower to move forward with a $120,000,000 bond issuance by CSCDA. During the original TEFRA hearing held in February 2019, the City Council requested that KDF develop a security plan for the site, add the expansion of the family resource center and the conversion of the tennis court to a soccer field to the proposed rehabilitation budget for the site. KDF has addressed these three items by submitting the security plan and the scope of services for the rehabilitation. Subsequently, additional concerns related to the Development and its resident services and security have been raised by community organizations and residents. These concerns include limited access to onsite facilities for resident services and retaliatory actions from the property management company, VPM Management. Negotiations are currently taking place with KDF and the bond issuer to the City's conditions and monitoring to address these concerns and will be added to the Development's Bond Regulatory Agreement. A supplemental memo will be provided regarding the specific terms.

BACKGROUND

Prior City Council Action

On February 5, 2019 a public hearing was held for the TEFRA, and the allowance of the issuance of a tax exempt bond in the amount of $120,000,000 by JPA issuer CSCDA for the acquisition and rehabilitation of the Valley Palms Apartments Development in San Jose, CA. After the public hearing City Council adopted the resolution approving the issuance of Tax-Exempt Revenue Bonds by CSCDA and gave the following direction:

Direct the City Manager to:

(a) In line with the due diligence staff carried out in preparation of this item, continue to monitor the scope of work and fulfillment of the commitments made by the applicant in seeking the issuance of Tax-Exempt Multifamily Revenue Bonds;

(b) Work with KDF Valley Palms, L.P. and subsequently Valley Palms 2018 LP and seek implementation of the priorities that have been identified by the tenants:

- Establish and implement a security plan for the site;
- Expand existing family resource center to provide more space for services to the residents;
- transform existing tennis court into a turf soccer field;

(c) Provide a report back to Council in October of 2019.

Staff has provided, in the Analysis section of this memorandum, an update on the above Council directed items.

Proposed Issuance Structure

CSCDA has requested that the City of San José ("City") consent to its issuance of an amount not to exceed $120,000,000 in tax-exempt private activity bonds ("Bonds") for the Development. The bond proceeds and other sources, including low income housing tax credit equity, will finance the acquisition and rehabilitation of the existing restricted affordable Apartments. The regulatory agreement will extend the affordability of the property an additional 55 years.

CSCDA is a statewide Joint Powers Authority, of which the City is a member. For CSCDA to issue bonds in San José, it must request permission pursuant to its membership agreement. City staff then determines whether the issuance comports with the City's current Policy for Issuance of Multifamily Revenue Bonds ("the Policy"). The proposed issuance is consistent with the Policy, under Section I. B, as discussed in the Analysis section, and CSCDA requests that the City Council approve CSCDA's bond issuance and hold a public TEFRA hearing on the forthcoming issuance.

<u>Property Owner</u>

KDF Valley Palms, L.P., an affiliate of KDF Communities ("KDF"), is the existing Development owner. KDF purchased the property in 2002 and is now seeking funding to recapitalize and rehabilitate the Property.

<u>Property Overview</u>

The Property was built in 1966, last renovated in 2002, and already offers restricted affordable rents. The current restricted rents are enforced by CSCDA's bond regulatory agreement from 2002, in which the City is a third-party beneficiary. The current unit restrictions will continue the same as they are now:

- 106 apartments (30%) will continue to be rent restricted serving tenants with maximum incomes of 50% of the area median income ("AMI"). The current income for a 50% AMI level, is **$58,550** for a two-person family in a one-bedroom apartment. Using the HCD guideline on occupancy, rents are initially expected to range from **$1,464 for a one bedroom to $1,646 for a two bedroom;**

- 244 apartments (70%) will continue to be rent restricted serving tenants with maximum incomes of 60% of the area median income ("AMI"). The current income for a 60% AMI level, is **$70,260** for a two-person family in a one-bedroom apartment. Using the HCD guideline on occupancy, rents are initially expected to range from **$1,757 for a one bedroom to $1,976 for a two bedroom**; and

- Four two-bedroom apartments for resident managers will be unrestricted.

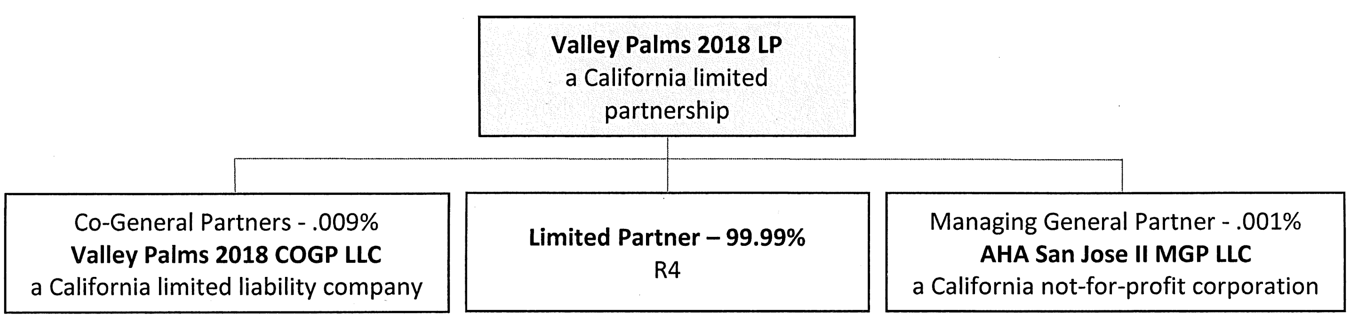
The Development is located within a mixed-use neighborhood with major shopping, schools, and recreational amenities located within a short distance. Access to groceries, pharmacy and shopping is convenient and is within reasonable walking distance. Located on a large 17-acre lot, the Development also offers a clubhouse, tennis court, basketball court, two swimming pools, two playgrounds, laundry facilities and covered parking.

Borrower

The Borrower for the proposed Development, is Valley Palms 2018 LP, new limited partnership that was formed in January of 2019 to purchase the property. Valley Palms 2018 LP is a California limited partnership. Valley Palms 2018 LP will purchase the Development from KDF and become the new Development owner.

A new partnership has been formed for purchase of the Development that will consist Affordable Housing Access, Inc. ("AHA"), Valley Palms 2018 COGP, LLC as co-general partners. AHA is an existing California nonprofit public benefit corporation. The limited partner for Valley Palms 2018 LP will be R4 Capital. Please see below, the Organization chart for the Valley Palms Development.

VALLEY PALMS APARTMENTS
OWNERSHIP ORGANIZATIONAL CHART



The recapitalization for this Development is a typical action for existing low-income housing tax credit properties. Typically, at the end of the tax credit compliance period of 15 years, it is allowable under IRS rules that an existing development apply for new tax credit allocation to rehabilitate the property. Concurrently, a change in ownership of the Development will also take place. For the purposes of this financial recapitalization, KDF has requested that CSCDA apply to the California Debt Limit Allocation Committee (CDLAC) for a bond allocation for the Development, and low income housing tax credits (LIHTC), with a tax credit equity investor.

A portion of tax-exempt bond proceeds must be spent on physical improvements; therefore, KDF has indicated a proposed budget in their application submitted to CDLAC. Approximately $15,705,017 in property improvements that will be made in conjunction with this transaction. Per the developer KDF, the remainder of the Bond proceeds and tax credit equity will be used to finance the acquisition of the property, pay for hard and soft transaction costs, pay any relocation costs, fund initial development reserves, and the funding of a developer fee. Please see the below proposed Budget:

Project Cost Summary at Application	
Land and Acquisition	$110,500,000
Construction Costs	$0
Rehabilitation Costs	$15,705,017
Construction Hard Cost Contingency	$2,355,752
Soft Cost Contingency	$50,000
Relocation	$432,000
Architectural/Engineering	$173,100
Construction Interest, Permanent Financing	$8,116,951
Legal Fees	$150,000
Reserves	$1,659,767
Other Costs	$405,291
Developer Fee	$17,964,000
Commercial Costs	$0
TOTAL	**$157,511,878**

Scope of Work

According to KDF, the scope of rehabilitation will address health and safety issues, accessibility requirements, deferred maintenance, and energy efficiency enhancements. The rehabilitation includes scope of work includes installation of 159 carport LED canopy light fixtures, 54 medium LED flood lights, 41 small LED wall pack fixtures, fourteen 1000 watt fixtures, 325 hallway LED light fixtures, 240 porch and patio LED lights and 36 LED laundry room light fixtures. While the lighting plan is comprehensive, the amount of light that radiates from the property must strike an appropriate balance between public safety and excessive light output to neighbors and tenants. The lighting plan has been submitted to the City for review and approval. Additionally, security cameras, rebuilding a family resource center and conversion of tennis courts to a soccer field were added to the rehabilitation scope of work.

Work is expected to start in May of 2020 and conclude in November of 2021. According to KDF, while it is possible that some residents may need to stay briefly in another location so that their apartments can be renovated, most of the rehabilitation is expected to take place with the tenants in place. KDF indicates that no significant permanent displacement of residents is anticipated from the rehabilitation or the financial restructuring.

ANALYSIS

The City Council provided clear direction that staff work with KDF to ensure the following actions took place:

1) Establish and implement a security plan for the site;
2) Expand existing family resources center to provide more space for services to the residents; and
3) Transform the existing tennis court into a turf soccer field.

Since the public hearing held on February 5, 2019, it has come to the attention of the Director of Housing, that there are additional concerns that have been raised by the community regarding the Valley Palms Development. The Housing Department received feedback from residents in the community through a neighborhood community based organization, Valley Palms Unidos, and the Santa Clara County of Juvenile Probation Department/Neighborhood Safety/Services Unit. Both organizations identified that there were still many concerns that exist at the property. Concerns include gang activity, violence in the neighborhood and difficulty working with the current property management company, VPM Management Inc. (VPM) and Project Access, whom provides resident services at Valley Palms.

On February 10th, 2020 the Director of Housing issued a letter to KDF requesting documentation of the three City Council priorities from last year's Council meeting (**Attachment A**). Staff requested documentation that the Council priorities were being incorporated into the current budget for the rehabilitation, and a have a prepared plan for the ongoing operations of the

Development. On February 19, 2020, KDF responded with a letter describing progress to date. This response is included as **Attachment B**.

The section below provides an update on the three priorities originally identified by the City Council and the subsequent concerns raised by the community.

Security Plan for the Site

KDF submitted a security plan for the site and revised the property management plan to incorporate key elements of the security plan. Following the City Council direction in February 2019, KDF took action to increase onsite security in August 2019 and the security gates were repaired. The rehabilitation budget now includes funding for security cameras and improved exterior lighting. The section below outlines each of the components of KDF's security plan.

Armed Security Guards – KDF hired the security service company Personal Protective Services in August 2019 to patrol the property with armed security guards. The security guards patrol between Valley Palms and Foxdale Village (a sister property located two miles from Valley Palms) during 8 hour shifts per day. The days and times vary depending on the needs of the two properties. There may be anywhere from 4 to 10 armed guards patrolling at one time. The number of guards may be increased or decreased due to criminal activity in the area and specific needs of the properties. The security company works closely with the San José Police Department and Police Captain, can make citizens' arrests when necessary and participates in community outreach and building trust amongst the residents.

Security Gates – The security gates have been changed to allow for one-way traffic only in and out of the property. There is one entrance gate near the center of the property near the leasing office that is used to enter the property and two exit gates on the far right and left sides of the property along Lanai Avenue to exit the property. The entry gates remain open during normal leasing office business hours. Outside of normal business hours, vehicles can only access the property with the use of an electronic remote. Property management has been notified by KDF that maintenance of the gates is a high priority item and that gates need to be fixed immediately when broken.

Security Cameras – As part of the planned scope of renovation, KDF will install security cameras throughout the property to cover activity in common areas, back corners of the property, carports, garbage areas, laundry rooms, entrance gate, exit gates and pedestrian gates. Cameras directed towards gates and driveways will be able to capture license plate numbers. The contractor bid and specifications for the security cameras are included in **Attachment B**.

Enhance Exterior Lighting – 100% of the current exterior lighting will be upgraded to new LED fixtures. The new fixtures will provide maximum output per City standards and code. The lighting scope of work includes installation of 159 carport LED canopy light fixtures, 54 medium LED flood lights, 41 small LED wall pack fixtures, fourteen 1000 watt fixtures, 325 hallway LED light fixtures, 240 porch and patio LED lights and 36 LED laundry room light fixtures.

While the lighting plan is comprehensive, the amount of light that radiates from the property must strike an appropriate balance between public safety and excessive light output to neighbors and tenants. The contractor bid and specifications is also included in **Attachment B**.

Family Resource Center

The Family Resource Center is located onsite and provides a space in which services are provided to the tenants of Valley Palms. The non-profit service provider Project Access has provided tenant services at Valley Palms since 2002. Project Access provides approximately 24 hours of resident services per week. In 2016 the County of San Mateo Neighborhood Safety/Services Unit (NSU) also began providing services at the Family Resource Center. NSU provides approximately 16 hours of resident services per week. In January 2019 the City informed KDF of the community's desire to have the existing Family Resource Center building enlarged to accommodate an expanded calendar of workshops, programming, classes and events. KDF originally looked at expanding the existing space at the Family Resource Center but they determined there was insufficient room to do so. Instead, KDF proposed to construct a second building on the property. Drawings for the building have been completed and the cost of the building ($265,500), which is included in the resyndication renovation budget. The drawings for the building are included in **Attachment B**.

Soccer Field Conversion

In January 2019, the neighborhood association Valley Palms Unidos informed KDF they were interested in converting the tennis court at Valley Palms into a turf soccer field stating that the tennis court area is an underutilized space and that converting it to a soccer field would have a positive impact to the community. In February 2019, KDF obtained bids from qualified contractors and selected FlexGround, a contractor that is familiar with tennis court conversions. The estimate from FlexGround to convert the tennis court to a soccer field, in total is $177,000 with $107,633 to convert the field and an additional $69,367 for the demolition, lighting, and fencing. The total amount of $177,000 is included in KDF's resyndication rehab budget. **Attachment B** includes the contractor bid, information on soccer field conversions and pictures of a comparable soccer field conversion and specifications.

Assessment of City Council Requests

Per City Council direction provided in February 2019, the specific requests for a security plan, expanded family resource center, and the conversion of the soccer field, have been reviewed and accepted by the Housing Department staff. Staff will continue to coordinate with KDF to ensure the proposed improvements are completed as a part of the rehabilitation plan for the Development within a reasonable timeline.

Additional Community Concerns

Over the past year, following the February 2019 City Council discussion, staff has interacted with community groups regarding their concerns about the Development. Concerns were raised by the community including ongoing gang activity, violence in the neighborhood, difficulty working with the current property management, VPM Management, and challenges coordinating resident services with Project Access, the onsite resident service provider.

On February 12, 2020, a shooting took place on site at the Development. The Police Department took the lead on responding to the shooting, however, it is an indicator of ongoing violence at the Development.

On January 31, 2020, the Santa Clara County Department of Probation submitted a letter to the City indicating concerns regarding the Valley Palms Development (included in **Attachment A**). The letter states that the Valley Palms apartment complex has experienced problems with violence and it outlines strategies to address these concerns at the property. The letter also states, that long-term violence prevention strategies are most likely to have a positive impact when involving a mix of approaches, including but not limited to, leadership Development, presence of strong social networks, community organizing efforts (grass roots organizing), and civic participation.

The community group Valley Palms Unidos, indicates in their letter dated January 30, 2020, that there are six actions requested to address concerns at the Development (**Attachment A**). The first three actions were the original actions requested by the City Council – implementation of a security plan, expansion of the family resource center, and conversion of the tennis court to a soccer field. These three items were addressed in the discussion above. Additionally, three new actions were requested: implementation of a shared-space agreement addressing access to the family resource center, replace Project Access as the resident service provider and update accountability of the property management company, VPM Management.

Proposed City Requirements for Inclusion in the Regulatory Agreement

Due to the City's limited role in this financing, there is an opportunity to collaborate with CSCDA to document additional requirements in the bond regulatory agreement. In this case, the City has requested the ability to comment and propose additional language regarding the expectations from the community in the regulatory agreement. A new exhibit to the bond regulatory agreement will be documented will be provided to the City Council via a supplemental memo and the Bond Regulatory Agreement with the agreed conditions will be executed and recorded upon closing of the Development's financing. A breach of the terms included in the regulatory agreement are treated as contractual and may be challenged in court if they are not upheld.

City Council Policy for the Issuance of Multifamily Housing Revenue Bonds

The Policy 1-16 requires that the City be the issuer of tax-exempt private-activity bonds for housing developments located within the City of San José. When the City is not the issuer, of the Policy, under Section I.B., allows the City to authorize another conduit bond issuer, in this case, CSCDA to issue bonds if two conditions are met: 1) the City is not making a loan or grant to the development; and 2) the development is one of multiple developments in the same round of CDLAC allocations under a similar financing program so as to result in economies of the costs of issuance. Although it is the City's practice to require that the City be the issuer of bonds for all developments in San José, on rare occasions, the City Council and/or City staff have approved developers' use of an alternate issuer pursuant to the Policy.

This proposed transaction meets the conditions for approving, CSCDA as the conduit issuers under Section I.B of the City's Policy. The first of the Policy's conditions is met, there is no prior, existing, or future City loan or grant on the Development. In addition, the second of the Policy's conditions regarding multiple concurrent issuances is also met: KDF is submitting three separate developments to be issued through CSCDA approved in this CDLAC allocation round. KDF will be able to achieve significant time and cost savings, economies of issuance, by utilizing the same finance team for the developments.

The Development also has an existing bond regulatory agreement from CSCDA's 2002 bond issuance. CSCDA must continue to report to CDLAC for the next 55 years from the Closing date, as required by CDLAC conditions. The City is currently listed as a third-party beneficiary to the regulatory agreement, which provides the City the right, but not the obligation) to enforce, separately or jointly with the Issuer and/or the Trustee, or to cause the Issuer or Trustee to enforce, the terms of the bond regulatory agreement. As the Issuer, the City has greater control over the Development. However, when the City is not the Issuer, the reduction of control for this Development is mitigated when the City is a third party beneficiary to the regulatory agreement. Because this proposed transaction meets Section I.B of the City's Policy and because the City will be named a third-party beneficiary, the City staff recommends CSCDA request to be the Issuer for this Development as acceptable under Policy 1-16.

TEFRA Hearing

Federal tax law limits the types of developments that may be funded with tax-exempt bond proceeds since the interest earned on such bonds is exempt from federal taxation. Pursuant to the Code, the issuance of the Bonds by CSCDA requires the City's approval because the Development is located within the territorial limits of the City. In order for the interest on the Bonds to be excluded from the gross income of the owner of the Bonds (i.e. tax-exempt), an "applicable elected representative" of the government unit must approve the issuance of the Bonds after the TEFRA hearing; The form of government approval is the resolution. The City Council's approval of CSCDA's issuance of the Bonds and the use of the proceeds serve to meet the applicable Code requirements. The City Council's approval of this action is not approval of the Apartments for any other purpose.

Due to the expiration of the February 5, 2019 TEFRA approval, the Borrower has requested that the City Council hold a second public TEFRA hearing and approval for the Valley Palms Development prior to the expiration of the Development's bond allocation in April, 2020. Approval of the recommended action will authorize the CSCDA to issue tax-exempt bonds and permit the acquisition and rehabilitation of the Development and, will ensure that the Development can close prior to the expiration of its CDLAC allocation in April 2020.

CONCLUSION

It is the priority of the City to engage the community and partners such as Valley Palms Unidos, the County of Santa Clara and KDF to work together to provide safe, sustainable affordable housing for our residents. The resyndication of Valley Palms provides an opportunity to bring these partners together to ensure the long-term success of the Valley Palms community. The proposed terms to the bond regulatory agreement will support the community while allowing the new financing structure to move forward.

EVALUATION AND FOLLOW-UP

The Regulatory Agreement will contain measurable outcomes that will be monitored by the Housing Department.

CLIMATE SMART SAN JOSE

The recommendation in this memo has no effect on Climate Smart San José energy, water, or mobility goals.

POLICY ALTERNATIVES

To arrive at this proposal, staff considered the following options:

Alternative #1: ***Deny CSCDA's bond issuance request.***

Pros: The City would have more time to negotiate with the borrower regarding community concerns, as the Development would likely need to re-apply to CDLAC.

Cons: If the City does not consent to renew its approval of the issuance, it is possible the Development will lose its CDLAC allocation, and be required to reapply in a subsequent round. This is a conduit bond issuance where five other affordable housing developments are wrapped into the same bond issuance. These developments are located in the cities of Fremont,

	Riverside, Redwood City, Salinas and Huntington Beach. The entire package may be compromised.
	If the financing does not move forward, there may be additional negative consequences for KDF and CSCDA when either party seeks future funding from CDLAC.
Reason for not recommending:	Staff does not support this alternative and instead recommends approval of CSCDA's bond issuance.

PUBLIC OUTREACH

This report will be posted to the agenda website for the City Council's March 10, 2020 meeting.

COORDINATION

This memorandum has been prepared in coordination with the City Attorney's Office, Finance Department, and the City Manager's Budget Office.

COMMISSION RECOMMENDATION/INPUT

This item was not heard by the Housing and Community Development Commission, as approvals of affordable development financing do not fall under the functions, powers, and duties of the Commission delineated in Section 2.08.2840 of the San José Municipal Code.

COST SUMMARY/IMPLICATIONS

By not exercising its option to not be the bond issuer, the City will forego its standard issuance fees and possibly the annual fees associated with the bond monitoring obligation. The typical fees collected by the City when acting as the bond issuer include an issuance fee and annual ongoing fees. However, as consideration for this request, the City will receive a $5,000 TEFRA hearing fee for non-City bond issuances. There are no other fiscal impacts to the City as there are no City funds allocated to the Apartments. Repayment of the tax-exempt bonds issued by CSCDA will be secured solely by the Development's revenues.

FISCAL/POLICY ALIGNMENT

This action is consistent with the City's Consolidated Plan 2015-2020, adopted by the City Council on May 5, 2015, and with the City's Adopted Housing Element 2014-2023 in that the action preserves existing homes for very low-income households.

CEQA

Not a Project, File No. PP17-004, Government Funding Mechanism or Fiscal Activity with no commitment to a specific development which may result in a potentially significant physical impact on the environment.

/s/
JACKY MORALES-FERRAND
Director, Housing Department

For questions, please contact Rachel VanderVeen, Deputy Director, at (408) 535-8231.

Attachment A: February 10, 2020 City Letter to KDF
Attachment B: February 19, 2020 Response Letter from KDF