



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Jacky Morales-Ferrand

SUBJECT: SEE BELOW

DATE: October 31, 2019

Approved

D. D. Syl

Date

11/1/19

COUNCIL DISTRICT: 7

**SUBJECT: STATUS OF THE LEASE NEGOTIATIONS WITH CALTRANS FOR A
BRIDGE HOUSING COMMUNITY**

RECOMMENDATION

- (a) Accept the staff report on the status of the lease agreement with Caltrans for the proposed Bridge Housing Community located at the South/West Quadrant of State Highways 280, 101 and 680, adjacent to Felipe Avenue.
- (b) Adopt a resolution documenting the City of San José efforts to negotiate a lease agreement with Caltrans in good faith and Caltrans has not met the spirit of Senate Bill No. 519.

OUTCOME

This report provides City Council with the status of the lease negotiations with Caltrans for the Bridge Housing Communities (BHC) site located at the South West Quadrant of State Highways 101 and 680, adjacent to Felipe Avenue, as well as the impact that the lease provisions will have on the development and operations of the BHC.

BACKGROUND

On January 1, 2017, Assembly Bill 2176, which amended the Shelter Crisis Act, became effective. AB 2176 authorizes a five-year pilot program allowing the City of San José, upon declaration of a shelter crisis and adoption of an ordinance establishing local standards, to create BHCs to provide shelter for the homeless. This includes temporary housing in new or existing structures on City-owned or City-leased property. AB 2176 also requires that each person who enters a BHC must have a transition plan to move them out into a permanent housing location.

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On August 29, 2017, the Housing Department provided the City Council with an update on the proposed site selection process for the BHC. Subsequently, the Mayor sent letters to several public agencies seeking support for the City's temporary homeless housing structures "proof of concept." The Mayor sought support from public partners in the form of potential BHC sites for lease or transfer. Three agencies, the Valley Transportation Authority (VTA), Caltrans, and Santa Clara Valley Water District, provided a combined total of 23 sites for the City to evaluate for potential BHC Pilot projects. Between September 2017 and December 2018 Housing Department staff developed the final BHC site recommendations for review and approval by City Council.

City Council Direction

On December 18, 2018, the City Council approved the Housing Department's recommendations to proceed with two sites to construct two Bridge Housing Communities. One site, owned by the Valley Transportation Authority, is located at ("the Mabury Road site"). The other site owned by Caltrans, is located at the South West Quadrant of State Highways 101 and 680, adjacent to Felipe Avenue ("the Felipe Avenue site").

In addition to the site selection, the City Council authorized the City Manager to negotiate and execute agreements with both agencies to secure the two parcels. Staff immediately notified both VTA and Caltrans of the City Council's site selection approval and of the City's desire to initiate lease negotiations with each agency.

VTA Negotiations

Once discussions began, City staff and both partner agencies realized that developing a lease agreement for such a unique and unprecedented use would present complex challenges. Negotiating lease terms (including contractor insurance requirements, mutually acceptable indemnification), and navigating multiple public agency processes, were just a few of the challenges that had to be addressed. While taking longer than both City and VTA staff originally anticipated, the City and VTA worked together to complete the tasks required to negotiate and execute the agreement in June 2019. These tasks included finalizing the legal agreements, completing VTA's plan review process, and securing the required contractor insurance. The City's selected developer, Habitat for Humanity, began construction at the Mabury Road site in the first week of July. Construction is targeted for completion in November 2019.

Caltrans Negotiations

Unfortunately, negotiations with Caltrans for the Felipe Avenue site have not progressed as anticipated. In late October 2018, City staff completed a comprehensive review of the airspace lease provided by Caltrans and identified concerns with the lease agreement provisions. Some of the terms drafted by Caltrans would have prevented the City from constructing and operating BHC in accordance with AB 2176 as approved by City Council. For example, improvement and construction standards in the agreement were different than the City of San José's recently

adopted BHC standards. Others required the City to accept unreasonable liabilities and significant ongoing financial commitments. Specific provisions which were not acceptable to the City included:

- City insurance requirements;
- Immediate termination clauses with no opportunity to remedy defaults;
- Unreasonable assignment of liability to the City;
- No prior notification for Caltrans site and sleeping cabin inspections;
- Prohibitions on resident services; and
- Incorrect representation of the site and existing conditions.

Between October 2018 and June 2019, City staff continued to pursue acceptable changes to Caltrans lease. Unfortunately, little progress was made in resolving the City's fundamental concerns. Subsequently, pending legislation targeting Caltrans property statewide for homeless shelter and feeding programs prompted Caltrans to expand the lease discussions beyond the Caltrans District 4 regional team to include staff from headquarters offices. Caltrans wanted to create a standard lease that could be used with other cities requesting Caltrans sites under the pending legislation. This caused additional delays, as the City worked to solve Caltrans concerns, Caltrans introduced additional requirements and obstacles.

However, several productive phone meetings were conducted to address each of the unresolved lease provisions. Through these meetings, the two agencies agreed in principle to several changes which addressed a number of the City's concerns. However, Caltrans introduced a substantially revised draft agreement in the form of a Right of Way Use Agreement. The new agreement introduced several new restrictions on the use of the Caltrans property, including:

- A prohibition on any type of rent or fees charged to residents/program participants; and
- A use restriction limiting the amount of time a resident/program participant could stay on site to 30 consecutive days with a cumulative limit of 90 days.

By early September 2019, several existing and newly introduced concerns remained unresolved. On September 27, following direction from the Mayor's September 24 memorandum, the City Manager issued a letter to the Caltrans District Director (**See Attachment A**) outlining five remaining issues preventing further progress in the negotiations. These issues are summarized below.

1. *Caltrans insurance requirements are unworkable* – Caltrans has persistently maintained requirements for the City to carry \$20M in Commercial General Liability or certify that its self-insurance meets specific dollar amounts and provides equivalent coverage to a commercial insurer.
2. *Time Limits on participant occupancy* – This provision limited a resident's/participant's occupancy to 30 consecutive days and 90 days cumulatively.

3. *Lease termination provisions* – Several sections throughout the lease called for immediate termination of the lease agreement for defaults or lease violations.
4. *Specified Use* – City staff had requested that Caltrans include BHC as an approved shelter use within the specified use section.
5. *Unreasonable assignment of liability to the City* – Several sections throughout the lease require the City to accept liability for conditions unrelated to the lease or the proposed BHC.

The City Manager's letter also included the desired revisions to address these issues and established a deadline of September 30, 2019 for Caltrans to respond. On September 30, the Caltrans District Director responded to the City Manager that he believed the City and Caltrans could reach workable solutions to the remaining issues, but that they were looking for clarification on the specified use provisions. Late, on October 11, Caltrans staff followed-up with a revised agreement that include updated language for each of the five issues identified in the City Manager's letter. On October 18, City staff provided comments on the proposed revisions on version 19 of the agreement. As of the date of this memo, the City has not received a response from Caltrans to the latest round of comments.

ANALYSIS

Resolved Lease Provisions

Throughout the lease negotiations, Caltrans has agreed to revise several problematic requirements. One of the highly problematic provisions identified in several sections of the lease was Caltrans ability to immediately terminate the agreement for defaults or lease violations. Caltrans has revised the latest version of the agreement to be consistent with Senate Bill 211 requirements which call for a 120-day notice for termination.

Accepted Lease Provisions

In the interest of advancing the lease agreement and resolving some of the last remaining issues, City staff has accepted certain unfavorable requirements within the latest agreement that had previously been identified as concerns. Specifically, City staff will work within the newly proposed parameters of the following lease provisions:

- *Specified Use* – Caltrans has adapted the new Right of Way Use Agreement as a standard agreement for the recently adopted SB 211. This authorizes public agencies statewide to use Caltrans property for emergency shelter and feeding programs for \$1 a year. The City's challenge with this approach is Caltrans has elected to use a narrow definition of shelter that limits the amount of time BHC participants can stay on the Caltrans site. The limited shelter definition also

prohibits collection of rent or fees, which is contrary to the AB 2176 legislation that authorizes the City to operate BHC. The program anticipated that monthly fees would 1) better prepare program participants for their transition to permanent housing; 2) reduce temptations to prolong their stay at the BHC; and 3) provide opportunities to bank these fees as a savings program for participants to use in their transition to permanent housing.

- *Time limits on participant occupancy* – Caltrans has revised this section of the agreement to limit program participant’s occupancy to six months. While not ideal, this revision from 90 day limits is workable. It will require that any BHC participant who is unable to locate a permanent housing location within six months would need to be moved to another interim housing site.

Other requirements that the City has accepted include:

- *Environmental Testing Standards* – In preparation for use of the site, Housing Department staff worked with Environmental Services Department to complete a Phase 1 environmental report. This established site conditions and the potential need for remediation of hazardous materials. Environmental Services Department completed the Phase 1 report in accordance with industry protocols. Provisions added to the latest version of the lease apply additional Phase 1 protocols specific to Caltrans. Acceptance of these provision will require additional testing. Further environmental investigation may be required per Caltrans discretion and could potentially extend the project schedule and cost. These additional protocols will add a minimum of three weeks in the pre-development process and the outside lab testing will increase the testing cost by \$2,000 to \$3,000.
- *Bonding Requirements* – The Right of Way Use Agreement requires the City to provide assurance of sufficient project funding. The City must provide satisfactory evidence of its ability to fund the project. A completion bond and/or payment bond may be required at Caltrans’ discretion. Procuring these bonds would extend the project schedule minimally by three to four weeks and increase the project budget by \$100,000 to \$200,000 depending on the level of coverage required by Caltrans.

Unresolved Lease Provisions

While the City and Caltrans have been able to address a number of issues, there are still two major areas which are yet to be resolved:

Unreasonable Caltrans Insurance Requirements – Caltrans has, in a break from past practice, required the City to provide commercial insurance, or to represent that its self-insurance is the same as commercial insurance and that it will be subject to the Insurance Code regulations that apply to commercial insurers. Self-insurance is not commercial insurance and the City (like other

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public entities) is not a commercial insurer, so such representations and agreements are unreasonable. This issue has become the primary point of contention in the lease negotiations. Throughout the lease discussions, the City has repeatedly requested that Caltrans accept the City's standard self-insurance letter because the City cannot provide commercial endorsements or certify specific amounts of insurance. City staff has made clear to Caltrans that in order to include a guarantee certification of specific self-insurance amounts for this project only, such as the \$15 million required under the lease, the City must appropriate that amount in the City budget for that specific project. Additionally, Caltrans was informed that the City maintains a catastrophic insurance reserve of \$15 million, preventing the City from entering into an agreement with liability limits above that amount. Finally, including the \$15 million Workers' Compensation/Catastrophic Reserve, the City provided Caltrans with evidence of over \$87 million in the General Purpose reserves (Contingency Reserve - \$40 million; Budget Stabilization Reserve - \$32 million), to demonstrate that the City has the financial capacity to satisfy its self-insurance obligations.

As a potential solution, City staff has proposed including the following new language in the City's self-insured letter:

1. The City certifies it will maintain a minimum \$15 million in the catastrophic insurance reserve during the lease term; and
2. The City will prioritize claims made related to the Felipe Avenue site or the lease from Caltrans ahead of all other claims with respect to the reserve

This proposed language was submitted to Caltrans on October 18. As of the date of this memo, the City has not received a response.

Unreasonable Assignment of liability – In addition to the amount of insurance, the remaining unresolved lease requirements relate to unreasonable assignment of liability. Several items related to liability have been resolved through the negotiations process. However, three sections remain problematic. The first, states that the City is “conclusively deemed” responsible for remediating all hazardous material found on the site once the lease has commenced. The City has requested that, consistent with more typical lease terms, the City's obligation to remediate hazardous materials discovered after lease commencement be limited to the substances introduced, exposed or disturbed during the lease term. Under the current language, the City would be responsible for addressing any hazardous substance issue that may have existed prior to the City's use of the site or aerially deposited lead deposited in connection with the use of the freeway.

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The second is a general statement in the agreement holding the City liable for claims related to any to a person on the site (or entering/exiting the site) regardless of the relationship to the lease use (e.g., a drunk driver runs off the road and hits a tree on the site). As with the previous provisions, there is no nexus to the City's use of the site. The final issue concerns the lease requiring the City to indemnify Caltrans prior to the resolution of liability.

The City has proposed clarifying language that it believes will resolve these last remaining issues. As of the date of this memo, the City has not received a response on these issues.

Revised Project Schedule

The goal of City staff throughout the lease negotiations has been to negotiate terms and conditions that will allow the City to construct and operate the BHC as designed through thoughtful planning, community input, and City Council direction, while accepting reasonable and proportionate risk and liability as with the VTA agreement. Additionally, City staff focused on revisions aimed at streamlining the pre-development and construction timeline.

Unfortunately, additional delays may result because the agreement provides several additional steps in the site review and approval process. While SB 211 provides some regulatory relief to the site standards, Caltrans, the State Fire Marshal, and the Federal Transportation Department must all review and approve the BHC site plan. City staff has persistently inquired about Caltrans timelines, including the timeline for lease execution once agreement is reached as well as the timeline for site review and approval. Given the additional requirements within the Caltrans lease, City staff estimates construction of the second BHC site will begin in spring of 2020 with occupancy in late summer 2020.

CONCLUSION

Although the responsiveness of District 4 Director, Tony Tavares, is greatly appreciated, the lease negotiations between the City of San José and Caltrans for the Felipe Avenue parcel have been difficult. The extensive negotiations have already delayed the start of construction of the second BHC by over six months to date, and over a year when all is said and done. As is noted in this report, the various requirements within the lease agreement will significantly impact the project schedule and budget as well as alter the BHC operations as originally planned. However, City and Caltrans District 4 staff have dedicated significant time and effort to developing a lease agreement that will be mutually workable. That said, this process of collaboration and negotiations continues to be plagued by conflicting pieces of legislation in Sacramento and legal concerns from Sacramento. Without better direction and collaboration from Sacramento this project, and others related to homelessness will further delay solutions that are ready to be implemented today. For this reason, staff has recommended a Council resolution.

Throughout the BHC planning and development process, staff has learned that every process for this project is new and undefined. The City's BHC efforts have resulted in new standards and established new precedents. The Caltrans lease is no exception. The City Council may choose to

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direct the City Manager to continue negotiations but also re-evaluate alternative sites. Though, once the City and Caltrans have completed the lease processes, the path will be open to new opportunities. SB 211 authorizes jurisdictions to access up to ten Caltrans parcels for emergency shelter use. Given the difficulty locating sites for BHC and other shelter uses, the City Council should take this into account when weighing their direction. In addition, staff will re-evaluate the various pieces of legislation that overlap with these projects and seek legislative changes and/or clarity.

EVALUATION AND FOLLOW-UP

The Housing Department will continue to provide periodic updates on the status of the BHC developments. As indicated in the December 18, 2018 approved Council report, the Housing Department will return to City Council one year after the first site is open to report on the BHC performance. Additionally, the City will be submitting a report on AB 2176 to the State legislature on January 1, 2020. This report will be posted on the Housing Department Website.

CLIMATE SMART SAN JOSE

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

PUBLIC OUTREACH

This memorandum will be posted on the City's Council Agenda website for the November 5, 2019 Council Meeting.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.

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CEQA

Not a Project, File No. PP17-007, Preliminary direction to staff, eventual action requires approval from decision-making body and File No. PP17-009, Staff Report Assessments, Annual Report, and Information Memos that Involve no approvals of City action.

/s/

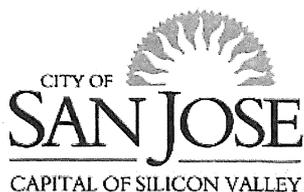
JACKY MORALES-FERRAND

Director, Housing Department

For questions, please contact James Stagi, Acting Division Manager, at (408) 535-8238.

Attachment A - City Manager letter to Caltrans District Director

Attachment A



Office of the City Manager

September 26, 2019

Tony Tavares
District Director
Caltrans Bay Area
111 Grand Ave
Oakland, CA 94612

SUBJECT: CALTRANS LEASE PROVISIONS

Dear Mr. Tavares:

Under the authority of Assembly Bill 2176, San José is building emergency bridge housing communities to temporarily house the City's homeless resident while they are matched to affordable permanent housing. On September 5, 2017 San José Mayor Sam Liccardo sent letters to several public agencies seeking surplus land suitable to develop one or more Bridge Housing Communities.

On September 15, 2017, Caltrans responded positively, offering the City eight properties as potential bridge housing sites. After evaluating 122 potential sites, including the eight Caltrans properties, City staff identified the Caltrans property adjacent to Felipe Ave, in the South/West quadrant of interstate 280/680/101 as one of the top potential sites for one of San José's Bridge Housing Communities.

In February 2018, City staff started working with Caltrans to prepare for the final City Council site approval and began taking the necessary steps to secure the site for construction. On December 18, 2018, the San José City Council approved staff's recommendations to move forward with the Felipe site. Between February and December, City staff completed the environmental review required under CEQA, completed a draft site plan for Caltrans review, and developed a project scope and budget in anticipation of starting construction of the Bridge Housing Community. Unfortunately, during that time, the City and Caltrans made little progress resolving what the City considers to be fundamentally unmanageable provisions within the lease agreement.

In July and August 2019 there was a renewed sense of urgency to finalize the lease and several productive phone meetings with my staff and Caltrans. However, we have not received comments back on the most recent document and no date has been communicated on when we can expect to receive comments. On Tuesday, September 25th, the City Council directed confirmation by September 30, 2019 that we have reached a resolution with Caltrans on the most significant lease provisions. We must return to City Council immediately with a proposed resolution if we can't come to an agreement with Caltrans.



Below is the list of remaining concerns preventing further progress in negotiating and executing a lease agreement. The following provisions are unacceptable because they would make it infeasible and impractical to operate the facility in their current form.

1. Caltrans Insurance requirements are unworkable

The City is self-insured and the lease must include acceptance of the city's standard self-insurance letter. The lease cannot include requirements for certification of specific amounts, or requirements that the City's coverage or role be equivalent to a commercial insurer. In addition, the City cannot execute an agreement that includes limits in excess of \$15M. The City has solicited quotes from many commercial insurers for \$5M of excess coverage to support its self insurance; the single informal quote received from this effort was \$250,000 for \$1M of additional coverage. The City is requesting that Caltrans accept the City's standard self-insurance letter and the insurance limits are reduced from its current \$20M limit to \$15M in the Lease Agreement.

2. Time Limit on Participant Occupancy - Section 5.13 Shelter/feeding Program Operations - Each shelter/feeding program client shall be subject to Tenant's established rules of entry, continued occupancy, and client service but in no event, shall a shelter/feeding program client be permitted to remain in the emergency shelter for a continuous uninterrupted stay of more than (30) days, and shall not accumulate a total stay of over 90 days within a six-month period"

After negotiating lease terms and conditions since late 2018, in the most recent version 16 of the lease, Caltrans included the above new, significantly restrictive occupancy standards. This is not consistent with the purpose of the emergency bridge housing statute which is intended to provide enough time for completion of a matching plan between the tenant and permanent housing. The lease cannot limit the total time a participant can be part of the Emergency Bridge Housing program if the City is to comply with AB 2176. The City is requesting that Caltrans remove this newly added time limited occupancy requirement from the agreement.

3. Lease Termination Provisions - The lease calls for *immediate* termination in several sections within the proposed lease agreement (violations due to commercial activity, failure to maintain fencing, etc.).

Given the City's significant investment in the site and the substantial impact on the lives of the Bridge Housing residents, the City is requesting revisions in the lease language allowing the City 30 days to correct defaults vs. immediate termination of the lease. This revision is consistent with other provisions that provide for 90-day notice.

4. Specified Use - Section 5.1 includes the following language "Tenant's use in violation of this specified use will result in Lease termination. The parties agree that use of the Premises for any purpose not specifically authorized above in section 5.1 is prohibited."

Caltrans deleted the reference to Bridge Housing Communities in Section 5.1 Given that emergency shelter and feeding programs are not clearly defined in the Streets and Highways Code authorizing statutes, the City is requesting that language be added to

Section 5.1 to include the City Bridge Housing Communities as an emergency shelter program, since the penalty is lease termination. The Emergency Bridge Housing Community must be listed as an approved use, either by inclusion in the emergency shelter definition, or as a separate express provision.

5. Unreasonable Assignment of Liability to the City - Section 5.2.1.

- a. That any hazardous material later found on site shall be “conclusively deemed to have been released” by the City and all costs associated shall be borne by the City.

This provision intended for sale of a property, not a temporary lease where title returns to the owner. City has provided minor edits in the latest response to include an opportunity to cure pursuant to article 15 and provide exception for work performed by Caltrans or their contractors and to limit the scope to the Premises controlled by the City. Given the lease has standard terms for liability for hazardous materials in Section 5.6, and in Section 10.3, it does not appear that this additional language is needed and we request that it be removed.

- b. City has “sole full responsibility for any illness, personal injury, death, property damage, or any other injury or damage related to the normal use of a State Highway, including the reasonably foreseeable misuse by motorists and members of the traveling public, including but not limited to ADL and vehicular emissions.”

This is beyond what is needed for protecting the Landlord, which is already present in the indemnity. Currently, it implies that the City has sole liability regardless of who is at fault, including passing motorists. The City and Caltrans have discussed changes to this provision, and we are requesting that these changes be incorporated into the lease.

The City of San José appreciates the opportunity to continue partnering with Caltrans in our efforts to address homelessness in San José. I also want to thank you for personally discussing this project with me in several phone calls and emails. Unfortunately, the City has reached a point where we must decide if continuing to pursue the Felipe Avenue site is prudent. The City would greatly appreciate a response to the list of concerns outlined in this letter by September 30, 2019.

Sincerely,



David Sykes,
City Manager