



CITY OF MILPITAS

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12/19/2017
Agenda Item No. 4



ATTACHMENT RELATED TO AGENDA ITEM AFTER AGENDA PACKET DISTRIBUTION





December 19, 2017

Mayor Tran and Members of the Milpitas City Council
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Via Email and U.S. Mail

RE: 199-Unit Senior Assisted Living Residential Development (Phase I of South Main Street Senior Facility)
Address: 1620 S. Main Street
Developer: Milpitas Phase 1, LP

Honorable Mayor Tran and Members of the Milpitas City Council,

The agenda for this evening's City Council meeting includes the Council's consideration, approval and authorization for the City Manager to execute the Subdivision Improvement, Public Street Maintenance and Reimbursement Agreements for the referenced project, which are critical items to close the transaction contemplated in the DDA.¹ During the Council's consideration of these three agreements at its December 5, 2017 meeting (continued from its November 21, 2017 meeting), the Council asked if the number of affordable units in the first phase could be increased by accelerating construction of some of the affordable units planned for the second phase. We would like to explain why this is not possible, and to offer a potential alternative to explore as part of the second phase of the project that could result in an increase in the total number of affordable units. In addition to this explanation, we hereby respectfully request that the Council approve the three implementation agreements, which will help to ensure the construction of a critical senior facility, while also providing opportunities to develop even more senior affordable housing in the City as part of the project's full buildout.

¹ Consistent with the City Attorney's explanation to the Council during its December 5, 2017 meeting on this matter, these ministerial agreements simply implement the transaction contemplated in the DDA, are standard in form, and are designed to protect the City by ensuring the construction and maintenance of the specified public improvements. The City Engineer has approved these agreements as to substance, and the City Attorney has approved them as to form.

By way of brief background, since the execution of the amended DDA in 2013, the development team has worked productively in partnership and in good faith with the City to bring the first phase (assisted living) of the project to fruition. Among other things, the developer processed and obtained the City's approval of the Vesting Tentative Map, Site Development Plan, Density Bonus, Conditions of Approval and Parcel Map for phase one (assisted living). Consistent with these approvals, the developer then prepared, processed and obtained City approval of construction plans for phase one and the related on- and off-site improvements, and satisfied the conditions for issuance of its building permits upon payment of the requisite fees. Currently, the construction lender and equity investor for phase one are completing their final underwriting in anticipation of closing the construction financing by year end in accordance with the parties' obligations for phase one under the DDA. Furthermore, binding construction bids for labor and pricing contingent on a January 2018 commencement of construction are in place for phase one.

Please be assured that the members of the development team for this project understand the City's need for affordable housing, and are committed to working with the City to help provide this much-needed housing. To that end, when we negotiated the amendment to the Disposition and Development Agreement (the "DDA") for our Milpitas senior continuum of care retirement community with the City² in 2013, we agreed to numerous conditions requested by the City to enhance the affordable component of the retirement community, including the following:

- (1) *Construct the affordable units*, which is much more costly than the alternative of paying an in-lieu fee, and disproportionately more expensive for an assisted living facility with extensive public areas, amenities and services as compared to a standard apartment building;
- (2) *Provide a greater percentage of affordable units in total* – 5% of the units in the first phase assisted living project and 20% of the units in the second phase independent living project – as compared to the minimum required by the City at the time for a standard apartment building;
- (3) *Provide for a deeper level of affordability* through the restriction of all of the affordable units to very low-income households rather than the allowable (and typical) mix of very low, low and moderate income households; and
- (4) *Pay property taxes on the affordable units* rather than take advantage of the property tax exemption allowed under state law for these units. The property taxes and other taxes generated by the first phase assisted living project will result in an annual benefit to the City and community of Milpitas in excess of \$300,000 per year.

In addition, owing to the City's significant need for housing for disabled persons of all ages, and particularly senior citizens, we agreed to:

² At that time, these negotiations were formally handled by the City's Redevelopment Agency ("RDA"), which, as you know, has since been dissolved.

(5) *Design and construct 100% of the phase one units to be accessible to the disabled, enabling residents to age in place; and*

(6) *Construct an all steel and concrete building, at a cost that is more than 30% greater than the cost of a typical wood frame building, to allow residents to age in their units rather than relocate to another unit as their needs for personal care and services increase with age.*

Furthermore, in recognition of the significant and rapidly increasing need for memory care services, we:

(7) *Redesigned the building to add a secure memory care wing with its own separate amenities (dining room, activity rooms, courtyard, and more) to serve these residents; and*

(8) *Built into the project costs the ability to pay prevailing wage rates to the construction workers in recognition of the high housing cost burden on construction workers and the elderly parents many of them support, thereby increasing our construction budget by approximately 25%.*

Additionally, to reduce the expenditure of City capital improvement funds and for the benefit of the broader community, we agreed to (9) *construct and maintain public streets, a signalized intersection and public utilities at the project's expense as part of phase one (rather than deferring some of these costs to phase two).*

In exchange for the developer's voluntary agreement to provide these substantial community benefits and to take on the risks associated with developing this type of senior facility, including absorbing these significant upfront costs, the City and developer structured the conveyance of the raw, unentitled land for each of the two phases of the retirement community in a manner to help ensure its economic feasibility so that this project could actually be built in Milpitas.³

The community benefits outlined above impose a very heavy up-front cost on the first phase of the project (assisted living), which is much greater than the cost that similar affordability restrictions (not to mention the other benefits) would impose on a typical apartment building. Furthermore, as an assisted living/memory care facility, it is not eligible for other local, state and federal subsidies (such as low income housing tax credits) available to apartment projects to help offset the costs of affordability restrictions.

For these reasons, and to help ensure the economic viability of the project so that it could come to fruition, the City agreed to allocate the bulk of the affordable units to the second phase of the project to enable the developer to shift costs accordingly to the independent living phase (which involves comparatively fewer overall costs to develop). In the aggregate, the public subsidy for the affordable units in phases one and two combined is approximately \$258,000 per

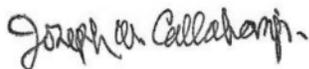
³ During the Council's November 21, 2017 meeting where it first considered the three implementation agreements, the development team provided the Council and the public with a detailed presentation of the cost-benefit analysis that summarized the DDA conveyance structure.

affordable unit. To put this in perspective, compare this to the approximately \$295,000 per affordable unit public subsidy (including City, County and Federal subsidies) provided to the DeVries Place senior affordable housing project on Main Street in Milpitas. Owing to the high cost burden imposed by the affordable units and other community benefit obligations on phase one (assisted living) of the project – both in construction costs and costs to subsidize the rent and provision of heightened assisted living care and services – it is not financially feasible to shift a portion of the affordable units from the second phase (independent living) of the project to the first phase. So doing would reduce the loan amount and correspondingly increase the amount of equity required. The project would not generate a return sufficient to attract the additional equity investment required and to justify the risks of developing an assisted living facility. *In other words, the development team believes that imposing this additional burden on the first phase of the project would seriously jeopardize the entire project from moving forward, contrary to the City's and the developer's intentions as reflected in the DDA.*

We embrace the City Council's desire for more affordable units, and genuinely regret that we are not able to provide more affordable units in the first phase (assisted living) of the project. That said, in a good faith effort to continue to work collaboratively with the City to meet its need for affordable housing, we would welcome a chance to explore opportunities during the entitlement process for phase two (independent living) of the project with City staff and the City Council to incorporate additional affordable units (beyond the current obligation) in phase two.

The development team continues to be committed to working with the City, as provided under the DDA, to bring this project to fruition, which will provide critical housing and support services to the senior community, while also facilitating other significant community benefits, including affordable housing, significant economic revenue, and more than 100 permanent jobs. Accordingly, we respectfully request that the City Council approve the three implementation agreements on this evening's agenda so that we may proceed to closing and commence construction of phase one in January 2018.

Respectfully,



Joseph W. Callahan, Jr.
Manager, South Main Senior Lifestyles, LLC



Ryan Leong
Principal, SRM Development, LLC

On behalf of Milpitas Phase 1, LP

cc. Chris Diaz, City Attorney
Seth Merewitz, Best Best & Krieger