CITY OF OAKLAND

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MARCH 9, 2004

IGNACIO DE LA FUENTE, PRESIDENT
CITY COUNCIL
OAKLAND, CALIFORNIA

PRESIDENT DE LA FUENTE AND MEMBERS OF THE CITY COUNCIL

SUBJECT: A RESOLUTION AUTHORIZING A GRANT IN AN AMOUNT NOT TO EXCEED $1,100,000 TO MACARTHUR PARK DEVELOPMENT ASSOCIATES, LLC, TO COVER ADDITIONAL COSTS FOR THE DEVELOPMENT OF THE FINAL PHASE OF THE PALM VILLAS PROJECT ON MACARTHUR BOULEVARD BETWEEN 90TH AND 94TH AVENUES

PURPOSE AND SCOPE

In accordance with the Measure H Charter Amendment, which was passed by the voters at the General election of November 5, 1996, we have made an impartial financial analysis of the accompanying Council Agenda Report and Proposed Resolution. In making our analysis we also held meetings with Agency staff, obtained copies of financial data of the MacArthur Park Development Associates, LLC, and obtained copies of liens against the Palm Villas project that had been filed with the Alameda County Recorder.

Since the Measure H Charter Amendment specifies that our impartial financial analysis is for informational purposes only, we did not apply Generally Accepted Government Auditing Standards as issued by the Comptroller General of the United States. Moreover, the scope of our analysis was impaired by Administrative Instruction Number 137, effective May 21, 1997, which provides only one (1) week for us to plan, perform and report on our analysis. Due to this time constraint and our overall workload, we did not verify the financial data prepared by the MacArthur Park Development Associates, LLC.

SUMMARY

In 1999 the Agency entered into an agreement with MacArthur Park Development Associates, LLC., a joint venture between Baines & Robertson, Inc. and Em Johnson Interest (MPDA) for the development and sale of the Palm Villas Project, which was to consist of 78 affordable housing units completed in three phases. MPDA is both the developer and the general contractor for this project.

To date, 62 of the 78 units have been completed (all of Phases I and II, and part of Phase III), and the new owners have already closed escrow and moved in. However, MPDA has experienced cash flow problems, which have caused them to practically shut down the project, and requests that the Agency approve a $1,100,000 grant. If the proposed grant is approved, and MPDA receives a proposed immediate infusion of cash from the construction lender, Bank of America Community Development Bank, MPDA anticipates that the remaining 16 units will be completed by the end of June 2004.

FISCAL IMPACT

Why the $1,100,000 grant is needed

Over the past several years, the Agency has provided substantial subsidies towards the development of this project. Before MPDA took over the project, the Agency spent $2,831,000 acquiring the land and paying for other work performed by the previous developer. In 1999, when MPDA took over the project, the Agency provided the land to MPDA at no cost. The Agency and MPDA also entered into a forgivable development loan agreement for $3,253,000. To complete the funding package, Bank of America Community Development Bank provided a $10,600,000 construction loan.

The intent was for MPDA to build a group of units, sell them, and use the sales proceeds to build another group of units, until all 78 units had been built and sold. Because it has taken much longer than expected to complete and sell the units, the anticipated sales proceeds from a group of completed units were not available when they were needed to pay for the next group. These delays in construction have also resulted in a major increase in the total project cost (not including profit) from an estimated $17.2 million in 1999 to more than $25 million by 2004. Some of this increased cost has been absorbed by the increase in the sales prices for Phase II and Phase III units, some by additional Agency funding, and some from MPDA's overhead costs.

In 2002, because of the cash flow problems and increased costs the developer requested that the original $3,253,000 loan be forgiven and that the Agency provide additional funding. Pursuant to Resolution No. 02-33, the Agency authorized the conversion of the $3,253,000 forgivable loan to a grant. Pursuant to Resolution No. 02-34, the Agency also authorized an additional $1,000,000 forgivable loan to MPDA, a portion of which provided silent second mortgages to eligible Palm Villas homebuyers. In April 2003, MPDA again returned to the Agency to request that the $1,000,000 loan be forgiven because of continuing cash flow problems and additional costs that had been incurred. Pursuant to Resolution No. 2003-20, the Agency authorized the conversion of that loan to a grant.

MPDA continues to experience cash flow problems, which have caused them to practically shut down the project, and requests that the Agency approve a $1,100,000 grant.

Redevelopment Agency's investment

With the approval of the proposed $1,100,000 grant, the Agency's investment in the project will total $8,184,000, as summarized below:

Description	Amount
Converted a forgivable development loan to a grant	$ 3,253,000
Converted a forgivable bridge loan to a grant	1,000,000
Grant currently proposed	1,100,000
Total grants	$ 5,353,000
Cost of donated land, and work done by previous developer	2,831,000
Total Redevelopment Agency investment	$ 8,184,000

Funds are available from the Low and Moderate Income Housing Fund - Fund: 9580, Project: P209310, Project Area: Central District. Approval of the grant will leave a balance of $2,018,850 in Redevelopment Agency affordable housing funds remaining for this fiscal year.

MPDA's investment

When MPDA began the project in 1999, they expected to receive $2,037,398 from the Palm Villas Project: $1,503,000 in profit and $534,398 in overhead costs. MPDA has already foregone some of their overhead costs to cover earlier cost overruns, and will now forego all of its originally anticipated profit.

Baines & Robertson's financial position

We are concerned that the financial position of Baines & Robertson, which holds a 66-2/3 percent interest in the joint venture, places the completion of the project in jeopardy.

According to unaudited financial statements, Baines & Robertson's current liabilities exceed its current assets. Therefore, MPDA has been unable to pay its creditors, causing the latter to file liens on the property totaling $553,458 as of February 6, 2004. According to Agency staff, most of these liens have been paid off, with the notable exception of liens totaling $226,476 filed by the Internal Revenue Service; however, we have not verified this.

After reviewing MPDA's latest financial projections for completing the project and researching other options, staff concurs with MPDA that it is necessary to provide $1,100,000 in additional funding as a grant instead of as a loan, so that MPDA will be able to finish the project and break even.

AGENCY SAFEGUARDS

In order to safeguard Agency funds and to ensure that the remaining 16 units are completed, the Agency will not release any of the $1,100,000 to MPDA until 12 of the remaining 16 units have been completed and staff has confirmed that those 12 units can be transferred, without encumbrances, to the qualified homebuyers. The funds would be released only on an as-needed basis, as determined by the Agency at its sole discretion, to provide sufficient cash flow to allow all 4 of the remaining units to be completed. At the completion of the project, any outstanding liens will be paid off through escrow.

ALTERNATIVE RECOMMENDATION

As an alternative, the Agency may wish to deny the request for this additional funding. However, because of the negative impact this would have on the project and the potential buyers of the remaining 16 units, staff does not recommend that the Agency deny the request.

CONCLUSION

The costs of the Palm Villas Project to date have been greater than planned. The staff's proposal is directed at protecting the Redevelopment Agency's interests: namely,

> **"not to release any of the $1,100,000 grant to MPDA until 12 of the remaining 16 units have been completed, and staff has confirmed that those 12 units can be transferred without encumbrances to the qualified homebuyers"**

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Report completion date:
March 1, 2004