

Oakland Oversight Board

Memorandum

TO: Oakland Oversight Board
SUBJECT: 1100 Broadway Project OPA
Amendment

FROM: Fred Blackwell
DATE: February 4, 2013
ITEM: #4

EXECUTIVE SUMMARY

On September 6, 2007, the former Redevelopment Agency, pursuant to Resolution No. 2006-88 C.M.S., executed an Amended and Restated Owner Participation Agreement (OPA) with SKS Broadway, LLC (SKS) for a proposed mixed-use office project, including the rehabilitation of the adjacent historic Key System Building, at 1100 Broadway. In June of 2010, pursuant to Resolution No. 2010-54 C.M.S., the Redevelopment Agency amended the OPA to extend performance deadlines to their current dates. Pursuant to the amended terms of the OPA, the deadline to start project construction is June 25, 2013, and the deadline to complete project construction is April 27, 2015. SKS will not meet these deadlines because of unfavorable conditions in Oakland's office market. SKS inability to perform will constitute a default under the OPA, unless the agreement is amended to extend the deadlines. SKS must pay liquidated damages of \$440,000 if it defaults on the OPA. ORSA can put SKS in default, but still hold SKS to the other provisions of the OPA, except to any schedule of performance controlling the development timeline of the project.

The Oakland Redevelopment Successor Agency (ORSA) stepped into the rights and obligations under the OPA when the Redevelopment Agency dissolved. ORSA is requesting approval from the Oakland Oversight Board of the ORSA board's action of December 18, 2012, approving an amendment to the OPA between ORSA and SKS to extend certain development deadlines to avoid a default by SKS.

In consideration of the looming deadlines, the ORSA board approved legislation authorizing an amendment to the OPA that will (1) extend the deadlines for SKS to complete a number of pre-construction activities by two years, (2) extend the date on which SKS must start project construction by two years, to June 25, 2015, and the date by which it must complete project construction by two years, to April 27, 2017, and (3) give SKS an option to extend the new construction commencement and completion dates by an additional 24 months at no cost to SKS.

SKS has also entered into a Purchase and Sales Agreement ("PSA") for a City-owned 145-space garage located at 409 – 12th Street (the "UCOP Garage") inside the University of California Office of the President building at 1111 Franklin to satisfy the parking needs of the project. This garage was built to supply parking for a project at 1100 Broadway in order to maximize the placement of retail space along Broadway. The City has approved an amendment to the PSA conforming its terms to the proposed amended terms of the OPA.

OUTCOME

Maintaining the OPA between ORSA and SKS by extending development deadlines will give SKS additional time to market the project to potential tenants. Once the developer has signed up an anchor tenant, they will be able to secure debt financing, complete design documents and start construction within the extended time frame proposed in the amendment to the OPA. Approval of the proposed amendment will provide ORSA, the City and other taxing entities control and a measure of certainty about the project scope and development schedule, and about the amounts and timing for receipt of property taxes.

BACKGROUND/LEGISLATIVE HISTORY

Owner Participation Agreement

On September 6, 2007, the former Redevelopment Agency, pursuant to Resolution No. 2006-88 C.M.S., executed an Amended and Restated OPA with SKS. In June of 2010, pursuant to Resolution No. 2010-54 C.M.S., the OPA was amended to extend performance deadlines to their current dates. Under the OPA, the deadline to submit project construction drawings is December 10, 2012, the deadline to start project construction is June 25, 2013, and the deadline to complete project construction is April 27, 2015. SKS must pay liquidated damages of \$440,000 to ORSA if ORSA declares the developer to be in default for failing to meet the dates for project construction commencement and completion. SKS' payment obligation is secured by a letter of credit.

When the Redevelopment Agency dissolved on February 1 of this year, the OPA was assumed by ORSA. Thus, ORSA has the authority to approve the OPA amendment, and would be entitled to receive any liquidated damages. Per the dissolution statute, any liquidated damages would become part of ORSA's cash assets and be subject to redistribution by the County to the other taxing entities. On December 18, 2012, the City Council sitting as the ORSA board, pursuant to Resolution No. 2012-13 C.M.S., authorized an amendment to the OPA to extend development deadlines.

ANALYSIS

Under the dissolution statute, the oversight board directs the successor agency to determine whether any contracts, agreements, or other arrangements between the dissolved redevelopment agency and any private parties should be terminated or renegotiated to reduce liabilities and increase net revenues to the taxing entities, and to present proposed termination or amendment agreements to the oversight board for its approval.

In the case of the 1100 Broadway Project, the issue is whether ORSA should amend the OPA to extend development timelines or declare SKS in default of the OPA and collect liquidated damages of \$440,000 for distribution to the taxing entities. ORSA can put SKS in default, but still hold SKS to the other provisions of the OPA, except to any schedule of performance controlling the development timeline of the project.

Oakland's Office Market

Despite SKS' on-going marketing efforts, the developer has been unable to enlist an anchor tenant for the project. For example, in 2011, SKS worked closely with City staff, and invested significant resources to respond to a Request for Proposals related to the development of a new multi-agency Regional Agency Headquarters for the Metropolitan Transit Commission (MTC), the Association of Bay Area Governments (ABAG), the Bay Area Air Quality Management District (BAAQMD), and the Bay Conservation and Development Commission (BCDC).

Commercial lenders have substantial pre-leasing requirements and the lack of tenants for the project has prevented SKS from obtaining debt financing and starting construction per the terms of the OPA. While current economic indicators for downtown Oakland suggest slowly improving conditions in the Class A office market, they do not yet render the development of a new office building financially feasible in the near term. Market data for the third quarter of 2012 suggests a vacancy rate of 10 percent for Class A office space in the Central District, while asking rental rates slightly decreased to \$2.64 per square foot. By comparison, the robust Class A office market in San Francisco's financial district, which posted average rents of \$4.05 per square foot in the third quarter of 2012, is gradually adding new office space (780,000 square feet currently under construction). This suggests that office rents in Oakland's downtown Class A office market still have to increase significantly to make any new office building construction economically feasible.

Because of the lackluster performance of Oakland's office market, SKS and its investor partner, Prudential Real Estate Investors, a union pension fund, have not yet expended the substantial funding needed to proceed with predevelopment work necessary for a June 2013 start of project construction. However, as the vacancy rate for office space in Oakland's Central Business District continues to decline, while rents increase in San Francisco and the Peninsula, it is not unreasonable to anticipate that market conditions will gradually improve in downtown Oakland as businesses seek less expensive alternatives in transit-oriented East Bay locations.

If SKS is declared in default under the OPA for failing to start construction by June of 2013, it would be the result of the lingering effects of the Great Recession that continue to adversely affect the growth of the local office market. The default provisions of the OPA were designed to penalize SKS if it made insufficient efforts to develop the property according to OPA parameters and timelines. This is clearly not the case, since SKS has diligently and in good faith marketed the project to potential tenants, while also becoming a key member in the Downtown Oakland Association.

If the OPA is not amended as proposed, there may be several potential undesirable outcomes for ORSA and the taxing entities.

First, SKS will no longer be obligated to complete key project deliverables based on a schedule of performance enforceable by ORSA, which will create uncertainty about the start of the project and the timing for the receipt of property taxes.

Second, SKS may seek a new buyer/developer for the site, which would cast further doubt on the timing of property taxes revenues from the project. The Redevelopment Agency pursued the redevelopment of this critical downtown property and the adjacent historic building for more than two decades to eliminate a major contributor of blight in the downtown. The earthquake-damaged historic landmark has been vacant since 1989, and finding a new development entity with suitable experience in historic rehabilitation and adaptive reuse in combination with new construction could be challenging and may result in the separation of the development of the vacant site and the rehabilitation and reuse of the Key System building. This would create an uncertain future for the revival of this significant landmark, and perhaps for the development of the site as a whole. SKS is a highly qualified developer with extensive experience in the rehabilitation of historic buildings and new construction. SKS made the rehabilitation of the Key System building a key component of their development strategy for the site. In addition, a new developer may reduce the project scope based on the minimum requirements of the OPA, which would decrease the amount of property taxes currently projected to be generated by SKS's proposed project. Lastly, if SKS sells the property and the Key System Building to another developer, they may no longer have an interest in the acquisition of the UCOP Garage. This would keep the facility under public ownership and maintain its exemption from property taxes.

In consideration of these factors, ORSA staff negotiated an amendment to the OPA that would extend the deadlines for development of the project by two to four years, and delay the receipt of tax benefits accordingly. The following table shows the current and proposed development milestone deadlines for the 1100 Broadway project:

OPA Milestones	Current OPA Milestone Dates	Proposed Extension of Current Milestone	Proposed New Milestone after Optional Extension
Submission of Final Construction Plans	12/10/12	12/10/14	12/10/16
Submission of Final Construction Contract	2/04/13	2/04/15	2/04/17
Submission of Final Plan for Project Financing	2/04/13	2/04/15	2/04/17
Construction Commencement	6/25/13	6/25/15	6/25/17
Construction Completion	4/27/15	4/27/17	4/27/19

COST SUMMARY/IMPLICATIONS

Failure to perform according to the current schedule of performance in the OPA will trigger payment of liquidated damages of \$440,000 to ORSA. Any payments of liquidated damages would become part of ORSA's cash assets and would be subject to redistribution by the County to the other taxing entities after satisfaction of ORSA's enforceable obligations, per the redevelopment dissolution statute. Extending the deadlines in the OPA schedule of performance will delay payment of these liquidated damages by up to 48 months.

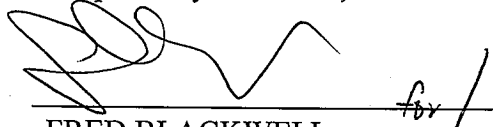
Extending the closing date will also delay the taxing entities' receipt of annual property taxes of approximately \$1.6 million from the project and \$70,000 from a privatized UCOP Garage by 24 to 48 months, depending on whether SKS exercises its option to delay the project construction date by another 24 month from 2015 to 2017.

In addition to the tax benefits to be generated by the project, the 1100 Broadway Project would also create one million craft labor hours (an average of 215 construction jobs per day during the 26-month construction phase), and approximately 1,600 permanent jobs after project completion and full occupancy of the building.

In order to maintain ORSA control and a measure of certainty about the project scope and development schedule, and about the timing for receipt of taxes, ORSA is requesting approval from the Oakland Oversight Board of ORSA's action approving an amendment to the OPA between ORSA and SKS to extend certain development deadlines.

For questions regarding this report, please contact Jens Hillmer, Urban Economic Coordinator at 238-3317.

Respectfully submitted,


FRED BLACKWELL
Assistant City Administrator

Reviewed by:
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Office of Neighborhood Investment

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Office of Neighborhood Investment

OAKLAND OVERSIGHT BOARD

RESOLUTION No. 2013-_____

A RESOLUTION APPROVING AN AMENDMENT TO AN OWNER PARTICIPATION AGREEMENT BETWEEN THE OAKLAND REDEVELOPMENT SUCCESSOR AGENCY AND SKS BROADWAY LLC TO EXTEND DEVELOPMENT DEADLINES FOR A MIXED-USE PROJECT AT 1100 BROADWAY

WHEREAS, on September 6, 2007, the former Redevelopment Agency of the City of Oakland (the "Redevelopment Agency") entered into an amended and restated owner participation agreement ("OPA") with SKS Broadway, LLC ("SKS"), pursuant to Redevelopment Agency Resolution No. 2006-0088 C.M.S., with regard to the development of a mixed-use office project ("Project") located at 1100 Broadway ("Property") in the Central District Redevelopment Project Area; and

WHEREAS, the OPA, as amended, establishes various parameters for the Project, provides the Redevelopment Agency certain approval rights regarding the 1100 Broadway Project, and requires SKS to accomplish a number of specific development milestones by specific deadline dates; and

WHEREAS, on June 1, 2010, pursuant to Resolution No. 2010-54 C.M.S., the OPA was amended to extend performance deadlines to their current dates; and

WHEREAS, SKS has made good faith efforts to reach those specific development milestones by the specified dates, but has been unable to do so because of lingering adverse economic conditions in Oakland's downtown office market that hinder SKS's efforts to obtain the required anchor tenants and debt financing for the Project; and

WHEREAS, SKS has to pay liquidated damages in the amount of \$440,000 to ORSA if it fails to meet the current development milestones and defaults on the OPA; and

WHEREAS, SKS has requested to extend the deadlines for Project construction commencement and completion as defined in the OPA; and

WHEREAS, the Redevelopment Agency dissolved on February 1, 2012, and the Oakland Redevelopment Successor Agency ("ORSA") has taken over the interests and obligations of the Redevelopment Agency with respect to the OPA and the Project; and

WHEREAS, on December 18, 2012, the ORSA board approved Resolution No. 2012-13 C.M.S., authorizing the ORSA Administrator, or her designee, to negotiate and execute an amendment to the OPA to (1) extend the date on which SKS must start Project construction by two years, from June 25, 2013, to June 25, 2015, and the date by which it must complete Project construction by two years, from April 27, 2015, to April 27, 2017; (2) give SKS an option to extend the new construction commencement and completion dates by an additional 24 months at no cost to SKS; and (3) extend the deadlines for submission of final construction plans, the construction contract, and the financing plan to ORSA until such dates as deemed appropriate and reasonable by the Administrator or her designee such that SKS is able to meet the commencement and completion deadlines above; and

WHEREAS, California Health and Safety Code Section 34181(e) provides that the oversight board shall direct the successor agency to determine whether any contracts, agreements, or other arrangements between the dissolved redevelopment agency and any private parties should be terminated or renegotiated to reduce liabilities and increase net revenues to the taxing entities, and present proposed termination or amendment agreements to the oversight board for its approval, and that the board may approve any amendments to or early termination of those agreements if it finds that amendments or early termination would be in the best interests of the taxing entities; and

WHEREAS, the Property and development of the Project, in conjunction with the sale of a City-owned parking garage on an adjacent property will generate financial benefits in the form of property taxes and sales taxes, and such property and sales taxes will be distributed to specified taxing entities in Alameda County pursuant to state law; and

WHEREAS, it is estimated that the developed Project on the Property will produce \$1.6 million in property taxes per year for the taxing entities upon completion of construction; and

WHEREAS, it is estimated that the net present value over a 10-year period accruing to the taxing entities from property taxes generated by the completed Project is \$13.7 million, and

WHEREAS, termination of the OPA would leave the future of the Property and the Project uncertain; now, therefore,

Based on the foregoing recitals and the documentation presented to the Oakland Oversight Board at a public meeting, the Oakland Oversight Board does resolve as follows:

SECTION 1. The Oakland Oversight Board finds and determines that the proposed amendments to the OPA as approved by ORSA will be of benefit to the taxing entities that will reap substantial additional property taxes from the Property, and that

the proposed amendments under such conditions and yielding such benefits will best maximize the value of the Property for the taxing entities.

SECTION 2. The Oakland Oversight Board hereby approves the action of the ORSA board authorizing the ORSA Administrator to negotiate and enter into an amendment to the OPA with SKS consistent with the terms of this Resolution, and consistent with all applicable laws, to

- (1) extend the date on which SKS must start Project construction by two years, from June 25, 2013, to June 25, 2015, and the date by which it must complete Project construction by two years, from April 27, 2015, to April 27, 2017;
- (2) give SKS an option to extend the new construction commencement and completion dates by an additional 24 months at no cost to SKS; and
- (3) extend the deadlines for submission of final construction plans, the construction contract, and the financing plan to ORSA until such dates as deemed appropriate and reasonable by the ORSA Administrator or her designee such that SKS is able to meet the commencement and completion deadlines above.

SECTION 3. The Oakland Oversight Board requires that the amendment to the OPA, shall be reviewed and approved as to form and legality by ORSA and Oversight Board General Counsel prior to execution by ORSA, and shall be placed on file with the ORSA Secretary.

ADOPTED, OAKLAND, CALIFORNIA, _____, 2013

PASSED BY THE FOLLOWING VOTE:

AYES- CARSON, GERHARD, LEVIN, ORTIZ, QUAN, SMITH, TUCKER

NOES-

ABSENT-

ABSTENTION-

ATTEST: _____
SECRETARY, OAKLAND
OVERSIGHT BOARD