



EXECUTIVE SUMMARY

HOUSING COMMISSION EXECUTIVE SUMMARY SHEET

MEETING DATE: May 31, 2022

HCR22-088

SUBJECT: Mariner's Cove Letter of Intent for Third Amended and Restated Lease

COUNCIL DISTRICT(S): 2

ORIGINATING DEPARTMENT: Real Estate Division

CONTACT/PHONE NUMBER: Emily S. Jacobs (619) 578-7423

REQUESTED ACTION:

Recommend authorizing the execution of a non-binding Letter of Intent (LOI) to enter into a Third Amended and Restated Lease (TARL) with the Lessee, Lincoln Mariners Associates Limited, at a subsequent date for Mariner's Cove on terms and conditions referenced within this report, and approve a resolution to forward this matter to the Housing Authority of the City of San Diego for action pursuant to San Diego Municipal Code Section 98.0301(e)(2)(A) because the proposed action is a substantial proposal to potentially add 272 units, composed of 266 new market-rate units and six new units at or below 60 percent of San Diego's Area Median Income (AMI). These new units are in addition to the 500 units that currently exist on the property, which will be demolished and replaced with new units constructed as part of the project. The affordability on the 500 units being demolished and replaced with new units will be the same as currently exists, which is 200 market-rate units, 200 units at 120 percent of AMI and 100 units at or below 80 percent of AMI.

EXECUTIVE SUMMARY OF KEY FACTORS:

- In December of 1982, the Housing Authority and the current Lessee's predecessor entered into a 55-year ground lease for approximately 30.21 acres of land in the Midway area of the City of San Diego, located within Council District 2.
- Under the terms of the ground lease, the Lessee was to construct 100 rental units affordable to households with income up to 80 percent of San Diego's Area Median Income (AMI), 200 units affordable up to 120 percent of AMI, and 200 market-rate units. The ground rent payable to the Housing Commission as the administrative agent of the Housing Authority was 6 percent of the gross income of the project and was approximately \$500,000 per year.
- A Second Amended and Restated Lease (SARL) was executed in 2015, with a requirement for the Lessee to complete \$25 million in improvements to the property by July 1, 2021. This was extended to July 1, 2022, because of the proposal to potentially demolish all of the units and construct 772 new units on the property.
- After substantial negotiations, the parties agreed to tentative deal points for a non-binding LOI to enter into a TARL at a subsequent date, even though not all of the deal points have been agreed to and are being submitted to the Housing Authority for direction. The execution of the LOI and subsequent TARL are subject to the approval of the Housing Commission Board and the Housing Authority.
- A full listing of conditions for the non-binding LOI is in Attachment 1 to the staff report.
- The approval of this matter will continue to provide affordable and workforce housing within Council District 2 until the end of 2070, potentially to the end of 2090, if the 20-year option to extend is exercised. There will be 772 new units constructed on the site, if the TARL is executed.



REPORT

DATE ISSUED: May 27, 2022

REPORT NO: HCR22-088

ATTENTION: Chair and Members of the San Diego Housing Commission
For the Agenda of May 31, 2022

SUBJECT: Mariner's Cove Letter of Intent for Third Amended and Restated Lease

COUNCIL DISTRICT: 2

REQUESTED ACTION

Recommend authorizing the execution of a non-binding Letter of Intent (LOI) to enter into a Third Amended and Restated Lease (TARL) with the Lessee, Lincoln Mariners Associates Limited, at a subsequent date for Mariner's Cove on terms and conditions referenced within this report, and approve a resolution to forward this matter to the Housing Authority of the City of San Diego for action pursuant to San Diego Municipal Code Section 98.0301(e)(2)(A) because the proposed action is a substantial proposal to potentially add 272 units, composed of 266 new market-rate units and six new units at or below 60 percent of San Diego's Area Median Income (AMI). These new units are in addition to the 500 units that currently exist on the property, which will be demolished and replaced with new units constructed as part of the project. The affordability on the 500 units being demolished and replaced with new units will be the same as currently exists, which is 200 market-rate units, 200 units at 120 percent of AMI and 100 units at or below 80 percent of AMI.

STAFF RECOMMENDATIONS

That the San Diego Housing Commission (Housing Commission) Board of Commissioners (Board) take the following action and recommend that the Housing Authority of the City of San Diego (Housing Authority) take the following actions:

Housing Commission Board

- 1) Approve a resolution to forward this matter to the Housing Authority for consideration pursuant to San Diego Municipal Code Section 98.0301(e)(2)(A) for direction on the terms of the non-binding Letter of Intent (LOI) between the Housing Commission, as the administrative agent of the Housing Authority of the City of San Diego, and Lincoln Mariners Associates Limited, as referenced within this report.

Housing Authority

- 1) Authorize the Housing Commission, as administrative agent of the Housing Authority of the City of San Diego, to execute a non-binding Letter of Intent (LOI) to enter into a Third Amended and Restated Lease (TARL) with Lincoln Mariners Associates Limited (Lessee) at a subsequent date based upon the direction given by Housing Authority on the terms for which direction is sought in this report, in Attachment 1, subject to Housing Authority approval, for Mariner's Cove at 4392 West Point Loma Boulevard, San Diego, 92107.
- 2) Authorize the Housing Commission's President & CEO, or designee, to execute all necessary documents and instruments that are necessary and/or appropriate to implement these approvals,

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in a form and format approved by General Counsel, and to take such actions necessary and/or appropriate to implement these approvals. Housing Commission staff will notify the Housing Authority and the City Attorney's Office about any subsequent amendments or modifications to the transaction, and other required documents, including amendments to any documents.

BACKGROUND

In December of 1982, the Housing Authority and the current Lessee's predecessor entered into a 55-year ground lease for approximately 30.21 acres of land in the Midway area of the City of San Diego, located within Council District 2. Under the terms of the ground lease, the Lessee was to construct 500 rental units. One hundred of the units were the subject of a Project-Based Housing Assistance Payment Agreement (HAP Agreement) with the U.S. Department of Housing and Urban Development (HUD), and these units are occupied by households earning not more than 80 percent of San Diego's Area Median Income (AMI), as established by HUD from time to time. Two hundred units were restricted to occupancy by moderate-income households, earning at or below 120 percent of AMI. The remaining 200 units were to be market-rate rental units. The ground rent payable to the Housing Commission as the administrative agent of the Housing Authority was 6 percent of the gross income of the project and was approximately \$500,000 per year.

In 2010, the Lessee, Lincoln Mariners Associates Limited approached the Housing Commission about acquiring the land upon which the project is constructed. No agreement was reached on selling the land. In 2014, the Housing Commission and the Lessee entered into negotiations to extend the term of the lease. After substantial negotiations, the parties came to an agreement on deal points for an amended and restated lease. The execution of a Second Amended and Restated Lease was subject to the approval of the Housing Commission Board and the Housing Authority. Before the approval of the Second Amended and Restated Lease, the City of San Diego's Office of the Independent Budget Analyst (IBA) reviewed and approved the amendment. The approvals for this Second Amended and Restated Lease (SARL) were granted on May 8, 2015, and June 16, 2015, respectively.

The executed SARL (Attachment 2) required the Lessee to complete \$25,000,000 in improvements to the property by July 1, 2021. This was extended to July 1, 2022, because of the proposal to potentially demolish all of the units and construct 772 new units on the property. As the deadline is approaching, the matter is being brought to the Housing Authority for consideration and direction.

In 2020, the Lessee approached the Housing Commission with a concept of adding additional units to the site. After discussions with the Lessee, the deadline for completion of the improvements was extended to July 1, 2022 as it would not be reasonable to have the property be demolished shortly after the improvements were completed.

If the proposed project is eventually approved, 500 units will be demolished and reconstructed along with the 272 new units. Housing Commission staff is recommending that proposal be presented to the Housing Authority for consideration.

After substantial negotiations, the parties agreed to tentative deal points for a non-binding LOI to enter into a TARL at a subsequent date, even though not all of the deal points have been agreed to and are being submitted to the Housing Authority for direction. The execution of the LOI and subsequent TARL are subject to the approval of the Housing Commission Board and the Housing Authority.

The Housing Commission engaged Keyser Marston Associates, Inc. (KMA) in May 2020 to assist the Housing Commission in determining the estimated land value and annual ground rent supported by the development of the proposed project. Over the past two years, KMA prepared financial models illustrating the financial outcomes of a series of proposals and counterproposals presented by both the Housing Commission and the Lessee. A summary of the negotiations is attached hereto as Attachment 3. KMA also tested alternative inputs/assumptions to evaluate the financial impact of selected deal points. A summary of the financial analyses prepared by KMA is presented in Attachment 4.

Similarly to how the Housing Commission engaged KMA as the financial consultant, the Lessee engaged London Moeder Advisors (LMA) to provide financial analysis from their end. Reports and letters prepared by LMA, the financial advisor for the lessee, are attached as Attachments 5, 6 and 7. The counteroffer by the lessee is attached hereto as Attachment 8.

One of the issues that has not been tentatively agreed by the parties is staff's recommendation per Council Policy 700-10 (Attachment 9) to review the rent every 10 years to ensure the property is paying fair market rent as determined by a financial analysis. On page 11 of 16 of Attachment 9, under subsection G. Flat Rate Leases, the directive involved in this matter is set forth. It provides:

G. Flat Rate Leases

Market Rate Adjustments

Flat rate leases shall provide for upward adjustment of rent every ten (10) years to current fair market rent. In no event shall the adjusted rent be lower than the rent in existence immediately preceding the adjustment.

Consumer Price Index Adjustments

Flat rate leases shall provide for upward adjustment of rent in the interval term between market rate adjustments by changes in the consumer price index. In no event shall the adjusted rent be lower than the rent in existence immediately preceding the adjustment. The index used for consumer price index adjustments will be the All Urban Consumers index for Los Angeles - Riverside - Orange County, California with a base year of 1982-84. If the U.S. Department of Labor indices are no longer published, another substitute index generally recognized as authoritative will be used. Flat rate leases may include pre-determined periodic increases to rent instead of consumer price index adjustments. These periodic increases would occur at least every five (5) years

As previously stated, as the item has not been tentatively agreed upon, staff seeks direction from the Housing Commission Board and Housing Authority on this provision.

Potential Conditions for LOI

The potential conditions for the non-binding LOI for Mariner's Cove, for which directions are being sought by staff, are attached to this report as Attachment 1. The following is a summary of the potential conditions for conditional approval. For a full listing of all the conditions, please refer to Attachment 1.

1. Any agreement concerning the LOI is subject to and contingent upon the subsequent approval of the Housing Commission's President & CEO, the Housing Commission Board, and the Housing

Authority. This LOI is not intended to, and does not, create or constitute a binding agreement between the Housing Commission, the Housing Authority, and the Lessee unless and until all approvals have been obtained.

2. Direct Housing Commission staff to confirm and obtain evidence from the State of California Department of Housing and Community Development (HCD) that the Surplus Land Act does not apply to the amendment of an existing ground lease, where the current affordability of the 500 units does not change in the TARL.
3. Direct Housing Commission staff to submit the feasibility analysis prepared by London Moeder Advisors (LMA) and Keyser Marston Associates (KMA) together with the proposed LOI to the City of San Diego’s Office of the Independent Budget Analyst (IBA) for review and recommendation to the Housing Authority before final approval of the LOI by the Housing Authority and the TARL.
4. As the TARL is being considered for approval based on the feasibility analyses, which rely on assumptions that may not occur during the term of the lease or even before the commencement of the TARL, the parties shall evaluate the situation every 10 years to determine whether the Internal Rate of Return (IRR), which has been estimated before lease commencement based various assumptions, is correct. Should the actual conditions generate returns greater than these projections by an amount or percentage subsequently determined through financial analysis, then the ground rent to be paid to the Housing Commission shall be increased by an amount to be determined in further financial analysis. This process shall be followed every 10th year thereafter in accordance with the provisions of Council Policy 700-10. If the TARL is approved by the requisite entities, including the Housing Commission’s President & CEO, the Housing Commission Board the Housing Authority and the lessee, it shall be effective only if and when the potential project and Final EIR have been approved by the City Council. The TARL shall be subject to reasonable approval by both the Lessee and the Lessor.
5. The lessee has requested that the current CPI increases in the SARL of not to exceed (NTE) 3 percent per year be suspended during demolition and construction of the new project. Staff does not recommend any change in the economic structure of the existing lease, other than the extension of time to invest the \$25,000,000 in the project, referenced above.

PROPOSED UNIT MIX

Unit Type	AMI & Annual Income	# of Units	Gross Rent (Using 2021 Rents)
Studio	60% (currently \$54,660/year for a one-person household)	1	1,274
Studio	Market	78	-----
Studio subtotal		79	
1 bdr	60% (currently \$62,460/year for a two-person household)	2	1,455
1 bdr	80% (currently \$83,300/year for a two-person household)	24	1,940

1 bdr	120% (currently \$102,650/year for a two-person household)	92	2,283
1 bdr	Market	166	-----
1 bdr subtotal		284	
2 bdr	60% (currently \$70,260/year for a three-person household)	2	1,637
2 bdr	80% (currently \$93,700/year for a three-person household)	68	2,183
2 bdr	120% (currently \$115,450/year for a three-person household)	106	2,568
2 bdr	Market	185	-----
2 bdr - mgr		1	-----
2 bdr subtotal		362	
3 bdr	60% (currently \$78,060/year for a four-person household)	1	1,818
3 bdr	80% (currently \$104,100/year for a four-person household)	8	2,425
3 bdr	120% (currently \$128,300/year for a four-person household)	2	2,853
3 bdr	Market	17	-----
3 bdr - mgr		1	-----
3 bdr subtotal		29	
Townhome	Market	18	-----
Townhome subtotal		18	
Total		772	

SURPLUS LAND ACT (SLA)

Analysis of the SLA leads to the conclusion that the proposed transaction is not subject to the provisions of the SLA, which was amended to affect Housing Authorities for the first time in 2019. The instant the SARL, Attachment 2, was executed in 2015, it was not subject to the SLA when it became operative. General Counsel is seeking a confirmation in writing from the California Department of Housing and Community Development (HCD) that this transaction is not subject to the provisions of the SLA. Any action to approve a TARL is expressly contingent upon a verification from HCD that the SLA does not apply to this transaction.

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AFFORDABLE HOUSING IMPACT

With the proposed addition of 272 units, 40 percent of the rental units located on the project will be maintained as low- and moderate-income units until the end of 2070 and potentially to the end of 2090, if the option to extend the lease is timely exercised.

FISCAL CONSIDERATIONS

With approval of the non-binding LOI, the Housing Commission's Fiscal Year (FY) 2022 and FY 2023 budgets will not be impacted. If a TARL is negotiated and approved within the timeline described above, a budget impact will be determined at that time.

HOUSING COMMISSION STRATEGIC PLAN

This item relates to Strategic Priority Area No. 1 in the Housing Commission Strategic Plan for Fiscal Year (FY) 2022-2024: Increasing and Preserving Housing Solutions.

KEY STAKEHOLDERS and PROJECTED IMPACTS

The approval of this matter will continue to provide affordable and workforce housing within Council District 2 until the end of 2070, potentially to the end of 2090, if the 20-year option to extend is exercised. There will be 772 new units constructed on the site, if the TARL is executed.

ENVIRONMENTAL REVIEW

Any approval of the eventual project is subject to the approval of a final Environmental Impact Report (EIR) and the approval of the plans submitted for approval to the City of San Diego's Development Services Department (DSD). Nothing contained in the directions from the Housing Authority concerning the potential project by the Housing Authority, the City of San Diego or the Housing Commission shall impair the right and power of the City of San Diego, the Housing Authority, or the Housing Commission Board from exercising their unfettered legislative discretion in connection with any subsequent decisions concerning the potential project, which are not altered in any way by the actions taken in this report. This action in providing contingent approval of potential changes to the ground lease shall not preclude any mitigation required in the final EIR, including the "no project" alternative. Any proposed lease amendment shall incorporate any and all mitigation measures, if any, required by the Final EIR.

Entering into an Exclusive Negotiation Agreement is not a "project" for the purposes of the California Environmental Quality Act (*Save Tara v. City of West Hollywood* 45 Cal.4th 116.). Similarly providing direction to enter into a non-binding LOI, is also not "a" project. This activity is not a project as defined by the California Environmental Quality Act Section 21065 and State CEQA Guidelines Section 15378(b)(5), as it is an administrative activity of government that will not result in direct or indirect physical changes in the environment because this does not constitute a final approval of the project. Further, any action on a TARL is specifically contingent upon the approval of a Final EIR and approval of the potential project, and action concerning the TARL shall not be heard by the Housing Authority unless and until such Final EIR for the potential project is obtained.

To the extent the activity herein is a project, it is exempt from CEQA pursuant to CEQA Guidelines Section 15061(b)(3) (Common Sense) which states that CEQA applies only to projects that have the potential for causing a significant effect on the environment. The Common Sense Exemption is applicable where it can be seen with certainty that there is no possibility that the activity in question may have a significant effect on the environment. This would not, on its own accord, cause a significant

effect on the environment, because the only action being taken is the potential execution of a non-binding Letter of Intent.

Processing under the National Environmental Policy Act is not required as no funds are involved.

Respectfully submitted,

Emily S. Jacobs
Emily S. Jacobs
Executive Vice President, Real Estate
San Diego Housing Commission

Approved by,

Jeff Davis
Jeff Davis
Interim President & Chief Executive Officer
San Diego Housing Commission

- Attachments:
- 1) Direction Sought from Housing Authority
 - 2) Second Amended and Restated Ground Lease for Mariner's Cove
 - 3) Summary of Developer Negotiations and Financial Analysis
 - 4) SDHC Mariners Cove Analysis
 - 5) LMA Report 12.09.21
 - 6) LMA Report 2.11.22
 - 7) LMA Letter 3.31.22
 - 8) AIMCO Air Mariners Counteroffer
 - 9) Council Policy 700-10
 - 10) Draft SDHC Board Resolution

Docket materials are available in the "Governance & Legislative Affairs" section of San Diego Housing Commission website at www.sdhc.org.