CITY OF OAKLAND

Agenda Report

TO: Office of the City Manager
ATTN: Robert C. Bobb
FROM: Community & Economic Development Agency
DATE: May 26, 1998

RE:

1. **A RESOLUTION APPROVING THE SALE OF REAL PROPERTY LOCATED AT 300 FRANK H. OGAWA PLAZA IN THE CENTRAL DISTRICT REDEVELOPMENT PROJECT AREA BY THE REDEVELOPMENT AGENCY TO ROTUNDA PARTNERS I FOR THE DEVELOPMENT OF THE ROTUNDA BUILDING FOR COMMERCIAL USE**

2. **A RESOLUTION AUTHORIZING THE AGENCY ADMINISTRATOR TO ENTER INTO A DISPOSITION AND DEVELOPMENT AGREEMENT WITH ROTUNDA PARTNERS I FOR THE SALE AND RENOVATION OF THE ROTUNDA BUILDING LOCATED AT 300 FRANK H. OGAWA PLAZA IN THE CENTRAL DISTRICT REDEVELOPMENT PROJECT AREA**

3. **RESOLUTION AUTHORIZING A DEFERRED LOAN NOT TO EXCEED $12,000,000 TO ROTUNDA PARTNERS I TO FUND PREDEVELOPMENT AND CONSTRUCTION COSTS OF THE ROTUNDA BUILDING RENOVATION PROJECT**

TITLE

The purpose of this report is to recommend the adoption of two Redevelopment Agency resolutions and one City Council resolution related to the financing and property disposition for the Rotunda Building Project (the "Project")

In conjunction with this agenda item, a joint Public Hearing of the Oakland City Council and the Redevelopment Agency of the City of Oakland is scheduled which recommends the sale of the Agency owned property to Rotunda Partners I for the development of the Project.

The following resolutions have been prepared:

1. A resolution approving the sale of real property located at 300 Frank H. Ogawa Plaza in the Central District Redevelopment Project Area by the Redevelopment Agency to Rotunda Partners I for the development of the Rotunda Building for commercial use; and

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2. a resolution authorizing the Agency Administrator to enter into a disposition and development agreement with Rotunda Partners I for the sale and renovation of the Rotunda Building located at 300 Frank H. Ogawa Plaza in the Central District Redevelopment Project Area; and

3. a resolution authorizing a deferred loan not to exceed $12,000,000 to Rotunda Partners I to fund predevelopment and construction costs of the Rotunda building renovation project.

EXECUTIVE SUMMARY

Three resolutions have been prepared providing City Council approval to sell the Agency-owned Rotunda Building, authorizing the Agency Administrator to enter into a Disposition and Development Agreement ("DDA") with Rotunda Partners I ("RPI") for the sale and renovation of the Agency-owned Rotunda building located at 300 Frank H. Ogawa Plaza, and authorizing a deferred loan not to exceed $12,000,000 to RPI to fund predevelopment and construction costs of the Rotunda building renovation project.

RPI proposes to rehabilitate the historic Rotunda building into a mixed-use commercial retail and office project. RPI has estimated total project costs to be $32 million and requests that the Oakland Redevelopment Agency ("Agency") provide a deferred loan of $12,000,000 to cover predevelopment and construction costs. The DDA between the Agency and RPI incorporates the terms and conditions under which the Agency will transfer the property and fund the loan (see Attachment A for details). The property would be sold for a purchase price of ninety-nine dollars. The Agency loan will be for a term of 20 years and require no principal or interest payments until the year 2013. Interest from 2013 to 2017 will be paid at 3 percent annually. Upon sale of the building RPI will repay the Agency loan, plus 50 percent of net sales proceeds above $38 million.

FISCAL IMPACT ANALYSIS

The proposed Agency budget for the Rotunda commits a total of $14,205,000 million to the project through Fiscal Year 2000/01, as shown in Attachment B. Budgeted funds consist of a loan of $12.0 million to RPI (an $11.0 basic loan, plus a $1.0 million project contingency), plus an additional $2.2 million that would fund ancillary project costs which the Agency would be expected to undertake. Ancillary expenses include:

1. DDA preparation costs (consulting fees to firms advising the Agency on the transaction);

2. DDA administration costs (the Agency's expenses for overseeing DDA implementation, as well as a contribution to the marketing costs for the project);

3. Public improvements (ancillary construction projects in and around the site, including the stabilization of the north and south walls of the building; parking, sidewalks, and related engineering and construction management); and

4. Ongoing CEDA staff costs.

The approved budget for the Rotunda project during Fiscal Years 1997-99 is $9,112,000, compared with the currently proposed project budget of $14,205,000. Staff proposes that the additional $5,093,000 be funded as follows: $1,600,000 million from the City Center West Garage Reserve; and $3,493,000 million from the Uptown project budget. It is not certain at this time when the Agency will be able to restore funding for the Uptown Project; however, a continued strong economy should produce sufficient tax increment funds to cover existing Agency debt service obligations and provide additional funds for all projects, including replenishing the Uptown Project. Within the next three months, the Agency will work with the Budget and Finance Agency to prepare an up-to-date projection of Agency revenues, and at that time a schedule will be established for reappropriating the funds for the Uptown project.

BACKGROUND AND DISCUSSION

History

Since the Agency purchased the Rotunda Building in November of 1991, there have been numerous efforts to renovate and develop this nationally recognized historic project. Proposed uses have included office space for the City of Oakland, expansion of the Bay Area Rapid Transit District's program, a retail shopping center with an international theme, an office building, a hotel, a High Technology Commercial Center, and the Rotunda Higher Learning and Innovative Technology Center.

In August 1997, a Request for Proposals was published in the Wall Street Journal, and in September three responses were received. On October 28, 1997, pursuant to Agency Resolution No. 97-64 C.M.S., the Agency approved an Exclusive Negotiation Agreement ("ENA") with RPI, a local developer. The ENA specified that the Agency and RPI would work diligently for 120 days to prepare conceptual and schematic design plans for the project; investigate project development costs; secure preliminary leasing commitments from office and retail tenants; evaluate project economics; and negotiate a DDA detailing the terms and conditions for sale and development of the project.

Project Scope and Schedule

RPI has proposed that the project be developed as a mixed-use retail and office complex with approximately 106,000 square feet of retail space, and 130,000 square feet of office use on the upper floors of the building. Project scope will include a complete structural upgrade; retrofit of the building's mechanical, electrical, plumbing, and conveying systems; architectural finishes to all interior and exterior spaces, including the seven-story atrium; and outfitting of tenant spaces for the retail & office uses. The proposed project development schedule is as follows:

• Start Design Development	May 1998
• Complete Construction Documents	September 1998
• Issue Permits, Start Construction	November 1998
• Complete Demolition, Structural, Rough-ins	May 1999
• Complete Core/Shell, incl. Utilities & Finishes	November 1999
• Complete Retail Tenant Improvements; Grand Opening	April 2000
• Complete Office Tenant Improvements & Lease-up	December 2002

Increased Project Cost

Construction Cost. In 1995 and 1996 the Agency contracted with Carey & Co., an architectural firm specializing in historic renovation projects, to prepare a comprehensive analysis of the Rotunda Building, including a Historic Structure Report, an Existing Conditions Report, a Cost Estimate, and other studies related to the development potential of the building. The Carey & Co. Cost Study showed an estimated $16.6 million in construction cost, and a total project cost of $26 million.

During the ENA period, RPI conducted a due diligence review of the building with a team consisting of Architectural Dimensions (architect), Alan Dreyfuss (historic architect), KPa Engineers (structural engineer), and Charles Pankow Builders (construction contractor). The team was charged with preparing schematic designs and cost projections for architectural, structural, electrical, mechanical and plumbing improvements, and an assessment of tenant requirements for outfitting the completed shell space.

Table 1 compares the Carey & Co estimate (July 1996) with the recent RPI estimate (March 1998). The $4.2 million increase derives mainly from increased costs for the structural upgrade, demolition, and architectural core and shell improvements. The current project introduces a new structural design concept with a stiffer frame, consistent with retail requirements. There has also been a more extensive evaluation of the electrical and mechanical requirements, including re-use of existing equipment and systems. By including on the team a general contractor with extensive experience in this type of project, RPI has produced estimates that are more accurate estimates and based on current market costs. It is important to note in this context that construction material and labor costs in the Bay Area have increased significantly since Carey & Company completed their cost evaluation.

Table 1
Construction Cost Estimate Reconciliation ($ thousands)

	Carey & Company July 1996	**RPI March 1998**	**Cost Difference**
Structural	3,413	4,759	1,346
Demolition	50	1,567	1,517
General Core & Shell	2,758	6,296	3,538
Mechanical/Plumbing	2,194	1,921	(273)
Electrical	1,753	2,492	739
General Conditions	998	2,237	1,239
Contingency	4,416	1,000	(3,416)
Escalation	456	0	(456)
Total	**16,038**	**20,272**	**4,234**

Table 2 shows RPI's total estimated project development costs. Nearly $700,000 in value engineering items have been identified which can be eliminated, phased, or altered to save cost.

Table 2
Rotunda Project: Summary Capital Budget ($ thousands)

Item	**Amount**
Construction Costs	20,272
Value Engineering	(672)
Softs Costs	
A&E, Insurance, Legal fees	2,500
Developer Fee	300
Leasing Commissions	1,000
Financing Fees	2,593
Operating Reserves	100
Subtotal	6,500
Tenant Improvements	5,900
Total Project Capital Costs	**32,000**

The current $32 million estimated project cost represents an increase of $6 million over the $26 million estimate supplied by Carey & Co. This increase is proposed to be funded by raising the Agency long term loan from $7.5 million to $11.0 million; by increasing initial developer equity from $3.5 to $4.2 million; and by increasing borrowing from private sources by another $1.8 million.

Table 3 shows the proposed financing structure for the project. During the construction period, the $32 million project cost will be funded through a combination of Developer Equity, Agency Loan, and Construction Loan, plus Cash Flow derived from early retail and office tenancies. Permanent financing will be put in place three years into the project: Historic tax credits of approximately $4.0 million and a conventional take-out loan of $12.0 million will provide new funding, which will be applied to repay the construction loan and reimburse a portion of developer's equity/cash flow contribution. The Agency Long Term Loan will remain in place.

Table 3
Construction and Permanent Financing ($ millions)

	Construction Financing	**Permanent Financing**
Developer Equity	4.2	1.2
Agency Long Term Loan	11.0	11.0
Cash Flow	3.8	3.8
Construction Loan	13.0	0
Historic Tax Credits	0	4.0
Permanent Loan	0	12.0
Total	**32.0**	**32.0**

To evaluate the reasonableness of the proposed deal, the Agency retained Keyser Marston Associates ("KMA"), to test RPI's economic projections and project proforma. KMA has determined that the projected rents ($11/sf for retail and $17/sf for office tenants) are reasonable in the current marketplace, and that a low-interest Agency loan is required because the projected rents are not sufficient to cover the estimated project cost. KMA is also preparing a summary report of the project which is required pursuant to Section 33433 of the California Community Redevelopment Law.

Tenant Issues

During RPI's discussions with prospective retail tenants, the key issues that have emerged are parking, signage, and safety/maintenance.

Parking. The estimated parking requirement is 170 spaces for retail and 180 spaces for office tenants. Although office parking can be at a remove of several blocks from the building, retail parking must be close to the stores. RPI reports that in their discussions with retailers the need for ample parking adjacent to the project has been the retailers' single most critical issue, and may determine the long term success of retail operations in this location. Staff proposes to handle the parking in two phases. Initially, tenants and retail patrons would make use of 117 spaces in the Dalziel Building and 90 spaces on the Agency-owned portions of the surface lot at 16th & San Pablo. Preferential parking rates would be given to Rotunda patrons through a validation program for Rotunda merchants. The validation program would be funded by the revenues from the 16th & San Pablo lot. Within 3-5 years the City would make a good faith effort to develop a 400+ space garage in close proximity to the site, preferably with retail in the ground floor. Development of this garage may be done through a public/private partnership.

Signage. Staff and RPI will work together to accommodate the signage requirements of the tenants, including signage in the vicinity identifying the Rotunda Building. Staff will also coordinate Landmarks Preservation Board review of any signage that is to be attached to the building.

Area Safety/Maintenance. The City has agreed to improve lighting in the area, and has included funding for ancillary public improvements in the Agency budget. City Hall Plaza will be maintained in accordance with a plan under development by Public Works. Policing of the area will receive increased emphasis when the new Administration buildings are online.

Assessment of the Proposed Deal: Risk Analysis

There are several significant risks associated with the proposed development agreement. Staff has worked with RPI to address these risks in a constructive manner so as to protect the Agency's interest in the project, and to enhance the prospects for successful completion and opening.

Potential for cost increases

The Agency retained Advanced Resources for Construction Services (ARCS) to evaluate the construction cost estimate prepared by the RPI team. ARCS identified four key areas of potential cost increases: the upgrade to the building structural system; the reliance on re-use of existing mechanical, electrical and plumbing systems and equipment; construction escalation; and construction contingency. The Agency also asked Keyser Marston Associates (KMA) to evaluate RPI's soft costs; KMA found that architectural and engineering fees, as well as costs for legal service, taxes and insurance were lower than is typical for the industry, and that construction interest costs may have been understated given RPI's assumption that cash flow would be available to fund the later tenant improvement construction. Taken together, ARCS and KMA have advised the Agency that there is a risk that actual cost of this project may be understated by as much as $4 to $6 million which could result in total project development costs of $38 million.

To address the risk of cost overrun, the Agency has incorporated specific provisions in the DDA that:

1. Establish a $1.0 million Agency contingency that can be drawn down for specific purposes (i.e., structural upgrade; Agency-requested change-orders; key tenant inducements; or unforeseen conditions);
2. Require the developer to seek a larger construction loan commitment to allow additional construction contingency funds;
3. Encourage the developer to arrange a potential $2.0 million advance against the Historic Rehabilitation Tax Credits; and
4. Augment the Developer's management team to provide additional administrative and construction management support, to enhance the management of the project.

Need for Funding Commitments

Completion of the construction phase of the project depends on the availability of adequate financing to fund improvements to the building. The DDA stipulates that a fully executed Construction Loan Agreement must be in place, before the Agency will convey the property to the Developer and fund the Agency Loan. Funding of the Agency Loan is also dependent on the Developer establishing an acceptable mechanism for receiving Historic Tax Credits.

Leasing

RPI has attracted significant interest from major retail and office tenants, but has not yet received firm commitments from either retail or office tenants. At this stage of development this is not unusual--however, to ensure that long-term take-out financing will be available when construction is complete, the DDA specifies that signed leases should be in place for one-half of the retail and office spaces, prior to conveyance. If necessary, the Agency is prepared to assist the Developer in attracting tenants, both through the marketing funds established in the project budget, and also, potentially, through selective use of some portion of the Agency's contingency funds.

RECOMMENDATION

Given the long history of the City's attempts to develop the Rotunda Building, the historical value of the building and its prominent location on Frank Ogawa Plaza, and the desire to catalyze development in Uptown, the proposed DDA represents a viable opportunity to complete this project in time to take advantage of the current active real estate market. The sale and development of the Rotunda will leverage significant private financing to restore a building that has been vacant for many years, generate sales and business taxes for the City and the Agency, provide major retail opportunities currently lacking in the Central District, create approximately 150 new retail job opportunities for Oakland residents, and satisfy the City's obligations with regard to the rehabilitation of this historic resource as required by the Environmental Impact Report for the City Center Administration Complex. Therefore, staff recommends approval of the attached resolutions to authorize:

1. the sale of real property located at 300 Frank H. Ogawa Plaza in the Central District Redevelopment Project Area by the Redevelopment Agency to Rotunda Partners I for the development of the Rotunda Building for commercial use; and

2. authorizing the Agency Administrator to enter into a disposition and development agreement with Rotunda Partners I for the sale and renovation of the Rotunda Building located at 300 Frank H. Ogawa Plaza in the Central District Redevelopment Project Area; and

3. authorizing a deferred loan not to exceed $12,000,000 to Rotunda Partners I to fund predevelopment and construction costs of the Rotunda building renovation project.

Respectfully Submitted,

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Interim Agency Director

Prepared by:

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Chief Negotiator

Concurred by:

Roy L. Schweyer
Chief of Projects

Attachments

APPROVED FOR FORWARDING TO
THE COMMUNITY AND ECONOMIC
DEVELOPMENT COMMITTEE

Robert C. Bobb
Agency Administrator

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