



FEBRUARY 6, 2007

SUBJECT: Approval of Amended and Restated Disposition and Development and Owner Participation Agreement with Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company)

REPORT IN BRIEF

Staff is recommending that the Agency Board approve the Amended and Restated Disposition and Development and Owner Participation Agreement (ARDDOPA) with Downtown Sunnyvale Mixed Use LLC (New Developer), a joint venture of RREEF and Sand Hill Property Company.

On April 27, 2004, the Agency selected Fourth Quarter Properties XLVIII, LLC, a development entity formed by Forum Development Group and Lehman, ALI, as the master developer for the City's Downtown Center redevelopment project. After negotiations, Fourth Quarter Properties XLVIII, LLC agreed to a Disposition and Development and Owner Participation Agreement (DDOPA) for redevelopment of the Town Center Mall (Town Center) property with the Sunnyvale Redevelopment Agency (Agency). In early 2006, however, Fourth Quarter missed and failed to correct several construction milestones and the Agency found Fourth Quarter in default and gave notice that it intended to exercise a purchase option for the Town Center property. On October 2, 2006, Fourth Quarter Properties requested permission from the Agency to transfer the project to RREEF America III (RREEF) and Sand Hill Property Company. Under the terms of the DDOPA, the Agency can approve or disapprove the transfer in its discretion. Staff utilized ten criteria to evaluate the ability of RREEF/Sand Hill to successfully complete the redevelopment project. On December 12, 2006, the Redevelopment Agency Board gave preliminary approval, with conditions, to the request of Fourth Quarter Properties XLVIII, LLC, to transfer the project to the New Developer. This preliminary approval started a 60 day period, which expires on February 10, 2007, to complete conditions required for the final transfer approval.

Redevelopment Agency staff and RREEF/Sand Hill Property Company have been working diligently to complete the negotiations and planning review required prior to the February 10, 2007, deadline. This report presents the Amended and Restated Disposition and Development and Owner Participation Agreement with Downtown Sunnyvale Mixed Use LLC. This report recommends that the Redevelopment Agency enter into the attached Amended and Restated

Disposition and Development and Owner Participation Agreement (ARDDOPA)
with Downtown Sunnyvale Mixed Use LLC.

The ARDDOPA will require Downtown Sunnyvale Mixed Use LLC, among other things, to: demolish the Mall and the former J.C. Penney building; construct and operate an open-air mixed-use development containing retail, office and residential uses; build, maintain, repair and replace public parking structures; build, maintain, repair and replace designated public streets; and build and maintain a "Redwood Square" of at least 33,000 square feet. The ARDDOPA provides for Downtown Sunnyvale Mixed Use LLC to receive payments equal to all of the net new secured property tax generated by this specific development ("project tax increment") up to a cumulative annual cap of \$4.5 million, plus 50% of any amount over \$4.5 million until 2026. The ARDDOPA provides for an exchange of land in equal amounts between the developer and the Agency, such that the Agency will own the land under the public streets and public parking structures.

The ARDDOPA with Downtown Sunnyvale Mixed Use LLC has some significant changes from the DDOPA with Fourth Quarter. The Agency has added a more aggressive construction schedule, with new financial penalties of \$167,000/month if the project is not timely completed. The ARDDOPA also includes as an attachment the site plan with changes including the addition of a grocery store, minor changes to street locations to improve traffic flow, lowering the movie theatre, and changes to the location of some retail and offices to enhance the Project appearance. The ARDDOPA has added provisions acknowledging that Target will be building a new store as part of the redevelopment of the Town Center. Sections of the original DDOPA were amended to support the financial feasibility of the Project; these changes increase the annual increment cap to \$4.5 million, reduce the Minimum Project size based on current plans and allow for phasing of the Project with the initial retail and residential buildings delivered for tenant improvements by March 31, 2009. Finally, recently discovered environmental conditions will require an additional environmental due diligence period prior to closing.

Downtown Sunnyvale Mixed Use LLC has met all December 12, 2006, conditions for approval of the ARDDOPA within its control and has agreed to an accelerated construction schedule with penalties for non-performance. The remaining conditions – final RREEF investment committee approval, Reciprocal Easement approval by Macy's and Target, and closing of the property transaction with Fourth Quarter – have been diligently pursued by Downtown Sunnyvale Mixed Use LLC and are anticipated to be completed promptly after Agency approval of the new ARDDOPA (which is effective only upon the closing of the property transaction). During the New Developer's due diligence investigation, it located several areas of possible environmental contamination which have been addressed in the ARDDOPA.

Staff recommends that the Agency board approve the ARDDOPA with Downtown Sunnyvale Mixed Use LLC. The ARDDOPA will become effective on the closing of the property transaction between Fourth Quarter and Downtown Sunnyvale Mixed Use LLC, no later than April 15, 2007. This approval will allow the redevelopment of the Downtown Center Project to continue with a new developer that presents the best opportunity for the timely and successful completion of the Sunnyvale Downtown.

BACKGROUND

Formation of Sunnyvale Redevelopment Agency

The Sunnyvale Redevelopment Agency was established pursuant to provisions of the community redevelopment laws of the State of California by a resolution of the City Council on November 19, 1957. The Agency has only one redevelopment project, the 184 acre Central Core Redevelopment Project. Under California law, redevelopment agencies have two powers not otherwise available to cities:

- Power to acquire property for the purpose of resale to a private developer, utilizing eminent domain if necessary.
- Tax increment financing, whereby all increases in property tax (including portions that would normally go to the county, school districts and special districts) flow to the redevelopment agency for the sole purpose of paying back funds borrowed for land acquisition and public infrastructure improvements.

The primary activity of the Agency since its formation has been to assist in the development of the Town Center Mall. On March 1, 1978, the Agency entered into a Construction, Operation and Reciprocal Easement Agreement (REA) with Mall developer Sunnyvale Town Center Associates (a limited partnership formed by Ernest W. Hahn, Inc.), Macy & Co., and Montgomery Ward; in 1992, the REA was amended to include J.C. Penney. Among the obligations of the Agency through the REA was the responsibility to construct the parking deck along Mathilda Avenue.

In 1977, \$16,800,000 of tax allocation bonds were sold to fund the acquisition of property, relocation, demolition and public improvements. Sunnyvale Town Center Associates subsequently purchased a portion of the site from the Agency for \$5,500,000. The bonds were twice refinanced. The current outstanding balance of the bonds is \$7,105,000. The debt service is fully covered by current tax increment receipts; the debt is scheduled to be retired in 2023.

Also in 1977, two issues of lease revenue bonds totaling \$22,300,000 were sold to construct the parking deck along Mathilda Avenue. These bonds were twice refinanced. The current outstanding balance of the bonds is \$13,400,000. The debt service is fully covered by the Agency's current tax increment receipts; the debt is scheduled to be retired in 2023.

In addition, there is an outstanding loan from the General Fund of approximately \$54 million not including bonded indebtedness.

History of the Downtown Mall

Town Center Mall opened on September 26, 1979. After years of successful operation, Sunnyvale Town Center Associates decided to sell the property. On July 9, 1998, American Mall Properties (AMP) became the new owner. AMP proposed to expand the Mall, by adding 205,000 square feet of new retail space in an outdoor appendage extending to Mathilda Avenue along the McKinley Avenue alignment (extended); it also proposed to add an entertainment component in the form of a 4000-seat, 20-screen movie theater. On March 11, 1999, the City Council approved the expansion plans of AMP, and on December 3, 1999, the REA was amended to accommodate the AMP expansion plan. A major part of the amendment dealt with a land "swap" between the Agency and the developer, wherein the Agency deeded to the developer 5.33 acres of property, including certain properties fronting on Mathilda Avenue and approximately 1/3 of the parking deck centered roughly along the alignment of McKinley Avenue (extended); the developer deeded to the Agency 4.07 acres of property on the Sunnyvale Avenue side of the property where two new parking structures were planned, and paid the Agency \$1,495,000, for the difference in the amount of land exchanged. (This amounted to approximately \$27/sq.ft. for the 1.29-acre difference in the land exchange.)

In late 2002, American Mall Properties completed construction of the public parking structure at Sunnyvale and Iowa. AMP was unable to proceed with implementation of the approved project due to difficulties in signing retail leases and bankruptcy of their primary lender, Finova. On September 24, 2002, AMP filed for bankruptcy protection. On June 2, 2003, the Chief Building Official ordered that the second level of the parking deck along Mathilda Avenue be closed for safety reasons. Attorneys for AMP immediately filed papers with the Agency, alleging that the Agency is responsible, under the REA and a related Parking Lease Agreement, for the repair and replacement of the parking structure. The Department of Public Works estimated that it would cost \$15 million to replace the deck in kind (because the Agency owns only approximately 2/3 of the structure, its share of the replacement cost would be about \$10 million). Such reconstruction, however, would be contrary to the desire of the developer and of the City to extend McKinley Avenue into Block 18; the more appropriate replacement of 2,400 parking spaces in an above ground structure would cost more than \$30 million.

On December 2, 2002, in recognition of the many challenges facing the redevelopment of Block 18 (which challenges included multiple ownership of significant parcels within the block, the deteriorated condition of the parking deck, and the bankruptcy and closure of the Mall), the Agency designated all of Block 18 (except for the Bank of the West property) as a Master Development Area, and directed staff to solicit proposals from owners of property in the Master Development Area. One proposal was received from Fourth Quarter Properties XLVIII, LLC. The Agency acted on April 27, 2004, to select Fourth Quarter Properties as Master Developer for the subject site. Staff was directed to negotiate a business agreement whereby the project could be successfully developed.

Disposition, Development and Owner Participation Agreement with Fourth Quarter

In March, 2003, the Agency Executive Director (City Manager) appointed a negotiating team for the Agency consisting of Robert Paternoster, Director of Community Development; Mary Bradley, Director of Finance; Jerry Keyser, Agency consultant in real estate economics; and Lee Rosenthal, Agency redevelopment counsel. The Agency set forth three major initial parameters or objectives for the negotiations:

1. To minimize risk for the Agency and the City

The Agency did not want a repeat of the present situation, where the Agency is still paying back loans for the development of a Mall which has since closed.

2. To recreate as much of the historic public street grid as possible

The Agency wanted to integrate the project into the historic downtown by extending public streets through the project, but desired no additional on-going cost to the City for maintenance and repair of the streets and other infrastructure.

3. To get out of the parking business

The Agency wanted no responsibility for building, maintaining, repairing and replacing public parking facilities, noting the present problems with deterioration of the parking deck along Mathilda Avenue.

In subsequent meetings with the negotiating team, the Agency added three other parameters or objectives:

4. None of the new sales tax generated by the project and other revenues flowing to the City's General Fund should be committed to the developer to support the project, although the Agency and City were willing to

consider investing in the project an amount equal to some portion of the new project-generated secured property tax which flows to the Agency (the "project tax increment").

5. Any increase in project tax increment beyond what is reasonably required in exchange for public facilities should be shared equally between the Agency and the developer.
6. The developer should place underground as much parking as is feasible.

Those negotiations produced the original 2004 Disposition and Development and Owner Participation Agreement with Fourth Quarter Properties. The DDOPA included a site plan for the Town Center Project with specific housing, retail and office requirements and limits that were also reflected in City approval of a Special Development Permit (SDP) for the project. The DDOPA also set out deadlines for the completion of the planning, permitting and construction of the Town Center Project.

Fourth Quarter Default And Preliminary Transfer Approval To RREEF/Sand Hill Property Company

Fourth Quarter Properties appeared to be making a good-faith effort to meet the DDOPA deadlines through 2005, and completed the scheduled demolition of the damaged parking structures in the fall of 2005. Unfortunately, Fourth Quarter Properties missed subsequent deadlines for the submission of construction plans and commencing construction. The Redevelopment Agency first gave notice of the missed deadlines on February 2, 2006, and the City Attorney issued a Formal Notice of Default and Opportunity To Cure Default on March 8, 2006. Fourth Quarter Properties contended that the missed deadlines were due to events beyond its control and extensive efforts to reach a negotiated cure of the DDOPA defaults were unsuccessful. Consequently, the Redevelopment Agency notified Fourth Quarter Properties on August 9, 2006, that Sunnyvale intended to exercise its right under the DDOPA to purchase the Town Center property owned by Fourth Quarter Properties for fair market value based on the continuing default. Fourth Quarter Properties continues to dispute that it was in default under the DDOPA and litigation would be required to establish the Sunnyvale Redevelopment Agency's right to purchase the Town Center property.

On October 2, 2006, Fourth Quarter Properties proposed transferring the Town Center Project to a new developer as an alternative to litigation. The DDOPA allows Fourth Quarter Properties to transfer the project, but only with the prior written approval of the Redevelopment Agency, which can be granted or withheld in the Agency's discretion. Fourth Quarter Properties proposed a transfer of the Town Center Project to RREEF, a large real estate investment trust, which would develop the property in joint venture with Sand Hill

Property Company, a local developer. To allow the Redevelopment Agency the ability to adequately evaluate RREEF/Sand Hill, the parties negotiated an Evaluation Agreement executed on October 23, 2006, to “conduct a thorough due diligence review of the Proposed Developer, so that (the Agency) may evaluate and decide whether the Proposed Developer is qualified to take over the Project.” The Evaluation Agreement required both Fourth Quarter Properties and RREEF/Sand Hill to provide extensive information including the transfer agreement, structure of the RREEF/Sand Hill Partnership, management teams, relevant project experience, financial structure and backing, financial spreadsheets, tenant information, and design and construction partners.

On December 12, 2006, the Agency approved the preliminary transfer of the Town Center Project to RREEF/Sand Hill subject to these conditions:

1. Agency approval of and RREEF America, LLC agreement to execution of amendments to the DDOPA implementing any Agency-approved changes to the Approved Plan.
2. Agency approval of and RREEF America, LLC agreement to execution of amendments to the DDOPA implementing a new schedule for performance of Developer obligations under the DDOPA.
3. Agency approval of and RREEF America, LLC agreement to execution of amendments to the DDOPA implementing a system of financial penalties designed to encourage Developer performance under the DDOPA and to compensate the Agency and City from revenue lost as a result of delay in performance.
4. Conveyance by Fourth Quarter Properties LLC to RREEF America, LLC of all Town Center Project property owned by Fourth Quarter Properties LLC and development by joint venture comprised of RREEF/Sand Hill Properties.
5. Assignment by Fourth Quarter Properties LLC, in a form acceptable to the Agency, of its rights and obligations under the DDOPA and any other relevant agreement concerning the development and operation of the Town Center Project.
6. The above conditions to be completed within 60 calendar days following Agency Board action in approving the transfer (unless such time is extended by mutual agreement of the Agency, Fourth Quarter Properties LLC and RREEF America, LLC).

Council designated City Manager Amy Chan as principal negotiator, with legal support from City Attorney David Kahn and staff support from Community Development Director Robert Paternoster. Extensive negotiations over the last four weeks resulted in a Restated and Amended Disposition and Development Owner Participation Agreement that preserved the important business deal points in the prior DDOPA with Fourth Quarter and resulted in the negotiation of some additional business deal points based on certain improvements to the site plan, requested amendments by both the Developer and Agency, and significantly increased project costs. This Report on the Amended and Restated Disposition and Development and Owner Participation Agreement is before the Agency Board and City Council. The City Council is considering at the same meeting the revised site plan and Special Development permit, a request for initiation of a General Plan amendment, and a construction mitigation plan.

EXISTING POLICY

Implementation Plan, Sunnyvale Central Core Redevelopment Project:

Goal 1 Meet the Agency's Existing Financial and Administrative Obligations.

Objective 1.5 Continue to invest in downtown and encourage and nurture private investment in commercial developments.

Goal 2 Establish the downtown as the cultural, retail, financial and entertainment center of the community, complemented by employment, housing and transit opportunities.

Objective 2.1 Establish a 24-hour downtown with Class A office buildings around a vibrant retail district with easy parking and public transportation and easy access from a variety of housing types.

Objective 2.2 Continue public/private partnerships in the development of office, retail, housing, hotel and open space facilities.

Objective 2.3 Create a unique shopping, dining, entertainment experience in Downtown, combining new restaurants with small shops, major retail stores and theatre with easy, available parking and strong pedestrian connections to other parts of the Downtown.

Goal 3 Implement Specific Actions such as the Provisions of Public Improvements in an attractive and cohesive physical form, which clearly identifies Sunnyvale's downtown.

Objective 3.2 Complete priority streetscape projects to facilitate an attractive pedestrian environment and to promote development on adjacent parcels.

Goal 4 Development and implementation of an overall parking strategy that meets the needs of retail, office, housing and visitor demand

Objective 4.1 Implement overall parking strategy that optimizes parking use based on office, retail, and entertainment peaks.

Objective 4.2 Replace existing public parking as required.

Goal 5 Increase housing opportunities.

Objective 5.2 Encourage mixed housing consisting of market rate and affordable housing in appropriate locations on transit corridors in or near the downtown.

Downtown Specific Plan:

Goal B. Establish the Downtown as the cultural, retail, financial and entertainment center of the community, complemented by employment, housing and transit opportunities.

Policy B.3.

Improve the Town Center area by reinforcing connections into and through the mall and improve the quality of the tenant mix and the mall's physical environment

Land Use and Transportation Element:

Action Statement C1.2.1 Promote Downtown as a unique place that is interesting and accessible to the whole City and the region.

Policy N1.12

Permit more intense commercial and office development in the downtown, given its central location and accessibility to transit

Action Statement N1.12.1 Use the Downtown Specific Plan to facilitate the redevelopment of downtown.

Socio-Economic Element:

Goal 5.1C Endeavor to maintain a balanced economic base that can resist downturns of any one economic sector

Policy 5.1C.

Support efforts to establish Sunnyvale's downtown area as a strong commercial center for the city.

Community Development Strategy Goals:

Tax Base: to retain and attract businesses which will provide a stable tax base to support City services

Retail Services: to retain and attract businesses which provide a variety of needed retail services for our residents at locations which are convenient for them.

DISCUSSION

Summary of Amended and Restated Development, Disposition and Owner Participation Agreement With Downtown Sunnyvale Mixed Use LLC

The Amended and Restated Disposition and Development and Owner Participation Agreement (ARDDOPA) is the legal agreement between the Redevelopment Agency and Downtown Sunnyvale Mixed Use LLC which provides for the redevelopment of Block 18 of the Downtown Specific Plan. It provides the mechanism for property transfers between the Agency and the developer, for construction by the developer of specified public and private improvements which constitute the project, and for certain payments to the developer to support the construction of the public improvements.

The team on the transfer from the Agency consists of City Manager Amy Chan and City Attorney David Kahn, supported by many City staff, spent many hours meeting and negotiating with the Developer. The negotiating team met frequently during the course of the negotiations with the Redevelopment Agency in Closed Session to provide status reports on the negotiations and to obtain authority from the Agency Board on negotiating points. The proposed business deal in the ARDDOPA meets the parameters and objectives set forth by the Agency. In sum, the ARDDOPA is similar to the original DDOPA, but makes changes to entitlements for restaurant space, reduces the height of the theatre, improves traffic flow, modifies the Minimum Project to reflect current plans, acknowledges the proposed new Target store, and has a revised construction schedule with financial penalties for missing deadlines. It also increases the annual cap on tax increment to \$4.5 million to reflect significant increases in construction and other costs since 2004.

The main elements of that agreement incorporated from the 2004 DDOPA are as follows:

- The New Developer will demolish the Mall and the former J.C. Penney building. Macy's and Target will remain on their parcels, as will the new parking structure at Sunnyvale and Iowa Avenues. (The Mathilda parking garage was demolished by the prior developer.)
- The New Developer and the Agency will exchange land of approximately equal area¹ and equal value as shown in Attachment

¹ The ownership delineated in the Tentative Map shows that the Agency actually comes out slightly ahead in the land swap, with a net increase of approximately 4,445 square feet.

A. The Agency will obtain fee title to the land where the public parking structures are located (excepting that area of the parking structures over which private residential units are developed), and to all of the land under the new street grid, guaranteeing that the public will have perpetual control over these rights-of-way.

- The New Developer will build, maintain, repair and replace all parking structures. A minimum of 4,950 parking spaces will be provided (inclusive of the private parking spaces for the residential units), 1,112 of which will be underground. The long-term financing for the parking structures will be, at the developer's option, either private or Mello-Roos financing.²
- The New Developer will build, maintain, repair and replace all public streets in Block 18. The developer will also construct all sidewalks within the block and along the adjacent streets which bound the block; these sidewalks will be consistent with the Downtown streetscape standards, including new street lights, decorative paving, benches, waste receptacles, and street trees in decorative grates.
- The New Developer will construct and maintain a "Redwood Plaza" of at least 33,000 square feet around the six heritage redwood trees, and make it available at no cost to the City for public events up to 15 times per year. The square is intended to remain open to the public at all times.
- The developer will establish a private security force to provide security and traffic control for the project, such that the Department of Public Safety will not be required to provide routine patrol, but will respond to emergencies, crimes in progress and other events that are beyond the scope of routine patrol.
- Upon approval of the City Council of a Special Development Permit, the Developer will build, lease and operate a mixed-use, open-air development consisting of approximately 992,000 sq. ft. of retail (including a 2,624 seat movie theater complex, the existing Macy's

² This special financing, authorized by the State, can provide a lower interest rate to the developer. The developer would pay the debt service through a special tax on its property, which will be the sole collateral for the loan. The City and the Agency would bear no financial risk or obligation for payment of debt service. Should the property owner fail to pay the special tax for debt service on the bonds, the City may be obligated to participate in an accelerated foreclosure process on behalf of the bond holders. City costs for this process are ultimately recoverable from the developer.

and new Target store), and 275,000 sq. ft. of office; and will build up to 292 for-sale housing units.

- The Developer is required to be supportive of the existing Downtown business community and residents, and to minimize negative impacts of construction activity upon these businesses and residents. Specifically, the developer is required to meet at least monthly with Downtown businesses and residents during construction, and to prepare and implement a construction mitigation program which will prescribe construction truck travel routes, location of construction worker parking, enforcement mechanisms to keep workers and suppliers out of retail customer parking spaces, and signs indicating that stores are open for business during construction. The developer and his contractors are also required to meet regularly with a representative of the City to facilitate coordination with City agencies and to resolve construction issues affecting Downtown businesses and residents. The developer is required to make good faith efforts to attract local merchants to lease spaces in the new development. The developer is also required to be supportive of a business improvement or property improvement district, if one is formed to support Downtown businesses, and to work with the Downtown business community in producing special events, programs and advertising to promote the entire Downtown area.
- In consideration for the above and, in particular, for replacing the Agency's Mathilda Avenue parking deck, for placing a substantial amount of the new parking underground, and for constructing, repairing and replacing public streets and other public amenities, the developer will receive annual payments³ from the project tax increment. The project tax increment is the increase in secured property tax generated by the development over and above the existing secured property tax (2003-2004 secured tax roll) which comes to the Agency after deduction of required set asides and payments to other taxing entities. The annual payments will be made for each year between the base year of 2003-2004 until November 26, 2026; however, no funds will be payable to the developer until the first year after completion of the project. The estimated present value of this tax increment in 2004 was approximately \$39.5 million and is

³ The annual payment will initially come from the City (by way of lease payments under the Public Parking City Lease) and will be made from revenues the City receives from the Agency for repayment of past City loans to the Agency. Once those loans are repaid, the annual payment will be made directly by the Agency with tax increment funds. By using the existing loans from the City as the vehicle for making the annual payment, the Agency avoids encumbering new debt that would trigger set asides which would reduce the available tax increment. No City General Funds will be used to make the annual payment.

now approximately \$43 million. To protect against an unanticipated windfall to the developer in the event the assessed value rises more rapidly than projected, the payments are limited to a cumulative cap of \$4.5 million/year, plus an amount equal to 50% of any tax increment in excess of this limit. This cap is an increase from the 2004 cap of \$4.050 million per year because of the increased costs of construction and related costs since 2004. The Agency should receive as much or more tax increment under this raised cap, however, as under the prior cap.

The ARDDOPA includes the preceding elements of the original DDOPA. It also sets forth new performance criteria for the developer, in the form of specific milestones which must be achieved or penalties will be triggered. Key milestones are

- Commencement of demolition and excavation by October 15, 2007.
- Substantial completion of demolition and excavation by December 31, 2007.
- Substantial completion of all structural systems (for minimum project) by December 31, 2008.
- Delivery of completed retail building shells (for minimum project) to tenants for tenant improvements by March 31, 2009.
- The former DDOPA provided that the Agency remedy for default was termination of the agreement or an option to purchase the property at fair market value. An important new provision of the ARDDOPA is the addition of significant financial penalties⁴ if the Developer fails to timely complete the milestones and minimum project. (The Minimum Project for purposes of liquidated damages is the retail on McKinley to Murphy Avenue and retail surrounding Redwood Plaza.)

As part of the transfer negotiations, Downtown Sunnyvale Mixed Use LLC has maintained the concept approved in 2004 by the City and Agency for the Downtown Center project while proposing some changes to the layout and allocation of new space. These changes have been reviewed by the City and Agency and are recommended where determined that they are consistent with the original project and either do not change or significantly improve the project, or are required for reasonable construction scheduling. These approved changes have been incorporated into the ARDDOPA and include:

⁴ Penalties of \$167,000 per month up to \$5 million dollars are imposed if the project is not completed on time. There are also penalties for missing the excavation and structural steel completion deadlines.

- New site plan with improved public street layout and circulation.
- Addition of new one-level Target store with associated parking.
- Change in Minimum Project (for receipt of tax increment) to 300,000 square feet of new retail, 130,000 square feet of new office, and 200 housing units.
- Increase in restaurant space from 70,000 square feet to 90,000 square feet.
- 1,112 fully underground parking spaces and 4,950 (subject to traffic study) total parking spaces.
- Other clarifying and administrative amendments.

The ARDDOPA requires that all contractors and subcontractors pay prevailing wages, pursuant to Labor Code Sections 1720 and regulations of the California Department of Industrial Relations.

A copy of the ARDDOPA accompanies this report. The ARDDOPA incorporates a number of exhibits and legal documents, including:

- Public Street and Utility Maintenance Agreement: providing for the developer to operate and maintain the publicly owned streets, sidewalks and utilities within the boundaries of the project.
- Public Parking Easement: providing for the City's ability to use and control the public parking structures for dedicated public parking.
- In accordance with Section 33433 of the California Health and Safety Code, the Agency is required to prepare a report to inform the public about the terms of the land transfers proposed in the DDOPA. Attachment C to this document is a copy of the required report.

Agency Business Objectives Achieved in the ARDDOPA

The proposed business deal in the ARDDOPA achieves the objectives of the Agency. Paramount among these is the minimization of risk to the Agency and the City. Under this agreement, the Agency and the City will borrow no money (no new debt), will construct no streets, parking facilities or other infrastructure, and will assume no additional responsibility for infrastructure maintenance, repair or replacement. The developer assumes:

- Construction cost risk

Because the developer is designing and constructing all improvements, including all public streets and public parking structures, the developer will be responsible for cost overruns.

- Financing risk

Because the developer is financing the construction of all of the improvements, the developer assumes the risk that interest rates and other borrowing terms will become less desirable in the future.

- Performance risk

The amount of secured property tax increment generated by the project is dependent upon the developer's performance in building a center of high value and maintaining that value through proper leasing and operation. Because the annual payments to the developer are based only on the amount of secured tax increment which the project actually generates each year (i.e., the Agency does not guarantee the developer any specific amount), the risk for performance rests with the developer. This is particularly important should the project close down, as is the present case with the Mall.

- Responsibility for maintenance, repair, and replacement

The agreement places sole responsibility for maintenance, repair and replacement of the parking facilities and of all of the public streets upon the developer.

All of the sales tax revenue generated by the development will go to the General Fund. This represents new General Fund revenue for the City of approximately \$2.0 million per year when the project is completed.

The ARDDOPA imposes one major financial responsibility upon the Agency and the City: to return to the developer a major portion of the secured property tax increment that the project generates through 2026. In 2004, it was estimated that the project would result in a \$4.0 million plus increase in the tax increment received by the Agency each year. The City pledged to return up to \$4,050,000 of the increment received each year to the developer, plus 50% of any tax increment income over that amount, in return for the developer's assumption of all financial responsibility to construct, maintain and replace public streets and public parking, much of which would be placed underground at the City's request at considerable increased cost. At that time, it was estimated that the present value of the tax increment which would be returned to the developer through 2026 was \$40 million, with the Agency realizing increased tax income with a present value of about \$1.4 million. In light of the increased cost of construction since 2004, which results in a higher

assessed value of the project, the current estimate of annual tax increment generated by development of the project is \$4.7 million. To maintain the economic feasibility of the project, the ARDDOPA now allows up to \$4.5 million of the increment received each year to be returned to the developer, resulting in a present value of \$43 million through 2026. The estimated present value of the Agency's share is \$1.7 million, which actually exceeds the amount anticipated in the original business agreement.⁵ The amount of tax increment returned to the developer is limited by the actual tax increment generated by the project; in no case is the City obligated to provide funds to the developer in excess of the tax increment which the development project actually generates.

A copy of the Amended and Restated Disposition and Development and Owner Participation Agreement is attached to this Report as Exhibit A.

Alternative To Approval Of Amended and Restated Disposition and Development and Owner Participation Agreement (ARDDOPA):

If the Agency does not approve the ARDDOPA and related Project transfer documents to Downtown Sunnyvale Mixed Use LLC, the Project reverts to the same status it was in on October 11, 2006. The City Attorney issued a Formal Notice of Default and Opportunity to Cure Default on March 8, 2006. Fourth Quarter Properties contended that the missed deadlines were due to events beyond its control and extensive efforts to reach a negotiated cure of the DDOPA defaults were unsuccessful. Consequently, the Redevelopment Agency notified Fourth Quarter Properties on August 9, 2006, that Sunnyvale intended to exercise its right under the DDOPA to purchase the Town Center property owned by Fourth Quarter Properties for fair market value based on the continuing default. Fourth Quarter Properties continued to dispute that it was in default under the DDOPA. Litigation would be required to establish the Sunnyvale Redevelopment Agency's right to purchase the Town Center property, or the Agency could elect to continue with the redevelopment of the Town Center with Fourth Quarter as the developer.

Status of December 12, 2006, Conditions for Transfer

The ARDDOPA, with the changes agreed to by Downtown Sunnyvale Mixed Use LLP, satisfy conditions 1, 2 and 3 from the December 12, 2006 preliminary transfer. It addresses the conditions of the revised Agency-approved site plan, a new construction schedule, and financial penalties for non-performance.

Condition 4 requires the transfer of the Town Center Property to a RREEF/Sand Hill Properties joint venture. The joint venture, Downtown Sunnyvale

⁵ It should be noted that the City also anticipates receiving, as a result of the increased cost and complexity of the project, development impact fees, permit fees and other charges totaling \$14.6 million, compared to an estimated \$7.2 million for the original project in 2004.

Mixed Use LLC, has been established. There is a Purchase and Sale Agreement providing for the closing of the property sale and the Developer has invested significant capital in engineering and construction plans. RREEF's representative states that closing is subject to final approval by the RREEF investment committee, after Agency approval of the ARDDOPA. The investment committee has been kept regularly informed of the status and economics of the Project. RREEF has advised that the closing date is no later than April 15, 2007. There remain title issues that the City and Fourth Quarter have been cooperating to fix but still require action by the bankruptcy court prior to the closing of the property sale. We anticipate the title issues will be completed in advance of the closing date.

Condition 5 requires City Attorney review of the proposed form of assignment from Fourth Quarter to Downtown Sunnyvale Mixed Use LLC. The assignment form has been reviewed and approved and Condition 5 is satisfied.

Condition 6 requires the five prior conditions to be completed within 60 days of preliminary approval on December 12, 2006 (which is February 10, 2007), unless time is extended by mutual agreement. The Agency, City, and Developer have worked diligently to complete what is normally many months of planning, drafting and negotiations in less than 60 days. Accordingly, Conditions 1-3 and 5 and the joint venture requirement of Condition 4 have been completed within the 60 day period. The remaining condition of completion of the closing of the property sale from Fourth Quarter to Downtown Sunnyvale Mixed Use LLC could not be completed prior to the approval of the ARDDOPA on February 6 and the ARDDOPA is conditioned on closing of the property transaction no later than April 15, 2007, unless extended for good cause.

Environmental Contingency Condition

The New Developer conducted environmental testing on the Project site as part of its due diligence prior to acquisition. Its test results showed evidence of some contamination in certain locations on the site. The Agency conducted independent tests and confirmed the presence of contamination. Because it is impossible to determine the exact source of the contaminants and both the Agency and Developer property have potential sources, the Agency and New Developer, as part of the ARDDOPA, have allocated responsibility for any required cleanup 50-50, with a cap on the Agency's contribution of \$1 million and no cap on the New Developer's contribution. Because new environmental data was received as late as January 30, and additional testing is required to determine the final cost of cleanup, the ARDDOPA provides for an additional period of due diligence no later than April 15, 2007, prior to New Developer's closing of the property transaction with Fourth Quarter during which both the Agency and New Developer can perform additional testing and request re-

negotiation limited to the allocation and Agency cap for environmental clean-up costs.

FISCAL IMPACT

Approval by the Agency of the Amended and Restated Disposition and Development and Owner Participation Agreement requires no expenditure of funds by the City of Sunnyvale General Fund. The Redevelopment Agency will incur the financial obligation of the transfer to the developer of all project-generated secured property tax increment between the base year of 2003-2004 and November 26, 2026, up to a cumulative maximum of \$4.5 million per year and 50% of tax increment above \$4.5 million with the Agency receiving the other 50%. These funds do not exist today, and will become available only when a project is developed and the assessed value increases. These funds go to the Redevelopment Agency and can be used only to support the Central Core Redevelopment Project.

The completed project is estimated to generate \$2.0 million per year in new sales tax for the City’s General Fund. The New Developer will also pay one-time construction taxes, permit fees, utility connection fees, impact fees and other charges to the City of approximately \$13 million dollars.

The Project will result in no net increase in infrastructure cost to the City. The developer will be required, through the Amended and Restated Disposition, Development and Owner Participation Agreement and the Conditions of Approval of the Special Development Permit, to construct at its cost all public streets and sidewalks within the Project, and to improve all affected intersections adjacent to the Project. Sidewalk improvements will be made along Mathilda, Washington, Sunnyvale and Iowa, including enhanced paving, new streetlights, benches, and street trees with ornamental grates. Unlike most other public infrastructure, the developer will also be required to repair and replace all streets, utilities and sidewalks within the boundaries of its project.

In addition, the project will contribute to provision of public infrastructure on a city-wide basis through the payment of impact fees, approximated as follows:

Traffic impact fee	Approximately \$1.9 million
Park Dedication fee	Approximately \$2.3 million

The Developer will also pay the Sunnyvale School District and Fremont Unified High School District impact fees of approximately \$1.6 million for the residential units.

With regard to ongoing service costs to the City, both Public Works and Parks and Recreation estimate that there will be no or minimal increases in demand

for general City services. Due to potential higher activity in the entire new downtown, public safety estimated service level increase requirements of approximately \$1 million dollars. The City's utility rates for water, sewer, and refuse will cover all ongoing costs for these services on a full cost recovery basis.

Environmental cleanup issues discovered during the due diligence period will require funding. The Agency has committed a cap of \$1 million dollars toward its share of cleanup costs, and this amount could be renegotiated either up or down based on additional environmental findings prior to the closing. The Agency's potential share of cleanup costs could, in a worst case scenario, be approximately \$2.5 million dollars.

ENVIRONMENTAL REVIEW

A Mitigated Negative Declarative (MND) was prepared for the Town Center Mall Redevelopment Project, tiered off the 2003 Final EIR for the Downtown Improvement Program Update. The MND evaluates site specific environmental impacts of the Special Development Permit and the Disposition and Development and Owner Participation Agreement that were not evaluated in the EIR. The City Council adopted the MND for Fourth Quarter site plan and DDOPA on August 17, 2004. Since the ARDDOPA has substantially the same environmental impacts as the prior plan, no additional environmental review is required. An addendum to the MND will be prepared if required after completed environmental testing but no changes to the environmental impacts are anticipated.

PUBLIC CONTACT

On February 2, 2007, this report and the recommended Amended and Restated Disposition and Development and Owner Participation Agreement were made available to the public at the Department of Community Development, the City Clerk's Office and the Library; in addition, they were posted on the City's Web site. The Council agenda was posted on the City's official notice bulletin board. Although earlier availability would have been preferable, the extremely tight timelines for moving this project forward between the Council's preliminary approval on December 12, 2006, and the February 6, 2007, final approval date precluded this as negotiations on the Project continued until February 1, 2007.

On January 20 and 24, 2007, two Community Meetings were held at the Senior and Community Centers to provide an opportunity for the public to ask questions regarding the proposed development plan and ARDDOPA. They were held at 9:00 a.m. and at 7:00 p.m. City staff from involved departments and representatives of the developer and financing group were present to explain the plans and documents and to answer questions.

ALTERNATIVES

1. Approve Resolution authorizing the Agency Executive to execute the Amended and Restated Disposition and Development and Owner Participation Agreement With Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company).
2. Approve the Resolution authorizing the Agency Executive to execute the Amended and Restated Disposition and Development and Owner Participation Agreement With Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company) as revised by the Agency.
3. Do not approve the Resolution authorizing the Agency Executive to execute the Amended and Restated Disposition and Development and Owner Participation Agreement With Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company) and direct staff to return to the October 11, 2006 status with Fourth Quarter Properties, Inc.

RECOMMENDATION

Staff recommends Alternative No. 1, Approve the Amended and Restated Disposition and Development and Owner Participation Agreement With Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company).

On December 12, 2006, Council gave preliminary approval to the transfer of the Downtown Center Project and DDOPA from Fourth Quarter Properties to RREEF/Sand Hill Property Company contingent on the completion of conditions requiring revisions of the DDOPA, site plan and construction/penalty schedule acceptable to the Agency.

The Council found on August 17, 2004 that the project and the DDOPA were consistent with the goals and objectives of the Implementation Plan for the Sunnyvale Core Redevelopment Project, as set forth in the Existing Policy section of this report. Staff finds that the project and ARDDOPA continue to be consistent with these goals and objectives, and that site plan modifications by Downtown Sunnyvale Mixed Use LLC improve the overall project.

Staff also believes that the development plan submitted by Downtown Sunnyvale Mixed Use LLC Properties will achieve the vision of the 2003 Downtown Specific Plan: to create “an enhanced, traditional downtown serving the community with a variety of destinations in a pedestrian-friendly environment”. The isolation of an interior-oriented mall is replaced by an open-air project on public streets which recreate much of the original street grid, thereby integrating the new development with the historic downtown. This redevelopment should have the positive spin-off effect of stimulating substantial redevelopment and property improvements elsewhere in

Downtown. At the request of the Agency, the developer has made all of the housing units for-sale, placed approximately 20 percent of the parking underground and agreed to construct a town square as part of the project. The developer has also agreed to take all responsibility for construction, maintenance and replacement of public streets, utilities and parking structures, completely removing the City and the Agency from the “parking business.”

An independent analysis in 2004 by Keyser Marston Associates of the projected income and costs to a developer has indicated that these public facilities and maintenance requirements add significant cost to the project and make it economically infeasible without financial support from the Agency. The public facilities and ongoing repair and maintenance obligations by the developer, together with the developer’s proposal to rebuild a substantial portion of Downtown Sunnyvale, support the proposed payments based on project generated secured tax increment. These funds will be paid to the Agency only when and if the project is developed; no new tax increment will exist if the Mall is not redeveloped.

The important provisions in the DDOPA approved by the Council in 2004 with Fourth Quarter are maintained in the ARDDOPA with Downtown Sunnyvale Mixed Use LLC. The Agency is not required to acquire property or to assume additional debt, and is not guaranteeing to the developer any minimum annual payment. The City is not required to commit monies from the General Fund. The financial, construction, and performance risk is assumed by the developer. The development will create below market rate housing units and generate tax increment funds to be set aside, in accordance with State law, for construction of affordable housing. There is no cost to the City or Agency for construction, maintenance and repair of new infrastructure and parking facilities within the Project boundaries. Cost to the City for infrastructure improvements surrounding the property are less than \$1.0 million. In addition, the City’s General Fund will benefit from an estimated \$2 million per year in new sales tax revenue.

Furthermore, the ARDDOPA adds additional provisions to the agreement between the Agency and Developer that are to the Agency’s advantage. The ARDDOPA includes an aggressive construction schedule, with financial penalties if milestones and completion are missed.

Therefore, staff recommends that the Agency adopt Alternative 1.

Prepared by:

David Kahn
General Counsel, Redevelopment Agency

Reviewed by:

Robert Paternoster,
Secretary, Redevelopment Agency

Mary Bradley
Treasurer, Redevelopment Agency

Approved by:

Amy Chan
Executive Director, Redevelopment Agency

Attachments:

- A – Amended and Restated Disposition and Development and Owner Participation Agreement with Downtown Sunnyvale Mixed Use LLC (RREEF and Sand Hill Property Company)
- B – Resolution of Agency Board approving the Disposition and Development and Owner Participation Agreement and authorizing the Executive Director to sign the Agreement.
- C – Resolution of City Council approving the Disposition and Development and Owner Participation Agreement and authorizing the City Manager to sign the Agreement.