



DATE: August 9, 2019

TO: City Finance Committee

FROM: Block 88 Negotiating Team

RE: Block 88 Air-Rights Negotiation Progress Report

**Introduction:**

The City's Block 88 Negotiating Team has continued to work with Gebhardt Development to negotiate a development agreement for the Block 88 air-rights. On Monday, August 12<sup>th</sup>, the negotiating team will meet with the Finance Committee on the status of the negotiations. This summary memo outlines the key issues and choices to be discussed with Committee. The key deal points for deliberation on Monday are:

1. *Strategy to achieve the affordable housing units.* In response to the feedback to July 8<sup>th</sup> progress discussion with the Finance Committee, Gebhardt Development has developed three options to disperse the affordable units throughout the building instead of placing the affordable unit on three floors of the building as a separate condominium unit. The options are reviewed in this memo and the negotiating team seeks direction from the Finance Committee on which strategy to pursue.

2. *Strategy to achieve the Podium/Garage structural modifications to accommodate the proposed air-rights development.* At the July 8<sup>th</sup> progress discussion, the original proposal for CLT (mass timber) construction was determined to be infeasible for, primarily, timing reasons due to fact that CLT is not yet a component of the State Building Code. The construction technique to be used for the air-rights component has a direct impact on the cost of the project, the proceeds to be received by the City for the air-rights and the timing of the opening for the City's new underground garage on Block 88. This issue is previewed in this memo and the negotiating team is seeking guidance on the relationship between the affordable housing cost, financial return to the City on the purchase of air rights and the timing to open the municipal garage on Block 88.

**Strategy to Achieve the Affordable Housing Units:**

The City of Madison uses a variety of types of subsidies to allow landlords to reduce their rents to levels that are affordable to low-income households. Without subsidy, new construction housing (particularly projects located in desirable infill locations) have to charge rents targeted at middle and upper income

households to cover the cost of land, construction, and financing. The City has two funding sources to support the construction of new affordable housing units:

- Federal Funds
  - HOME, CDBG, etc
  - Supports units designated for households earning up to 80% of AMI
  - Relatively constrained amount of funds
  - High compliance requirements
  - Typically offered only to non-profit developers
  - Too late in process to use for Block 88
  
- Affordable Housing Fund
  - Funded through the closure of TIF districts and General Obligation Debt
  - Annual allocation of \$4.5 million, with roughly \$1.75 million currently anticipated for Block 88
  - Has supported, though not by ordinance, units designated for households earning not more than 60% of AMI
  - Typical allocation of \$20-30K per unit targeted at a combination of 30%, 50%, and 60% of AMI units
  - Paired with Park Impact Fee waiver which is available, by ordinance, only for units designated for households earning up to 60% of AMI
  - 30-year period of affordability, by policy if AHF used, and by ordinance, if park impact fee waiver is claimed

Given the constraints of the project, the City has planned on using the Affordable Housing Fund which is designed to be compatible with other non-city funding sources to reduce the city contribution per unit or to allow our funding to reach lower income households. These capital funding stacks can take a few different forms:

- 9% Low Income Housing Tax Credits
  - Administered by WHEDA and IRS
  - Can pay for more than 50% of cost of construction
  - Mixes incomes (30, 50, 60% of AMI and some market rate)
  - Highly competitive, annual funding cycle, very long time to close on financing
  - Not feasible with the Block 88 timeline
  
- Low-Income Housing Loans
  - Ex. WHEDA 7/10
  - Offer below market interest rates or longer amortization to reduce monthly loan payments
  - Typically require 20% of units to serve 80% of AMI
  - Does not supply a deep subsidy to reach 60% of AMI

- 4% Tax Credits
  - Administered by WHEDA and IRS
  - Can pay for around 30% of cost of construction
  - Typically targets 60% of AMI units
  - Not competitive, continuous funding, moderate time to close
  
- 100% City Subsidy
  - No outside subsidy
  - Flexible terms
  - City assumes all compliance responsibility
  - Requires much higher levels of City support for comparable levels of affordability

Given the timeline and complexity of the Block 88 transaction, Gebhardt has proposed options that utilize the 4% tax credit program or 100% city subsidy to provide units that are affordable to low-income households.

- Original Proposal - Pursue 4% Tax Credits
  - \$1.75 million in City subsidy
  - 78 units at 60% AMI
  - Consolidate affordable units on three floors
  - Potential for 30+ year affordability through non-profit ownership
  - Affordability compliance through WHEDA, IRS, and City
- Option 1 – 100% City Subsidy on 62 Units at a 60%, 70%, and 80% AMI Mix
  - \$2.32 million in City Subsidy
  - 30 units at 60%, 16 units at 70%, 16 units at 80% AMI
  - Dispersed affordable units throughout building
  - Would require departure from City policy to offer AHF funds only for units below 60% AMI
  - Park impact fee waiver not available for 70% and 80% AMI units
  - 30-year affordability
  - Affordability compliance burden falls on City
- Option 2 – 100% City Subsidy on 40 Units at a 60% AMI
  - \$2.45 million in City Subsidy
  - 40 units at 60% AMI
  - Dispersed affordable units throughout building
  - 30 year affordability
  - Affordability compliance burden falls on City
- Option 3 – 100% City Subsidy on 78 Units at a 60% AMI Mix
  - \$4.15 million in City Subsidy
  - 30 units at 60%, 16 units at 70%, 16 units at 80% AMI
  - Dispersed affordable units throughout building
  - Would require departure from City policy to offer AHF funds for units below 60% AMI
  - Park impact fee waiver not available for 70% and 80% AMI units
  - 30-year affordability
  - Affordability compliance burden falls on City

Each of the four options presents a tradeoff between cost to the City, number of affordable units, and the desire to disperse affordable units throughout the building.

**Strategy to Achieve the Podium/Garage Structural Modifications:**

The cost of the modifications to the Podium/Garage structure that will be needed to accommodate the air-rights development was estimated at \$2,078,000 in the Gebhardt proposal and would be a deduction from the gross purchase proceeds being paid to the City. This cost element is very important to thoroughly understand given the significant impact it has on the net proceeds the City will receive for the purchase of the air-rights and the Podium.

Since the initiation of negotiations, Gebhardt's designer (Iconica) has produced more detailed structural load calculations for the air-rights development and the City's structural engineer for the Podium/Garage has reviewed the resulting structural modifications that would be needed to accommodate the air-rights development. This more detailed analysis has concluded that the scope of the required structural modifications to the ramp to bear the weight and wind loads of the post-tensioned (PT) concrete frame has increased along with the cost of those modifications. In addition, it became clear that the opening of the City's new municipal garage on Block 88 would have to be delayed for up to six months in the worst case scenario to allow for the structural modifications to be made.

Upon recognition of these issues, the City negotiating team asked Gebhardt/Iconica to consider the use of a lighter construction method, Cold Formed Steel Framing (CFSF), to reduce the in-place weight of the proposed air-rights development and minimize the required structural modifications to the Podium/Garage structure and its resulting cost to the City. CFSF is steel stud framing that has been previously used on mid-rise developments of nine to ten stories. Iconica has used this method for the seven-story wing at 306 West Apartments on South Henry and West Main Streets in downtown Madison. A case study of CFSF's use at City Green apartment project in Milwaukee, completed in 2007, can be found at [https://sfia.memberclicks.net/assets/CaseStudies/city-green\\_web.pdf](https://sfia.memberclicks.net/assets/CaseStudies/city-green_web.pdf). For the Block 88 project, the east half of the Gebhardt development above the Podium could potentially be post-tensioned concrete frame and the west half could potentially be CFSF or a combination of PT and CFSF.

According to the Steel Framing Industry Association, CFSF provides cost efficiencies, durability, and sustainability, is non-combustible and resilient, and is easy to install. CFSF has the highest strength to weight ratio of any building materials and has a proven track record of providing cost-effective benefits over the entire construction cycle due to shorter project cycles, predictability and accuracy of steel components, and improved design efficiency. CFSF contains at least 25% recycled steel (and often more than 70% recycled steel) and meets the highest sustainability requirements of all major green building standards and rating programs. CFSF is resistant to extreme environmental and seismic loads making it one of the most resilient building materials available. CFSF is light, making it easy to ship, handle, and assemble. CFSF wall and floor sections can be assembled off-site in a controlled environment, which can minimize costly weather delays and ensure greater quality.

Further analysis is needed to confirm the preliminary assumptions that this new approach will reduce the impact of the air-rights development on the Podium/Garage, including potential cost reductions and minimizing possible delays to opening the Block 88 garage. The City negotiating team will continue to keep the Finance Committee apprised of progress on this issue.

	Gebhardt Proposals					
	Original Proposal	Affordable Housing Options			Mandel Group	Stone House
		Option 1	Option 2	Option 3		
Podium Purchase Price	\$ 7,541,825	\$ 7,541,825	\$ 7,541,825	\$ 7,541,825	\$ 5,700,000	\$ 5,000,000
Podium Alterations	\$ (2,078,000)	\$ (2,078,000)	\$ (2,078,000)	\$ (2,078,000)		
Net to City	\$ 5,463,825	\$ 5,463,825	\$ 5,463,825	\$ 5,463,825	\$ 5,700,000	\$ 5,000,000
Affordable Housing Fund	\$ 1,750,000	\$ 1,750,000	\$ 1,750,000	\$ 1,750,000	\$ -	\$ 600,000
60% Affordable Units	78	30	40	78	-	20
70% Affordable Units	-	16	-	-	-	-
80% Affordable Units	-	16	-	-	29	17
Market Rate Units	119	135	157	119	115	122
Total Units	197	197	197	197	144	159
Retail SF	7,845	7,845	7,845	7,845	7,000	7,000
Commercial SF	22,600	22,600	22,600	22,600		
Total Project Budget	52,569,307	49,977,787	49,934,642	49,743,315	38,200,000	40,000,000
Projected Assessment*	40,000,000	42,500,000	42,400,000	40,000,000	28,000,000	29,000,000
Est. Tax Credit Proceeds	4,754,008					
NPV of Decreased Revenue over 30 Years**		(2,115,524)	(2,331,272)	(4,146,922)		
Park Fees***	(452,200)	(657,400)	(596,600)	(452,200)		
Projected Gap from Original Proposal****	0	(570,724)	(725,672)	(2,396,922)		

Stone House proposal reflects RFP revisions included in May 16th presentation to Finance Committee

Mandel Group proposal reflects RFP revisions in May 28th memo to George Austin, including \$1.5 million upfront payment and lease payments with NPV in year 10.

Gebhardt Notes:

\*Gebhardt Affordable Housing Options Projected Assessments provided by developer

\*\*Developer estimate using discount rate of 6% and 2% annual inflation factor

\*\*\*Park Impact Fees are reduced for each affordable unit.

\*\*\*\*Gap to be filled for the developer to have no effect from original proposal over a 30-year period due to reduced rents associated with affordable units.