



MEMORANDUM

TO: Members, Capital Planning Committee

FROM: Elaine Forbes, Port of San Francisco, Executive Director

SUBJECT: Resolution Authorizing the Issuance of Development Special Tax Bonds – City and County of San Francisco Special Tax District No. 2020-1 (Mission Rock Facilities and Services) - Not to Exceed Aggregate Principal Amount of \$50,100,000

Resolution Authorizing a Pledge Agreement Related to City and County of San Francisco Infrastructure Financing District No. 2 (Port of San Francisco) Sub-Project Areas I-1 through I-13 and Special Tax Bonds Issued by City and County of San Francisco Special Tax District No. 2020-1 (Mission Rock Facilities and Services)

DATE: November 9, 2020

Recommended Action

We respectfully request that the Capital Planning Committee review and consider for recommendation to the Board of Supervisors (“Board”) the resolution authorizing the issuance of not to exceed \$50,100,000 aggregate principal amount of Development Special Tax Bonds for City and County of San Francisco Community Special Tax District No. 2020-1 (Mission Rock Facilities and Services) (“Mission Rock CFD”) (“Bond Resolution”) and the resolution authorizing the Pledge Agreement between the Infrastructure Financing District No. 2 (Port of San Francisco) Sub-Project Areas I-1 through I-13 (“IFD Project Area I”) and the Mission Rock CFD (“Pledge Agreement Resolution”).

Executive Summary

On January 30, 2018, the Port Commission approved a mixed-use development project known as Mission Rock at Seawall Lot 337 and Pier 48 (“Project” or “Mission Rock Project”). Subsequently, on February 13, 2018, the San Francisco Board of Supervisors (“Board”) approved the Project and on August 15, 2018 the Port and Seawall Lot 337 Associates signed all Project-related documents. The Port owns the land in the Project and leases it for development.

The Port’s partner for development of the Project is Seawall Lot 337 Associates, LLC (“Developer”), an affiliate of the San Francisco Giants and Tishman Speyer. The Disposition and Development Agreement

("DDA") and related agreements between the Port and the Developer govern the Project's development.

The entitled Mission Rock Project anticipates up to 1,200 units of new rental housing including 40 percent affordable units, 1.4 million square feet of new commercial and office space, rehabilitation of historic Pier 48, space for small-scale manufacturing, retail and neighborhood services, waterfront parks, and public infrastructure. The Mission Rock Project is located at SWL 337 and Pier 48 bound by China Basin Channel, Third Street, Mission Rock Street, and San Francisco Bay.

The Project, now on the precipice of construction, represents 11 years of effort, led by the Port Commission, Port and City staff, and the Developer. These efforts include state legislation; neighborhood planning and neighborhood outreach; infrastructure planning and design; shoreline and sea level rise resiliency planning; development of a Special Use District; and successful collaborations with regulators and partner agencies related to topics like workforce development, affordable housing, transportation, public access, and park development.

Proceeds from the issuance of bonds issued by the City and paid with revenues from financing districts formed within Seawall Lot ("SWL") 337 will fund the horizontal infrastructure improvements. In 2018, the City formed Project Area I of Infrastructure Financing District No. 2 (Port of San Francisco) at SWL 337 ("IFD Project Area I"), and in 2020, the City formed Special Tax District No. 2020-1 (Mission Rock Facilities and Services) ("Mission Rock CFD"). It is intended that the proposed financing ("Bonds") will utilize both funding sources, with the City issuing the Bonds on behalf of the Mission Rock CFD, which are primarily secured by special taxes levied in the Mission Rock CFD. To the extent sufficient tax increment is generated in IFD Project Area I, it will be used as an offset against the primary pledge of special taxes (tax increment will become available to service debt when the assessed value of the Project increases in an amount sufficient to generate \$100K of tax increment in a Sub-Project Area as a result of completed development).

The Mission Rock CFD will finance certain improvements through the levy of special taxes on the leasehold interests in the Project, while the IFD Project Area will finance improvements through the growth of tax increment in the assessed value of such leasehold interests.

STRATEGIC PLAN

This item and the Mission Rock Project as a whole support the efforts of the Port's Strategic Plan to enhance and balance the Port's maritime and economic purpose, rich history, and changing relationship with the City so the waterfront continues to be a treasured destination.

PROJECT BACKGROUND

On January 30, 2018, the Port Commission approved a mixed-use development project known as Mission Rock at Seawall Lot 337 and Pier 48 ("Project" or "Mission Rock Project"). Subsequently, on February 13, 2018, the San Francisco Board of Supervisors ("Board") approved the Project and on August 15, 2018 the Port and Seawall Lot 337 Associates signed all Project-related documents. The Port owns the land in the Project and leases it for development.

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FINANCING BACKGROUND

On September 20, 2019, the Port Commission approved the Phase 1 Budget of the Project, which outlined the expected costs and revenue sources for the phase improvements. The Phase 1 budget included:

- **Project Costs.** Projected hard costs, soft costs, and return on Developer equity for the Phase 1 Horizontal Infrastructure improvements.
- **Pro Forma Project Revenues.** Sources include:
 - The four Phase 1 prepaid leases
 - Public financing sources including Mission Rock CFD bond proceeds (including the proposed Bonds), Mission Rock CFD pay-as-you-go (“pay-go”) special taxes (those not dedicated to bond debt service), and IFD Project Area I pay-go tax increment

Broadly, the DDA requires the Developer to build horizontal improvements and the Port to reimburse the Developer for horizontal expenses from available sources. Available sources include proceeds from transactions of the Port’s land within the project area (“Development Rights Payments”), special taxes from the Mission Rock CFD, and tax increment from IFD Project Area I. In addition to reimbursement for horizontal improvement expenses, the Port must also reimburse the Developer for an 18 percent return on its project investment. Table 1 below summarizes the Phase 1 budget sources and uses.

Table 1. Phase 1 Overview of Sources and Uses (\$ millions)*

Description	Entitlement	Phase 1	Total Phase 1
Uses			
Total Horizontal Costs	29.3	145.4	174.8
Developer Return*	<u>16.9</u>	<u>73.8</u>	<u>90.7</u>
Total Phase 1 Uses	46.2	219.3	265.5

Sources			
Net Development Rights Payments Advances	42.2	-	42.2
CFD Bonds - Unimproved Land	4.0	31.2	35.2
CFD Bonds - Completed Buildings	-	140.8	140.8
Excess Pay Go Tax Increment	-	47.2	47.2
Total Phase 1 Project Sources	46.2	219.3	265.5

**Numbers are rounded and thus may not appear to sum precisely.*

The Board passed an ordinance establishing IFD Project Area I on February 27, 2018, which the Mayor signed on March 6, 2018.

On April 14, 2020, the Board passed a resolution approving the formation of the Mission Rock CFD. The Mayor signed this resolution on April 24, 2020. On May 5, 2020, after a public hearing and landowner vote, the Board approved a resolution determining a not to exceed limit on bonded indebtedness and other debt of \$3,700,000,000 for the Mission Rock CFD, which the Mayor signed on May 15, 2020. Finally, the Board passed an ordinance levying special taxes within the Mission Rock CFD on May 12, 2020, which was signed by the Mayor on May 22, 2020 (“Ordinance 79-20”).

IFD Project Area I generates revenues for the Project by capturing the tax increment generated by application of the 1% ad valorem tax to increases in the assessed value of the taxable leasehold interests in the Project above the value in the base year of 2017-2018. Tax increment may begin to be allocated to the IFD from each Sub-Project Area when the amount of increment available to be allocated from the Sub-Project Area in the fiscal year is equal to at least \$100,000.

The Mission Rock CFD includes four separate special taxes:

1. **Development Special Tax** – funds horizontal infrastructure on the site; expected 45-year life. The financing plan for the Project assumes that, over time, the City will not need to levy the Development Special Tax to pay debt service because it will be offset by tax increment generated in IFD Project Area I.
2. **Office Special Tax** – funds horizontal infrastructure on the site; 120-year life
3. **Shoreline Special Tax** – a source for ongoing shoreline protection studies and facilities; Shoreline Taxes from Phase I can also fund horizontal infrastructure on the site; 120-year life
4. **Contingent Services Special Tax** – funds ongoing maintenance and services of the area if the Homeowners’ Association dues do not fund these services

The proposed Bonds will only be secured by the payment of Development Special Taxes. No other Mission Rock CFD special taxes will be pledged to the repayment of the Bonds. However, the IFD Project Area I tax increment will provide an additional security for the Bonds, as discussed below.

Mission Rock CFD Special Tax Bonds

The proposed Bond Resolution would authorize the first sale of special tax bonds for the Mission Rock CFD, in an amount not to exceed \$50,100,000. The proposed Bonds will be secured by a pledge of the Development Special Tax levied on taxable leasehold interests in the Mission Rock CFD in accordance with Ordinance 79-20 and the Rate and Method of Apportionment of Special Taxes for the Mission Rock CFD (“RMA”) adopted at formation.

Bond Security and Pledge of Tax Increment

The proposed Bond financing will be payable from both the Mission Rock CFD and IFD Project Area I sources. The Development Special Tax is the only Mission Rock CFD special tax that will be pledged to debt service on the Bonds; the Bonds will not be payable from any of the other three Mission Rock CFD special taxes listed above. As additional security, the Bonds will also be payable from tax increment generated in IFD Project Area I. The proposed structure allows tax increment generated in IFD Project Area I to “offset” the Development Special Taxes. The offset increases the value of the Port’s land by reducing the long-term tax burden on the site. Under this offset structure, tax increment from one year acts as a credit for the next year’s Development Special Tax obligation once the developed property is assessed. Table 2 below illustrates a simplified example of the relationship between Development Special Taxes and tax increment generated in IFD Project Area I.

Hypothetical (for informational purposes only). In Year 1, the property lessee owes Development Special Taxes and ad valorem property taxes. The IFD tax increment generated in early years will not act as a credit until the property meets certain milestones, which are assumed to occur in Year 2. In Year 2, the lessee owes both Development Special Taxes and ad valorem property taxes. The IFD Project Area I tax increment generated in Year 2 now serves as a credit for Development Special Taxes in Year 3. In Year 3, the lessee continues to pay ad valorem property taxes but receives a credit for the Development Special Taxes that would otherwise be levied from the prior year’s IFD Project Area I tax increment (they can only receive a credit up to the maximum Development Special Tax). In Year 4, the lessee owes ad valorem property taxes but again receives the benefit of the prior year’s IFD Project Area I tax increment as a full credit offset for the Development Special Taxes that otherwise would be levied. This pattern will continue for the life of the Development Special Tax and IFD Project Area I, assuming no changes to the property. Depending on the timing of development, the assessment of properties, the real estate market, and other factors, the offset may not occur until a later year and may also not fully offset the Development Special Tax.

Table 2. Mission Rock CFD Offset Structure

	Year 1	Year 2	Year 3	Year 4
Development Special Tax	1,000,000	1,000,000	1,000,000	1,000,000
IFD Project Area I Tax Increment	400,000	1,100,000	1,100,000	1,100,000
Offset to Development Special Tax	0	0	(1,000,000)	(1,000,000)
Total Taxes	1,400,000	2,100,000	1,100,000	1,100,000

*Arrows show the Tax Increment from the previous year acting as a credit to the Development Special Tax.

To ensure tax increment from IFD Project Area I is available to pay debt service on the on the proposed Bonds, the Bond Resolution and the IFD Pledge Agreement Resolution approve a form of Pledge Agreement, pursuant to which the IFD Project Area I pledges to pay tax increment for debt service on the Bonds. Therefore, once the Mission Rock properties are assessed, the ongoing tax increment from IFD Project Area I will be pledged to fund debt service payments on the Mission Rock CFD special tax bonds (including the Bonds). Table 2 shows this debt service payment structure in Years 3 and 4, which is anticipated to continue for the life of the Bonds.

The City began levying Mission Rock CFD special taxes on the Undeveloped Property (as defined in the RMA) within the Mission Rock CFD in Fiscal Year (FY) 2020-21. Additionally, the Port executed Vertical

Parcel Leases for Parcel G on June 25, 2020 and Parcels A, B, and F on October 6, 2020. The execution of these Parcel Leases initiates a 24-month or longer countdown for the levying of the Mission Rock CFD special tax on Developed Property (as defined in the RMA), whereby the levy on Developed Property begins in the Fiscal Year after the 24-month anniversary of Parcel Lease execution. Thus, the Mission Rock CFD special tax levy on Developed Property for Parcel G will begin in FY 2022-23 and for Parcels A, B and F in FY 2023-24. Prior to then, the Development Special Tax will be levied on the Undeveloped Property based upon each parcel's expected square footage and use, in accordance with the RMA, to provide revenues to fund any debt service obligations. The IFD Project Area I tax increment offset mechanism will begin when the Assessor finalizes the assessment of each parcel, which is not anticipated to occur until after the Mission Rock CFD special tax levy on Developed Property begins.

The proposed Bonds will be sold without a rating ("Non-Rated"). The real estate development is in relatively early stages and likely would not receive an investment grade rating. Non-Rated special tax bonds have unique credit considerations and risk factors for investors, which are discussed in the Special Risk Factors section of the Preliminary Official Statement. The Bonds are limited obligations of the City, secured by and payable solely from a pledge of the Development Special Taxes levied in the Mission Rock CFD and tax increment generated in IFD Project Area I.

The General Fund of the City and the Port Harbor Fund are not liable for the payment of principle or interest on the Bonds, and the credit of the City, the credit of the Port, and the General Fund of the City are not pledged to the payment of the Bonds. Other than the Special Taxes and the IFD tax increment, the City is not obligated to levy any taxes for repayment of the Bonds.

Under the Fiscal Agent Agreement, the City, on behalf of the Mission Rock CFD, has covenanted for the benefit of the owners of the Bonds that, under certain circumstances, the City will commence judicial foreclosure proceedings with respect to delinquent Development Special Taxes on the leasehold interest in properties within the Mission Rock CFD, and will diligently pursue such proceedings to completion.

Bond Sizing and Value-to-Lien Ratio

Two factors limit the amount of Mission Rock CFD bonds that may be sold: 1) the ongoing tax revenue capacity; and 2) an appraisal or assessment of the value of the taxable leasehold interests in the Mission Rock CFD.

Ongoing Development Special Tax capacity must be at least 110 percent of the debt service requirement on any Mission Rock CFD Development Special Tax bonds. For example, if the annual debt service payments are \$1.0 million, the annual Development Special Tax capacity (after setting aside amounts for administrative expenses) must be at least \$1.1 million.

Because the City will foreclose on the taxable leasehold interests in the Mission Rock CFD if they are delinquent in the payment of the Development Special Tax, the value of the leasehold interests – determined by an appraisal in this instance – is an important credit consideration for purchasers of the Bonds. Under the City's *Amended and Restated Local Goals and Policies for Community Facilities Districts and Special Tax Districts*, the City must sell the Bonds to achieve at least a 3-to-1 value-to-lien ratio based on 1) the appraised value or the assessed value of the leasehold interests in the taxable parcels in the Mission Rock CFD and 2) special tax and assessment debt encumbering such leasehold interests (including the Bonds). This policy means that the value of the leasehold interests in the Mission Rock

CFD must be three times the outstanding amount of the Bonds and any other special tax and assessment debt.

Integra Realty Resources, Inc. (“Appraiser”) prepared an Appraisal Report dated October 12, 2020, with a valuation date of April 22, 2020, estimating the market value of the leasehold interest of 11 of the 12 blocks within the Mission Rock CFD to be \$150,400,000. Parcel D2 is excluded because it is not subject to the Lien of the Special Tax as a parking facility; separately, Pier 48 is not part of the Mission Rock CFD presently but may be annexed into the Mission Rock CFD in the future.

The not to exceed par amount of \$50,100,000 for the Bonds is based on a 3.0-to-1 value-to-lien ratio based on the current appraised value (as of April 22, 2020) of the leasehold interests in the Mission Rock CFD of \$150,400,000. The Appraisal Report is subject to certain assumptions and limiting conditions set forth therein. Additionally, the unprecedented economic effects of the COVID-19 pandemic created additional challenges to estimating the value of the leasehold interests within the Mission Rock CFD. Integra is currently preparing a revised appraisal to update the valuation to include the latest known information about COVID-19’s economic impacts. If the appraised value of the Mission Rock CFD properties changes, the issuance will maintain at least a 3-to-1 value-to-lien ratio and not exceed a par amount of \$50,100,000.

The value of individual leasehold interests in the parcels in the Mission Rock CFD may vary significantly, and no assurance can be given that should Development Special Taxes levied on one or more of the leasehold interests in the parcels become delinquent, and should the delinquent leasehold interests in the parcels be offered for sale at a judicial foreclosure sale, that any bid would be received for the leasehold interest in the property or, if a bid is received, that such bid would be sufficient to pay such parcel’s delinquent Development Special Taxes.

While this value-to-lien calculation incorporates the value of all the leasehold interests in the Mission Rock CFD, the Bonds are sized based on the Development Special Taxes from only the four Phase 1 parcels. The Development Special Tax capacity on the first four parcels will far exceed the coverage required for the initial Bonds with a not-to-exceed amount of \$50,100,000. Table 3 below shows the expected annual Development Special Tax levies.

Table 3. Mission Rock CFD Projected Development Special Tax Levy

Planning Parcel	FY20-21 Expected Maximum	FY20-21 Actual Levy	FY21-22 Actual Levy	FY22-23 Actual Levy	FY23-24 Actual Levy
Parcel A	\$1,598,937	\$207,107	\$246,340	\$35,566	\$1,696,805
Parcel B	\$1,690,703	\$218,993	\$260,477	\$37,607	\$1,794,188
Parcel F	\$988,931	\$128,094	\$152,359	\$21,997	\$1,049,461
Parcel G	\$1,878,431	\$243,309	\$289,400	\$1,954,320	\$1,993,407
Other Parcels	\$8,025,363	\$1,039,507	\$1,236,424	\$178,510	\$0
Total	\$14,182,366	\$1,837,010	\$2,185,000	\$2,228,000	\$6,533,860

Notes: Other Parcels includes all eight parcels from Phases 2-4 except the proposed parking garage in Parcel D. Actual tax levy shows amounts for debt service on the Bonds only.

Use of Proceeds

The Bond proceeds will 1) finance or reimburse entitlements and horizontal improvements for the Project, 2) fund a debt service reserve fund for the Bonds, 3) fund capitalized interest on the Bonds, if any, 4) fund administrative expenses, and 5) pay costs of issuance. Proceeds of the initial issuance of Bonds will reimburse the Developer for outstanding entitlement costs related to horizontal improvements and the initial stages of Phase 1 horizontal improvements (e.g. utilities, streets, sidewalks, parks, etc.).

Table 4 below summarizes the estimated sources and uses for the Bonds, based on current market conditions and the current appraised value.

Table 4. Estimated Sources and Uses of the Special Tax Bonds, Series 2021

Sources	Amount
Bond Proceeds	
Par Amount	\$50,100,000.00
Premium	\$3,800,506.75
Total Sources	\$53,900,506.75

Uses	Amount
Improvement Fund	\$48,094,043.75
Debt Service Reserve Fund	\$4,430,463.00
<i>Delivery Date Expenses:</i>	
Cost of Issuance	\$875,000.00
Underwriter's Discount	\$501,000.00
Total Uses	\$53,900,506.75

Source: Stifel & PFM

Interest Rate and Projected Debt Service

Based upon current market conditions, a 30-year term, and a true interest cost of 4.45 percent, which assumes the issuance of all Bonds on a tax-exempt basis, Stifel estimates average annual debt service of approximately \$3.4 million. If issued at the not to exceed total par amount of \$50.1 million is estimated to result in approximately \$51.0 million in interest payments over the life of the Bonds. The total debt service over the life of the Bonds is estimated at approximately \$101.1 million.

Method of Sale and Bond Purchase Agreement

Given that the proposed Bonds will be unrated, and the underlying project is a new real estate development project, the City's independent municipal advisor recommend a negotiated sale for this transaction. The Bonds will be secured as to repayment from Development Special Taxes from specific leasehold interests within the Mission Rock CFD and are outside of the City's customary credit profile. Prior to formation, the Port selected Stifel, Nicolaus & Company, Incorporated ("Stifel") to serve as the Underwriter. Stifel is in the City's Underwriter Pool, which was established via a competitive process, and was selected for this transaction through a competitive RFP. The Bond Resolution will approve the

form of the Bond Purchase Agreement, which provides the terms of sale of the bonds by the City to Stifel.

The Capital Plan

The Bonds are limited obligations of the City payable solely from the Development Special Tax revenues and tax increment generated in IFD Project Area I and therefore are not subject to policy constraints of the Ten-Year Capital Plan.

ADDITIONAL INFORMATION

The proposed Bond financing requires two separate actions by the Board of Supervisors: (i) the Board of Supervisors, as legislative body of the Mission Rock CFD, must adopt the Bond Resolution approving the issuance of the Bonds and related documents and actions and (ii) the Board of Supervisors, as legislative body of the IFD, must adopt the IFD Resolution approving the Pledge Agreement and related documents and actions.

The two resolutions are expected to be introduced at the Board of Supervisors meeting on Tuesday, November 10, 2020. The forms of the financing documents related to the Special Tax Bonds—including the Bond Purchase Agreement, Fiscal Agent Agreement, Pledge Agreement, Preliminary Official Statement, the Continuing Disclosure Certificate — will also be submitted.

NEXT STEPS

Port and OPF staff anticipate the Bond Resolution, the IFD Pledge Agreement Resolution and related documents will be introduced to the Board of Supervisors on November 10, 2020. With Board approval and the Mayor’s signature, OPF will lead the distribution of the POS and sale of the Bonds. Table 4 below shows an estimated timeline of key financing items.

Table 5. Anticipated Mission Rock CFD Financing Schedule

Item	Date
Introduction of Legislation to Board of Supervisors	November 10, 2020
Budget & Finance Committee Hearing	December 2, 2020
Board Approval of Legislation	December 8, 2020
Sale and Closing of Bonds	Jan/Feb 2020