



MEMORANDUM

TO: Honorable Members, Health Commission

FROM: Nadia Sesay, Public Finance Director
John Updike, Director of Property

SUBJECT: Resolution Endorsing and Approving the Leasing and Subleasing of Portions of the Zuckerberg San Francisco General Hospital Campus [Buildings B2, 9, 30, 40, 80, 90, and Behavioral Health] to Serve as Security for Tax Exempt and/or Taxable Short Term Certificates of Participation in an Amount Not to Exceed \$160,000,000 to Finance a Portion of Phase 1 of the Transbay Transit Center Project

The City wishes to obtain the endorsement and approval of the Health Commission of the transactions and pledge of the properties as discussed below.

Background

On June 21, 2005, the Board of Supervisors approved the Transbay Redevelopment Plan (initiated by the former San Francisco Redevelopment Agency, currently the successor agency of the Office of Community Investment and Infrastructure (“OCII”)), which provided for the redevelopment of a 40-acre area in the City and County of San Francisco generally bounded by Mission, Main, Second and Folsom Streets, and included redevelopment of the previous Transbay Terminal at First and Mission Streets. The Transbay Joint Powers Authority (“TJPA”) was created to finance, design, develop, construct and operate the Transbay Transit Center Project (“Transbay Center Project”).

Phase 1 of the Transbay Center Project includes the design and construction of a temporary terminal, demolition of the old Transbay Terminal and subsequent development of a permanent new six-story Transbay Transit Center with concourse retail and circulation level, above grade bus level, rooftop park, and two below-grade levels to serve future Caltrain and California High Speed Rail services (“Train Box”), a new off-site bus storage facility and new dedicated bus ramps to connect the Transbay Transit Center, the bus storage facility and the San Francisco-Oakland Bay Bridge. Construction of Phase 1 began in 2008, the previous Transbay Terminal was demolished in 2010 and completion of Phase 1 is anticipated in 2017.

Phase 2 includes the extension of Caltrain rail tracks from their current San Francisco terminus at Fourth and Townsend Streets to a new underground terminus beneath the Transbay Transit Center, for Caltrain and California High Speed Rail.

As reported by the Metropolitan Transportation Commission (“MTC”), since 2008, the projected cost of Phase 1 has increased significantly due to many factors, including but not limited to, a complex design which led to fewer qualified bidders, design changes required to incorporate risk and vulnerability assessment, and higher bid margins due to greater number of competing projects for material and labor. Currently, there is a projected shortfall of approximately \$250,000,000.

Funding

The current committed funding sources for Phase 1 include a combination of federal, state and local sources. On May 3, 2016, the Board of Supervisors (“Board”) adopted Resolution No. 166-16, approving and authorizing the execution and delivery of tax exempt and/or taxable lease revenue commercial paper certificates of participation (“COP”) and tax exempt and/or taxable direct placement revolving certificates of participation in a combined aggregate principal of an amount not to exceed \$260,000,000 (including financing fees and expenses and potentially capitalized interest) to provide interim financing for Phase 1. The short-term certificates cannot exceed 15 years.

COPs represent an undivided interest of an investor to lease payments made by the City. COPs are payable from the City’s general fund, subject to abatement and non-appropriation. COPs have the following characteristics: (1) the authority for issuance is City’s authority to lease property, and the City is only obligated to pay rent under the lease if it has beneficial use and occupancy of the property; (2) City is obligated to make payments from any legally available funds, which the City promises to place the obligation in the annual budget.

[Laguna Honda Replacement Project, 525 Golden Gate, War Memorial Veterans Building Seismic Upgrade and Improvements and One South Van Ness have all been finance with COPs.]

Under the proposed structure, \$160 million will be privately placed with Wells Fargo Bank, N.A. (“Wells Fargo”) and \$100 million will be held by MTC.

In addition, as part of the interim financing proposal, the City and MTC are establishing a Cost Review Committee to be staffed by representatives of the City, the TJPA and the MTC, to oversee the TJPA’s budget and certain expenditures. Additionally, the City’s Department of Public Works (“SFPW”) will be entering into an agreement with the TJPA regarding SFPW providing construction management and oversight services.

Transactions

Pursuant to Resolution No. 166-16, the Board also approved forms of: (a) Trust Agreement, (b) Site Lease – City Property, (c) Site Lease – Train Box, (d) Subleases, and (e) Leaseback Lease and related Agreements.

City Property Lease and Sublease - Wells Fargo: Pursuant to the Site Lease - City Property, the City will lease City-owned properties that have a market value at or above the par value of the COP to a third party Trustee (U.S. Bank, N.A.). Pursuant to the Sublease, the City leases back the same City-owned properties (the leased property) from the Trustee. The City will make annual base rental payments to the Trustee in amounts required to pay debt service on the short term certificates. When the short term certificates are repaid in full, the Lease and Sublease terminate. The City’s general fund will secure the repayment of the short term certificates. The term of the short term certificates is 3 years.

Among other things, the Sublease requires the City to maintain general liability and rental interruption insurance to cover loss, total or partial, of the use of the leased property, such additional rental shall be paid for by the City's general fund [not by DPH]. In addition, in the event of default of non-payment, the Trustee has the right to recover base rental payment under the Sublease pursuant to Section 1951.4 of the California Civil Code and to otherwise enforce performance by the City, and to pursue remedies available in law or in equity (such as the right to sue for rent due but the Trustee cannot repossess the property).

As reported to the Board, it is proposed that a portion of the campus at the Zuckerberg San Francisco General Hospital will serve as leased property for the Wells Fargo notes.

TJPA Property Lease, Sublease and Leaseback – MTC: The City has entered into similar agreements with MTC for a term of 5 years under which the TJPA will lease the Train Box real property to the third party trustee (MTC), the City will sublease the Train Box from the Trustee, and the City will then leaseback the Train Box to the TJPA for their operation and management.

The Leased Property: A portion of the campus at the Zuckerberg San Francisco General Hospital ("ZSFGH") or a portion of the campus at the Laguna Honda Hospital (the "Leased Property") will serve as the Leased Property for the short-term certificates.

The City's Director of Property analyzed the ZSFGH north campus assets (north of 22nd Street), specifically Building 80 (66,832 square feet), Building 90 (39,159 square feet), Building B2 (39,171 square feet) and the Behavior Health building (98,849 square feet) and based upon a review of comparable sales of offices (comparable sales methodology), taking into consideration the age and some known system repairs that have been deferred, and the income potential from these assets if they were leased (income methodology) estimated a reconciled value of \$115,000,000.

The City's Director of Property analyzed the ZSFGH portion of campus south of 22nd Street, specifically Block 4154, Lot 1, Building 30 (53,417 square feet), Building 40 (44,470 square feet) and Building 9 (33,559 square feet) and based upon a review of comparable sales of offices (comparable sales methodology), taking into consideration the age and some known system repairs that have been deferred, and the income potential from these assets if they were leased (income methodology) estimated a reconciled value of \$62,000,000.

Total estimated value of the City Lease Property: \$177,000,000.

Another example of the use of this structure by the City approved by the Health Commission includes the issuance of \$163.3 million in Certificates of Participation (COP) to finance the construction and/or reconstruction and equipping of Laguna Honda Replacement Project. A portion of Laguna Honda Campus served as leased property for the COPs.