

THE REDEVELOPMENT AGENCY OF THE CITY OF SAN JOSE

MEMORANDUM

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| TO: REDEVELOPMENT AGENCY BOARD | FROM: HARRY S. MAVROGENES EXECUTIVE DIRECTOR |
| SUBJECT: SEE BELOW | DATE: FEBRUARY 12, 2009 |

SUBJECT: AUTHORITY TO NEGOTIATE AND EXECUTE AN OWNER PARTICIPATION AGREEMENT WITH BLACK SEA GALLERY DEVELOPMENT, LLC

RECOMMENDATION

It is recommended that the Redevelopment Agency Board adopt a resolution authorizing the Executive Director to negotiate and execute an Owner Participation Agreement with Black Sea Gallery Development, LLC, to facilitate the occupancy of a Ross Dress For Less at 27 South First Street, and such other documents as necessary to facilitate the transaction.

OUTCOME

Approval will allow the Executive Director to finalize an Owner Participation Agreement with Black Sea Gallery that will enable Ross Dress For Less to begin construction on a Ross retail store in May 2009 at 27 South First Street. (Site map attached)

BACKGROUND

In December 2003, the Redevelopment Agency Board approved a Disposition and Development Agreement (DDA) with Black Sea Gallery Development, LLC, (BSG) for the purchase and rehabilitation of an Agency-owned property located at 27 South First Street for the purpose of operating a retail furniture store. Black Sea Gallery operates several locations throughout the Bay Area that specialize in imported furniture, rugs, handicrafts, and other home accessories.

Under the terms of the DDA, BSG purchased the property from the Agency for \$1,000,000. A total of \$500,000 was paid at the close of escrow and \$500,000 was financed by the Agency through a Promissory Note. As required under the DDA, Black Sea expended an additional \$1,000,000 in construction costs to improve the interior and exterior of the property prior to the opening of the store.

The Agency recorded certain covenants against the property that required the operation of a Black Sea Gallery store for ten years, provided the Agency with revenue participation rights if BSG sold the property within the same ten year period, and limited the rights of BSG to place a mortgage on the property. BSG completed the required building and facade improvements and received its Certificate of Occupancy for the project on August 24, 2005, and the downtown location opened for business shortly thereafter.

The principal amount of the Agency Promissory Note was \$500,000 with a term of ten years at an interest rate of 3%. The Promissory Note provided that reductions to the principal amount could be made through either cash payments or additional Agency-approved building improvements. The balance currently outstanding on the Note is \$406,035.

Last year, BSG approached the Agency and expressed interest in pursuing another retail venture at the property. The total 22,000 usable square feet in the building is divided between 16,000 square feet of the original Black Sea Gallery retail space and the remaining unused 6,000 square feet which included a café, office space, and storage in the former Woolworth's department store. After considering a restaurant use for this portion of the property, Black Sea commenced negotiations with Ross Dress For Less (Ross). Ross intends to utilize the entire 22,000 square foot floor plate. To facilitate the development with Ross, BSG has requested certain modifications to its agreements with the Agency.

ANALYSIS

Ross is a nationwide retailer specializing in clothing fashions for men, women, and children at competitive prices. This retail use addresses an ongoing demand for a broader array of retail goods and services available to residents and workers in the downtown. Ross proposes to occupy the entire 22,000 square foot ground floor space of the property.

The proposed Owner Participation Agreement would amend the Agency's existing Promissory Note as well as the Covenants and Deed of Trust recorded against the property. Key provisions of the OPA include:

- Contingent upon the execution of a lease with Ross for retail space located at 27 S. First Street, the Agency will modify certain provisions contained in the Promissory Note, Declaration of Covenants and Restrictions (Covenants), and the Deed of Trust. The Covenants currently require BSG to operate a Black Sea Gallery store for ten years and provides for a radius restriction on the opening of new Black Sea Gallery stores. Upon execution of a lease between Ross and BSG for the property, the use restriction on the building and the radius restriction on the operation of Black Sea stores would terminate. The Covenants would also be amended to allow for the use by Ross.
- If Ross continues to operate at 27 S. First Street for four years, the outstanding principal of the Promissory Note (\$406,035) would be forgiven. For every year the Ross store operates, principal (and any corresponding interest accrued) would be forgiven under the following schedule:
 - Years 1-3 \$100,000
 - Year 4 \$106,035
- BSG will be required to immediately repay any unpaid principal owed and interest accrued if Ross closes the 27 S. First Street store prior to expiration of the four year period.
- The original DDA between BSG and the Agency limited BSG's ability to refinance the property. Approval of the proposed action would allow for the removal of those restrictions as well as the removal of the Agency's Right of Reverter and Right to Repurchase.
- BSG's obligation, as set forth in the original DDA, to share with the Agency a portion of any sales proceeds of the property if sold during a ten year period will remain in effect. However, approval of the proposed action would move the commencement of the ten year period from the Certificate of Compliance date (January 30, 2007) to the Certificate of Occupancy date (August 24, 2005).

On the effective date of the OPA, the original DDA with Black Sea Gallery will be terminated. Those provisions from the original DDA to remain in effect, as described above, will be incorporated into the new OPA documents. The business terms for the new Ross project will be contained in the OPA and in an amended and restated Note and amended and restated Covenants, which will be attachments to the OPA.

The authority to negotiate and execute the OPA is necessary to maintain the project on the schedule established by Ross, which accepts new retail projects only on a semiannual basis. Authority to negotiate and execute the Owner Participation Agreement will allow Ross to conform to its strict development milestone schedule. Ross is scheduled to take possession of the property currently occupied by the Black Sea Gallery in May 2009 and will fund \$1,000,000 in construction costs to improve the property for its uses. It is anticipated that Ross will open the store in Fall 2009.

PUBLIC OUTREACH/INTEREST

The proposed action does not meet any of the criteria for additional outreach efforts. This staff report was posted on the Agency's website and made available for public review in the Agency's public lobby area.

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater.
- Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City.
- Criterion 3:** Consideration of proposed changes to service delivery, programs, or staffing that may have impacts to community services and have been identified by staff, the Board or Council, or a community group that requires special outreach.

COORDINATION

The proposed action has been coordinated with the Agency's General Counsel

FISCAL IMPACT

The proposed amendment would result in a reduction in the principal amount due of \$406,305.10 and interest income of \$79,176.85 over the balance of the loan amortization schedule. The proposed OPA will result in a total reduction of \$485,481.95 to the Agency's Capital Reserve over the amortization period of the current agreement.

CEQA

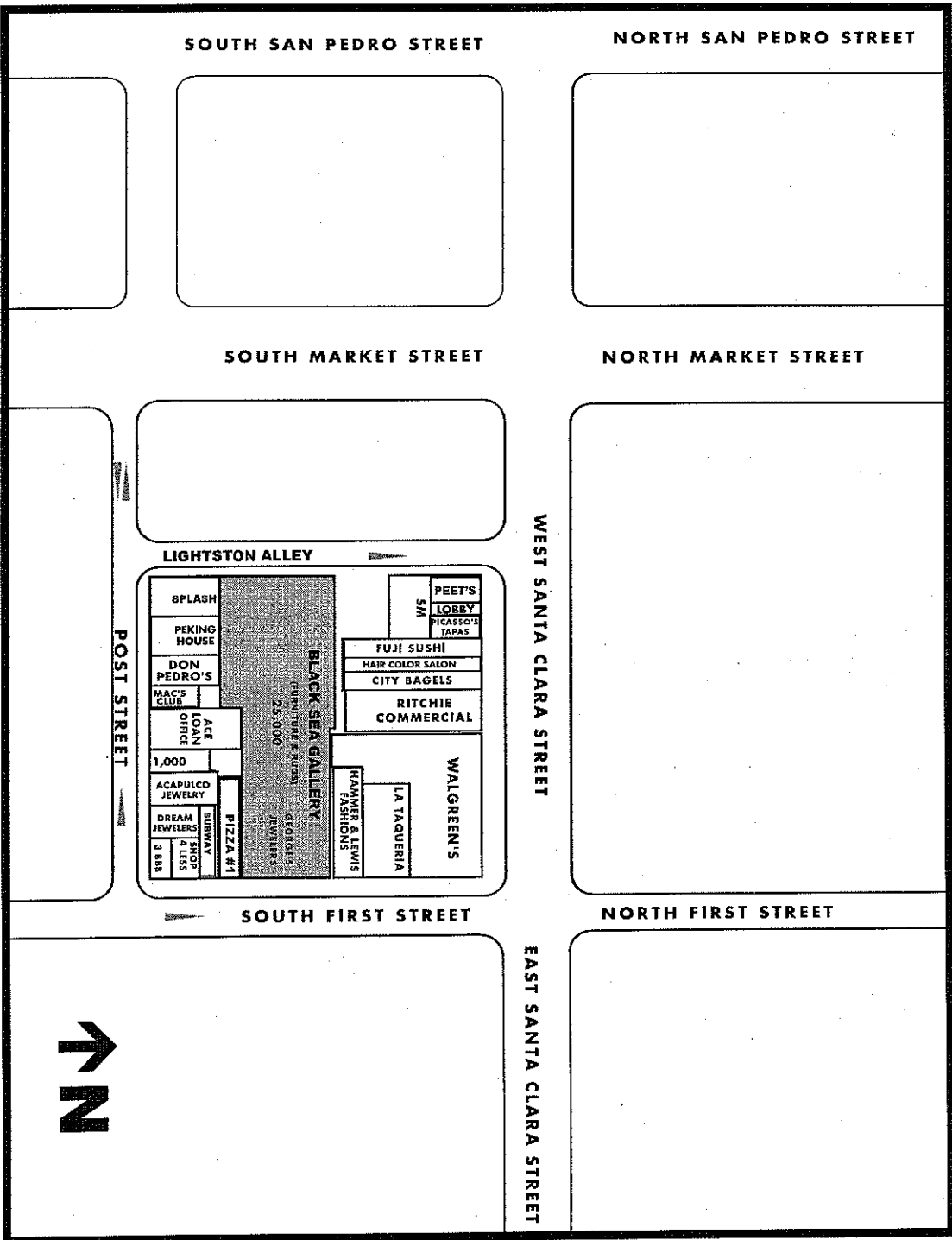
Resolution No. 72767, Use of San Jose Downtown Strategy 2000 FEIR, File No.
PP09-025.



HARRY S. MAVROGENES
Executive Director

Attachment

BLACK SEA GALLERY 27 S. FIRST ST.



BLACK SEA GALLERY

ATTACHMENT