April 19, 2021

C.A.R. HEADQUARTERS PROPERTY ALTERNATIVES AND THE PATHWAY TO HOMEOWNERSHIP PROPOSAL

This Issues Briefing Paper has not been reviewed or approved by the C.A.R. Strategic Planning and Finance Committee, the C.A.R. Executive Committee or the Board of Directors.

Executive Summary

The Association's Headquarters property consists of an office building and a surface parking lot in the densely populated Koreatown neighborhood of Los Angeles. The Board of Directors authorized an effort to seek entitlements (permits) to develop a mixed-use project on the site, proposing to create 130 affordable workforce housing units, and a new office facility. After investing up to $3 million to obtain the entitlements, the property has been appraised at a value in excess of $20 million, up from $10.5 million before entitlements. Broker opinions of the value of the property are lower – from $16 million to $17 million.

C.A.R. advocates for increased housing supply, and supports public policy that addresses the need to create more affordable housing in California. While C.A.R. cannot solve California's affordable housing crisis alone, it can play a role in advocating creative solutions, and if it chooses to do so, it can play a direct or indirect role in creating housing on the property it owns.

With the entitlements pending final approval by the City of Los Angeles, the Board of Directors has the opportunity to decide if the proposed development of housing should proceed, and if so, whether the Association should undertake the development itself, partner with a developer, sell some or all of the subdivided property, or delay making a decision to a future time.

Background

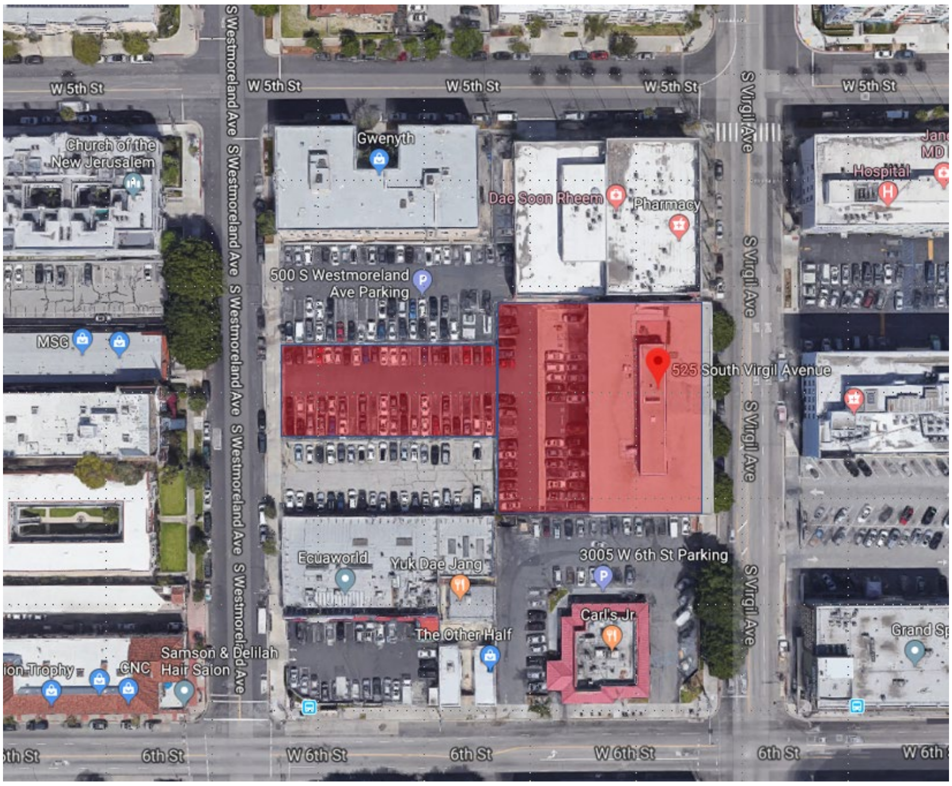
In 1980, C.A.R. purchased its Headquarters facility at 525 S. Virgil Avenue, about three miles west of downtown Los Angeles, for $1,040,010. The four story, 56,072 square foot building, built in 1965 on a nearly one acre site a block north of Wilshire Boulevard and two blocks east of Vermont Avenue, includes a large surface parking lot striped for about 100 vehicles. C.A.R. occupied two floors when the Association moved to this location in 1981 from another location one block away that had been occupied by C.A.R. since 1974. Prior to 1974, the Association's offices were in downtown Los Angeles.

By 1989, the Association's staff had grown to the point that, as tenant leases expired, the Association occupied the entire building. Some improvements to the facility have been made over the years, and the property is generally well maintained. The mortgage on the property has long since been paid off.

Three similar office buildings nextdoor and across the street currently serve as medical offices. Nearby are primarily multifamily housing, both for sale condominiums and rental apartments, with business, retail and restaurants along the major arterial roadways of Wilshire Boulevard , Vermont Avenue, and Sixth Street. Southwestern University Law School and several churches are also well established in the neighborhood. A Metro subway station is located at Wilshire and Vermont, two blocks away, and several bus routes serve the area.

The area known as Koreatown is one of the most densely populated sections of Los Angeles. Since the Association's arrival in the neighborhood in 1974, it has been an area in constant transition. Once an important shopping destination, with department stores such as Bullock's and I. Magnin on Wilshire Boulevard, and the formerly upscale Sheraton Townhouse Hotel and the famous Brown Derby Restaurant helping to anchor a thriving business district, the neighborhood has seen decline, redevelopment, gentrification, and the construction of Los Angeles' Metro system. The department stores, grand hotels, and restaurants have been replaced by many smaller businesses and alternative uses, and with a significant number serving the Korean community, even though the neighborhood is on the edge of the Koreatown area. Starbucks, Coffee Bean & Tea Leaf, Chipotle, Subway, and other outlets also have become well established in the area. The County of Los Angeles still maintains some of their offices at Wilshire and Vermont, and other office towers and high rise residential buildings occupy several blocks around that intersection.

The property is located in a Transit Oriented Communities zone, a State Enterprise Zone, and an Opportunity Zone. The Transit Oriented Communities Incentive Program encourages the construction of affordable housing near bus and train stations.



Today the Assessed Land Value for the 0.97 acre property is $1,624,453, and the Assessed Improvement Value is $4,392,898. An appraisal conducted by a Commercial Appraiser (MAI) in 2018, prior to receiving any new development entitlements from the City, concluded that the Residual Land Value of the property was $10,500,000.

The 525 S. Virgil property itself was comprised of six legal lots, which have been combined into two separately zoned parcels, one zoned for commercial use, fronting Virgil Avenue, on which the office building is located, and one zoned for multifamily residential use or parking, with access on Westmoreland Avenue.

In discussions that took place in late 2017, the concept was suggested to create housing on the parking lot parcel, or to add residences to the top of the existing office building. A structural engineering analysis determined that it would not be feasible to add additional floors to the building, nor would it be cost effective to make any significant investment in rehabilitating the structure, which is in a category of office building construction that *does not meet updated seismic safety standards* in the City of Los Angeles. Local ordinances require that the C.A.R. building be brought up to these standards, or be replaced, by 2042, and that a plan must be submitted to the City by 2027 to show that the building will be retrofitted or demolished.

These initial discussions and research led to a decision by the 2018 C.A.R. Leadership Team to appoint a small volunteer Advisory Group to explore the potential of creating housing at the site of the C.A.R. Headquarters.

The Pathway to Homeownership Proposal

From early 2018 until the present, the C.A.R. Leadership Team and a handful of volunteers refined the initial concept for what became to be known as the Pathway to Homeownership proposal. The objectives established by the Advisory Group, and shared with the Directors as they were continually refined, are as follows.

OBJECTIVES: The Pathway to Homeownership Affordable Housing Project proposes to create affordable workforce for sale and rental housing at the site of C.A.R.'s Los Angeles Headquarters.

1. Provide affordable housing for individuals and families in the 50% to 150% range of Area Median Income, addressing the state's housing crisis for nurses, firefighters, teachers, police and others who are eligible.
    a. 14% of the units would be set aside for veterans in the 50% AMI or lower income range.
2. Provide a pathway for renters of affordable housing to become homeowners, enable them to build equity, strive to achieve homeownership, and then move up to a market rate home.
3. Design a modern and efficient office facility to accommodate the Association's Headquarters operations.
4. Create a model project which can serve as the basis for similar projects throughout the state, especially for local Associations of REALTORS® which own their own property, and which is financially sustainable.
5. Achieve a "Green Building" Leadership in Energy and Environmental Design (LEED) certification for the project.
6. Demonstrate to our Association membership, the state legislature and local governments that C.A.R. is a leader in advocating for affordable workforce housing in California.

The "Pathway" described in Objective 2 above includes an onsite counseling service to advise renters and owners of the affordable workforce housing, and to help them prepare to find their own path to market rate home ownership.

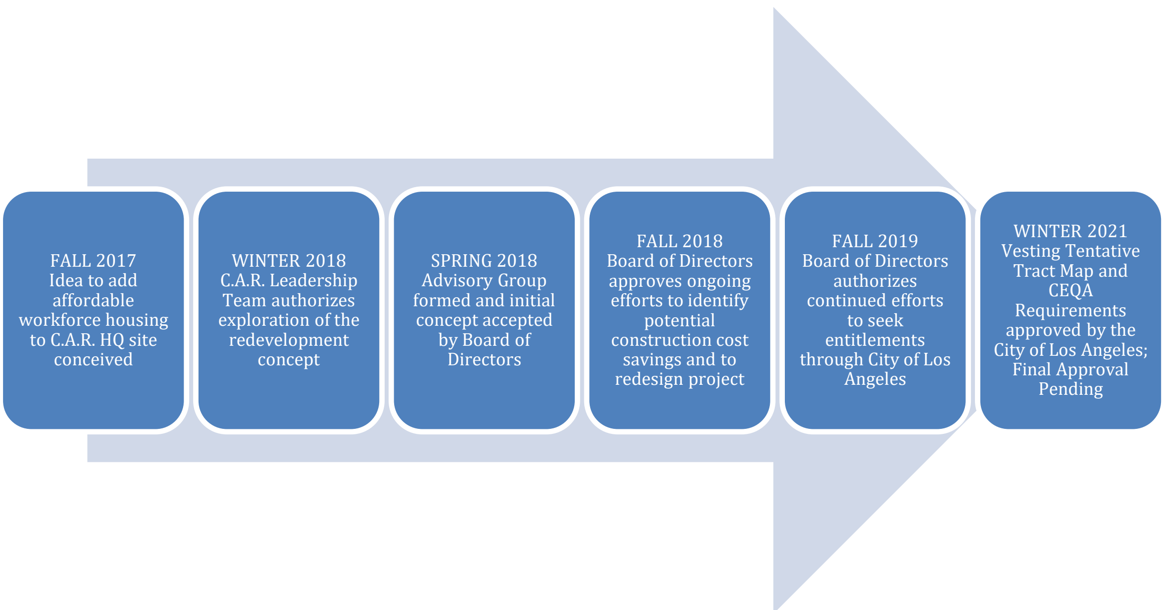
C.A.R. partnered with Thomas Safran and Associates, a premiere developer of affordable multifamily housing in the Southern California region, and Ehrlich Yanai Rhee Chaney Architects, a respected architectural design firm with offices in Culver City and in San Francisco, to design, and then redesign, a proposed 132,367 square-foot mixed-use development, taking advantage of density bonus incentives and the favorable zoning of the property, to include the following elements.

- an eight-story (86 feet tall) residential apartment building (84 units)
- a six-story (69 feet tall) condominium building (46 units)
- a total of 130 housing units (111 market rate units and 19 affordable units [14 percent])*
- a three-story (42 feet tall), commercial/office component containing approximately 26,632 square feet
- all three structures sit atop a one-story podium, as well as two levels of subterranean parking, which together include:
- 111 parking spaces dedicated to residential parking
- 55 parking spaces dedicated to commercial/office uses

With a Floor Area Ratio (FAR) limit of 4:1, the maximum developable square footage allowed without a variance is just over 160,000 square feet. The project as designed does not maximize the potential of the property.

Although only 14% of the residential units are required to be below market rates, the Pathway to Homeownership concept proposes that the entire 130 units consist of affordable workforce housing.

The Board of Directors and the Leadership Team directed the Advisory Group to bring back a proposed conceptual design that would meet the objectives, and authorized funding at several progress points during the course of the research and design phases of the proposed project.



PROJECT FUNDING AUTHORIZED BY THE BOARD OF DIRECTORS AND THE LEADERSHIP TEAM

WINTER 2018	$50,000
SPRING 2018	$825,000
FALL 2018	$250,000
FALL 2019	$406,000
WINTER 2021	$1,550,000
TOTAL AUTHORIZED	$3,081,000

Note: Actual Expenditures as of April 13, 2021: $1,891,629.89
Work in Progress/Not yet Invoiced: $1,181,000 est.

The proposed development was submitted to the City of Los Angeles for approval in May of 2020, and after several public hearings at the Neighborhood Council and at the administrative agency level, was approved by the Los Angeles City Council by a vote of 15-0 on January 26, 2021. At this writing, it is anticipated that the final statutory appeals period (the period during which a member of the public may appeal the City's approval of the development permits sought by the Association) will expire by the end of the month, and the City of Los Angeles will finalize the entitlements.

The approved entitlements consist of three components.

1. A new Vesting Tentative Tract Map, which subdivides the property into five lots (a ground lot and four airspace lots)
    a. a ground lot
    b. an apartment building above ground
    c. a condominium building above ground
    d. a commercial office building above ground
    e. a subterranean parking garage spanning the entire site
2. A determination that the proposed development qualifies for the Transit Oriented Communities Affordable Housing Incentive Program
3. A Notice of Exemption required by the California Environmental Quality Act (CEQA) indicating that the project qualifies for the Sustainable Communities Project Exemption (SCPE)

In order to evaluate whether or not to build the proposed development, the Association's Board of Directors, as the owner of the property, asked that a number of alternatives be explored and presented.

Alternatives for the 525 S. Virgil Avenue Property

The Association is well positioned to make a decision, or a series of decisions, regarding the future of the Headquarters site. Some of the most likely alternatives are discussed in the next section of this report, with a number of permutations outlined for some of those alternatives.

I. **Sell the Entitled Property**
   A. Sell to a Developer who will agree to develop the project as designed
   B. Sell to a Developer who will develop a modified version of the project and agree to include more than 14% affordable housing units
      i. With an onsite office for C.A.R.
      ii. Without an onsite office for C.A.R.
   C. Sell to a Developer who will develop a project of their choice

II. **Sell a portion of the Subdivided Property**
   A. Sell the residential portion(s) and build a new office building for the Association's Headquarters

III. **Partner with a Developer**
   A. TSA Alternative A
   B. TSA Alternative B
   C. TSA Alternative C
   D. Other Partnership/Joint Venture Opportunities

IV. **Build the Proposed Project**
   A. Build as designed
   B. Redesign the Commercial Office (smaller based on the changing need following the pandemic as most employees work remotely)

V. **Delay Making a Decision/Gather More Information**
   A. Some Employees Return to Existing Building
   B. Lease Space in the Existing Building to Tenants
   C. Lease Entire Building and Relocate C.A.R. Headquarters

Discussion of Alternatives

I. Sell the Entitled Property

A. Sell to a Developer who will agree to develop the project as designed; lease back office space
B. Sell to a Developer who will develop a modified version of the project and agree to include more than 14% affordable housing units
i. With an onsite office for C.A.R.
ii. Without an onsite office for C.A.R.
C. Sell to a Developer who will develop a project of their choice

The entitlements which have been approved add value to the property, so it is natural to consider whether it makes financial sense for the Association to sell the asset, and to relocate to another site.

A new commercial property appraisal was conducted, and concluded that the Residual Land Value with entitlements is $20,400,000, up from $10,500,000 before entitlements in 2018. After considering expenses incurred and still projected to obtain the entitlements, estimated to be $3,100,000, this suggests a net increase in value of almost $7,000,000. The appraisers evaluation was based on the entitlements, which allow for a market rate development for most of the residential units, and only restrict 14% of the units to below market rate rents or sale prices.

C.A.R. also sought the opinion of two commercial brokers who are active and knowledgeable in the office and multifamily residential market in the immediate neighborhood. Their opinions of value come in lower than the appraisal, in the $16,000,000 to $17,000,000 range, suggesting a net increase in value of $2,400,000 or more.

While it is apparent that this Alternative of selling the property would be the quickest, cleanest and least risky option, most of the objectives established to guide the Pathway to Homeownership project would not be achieved unless the buyer is well aligned with C.A.R.'s philosophy regarding affordable housing supply. Such alignment would probably come at a cost, with the Association having to sell at a discount in order to achieve the objective of a 100% below market rate development, or having to compromise on other objectives in order to ensure that the Association can maintain a presence with its Headquarters onsite.

Does it make financial sense for the Association to relocate in terms of its cost of operations? In 2021, the operating costs for the Building program are budgeted at $511,800, including salaries and human resources costs.

A hypothetical 20,000 square foot commercial space at a least rate of $2.25 per sf per month FSG would result in annual rent of $540,000, without any salary or HR costs, without tenant improvements, without furniture, fixtures and equipment, and without factoring the cost of moving once, or possibly twice.

The Association also maintains a physical presence in Sacramento, with an office a block away from the State Capitol. C.A.R. has just entered into an eight year lease term for an office suite at 920 L Street, having previously occupied leased office space in several locations in the immediate area for more than 35 years. While selling the Los Angeles Headquarters and relocating to one facility in Sacramento has been mentioned as a *possibility, there are several factors that appear to make this solution less than desirable. First, the disruption to the Association's office based staff would be significant. Second, the cost of leasing or buying a sufficient amount of space in the vicinity of the State Capitol would be high because of the level of demand in that submarket. Third, the population of California, and the membership of C.A.R., tilts strongly to the south, and maintaining the Headquarters within a two hour drive of more than 60% of the Association's members is a strategic advantage.*

II. Sell a portion of the Subdivided Property

A. Sell the residential portion(s) and build a new office building for the Association's Headquarters

Because the Pathway to Homeownership design process led to the subdivision of the air lots for each building, the Association also has the option of selling only some portion of the property, for example the condominium building, the apartment building, or both. Without getting caught up in the details of how such a scenario would play out in terms of common area usage or shared parking garage logistics, it offers the Association a way to achieve the objective of creating housing on the site, while continuing to maintain a physical presence with an office that it would own and occupy.

C.A.R. asked the appraiser to evaluate the value of each component of the proposed development once completed, based on market rates, except for the 14% of units required to be sold or rented at below market rates. In summary form, their conclusions are as follows.

$29,000,000 Indicated Value – Apartments ($345,238 per unit)
$18,000,000 Indicated Value – Office ($676 per square foot)
$16,500,000 Indicated Value – Condominiums ($358,696 per unit)

A separate fiscal analysis was conducted by a consultant, and determined that the valuation of the below market rate Apartments when built, based on net cash flow, would be $37,000,000. The Office valuation was found to be $11,000,000 based on net cash flow, assuming that the Association would pay itself a relatively low rental rate to occupy the space. The condominiums were projected to sell for a total of $19,000,000.

The housing that would be created by a new owner may or may not meet C.A.R.'s original objectives. Some units may be offered at market rates, for example.

III. Partner with a Developer

A. TSA Alternative A
B. TSA Alternative B
C. TSA Alternative C
D. Other Partnership/Joint Venture Opportunities

When the concept of creating affordable housing at the Headquarters site first arose, C.A.R. met with several affordable housing developers to gain a better understanding of the possibilities. One of those developers, Thomas Safran and Associates (TSA), demonstrated that they were well aligned with C.A.R.'s initial thinking about the prospects for developing affordable workforce housing, and ultimately C.A.R. and TSA entered into a Memorandum of

Understanding to work together on selecting various professionals and consultants to design the project and to undertake the steps necessary to prepare to submit the project to the City of Los Angeles for approval. TSA provided sound and valuable advice to C.A.R. at each step of the process, and devoted significant resources to the effort. TSA is interested in serving as a Fee-Based Developer if C.A.R. decides to build the proposed project, and in operating the rental apartments.

In order to evaluate the type of partnership or joint venture that might help C.A.R. to meet its objectives of creating housing at the 525 S. Virgil Avenue property, C.A.R. asked TSA to propose alternative scenarios under which TSA would take on the project, or a modified version of the project, not on a fee basis, but as the Developer themselves. TSA has responded with three alternatives which are summarized below, each of which may serve as a starting point for additional discussion.

> TSA ALTERNATIVE A: Project would be built with apartment and office structures, no for sale condos, but with C.A.R. no longer responsible for funding or managing the residential component. TSA would construct the office; C.A.R. would finance and occupy/manage the office. Affordable rents would not exceed 120% AMI. Some of the structures and the open space may be redesigned in conformance with the city entitlements. C.A.R. would provide a $1 ground lease for a term of 99 years. C.A.R. would be entitled to a share of residual receipts.
>
> TSA ALTERNATIVE B: Similar to Alternative A, but the office would be eliminated, and the project would be 100% residential apartment rentals in three structures, with the originally designed condo and apartment structures decreasing in size to maintain the same 130 total residential units entitled by the city. Affordable rents would not exceed 120% AMI. C.A.R. would provide a $1 ground lease for a term of 99 years. C.A.R. would be entitled to a share of net proceeds, which could include the developer fee, design and entitlement expenses, cash flow or other proceeds.
>
> TSA ALTERNATIVE C: Similar to Alternative B as to the elimination of the office and the 100% rental housing. In conjunction with the California Statewide Communities Development Authority (CSCDA) Workforce Housing Program (https://cscda.org/workforce-housing-program/), C.A.R. would sell the property to this Joint Powers Agency, and TSA Housing would serve as the administrator for the transaction. This new program has not been used for new construction. The program has been used to acquire market rate buildings through the issuance of tax exempt government bonds, and convert them to affordable rental housing. C.A.R. would be entitled to a share of net proceeds, which could include the developer fee, design and entitlement expenses, cash flow or other proceeds.

For the purpose of C.A.R.'s initial evaluation of Alternative B, TSA has suggested that they might propose a five percent share of net proceeds, and that there might be a mutually agreed upon time period during which TSA puts together financing for the project, likely utilizing low income housing tax credits or other public funding sources. At the conclusion of that time period, when the actual budget for the project would be known, C.A.R. would have the option of accepting the agreed upon five percent per year, paying a fee to TSA to terminate the agreement, or renegotiating the terms of an agreement.

The benefit of these proposed alternatives is that C.A.R. would achieve its primary objective of creating affordable housing, and would expose the Association to minimal risk, especially in Alternative B. In both Alternatives A and B, C.A.R. would continue to be the property owner. However, in each of the Alternatives, C.A.R. would have to compromise on the creation of for sale housing, which TSA's proposals would exclude, and only Alternative A would keep the C.A.R. Headquarters Office onsite.

It is possible that C.A.R. could partner or establish a joint venture with a different developer, or developers, if the Association desires to keep home ownership opportunities in the mix by developing condominiums. In fact, meeting with other developers would probably be a wise business decision if a partnership of any kind is contemplated, even if C.A.R. favors a partnership with TSA for the construction and operation of rental housing on the site. This is an alternative to be explored pending the decisions of the Directors. However, it should be noted that identifying a new partner or partners will take time, and delay the ultimate outcome.

IV. Build the Proposed Project

A. Build as designed
B. Redesign the Commercial Office (smaller based on the changing needs for office space observed during the pandemic as most C.A.R. employees work remotely)

C.A.R. has gathered information to prepare a budget pertaining to the actual construction and operation of the proposed development. Sources of the budget data include TSA Housing, a General Contractor, a Landscape Contractor, Architects, a land use and zoning consultant, a utilities consultant, a financial consultant, the appraisal, the opinions of commercial real estate brokers, attorneys, the City of Los Angeles, and others.

It is estimated that the development costs would total approximately $120,000,000. A financial analysis indicates that the total amount of a construction loan, based on the residential components of the project, is projected to be $41,000,000, meaning that C.A.R. would need to take an equity position of $79,000,000 to create the project as designed. This equity could come from C.A.R. reserves, from the disposition of other assets, or from membership dues or fees. No analysis of the impact of a membership dues increase or imposition of a fee has been performed, as there is no interest in pursuing that strategy.

Upon completion of construction, which is assumed to be three years from the date a decision is made to proceed (12 months of pre-work and 24 months of demolition and construction), if C.A.R. sold all of the 46 affordable condominiums for an estimated total of $19,000,000, and refinanced the construction loan with a permanent (30 Year) loan in the amount of $34,000,000, it is estimated that the Association could obtain $13,000,000 in cash from the refinancing, and that the net cash flow could be positive beginning in year six.

Of course, C.A.R. could step back and reconsider the design and construction materials which have been selected, and it may be possible to identify substantial savings in the budget, which would decrease C.A.R.'s contribution to the project, while potentially maintaining the loan amounts for which C.A.R. would qualify at the same levels indicated above. There would be some costs involved in such "value engineering," but it could alter the outlook for the build-it-ourselves scenario. It should also be noted that construction materials, including lumber and steel, have experienced significant price increases in recent months, and the outlook is uncertain regarding the impact this could have on this project, depending on the timing of actual construction.

Other considerations for the builder/developer of the proposed project include the need to contract with a rental property management company, hire a facilities manager, potential exposure to construction defect claims, establishment of a home owners association, and so forth.

In addition, if C.A.R. undertakes the risk of building this project, the exit strategy always exists to sell the property if the Association's priorities change of if market conditions shift, but there is inherent risk in this strategy as well, since we cannot predict the future.

Why is Rental Housing included if C.A.R. promotes property ownership, and Why Rent or Sell at Below Market Rates? A main objective of the Pathway to Homeownership proposal is to create a pathway for renters to achieve home ownership, and eventually to help those owners to be able to build equity and purchase a market rate home. The Association's recognition of its members' role in providing fair housing opportunity for all communities, especially those which have historically had much lower rates of homeownership, is also a consideration in determining whether this is an effort appropriate for C.A.R. to take on at this time. By providing below market rate housing, this project could help 130 individuals and families save money or build equity to purchase a home. This pathway could be key to creating wealth for those who may not have otherwise had access to that opportunity. The Pathway to Homeownership project, if built, is intended to bring in enough income to pay its own operating costs. However, the risk to the Association is that, because of the shamefully high cost of creating affordable housing, especially in a densely populated area that needs it most, this project may never see a full return on the initial investment, and may require an ongoing subsidy from the Association in order to operate.

V. Delay Making a Decision/Gather More Information

A. Some Employees Return to Existing Building
B. Lease Space in the Existing Building to Tenants
C. Lease Entire Building and Relocate C.A.R. Headquarters

There is no need for the Board of Directors to make a decision at this time, and there may be good reasons to delay. Such reasons might include a desire to obtain more information about one or more of the alternatives presented here, or to avoid the perceived risk of making the wrong decision, or to wait out the pandemic and its impact on the market for urban rental housing, or simply to take more time to think about the choices available to the Directors as the owner of the property.

However, there are also arguments to be considered to move forward sooner rather than later. The existing building is more than 55 years old, and no longer suits the changing needs of today's workforce. There are some deferred maintenance issues, but none that make the building unsafe or less functional. The clock is ticking on the City's seismic standards ordinance, and while the approved entitlements would address that, the entitlements are in place for a period of three years, with the possibility that they could be extended to up to a seven year period before construction begins. Construction costs, including labor and materials, could increase significantly. Other changes could occur in the economy, the pandemic could surge, the value of the property could decrease, government regulations could change, or unknown external factors could impact the alternatives available to C.A.R.

If the Association does decide not to build or to sell at this time, given the change in the usage of the facility, it may make sense to consider leasing some of the space to tenants, even though the office market is going to take some time to recover from the pandemic's impact.

Additional Materials

Located at https://car.sharefile.com/d-s5c84abf0e4724c72bf08856cea8e2630

Appraisal (2018)
Appraisal (2021)
Construction Cost Estimate
Presentation of Broker Opinion of Value
Fiscal Analysis (Excerpts)
Letter of Determination – Transit Oriented Communities
Letter of Determination – Vesting Tentative Tract Map
Market Study of Comparable Sales and Rental Rates
Site Information and Unit Mix (Proposed)