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Meeting Summary
April 7, 2016
Unreinforced Masonry Building Seismic Retrofit Project Policy Committee

Committee Members Present: Hermann Colas, Sean Hubert, Tom Sjostrom, Matthew Illias, Jonna Papaefthimiou (for Carmen Merlo), Dennis Andersen, Mathew Eleazer, Walter McMonies, Margaret Mahoney, Heather Hoell, Reid Zimmerman, Jen Sohm, Peggy Moretti, Tom Corollo, Ken Rust, Javier Mena, Amit Kumar, Brian Emerick.

Other attendees: Peter Englander, Eric Johansen, Ken McKinney, Gwenn Baldwin, Alex Roth, Mike Haggerty, Jessica Kinard, Peter Finley Fry

Welcome and Intro

Margaret Mahoney welcomed the group, updated the agenda to included remarks by City of Portland's risk management staff, and introduced attendees from City Risk.

City Risk

Deborah Leopold Hutchins, Insurance and Loss Prevention Manager and Mindy Shane, Risk Manager, Insurance Specialist, were present.

Deborah provided her background; she has extensive experience in Risk Management and was invited by Carmen Merlo to talk about insurance marketplace and how it relates to earthquakes.

Deborah: URMs are not good risks when it comes to insurance, especially if they are very old and not upgraded; industry does not have a lot to offer buyers of insurance. In the marketplace, limits are low, but if you have a URM, you're going to be on the lower end of getting those earthquake limits.

Three or four months ago, earthquake rates were running at 15-20 cents per $100 value, 2-3% of the value of the building. There has not been a significant number of earthquakes throughout the US, so the earthquake market is going soft – rates are coming down, even for URM buildings. Some rates are as low as 2-6 cents per $100. But the marketplaces is cyclical, so that could change rapidly if we experienced a catastrophic event somewhere else in the world.

City only has a $750 million earthquake limit. And it's unusual for a business to buy earthquake insurance at all.

Heather: For small owners that the group is looking at, can they get earthquake insurance? And can they afford it?

Deborah: The can probably get it. Whether they can afford it depends on the marketplace when they go out to get it.

There are new products coming out in the marketplace; they may not be favorable for small property owners, but are better for larger organizations like City. New products allow you to basically write your insurance as you go. New products might be a little more do-able for the property owners. Still, the insurance industry won't seek out small property owners – insurance companies are looking for the best risk, and looking for upgrades and retrofits.

Hermann: Are the companies that are providing insurance well-capitalized, able to handle a large-scale event?

Deborah: Most insurance companies are required to have a three to one ratio to cover liabilities. When it comes to earthquake, most do not retain the risk. It's called re-insurance. They have that insured through another company. Called a reinsurance market.

Walt: I have about 8 buildings, half are URMs. I'm paying about $80K for insurance on those buildings, half the total premium on earthquake. My policies are through Lloyds of London, generally a very high deductible, closer to 20%.

Deborah: Lloyds of London is a syndicate, not an insurance company. A syndicate is a group of companies that pool their moneys together. Usually you don't use Lloyd's unless you have an unusually high risk.

Walt: Some of my buildings are high risk; they need retrofits.

Deborah: It seems like a high deductible.

Peter Englander: What is industry knowledge of the difference in cost between buildings that are or are not retrofitted?

Deborah: In today's marketplace, a building that is retrofitted, steel frame, could get a 2% rate.

Peter: What is the difference between standards: life safety versus protecting the asset?

Deborah: Any kind of retrofitting helps with underwriting.

Private Financing – Peter Englander (See PPT slides)

I conducted a survey of Portland lenders. I talked big and small lenders to get feedback on the market. Wells Fargo, Pacific Continental, Columbia Bank, Albina Bank, Melvin Mark, others. I also did many of PDC's seismic loans.

I found three categories of buildings that required financing: non-retrofitted buildings; buildings that are now triggering retrofit; and buildings that have already been retrofitted to code.

Categories of lenders:

- Institutional lenders, a conduit for Federal programs:

    - These have relatively strict rules, but if you meet their requirements, then they are very good programs.
    - Our own Walt McMonies has written a god deal about these programs.
    - They generally won't lend on un-retrofitted structures.
- Banks (National and Regional/Local):
    - National: Loan to the "best" borrowers, well-positioned applicants who are more aware and have capacity.
    - Local: Are more relationship-based, will accept greater risk for clients they know well, and are less aware of earthquake risk generally. They will only loan on retrofits to the strongest borrowers.
- Finance Companies & Private Lenders: such as GE Capital, or even individuals. They will take the greatest risk but also have the greatest cost.

There is one local bank that won't finance URMs, period.

Heather: In the Portland market or in the local URM market?

Peter: The bank won't finance any URMs anywhere, Portland or beyond.

Walt: Chase won't lend.

Peter: Underwriting trends are:

- Lenders underwrite URMs more carefully.
- There is increased knowledge about earthquake risk generally.
- More talk about doing probable maximum loss reviews (PML) and setting a benchmark over which they will not finance. The benchmark is usually about 20%.
- Some lenders won't allow subordinate debt, which is often required for retrofits.

The whole theme is that it's really tough to do this. Banks are getting smarter and there's more risk.

Lender will finance retrofits if there's a strong relationship between the lender and the URM building owners. They will require higher construction contingencies (up to 15%). This adds to the cost.

Financing retrofits (See slide): It could also take two to three times longer to finance a project when dealing with retrofits. It becomes a more complex deal financially and it requires a more sophisticated borrower with more resources.

Conclusions: Financing of URMs seems to fall into 3 categories (See slide)

It very quickly becomes more difficult and more expensive to finance these kinds of building retrofits. A Retrofit Loan Program would need to be accessible to area lenders. It might depend on SBA/CRA applicability, and it could work with SB 85 property assessment security structure (clean energy pilot underway).

Actions required to implement this would be:

- Political will
- Eligible public capital source

- Partnerships within the lender community
- Create value > cash flow > debt service

Heather: If we come out of this task force and we make recommendations, it will necessitate retrofits. Is there an economy of scale that can be leveraged?

Walt: Can we put together a portfolio of loans? But the problem is, you're not diversifying the risk because all the buildings are URMs…

Sean: I think we're asking banks to concentrate their risk, and I don't know how that's going to go.

Peter: What I've seen with this agency is an ability to convene and problem solve; possibly address it one way or another. Any chance to be able to convene a market of people to discuss that is helpful.

Returning to the presentation; please see slides on Financial Assistance recommendations

Tom Corollo: We've seen lenders becoming much more in tune with seismic risk, asking for more earthquake insurance. Seems like lenders' opinions are evolving.

Peter: Larger institutions say they've always had this approach. Smaller institutions didn't know... almost stuck their head in the sand. Community lenders: one said, "Based on the discussion we just had, we're changing our lending standards." Some are indeed getting smarter about the situation and risk.

Walt: For an existing owner of URM, the kind of financing that would be more crucial for City to provide support on is the ability to get subordinate debt. Not everybody can get their first lender to get a secondary loan.

Peter: When we went through this several years ago, Mayor Katz asked us to start a seismic lending program… Our difficultly now is that resources are reduced. There are few areas of the City where we can continue to do that. Many Urban Renewal Areas are expiring. The funding stream has changed. URA funding only ever applied to certain parts of the city, at most 15%. And it is harder to get new districts approved now. URAs are a tool that's going away and not going to come back.

When talking to lenders, I saw that they had little understanding of the code. They don't know that retrofits usually do nothing to preserve the asset.

Public Financing, Ken Rust / Eric Johansen, "City of Portland Financing Tools" PPT

Characteristics of City Debt Instruments (see slide)

Types of Debt for City-Owned Facilities (see slide)

Matching bureaus to types of debt (see slide). City has good credit; high ratings on revenue bonds.

Tools for privately-owned buildings and facilities:

- Property tax abatements
- Grants
- Loan Programs
- Property Assessed Clean Energy structures (authorized by legislature in 2014)

Buildings Owned by non-profits: grants (subject to lending of credit restrictions).

Ken: The bottom line for the City is that when we try help out non-governmental entities, it gets tricky; there is a constitution limitation against the lending of credit, even for a non-profit housing provider. The interpretation even for grant money has become much stricter.

All we can do is loan money, the same as others in the market. We can prioritize capital to these loans but we cannot subsidize them. We can also use the PACE-like mechanism from SB 85 to provide money against the property in the form of a lien.

Peter: The main advantage of this is that it provides financing that moves with the building ownership.

Ken: Yes, and with a for-profit building that also has tax liability that can be offset with a tax rebate, then you may have a funding stream and a way to finance. But there is a real challenge for a non-profit which has no tax liability. Solving the problem for a taxable property is less challenging. Government also has the ability to finance, access to funds, if they determine to do it. But the non-profit case, there aren't the incentives there are in the for-profit world and they don't have access to public money, and they often cannot take on more debt.

Walt: Tax abatement works well for for-profit housing. Special assessment for historic also helps.

Ken: Brownfield tax might be a good model to look at for URMs. With brownfields, the law currently allows local governments to adopt a special property tax assessment on brownfields land or a property tax exemption on improvements and personal property located on the brownfield. This is a direct financial incentive to parties willing to redevelop them. However, it requires the agreement of at least 75% of the taxing districts within a municipality to agree before it can become effective.

Peggy: How does that idea stack up against the state historic tax credit that Restore Oregon has been working on? This is a 25% rebate on rehabilitation that's provided by the state... well, the money comes from the state. But I don't want that idea to be lost in our looking at various tools as well.

Peter: A tax credit could work for non-profits because they can sell it; abatement could provide cash flow. May be advantages to both. Still tough to get through the legislature.

Margaret introduces Historic and Affordable Housing Subcommittee recommendations for discussion.

Sean speaks to the historic subcommittee recommendations. Gives historical context: many affordable units were lost in the past as building codes / standards were increased. Recommendations seek to avoid more housing unit loss, encourage a comprehensive preservation strategy for existing housing, and provide an additional tool to incentivize long-term affordability of existing URM apartments. Recommendations require assessment and parapet / roof upgrades, the same as for all other building types. Affordable housing would be exempt from steps 3 and 4 if owners have agreement with PHB that says owners are committed to keep units affordable and do upgrades on an agreed-upon timeline. Timeline is presently uncertain; might exceed set timeline (or might not).

Javier Mena adds that the affordable housing has many constraints because of tenants' limited resources. PHB doesn't have resources to do all units at the same time, they need to stagger investments and just need time to figure out the timeline and resources needs.

Heather: How do you define "long-term"?

Sean: TBD in the agreement, but usually long term affordable means 60 years.

Hermann: Since you cannot increase the rents much, are you assuming you will amortize the costs over a very long time?

Sean: That is a part, but moreover, we need time to figure out other financing mechanisms, and also figure out where people can live while we do the work. It may mean building 1-2 additional buildings to use as a hotel space while people are out of their own buildings. Tenant relocation issues are especially difficult for affordable housing residents because they have barriers to housing even in a soft market.

Tom: How many buildings or units are subject to this?

Javier: I forget how many, we do have a list.

Margaret: Committee discussed the fact that among URM residential buildings, some are rent-restricted. The City has already made investments in these and has regulatory agreements. But some URMs are “affordable” because they are low market rate units, not restricted/regulated. We know some ballpark numbers, but until PHB does more review, we don’t have a lot to project. That would be part of the recommendation, City Council charging them to go work on this and come back with a list.

Amit: I think there are about 20 URM buildings that have restricted rents.

Heather: Might any of the housing emergency funding be available for this?

Javier: Emergency funds are not being set aside for this purpose; this money is for new units. The bulk of money go to help homeless who are not now in any housing. The $20 million the mayor promised is to get people off the streets into housing.

Heather: Hate to let an “emergency” go to waste.

Tom: Isn’t the proposal from the task force that owners already have 30 years? That seems like a long time already. How much time do you need?

Sean: Say there are 20 buildings on this list. And there are competing priorities, because there’s already a shortage of housing. My guess is we’ll be able to get one retrofit done every couple of years. So, it could go beyond 30 years. The subcommittee says, because we don’t yet have an analysis of resources and buildings’ needs, let’s give ourselves time.

Tom: Every building owners is uncertain about where they’re going to get the resources.

Javier: Agreed. The fact is, the City has investment in many more buildings than other property owners, and we need more time to figure out how we can get them all done.

Tom: Once a building owner enters into an agreement, is it just going to extend the time they have to work on their building?

Javier: It could.

Tom: Doesn’t seem to me like good public policy to extend the time frame for buildings that house our most vulnerable people.

Walt: Agreed. Steps one and two don't seem like much of a commitment. You're spending very little and getting a pass for 40 or 50 years.

Sean: I don't think you're seeing the differences. You've got units where you cannot do a rent increase. At least with the market, there are tax incentive programs that might increase your revenue. You're converting from one class office space to another with upgrades, and there's at least the ability to have some additional revenue, with affordable housing, there's not.

Tom: Most of these buildings there's not… Depending on how you go about a seismic upgrade, if you do a to-code seismic upgrade, you are not going to enhance your revenue in any way. This building [PDC office] probably rented for more than it would have without the partial seismic upgrade, but they did a lot of other stuff—they redeveloped it.

Sean: I've managed market-rate and affordable housing. With market-rate, I've been able to re-do it and attract a different type of tenant that can pay higher rent. That just can't happen with affordable. But if there are 20-30 buildings, hopefully most of these buildings get retrofitted within this existing window. Hopefully we're only talking about a couple of buildings that are outside.

Walt: If we had a cap, say 40 years or something, that would seem better. The Oregon Resiliency Plan says 50 years, it would be a shame if other sectors were meeting this goal and affordable housing was left behind.

Sean: I'm open to a cap. But because we know we're in a housing crisis already and because the city hasn't had time to study this, we're saying, let's give us some time. At the end of the day, if this group wants to recommend some kind of cap, we can do that, and 40 years will probably be sufficient. But we don't have good data to make a commitment.

Tom: I'm hearing a group from the city say, "We need time, we need to be exempt, but the rest of you have to swallow this bitter pill." It takes away your moral authority.

Javier: I hear you. For us, it is an unknown as to what we're looking at. Even a cap of 40 years, it would be an arbitrary one, because we don't know what we're committing to. With this struggle of finding new units and preserving what's there, it would be disingenuous for us to say, yes, 40 years would be appropriate. We understand this is a mandate citywide, and other owners will have to do this too. But there's 20 or 30 buildings… It's not one or two or four, or twenty years would be no problem.

Sean: I come back to – the city has done a study, we know we are about 30,000 units short of the number of units we need for affordable housing. The committee does have to look at the fact that, is the city recommending a policy that could increase that?

Hermann: We need to do research but we can also guess costs by number of units. The real question is not really what money do we need, it is where is that stream of money going to come from to do this?

Javier: Two fold issue: what is the size of the problem, and where is the money going to come from to address? In terms of find the number, we can do that. Finding the resources is another thing. We cannot go out and get a bond, as Ken says. So where are the resources?

Margaret: This discussion was an attempt to get the conversation from last week into written form so you could see it. Now perhaps this ties to the conversation about financing tools and what kind of work it takes to get these done over the next couple of years.

Peggy: Summarizes Historic Subcommittee Recommendations (also see document):

- Retrofit should be to life-safety standards.
- Designated historic properties might be prioritized for incentives.
- A concierge service is needed for people who don't have teams of lawyers and contractors; the main-street-sized property owners are going to need some help to navigate this.
- A state historic tax credit would go a long way towards financing this.
- Post-earthquake, historic buildings should be known to inspectors so they aren't lost unnecessarily, if the owner wants to rebuild.
- Materials should be salvaged if a building is a total lost.
- There is interest growing for a project similar to LEED to create demand for retrofitted properties.

Walt: Many buildings are historic but aren't declared as historic because of the owner consent that's needed. And there are already tax programs to benefit historic buildings. This could create another incentive. But historic already has some significant tax subsidies; this makes market-rate non-historic housing the stepchild of both historic and affordable buildings.

Peggy: Resources are limited, we can't save everything; shouldn't we allocate resources to buildings that have the most cultural significance?

Hermann: I would say that should be the approach. It is cheaper to take down a building that is not strong and replace it to protect the people inside it, than to upgrade it. Even an upgraded building might be a total loss. So we should prioritize. We need to save some significant buildings that tell the story of this place. But we cannot save every building, not even all those that are historical.

Heather: The City has not updated its historic assets list for more than two decades. Saying there's going to be all these extra standards for a range of historic buildings when we can't even find money to update the list seems problematic.

Peggy: Historic inventory is very out of date, but the good news is that buildings that have become eligible in the last twenty years are probably not URMs. They stopped making URMs in 1935.

Heather: Also concerned about prioritizing non-conforming buildings. Non-conforming zoning can have a big impact on a small businesses district.

Peggy: I think you are referring to non-conforming uses, not non-conforming structures.

Brian: We did a project where a historic market in a district with blanket residential zoning was upgraded. If we hadn't been able to continue the non-conforming use, then the neighborhood would have a lost a market that had been there since the 1920s.

Policy Considerations, wrap-up and next steps

Margaret notes time is nearly over. Next meeting May 12; will focus on schools, religious facilities:

Margaret: Specific topics you'd like staff to further investigate?

Walt: Brownfield legislation is of interest. Ken will get more.

Peggy: Other places dealt with same questions. Is there a report or review of how other states have addressed the financing? Do we need to reinvent the wheel?

Peter: as I understand it, in other places, primarily in SF and LA, the market dynamics were different and there were various tools that were used or not used. Seattle is struggling with same issues. Don't think they're any further along. As I see it, we have to offer a variety of solutions one size does not fit all. In SF $200 million of bonds were issued and no one used them because of the strictures on public financing. Our market is surely not that strong. Overall we have to offer a variety of tools because owners are in so many different situations, sizes, etc. In my interviews, I found new ideas were lacking even among bankers: in my interviews, they weren't coming up with solutions. So we need to do some of this convening. Say this is a problem we're trying to solve. Let's put our heads together as people who work in financial markets. Can be effective people in coming up with solutions. Increased awareness helps. Committee can recommend how important it is to create the market differential for seismic improved building.

Peggy: Perhaps we should dive into market demands a bit deeper.

Margaret: Notes that the group has not yet heard public comment, asks for comment.

PUBLIC TESTIMONY: Peter Finley Fry, representing himself.

Three points I want to make:

1) Our earthquake codes are based on San Francisco earthquakes but our geology is different. We don't have a lot of crustal quakes. Our codes need to reflect our kind of earthquake.

2) I deal with historic buildings, and the interior is as important as exterior. Upgrades can destroy the interior in an effort to preserve the exterior.

3) In Downtown, Old Town, and the Central Eastside, the market is strong enough to convince lenders to support restoration projects. In Kenton and similar areas, there is not a strong enough market to protect these buildings. I'm concerned we'll allow those buildings to all go down.

PUBLIC TESTIMONY: Gwenn Baldwin, representing Masonry Building Owners of Oregon

It boils down to money. Seattle is ahead of us, but are still stymied because of the money. The Council needs to follow the money. If the money isn't there, the end result will be many more demolitions. I don't think that's in any of our interest. We need to make sure that the money remains linked to the wider effort.

On the affordable piece, it might make more sense to look at giving rent restricted properties a longer window. You can't adjust the rents to pay for retrofits. Those buildings are already in a bind.

Last piece, with historic buildings: no question we have to go down to Salem for a second year to ask for a tax credit. But if our focus is on saving lives, I'm not sure why we would put a priority on historic buildings. It would make more sense if they were retrofitted to a higher standard where the structure could be saved.

Walt: The state of California did a summary in 2003 of everything they did. They had mandatory retro-fits in 1986. And Seattle did a great summary as well.

Amit: That stuff is on the website now.

Tom: Can you share with us what has been done to advertise this work?

Jonna: PBEM has been working on an outreach plan, it could go into the agenda for the next meeting.

Margaret: Yes, what distribution has there been? What's the plan to get people involved?

Tom: The Central City Plan and the Comp Plan relate to this work. Can someone report to us on what's been done with these plans?

Jonna: BPS has participated in our process intermittently; we can ask them to come back and make the connection to this work if there is interest.

Margaret: We will have a very full agenda for the next meetings.

The meeting was adjourned.