



COMMUNITY DEVELOPMENT DEPARTMENT

Council Meeting Date: March 4, 2008

Staff Report #: 08-033

Agenda Item #: H1

INFORMATION: Submittal of an Application to the State Department of Housing and Community Development for Transit Oriented Development Housing Program Infrastructure Grant Funding Associated with the Derry Mixed Use Project Located at 550-580 Oak Grove Avenue and 540-570 Derry Lane.

This is an information report. Council action is not required at this time.

BACKGROUND

The revised Derry project is a proposal for the development of 108 residential units and 24,925 square feet of commercial space on property located on the north side of Oak Grove Avenue immediately west of the Caltrain right-of-way and approximately 150 feet east of El Camino Real. The project is currently undergoing review. A separate staff report related to the review process, and specifically to the Development Agreement, for the Derry project is also on the March 4, 2008 Council agenda.

At its meeting of February 26, 2008, the City Council adopted a resolution authorizing the submittal of an application to the City/County Association of Governments of San Mateo County (C/CAG) for a transportation project grant associated with the revised Derry project. The grant provides funding to the City for an as yet unidentified transportation project. The transportation project is not required to be associated with the Derry project and may be used for an unrelated transportation project in the city. The subject of this staff report is consideration of a second grant related to the Derry project. The proposed grant is unrelated to the grant application recently submitted to C/CAG.

ANALYSIS

Transit Oriented Development Housing Program

The Transit Oriented Development (TOD) Housing Program of the State Housing and Community Development Department (HCD) was funded by Proposition 1C, the Housing and Shelter Trust Fund Act of 2006. Its primary objectives are to increase the overall supply of housing, increase the supply of affordable housing, increase public transit ridership, and minimize automobile trips. The program seeks to accomplish these objectives by providing financial assistance for the development of housing and related infrastructure near public transit stations. A total of \$285 million will be made

available over approximately three years. The first funding cycle was recently announced, offering \$95 million for eligible TOD projects in California. Additional information on the grant program is available through the HCD website at <http://www.hcd.ca.gov/fa/tod/>.

Under the program, low-interest loans are available as gap financing for rental housing projects that include affordable units and as mortgage assistance for homeownership developments. In addition, grants are available to cities, counties and transit agencies for infrastructure improvements necessary for the development of specified TOD housing developments, or to facilitate connections between these developments and transit stations.

The program outlines eligibility requirements that must be met in order to be considered for a grant award. Specifically, an eligible project must consist of a minimum of 50 new or substantially rehabilitated units, be located in an urbanized area and within close proximity to a transit station, include a minimum of 15 percent affordable units, and have a minimum net density (Floor Area Ratio) approaching 150 percent.

The program also outlines additional eligibility criteria for the infrastructure grant funding. Specifically, the infrastructure grant funding is intended to assist private housing projects that might not otherwise be financially feasible. Projects must demonstrate that the grant will not result in developers realizing a profit that exceeds the commercially reasonable range for other developments of similar size and level of risk. The applicant must show that program funds are reasonably necessary for project feasibility through submittal of market studies, construction contracts and other project economic information and that no other source of compatible funding is reasonably available.

The infrastructure projects that may be considered are those required by a local government as a condition to the development of the project, such as sewer or water system upgrades, street improvements, and drainage improvements, and/or improvements that substantially enhance public pedestrian or bicycle access from the housing development to the transit station.

Funds will be allocated through a competitive process based on the merits of individual development projects. The application selection criteria focuses on traditional concerns of housing projects, such as affordability and readiness, and on the extent to which developments realize the program objectives of reducing automobile trips and increasing transit ridership.

Submittal of Grant Funding Application

The Derry project sponsor is interested in pursuing a TOD Housing Program infrastructure grant, stating that the combination of project revisions and changes in the housing market are a risk to the feasibility of the project. The project sponsor has specifically noted that a construction loan will be needed to finance the project and that

construction lenders have minimum financial thresholds which must be met as a condition of providing construction financing. According to the project sponsor, at the time the Settlement Agreement between O'Brien Homes LLC and Menlo Park Tomorrow was negotiated in May 2007, the project profitability and other financial metrics were reduced to levels at or below the minimum levels required by construction lenders. The project sponsor asserts that this is as a result of the 20 percent reduction in the residential density while maintaining the quality of building materials and finishes and the supplemental payment of two million dollars to the City in addition to all normally required fees. Since that time, the residential market has not improved, construction costs have not dropped, and the lending environment has tightened considerably due to the sub-prime mortgage issue and related credit crunch. Consequently, the project sponsor has determined that there is a significant risk that the Derry project will not be viable without TOD Housing Program funding if an attempt to obtain construction financing for the project is made in the current marketplace.

HCD has stated that due to the short timeline between announcement of the grant funding and deadline for submittal of an application, it will be accepting preliminary applications by the deadline of March 7, 2008, with detailed financial information to follow at a later date. A future Council action to approve a City resolution supporting the filing of the application would also be required to be submitted within 60 days of the filing of the preliminary application. Staff will review the more detailed financial information as a part of preparing the resolution for Council consideration.

The infrastructure grant funding requires that the application be submitted by the City on behalf of a specified housing project. A 20 percent match of the grant funds is also required. The Derry project sponsor would be completing the application materials for review by staff and would be providing the 20 percent matching funds.

The infrastructure grant funding is based on the total number of units in the housing development. At \$35,000 per unit, the Derry project with 108 units would be eligible for a maximum of \$3,780,000. To provide some perspective for the grant funding, the current project valuation is estimated at \$34 million. The grant funding would be provided to the City on a cost reimbursement basis. The City would then forward funding on to the developer, who is responsible for the infrastructure improvements associated with the project.

All funding from the State is contingent on the grant being necessary to make the project financially feasible. If conditions in the residential real estate market or construction lending market change in a favorable direction prior to the award of the grant such that the project is viable without the TOD Housing funds, then such funds would no longer be necessary or available.

It is staff's intent unless directed otherwise to file the preliminary application. This would create a "placeholder" and allow the Derry project sponsor adequate time to prepare the complete application with detailed financial information. Staff has also contacted a representative of Menlo Park Tomorrow to advise them of the request for the City to file

the preliminary application on behalf of the Derry project. Staff would return to Council within the next 60 days for review of the complete application, including detailed financial information, and consideration of a resolution supporting the application. If the Council opts to not adopt the resolution at that time, the City would withdraw the preliminary application.

IMPACT ON CITY RESOURCES

The grant application process and potential funding is directly related to the Derry project, therefore all staff time related to the grant application process is fully recoverable through fees charged to the applicant.

POLICY ISSUES

The filing of a preliminary application does not represent any change to City policy, but creates a placeholder to allow for consideration of a resolution supporting the filing of the application at a later date.

ENVIRONMENTAL REVIEW

Application for grant funds is not a project under the current California Environmental Quality Act Guidelines. A Final EIR for the development project has been certified and an Addendum is currently being prepared.

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Report Author

PUBLIC NOTICE

Public Notification was achieved by posting the agenda, with this agenda item being listed, at least 72 hours prior to the meeting. In addition, the staff report was posted on the Derry Mixed-Use Project webpage on the City's website, and an email bulletin was sent to all subscribers to the page.

ATTACHMENTS

None