

**DATE:** September 11, 2018

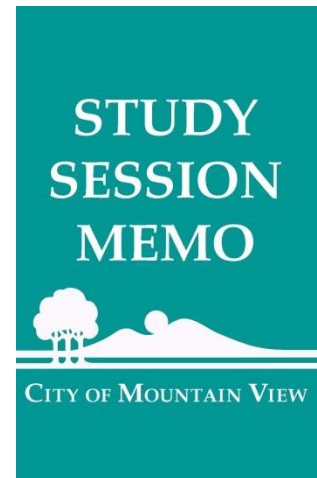
**TO:** Honorable Mayor and City Council

**FROM:** Martin Alkire, Principal Planner  
Wayne Chen, Assistant Community  
Development Director

**VIA:** Daniel H. Rich, City Manager

**TITLE:** **Possible Alternatives for 1255 Pear Avenue  
Gatekeeper Development Proposal**

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## **PURPOSE**

The purpose of this Study Session is for the City Council to consider potential alternatives regarding the development proposal for 1255 Pear Avenue. Following direction from the City Council at this meeting, the project could be modified, and would then proceed to a Zoning Administrator public hearing and City Council meeting for consideration of entitlements.

## **BACKGROUND**

The Sobrato Organization (Sobrato) received Council Gatekeeper authorization in 2015 for a new mixed-use office and residential project at 1255 Pear Avenue, located within the North Bayshore Precise Plan (Plan) area. Since that time, staff has worked closely with Sobrato during the entitlement process to comply with the Plan's development standards and guidelines. Subsequent to the December 2017 adoption of the Plan, Sobrato has also been in discussions with the local school districts regarding their local school strategy requirement to satisfy the Plan's voluntary Bonus FAR tier requirements. The project was scheduled for a Zoning Administrator and City Council meeting in May/June, but Sobrato requested a continuance due to concerns about the project's viability (See Attachment 1).

### *Gatekeeper Proposal*

Sobrato's development proposal includes the following key elements:

- New 231,000 square foot office building.
- 635 market-rate apartments.
- New Inigo Way extension.

- Dedication of a 1.4-acre parcel for affordable housing.
- Site improvements, including new bike/pedestrian greenway and pedestrian paths.
- Proposed community benefits (below-market leases to small businesses – Center of Balance Yoga studio and Pear Avenue Theater).

The illustrative project site plan is shown below.

**Figure 1: Current Project Proposal: Illustrative Site Plan**



*North Bayshore Precise Plan Affordable Housing Requirements*

The Plan requires that the project include at least 15 percent affordable housing (BMR) units for Tier I projects in the General character area that propose up to 2.50 FAR. For Sobrato's 635 market-rate units, the required BMR unit obligation would be 95 units (635 x 15 percent).

To meet their BMR obligation, Sobrato proposes to dedicate an adjacent 1.4-acre parcel to the City to accommodate a future affordable housing project instead of building the 95 units on-site. Based on recent affordable housing developments in the City, the 1.4-acre parcel could potentially accommodate between 100 and 140 affordable units (or 16 percent to 22 percent of the 635 market-rate unit total), depending on the design, size of units, target population, and parking configuration. Any units above the required 15 percent affordable requirement would be considered community benefits. The City would still need to issue a Request for Qualifications (RFQ) to find qualified affordable housing developers and/or issue a Request for Proposals (RFP) for affordable development proposals and might be asked to contribute additional funds.

*Project Construction Phasing*

Sobrato proposes a phased construction schedule for this project. Under this proposal, Sobrato would not dedicate the 1.4-acre site to the City for affordable housing until 2022. This is because Sobrato is requesting use of the parcel as a staging area to accommodate the proposed construction phasing for their project as shown below.

**Table 1: Sobrato’s Proposed Construction Phasing Schedule**

	<b>Description</b>	<b>Estimated Completion</b>
Phase I	Demolish buildings on North and South Parcels; Construct temporary parking on North Parcel	May 2019
Phase II	Build South Parcel parking garage	January 2020
Phase III	Build South Parcel office building	July 2020
Phase IV	Build South Parcel residential units	March 2021
Phase V	Demolish temporary parking on North Parcel; build North Parcel permanent garage and residential units	March 2022
Other	Construct Inigo Way street extension	March 2022
	1.4-acre parcel dedication turned over to City	March 2022

*Developer Feasibility Concern*

As noted earlier, Sobrato has recently discussed with staff their concerns over the financial feasibility of the project. According to Sobrato, this is primarily due to the required Park Land fees and the developer’s support of the Plan’s local school strategy as part of the developer’s community benefits for increased FAR. On September 4,

2018, the City Council discussed the issue of the cost of residential development in North Bayshore and concerns about development feasibility. The Council directed staff to develop options for meeting the parkland requirements, including a tiered credit system, establishing and locking in a park fee amount earlier in the process, and hybrid options. The Council also clarified that it did not expect residential developers to pay for the full cost of the local school strategy and directed staff to facilitate continued discussions with developers and the school districts. For more information on the cost of residential development in North Bayshore, please see the attached Council Report (See Attachment 2: September 4, 2018 City Council Report).

### Gatekeeper Status

This project alternatives discussed below are similar in large part to the Gatekeeper application submitted by Sobrato. The affordable housing component has been modified substantially, but the general layout and uses are the same. Therefore, staff does not believe the alternatives would require formal authorization by the City Council.

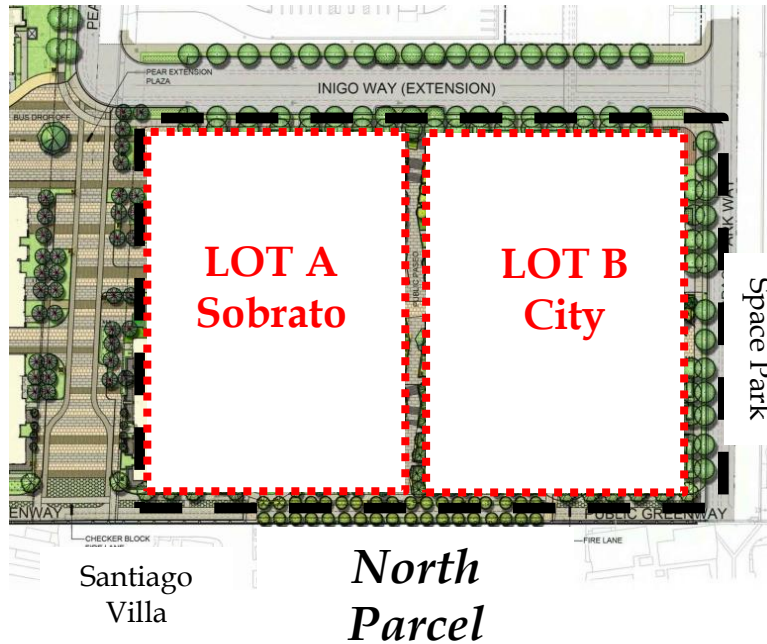
### *Project Alternatives*

During the past several months, Sobrato has proposed alternatives to revise the North Parcel part of their project to address their concerns regarding financial viability. The alternatives below could result in a more viable project while still implementing key City objectives for residential development in North Bayshore, as outlined in the Precise Plan. The potential “tradeoffs” and options for Council regarding these alternatives are discussed later in this report.

Both of the alternatives involve changes only to the North Parcel; the South Parcel would remain as proposed (220 market-rate apartment units and a new office building).

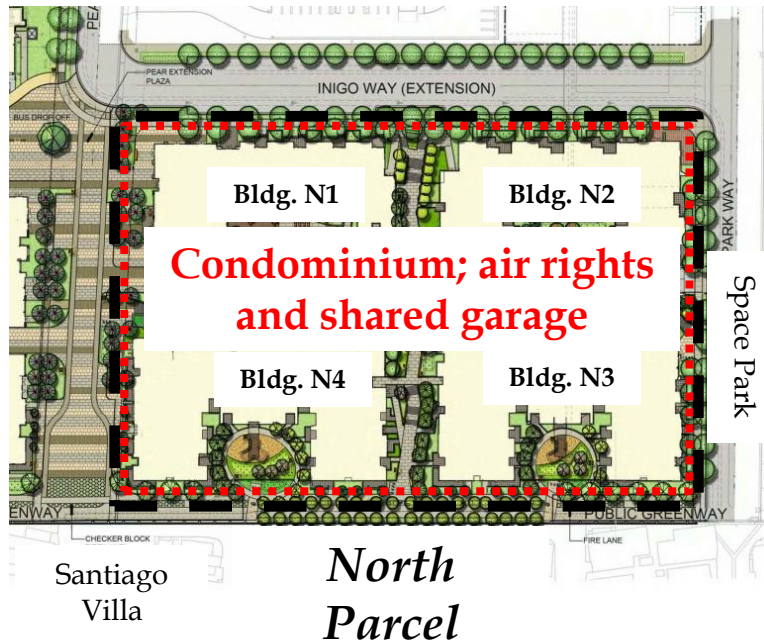
A brief description of the alternatives, only focusing on changes to the North Parcel as shown below, includes:

- Alternative 1: North Parcel Split; City Ownership



- North Parcel is divided into two lots – Lots A and B.
- 427 total market-rate units. Lot A owned by Sobrato and developed with 207 market-rate units. South parcel would have 220 market-rate units.
- City purchases Lot B of North Parcel for development of affordable housing units (potentially 210 units or more).

- Alternative 2: North Parcel Condominium; City Ownership



- North Parcel is split into condominium ownership.
- City and Sobrato jointly own the parking garage.
- Sobrato owns the “air rights” to Buildings N1 and N4; City owns the “air rights” to Buildings N2 and N3.
- 404 market-rate units (220 units on the South Parcel and 184 units on the North Parcel).
- Up to 231 affordable housing units on City-owned Buildings N2 and N3.

To help frame this discussion, the following table compares the key parts of the Gatekeeper proposal with the two alternatives. Further discussion of the advantages follows the table.

Alternatives	Overview					Fees & Requirements		Land Cost or Subsidy	
	Ownership structure	Market Rate Units	15% Affordable Housing Requirements	Compliance with Affordable Housing Requirements		Total Units	Parkland Dedication Ordinance Compliance	Local School Strategy Responsibility	Potential City Subsidy
				Land Dedication or Sale	Number of Affordable Housing Units				
<b>Gatekeeper proposal</b>	Sobrato owns all parcels	635	95 units	1.4-acre parcel dedication	Approximately 100-140 units on dedicated parcel	785 to 855	~ \$38 million  No park dedication	Sobrato	Up to \$30 million
<b><u>Alternative 1:</u></b>  <b><i>North Parcel Split; City Ownership</i></b>	Sobrato owns North, Lot A  City owns Lot B	427	64 units	City purchases 2.57 acres (North, Lot B)	Approximately 208 (North, Lot B)	635	~ \$11.5 million and 1.4-acre park dedication	City/Affordable Housing Developer	Approximately \$16.3 million for land purchase
<b><u>Alternative 2:</u></b>  <b><i>North Parcel Condominium; City Ownership</i></b>	City and Sobrato own air rights to North buildings and shared garage ownership	404	61 units	City purchases 2.88 acres (North, condo)	Approximately 231 (North Parcel, Lot B)	635	~\$10 million and 1.4 acre park dedication	City/Affordable Housing Developer	Approximately \$19.9 million for land purchase

## DISCUSSION

In this discussion, staff compares the Gatekeeper proposal and two alternatives, highlighting the key differences between the alternatives, including advantages, concerns, and further issues to consider.

### *Gatekeeper Proposal – 635 Market-Rate Units*

#### *Advantages*

- Developer proposes to satisfy the affordable housing requirement by dedicating a 1.4-acre parcel to the City. This parcel would be used for affordable housing, which could accommodate between 100 and 140 units (16 percent to 22 percent of the project's 635 market-rate units), which exceeds the Precise Plan's 15 percent affordable housing requirement.
- City receives approximately \$38 million in park fees.
- Minimal additional legal agreements needed.

#### *Considerations*

- Development viability in question.

#### *Further Issues or Questions to Consider*

- Developer proposes a phased construction plan and use of 1.4-acre parcel for staging during construction. Developer proposes transferring title to the parcel to the City prior to issuance of the first building permit for Phase 1 and the City would lease back the site for construction staging.
- Is condition of 1.4-acre parcel (i.e., any required site cleanup) suitable for residential development?
- Affordable housing strategy and process: the City would send out an RFP to affordable housing developers for development of affordable housing on the dedicated parcel.



### *Alternative 1 – North Parcel Split; City Ownership*

This alternative modifies the site plan by subdividing the North Parcel into two equal parcels, Lots A and B. The City would purchase Lot B (about 2.57 acres), which would be used for an affordable housing project. Each North Parcel lot would have their own separate podium garage structures. The 427-unit market-rate project's affordable housing obligation under this alternative is 64 BMR units.

Instead of building the units, Sobrato would pay or provide \$9.4 million credit towards the purchase of Lot B. This payment/credit represents the value of 0.94 acre of land (at \$10 million per acre) that would have been dedicated to meet the project's affordable housing obligation. The \$10 million per acre amount is the City's estimate of land value that was used to calculate the project's parkland dedication requirement.

#### *Advantages*

- City buys and owns Lot B (approximately 2.57 acres) outright to use for affordable housing.
- The number of potential affordable units that could be constructed on Lot B (potentially 210 units or more) would exceed the range in the current Gatekeeper proposal (100 to 140).
- Since the City would own Lot B, site control would allow the City to consider its own specific affordable housing priorities and goals for the site. This could result in a different unit mix, amount of parking, building design, or particular population served.
- No need for CC&R's, vertical subdivision, reciprocal easements, etc., if there are no shared elements and no need for access rights.
- City receives the 1.4 acres, designated under the current proposal for affordable housing, for use as a public park to partially satisfy the project's Park Land fees requirement.

#### *Considerations*

- Total number of rental housing units could be less than the Gatekeeper proposal due to North Parcel site subdivision, building modifications, and parking reconfigurations (pending further study).

- City would receive \$9.4 million credit to satisfy the project's affordable housing obligation.
- Net cost to the City to buy the land would be approximately \$16.3 million.
- The City and/or a future affordable housing developer, would assume responsibility for complying with the Plan's local school strategy.
- City would receive approximately \$11.5 million in Park Land fees and a 1.4-acre land dedication for a park.
- A number of legal agreements would be needed for this alternative (purchase and sale agreement, ground lease or Disposition and Development Agreement, Rent Regulatory Agreement, Development Agreement, License Agreements, and potentially City loan documents, depending on funding source).
- Unlikely to resolve outstanding issues in time for the October 23, 2018 City Council meeting.

*Further Issues for Consideration*

- Affordable housing strategy and process: the City would send out an RFQ or RFP to affordable housing developers for development of affordable housing on Lot B.
- Would need to entitle Lot B, which could add time/process to develop affordable housing.
- Funding of affordable housing project on Lot B would need to be resolved prior to construction of North Parcel if Sobrato were to build all North structures and garages.
- Changes to site plan and parking garage would need further staff review postentitlement; this could require Development Review Committee, Zoning Administrator, and possibly Council review, depending on the significance of any changes.
- The timing of the dedication of the land needs to be addressed in the context of the phased construction plan, the use of the North Parcel for parking during the initial phases of construction, and ensuring the developer meets the affordable housing requirements even if the second phase of the project were never built. The Affordable Housing Guidelines for the Plan require land to be dedicated prior to

the issuance of a building permit and that the dedicated site be able to be developed prior to the issuance of building permits for the project.

- Phasing plan and use of 1.4-acre parcel for construction staging and timing of parcel being turned over to the City for a park.
- Is condition of 1.4-acre parcel (i.e., any required site cleanup) suitable for a public park?

### *Alternative 2 – North Parcel Condominium; City Ownership*

This alternative would keep the current site plan and building configurations, including the shared podium garage structure, mostly intact. A condominium plan would be created, with the City and Sobrato jointly owning the shared podium garage, the City owning the “air rights” to the two North Parcel buildings (N2 and N3, shown on the site plan), and Sobrato owning “air rights” to N1 and N4. The N2 and N3 buildings would be leased to an affordable housing developer. The project’s affordable housing obligation as a result of the 404 market-rate units under this Alternative is 61 BMR units. Instead of building the units, Sobrato would pay or provide as a credit toward the purchase of Lot B an estimated amount of \$8.9 million. This payment/credit represents the value of 0.89 acre of land (at \$10 million per acre) that would have been dedicated to meet the project’s affordable housing obligation. The \$10 million per acre amount is the City’s estimate of land value that was used to calculate the project’s parkland dedication requirement.

#### *Advantages*

- Total units remain as proposed (635 overall units).
- The two City-owned buildings, N2 and N3, would include approximately 231 affordable units, which represents 36 percent of the 635 market-rate units.
- The site plan and building designs would remain as proposed with the current proposal, unless the City decided to modify Buildings N2 and N3 to accommodate a target population.
- Sobrato could build both the market-rate and affordable housing elements of the project, provided an affordable housing developer secures funding.

### *Considerations*

- The City, as part owner, would be responsible for joint maintenance and ownership responsibilities of the shared parking garage.
- The City would not have the site control that it would have under Alternative 1 because it does not possess sole ownership of the property. Future uses of the City's ownership interest in Alternative 2 is more limited/complex.
- City would receive \$8.9 million as payment/credit to satisfy the project's affordable housing obligation.
- Cost to the City to buy the "air rights" could be approximately \$19.9 million after the \$8.9 million credit was applied, although the amount could be slightly less depending on how the "air rights" were ultimately valued.
- The City and/or a future affordable housing developer, would assume responsibility for complying with the Plan's local school strategy.
- City would receive approximately \$10 million in Park Land fees and a 1.4-acre land dedication for a park.
- A number of agreements would be needed to implement this alternative, including a Purchase and Sale Agreement, CC&Rs, Owners Association Agreement, Ground Lease, City Regulatory Agreement, City Loan documents if the City provides any financing, a garage construction agreement, and a Development Agreement between the City and Sobrato that addresses the time frame for the completion of the subdivision, conveyance, garage construction, and housing construction.
- The City would need time to develop any required legal agreements as part owner of the site.
- Unlikely to resolve all outstanding issues in time for the October 23, 2018 City Council meeting.
- Phasing plan, and use of the 1.4-acre parcel for construction staging, and timing of parcel being turned over to the City for a park.
- Is the condition of the 1.4-acre parcel (i.e., any required site cleanup) suitable for a public park?

- The timing of the condominium subdivision and transfer to the City needs to be addressed in the context of the phased construction plan, the use of the North Parcel for parking during the initial phases of construction, and ensuring the developer meets the affordable housing requirements even if the second phase of the project were never built.

### *Further Issues for Consideration*

#### Affordable Housing Process and Cost

##### *Gatekeeper Proposal*

Under the current proposal, Sobrato would satisfy their affordable housing obligation (15 percent of total units) by dedicating 1.4 acres to the City. The City could then potentially build between 100 and 140 affordable housing units on this parcel. It is unclear if additional City contribution beyond the land would be necessary for a project.

##### *Alternatives 1 and 2*

Under both Alternatives, the 1.4-acre parcel proposed for dedication to the City would be used to satisfy, in part, the City's Park Land Dedication Ordinance.

To satisfy their affordable housing obligation, Sobrato proposes to give the City an \$8.9 million to \$9.4 million credit toward the purchase of the North Parcel Lot proposed for affordable housing, depending on the Alternative. The credit figure is based on the proportional value of the current proposal (635 units) to satisfy their affordable housing obligation through dedication of 1.4 acres when compared to the alternatives. Under Alternative 1, which includes up to 427 market-rate units, the credit would be approximately \$9.4 million. Alternative 2, which includes up to 404 units, would be approximately \$8.9 million.

The costs to develop under Alternative 1 would likely be higher since Lots A and B would not share a podium parking garage, but staff does not have a cost estimate at this time.

It is important to note that the City's expectation of the amount of City subsidy for the affordable housing component of Alternative 1 or 2 would be the value of the land, and that the affordable housing developer maximizes the amount of external funding sources leveraged to finance the project. However, if the affordable housing developer

is unable to secure all of the external funding needed, the City could be asked to provide an incremental amount of subsidy on top of the land.

### *Implementation and Risk*

Sobrato intends to construct the project in two phases, a South phase and a North phase. In the current phasing plan, the South phase is built first, but the affordable housing component under the Alternatives is in the second (North) phase. Council would need to approve this exception to the guidelines. There is some risk to the City in such a phased construction approach. In order to ensure the developer meets its affordable housing obligations, staff believes the City should acquire the property earlier in the process so that if, for any reason, only the South phase is built, the City would have control of the land that is to be dedicated by the developer to satisfy its obligation.

If the North Parcel affordable housing funding gap is not resolved under Alternative 2 (condo subdivision and shared parking garage) within a certain timeframe, then there exists the potential that the rental units on the North Parcel could not be constructed together (i.e., podium garage and buildings). The Council could consider a condition to insure the developer complies with the affordable housing obligations required for the project approval. If the Council is inclined to direct staff to move forward with Alternative 2, then staff would work with the developer to draft a condition to address this concern.

**Question No. 1:** Does Council prefer the original gatekeeper proposal, Alternative 1, or Alternative 2?

### **RECOMMENDATION**

Provide direction on a preferred development proposal as outlined in the report.

### **NEXT STEPS**

Following Council direction from this meeting, Sobrato will submit any required plans or information to the City. Staff will then review this information for completeness in preparation for a Zoning Administrator public hearing and planned City Council meeting on October 23, 2018. However, if Alternative 1 or 2 are preferred by Council, the October Council date would be very difficult to meet, and likely delayed, due to the number of additional details that would need to be worked out in the coming weeks.

**PUBLIC NOTICING**

Agenda posting, and notifications sent to property owners within a 500' radius of the project, including the Santiago Villa mobile home residents.

MA-WC/3/CAM  
891-09-11-18SS

Attachments: 1. Sobrato May 2018 Letter  
2. September 4, 2018 City Council Report