



# Memorandum

**TO:** HONORABLE MAYOR,  
CITY COUNCIL AND  
SUCCESSOR AGENCY BOARD

**FROM:** David Sykes

**SUBJECT:** SEE BELOW

**DATE:** March 25, 2016

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**COUNCIL DISTRICT:** 10

**SUBJECT: POTENTIAL ACQUISITION OF 5647 GALLUP AND 1171 MESA FOR A FUTURE AFFORDABLE HOUSING DEVELOPMENT**

## **RECOMMENDATION**

(a) City Council adopt a resolution:

- (1) Authorizing the Director of Housing, on behalf of the City, to negotiate and execute: (i) a purchase and sale agreement to acquire that certain real property located at 5647 Gallup and 1171 Mesa in San José from the Successor Agency to the Redevelopment Agency (SARA) of the City of San José for \$1,170,000 from the Community Development Block Grant (CDBG) Fund for a future affordable housing development; and (ii) such other documents as necessary to close escrow to acquire the properties; and
- (2) Authorizing the Director of Housing to issue a Request for Proposal (RFP) for development of a future affordable housing community located at 5647 Gallup and 1171 Mesa, if the City is successful in acquiring the properties.

(b) Successor Agency adopt a resolution authorizing the Managing Director to negotiate and execute (i) a purchase and sale agreement to sell that certain real property located at 5647 Gallup and 1171 Mesa in San José to the City of San José for a purchase price of \$1,170,000; and (ii) such other documents as necessary to close escrow to acquire the properties.

(c) City Council adopt the following 2015-2016 Appropriation Ordinance amendments in the Community Development Block Grant Fund:

- (1) Increase the appropriation to the Housing Department for Property Acquisition in the amount of \$510,000; and
- (2) Decrease the Land Acquisition Reserve appropriation in the amount of \$510,000.

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## **OUTCOME**

Approval of the recommended actions will allow the Successor Agency to sell and the City to acquire the real property located at 5647 Gallup and 1171 Mesa, which property will be used for a future affordable housing development.

## **BACKGROUND**

San José is currently experiencing a housing crisis. Approximately 44% of the City's residents are "cost burdened" - i.e. are paying more than 30% of their gross incomes on rent. As of June 30, 2015, the average rent for a two bedroom two bath apartment in San José was \$2,750. This represents a 37% increase over the past five years. In 2015, the annual Area Median Income (AMI) for a household of two in San José was \$85,050 while the annual salary required to afford a two bedroom two bath "market rate" apartment was \$112,519. Over the past year, apartment vacancy rates have fluctuated from 3.3% to 5.4%. As reported by Real Facts, rents are predicted to increase an additional 7% to 10% in 2016. As a result, there is currently a severe shortage of adequate, affordable housing for extremely low-, very low-, low-income, and moderate-income households.

Although the aforementioned affordability imbalance negatively impacts a large number of San José residents, the City's most vulnerable population – those living without shelter – experience even greater challenges in finding safe, stable, and affordable places to live. To address this significant issue, City Council has taken several recent actions to create housing solutions for homeless individuals, including: permanent supportive (489 units), interim (349 units), and emergency shelter (165 beds) options. Staff plans to return in late Spring to both the Neighborhood Services and Education Committee and the Community Economic and Development Committee to provide a comprehensive update on the status of these and other initiatives that will expand the number of housing options for the homeless in San José.

While the need for continued focus on homeless housing persists, some development opportunities may be more suitable for a mixed-income affordable housing. The Housing Department has identified two properties, currently owned by SARA that would be ideal for the development of a future affordable housing community.

### **Disposition Process for SARA Property**

As part of the dissolution process of the former Redevelopment Agency (RDA), SARA was required to prepare a Long Range Property Management Plan ("LRPMP"), which addressed the disposition and use of the real properties owned by SARA. Final approval of the LRPMP by the Oversight Board and the State Department of Finance ("DOF") was obtained in September 2014. The Property is designated for sale in SARA's LRPMP. In connection with approving the LRPMP, the Oversight Board also approved a Disposition Process which provides two methods of selling SARA owned property: an open solicitation process and a direct sale process. Under

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the direct sale process, taxing entities and certain non-profit organizations were allowed to acquire property directly from SARA at the appraised value of the property as established by an appraiser approved by the Oversight Board.

On September 17, 2014, SARA staff sent a letter to the City Manager stating that the City had until October 21, 2014, to indicate interest in acquiring any of the SARA owned properties that were designated for sale. The City responded to SARA within the applicable time period, indicating an interest in acquiring the following properties: The Central Place Parking Garage located at 88 East San Fernando Street; two adjacent parcels located at 5647 Gallup Drive and 1171 Mesa Drive in the Hoffman Via Monte area of San José; a parking lot located at 226 Balbach Street; and a small 10,000 square foot strip of land located adjacent to the Mexican Heritage Plaza at 1770 Alum Rock Avenue.

### **5647 Gallup Drive and 1171 Mesa Drive**

5647 Gallup Drive and 1171 Mesa Drive (“the Properties” or “the Site”) are adjacent sites that combine to be a total of .38 acres. The Site is suitable for an affordable mixed-income housing development. The former Redevelopment Agency acquired the Properties as part of a land assemblage in 2008 for \$2,060,000.

In December 2015, the Housing Department commissioned an appraisal of the Properties. If the Properties were purchased from SARA, the Housing Department anticipates the potential of creating a 25-40 unit affordable housing community. However, the total number of units and tenure (rental vs. for-sale) will not be known until a developer is selected, the City enters into an Exclusive Negotiation Agreement and pre-development work is completed.

## **ANALYSIS**

### **Appraisal**

Pursuant to the Disposition Process, the City selected J Kaeuper & Company (Kaeuper) to prepare and complete an appraisal. Kaeuper was instructed to appraise the site at its highest and best use at fair market value in accordance with the Disposition Process. In February 2016, the Housing Department received the Appraisal from Kaeuper. The fair market value of the Properties was determined to be \$1,160,000.

### **Proposed Approach**

The Oversight Board will consider the City’s acquisition of the Properties for the appraised value of \$1,160,000 on March 24, 2016. If the sale of the Properties is not approved on that date, the Housing Department will update City Council via a supplemental memorandum prior to the meeting on March 29, 2016. If the sale of the Properties is approved on March 24, 2016, and

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City Council directs staff to acquire the Properties on March 29, 2016, staff estimates that the acquisition will be completed in April 2016.

Once the Housing Department purchases the sites from SARA, the Housing Department would issue a Request for Proposals (RFP) to obtain development proposals for the Properties. The RFP will require respondents to submit a proposal that clearly states the overall objective for the development. RFP responses will also address the following items:

- The development's financial viability
- The respondent's qualifications in developing affordable housing
- The financial capacity of the organization to perform
- A public outreach plan to engage with the neighborhood and other stakeholders
- A comprehensive schedule for completing the project

Respondents will be judged by criteria including the following elements:

- Professional qualifications and experience of staff and experts
- Development concept for the Properties
- Understanding the regulatory approval process
- Demonstrated ability to finance development projects
- Developer's ability to perform
- Cost to the City of San José
- Strength of professional references
- Status of the developer as a small business or local business

Once a developer for the future affordable housing development has been selected, the Housing Department will return to the City Council for consideration of an Exclusive Negotiation Agreement (ENA).

### **Due Diligence**

The Housing Department completed internal due diligence before advancing its recommendation to acquire the Properties. As noted previously, the Housing Department commissioned an appraisal of the Properties, resulting in a value of \$1,160,000 or \$70 per square foot. This figure is less than the Housing Department has commissioned recently - including the Plaza Hotel which was valued at \$165 per square foot. Further, the per square foot cost for the 226 Balbach property is significantly lower than the \$200 per square foot value that the SARA received for the Car Wash site located directly across the street from City Hall. The primary reason for the difference in these figures has to do with the fact that land costs downtown tend to be more expensive.

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The Properties' acquisition cost of \$1,160,000 is priced at a level that will make a future affordable housing development feasible. In addition to the cost of acquisition, the Housing Department is requesting up to \$10,000 to cover closing costs.

The Housing Department recently conducted an analysis of the previous five affordable projects that the City funded. This analysis showed that the average purchase price of each of the five development sites was nearly \$6,200,000 or \$62,000 per unit. Taking into account the Housing Department's goal of developing 25-40 affordable units on the Properties, the per-unit acquisition cost of \$29,000 - \$46,400 per unit is very reasonable.

Once the Properties are owned by the City, the Housing Department will conduct a competitive process to select a developer for the Site. Working with the City, the developer will identify the target population, proposed income and affordability mix, and embark on a comprehensive community process. The Housing Department has not determined when the RFP for the site will be released, but it will likely be sometime next fiscal year.

Finally, the development team will conduct extensive due diligence to research and determine the appropriate number of units for the future affordable housing development based on numerous factors including:

- Conformance with the General Plan;
- Determination regarding the site's zoning;
- Analysis on the site's density potential;
- Compliance with the California Environmental Quality Act (CEQA); and
- Potential for securing Federal, State, and local funding sources to develop a future affordable housing community.

At the conclusion of the due diligence period, when the development opportunities are better understood and a proposed development plan is deemed appropriate for the site, the Housing Department will seek City Council approval to move the project forward.

### **EVALUATION AND FOLLOW-UP**

The status of the Site will be reported to the public in the Housing Departments periodic Production report, posted to its website in the Data and Reports section at [www.sjhousing.org](http://www.sjhousing.org). Housing staff will return to Council to seek funding for a proposed project when the development plan has been finalized and a developer has been selected.

## **POLICY ALTERNATIVES**

To arrive at this proposal, staff considered the following option:

**Alternative:** Look for opportunities other than 5647 Gallup and 1171 Mesa as future affordable housing development sites.

**Pros:** The Properties would be sold through a solicitation process to the highest bidder which would potentially allow for private development of the properties.

**Cons:** Finding suitable sites for affordable housing at reasonable prices is extremely difficult.

**Reason for not recommending:** The Properties present a viable opportunity for the City to increase the supply of affordable housing in San José.

It should be noted that the acquisition of this site was included in the Housing Department's *Affordable Housing Investment Plan for FY 2015/16 – FY 2016-17*. However, if the City Council is not interested in acquiring the Properties for affordable housing, SARA staff will solicit proposals for the sale of the Properties. The Properties would then be sold to the highest bidder. In that case, City staff would look for alternative sites other than the Properties for the development of permanent supportive housing for the homeless.

## **PUBLIC OUTREACH**

The Housing Department hosted a community meeting on March 17, 2016 at the Almaden Hills Methodist Church. At the meeting, the attendees provided input on the City's intent to acquire the Properties. More specifically, the attendees asked that the Housing Department continue to engage with the community if/when the development moves forward. The Housing Department committed to working with the community throughout the project's future predevelopment and entitlement processes, if applicable.

The City will post this memorandum to the City's website for the April 5, 2016 City Council meeting.

## **COORDINATION**

Preparation of this report was coordinated with the Office of the City Attorney.

**COMMISSION RECOMMENDATION**

Review of specific affordable housing developments is not under the purview of the Housing and Community Development Commission (HCDC). The Commission did have the opportunity to provide input to the *Affordable Housing Investment Plan for FY 2015/16 – FY 2016-17* prior to its adoption by City Council. This plan included the acquisition of this site.

**FISCAL/POLICY ALIGNMENT**

This expenditure is consistent with: the City's *Envision 2040 General Plan and the 2014-23 Adopted Housing Element* in that it will help the City meet its Regional Housing Needs Allocation and the City's 15% affordable housing goal by providing affordable apartments for extremely low- and very low-income residents. It is also consistent with the City's *2015-20 Consolidated Plan* in that it will provide units that will be affordable for very low- and extremely low-income households. Acquisition of this site was included in the Housing Department's *Affordable Housing Investment Plan for FY 2015/16 – FY 2016-17*.

**COST SUMMARY/IMPLICATIONS**

**1. AMOUNT OF RECOMMENDATION:**

<b><u>EXPENSES</u></b>	<b><u>AMOUNT</u></b>
Acquisition	\$1,170,000
<b>TOTAL</b>	<b>\$1,170,000</b>

**2. SOURCE OF FUNDING:** Community Development Block Grant Fund (441)

**3. FISCAL IMPACT:** In the Community Development Block Grant Fund, \$660,000 of the \$1,400,000 budget for Property Acquisition will be allocated to this project. An additional \$510,000 is recommended to be added to this appropriation, which would allow for disbursement up to \$1,170,000 for the purchase of property located at 5647 Gallup and 1171 Mesa in San José.

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**BUDGET REFERENCE**

The table below identifies the fund and appropriations proposed to fund the actions recommended as part of this memorandum.

Fund #	Appn #	Appn. Name	Total Appn	Proposed Action	2015-2016 Adopted Operating Budget	Last Budget Action (Date, Ord. No.)
441	8463	Land Acquisition Reserve	\$1,555,387	(\$510,000)	XI-15	10/20/15 Ord. 29636
441	3115	Property Acquisition	\$1,400,000	\$510,000	XI-15	10/20/15 Ord. 29636

**CEQA**

Exempt, File No. PP16-007.



David Sykes  
Assistant City Manager and  
Executive Officer, Successor Agency

For questions, please contact Jacky Morales-Ferrand, Housing Director, at (408) 535-3855.

Attachment: Site Map

Attachment  
Map  
5647 Gallup and 1171 Mesa

