



City of Emeryville

CALIFORNIA

MEMORANDUM

DATE: November 16, 2021

TO: Christine Daniel, City Manager

FROM: Charles S. Bryant, Director of Community Development

SUBJECT: Study Session – EmeryStation Overland Project, 1580 62nd Street
Part 1: Conversion of Existing Live/Work Units to Below Market Rate Units for Development Bonus Points Under Flexible Community Benefit

RECOMMENDATION

Staff requests that the City Council consider this staff report and provide comment.

BACKGROUND

Wareham Development is proposing to construct a new 5-story, 300,000 square foot Research and Development building with a 496 space 7-level parking garage on the western portion of the block bounded by 62nd and 63rd Streets and Overland Avenue, to be called “EmeryStation Overland” (the “Project”). The Project will need 100 development bonus points for height because a portion of the site containing the proposed garage is in the 30’/55’ height district and the garage will have a height of 55’, the maximum allowable with a bonus. Pursuant to the Planning Regulations, 50 of the bonus points must come from paying an increased Affordable Housing Impact Fee, and the other 50 points must come from the provision of other community benefits. One of the categories of community benefits, called the “Flexible Community Benefit”, allows developers to propose a unique community benefit, which must be approved by the City Council based on 10 bonus points for every 1% of project construction valuation. Use of the Flexible Community Benefit also triggers City Council approval of the entire project upon a recommendation from the Planning Commission.

Wareham has proposed that, in order to earn 30 community benefit bonus points, a portion of the live-work units in the adjacent Hollis Street Building be set aside as Below Market Rate (BMR) units. On July 20, 2021, the City Council held a study session to consider this proposal and provide direction to staff. The City Council expressed openness to the concept of providing BMR units in the Hollis Street Building for Flexible Community Benefit Points and provided the following direction to staff:

- Form of Benefit – BMR units are to be regulated through a covenant in the form of an Affordable Housing Agreement consistent with the City’s established Affordable Housing Program (“AHP”) with a term of 55 years.

- Number of Units – Provide a minimum of nine BMR units. If the agreed-upon number of units is insufficient to provide the Flexible Community Benefit amount required, the developer should contribute the balance to a capital project specified by the City Council.
- Calculation of Flexible Benefit Amount – Utilize a Net Present Value model to calculate the current value of the future affordable rents to be provided, with a discount rate 2 to 2.5 percent higher than the assumed rental rate increase and incorporating an assumed vacancy rate.
- Affordable Rents – Rents are to be established pursuant to the City of Emeryville’s published Housing Affordability Table.
- Vacancy – Ensure BMR units are fully occupied, with a low vacancy rate.
- Marketing Plan – Require a marketing plan for the BMR units, consistent with the AHP.
- Continuing Use – Require that BMR units cannot be repurposed for uses other than affordable housing and prohibit demolition of the units during the term of the Affordable Housing Agreement.
- Natural Disaster – Include a plan for the relocation of BMR tenants if a natural disaster occurs that renders the units unlivable.
- Benefit Amortization – Amortize the value of the BMR units to ensure the full benefit value is realized over the 55-year term.
- Unit Condition – BMR units should be renovated and upgraded.

If Wareham ultimately decides not to pursue the Flexible Community Benefit, then approval of the project will be decided by the Planning Commission, whose decision will be appealable to the City Council. In order for the Council to remain unbiased in the event that the Flexible Community Benefit is not pursued and the Planning Commission decision is appealed, this study session focuses narrowly on the issue of the Flexible Community Benefit, with only enough information about the overall project to provide context for the Council’s discussion. On the other hand, if Wareham ultimately decides to pursue the Flexible Community Benefit, meaning that the decision on the project would be made by the City Council, then a Council study session on the full project will be held as a separate agenda item immediately following the Flexible Community Benefit discussion.

DISCUSSION

Using the City Council’s direction to staff as outlined above, staff has negotiated terms for the provision of development bonus points through the Flexible Community Benefit, which could form the basis for a potential Affordable Housing Agreement with Wareham. The terms are summarized in Attachment 1 and described further below.

Flexible Community Benefit

As described above, the Flexible Community Benefit is monetized as 10 bonus points for every one percent of Project construction valuation. The City’s practice is to use the Building Permit Valuation for the Project to determine construction valuation, which is defined by Emeryville Municipal Code (EMC) Section 8-1.04(v) and is a comprehensive definition of construction costs. Wareham provided a construction cost estimate prepared by contractor DPR Construction that indicates total Project costs are expected to be approximately \$163,990,000, inclusive of contingencies. To obtain 30 bonus points, the Flexible Community Benefit value must equal three percent of \$163,990,000 (i.e., \$4,919,730).

Designation of Affordable Units

Staff conducted a site visit to view the units at the Hollis Street Building to determine unit condition and configuration. The units are extraordinary in terms of size, openness, light and character, and are ideally configured for a wide range of creative activities. Due to the size of the units, staff recommends designating units that either have interior partitioned rooms or a second story loft area as one-bedroom units. Staff also determined current market rents based on the rent roll for the property. The current rents for all similarly sized units were used to derive a per-square-foot market rent, which was then applied to the square footage of each unit proposed to be BMRs. In terms of affordability levels, this proposal includes three very low-income and seven low-income units for a total of ten units. Moderate-income rents are not proposed as they are comparable to market rate rents, and therefore provide little benefit.

Pursuant to the City’s Housing Affordability Table, very low-income units are limited to households making up to 50% of the Area Median Income (AMI), and low-income units are limited to households making 51% to 80% of AMI. Very low-income rents are limited to 30% of 50% of AMI, and low-income rents are limited to 30% of 60% of AMI. The table below lists the ten units proposed for BMR use and their proposed affordability levels, with corresponding rents per the City’s current Housing Affordability Table:

Unit #	Square Feet	Designation	Affordability Level	Market Rent	Affordable Rent
1504	1,027	1 Bedroom	Very Low	\$2,593	\$1,256
1512	1,027	Studio	Low	\$2,593	\$1,319
1518	1,027	1 Bedroom	Low	\$2,593	\$1,508
1531	1,461	2 Bedroom	Low	\$3,688	\$1,696
1533	1,078	1 Bedroom	Low	\$2,721	\$1,508
1539	1,598	1 Bedroom	Low	\$4,034	\$1,508
1558	1,123	1 Bedroom	Low	\$2,709	\$1,508
1566	1,073	1 Bedroom	Very Low	\$2,835	\$1,256
1576	1,121	1 Bedroom	Very Low	\$2,830	\$1,256
1508	1,027	1 Bedroom	Low	\$2,593	\$1,256

Calculation of Flexible Community Benefit Value

In accordance with the direction of the City Council, staff utilized a net present value methodology to determine the value of providing the proposed units at the proposed affordability levels. This model principally relies on conservative assumptions that are industry standard for lenders' underwriting of affordable housing projects. Specifically, rent growth is assumed at 2.5% annually, the discount rate is 5%, and the vacancy rate is 7%. Vacancy rates are typically assumed at 5%, however, this proposal utilizes a higher vacancy rate for purposes of modeling the benefit value, for reasons discussed further below under "Amortization of Flexible Community Benefit".

When these assumptions are applied to the difference between the market rents and the affordable rents over a 55-year term, the net present value equals approximately \$4,960,000, which exceeds the required Flexible Community Benefit by approximately \$40,000.

Amortization of Benefit Value

During its study session on July 20, 2021, the City Council discussed the concept of "amortization" of the Flexible Community Benefit, with the intent of ensuring that the full value of the Flexible Community Benefit is realized over the term of the Affordable Housing Agreement. Staff understands this is intended to hedge against future risk that the difference between AMI (which is the basis for affordable rents) and market rate rents decreases over time (i.e. housing becomes more affordable), which would diminish the value of the Flexible Community Benefit.

AMI is less volatile than local area rents, and HUD is incentivized to avoid extraordinary fluctuations in AMI because affordable housing projects depend on the affordable rent limits derived from the AMI. HUD policy limits the annual decrease in area limits to 5% and limits the annual increase to 5% or twice the annual percentage change in the national median income if greater. Therefore, because AMI is independent of and more stable than rents, it is likely that in short-run time periods the benefit could be greater or less than modeled. Nevertheless, over a 55-year time period these differences would be expected to offset each other.

However, to provide some assurance that the value of the Flexible Community Benefit will be realized over time, this proposal relies on conservative assumptions for modeling the value of the benefit. The rent growth assumption of 2.5% is used by lenders underwriting the financing of affordable housing projects, as such it is a conservative figure. The discount rate of 5%, when applied to a net present value calculation for these purposes, is in part intended to hedge future risk. Finally, while a vacancy rate of 5% would be typical for underwriting standards, this proposal assumes 7% vacancy, which provides additional buffer for future conditions. This approach was used to address the amortization issue described above.

Renovations

All BMR units would be renovated to bring them to a comparable level of quality, including newer appliances, cabinets/vanities, countertops and floor coverings. Showers and tubs

would be replaced where visible staining or evidence of leakage or caulk deterioration is observed. All BMR units would be required to be inspected for life safety systems and unpermitted work, and any deficiencies corrected.

Marketing Program

A marketing program will be required by the Affordable Housing Agreement. The Marketing Program would be consistent with the City's Marketing Program Procedures and submitted to the City for review at least 120 days prior to lease-up.

Annual Report

Consistent with the City's AHP, an annual report that includes tenant income recertifications will be required.

Vacancy/Continued Use

The Affordable Housing Agreement would include a provision that automatically extends the term of the Affordable Housing Agreement if, as evidenced by the annual report, vacancy rates exceed 20% when reviewed at the third, tenth and twentieth year of the agreement. The developer may request a unit remain vacant for a defined period of time if extensive repairs are required, without counting against the 20% vacancy limitation. Consistent with the City's standard practice, the Affordable Housing Agreement would prohibit the demolition of any BMR unit during the term of the agreement.

Natural Disaster

In the event of a natural disaster that renders the affordable units unlivable, the developer would be required to provide relocation assistance for tenants of the affordable units. The relocation assistance would include actual and reasonable moving expenses plus the additional amount necessary to enable the person to rent a comparable replacement unit for up to 42 months, in an amount not to exceed \$5,250. This relocation provision is derived from state law.

Summary

Staff and Wareham have negotiated the above terms for providing a Flexible Community Benefit of providing ten BMR units at the Hollis Building, calculated at a value of \$4,960,000. The proposal presents an opportunity to add a unique type of housing to the City's affordable housing portfolio.

FISCAL IMPACT

This item is for informational and discussion purposes only and has no direct fiscal impact.

STAFF COMMUNICATION WITH THE PUBLIC

None.

CONFLICT OF INTEREST

None.

CONCLUSION

Staff requests that the Council discuss the proposed Flexible Community Benefit terms and provide feedback. If the City Council agrees with the terms and Wareham decides to continue with the proposed Flexible Community Benefit, the City Council is scheduled to hold a study session on the Project immediately following the conclusion of this item. Staff will continue to work toward implementing agreed-upon terms through an Affordable Housing Agreement, which will be presented to the City Council for approval at a future meeting.

PREPARED BY: Chadrick Smalley, Economic Development and Housing Manager

**APPROVED AND FORWARDED TO THE
CITY COUNCIL OF THE CITY OF EMERYVILLE:**



Christine Daniel, City Manager

ATTACHMENT:

1. EmeryStation Overland Affordable Housing Term Sheet