



Date: March 21, 2016
Current Meeting: April 7, 2016
Board Meeting: April 7, 2016

BOARD MEMORANDUM

TO: Santa Clara Valley Transportation Authority
Board of Directors

THROUGH: General Manager, Nuria I. Fernandez

FROM: Chief Financial Officer, Raj Srinath

SUBJECT: Amendment to Joint Development Policy to include VTA Affordable Housing Policy

Policy-Related Action: Yes

Government Code Section 84308 Applies: No

ACTION ITEM

RECOMMENDATION:

Approve the addition of a new Section VI of the *VTA Affordable Housing Policy* to the *Joint Development Policy Guidance Documents, Part II: Implementation Plan*, and renumber existing Sections VI, VII, and VIII to Sections VII, VIII, and IX, respectively. The VTA Affordable Housing Policy would set forth one or more VTA strategies, to promote affordable housing development at VTA Joint Development sites and on other real estate owned by VTA.

BACKGROUND:

Santa Clara County continues to have one of the most expensive real estate markets in California and the need for affordable housing has recently increased to what many consider a regional state of distress. Silicon Valley is known world-wide for its innovation and flourishing economy. However, the distribution of income and wealth is uneven and has resulted in a housing market in which new market-rate residential development is oriented towards upper income households.

Cities in the County and other high cost areas of the State have not seen sufficient housing production to meet the needs of households at all income levels, particularly low-income households. The dissolution of California's redevelopment agencies removed a key source of funding, creating an increased burden for local jurisdictions to fund affordable housing and legal challenges to inclusionary requirements¹ have created impediments to the ability of local

¹ Notably the case *Palmer vs. Los Angeles* found that inclusionary housing requirements for new rental units violate the limitations on rent control established by the Costa Hawkins Rental Housing Act of 1995.

jurisdictions to secure additional affordable housing within their borders.

Affordable housing advocates in California have, over the past several years, focused on how public agencies, including transit agencies, can use their land holdings to increase production of affordable housing. Locally, VTA has been approached by multiple affordable housing stakeholders in the region, including SV@Home, Working Partnerships, Silicon Valley Leadership Group and various affordable housing developers. VTA has no adopted policy regarding development of affordable housing as part of VTA's Joint Development Policy. These organizations are seeking for VTA to adopt a policy in support of affordable housing.

As noted in the Joint Development Program update, VTA intends to issue multiple competitive developer offerings for joint development opportunities this year and into 2017. We expect affordable housing advocates to push for VTA to include affordable housing in conjunction with each joint development offering and the Staff believes that a clear policy statement by VTA on this subject would expedite the creation of joint development agreements, by eliminating the need to revisit affordable housing issues each time a joint development is proposed or negotiated. VTA seeks to develop mixed-use communities around transit, and any Affordable Housing Policy adopted by the Board would be integrated into VTA's Joint Development Policy, and would advance the goal of creating mixed-income communities around transit.

DISCUSSION:

A. KEY CONSIDERATIONS

Any discussion of an Affordable Housing Policy for VTA Joint Development should be informed by several key considerations, including: (i) development feasibility, (ii) actions taken by local jurisdictions to encourage or develop affordable housing; (iii) actions taken by the state legislature to encourage the development of affordable housing; (iv) actions taken by California transit agencies to encourage affordable housing in transit-oriented development; and (v) potential impacts of an Affordable Housing Policy on VTA's Joint Development Policy including revenue generation.

(1) Development Feasibility

Developers perform financial modeling to determine whether a potential project is a sensible investment that provides a minimum required return on investment. This involves calculation of the total value of the completed project versus the total costs of development, in order to identify whether a project is feasible (i.e. can it cover all costs, including land) and provides the required return on investment. The required return on investment is identified by each developer based on market, development product type, available capital and an assessment of project risk.

From a developer's perspective, new requirements to produce additional affordable housing result in lower revenues, and this reduction in revenues must be offset from other costs. Since there is limited flexibility in construction costs and the required return on investment, reducing the amount paid for developable land is the most straightforward way to offset the impact of an affordable housing obligation or in-lieu payment requirement. Land owners, particularly those under no pressure to sell, are typically unwilling to reduce their sale price. When markets

experience increases in rental rates and sale prices, and therefore an increase in supportable land values, there is less impact to developers and land owners from new affordable housing requirements.

For-profit or non-profit developers who build residential projects with 100% affordable units make a different calculation on feasibility than market-rate developers. Development of affordable housing faces the challenge of layering multiple funding sources (often up to 10 or more) in order to be able to cover project costs, since the lower revenues from affordable units cannot support as much debt financing as market-rate development. While affordable housing developers often seek discounted or free land to reduce their costs, they also regularly pay fair market value for development sites in order to be able to compete with market-rate developers.

(2) Local Jurisdictions

Inclusionary Requirements. Inclusionary housing requirements for for-sale residential units have been implemented by local jurisdictions and such requirements have recently been upheld by the California Supreme Court.² Within Santa Clara County, cities that have adopted inclusionary housing requirements have generally set them in the range of 10% to 20% of all for-sale units.

In-lieu fees. A second mechanism for advancing development of affordable housing is through in-lieu fees or linkage (impact) fees. For cities that adopt these fees, each developer (including for commercial development) must pay a fee to the City in place of providing affordable units within the project, and/or to help fund the cost of the increased need for affordable housing created by the particular development project. This creates a funding source that can be applied to subsidize affordable housing developments.

Density Bonuses. State planning law requires cities to provide developers with a density bonus that authorizes additional development beyond what is allowed by local zoning, in return for using some of the additional development envelope to build affordable housing in the project.

More recently, advocates and some jurisdictions have expanded this concept to look at the value that is created any time a City “upzones” (increases allowable development) for a property, or takes other action that increases the value of land for development. The concept is to use “value capture” techniques so that landowners and developers are able to realize that value from denser zoning is conditioned upon their making additional voluntary payments, *i.e.* providing a public benefit, to fund affordable housing or other local needs.

(3) Actions taken by the State Legislature to Encourage Development of Affordable Housing.

In California, financial impetus for development of affordable housing is provided through a complex layering of local, state and federal funds as well as laws requiring inclusionary development and certain preferences given to affordable housing developers in the acquisition of government surplus properties. Action by the State Legislature has sought to provide more

² In 2015, the California Supreme Court upheld inclusionary requirements in the case *California Building Industry Association v. City of San Jose*. In February 2016, the U.S. Supreme Court declined to hear an appeal of that case brought by the California Building Industry Association.

support for affordable housing production, including:

(a) California Planning Law

The Regional Housing Needs Allocation (RHNA) is a state-mandated process to identify the allocated number of affordable housing units for each jurisdiction, which then must be reflected in the jurisdiction’s Housing Element, as a required part of its General Plan. The Association of Bay Area Governments (ABAG) administers the Sustainable Communities Strategy (SCS) known as *Plan Bay Area*, which forecasts the total housing needs for the San Francisco Bay Area for an eight-year period. Jurisdictions are required to update their Housing Elements to demonstrate how their portion of the responsibility will be achieved. The final RHNA for Santa Clara County for the eight-year period of 2014-2022 is shown in Table 1, below:

Table 1: *Plan Bay Area* - Regional Housing Needs Allocation for Santa Clara County, Dwelling Units by Household Area Median Income

Very Low < 50% AMI ³	Low 51-80% AMI	Moderate 81-120% AMI	Above Moderate 120%+ AMI	Total
16,158	9,542	10,636	22,500	58,836

*[http://www.abag.ca.gov/planning/housingneeds/pdfs/Final%20RHNA%20\(2014-2022\).pdf](http://www.abag.ca.gov/planning/housingneeds/pdfs/Final%20RHNA%20(2014-2022).pdf)

(b) AB 2 - California Revitalization and Investment Authorities

As noted above, legislation introduced by Governor Brown and approved by the legislature dissolved California redevelopment agencies as of February 2012 and removed the 20% set-aside of redevelopment tax increment that was one of the primary source of funds for affordable housing. Last year, AB 2 was passed which authorizes the creation of Community Revitalization and Investment Authorities (CRIA), along with the use of tax increment finance for allowed purposes in project areas. However, one of the requirements to establish a project area is that household income cannot exceed 80% of the *statewide* median, which severely limits the areas where it can be used in high-cost coastal areas, such as Santa Clara County and its cities.

(c) AB 2135 - Surplus land: Affordable Housing

In January 2015, AB 2135 became law. AB 2135 strengthened existing provisions of the California Government Code, originally adopted in 1968, that require local agencies disposing of “surplus” real property to adhere to a protocol intended to increase the likelihood that such surplus property will be developed for affordable housing. These provisions,⁴ require a public agency disposing of surplus land to offer it for sale first to private entities or public agencies for a number of specified uses (including affordable housing, schools, enterprise zones and open space) with preference given to the development of affordable housing. Under this law, if a

³ Housing affordability is defined by categories established by the US Department of Housing and Urban Development (HUD) and is generally categorized into four areas: “Moderate,” “Low,” “Very Low” and “Extremely Low.” These terms are based on a share of the Area Median Income (AMI) for various household sizes, which is calculated annually by the California Department of Housing and Community Development (HCD).

⁴ Currently found at Government Code Sections 55220-54233.

disposing agency receives notice that a party is interested in acquiring the surplus property for the purposes enumerated in Government Code Section 54222, it must first negotiate for the purchase and sale of the surplus property with the interested party (or parties). AB 2135 amended these provisions to require, among other things, that:

- (i) at least 25% of the units in any proposed affordable development must be made available at affordable housing cost.⁵
- (ii) if an agency is not able to reach agreement with interested agencies and the agency disposes of the land to an entity that uses the property for the development of 10 or more residential units, then that entity or a successor-in-interest must provide not less than 15 percent of the total number of units developed at affordable housing cost. (This amended the old law, which allowed sale without restriction if agreement could not be reached with, or no offer was forthcoming from, a party proposing development for one of the purposes set forth in Section 54222.)
- (iii) affordability restrictions must be preserved through deed restrictions on the surplus properties (thus the affordability requirements will follow the land).

AB 2135 also explicitly permits local agencies to sell properties at below market value. AB 2135 has not, however, changed the applicability of the properties to which the obligations under Section 54222 apply. Since its original adoption, this law has only applied to situations where a public entity disposes of property that it “determines” to be “surplus” to its needs. In the case of VTA, a joint development project that directly implements a public transit purpose is not “surplus” to VTA’s needs as VTA still retains an interest in the property, which is being utilized for a public transit purpose. As a result, such a project would not be subject to the provisions of the Government Code’s surplus property sale requirements.

(4) VTA Experience with Affordable Housing

VTA has to date completed two joint development projects with a total of 444 dwelling units, 55% of which are affordable (this includes 100% affordable housing development at the Ohlone/Chynoweth station). The proposed joint development project at the Tamien station, if rezoning is approved by the San Jose City Council, would include between 390 and 440 dwelling units, with the percentage that is affordable to be determined.

(5) Other Transit Agencies’ Approach to Affordable Housing

Metro (Los Angeles County) and BART are two other California transit agencies with rail service that have been engaged in discussions on including affordable housing in their joint development activities. SANDAG and MTS (San Diego County) and Sacramento Rapid Transit are following this issue, but they have yet to formulate policies regarding affordable housing in joint development. A brief summary of actions by BART and Metro follows:

- **BART.** The BART Board recently adopted a policy that sets a target for 20% overall

⁵ Prior to adoption of AB-2135, the law did not specify a minimum percentage of affordable housing required in affordable developments.

inclusion of affordable housing in each station area and for the system overall. This target would not apply to each joint development project: however, by the time of build-out of joint development sites at each station, and for the overall BART system, the 20% target would be realized. Competitive developer submittals for joint development would be evaluated based on the amount of affordable housing that would be created, with priority in evaluation for units for low-income household below 55% of Area Median Income. (Note that this policy affects BART-owned stations, and not stations in the SVRT project.)

BART has to date completed four joint development projects, with a total of 565 dwelling units, 33% of which are affordable (this includes a 100% affordable senior housing project). BART has five approved joint development projects, two of which are under construction, which will create 1,774 dwelling units, with 29% of those units affordable (this includes 100% affordable housing project at one station).

- METRO (LOS ANGELES COUNTY). Metro's Board has adopted a target for joint development across its system, rather than a project-level requirement, to result in 35% affordable housing production. To further this goal, Metro would consider up to a 30% write-down in land value for affordable housing development. Metro staff is currently working on implementation of this target.

Metro is currently working on joint development of two 100% affordable housing projects in East Los Angeles. These projects will involve significant land write-downs by Metro, and Metro has indicated that the Federal Transit Agency (FTA) has signaled its willingness to consider approval of joint development with a partial write-down of land value to support affordable housing as being consistent with FTA's Joint Development Circular and its community purposes provisions.

As the County's Congestion Management Authority, Metro is establishing a \$70 million Transit Oriented Affordable Housing Loan Fund to support predevelopment expenses, using a \$10 million contribution from Metro and \$60 million in contributions from other organizations (the concept is similar to MTC's recent TOAH fund). Metro is also working with other organizations to combine its funds and other donated funds to create a \$20 million Transit-Oriented Communities Loan Program to support affordable housing development and preservation of existing affordable units.

Metro has to date completed twelve joint development projects, with a total of 2,017 dwelling units, 31% of which are affordable (this includes four 100% affordable housing projects). Two joint development projects are under construction, which will add 149 dwelling units, with 72% affordable (the larger of the two is 100% affordable housing project). Metro is currently negotiating agreements for six additional joint development projects; two of the projects are 100% market-rate (no affordable housing) and total 168 dwelling units; the other four projects are 100% affordable housing developments and total 253 dwelling units.

(6) Impacts on VTA Joint Development Projects.

(a) Revenue Generation.

The VTA Joint Development Policy establishes revenue generation as a primary objective, with proceeds from joint development placed into the Joint Development Program Fund for, “the continued operation and development of the Agency.” The Joint Development Fund has been identified as one of the potential funding sources for the SVRT BART Phase 2 project.

Sale of joint development sites at fair market value to affordable housing developers should have no impact on the revenues that VTA receives from a project. However, requirements for including a set level of affordable units in a mixed-income residential joint development project, or providing partial or full write-downs in land value to support affordable housing development, would be expected to have an impact on the revenues that the Joint Development Fund receives. To the extent that residential sale prices and rental rates continue to rise, the extent of any impact may be reduced compared to land values based on current fair market value.

(b) Other Considerations.

Setting a fixed target for production of affordable housing units in each development project faces the challenge that its impact on development feasibility can vary at different points in the economic cycle. For example, in a market upswing with increasing residential sales prices and rents, the impact of a set target may be reduced. This is particularly the case for a project that involves rezoning to allow denser development - this is why some recent major San Francisco mixed-use developments with rezoning have been able to include 40% affordable units. Conversely, in a declining market where economic conditions are softening, a fixed requirement can move up the point in time where new residential development becomes infeasible. While these considerations might suggest inclusionary housing policies with targets that vary over time, based on economic conditions, many jurisdictions find it complex to create such programs and revise targets on an ongoing basis due to both administrative burden as well as the challenges of adopting a requirement in the first place.

B. RECOMMENDED POLICY

Based on the analysis presented above, Staff recommends that the Board develop a policy for affordable housing to be included in the Joint Development Policy. This should be done in order to address regional concerns related to the availability of affordable housing and expedite approval of VTA Joint Development Agreements for projects. The goal for a VTA-specific affordable housing policy would be to maximize the amount of affordable housing that would result while minimizing the financial impact to the Joint Development Program Fund.

1. Recommended VTA Affordable Housing Production Target for Joint Development

- a. Adopt an overall target for affordable housing production in joint development projects in VTA’s system.
- b. At least 50% of affordable housing units would be targeted at Extremely-Low and Very Low Income Households (households earning 50% of Area Median Income or less). For units in joint developments to be considered affordable, they must be targeted at households earning no higher than 80% of Area Median Income.

2. Business Strategies to Increase Affordable Housing in Joint Development

- a. On a per-project or per-station area basis, VTA would set a higher target for affordable housing production, to the extent that the local land use jurisdiction rezones the VTA joint development site to allow denser residential development (“upzones”) that would increase the value of VTA’s property. Up to one-half of the increased number of units from upzoning would be allocated to affordable housing production, up to a maximum of 33% affordable housing in either an individual joint development project or a station area.
- b. All VTA Joint Development competitive offerings for developer selection would contain competitive selection criteria that provides a scoring benefit to developers who include affordable housing developers in their development teams, and include a greater proportion of affordable housing units and/or deeper affordability in their development concept and development proposal submittals than the amount required by VTA policy.
- c. VTA would pursue partnerships with local jurisdictions to leverage their expertise and resources to increase affordable housing production at VTA joint development sites. This could facilitate access to low-income housing tax credits, local jurisdiction in-lieu fees, applications to the Affordable Housing and Sustainable Communities (AHSC) Program, and other resources. It could also include public education on the benefits of affordable housing production to generate local support.
- d. VTA would also provide endorsements and other support as appropriate for affordable housing developer applications or proposals for grant or other affordable housing funding. This would apply to projects on VTA joint development sites, as well as sites on property owned by others within station areas, where the project would increase transit ridership and where its land use type and density range reflects best practices for transit-oriented development.

3. Implementation Actions for VTA’s Affordable Housing Policy

- a. The General Manager would be authorized to prepare an individual joint development offering with 100% affordable residential units, as needed to enable VTA to achieve targeted levels of affordable housing production. For 100% affordable residential joint development projects, at least 50% of the units would be targeted at Extremely-Low and Very Low Income Households (households earning 50% of Area Median Income or lower), and all units would be targeted at households earning no higher than 60% of Area Median Income.⁶
- b. The General Manager would be granted authority to develop and implement new or flexible approaches for development of affordable housing pursuant to VTA’s affordable housing policy, in order to better advance its goals and respond to changes in market or other conditions.
- c. To the extent needed, the Board would conduct hearings for new resolutions of necessity to allow properties previously acquired by eminent domain for limited transit uses to be used for joint development affordable housing production.

⁶ VTA has previously done a 100% affordable housing development at the Ohlone-Chynoweth station.

- d. VTA would not provide write-downs in land value, or other direct financial assistance, for affordable housing units on joint development sites.
- e. If a local jurisdiction has an affordable housing production requirement that is equal to or exceeds those of VTA's policy, the local jurisdiction's requirement would apply.
- f. VTA would prepare an annual report identifying its affordable housing production to date as a percent of joint development residential units, and identify affordable housing units currently in pre-development or under construction.

ALTERNATIVES:

The Board may decide to approve a more limited policy than described in this memorandum, approve a different affordable housing policy, direct Staff to address affordable housing on a project-by-project basis, or request Staff to provide additional information or re-evaluate certain aspects of the policy.

FISCAL IMPACT:

Adoption of an affordable housing policy and implementation of affordable housing strategies, depending on the particular programs, market conditions, ability to secure approval for denser development, and various other considerations could result in anywhere from no effect to significant impact on the net proceeds that VTA receives from Joint Development projects.

ADVISORY COMMITTEE DISCUSSION/RECOMMENDATION:

The Technical Advisory Committee heard this item on March 10, 2016. The Committee unanimously passed a motion to approve the proposed policy as presented (no figure was identified for affordable housing in the motion).

The Policy Advisory Committee heard this item on March 10, 2016. The Committee approved a motion recommending the proposed policy to the Board of Directors, with a target of 30 percent affordable housing production for the overall joint development portfolio, and a target of 15 percent for each joint development project that includes residential. One member opposed the motion noting support of the proposed policy but with a higher minimum target for individual targets.

STANDING COMMITTEE DISCUSSION/RECOMMENDATION:

The Congestion Management Program and Planning Committee heard this item on March 17, 2016. Discussion included a request for more details about how rating criteria would be established to encourage developers to add affordable housing developers to their teams and provide higher levels of affordable housing; this should come back to the Board. Support was expressed for ensuring mixed-use joint development projects that include employment and housing.

A motion to approve the affordable housing policy as presented passed unanimously.

The Administration and Finance Committee heard this item on March 17, 2016. A motion was made and passed unanimously to recommend adoption of the draft affordable housing policy,

with a 30% overall target for affordable housing production in VTA's joint development program, with a target of 15% affordable housing production for each joint development project with residential uses, and that the ridership impacts of affordable housing and joint development are tracked. The motion also provides that the General Manager would notify the Administration and Finance Committee whenever the discretionary authority provided to the General Manager is exercised; that VTA will work to identify grants and other financial assistance that can be contributed to individual projects; a portfolio return calculation for the joint development program would be completed; the Joint Development Policy will be brought back to the Administration and Finance Committee for consideration of a strategy for investment in joint development sites and projects that is consistent with VTA's enabling statute; and that Staff follow up with the Administration and Finance Committee with a discussion on how to define and address surplus properties.

The Transit Planning and Operations Committee heard this item on March 17, 2016. A motion was made to adopt the policy, with a requirement of 30% affordable housing for VTA's joint development portfolio, and with evaluation of an in-lieu fee to allow developers the options of paying the fee rather than including affordable units in their project.

Prepared by: Ron Golem
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