



Housing and Community Development Division · 200 Georgia Street · Vallejo · CA · 94590 · 707-648-4507

Draft for Public Review -- June 23, 2014

_____, 2014

Ms. Maria Cremer, Director
Community Planning and Development
U.S. Department of Housing and Urban Development
600 Harrison St. 3rd Floor
San Francisco, CA 94107-1300

Dear Ms. Cremer:

The City of Vallejo is pleased to submit to the U.S. Department of Housing and Urban Development (HUD) an application for a Section 108 Loan Guarantee for the former Mare Island Naval Shipyard. The City is requesting \$4,700,000 in Loan Guarantee funds for demolition and clearance of up to 30 derelict buildings owned by the City of Vallejo in order to prepare the land for future development. At the present, these buildings are a detriment to Vallejo's citizens; once redeveloped this portions of Mare Island can create 1,000 jobs and benefit Vallejo as a whole.

This application was prepared in accordance with HUD regulations at 24 CFR 570.700 of the Community Development Block Grant program and the requirements of the Section 108 Loan Guarantee program. Thank you in advance for your assistance in reviewing and assessing this application for further consideration. If you have any questions regarding this application, please contact me at (707) 648-4408, or aputney@ci.vallejo.ca.us

Sincerely,

Anne Putney
City of Vallejo
Housing and Community Development Manager

**CITY OF VALLEJO APPLICATION FOR A SECTION 108 LOAN GUARANTEE
NORTH MARE ISLAND DERELICT BUILDING REMOVAL**

I. GENERAL INFORMATION

Applicant:	City of Vallejo
Status:	Entitlement Community
CDBG Number:	B-14-MC-06-0029
FY 14/15 Allocation:	\$943,998
Amount of Section 108 Requested:	\$4,700,000
Applicant Contact Information:	Anne Putney Housing and Community Development Manager (707) 648-4408 aputney@ci.vallejo.ca.us
	Guy L. Ricca Senior Community Development Analyst (707) 648-4395 gricca@ci.vallejo.ca.us

II. ELIGIBLE ACTIVITY/NATIONAL OBJECTIVE INFORMATION

The proposed activity is eligible as: 1) Acquisition of Real Property for Economic Development Purposes (24 CFR 570.703(a) which meets the National Objective of providing jobs to low and moderate income households under 570.208(4) for job creation under the standards outlined in 570.209 for guidelines for evaluating and selecting economic development projects, 2) Clearance, Demolition and Removal (24 CFR 570.703 (e)) and will also meet the National Objective of Elimination of Slums and Blight... (24 CFR 570.208(b)(2)), specifically the prevention or elimination of slum and blight on a spot basis. As such, this application will demonstrate the extent of and physical conditions that contribute to blight, and the benefits that would be created by removal of such blight.

The project meets the national objective of providing job creation benefit to low and moderate income people under HUD regulations at section "570.208(a)(4) An activity designed to create or retain permanent jobs where at least 50 percent of the jobs, computed on a full time equivalent basis, involve the employment of low- and moderate-income persons." Also, under 570.208(d)(1) "Where the assisted activity is acquisition of real property, a preliminary determination of whether the activity addresses a national objective may be based on the planned use of the property after acquisition. A final determination shall be based on the actual use of the property, excluding any short-term temporary use." It is the intent of the City for final determination purposes to create jobs for the low and moderate income community. Based on meetings with national developers there is demand at the site for distribution buildings. Current zoning allows 1.2 million square feet of light industrial buildings which is likely to create at least 120 distribution jobs of which 51% will be filled by or made available to persons from low and moderate income households.

III. DESCRIPTION OF CONDITION/PROJECT

North Mare Island is a 157 acre commercial and industrial development opportunity located along the San Francisco Bay, 30 minutes from downtown Oakland, 45 minutes from downtown San Francisco, and one hour from Sacramento, with direct ferry access to San Francisco, and freeway access via Highway 37 to I-80. The site is approved (EIR certified) for 1.2 million square feet of commercial/industrial development. Roughly 125 acres are currently owned by the City of Vallejo, with another 32 acres due to be transferred to the City by the Navy, by March 2017. There are over 30 derelict buildings on North Mare Island that impede its reuse. The project proposed is to demolish the worst condition buildings to ready the site for redevelopment

Since 1996 when Mare Island Naval Shipyard closed, the City has engaged in various entitlement activities with the goal of creating jobs for residents of the City and placing the currently vacant property on Mare Island to use for the benefit of the community. Various studies have been performed and Request for Proposals have been issued which have brought interest from bio tech, solar, manufacturing, and distribution users. Investigation of respondents has shown the demand for improved land is from financially responsible private parties. The demand for the property is based on its inner bay area location, good access to road networks in the North Bay and I-80 corridor, and proximity to the Port of Oakland.

The Navy has remediated underground environmental hazards. However, the City parcel requires substantial extraordinary costs to ready it for development. These extraordinary costs include: 1) Demolition of existing structures; 2) Redevelopment of surface and underground infrastructure; 3) Engineering of existing soils and/or providing structural support piers to foundations to support buildings under current building codes and market practice. Without the assistance of federal funds to pay a portion of the extraordinary costs, reuse of the property, and therefore low- and moderate-income job creation, will not occur.

If approved, funds from the Section 108 Loan Guarantee will be spent for acquisition of the City owned North Mare Island parcel by the Vallejo Economic Development Corporation and demolition of up to 30 buildings starting from the north and moving south. The project area suffers from adverse market perception due to the very poor condition of the above ground structures left by the Navy. By beginning demolition at the north end of the project and clearing only the above ground structures while leaving the footings and foundations in place, the greatest "curb appeal" impact can be realized. This is because the buildings at the north end are most visible from Highway 37 and the Mare Island exit both of which are next to and overlook the City parcel. This will have the effect of opening the site to a broad range of potential developers and tenants.

IV. FINANCE

City's Financial Position/Lack of Other Financing Options

The City has suffered more than almost any other city in the country from the recent economic recession. The U.S. Navy, the primary employer in the region until 1996, caused over 25,000 direct and indirect jobs to be lost in a very small geographical area upon its closure of the

shipyard on Mare Island. Later, as a result of the economic downturn and foreclosure crisis, unsustainable contract obligations, the City filed for bankruptcy in 2008.

Upon emerging from the bankruptcy three years later, the City's General Fund was slashed and vital City services, including public safety, were drastically reduced. The City continues to struggle with a variety of economic factors that preclude it from obtaining financing for this project from any other source. For example, as of March 2014, local unemployment was at 8.1%, significantly higher than the Solano County rate of 6.6%. Additionally, foreclosures, while down from previous years, are still having an impact on Vallejo's economy, and have reduced property values by 50% - 60%. This will negatively affect the City's budget for decades due to the State of California's Proposition 13, which requires property taxes to be reduced commensurate with current values, but increases are capped at 2% per year, thereby creating a long-term cap.

Finally, in December 2012, the California Supreme Court upheld legislation that ended a roughly 60-year old program intended to combat blight in California cities. As a result, more than 400 redevelopment agencies were dissolved, including the City of Vallejo Redevelopment Agency, thus eliminating another potential source of funding to address the issues on the North Island. While Standard & Poor's recently raised its underlying rating for Vallejo's 1999 Certificates of Participation (COPs) from C to CCC+ with a stable outlook, Vallejo's rating is still below investment grade and is considered to be at "junk bond" level, and among the lowest in California.

The vision of Mare Island was that it would be a vibrant, mixed-use community that would serve as the economic engine for the City and the region. The original 10-15 year build-out has been stalled by the environmental condition of the site, condition of the buildings, and complex entitlement and transfer issues as well of the impacts of the Great Recession on the regional economy. While investment on Mare Island is currently moving forward, the rate of investment would be accelerated if the dilapidated buildings on the North Island were demolished. The City does not possess a source of funds for this purpose, and the cost of surveying, remediation, and demolition is cost prohibitive when considered with all the other development costs. By not having a private entity on the North Island, the City is also foregoing critical tax revenue.

Repayment Information

The City is requesting the maximum loan term of twenty years. The City proposes principal repayment in 20 equal payments of \$235,000 with appropriate interest for the term of the loan.

Repayment of the HUD 108 loan will come from one of three sources. In order of priority they are:

- 1) Commitment of Measure B funds, a special tax described below.
- 2) Net sale proceeds from the sale of a nearby 2.55 acre infill development site to a developer.
- 3) Only in the event that sources one and two are not available, will future CDBG entitlement be used as needed to meet current debt service payments on the 108 loan.

The voter approved Measure B is a one percent sales tax to enhance City of Vallejo services, approved by voters on November 8, 2011 to help address unmet needs in the community and stimulate economic development. These funds were approved not to solve ongoing, structural budget problems but rather to invest in rebuilding the City's long-term stability. The measure will expire on March 31, 2022. In the 2014/15 budget year, it is projected that Measure B will generate \$12.4 million in revenue. Measure B budget projections include \$960,000 per year for North Mare Island building demolition, a sum which over the remaining term of Measure B will be sufficient to repay the loan.

While the CDBG Program allocation guarantees the loan, that allocation would be kept whole through the annual allocation of funds from Measure B to repay the loan. Because Measure B funds are sales tax based and therefore it cannot be projected with one hundred percent certainty that there will be sufficient funds to make loan payments, the City is requesting a loan term of 20 years so the impact to its CDBG program is minimized on the outside chance the CDBG funds are required to make the loan repayment.

Collateral

Along with the City's ability to repay the loan with future CDBG allocations, the City also pledges repayment from its Measure B funds. Additionally, the City will offer as collateral a 2.55 acre site located at the corner of Tennessee and Wilson Streets along the city's waterfront. This site is the former "Badge and Pass" building for the Mare Island Naval Shipyard. This is an infill development opportunity served by city infrastructure and zoned for mixed use development.

Custodial Account

The custodial account for this loan will be held at Wells Fargo Bank. There is an existing Fiscal Agent custodial agreement in place.

V. ENVIRONMENTAL

Mare Island Naval Shipyard was established in 1854 as the first United States naval installation on the West Coast. The shipyard was closed in 1996 and a Reuse Plan was adopted by the City. Since that time, the City has worked with Federal and State agencies to reuse and rehabilitate much of the Island's old and dilapidated infrastructure along with the City's private development partners. For more than a decade, the City has pursued potential funding mechanisms to help upgrade the infrastructure on Mare Island. Significant progress has been made. Environmental clean-up is approximately more than 50% complete, infrastructure is approximately 40% complete, commercial building rehabilitation is approximately 30% complete, and residential home development is approximately 20% complete (284 of the 1,400 homes have been built). Over 3,000,000 square feet of commercial property has been occupied, and over 2,100 permanent jobs have been created on the Island. This is part of an overall base conversion that is expected to create over 5,000 permanent jobs over the next 10 years.

Approximately $\frac{1}{4}$ of the developable area on Mare Island is located at the North Island (155 acres). Over 30 major buildings remain on the north end of the shipyard which are obsolete,

derelict, neglected, and a public nuisance. This loan would be used to demolish as many of these buildings as possible with the funds available. The U. S. Navy is obligated to investigate and remediate certain contaminants. Lead-based paint, asbestos-containing materials, mercury light ballasts, and other contaminants that are typically found inside buildings are not the responsibility of the Navy. However, in order to reuse the site, these issues must be addressed.

The site is subject to the land use regulations contained in the Mare Island Specific Plan, and the Environmental Impact Report (EIR) and the Environment Impact Statement (EIS) have been certified. The EIR/EIS addressed the expected demolition of buildings with hazardous materials (asbestos and lead) and found that due to State and federal regulations related to the handling and disposal of those hazardous materials, there were no significant impacts from the demolition and no additional mitigation (besides handling these materials in accordance with the law) was required. The EIR/EIS and Specific Plan also established parameters for the future development to address environmental impacts.

V. NEED/ANTICIPATED RESULTS

City Prior Efforts to Redevelop North Mare Island

Upon closure of the Mare Island Naval Shipyard, the City embarked on a process of finding developers who had experience with complex projects and significant financial resources to address the 150-year old infrastructure and existing historic building rehabilitation. The City addressed community needs such as education/civic, residential, community parks, design guidelines, infrastructure, land use, historic review, transportation guidelines, environmental review, and Mare Inland's unique access to water, open space, and recreation.

A golf course developer was selected in 1996 to rehabilitate the existing golf course. Lennar Mare Island LLC was selected in 1997 to develop approximately 650 acres. The North Island has seen five different development entities attempt to develop the site since 1996. In each case, the North Island development has been stopped by a combination of the environmental contamination (being cleaned up by the Navy), the cost of infrastructure, economy/market conditions, soils conditions, and the building abatement/demolition. The City continues to work closely with the Navy to address the environmental conditions for which the Navy is responsible and market conditions have stabilized. The City now believes that building abatement and demolition must move forward in order for the City to have a viable development opportunity.

Market Analysis for North Mare Island for Industrial Reuse

The City's contracted with National Development Council to review the site and conducted an industrial market feasibility study. The view of industrial developers is that Mare Island is attractive due to: 1) inner bay area location; 2) proximity to the Port of Oakland; and 3) good access to the road networks in the North Bay and I-80 corridor. Regional real estate brokers see strong demand for Mare Island product from industrial tenants in the 50,000-100,000 sq.ft. range because of the low vacancy in the surrounding markets and demand for industrial space coming out of the central Bay Area. Napa County's overall vacancy is 2.2% with neighboring American Canyon vacancy at .6%. This is very tight and wine driven. Solano County overall is at 9% vacancy, down from 15% in 2012. Fairfield's vacancy is 7.1%. Marin's overall vacancy is

10.6%, but there is no possibility of added supply in Marin. If available product does not work for a tenant, they must look elsewhere.

The view of the brokers is that the wine industry wants to be in Napa if at all possible and therefore wine tenants are second and third tier candidates for Mare Island space. However, tenants and owners/users from Marin and Fairfield are prime candidates for Mare Island due to the lack of alternatives. Expanding Marin companies that want to remain in the North Bay need to look at Petaluma or potentially Mare Island. Fairfield-based companies can easily be persuaded to relocate to Mare Island.

The product size most in demand is the 50,000-100,000 sq.ft. building. This size building fits companies currently occupying 30,000-70,000 sq.ft. seeking expansion space. This product can attract tenants from Petaluma (Mare Island is more central) and Napa (low-vacancy driven) as well as Fairfield and Marin. The brokers do not see a demand for 5,000-10,000 sq.ft. space on Mare Island because this type of space is usually taken by homegrown businesses and Vallejo has a small base of this type of company. They acknowledge the industrial uses currently on Mare Island but point out that these companies are generally highly price sensitive or have unique real estate requirements, neither of which fit within standard industrial building parameters. However, they also acknowledge that it makes sense to master plan the available land to allow for the construction of some buildings under 50,000 sq.ft. on a build to suit basis. Finally they note there is demand for larger buildings in the 200,000-350,000 sq.ft. range from growing tenants coming out of properties in the Hayward, San Leandro, Oakland, San Francisco, and Brisbane areas.

Lease pricing for standard industrial space (3%-5% office) in the 50,000 to 100,000 sq.ft. size is in the range of \$.38-.42 NNN per sq.ft./mo. Due to vacancy, rental rates are currently at the upper end of the range and are expected to rise to \$.45 by 2016. For a building in the 200,000-350,000 sq.ft. range, the rental rates are lower, in the range of \$.34-.35NNN per sq.ft./mo. These larger buildings are also subject to upward price pressure due to low vacancy. For comparison, cased goods, air conditioned, and insulated warehouse space in Napa currently leases in the \$.58-.62NNN per sq.ft./mo. range reflecting improvements above a standard cold shell industrial building. In conclusion, the very low vacancy in the surrounding markets combined with limits to industrial space growth and attractive freeway access point to a need for industrial space on Mare Island and a viable industrial development outcome. The site's extraordinary development costs impede realizing that development.

Job Creation

According to the Mare Island Specific Plan, North Mare Island will be developed primarily with light industrial, warehouse, and office uses in a contemporary office park. A small commercial retail area to serve primarily office park users will be located at the entrance. A proposed waterfront promenade will extend the length of the eastern edge of the area on the upland portion. It is envisioned that the area will require comprehensive redevelopment, including new buildings configured as a warehouse/distribution district or office park.

The creation of jobs on Mare Island, and throughout the City of Vallejo, continues to be a priority. In order for the City to implement the plan, create jobs for the community and create long-term tax revenue for vital City services, the risk to human health and the environment must be eliminated. With development of 1.2 million square feet of industrial park uses, at least 100 jobs will be created in businesses located in the North Island area after the clearance and demolition activities are completed. More than half of these are estimated to be in fields that would be filled by low- to moderate-income individuals.

V. CITIZEN PARTICIPATION

The City has taken a proactive position to community involvement and partnerships since the closure of the shipyard appeared to be imminent in 1992. Since that time, direct and indirect partnerships with numerous community groups have been established, including a homeless services facility, the Vallejo Unified School District, the Mare Island Historic Park foundation, the Greater Vallejo Recreation District, Touro University, Mare Island Heritage Trust, Mare Island residents, and Mare Island businesses. In 2012, after the latest North Mare Island development proposal failed, due in part to the cost of development, meetings were held in the community and before the Vallejo City Council to discuss the path forward.

As part of the City's Citizen Participation Plan as well as its commitment to transparent government, the City plans to host two public hearings for this application, and will also have a public comment period. The City held a public hearing in December 5, 2013 at the Housing and Redevelopment Commission to discuss the concept of this loan application. On March 18, 2014, the City Council had an informational study session focused exclusively on Mare Island and discussed plans for new development and using a Section 108 loan to undertake the necessary demolition. In addition, it will be posted on the City's website, on Open City Hall, and other forms of media the City uses to ensure dissemination of information to the public.