



# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Jacky Morales-Ferrand

**SUBJECT:** SEE BELOW

**DATE:** October 29, 2020

Approved

Date

**10/29/2020**

**SUBJECT: FY 2020/21 – FY 2020/23 AFFORDABLE HOUSING INVESTMENT PLAN**

## **RECOMMENDATION**

Accept the staff report on the FY 2020/21 – FY 2022/23 Affordable Housing Investment Plan updated to include Measure E Funds.

## **OUTCOME**

The City's Affordable Housing Investment Plan ("Investment Plan") summarizes the Housing Department's priorities for funding of affordable housing and outlines the funding available through FY 2022/23 to project performance in meeting the 10,000-unit goal. The Investment Plan is being updated to include Measure E funds as a new funding source for affordable housing development. Acceptance of this report will affirm the Housing Department's overall strategy and the use of available affordable housing funds. The Department's funding priorities are summarized in **Attachment A** and the Investment Plan is included as **Attachment B**.

## **BACKGROUND**

The Housing Department has brought forward an Investment Plan that has been updated over the span of several years. Prior versions of the plan can be viewed on the [Housing Department website](#). On April 9, 2019, the City Council approved an Affordable Housing Investment Plan Update outlining the funds needed to meet the Mayor and City Council's goal to produce 10,000 new units in a five-year period. The report stated that after aggregating all of the funds available, the City would need an additional \$541.5 million to fund the balance of 4,332 units in order to reach the 10,000-unit goal.

The Investment Plan outlined multiple strategies to introduce new funding sources for affordable housing. Since that time, two new funding sources have been created.

- ***Measure E Real Property Transfer Tax:*** On March 3, 2020, the voters approved a City measure (Measure E) for a new general fund real property transfer tax. This new tax is imposed at a tiered level for property transfers valued at \$2 million or more. City Council has adopted an allocation plan that directs funding to:
  - Permanent supportive and affordable rental housing for extremely low-income households
  - Affordable rental housing for low-income households
  - Below market-rate for-sale housing and rental housing for moderate-income households
  - Homelessness Prevention and Rental Solutions
  - Program Administration

Approval of the spending plan for Measure E Property Tax Revenue will provide \$30 million for the 2020-2021 fiscal year in total revenue. Of this amount, \$22.8 million will be made available for the development of new affordable housing in FY 2020/21. The Measure E Spending Plan will be considered by the City Council on November 10, 2020.

- ***Commercial Linkage Fee:*** The San José City Council voted on September 1, 2020 to begin charging commercial developers fees to fund affordable housing. Under the new fee program, office developers with projects involving more than 100,000 square feet will have two fee options:
  - \$12 per square foot if paid upon the certificate of occupancy
  - \$15 per square foot if paid in phases

For projects less than 100,000 square feet, the Council decided that the first 40,000 square feet will have a \$0 fee, with a cost thereafter of \$3 per square foot. Retail developers' fees will be \$0, regardless of their size, due to increased retail vacancies during the pandemic. Hotels and warehouses will pay \$5 per square foot.

The Investment Plan also set priorities and guidelines for funding of future developments that were incorporated into the scoring criteria for the Notice of Funding Availability. Priorities included project readiness, lower overall development cost, and leveraging of outside resources such as Affordable Housing and Sustainable Communities grant funds from the State. The Investment Plan also set a maximum subsidy of \$125,000 per unit for all new affordable developments.

On September 24, 2019, the City Council approved changes to the Investment Plan as a part of the annual update on the Housing Crisis Workplan. The changes included additional priorities for future funding of affordable housing. These priorities included a \$10 million set-aside for funding for acquisition and /or rehabilitation of existing apartments, a 45% minimum investment for Extremely Low-income units, and a place-based strategy for new affordable housing until the new Affordable Housing Siting Plan has been completed. It is anticipated that the Affordable Housing Siting Policy will be completed by the end of the fiscal year. Until the Council adopts a new policy, the Investment Plan directs that affordable housing will be located in these specific growth areas: North San José, Diridon Station Area, Downtown, West San Carlos Urban

Village, Berryessa Bay Area Rapid Transit (BART) Urban Village and the Blossom Hill/Snell Avenue Urban Village.

**ANALYSIS**

The Investment Plan quantifies the available funding for affordable housing, sets forth the priorities that will guide the investment of affordable housing, and identifies any gaps in meeting the 10,000-unit goal. It also includes the new funding sources available for investment in affordable housing. In previous iterations, the Investment Plan focused on quantifying the available funding for affordable housing and identifying an overarching goal as to how to invest its affordable housing resources. This update on the Investment Plan includes the following elements:

- City of San José Multi-Year Revenue Projection
- Additional Affordable Housing Being Developed in San José
- Future Development

**A. City of San José Multi-Year Revenue Projection**

The Housing Department manages the revenue that is collected by the City for the development of affordable housing. The Affordable Housing Investment Plan is summarized in **Attachment B**. The table below details the Housing Department’s expected fund balance by source at the end of the current fiscal year and over the coming three years. This provides a projection consistent with the time period set for the 10,000-unit goal. **Table 1** shows that the Housing Department has \$121 million in existing funds committed to new affordable housing developments and an additional \$222 million for development through FY 2022/23. Combined, the City of San José will have \$343 million to invest to in new multifamily affordable rental housing. This is an increase over the prior report on the Affordable Housing Investment Plan which identified nearly \$330 million for affordable housing in spring 2018. The increase of over \$10 million is primarily due to the recent passage of Measure E. A decrease in projected revenues is because of policy changes made to the Inclusionary Housing and to a redirection of HALA funds.

***Table 1 – Affordable Housing Revenue Projections Through FY 2022/23***

		FY 20/21	FY 21/22	FY 22/23
Source of Funding	Committed Developments	Estimated Revenue	Estimated Revenue	Estimated Revenue
Low and Moderate Income Housing Fund	113,590,960	20,000,000	20,000,000	3,000,000
Affordable Housing Impact Fees	4,000,000	20,000,000	5,000,000	1,000,000
Inclusionary Housing Policy In-Lieu Fees	4,000,000	10,000,000	14,000,000	10,000,000
Inclusionary Housing Ordinance In-Lieu Fees		3,000,000	5,000,000	30,000,000
Housing Authority Litigation Award		6,020,000	0	0
HOME		0	3,700,000	3,700,000

SB2 State Housing Trust Fund			0	0
Measure E		22,800,000	22,800,000	22,800,000
Commercial Linkage Fee		0	0	0
<b>TOTALS</b>	<b>121,590,960</b>	<b>81,820,000</b>	<b>70,500,000</b>	<b>70,500,000</b>
			<b>Total</b>	<b>222,820,000</b>

The projected revenue is received from various one-time and on-going revenue sources. These sources are discussed below:

- Low and Moderate-Income Housing Affordable Fund (LMIHAF):** The Housing Department has worked with a consultant to develop a projection for annual revenue coming from the existing loan portfolio. This model estimates that the City can anticipate \$3 million annually in LMIHAF repayments that can be dedicated to new affordable housing developments over the three years. Affordable housing developers typically will seek to reinvest in their existing projects after expiration of their tax credit compliance period because the project is eligible to receive new tax credit financing. It is anticipated that some developments will decide to repay their City loans each year when their tax credit compliance period ends. This accounts for the large increase in revenue projected for this Fund in FY 2020/21 and 2021/22.
- Affordable Housing Impact and Inclusionary In-Lieu Fees:** The Housing Department expects to receive revenue based on the development of market-rate housing. The revenue projections are based on Affordable Housing Agreements that have been executed for payment of fees after construction completion. Affordable Housing Agreements are executed by market-rate developers during the entitlement process. The Affordable Housing Impact Fee (AHIF) is being replaced by the rental provisions of Inclusionary Housing Ordinance (IHO). Therefore, no new fees are expected from the AHIF FY 2022/23. The prior plan included a development that was anticipated in paying \$21 million in Inclusionary Housing Ordinance fees, however, this development now qualifies for the Downtown High-Rise exemption. The revenue for the Inclusionary Housing Ordinance fees is adjusted to reflect this change.
- Housing Authority Litigation Award:** The Investment Plan incorporates \$6 million in one-time funding from the Housing Authority Litigation Award (HALA) funds. These funds are flexible in nature and may be spent on the development of affordable housing for a variety of target populations. The prior plan included \$22 million in this category. This category has been adjusted to \$6 million reflecting a shift in priority to funding homeless solutions.
- HOME:** The majority of the annual federal HOME allocation is currently used to fund rapid rehousing subsidies for homeless residents. Funds from the current FY 2020/21 year have been used to fund rent relief in response to the COVID-19 pandemic. The estimated amount of annual funding from the HOME program for new development is \$3.7 million a year.

- ***SB2 State Housing Trust Fund: SB2 State Housing Trust Fund:*** SB2 established a State Housing Trust Fund. This fund is generating approximately \$3 million per year. The priority for these funds in the coming five years is to provide operating subsidies for Bridge Housing Communities and Interim Emergency Housing sites. Funding for production of new affordable housing may be available in future years.
- ***Measure E Real Property Transfer Tax:*** On March 3, 2020, the voters approved Measure E, a new general fund real property transfer tax. The FY 2020/21 Measure E Spending Plan is also being considered by the City Council on November 10, 2020. The outcome of the spending plan will build the basis for the revenue available for new development. Based on the proposed Measure E Spending Plan, this new source of revenue will provide an additional \$22.8 million in annual revenue for the development of affordable housing.
- ***Commercial Linkage Fee:*** On September 1, 2020, the City Council voted to establish a commercial linkage fee. This fee will be charged on a square foot basis to new commercial development. Revenue will be collected at the time of occupancy or lease up. Collection of the fee will take place late in the development process, so it is difficult to predict when revenue will begin coming into the City. Revenue is expected to begin in three to four years. The updated Investment Plan does not include any revenue from this source through FY 2022/23.

## **B. Affordable Housing Development in San José**

Affordable housing is being developed throughout the City with and without City funds. It is estimated that 2,547 new affordable apartments will be added to the 1,263 units funded through the most recent Notice of Funding Availability. Additionally, there are 514 units that have been completed or are under construction. This will create a total of 4,324 new affordable rentals that will be funded, under construction, or completed, by the end of FY 2022/23 assisted by the City of San José.

It is estimated that Measure A and the No Place Like Home Program will have a capacity to fund nearly 400 affordable units within San José that will not receive any financing from the City. Additionally, the Valley Transit Authority (VTA) and Santa Clara County Housing Authority plan to develop affordable housing that may not require funding from the City.

In November 2019, the City Council provided direction to staff to develop changes to the Inclusionary Housing Ordinance encouraging the development of affordable housing onsite. Market-rate developers have responded positively to this change and have begun submitting affordable housing compliance plans demonstrating a commitment to building onsite affordable housing. Over the span of the Investment Plan, staff is anticipating nearly 200 new affordable housing units as a result of the Inclusionary Housing Ordinance.

Other sources of new affordable housing include educational institutions planning on developing affordable housing for their faculty and staff. These would generate affordable housing for

school employees. City Council also recently approved a funding commitment for Habitat for Humanity to acquire a site to develop for-sale housing for moderate income households. Creative solutions for moderate income housing are beginning to emerge and may increase production in this category through FY 2022/23. In addition, several developments are working through the entitlement process that will provide housing for low-income households but are not seeking funding from the City or County. These developments are considered to be private developments and account for 1,100 of the affordable housing currently in the affordable housing pipeline. Finally, the development of Accessory Dwelling Units (ADUs) is on the rise. Staff estimates that half of all ADUs are affordable to low-income households, accounting for over 1,000 new affordable housing units.

*Table 2 – Number of Affordable Housing Apartments that can be Created by FY 2022/23*

<b>OPPORTUNITIES</b>	<b>ESTIMATED NEW UNITS</b>
City of San José - Completed or Under Construction	514
City of San José - Prior NOFA	1,263
City of San José - Future Funding	1,783
Measure A and No Place Like Home	396
VTA sites	284
Housing Authority Sites	584
Inclusionary On-site	191
Teacher Housing	172
Moderate Income	14
Private Development	1,143
Accessory Dwelling Units	1,090
<b>Total:</b>	<b>7,434</b>

In total, these various programs, policies and strategies are projected to result in 7,434 new affordable units funded through FY 2022/23.

**C. Future Development**

The City is currently working with developers to reach affordable housing agreements on large-developments that are projected to include hundreds of new affordable housing units. Projections of the affordable housing units that are planned to be a part of these developments are not included in the above projections for new affordable housing because agreements have not been finalized. However, developments located near large transit stations including the Downtown West and Berryessa station development proposals are likely to include hundreds of additional affordable housing units. The City’s high priority of including affordable housing in these transit-orientated, large developments will further the City’s efforts to meet its aggressive affordable housing goals.

## **CONCLUSION**

The City's goal to have 10,000 new affordable housing units entitled, under construction or completed by 2023 is an aggressive goal challenging the City and its residents to explore every option possible to meet the overwhelming need for affordable housing in our community. As a result of this goal, prior iterations of the Investment Plan described the resources necessary to meet this goal. Over the last year, the residents of San José stepped forward with the passage of Measure E and the City Council voted to establish the Commercial Linkage Fee raising additional funds for affordable housing. Additionally, policy direction to make changes to the Inclusionary Housing Ordinance have encouraged developers to build affordable housing onsite. Homeowners are responding to the opportunity to build ADUs in their back yards, increasing the availability of homes for low-income households. These efforts, combined with proposed development near large transit stations, are bringing the 10,000-unit goal within reach.

## **EVALUATION AND FOLLOW-UP**

Once the City Council approves the update to the Investment Plan and the Underwriting Guidelines, also being considered by the City Council on November 10, 2020, the Housing Department will issue a Notice of Funding Availability. The Notice of Funding Availability is expected to be an over-the-counter process that will begin accepting application prior to the end of 2020. The Housing Department will bring forward funding commitments and appropriation approvals to the City Council for developments that meet the NOFA requirements. The periodic production report, posted on the City's website, will provide an update on the progress towards meeting the 10,000-unit affordable housing goal.

## **CLIMATE SMART SAN JOSE**

The recommendation in this memo has no effect on Climate Smart San José energy, water, or mobility goals.

## **PUBLIC OUTREACH**

The Affordable Housing Investment Plan will be posted on the City's website for the November 10, 2020 City Council meeting.

### **COST IMPLICATIONS**

There are no cost implications associated with the acceptance of the update to the Affordable Housing Investment Plan. Funding requests for specific developments will be brought forth individually to City Council for approval.

### **COORDINATION**

This memorandum was coordinated with the Attorney's Office and the City Manager's Budget Office.

### **COMMISSION RECOMMENDATION/INPUT**

This item was not heard by the Housing and Community Development Commission. The Measure E Spending Plan was reviewed by the Housing and Community Development Commission, serving as the Oversight Committee for this new funding source. Recommendations from the Commission will be considered when determining the Measure E Spending Plan, and will directly impact the funds available for the development of affordable housing in the Investment Plan.

### **CEQA**

Not a Project, File No. PP17-009, Staff Reports, Assessments, Annual Reports, and Informational Memos that involve no approvals of any City action.

/s/  
JACKY MORALES-FERRAND  
Director of Housing

For questions, please contact Rachel VanderVeen, Deputy Director, at (408) 535-8231.

### **ATTACHMENTS:**

**Attachment A:** Housing Department's Funding Priorities

**Attachment B:** Affordable Housing Investment Plan - Housing Revenue Projections Through FY 2022/23



**CITY OF SAN JOSE  
HOUSING DEPARTMENT'S FUNDING PRIORITIES**

**#1: Align funding with Measure A funded developments**

The City will seek funding opportunities to contribute to County Measure A funded developments for the purpose of providing apartments which would serve the extremely, very low-, and low-income households. This will enable Measure A developments to house residents with a range of incomes and populations.

**#2: Increase housing for homeless residents**

The City will make significant progress in investing in permanent supportive housing to address the needs of our homeless residents by working with both the County and the Housing Authority.

**#3: Limit funding to \$125,000 per unit**

Funding is limited to \$125,000 per unit to maximize the impact of the limited funds available.

**#4: Fund developments that can utilize cost saving construction techniques**

The City will prioritize developments that use cost saving construction techniques, such as modular housing to provide affordable apartments at a cost that is less than the \$125,000 per unit subsidy.

**#5: Prioritize developments leveraging the Affordable Housing and Sustainable Communities Grant Program**

The City will prioritize developments that leverage public funding by applying for grants from the State's Affordable Housing and Sustainable Communities (AHSC) Program. AHSC grants can fund both affordable housing and infrastructure for the City.

**#6: Fund acquisition/rehabilitation of existing apartments**

The City will set aside \$10 million for acquisition/rehabilitation of market-rate housing. An affordability restriction will be placed on the property, creating new affordable housing.

**#7: Provide minimum funding for Extremely Low-Income (ELI) housing**

The City Council set a minimum of 45% of total funds be used to fund extremely low-income (ELI) homes.

**#8: Placed-Based Strategy**

While work proceeds on the Affordable Housing Siting Policy, upcoming funding for affordable housing will be directed to growth areas throughout the City including North San Jose, Diridon Station Area, Downtown, West San Carlos Urban Village, Berryessa Bay Area Rapid Transit (BART) Urban Village and the Blossom Hill/Snell Avenue Urban Village.

**ATTACHMENT B**

**AFFORDABLE HOUSING INVESTMENT PLAN**

**Housing Revenue Projections Through FY 2022/23**

<b>Sources of Funding</b>	<b>Committed Developments</b>	<b>Estimated Revenue FY 20/21</b>	<b>Estimated Revenue FY 21/22</b>	<b>Estimated Revenue FY 22/23</b>
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<b>Totals:</b>	<b>\$121,590,960</b>	<b>\$81,820,000</b>	<b>\$70,500,000</b>	<b>\$70,500,000</b>

**Grand Total: \$222,820,000**

**Number of Affordable Housing Apartments that can be Created by FY 2022/23**

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