



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kim Walesh

SUBJECT: SEE BELOW

DATE: September 11, 2017

Approved

D. D. S. y L

Date

9/22/17

COUNCIL DISTRICT: 3

SUBJECT: APPROVAL OF DOWNTOWN HIGH-RISE RESIDENTIAL INCENTIVE FOR NORTH SAN PEDRO TOWER III AT 323 TERRAINE STREET

RECOMMENDATION

Conduct a Public Hearing regarding an economic development subsidy in connection with a reduction in construction taxes and parkland fees for a Downtown residential high-rise at 323 Terraine Street in the amount of \$4,084,091, pursuant to California Government Code Section 53083 and Open Government Resolution Section 2.3.2.6 C.

OUTCOME

Approval of an economic development subsidy in the amount of \$4,084,091 in conjunction with the Downtown High-Rise Residential Incentive Program, approved by City Council in December 2016 for the project at 323 Terraine Street in Downtown San Jose.

BACKGROUND

The number of residents in the Downtown has long been viewed as critical to support increased transit investment, diversification of retail, and the generation of more jobs in the City's core. With this objective, the City Council approved incentives for high-rise residential development in 2007 (parks-specific) and again in 2012 (parks and construction taxes). These programs resulted in the construction of 1,522 units.

The initial incentive expired in 2016 for new projects in the entitlement process or recently approved at a time when financial and market conditions were tightening for new high-rise development.

In this context, the City Council approved the extension of the [Downtown High-Rise Residential Incentive Program](#) on December 13, 2016 with the intent that the completion of additional high-rise projects will add housing units, spur more retail amenities, attract more employers, increase transit use, and improve public life through increased enjoyment of currently under-utilized public spaces. The memo for the December 13, 2016 Council action provided the data and analysis documenting the need for the Incentive Program.

The current Downtown High-Rise Residential Incentive Program suspends 50% of construction taxes on high-rise developments in the Downtown Area (Appendix A) and allows for payment of the taxes to be delayed until the issuance of the Certificate of Occupancy. The Incentive Program also sets the park impact in-lieu fees charged for residential downtown high-rise developments at 50% of the applicable park impact in-lieu fees for multi-family 5+ units in the Downtown Area and allows for payment of park impact in-lieu fees to be delayed until issuance of the Certificate of Occupancy.

On August 24, 2014 the San Jose City Council adopted Resolution 77135 which required that a public hearing be conducted for any public subsidy over \$1,000,000 and that notice of such public hearing be in the form of a memorandum addressed to the City Council posted on the City's web site 28 calendar days in advance of the City Council meeting at which a public subsidy is to be considered. The Resolution required that the staff memorandum contain the information found in first table in the Fiscal/Policy Alignment section of this memorandum. California Code Section 53083 (Assembly Bill 562) was also enacted in 2014 and requires local agencies to provide specified information to the public before approving an economic development subsidy over \$100,000. The state-required information is found in the second table in the Fiscal/Policy Alignment section of this memorandum.

ANALYSIS

North San Pedro Tower III is an 18-story mixed-used project, consisting of up to 313 residential dwelling units and up to 1,400 square feet of commercial space, with associated parking garage. The project site was originally acquired through the San Jose Redevelopment Agency, and is located just a few blocks away from San Pedro Square. While originally entitled as an apartment building, current ownership plans to sell the units as condominiums.

To be eligible for the Downtown High-Rise Residential Incentive Program a project must:

- Be in the Downtown Area as defined in the 2000 Downtown Strategy and 2040 General Plan.
- Be at least 12 stories in height.
- Secure a foundation permit by July 2018.
- Complete final inspection of 80% of the units by December 2020.
- Pay deferred fees and taxes prior to the final inspection of 80% of the units.
- Retain contractors licensed by the State of California for the construction of the project.

September 11, 2017

Subject: Downtown High Rise Residential Incentive for 323 Terraine Street

Page 3

- Employ only construction workers who possess necessary licenses and certifications required by the State of California.

Additionally, project developers should make a good faith effort to 1) comply with the State of California's apprenticeship program requirement, and 2) ensure that 25% of those apprentices are identified as having an employment barrier. The Downtown High-Rise Residential Incentive Program includes the park impact in-lieu fees and the City's two Construction Taxes applied to residential development.

Park Impact In-lieu Fees

The City's park impact in-lieu fees are imposed on each new housing unit and are based on the premise that each new unit should offset the impact of new residents on public park facilities. The Schedule of Fees and Credits for park impact in-lieu fees is codified in the Parkland Dedication Ordinance (PDO) (Chapter 19.38 of the Municipal Code) and the Park Impact Fee Ordinance (PIO) (Chapter 14.25 of the Municipal Code). In 1998 City Council enacted amendments to set the fees based on unit occupancy and observed land values throughout the City. Pursuant to the State Quimby Act and Mitigation Fee Act, which empower the City to enforce the PDO/PIO, new residential development projects are obligated to provide three acres of parkland for every 1,000 new residents added by the housing development. Projects can comply with this obligation by dedicating land for public parks, paying an in-lieu park impact fee, constructing new park facilities, providing improvements to existing recreational facilities, or a negotiated combination of these options. Since most projects in the Downtown area are not able to provide parkland, this requirement is often converted to the in-lieu fees based on an annual assessment of the observed value of land. These fees provide the City with the resources to provide new parkland and/or rehabilitate or redevelop existing park amenities for new developments and their surrounding neighborhoods. On September 20, 2016 City Council adopted Resolution 77926 to set the current Downtown fee at \$21,400 per unit.

Construction Taxes

The City's construction taxes include the Building and Structure Construction Tax (B&S) and the Commercial-Residential-Mobile Home-Park Building Tax (CRMP), both of which are based on the valuation of construction derived from the most current building valuation data table published by the International Code Council (ICC) or the developer's stated construction valuation, whichever is higher. The B&S tax rate on residential building construction valuation is 1.54%, and the CRMP tax rate on residential building construction valuation is 2.42%, for a combined tax of 3.96%. Proceeds are used to fund city-wide capital improvement projects such as repairs and redevelopment of existing recreational facilities and transportation-related projects and improvements, such as pavement maintenance, complete streets, pedestrian safety, and traffic calming projects.

Proposed Economic Subsidy

The proposed economic subsidy for this project is \$734,991 from the suspension of 50% of construction taxes and \$3,349,100 from the suspension of 50% of applicable Parkland Fees.

EVALUATION AND FOLLOW-UP

City staff has executed a Project Completion Agreement with North San Pedro SJ, LLC, as required under Resolution 78079, and will monitor project construction to ensure the requirements of the Downtown High-Rise Residential Incentive Program are completed prior to the sunset date of December 31, 2020. The project must still comply with its parkland dedication obligations per its entitlement conditions.

PUBLIC OUTREACH

The memorandum will be posted on the City's website for the October 3, 2017 City Council agenda.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office, the Department of Transportation, the Department of Housing and the Department of Parks, Recreation, and Neighborhood Services.

COMMISSION RECOMMENDATION/INPUT

No commission recommendation is associated with this action.

FISCAL/POLICY ALIGNMENT

The project aligns with the City's Economic Development Strategy to position Downtown as Silicon Valley's City Center to attract a diverse range of residents.

Benefits

- Estimated one-time revenue to the City: \$4,366,736
 - Construction Taxes: \$786,636
 - Parkland In-Lieu Fees: \$3,349,100
 - Business Cooperation Program: \$231,000

- Estimated recurring annual revenue to the City: \$255,524
 - Property Tax: \$168,000
 - Utility Tax: \$77,569
 - Business Tax: \$6,455
 - Sales and Transaction Tax: \$3,500

This project is within a Redevelopment Agency Project Area, therefore the majority of the tax increment revenue will go to the Successor Agency to the Redevelopment Agency to pay down Successor Agency debt until all its enforceable obligations are paid. It is expected that all enforceable obligations and bond debt payments will be completed in 2035. However, because the Successor Agency is receiving a substantial amount of tax increment in the Project Areas and the pending refunding of bond debt, the City will likely receive an increasing portion of property tax increment revenue from the project during the 2020s. After 2035 all the taxing entities will receive the normal distribution of property taxes. The City of San Jose receives 14% of one percent of assessed property value as property tax. The County of Santa Clara receives 18% of the property tax distribution. The corresponding school district (San Jose Unified School District) receives 44% of the property tax distribution. In addition, the corresponding school district will collect a fee of .56/square foot of living space (including commercial space) on this development.

Although not part of the incentive program that is the subject of this memo, the rental project described in this memo may benefit from the Affordable Housing Impact Fee's Downtown High-Rise Exemption if the project receives its final certificates of occupancy on or before June 30, 2021.

The table below addresses the requirements set forth in the City of San Jose's Resolution 77135 for publication of information related to an economic development subsidy of more than \$1,000,000.

<p>i. Accountability</p>	<p>The Downtown High Rise Incentive program suspends 50% of construction taxes for eligible developments and allows for payment of the taxes to be delayed until the issuance of the Certificate of Occupancy. The program also set the park impact fees at 50% of the applicable park impact fees and allows for payment of park impact fees prior to scheduling the first occupancy inspection for 80% of the residential units.</p>
<p>ii. Net fiscal impact</p>	<p>The project is estimated to generate one-time revenue of \$4,366,736 (Construction Taxes: \$786,636, Parkland In-Lieu Fees: \$3,349,100, Business Cooperation Program: \$231,000) and recurring annual revenue of \$255,524 (Property Tax: \$168,000, Utility Tax: \$77,569, Business Tax: \$6,455, Sales and Transaction Tax: \$3,500) to the City of San Jose. The construction tax revenue gained on this project is \$786,636 and the construction tax revenue forgone is \$734,991. The park impact fee gained on this project is \$3,349,100 and park impact fee forgone is \$3,349,100.</p>

<p>iii. Net job impact</p>	<p>This project is estimated to create approximately 1,000 full-time construction jobs. 80% of these jobs will generate an annual salary above \$80,000. Post construction, the project is estimated to create five on-site FTE positions in management, service and retail.</p>
<p>iv. Housing impact</p>	<p>This project will deliver 313 new market rate (above 120% of Area Median Income) housing units (689 estimated residents) to Downtown. No new demand for Extremely Low Income housing units is expected to be generated by employees of this project.</p>
<p>v. Source of funds</p>	<p>The incentive does not provide funds directly to the project but is a suspension of 50% of construction taxes and a 50% reduction in park impact fees. The project is estimated to generate one-time revenue of \$4,366,736 and recurring annual revenue of \$255,524.</p>
<p>vi. Neighborhood impacts</p>	<p>No significant impacts are anticipated on traffic or public infrastructure.</p>

The table below addresses the requirements set forth in the State of California AB 562 (Government Code 53083) for publication of information related to an economic development subsidy and a public hearing.

<p>i. Name/address of benefiting business entity</p>	<p>North San Pedro SJ, LLC 950 Tower Lane, Suite 870 Foster City, CA 94404</p>
<p>ii. Start and end dates for the subsidy</p>	<p>Projects will become eligible for the subsidy per the current Downtown High-Rise Residential Incentive Program. The subsidy will become finalized upon payment of fees prior to the sunset date of the Downtown High-Rise Residential Incentive Program, subject to conditions therein.</p>
<p>iii. Description of the subsidy, estimated total amount of expenditure of public funds or revenue lost</p>	<p>The City shall suspend 50% of construction taxes on the high-rise constructed at 323 Terraine Street and shall allow payment of the taxes to be delayed until the issuance of the Certificate of Occupancy. The City shall also set the park impact fees charged for 323 Terraine Street at 50% of the applicable park impact fees for multi-family 5+ units and provide for payment of park impact fees at time of issuance of the Certificate of Occupancy. The estimated economic development subsidy is \$4,084,091</p>

September 11, 2017

Subject: Downtown High Rise Residential Incentive for 323 Terraine Street

Page 7

iv. Statement of public purpose	To encourage the development of high-rise residential in the Downtown Area, spurring increased retail amenities, attracting more employers, increasing transit use, and improving public life in San Jose. The aggregation of these factors will increase the economic vitality of the City's urban core and will translate to increased property tax and sales tax revenue to the City of San Jose.
v. Projected tax revenue	Estimated recurring tax revenue to the City of San Jose is \$255,524, of which \$168,000 is derived from property tax.
vi. Estimated number of jobs created, broken down by full time, part-time and temporary positions	This project is estimated to create approximately 1,000 full-time construction jobs. 80% of these jobs will generate an annual salary above \$80,000. Post construction, the project is estimated to create five on-site FTE positions in management, service and retail.

CEQA

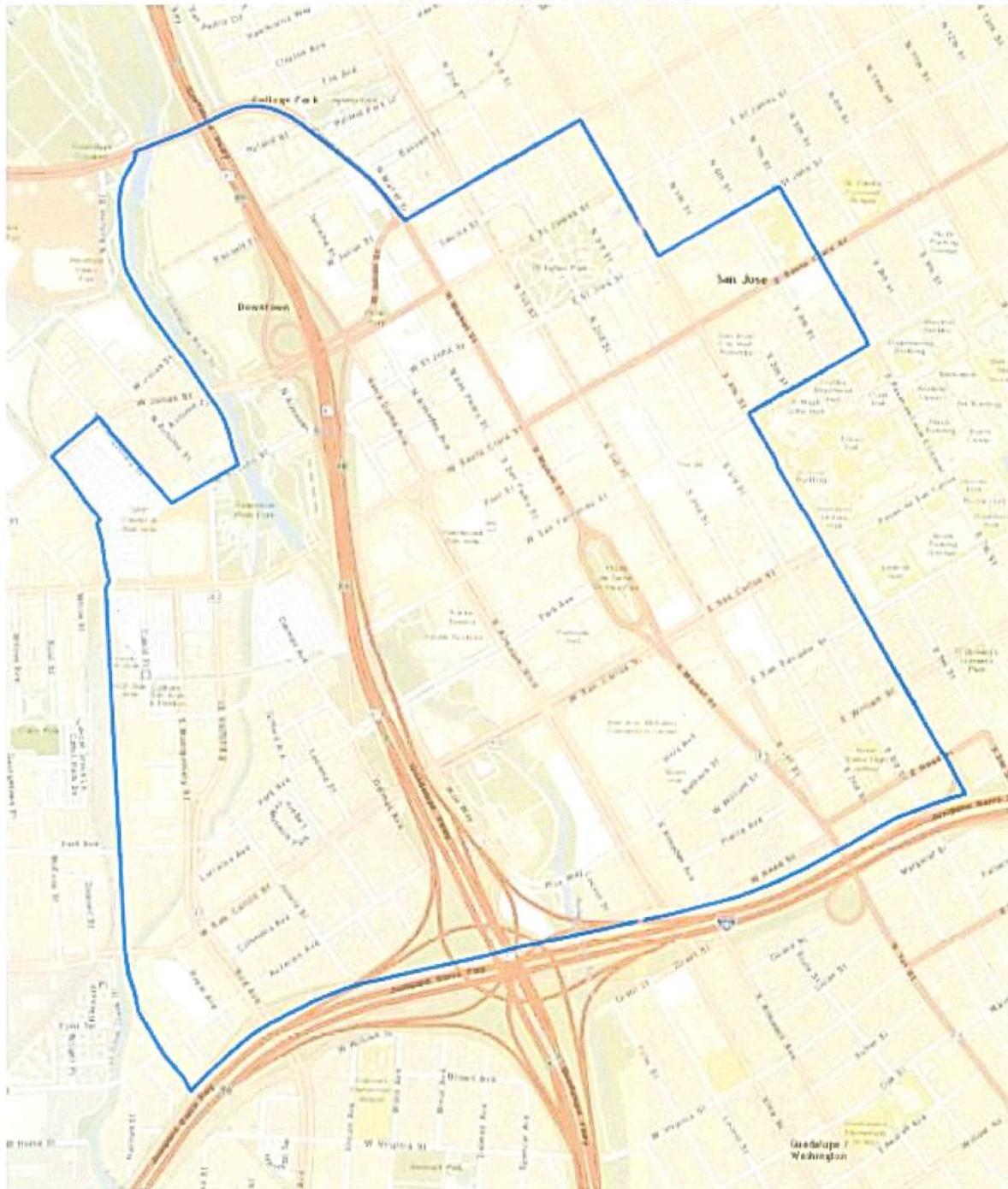
Addendum to the Brandenburg Mixed-Use Project/North San Pedro Housing Sites EIR, and the San Jose Downtown Strategy 2000 Final Environmental Impact Report, Planning File No. H14-037.

/s/
KIM WALESH
Deputy City Manager
Director of Economic Development

For questions please contact Blage Zelalich, Downtown Manager at (408) 535-8172.

Appendix A: Downtown Boundary Map and Location of Project

Envision 2040 San Jose General Plan
Downtown Growth Area



Map Prepared by the City of San Jose Planning Division, November 2016



Appendix B: Project Rendering



Figure 1 - View on Terraine Street



Figure 2 - View from W. Julian and Terraine streets