CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Councilmember Jimenez

SUBJECT: **Report on the Cost of Residential Development**

DATE: November 1, 2019

Approved

Date 11/1/2019

RECOMMENDATION

1. Direct staff to analyze the impact of development standards and zoning restrictions on the cost of residential development in San Jose. Staff should study the following:
    a. Parking requirements, including savings on development costs from reduced or eliminated parking requirements.
    b. Height maximums, including profit potential with each additional story added to prototype developments (across all construction types).
    c. Density limitations, including profit potential and impact on feasibility with density bonuses or elimination of density restrictions altogether.
    d. Commercial/retail requirements, including impact on financial feasibility with reduction or elimination of such requirements.
    e. Any other development standard or zoning restriction within the control of the City that has a material impact on the cost of residential development.
2. Direct staff to analyze the impact of development review, including the length of time taken to entitle and construct residential projects, on the cost of development. Include within this analysis:
    a. Cost comparisons between discretionary projects and by-right developments.
    b. Cost savings by reducing discretionary review. (For example, allowing approval at a Planning Director Hearing instead of Council approval.)
3. Direct staff to provide an analysis of land values, measured in dollars per acre, in other cities in Santa Clara County, and compare with land values in sub-areas within San Jose.

ANALYSIS

The analysis of the cost of residential development has provided the Council insight into the impact of fees and taxes on financial feasibility. However, so far, the analysis has not bought similar transparency into the cost implications of restrictive development standards and zoning regulations, nor has it studied the effects of lengthy development review processes. The Council has the discretion to modify these regulations and, to some extent, development review processes. Studying the development cost implications of reducing regulations and discretionary review may reveal additional opportunities to improve feasibility.

For example, the Keyser Marston Associates Conceptual Pro Forma Analysis of High-Density Apartment Development indicates that "at a ratio of one space per unit, the cost of parking currently accounts for approximately 13% of direct costs and 9% of total development costs for the seven-story apartment prototype" (p. 12). The Analysis assumes a cost of $50,000/space for above grade parking, and $80,000/space for below grade (Table A-8). These are significant costs that have a material impact on financial feasibility. As has been discussed previously, addressing financial feasibility concerns may not be as simple as eliminating parking; a zero-parking project may have difficulty securing financing in some cases, and an apartment unit in a building with zero parking may not command the same rent as a unit with an assigned space (or at least access to unbundled parking). Nevertheless, parking represents a significant cost that should be fully explored in any comprehensive analysis of residential development costs.

Similarly, restrictions on height, density, and building form generally can have major implications for financial feasibility. Following lengthy discussions about "one engine inoperative" (OEI) height constraints, the Council took action that unlocked tremendous development capacity in Downtown and the Diridon Station Area. Each additional story enhances the value and feasibility of Type 1 construction residential development. Likewise, reducing density limitations allows developers to include more revenue-generating units in the same building envelope. We must better understand how these restrictions affect the cost of development and reduce feasibility, and we should include exploration of how reducing these regulations may facilitate housing development. Staff should identify other development standards and zoning restrictions to include in the analysis.

The KMA Conceptual Pro Forma Analysis also indicates that "a local construction bid index projects Bay Area construction costs to grow by 5% to 6% over the next year" (p. 6). We have heard clearly from the development community that even a one-month delay can have a significant impact on the cost of development. While there are limitations to our ability to control the timeframe for environmental review, we do have some ability to reduce discretionary review and allow development by right. Community input is crucial, and changes to process should not be taken lightly. However, a serious analysis of the cost of residential development must include a review of discretionary process, as appropriate and meaningful changes will not only reduce the cost of development, but also allow us to achieve our housing goals more quickly.

Finally, the report compares rents across jurisdictions, but not land values. To allow for a meaningful apples-to-apples comparison of development costs, subsequent reports and analyses should provide the Council with information about land values in the jurisdictions we are comparing ourselves against.

The City controls much more than taxes and fees. While these are important to consider in analyzing development feasibility, we must also be open to exploring other changes to enhance feasibility and get the housing we desperately need built.