



Memorandum

TO: COMMUNITY AND ECONOMIC
DEVELOPMENT COMMITTEE

FROM: Lee Wilcox
Kim Walesh
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SUBJECT: SEE BELOW

DATE: November 4, 2019

Approved

Date

11/8/19

SUBJECT: CITY COUNCIL POLICY PRIORITY #9: COMMERCIAL LINKAGE FEE FOR AFFORDABLE HOUSING

RECOMMENDATION

Accept an update on the process of preparing a nexus and feasibility study on the Commercial Linkage Fee.

BACKGROUND

On March 12, 2019, the City Council directed staff to conduct nexus and feasibility studies for a Commercial Linkage Fee. A Commercial Linkage Fee is a fee assessed on new commercial development for the purpose of offsetting the need for affordable housing generated by that development. Staff's recommended scope for the study proposed analyzing up to eight development prototypes across a variety of geographic areas within San José. The Council approved staff's recommendation along with additional direction contained in a memo from Mayor Liccardo dated March 12, 2019, as follows:

- Consider including high tech office, single user office, retail, industrial, hotel, and office as commercial building types.
- Conduct sensitivity analysis of the impact of potential shifts in development costs and income on the feasibility of fees for different types of non-residential development.
- Ensure that the City's outreach plan includes developers, employers and other stakeholders.
- Bring back the final study results and policy proposals to Council no later than January 2020, or as soon as possible, for consideration.

In June 2019, staff issued a Request for Proposal (RFP) for a consultant to conduct the Commercial Linkage Fee study. The RFP received qualifying proposals from three consultants: David Paul Rosen & Associates, Strategic Economics, and Keyser Marston Associates. A review team made up of City staff rated the consultants' proposals and assigned the scores detailed in Table 1 below.

Table 1: Commercial Linkage Fee RFP Scoring

	Points	David Paul Rosen & Associates	Strategic Economics	Keyser Marston Associates
Experience of Proposer	30	24	18	27
Customer Satisfaction/Firm Reputation	20	18	18	18
Strength of Proposed Work Plan and Study Methodology in Meeting the Objectives Outlined in the RFP	25	22	16	25
Fee Structure (Cost)	15	15	15	15
Local Business Enterprise	5	0	0	0
Small Business Enterprise	5	0	0	0
TOTAL	100	79	67	85

Based on these results, Keyser Marston was awarded the contract. Staff has negotiated and executed a contract with Keyser Marston to conduct the nexus and feasibility study.

As part of its consideration of the Housing Crisis Workplan at the September 24, 2019 City Council Meeting, the Council directed staff to include an attachment with approved planning permits for all commercial development projects citywide notifying developers that they may be required to pay a commercial linkage fee pending completion of nexus and feasibility studies and approval of a fee program by the Council. The Department of Planning, Building and Code Enforcement has implemented this direction.

ANALYSIS

This memorandum provides an overview of the scope of the study as specified in the consultant contract, an update on the work Keyser Marston has conducted so far, and a review of the anticipated project timeline.

Project Scope

Given the diversity of San José's commercial development market, the nexus and feasibility studies will analyze a relatively large number of commercial prototypes, and the feasibility study will consider these prototypes across a variety of geographic areas within the city. The following bullets summarize the key elements of the project scope, including the high-tech office prototype and sensitivity analysis issues included in the City Council direction.

- **Development Prototype and Geographic Sub-Area Selection:** The nexus and feasibility studies will each analyze eight development prototypes. Prototypes are models of particular types of development characterized by tenant type, number of stories, floor area ratio, parking configuration and other features. The prototypes used for the nexus study will encompass broader categories than the feasibility prototypes to ensure that they include the full range of development activity within a category. For the feasibility study, prototypes will be analyzed across five or more geographic areas within the city to capture different market conditions. The contract requires the consultant to propose a high-tech office prototype for consideration as part of the study.
- **Nexus Study:** The consultant will conduct a nexus study that establishes the basis for the fee by assessing how new commercial development increases the need for affordable housing and providing evidence of a reasonable relationship between the need for affordable housing and the type of development.
- **Feasibility Study:** The consultant will conduct a feasibility study that analyzes the effects of a potential commercial linkage fee on the economics of each of the building prototypes within the identified geographic areas. The study will use a residual land value methodology that identifies land values supported by current development economics. The consultant will analyze the impact of a potential fee at a range of different levels. The consultant will also conduct a sensitivity analysis that evaluates the potential for feasibility of certain prototypes to change over the next several years based on trends or foreseeable changes in the market.
- **Fee Comparison and Policy Options:** The consultant will prepare information on commercial linkage fee programs established by other jurisdictions and will develop a series of fee policy options for the City's consideration, including fee levels by building type and geographic sub-area, and square footage thresholds for application of the requirement. The consultant will also use historic building permit activity to estimate the annual fee revenue that would be generated at various fee levels.
- **Meetings and Outreach:** The consultant will be available to attend outreach meetings as well as meetings of committees or the City Council. Outreach will be conducted primarily in two phases: to solicit feedback from stakeholders on the proposed prototypes and near the end of the process once a draft study has been released.

Status Update – Prototype Selection

Keyser Marston has prepared a memorandum, included as Attachment A, that outlines recommended development prototypes and market subareas for study as part of the nexus and feasibility studies. The prototype recommendations are based in part on a review of recent and planned non-residential projects in San José. The results of this review can be found in Appendix Table 4 attached to the Keyser Marston memorandum. Keyser Marston's recommendations for nexus study prototypes are summarized in Table 2.

Table 2: Proposed Building Types for Inclusion in Nexus Study	
Research and Development	
Office	
High-Tech Office	
Retail (would include service uses such as dry cleaners)	
Hotel	
Industrial	
Warehouse	
Residential Care/Assisted Living	

As noted above, the prototypes used in the nexus study will be different from the prototypes used in the feasibility study; they will encompass broader categories than the feasibility prototypes to ensure that they establish a nexus the full range of development activity within a category. The proposed feasibility prototypes, outlined in Table 3, are focused on the most active types of development, along with development types in which the Council has expressed a specific interest, such as high-tech office.

Table 3: Proposed Building Types for Inclusion in the Financial Feasibility Analysis	
Office/R&D – 1-2 stories	
Office/R&D – mid-rise	
Office – high-rise	
Office – high-tech owner / user	
Retail – Neighborhood or community retail center	
Hotel – mid-rise	
Light Industrial / R&D	
Warehouse / Distribution	

As part of the feasibility study, each prototype will be analyzed in the context of growth areas where it would be expected to develop. The growth areas proposed for this study are outlined in Table 4. Keyser Marston’s proposal for how to assign prototypes to subareas can be found on page 5 of Attachment A.

Table 4: Proposed Market Subareas for Inclusion in the Financial Feasibility Analysis	
Downtown and Vicinity	
Edenvale	
North San José and Vicinity	
West San José Urban Village	
Monterey Corridor	
South and East San José Growth Areas	

Over the next few weeks, staff will schedule stakeholder focus group meetings to gather feedback from both housing advocates and the business community on these prototype proposals. Once staff and the consultant have considered any feedback provided by stakeholders, the prototypes will be finalized.

Timeline

The below timeline shows the targeted project schedule. Stakeholder outreach on the proposed development prototypes and geographic sub-areas will occur in November. The consultant will then conduct the analysis and prepare the report, with the goal of returning to Council by April 2020.

Table 5: Project Timeline

Milestone	Timeframe
Draft development prototypes and geographic sub-areas. Stakeholder outreach on proposed prototypes.	November 2019
Nexus and feasibility draft technical analysis submittal	December 2019
Admin draft nexus and feasibility reports	January 2020
Public Review Draft Report	February 2020
Public Outreach Meetings on Public Draft	February-March 2020
Final Draft Report	April 2020
City Council Meeting	April 2020

COORDINATION

This memorandum has been coordinated with the City Attorney’s Office.

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