COUNCIL AGENDA: 09/01/20
ITEM: 8.2

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Mayor Liccardo
Vice-Mayor Jones
Councilmember Diep
Councilmember Davis
Councilmember Foley

SUBJECT: COMMERICAL LINKAGE FEE

DATE: August 28, 2020

APPROVED:

DATE: 8/28/20

RECOMMENDATION:

Approve the staff recommendation with the following changes:

1. For Downtown Office Space over 100,000 square feet, offer 3 options:

   - Option 1: $12/per square foot if paid upon Certificate of Occupancy (COO)

   - Option 2: $15/per square foot, paid in phases:
     - $5 at issuance of COO
     - $10 payable proportionate to the percentage of rentable building space for which there is Tenant Improvement (TI) certification, so that fees are paid as leases are secured, and prior to employees filling the building.

   - Option 3: Directly build affordable units
     - Deliver a prescribed number of affordable units equivalent to the applicable fee, based on a formula to be devised by Housing & OED staff for inclusionary fees on residential construction. The ground-breaking of the affordable housing project must precede the issuance of a certificate of occupancy on the commercial space.

2. For all office projects less than 100,000 square feet, the fee for the first 40,000 square feet is $0.

3. For citywide office projects over 100,000 square feet, provide "Option #2 ($2 at COO and $3 with Tenant Improvements) as well as Option #3 (opportunity to deliver affordable units).

4. For industrial projects over 100,000 square feet, provide "Option #2 ($1 at COO and $2 with Tenant Improvements) as well as Option #3 (opportunity to deliver affordable units).

5. For hotel projects, staff should provide Option #3 (opportunity to deliver affordable units).

6. In light of rapidly growing vacancy for all retail space, and severe loss of retail employment, set retail fees at $0, regardless of size.

7. All state-licensed Residential Care Facilities for the Elderly should be classified as a commercial use, regardless of what kitchen facilities the individual rooms have. The fee would be calculated on the square footage of residential rooms, instead of a per-unit IHO fee. This will ensure that amenity space will not be minimized. Staff should return to the City Council to verify the per square foot fee within 60 days. Staff should also examine how to address similar projects that solely serve disabled residents, and projects that include low-income units.

8. Explore credits for on-site historic preservation, or sustainability at the NetZero standard, not to exceed 20%. The credit could apply directly to this fee, or applied against the total fee calculation.

9. Conduct a new feasibility study, to be undertaken no more than two years from fee adoption. If new leasing comp's are not available, use other available data to assess commercial market dynamics such as availability rates and absorption.

10. As discussed in City Council Priority #8 (Universal Fee Framework) create a "single point of contact" within the existing Development Services staff.

DISCUSSION:

The Commercial Linkage Fee (CLF) is a long-discussed tool to increase desperately-needed affordable housing supply in our region. Its imposition in San Jose, however, raises unique challenges, due to our historically poor job-to-housing ratio, the lowest of any major U.S. city. The consequences of our jobs-housing imbalance include chronic fiscal shortfalls, inadequate city services, congested freeways, greater greenhouse gas emissions, and the most thinly staffed City Hall of any large city in the nation. This imbalance hits our low-income communities the hardest, depriving them of job opportunities and critical services like after-school programs, gang prevention services, emergency medical response, and senior nutrition programs.

The "boom" of the last decade did little to change the historic pattern of job development in our Valley, with jobs-heavy cities to our west and north growing rapidly, while San Jose continued to struggle to find resources to serve residents who work in those jobs. As the staff report reveals, two cities that together have about one-quarter of San Jose's population—namely Sunnyvale and Santa Clara—have seen five times as much commercial space built in their cities over the last decade as has job-poor San Jose. Now, of course, our community suffers with double-digit unemployment, and more than 70,000 San Jose residents have applied for unemployment benefits in the last half year.

Meanwhile, the affordable housing crisis persists--and has grown only more acute over the last decade. We must find more resources to address that crisis. In short, we need both jobs and housing—particularly jobs and housing accessible to historically underserved families in our community whose suffering has grown more intense in recent months.

Accordingly, we offer recommendations to find a balanced approach that enables millions of dollars more in funding for affordable housing than the recommendations proposed by staff—primarily by increasing office fees Downtown--while ensuring that we do not impose obstacles to job creation.

There has never been a more challenging time to impose additional costs on commercial builders. The uncertainty of the long-term effects of COVID-19 has brought commercial lending to a standstill. One prominent builder downtown halted their 1 million square-foot-project on Julian Street, after completing the shoring work. Six million of square feet have become vacant for sublease in the historically high-demand market of San Francisco. The feasibility study submitted to the City—which seemingly neglected to account for any of the reality we've seen in the office and industrial market over the past six months--was greeted with incredulity in the development community. Indeed, any commercial development dependent on external financing is infeasible at a commercial impact fee of $0, let alone anything higher.

The uncertain trajectory of this pandemic makes it impossible to answer key questions pertaining to rents. We must embark on further study in the near term to ensure that our decisions remain data-driven, and we urge that a subsequent feasibility study come back to Council within the next two years.

Although we recommend higher fees than staff does on large Downtown office space, we also recommend more flexibility to enable builders to fulfill Commercial Linkage Fee obligations during this time of great uncertainty. Giving builders an option of paying a higher fee over time--as the building is leased up--can hedge risk for builders, while increasing the aggregate affordable housing resources for the public. It also aligns fee payment with the actual justification for an affordable housing impact fee: occupancy of space by workers. The third option--giving builders the ability to directly deliver housing in lieu of paying fees--can dramatically accelerate affordable housing production.

Retail space is among the hardest hit sectors as a result of the pandemic. Large retail concepts will be no less affected, and COVID has underscored the importance of easy access to goods and services.

The Universal Fee Council Priority (#8 on the list) is intended to streamline the process of fee estimating and implementation. As we look to add this important fee, we should designate a position within the existing staff structure to ensure that fees are proactively collected.

BROWN ACT

The signers of this memorandum have not had, and will not have, any private conversation with any other member of the City Council, or that member's staff, concerning any action discussed in the memorandum, and that each signer's staff members have not had, and have been instructed not to have, any such conversation with any other member of the City Council or that member's staff.