CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO:	HONORABLE MAYOR AND CITY COUNCIL	**FROM:**	Christopher Burton
SUBJECT:	**See Below**	**DATE:**	October 27, 2025
Approved		Date:	11/5/25

COUNCIL DISTRICT: 6

SUBJECT: Temporary Deferral of the Diridon Station Area Basic Infrastructure Impact Fee for Non-Residential Development

RECOMMENDATION

Adopt a resolution pursuant to San José Municipal Code Section 14.35.040A:

(a) Authorizing the temporary deferral of payment of the Diridon Station Area Basic Infrastructure Impact Fee from building permit to occupancy for any non-residential development obtaining building permit for vertical construction by December 31, 2028; and
(b) Authorizing the City Manager or her designee to negotiate and execute project completion agreements to temporary defer payment of the Diridon Station Area Basic Infrastructure Impact Fee for any non-residential development obtaining building permit for vertical construction by December 31, 2028.

SUMMARY AND OUTCOME

Approval of this recommendation would align the timing of the Diridon Station Area Infrastructure Impact Fee with the intent of California Senate Bill 937, which requires local agencies to defer impact fees under the Mitigation Fee Act until occupancy for residential development. Extending similar flexibility to non-residential projects will provide near-term relief to maintain project viability during a period of weakened demand in the office market, while ensuring the City of San José (City) ultimately receives the full fee amount prior to building occupancy.

This action supports the continued revitalization of the Diridon Station Area by enabling entitled projects to proceed with critical construction activity without triggering substantial upfront costs that could otherwise stall or permanently halt progress.

BACKGROUND

On August 20, 2019, the City Council adopted Ordinance No. 30305, establishing the Diridon Station Area Basic Infrastructure Impact Fee to fund essential public improvements in transportation, stormwater, and public space categories.

The ordinance currently requires fee payment prior to building permit issuance. The purpose of this approach was to secure infrastructure funding early in the development process, consistent with the City's Mitigation Fee Act obligations. However, this structure also creates significant capital timing challenges for large-scale commercial projects, which must front-load fees before construction financing can be fully stabilized.

The City’s Downtown and Diridon market has since undergone considerable transition. Hybrid and remote work have fundamentally reshaped office demand across Silicon Valley, creating uncertain absorption forecasts and more conservative lender underwriting. Several entitled projects within the Diridon Station Area are currently paused, facing difficulty securing tenants and financing commitments.

ANALYSIS

The purpose of deferring payment of the Diridon Station Area Infrastructure Impact Fee until occupancy is to provide immediate flexibility for entitled projects that are struggling to move forward in the current economic environment. Several large developments in the area, including one that has already completed podium construction, face a difficult decision between pausing indefinitely or redesigning to meet new building code standards. Requiring full fee payment before building permit issuance places a significant upfront cost burden on these projects at a time when office demand remains weak, construction financing is constrained, and tenant commitments are uncertain. Allowing payment at occupancy would enable these projects to remain active, pull permits, and continue limited work while pursuing tenants and final financing, thereby maintaining construction momentum and preserving the City’s broader vision for the Diridon area.

This proposed change is consistent with the City’s ongoing effort to adjust its development fee framework to reflect current market realities. The Diridon Station Area was envisioned as a mixed-use employment hub that would anchor regional transit investments and extend downtown’s urban fabric westward. That vision remains sound, but the economic landscape has shifted dramatically since the fee was adopted in 2019.

Remote and hybrid work patterns have reshaped the office market across Silicon Valley, leading to persistently high vacancy rates and a sharp contraction in speculative office construction. At the same time, construction costs have risen by more than 25% since 2020, and lenders now require stronger pre-leasing and equity positions before committing to new projects. These conditions have created a challenging financing environment that is unlikely to recover quickly, but where small, time-limited policy adjustments can help keep projects viable until market confidence returns.

The proposed deferral aligns with state policy direction embodied in Senate Bill 937, which allows certain "designated residential development projects" to defer impact fee payments until final inspection or occupancy for residential development. While the statute does not extend to non-residential projects, reducing the timing pressure on projects during construction while still ensuring that the City ultimately collects the full amount prior to construction completion would promote these types of development. The approach is also consistent with San José's recent Multifamily Housing Incentive Program, which temporarily deferred construction tax and inclusionary housing payments to occupancy in order to signal stability and support project feasibility during a difficult market cycle. Extending a similar structure to nonresidential projects in the Diridon Station Area reflects a balanced, market-responsive application of the same principles.

From a fiscal perspective, this proposal does not reduce the total fee obligation or alter its eligible uses. It only adjusts when payment is due, which will impact the timing of Capital Improvement Program moving forward until fully funded. Staff will closely monitor progress of the project construction to ensure payment is received prior to final inspection or occupancy (whichever occurs first). The deferral will require a project completion agreement executed by the City Manager, or her designee, before building permit issuance, ensuring that the City retains a binding commitment for full payment before any final inspection or occupancy (whichever is first).

This modest administrative change could have an outsized impact on project viability. By allowing developers to move forward and maintain their financing pipeline, the City can avoid the longer-term risks of stalled or partially completed sites and the reputational cost of disinvestment in its primary downtown growth district. It is an important step to preserve momentum in the Diridon Station Area while maintaining the integrity of the City's infrastructure funding program and reaffirming the City's commitment to adaptive, economically grounded implementation of its adopted plans.

Although Senate Bill 973 does not include a formal sunset date, staff recognizes that current economic conditions may be temporary. For that reason, the proposed deferral provision would apply for a three-year period (building permit for vertical construction must be obtained by December 31, 2028 to qualify for the deferral program), allowing projects currently in the entitlement and permitting pipeline sufficient time to apply for and secure building permits. At the end of this period on December 31, 2028, staff will evaluate the program's effectiveness and any fiscal or operational impacts and return to the City Council with recommendations on whether to extend or modify the policy. This timeframe will also serve as a benchmark for analyzing how fee deferrals affect project timing, revenue collection, and overall development activity, providing data that can inform future policy decisions as part of the broader Development Fee Framework that is being developed as part of the Housing Catalyst Work Plan and included in the Housing Element.

EVALUATION AND FOLLOW-UP

Staff will enter into Project Completion Agreements with eligible projects and return annually to the City Council to report on progress of delivery of necessary projects. Further, staff envisions a regular update to the scope of projects included in the infrastructure needs of the fee area, as opportunities and needs arise in response to proposed or planned development.

COST SUMMARY/IMPLICATIONS

This action only modifies the timing of fee collection; it will not affect the overall financial position of the Diridon Station Area Impact Fee Fund. The proposed action would not change the total amount of fees owed by any development, nor would it alter how those revenues are allocated or spent. It would only adjust the timing of payment from building permit issuance to the first final inspection for eligible non-residential projects. This change would temporarily defer revenue collection during the construction period but would not reduce the City's total fee revenue or its long-term capacity to deliver planned infrastructure. The fee program was originally estimated to generate approximately $75 million (based on 2018 construction cost assumptions) to fund improvements to transportation networks, sanitary sewer and storm drainage systems, and public plazas within the district. These revenues are adjusted annually in accordance with the Construction Cost Index and are deposited into the Diridon Station Area Impact Fee Fund, where they are separately tracked by category to ensure transparency and compliance with the Mitigation Fee Act.

COORDINATION

This memorandum has been coordinated with the City Attorney's Office, City Manager's Budget Office, City Manager's Office of Economic Development and Cultural Affairs, Public Works Department, and Transportation Department.

PUBLIC OUTREACH

This memorandum will be posted on the City's Council Agenda website for the November 18, 2025 City Council Meeting.

COMMISSION RECOMMENDATION AND INPUT

No commission recommendation or input is associated with this action.

CEQA

Statutorily Exempt, File No. PP17-005, CEQA Guidelines Section 15273, Adjustment to Fees, Rates and Fares without changes to or expansion of services.

PUBLIC SUBSIDY REPORTING

This item does not include a public subsidy as defined in section 53083 or 53083.1 of the California Government Code or the City's Open Government Resolution.

/s/
Christopher Burton
Director, Planning, Building, and Code
Enforcement Department

For questions, please contact Alex Powell, Chief of Staff, Planning, Building, and Code Enforcement Department, at alex.powell@sanjoseca.gov or (408) 535-1258.