CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Councilmember Jimenez

SUBJECT: **SEE BELOW**

DATE: June 17, 2024

Approved

Date: 6/17/2024

SUBJECT: Downtown Residential High-Rise Incentive Program Extension

RECOMMENDATION

Approve staff recommendations (a), (b), and (c).

BACKGROUND

Although I have expressed concerns about extending the Downtown Residential High-Rise Incentive Program for many years, I urge my colleagues to approve staff recommendations (a), (b), and (c).

I appreciate the intent behind the memo from Mayor Mahan, Vice Mayor Kamei, and Councilmembers Torres, Davis, and Candelas. All of us share the goal to increase housing production in Downtown and Citywide. However, I have concerns about the approach described in recommendation #1.

First, I encourage the City Attorney to clarify whether eliminating fixed timelines complies with Chapter 14.10 of the San José Municipal Code. Exemptions from the definition of "Subsidy" require findings made by the Council that are supported by a financial feasibility study. The study must include the "anticipated duration of any condition(s) making construction of the Private Construction Projects in the specified Subcategory of Use Financially Infeasible" (14.10.310(C)(2)(c)). The October 2023 Cost of Residential Development report prepared by Century Urban does not appear to provide evidence for a finding to support extending the High-Rise Incentive Program indefinitely.

In prior Council deliberations regarding extension of the Incentive Program, City staff consistently referenced Chapter 14.10 when establishing deadlines. For example, in the memorandum dated August 6, 2020, staff advises:

> "Any recommendation to extend the fee reduction beyond the deadlines considered at the November 5, 2019, City Council meeting would require an updated feasibility analysis; otherwise, the reduction could be considered a subsidy under Chapter 14.10 of the San José Municipal Code. This means projects would be subject to workforce standards, including prevailing wage requirements" (page 6).

To the best of my knowledge, Chapter 14.10 has not been updated since then, and the same constraints apply. Without an updated report from a qualified consultant, applying a fee reduction or waiver arbitrarily to the next 10,000 units, regardless of changes in macroeconomic forces, could be deemed a subsidy and subject these units to workforce standards.

Second, I encourage my colleagues to be mindful of the caution advised by staff on page 11 of May 28, 2024, staff report: "Without the recommended timeframes, staff is concerned that the revised High-Rise Program would not incent development enough to get projects under construction quickly in line with policy goals." I understood this as both a recognition that a class of projects with entitlements was the focus of the structured approach to the proposed timeline, but also that the intent was not an open-ended subsidy to all residential downtown development without limit.

As the Cost of Residential Development report demonstrates, macroeconomic forces have a far greater impact on financial feasibility than do City fees and taxes. In fact, as stated in the October 19, 2023, staff memo:

> "Reduction of these taxes and fees to zero would improve feasibility slightly, but would not fundamentally change the outcome of the analysis; more importantly, such elimination would also significantly reduce City resources necessary to support transportation infrastructure, renovate and create new park infrastructure, and support affordable housing and related grant-matching requirements that support all these programs" (page 7).

Although not specifically quantified in the report, the impact of significant increases in interest rates and borrowing costs is not offset even by complete elimination of City fees and taxes. Even if it were possible to extend the High-Rise Incentive Program indefinitely, there is a great risk that many developers will not expedite construction, but instead wait until macroeconomic factors become more favorable, and then benefit from fee and tax reductions that were not actually necessary to achieve financial feasibility. The Council would benefit from a sensitivity analysis showing the relative impact of certain reductions in interest rates, compared with the proposed fee and tax reductions.

We should also take the time to reconsider some of the assumptions in the feasibility analysis itself. For instance, despite eliminating minimum parking requirements, the assumed parking ratio for for-sale residential is 1.1, and for rental is either 0.8 (pages 6 and 19) or 1.0 (pages 31 and 32). In any case, the cost of underground parking is significant, and it is not clear if this remains a defensible assumption given the City's recent elimination of parking requirements. A sensitivity analysis should be provided in future reports to demonstrate the impact of reductions to the parking ratio, and how this compares with the proposed fee and tax reductions.

If the Council wishes to extend the Downtown Residential High-Rise Incentive Program, it would be safest and most prudent to do so in accordance with the staff recommendations.

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.