CITY OF CUPERTINO

Summary and Recommendations
Below Market Rate Housing Mitigation Program

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CUPERTINO

Prepared by Keyser Marston Associates, Inc.

April 2015

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Prepared for:

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Submitted by:

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I. INTRODUCTION

This Summary and Recommendations report provides a concise version of the nexus analyses, findings and recommendations to the City of Cupertino for the update of its Below Market Rate (BMR) Housing Mitigation Program. The City engaged Keyser Marston Associates, Inc. (KMA) to assist with an overall update of the Program, including conducting residential and non-residential nexus analyses. The goal of the study is to update the program to ensure that it is an effective tool for creating new affordable housing in the context of the changed legal and economic environment in recent years.

A. Background and Context

The City of Cupertino's BMR Housing Mitigation Program imposes requirements on both non-residential and residential construction to assist in the creation of new affordable housing in the City.

The City's current Residential Mitigation Program, which applies to all new residential developments, was adopted in 1993 to mitigate the impact of market rate housing on the need for affordable housing. An ownership residential development is any residential development that includes the approval of a subdivision map and creates one or more units that may be sold individually. Ownership developments between one and six units may either pay an impact fee or provide one median-income BMR unit onsite. Ownership developments of 7 units or greater are required to set aside 15% of the units within the development as BMR units. Half of the onsite BMR units must be made available to median-income households and half to moderate-income households. A rental residential development is any residential development that creates new dwelling units that cannot be sold individually. For rental units, the City formerly required developers to set aside 15% of units as BMR units, and the affordability levels were set at 40% at low income and 60% at very low income. However, since the Court of Appeal's *Palmer* decision, cities have been precluded from requiring affordable units within rental projects unless the developer receives financial assistance or a regulatory incentive from the City. As a result, all new rental developments in Cupertino are currently required to pay the Housing Mitigation Program impact fee. The current Housing Mitigation Fee is $3.00 per square foot for both ownership and rental projects.

The Office and Industrial Mitigation fee program was also adopted in 1993, establishing a housing impact fee levied on all new office and industrial construction. Fee revenues are used to increase the supply of affordable housing in Cupertino. The fee program was supported by a study prepared in 1992 entitled *A Study to Examine the Relationship of Land Use and the Creation of Additional Housing Needs* by Planning Resource and Associates. In 2004, KMA prepared a jobs-housing linkage analysis, or nexus study, in support of adjusting fees and expanding the fee program to include hotel and retail development. The fee is currently set at $6.00 per square foot and applies to new office, industrial, hotel, retail and research and development (R&D) space.

The analysis presented in this report will enable the City to update its BMR Housing Mitigation Program for both Residential and Non-Residential development.

B. Organization of this Report

This report provides a summary of both the residential and non-residential analyses, including an overview of the methodology and a presentation of the findings. This report also provides a discussion of KMA's recommendations for the City of Cupertino. The complete analyses and other materials are contained in two separate reports: Residential Below Market Rate Housing Nexus Analysis and Non-Residential Jobs-Housing Nexus Analysis.

II. RESIDENTIAL NEXUS ANALYSIS SUMMARY

The residential nexus analysis establishes maximum supportable inclusionary percentages and housing impact fee levels. A brief overview is included here; full documentation can be found in the report titled Residential Below Market Rate Housing Nexus Analysis.

The underlying concept of the residential nexus analysis is that the newly constructed units represent net new households in Cupertino. These households represent new income in the City that will consume goods and services, either through purchases of goods and services or "consumption" of governmental services. New consumption generates new local jobs; a portion of the new jobs are at lower compensation levels; low compensation jobs relate to lower income households that cannot afford market rate units in Cupertino and therefore need affordable housing.

In collaboration with City staff, a total of six market rate residential prototypes were selected: four ownership prototypes and two rental prototypes. The intent of the selected prototypes is to identify representative development prototypes likely to be developed in Cupertino in the immediate to mid-term future.

A summary of the six residential prototypes is presented below in Exhibit 1. Market survey data, City planning documents and other sources were used to develop the information. Market sales prices and rent levels were estimated based on KMA's market research, in discussion with City staff.

Exhibit 1: Summary of Residential Prototypes

Prototype	*Larger Single Family Home*	*Smaller Single Family (SF)*	*Small Lot SF/ Townhome*	*Condominium*	*Lower Density Apartment*	*Higher Density Apartment*
Building Type	2 stories	2 stories	2 to 3 stories	3 to 4 stories, podium	4 stories, podium	Up to 8 stories
Avg. Net Unit Size (SF)	3,850	2,800	1,850	1,200	1,000	1,000
Avg. Gross Unit Size (SF)	NA	NA	NA	1,500	1,250	1,250
Avg. No Bedrooms	5 beds	4 beds	3 beds	2 to 3 beds	1,2,3 beds	1,2,3 beds
Lot Size / Density (units/acre)	9,500 sf	7,100 sf	10 – 20	25 – 35	25 – 35	35 - 110
Sale price/rent level	$2,600,000	$1,750,000	$1,110,000	$800,000	$3,250/mo.	$4,000/mo.
Price PSF (net)	$675	$625	$600	$667	$3.25	$4.00
Examples	20840 McClellan Rd. 10114 Crescent Ct. Bollinger Rd	Blaney Subdivision Charsan Lane	Foothill Blvd Live/Work Murano Circle Las Palmas Stevens Canyon	Metropolitan Villagio Oak Park Village Nineteen800	The Markham (formerly Villa Serra) Biltmore Adjacency Main Street N. Foothill Blvd	Monte Bello (sold as condos) The Hamptons

The nexus analysis is conducted for each of the six market rate residential prototypes. Using the sales price or rent level of the unit, KMA estimates the household income of the purchasing/renting household. Household income is then translated to income available for expenditures, which is then input into the IMPLAN model to estimate the employment generated by new household spending. The IMPLAN model is an economic model widely used for the past 35 years to quantify the impacts of changes in a local economy. The IMPLAN model estimates the number of jobs generated by the new households; for ease of presentation, the analysis is conducted for 100 market rate units. The results are shown in Exhibit 2 below.

Exhibit 2: Prototypical Residential Units, Household Income and Jobs Generated						
	Larger Single Family Home	*Smaller Single Family (SF)*	*Small Lot SF/ Townhome*	*Condo-minium*	*Lower Density Apartment*	*Higher Density Apartment*
Market Sales Price/ Rent	$2,600,000	$1,750,000	$1,110,000	$800,000	$3,250/mo.	$4,000/mo.
Gross Household Income	$445,000	$300,000	$208,000	$154,000	$130,000	$160,000
Household Income Available for Expenditures [Input to IMPLAN model]	$231,000	$165,000	$129,000	$103,000	$85,000	$104,000
Total Jobs Generated, 100 Units	142.2	101.4	79.3	63.4	50.8	63.9

See Residential Below Market Rate Housing Nexus Analysis report for full documentation.

The IMPLAN model estimates the total jobs by industry. KMA then uses its own jobs-housing nexus model to translate jobs by industry to jobs by occupation. Recent and local California Employment Development Department (EDD) data on compensation level by occupation is used to sort those jobs into new worker households by income level. The model estimates a range of new worker household sizes and number of workers per household based on Santa Clara County demographic data from the Census. The results of the jobs-housing nexus model are shown below in Exhibit 3.

Exhibit 3: New Worker Households by Income Level per 100 Market Rate Units						
	Larger Single Family Home	*Smaller Single Family (SF)*	*Small Lot SF/ Townhome*	*Condo-minium*	*Lower Density Apartment*	*Higher Density Apartment*
Very Low (Under 50% AMI)	30.2	21.5	16.8	13.5	10.9	13.6
Low (50%-80% AMI)	16.2	11.5	9.0	7.2	5.7	7.3
Moderate (80%-120% AMI)	8.8	6.3	4.9	3.9	3.1	4.0
Total, Less than 120% AMI	**55.2**	**39.4**	**30.8**	**24.6**	**19.7**	**24.8**
Greater than 120% AMI	11.0	7.9	6.2	4.9	4.0	5.0
Total, New Households	**66.2**	**47.2**	**36.9**	**29.5**	**23.7**	**29.8**

See Residential Below Market Rate Housing Nexus Analysis report for full documentation.

Housing demand is distributed across the lower income tiers. The finding that the greatest number of households occurs in the Very Low income tier is driven by the fact that jobs associated with consumer spending tend to be low-paying, such as food preparation, administrative, and retail sales occupations.

A. Inclusionary Percentages Supported

The analysis identifies how many lower income households are generated for every 100 market rate units. These findings are then translated to a supported inclusionary percentage, which represents the percent of units provided on-site within a project that would fully mitigate the affordable housing impacts as documented in this nexus analysis.

The inset table below presents the results of the analysis; each tier is cumulative, or inclusive of the tiers above.

Exhibit 4: Cumulative Inclusionary Percentage Supported by Nexus Analysis

	Larger Single Family Home	*Smaller Single Family (SF)*	*Small Lot SF/ Townhome*	*Condo-minium*	*Lower Density Apartment*	*Higher Density Apartment*
Very Low (Under 50% AMI)	23%	18%	14%	12%	10%	12%
Low (50%-80% AMI)	32%	25%	21%	17%	14%	17%
Moderate (80%-120% AMI)	36%	28%	24%	20%	16%	20%

See <u>Residential Below Market Rate Housing Nexus Analysis</u> report for full documentation.

Should the courts determine that the inclusionary percentages must be supported by a nexus analysis, this series of results would indicate that the 15% requirement in Cupertino is supported for all ownership prototypes. In fact, the analysis demonstrates that at least 20% is supported, based on the lowest of the ownership prototypes, the condominium. The supported inclusionary percentages for rental prototypes are presented for information only, since the on-site units for rentals cannot be required, per the *Palmer* decision. The developer may elect to negotiate with the City to include on-site units (in any number or percentage) with the City offering financial and/or regulatory concessions. Exhibit 4 indicates the percentage of affordable units that would be needed to fully mitigate the impact of the project.

B. Nexus Supported Maximum Fee Levels

The next step in the nexus analysis takes the number of households in the lower income categories associated with the market rate units and identifies the total subsidy required to make housing affordable. This is done for each of the prototype units to establish the ‘total nexus cost,’ which is the Maximum Supported Impact Fee supported by the nexus analysis. For the purposes of this analysis, KMA assumes that affordable housing fee revenues will be used by the City to subsidize affordable rental units for households earning less than 80% of median income, and to subsidize affordable ownership units for households earning between 80% and 120% of median income. Affordability gaps are calculated for each of the income tiers; the nexus costs are calculated by multiplying the affordability gaps by the number of households in each income level. The nexus costs at each income level are then summed to calculate the Maximum Supported Impact Fee. See Appendix C of either the Residential Below Market Rate Housing Nexus Analysis report or the Non-Residential Jobs-Housing Nexus Analysis report for more information on affordability gaps.

The Maximum Supported Impact Fees are calculated at the per-unit level and the per-square-foot level and are shown in Exhibit 5.

Exhibit 5: Maximum Supported Impact Fees

	Larger Single Family Home	*Smaller Single Family (SF)*	*Small Lot SF/ Townhome*	*Condo-minium*	*Lower Density Apartment*	*Higher Density Apartment*
Per Market Rate Unit	$118,100	$84,200	$65,900	$52,600	$42,300	$53,100
Per Square Foot*	$30.60	$30.10	$35.60	$35.10	$33.80	$42.50

* Excludes garage space for single family units. Unit sizes for condominiums and apartments are based on gross building area, and include an allowance for common areas.

These costs express the maximum supported impact fees for the six residential prototype developments in Cupertino. They are **not** recommended fee levels; they represent maximums justified by the nexus analysis.

III. NON-RESIDENTIAL NEXUS ANALYSIS

The non-residential nexus analysis quantifies and documents the impact of the construction of new workplace buildings (office, retail, hotels, etc.) on the demand for affordable housing. It is conducted to support an update to the City's Office and Industrial Mitigation Program. Full documentation of this analysis is contained in the report titled Non-Residential Jobs Housing Nexus Analysis.

The workplace buildings that are the subject of this analysis represent a cross section of typical commercial buildings developed in Cupertino in recent years and expected to be built in the near term future. For purposes of the analysis, the following building types were identified:

- Office (including high-tech, industrial, R&D, and medical office)
- Hotel
- Commercial / Retail / Restaurant

The nexus analysis links new commercial buildings with new workers; these workers demand additional housing, a portion of which needs to be affordable to the workers in lower income households. The analysis begins by assuming a 100,000 square foot building for each of the three building types and then makes the following calculations:

- The total number of employees working in the building is estimated based on average employment density data.
- Occupation and income information for typical job types in the building are used to calculate how many of those jobs pay compensation at the levels addressed in the analysis. Compensation data is from California EDD and is specific to Santa Clara County. Worker occupations by building type are derived from the 2013 Occupational Employment Survey by the U.S. Bureau of Labor Statistics.
- New jobs are adjusted to new households, using Santa Clara County demographics on the number of workers per household. We know from the Census that many workers are members of households where more than one person is employed and there is also a range of household sizes; we use factors derived from the Census to translate the number of workers into households of various size. Household income is calculated depending on the number of workers per household.
- The number of Very Low-, Low-, and Moderate-Income households generated by the new development is calculated and divided by the 100,000 square foot building size to arrive at coefficients of housing units per square foot of building area. The household income categories addressed in the analysis are the same as those in the Residential Nexus Analysis.
- The number of lower income households per square foot is multiplied by the Affordability Gap, or the cost of delivering housing units affordable to these income groups. This is the Maximum Supported Impact Fee for the non-residential land uses.

The Maximum Supported Impact Fees for the three building types are as follows in Exhibit 6:

Exhibit 6: Maximum Supported Impact Fees Per Sq. Ft. of Building Area	
Land Use	*Impact Fees per Sq. Ft.*
Office	$129.05 psf
Hotel	$49.15 psf
Commercial / Retail / Restaurant	$222.32 psf

Note: Nexus findings are not recommended fee levels.
See Non-Residential Jobs-Housing Nexus Analysis for detail.

The results of the analysis are heavily driven by the density of employees within buildings in combination with the occupational make-up of the workers in the buildings. Retail has both high employment density and a high proportion of low paying jobs.

These figures express the maximum supported impact fee per square foot for the three building types. They are not recommended levels for fees; they represent only the maximums established by this analysis, below which fees or other requirements may be set.

IV. RECOMMENDATIONS

An affordable housing nexus analysis does not establish a recommended fee level, but instead sets a ceiling for the fee. In this section, KMA provides recommendations for appropriate fee levels in Cupertino. Fee recommendations are based on several factors as shown below:

1. Findings of the nexus analysis – the nexus study establishes the maximum fee that may be charged to mitigate the impacts of new development on the need for affordable housing. However, KMA recommends that the fee levels and on site requirements be established below the maximum levels established in the nexus study, based on the considerations described below.
2. Policy objectives of the Housing Element
3. Requirements in neighboring jurisdictions – staying competitive with neighboring cities
4. Setting a fee high enough to support meaningful affordable housing projects and programs
   - For residential rental projects, since the Palmer case precludes the City from requiring on-site units, the fee is proposed to be high enough to mitigate the impact of rental development and to support the construction of affordable units.
5. Setting a fee low enough to not discourage development

A. Residential Mitigation Fee Program

KMA's recommendations for updates to the residential Mitigation Fee program, including onsite obligations and a fee option, are presented in this section, along with a summary of the factors considered by KMA.

1. Nexus Analysis Findings

The findings of the residential nexus analysis are summarized below.

Exhibit 7: Residential Nexus Findings

	Larger Single Family	*Smaller Single Family*	*Small Lot SF/ Townhome*	*Condo-minium*	*Lower Density Apartment*	*Higher Density Apartment*
Supported Inclusionary Percentage – through 120% AMI	36%	28%	24%	20%	16%	20%
Maximum Supported Fee Level						
- Per Unit	$118,100	$84,200	$65,900	$52,600	$42,300	$53,100
- Per Square Foot	$30.60	$30.10	$35.60	$35.10	$33.80	$42.50

Excludes garage space for single family units. Unit sizes for condominiums and apartments are based on gross building area, and include an allowance for common areas.
AMI: Area Median Income
Source: Keyser Marston Associates Residential Below Market Rate Housing Nexus Analysis, March 2015.

KMA recommends that fee levels and onsite requirements be set below the levels shown above.

2. Affordable Housing Requirements in Other Jurisdictions

KMA assembled and summarized the affordable housing requirements for the following cities selected by City staff: San Jose, Sunnyvale, Mountain View, Fremont, Menlo Park and Palo Alto. Table 1 at the end of this report is a chart summarizing the programs in these jurisdictions.

The fee levels in Cupertino, at $3 per square foot, are lower than the fees in the neighboring jurisdictions that have housing mitigation programs applied to residential projects. For rental projects, San Jose recently adopted a fee of $17 per square foot, Mountain View's City Council has approved a fee increase to $17 per square foot, Sunnyvale is considering a fee in the $10-$20 per square foot range, and Fremont's fee is $19.50 per square foot, to be phased in over two years. Palo Alto's rental program is currently suspended; the former in-lieu fee was set at 7.5% of the appraised value of the development. Exhibit 8 shows a summarized version.

Exhibit 8: Impact Fees in Other Jurisdictions – Rental Units	
City	*Impact Fee*
Cupertino	$3.00/sq. ft.
San Jose	$17.00/sq. ft.
Mountain View	$17.00/sq. ft.
Sunnyvale	$17.00/sq. ft.
Fremont	$19.50/sq. ft.
Palo Alto	Suspended (due to Palmer Court Case; nexus study underway); formerly 7.5% of appraised value
Menlo Park	Suspended (due to Palmer Court Case; nexus study underway)

*See Table 1 for more detail.

For ownership projects, Cupertino's onsite requirements are fairly consistent with the other cities. The onsite requirements for the cities analyzed are in the 10% – 15% range, with the exception of San Jose, which has suspended its ownership requirements pending a court case, and Fremont, which has a combined onsite obligation and fee payment. Under certain circumstances, Palo Alto requires a higher percentage of units to be set aside. Cupertino's fees, however, are significantly lower than the other cities' fees. Exhibit 9 briefly summarizes the programs.

Exhibit 9: Fees & Onsite Obligations in Other Jurisdictions – Ownership Units		
City	*Onsite*	*Fee*
Cupertino	15% of units; ½ at Moderate, ½ at Median	$3.00 psf (incl. garage)
San Jose	Suspended	
Mountain View	10% of units at Median	3% of sales price
Sunnyvale	12.5% of units at Moderate	7% of sales price
Fremont	Attached: 3.5% units at Moderate + $18.50 psf Detached: 4.5% units at Moderate + $11.50 psf	$27.00 psf Attached $26.00 psf Detached
Palo Alto	15% of units; $^1/_3$ at Moderate, $^2/_3$ at Median	7.5% of sales price
Menlo Park	10-19 units: 10% as BMR units 20+ units: 15% as BMR units	< 4 units: no fee 5-9 units: In-lieu fee (sliding scale)

*See Table 1 for more detail.

Several neighboring cities structure their fee as a percent of the market rate sales price. In Cupertino, a fee equal to 3% of sales price would result in fees ranging from about $16 - $20 per square foot for the residential ownership prototypes. A fee equal to 7% of sales price would result in in-lieu fees ranging from $37 - $47 per square foot as shown below in Exhibit 10.

Exhibit 10: Fees as a Percentage of Sales Price for Residential Ownership Prototypes				
Land Use	*Sales Price*	*Unit Size*	*Fee @ 3%*	*Fee @ 7%*
Larger Single Family	$2,600,000	3,850 sq. ft.	$20/ sq. ft.	$47/ sq. ft.
Smaller Singly Family	$1,750,000	2,800 sq. ft.	$19/ sq. ft.	$44/ sq. ft.
Small Lot SF/ Townhome	$1,110,000	1,850 sq. ft.	$18/ sq. ft.	$42/ sq. ft.
Condominium	$800,000	1,500 sq. ft.	$16/ sq. ft.	$37/ sq. ft.

Excludes garage space for single family units. Unit sizes for condominiums and apartments are based on gross building area, and include an allowance for common areas.

KMA notes that Cupertino's current practice of including garage space in the fee calculation is unique among the cities in the survey. Because of this, the per square foot fee in Cupertino is equivalent to a somewhat higher fee level in the other cities. KMA understands that the City intends to change this practice; therefore, the nexus analysis is conducted excluding garages for single family homes.

3. Program Recommendations for Ownership Units

a. Impact Fee Level

The nexus analysis limits the fees based on the residential prototypes listed above in Exhibit 5 to less than $30.60 per square foot for a larger single family residence, $30.10 per square foot for a smaller single family residence, $35.60 per square foot for a small lot single family residence/townhome and $35.10 per square foot for condominium ownership units. KMA recommends a fee in the range of $15.00 - $25.00 per square foot. This range would fall comfortably below the maximum set by the nexus analysis, it is in the range of neighboring jurisdictions, and it more accurately reflects Cupertino's market strength. Refinements within the range may be recommended by staff to take into account other policy objectives. Exhibit 11 shows the recommended range.

Exhibit 11: KMA Recommendations for Ownership Units	
Requirement	*Recommendation*
Impact Fee Level	$15 to $25 per square foot

b. Onsite Obligation

It is our understanding that the City intends to continue requiring projects above a certain size to include affordable units within the project. The City's current program requires ownership projects of seven units or more to designate 15% of units as affordable, with half of the units for

Moderate Income households and half for Median Income households. The nexus analysis supports this obligation.

KMA has estimated the financial impact on developers from requiring that 15% of homes be sold at prices affordable to Moderate and Median Income households; this is referred to as the 'onsite compliance cost.' Table 2 presents our estimates of onsite compliance costs for ownership units. With current market rate sales prices, the foregone revenue associated with designating 15% of units affordable at Moderate and Median Income Levels translates to $48 psf for condominiums and $62 psf for townhome units.

KMA notes that because of the very high home prices in Cupertino, the cost to the developer of setting aside 15% of units in a market rate project in Cupertino far exceeds $20 per square foot. Therefore, the threshold above which developers must include affordable units as opposed to paying the fee becomes important.

The nexus analysis supports an onsite obligation up to 20% for ownership units. The City's current program is within the range of neighboring jurisdictions. Therefore, KMA recommends maintaining the current program requirements of 15% of units set aside for Median or Moderate Income households.

4. Program Recommendations for Rental Units

When the City established its current fee level of $3.00 per square foot, the fee was designed only for small projects (fewer than seven units) or for fractional units. Rental projects of seven units or more were required to set aside units onsite at rents affordable to Low and Very Low Income units. After the Palmer decision, however, Cupertino could no longer enforce the onsite obligations for rental projects. The nexus analysis limits the fees to less than $33.80 per square foot for lower density projects and less than $42.50 for high density projects. Given the strength of the rental market in Cupertino, KMA recommends a fee in the range of $20.00 to $30.00 per square foot. This range would fall comfortably below the maximum set by the nexus analysis, it is in the range of neighboring jurisdictions, and more accurately reflects Cupertino's dominant market strength.

Table 3 presents the onsite compliance costs for rental units. Although the City cannot require developers to include affordable rental units in a project unless the developer receives financial assistance or a regulatory incentive from the City, it is helpful to understand the cost of complying with the former program. Also, it could be helpful if the City will be negotiating for future onsite units in rental projects. It can also be useful to understand these costs when setting impact fees.

On Table 3, we calculate how each 1% of an onsite compliance requirement translates to an equivalent fee amount. For example, requiring that developers set aside 1% of rental units for Low income households is equivalent to a fee of $3.28 per square foot for the lower density apartments and $4.44 per square foot for the higher density apartments (line 21). Setting aside Very Low income units is more costly, at $3.58 - $4.74 per square foot. The figures shown in line 21 can be used to calculate onsite compliance costs for various combinations of requirements. The onsite compliance costs of Cupertino's former program are estimated at $52 and $69 per square foot for the two prototypes.

Exhibit 12 summarizes the recommended range.

Exhibit 12: KMA Recommendations for Rental Units	
Requirement	*Recommendation*
Impact Fee Level	$20 to $30 per square foot

5. Conclusions

Given the maximums established by the nexus analysis, the strength of Cupertino's housing market, and the fees in neighboring jurisdictions, KMA recommends that the City's affordable housing impact fee be set in the range of $15.00 to $30.00 per square foot for both ownership and rental units. KMA further recommends that the City continue its current onsite obligations for ownership units.

B. Non-Residential Mitigation Fees

KMA's recommendations for updates to the non-residential Mitigation Fee program are presented in this section, along with a summary of the factors considered by KMA.

1. Nexus Analysis Findings

The KMA nexus analysis found very high supportable fee levels, particularly for office and commercial/retail/restaurant space, as shown in the table below. The high fee levels supported by the analysis are not unusual for high cost areas such as Cupertino. As stated above, the nexus analysis establishes only the maximums for impact fees and will bear little relationship to the lower fee levels the City may ultimately select. Exhibit 13 indicates the nexus analysis results.

Exhibit 13: Maximum Fee Per Square Foot of Building Area	
Land Use	*Fee Per Sq. Ft.*
Office / R&D / Industrial	$129.05 psf
Hotel	$49.15 psf
Retail / Restaurant	$222.32 psf

Note: Nexus findings are <u>not</u> recommended fee levels.

In our opinion, fee levels for cities should be selected based on a combination of the strength of the local real estate for the building types that will pay the fee, and local policy objectives. We also believe it is appropriate to take into account the fee levels in neighboring jurisdictions and cities that are comparable to Cupertino in real estate demand.

2. Fees in Other Jurisdictions

Table 4 is a chart summarizing the programs in several neighboring jurisdictions selected by the City, including Mountain View, Sunnyvale, Palo Alto, and Menlo Park. The fee levels in Cupertino are significantly lower than the fees in these other jurisdictions. KMA notes that most of the cities are in the process of examining and updating their fees. Mountain View's City Council voted in December to increase its fees to $25 per square foot for office and industrial space, while keeping the fee for retail and hotel unchanged at $2.47. In Sunnyvale, the City Council directed staff to draft an ordinance requiring $15.00 per square foot for office/industrial and $7.50 on retail and lodging. Palo Alto's current fee is $19.31 per square foot, and an update is in process. Menlo Park's current fees are $14.92 for Office/R&D and $8.10 for all other commercial development; its fees are also in the process of being updated. The jurisdictions with the highest fees tend to be in areas with very strong demand for non-residential space, such as Palo Alto, Menlo Park and Mountain View.

The cities of Fremont and San Jose do not have affordable housing fees on non-residential development at this time.

Exhibit 14: Non-Residential Housing Impact Fees in Other Jurisdictions	
City	*Impact Fee*
Cupertino	$6.00 psf
Menlo Park	$15.19 psf Office, R&D; $8.24 psf all other commercial and industrial
San Jose	None
Mountain View	Office/ Industrial $25.00 psf; $2.60 psf Retail, Hotel; no increase approved.
Sunnyvale	$9.74 psf Office, Industrial; Council considering $15 psf for Office, Industrial and $7.50 psf Retail, Hotel.
Palo Alto	$19.31 psf
Fremont	None

See Table 4 for more details.

3. Total Development Costs

KMA estimated the total development cost associated with each building type and examined fee levels in the context of total costs. This facilitates an evaluation of whether the amount is likely to affect development decisions. Six non-residential prototype projects were selected for review of total development costs. The prototypes include two Commercial / Retail / Restaurant projects, two Office projects and two Hotels. The cost estimates were prepared based on local information and our firm's extensive work with real estate projects throughout Silicon Valley and the Bay Area. More detail on the analysis can be found in the Non-Residential Jobs-Housing Analysis report. The results are summarized below in Exhibit 15.

Exhibit 15: Total Development Costs	
Land Use	*Cost*
Office/ R&D/ Industrial	$400-$550 per sq.ft.
Hotel	$400-$500 per sq.ft.
Commercial/ Retail / Restaurant.	$400-$650 per sq.ft.

One useful way to evaluate alternative fee levels is to examine them as a percent of total development costs. For example, at 3% or 5% of costs, we would see the following fee ranges:

Exhibit 16: Fees as Percent of Total Development Costs		
Land Use	*3%*	*5%*
Office/ R&D/ Industrial	$12 - $16.50 psf	$20 - $27.50 psf
Hotel	$12 - $15 psf	$20 - $25 psf
Commercial / Retail / Restaurant	$12 - $19.50 psf	$20 - $32.50 psf

4. Market Strength

KMA assembled information on the real estate market for non-residential space in Cupertino. Our findings are summarized below. More detail can be found in the Non-Residential Jobs-Housing Analysis report. The demand for non-residential space in Cupertino is very strong, predominantly driven by Cupertino's position as a center of employment for the high-tech industry, obviously dominated by Apple. Very low vacancy rates and high asking rents are indications of a tight market. High land costs and significant activity in the development pipeline also indicate a healthy market. This is particularly true for office development. The market for hotel, retail & restaurant space is viewed as less strong although there are recent signs of strength in all uses, including several new hotels in the development pipeline. A housing impact fee at any moderate level will not alter these conditions, in our opinion.

5. Recommended Fee Levels for Non-Residential

Given the maximums established by the nexus analysis, the strength of Cupertino's office, retail and hotel markets, and the fees in neighboring jurisdictions, KMA recommends an affordable housing impact fee in the range of $20.00 to $30.00 per square foot for office and industrial space and $10.00 to $15.00 per square foot for commercial, retail, restaurant and hotel space. Exhibit 17 presents the recommended range.

Exhibit 17: KMA Recommended Fee Levels	
Land Use	*Recommended Fee*
Office/ R&D/ Industrial	$20.00 to $30.00 psf
Hotel	$10.00 to $15.00 psf
Retail / Restaurant.	$10.00 to $15.00 psf

TABLE 1
COMPARISON OF BELOW MARKET RATE HOUSING PROGRAMS
CITY OF CUPERTINO, CA

	Cupertino	San Jose	Mountain View	Sunnyvale	Fremont	Palo Alto
Year Adopted / Updated	Est. 1993; update in process.	Est. 2010; inclusionary program suspended. Rental Fee 2014	Est. 1999; Rental Impact Fee in 2012; update in process	update in process	Nexus-based program est. in 2002; updated March 2015; full phase-in July 2017	Est. 1974; nexus analysis in process.
Residential Nexus?	In Process	For rental.	Yes.	Completed in 2012.	Yes.	In Process
Minimum Project Size						
For Fee Obligation	1 unit	1 unit	FS: 3 units R: 5 units Mixed: 6 units	8 units	2 units	5 units
For Build Requirement	7 units	n/a	10 units	20 units[1]	No build req.	5 units
For Sale Onsite Requirement						
Percent of Units	15%	Suspended.	10%	12.5%	Attached 3.5% plus $18.50 psf Detached 4.5% plus $17.50 psf	Base: 15% 20% if site > 5 acres 25% if loss of rentals
Income Level (% AMI)	1/2 @ 80-100% AMI 1/2 @ 100 - 120% AMI		80% - 100% AMI	Up to 120% AMI	Moderate: 80-110% (120% w/approval)*	Base: 10% @ 80-100% 5% @ 100-120%
Rental Onsite Option?	As alternative to fee.	No.	As alternative to fee.	In Process	No.	In Process
Impact / In-Lieu Fee	$3 psf	R: $17 psf Downtown highrises exempted for 5 years.	FS: 3% of sales price R: $17 psf	FS: 7% of sales price R: $17 psf.	**FS:** *Attached* $18.50 w. aff units; $27.00 no units *Detached* $17.50 w aff units $26.00 no units **R:** $17.50 no map; $27.00 w map	FS: 7.5% of sales price 10% of sales price is site > 5 acres 12.5% of sales price if loss of rental units
Fractional Units	<1 unit owed: pay fee >1 unit owed: round	n/a	pay fee or provide unit	pay fee or provide unit	pay fee or provide unit	pay fee or provide unit
Alternatives to Onsite Provision						
Fee Option	6 or Fewer Units	n/a	9 or Fewer Units	yes	yes	if infeasible onsite or offsite (w City approval)
Land Dedication (w City approval)	yes		no	no	yes	yes
Offsite (w city approval)	yes		no	yes	yes	yes
Other (W City approval)				Purchase existing units and convert to affordable. Preserve & rehab expiring units.	Purchase existing units and convert to affordable. Preserve at-risk units.	Rehab units.
Design of Inclusionary Units						
Smaller Units	not specified	n/a	no	yes	no	no
Lesser Interior Finishes	yes		no	no	yes	yes (FS only)
Other Design Standards	not specified				May be attached units; may be single story.	
Other Concessions	Fee waivers - park dedication and construction tax.	Downtown highrises exempted for 5 years.				

1. Not specified in Ordinance, but City documents indicate that projects with fewer than 20 units are eligible to pay fee.
Note: This chart presents an overview and terms have been simplified. Consult code and City staff for more information.
Abbreviations: R = Rental FS = For Sale PSF = Per Square Foot NSF = Net Square Feet

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TABLE 2
Cost of Onsite Compliance - Ownership Units
City of Cupertino

		Prototype 3 Small Lot Single Family / Townhome		Prototype 4 Condominium	
Gross Unit Size		1,850 sq ft		1,500 sq ft	
Number of Bedrooms		3		2.5	
Market Rate		***Per SF***	***Per Unit***	***Per SF***	***Per Unit***
Sales Prices[1]			$1,110,000		$800,000
Affordable Prices [2]			***Per Unit***		***Per Unit***
Moderate Sales Price			$410,000		$385,000
Median Sales Price			$270,000		$255,000
Affordability Gap [3]			***Per Unit***		***Per Unit***
Per Affordable Unit at Moderate			$700,000		$415,000
Per Affordable Unit at Median			$840,000		$545,000
Cost of Onsite Compliance		***Per SF***	***Per Unit***	***Per SF***	***Per Unit***
Inclusionary Percentage @ 15%	7.5% mod and 7.5% med	$62	$115,500	$48	$72,000
Inclusionary Percentage @ 20%	10% mod and 10% med	$83	$154,000	$64	$96,000

Note: Onsite compliance for single family units is not calculated because all ownership BMR units in Cupertino are condominiums and townhomes. The cost of onsite compliance for the single family units would be higher than the figures shown here.

1. See Residential Below Market Rate Housing Nexus Study Table 1.
2. Calculated by the City of Cupertino.
3. The difference between the market rate sales prices and the restricted affordable price.

TABLE 3
Cost of Onsite Compliance: Rental Units
City of Cupertino

		Prototype 5 Lower Density Rental Apartments		Prototype 6 Higher Density Rental Apartments	
1	Gross Unit Size	1,250 sq ft		1,250 sq ft	
2	Number of Bedrooms	2		2	
3	Household Size	3		3	
	Market Rate	***Per Unit***		***Per Unit***	
4	Rent per month	$3,250		$4,000	
5	Annual Rent	$39,000		$48,000	
6	Household Income	$130,000		$160,000	
7	Annual Operating Expenses[4]	($10,000)		($11,600)	
8	Annual Net Operating Income (NOI)	$29,000		$36,400	
9	Unit Value @ 6.0% Cap	$483,000		$607,000	
	Affordable Income & Rents	***Low Income***	***Very Low***	***Low Income***	***Very Low***
10	HH Income Limit [1]	$76,400	$47,750	$76,400	$47,750
11	Gross Rent [2]	$1,350	$1,120	$1,350	$1,120
12	(Less Utility Allowance)[3]	($62)	($62)	($62)	($62)
13	Net Rent	$1,288	$1,058	$1,288	$1,058
14	Annual Rent	$15,456	$12,696	$15,456	$12,696
15	Annual Operating Expenses[4]	($10,000)	($10,000)	($11,600)	($11,600)
16	Annual Net Operating Income (NOI)	$5,456	$2,696	$3,856	$1,096
17	Unit value @ 7.5% Cap	$72,747	$35,947	$51,413	$14,613
18	Gap in Unit Value	$410,253	$447,053	$555,587	$592,387
19	Cost of Onsite Requirement Per:	1%	1%	1%	1%
20	Per market rate unit	$4,103	$4,471	$5,556	$5,924
21	Per square foot	$3.28	$3.58	$4.44	$4.74
	Onsite Cost Equivalents, Prior Onsite Requirement @ 15%				
	6% Low, 9% Very Low — Per Unit	$64,850		$86,650	
	Per square foot	$51.88		$69.32	

1. California Department of Housing & Community Development, 2014.
2. City of Cupertino estimates.
3. Estimate based on figures published by Santa Clara Housing Authority. Assumes tenant pays for heat, cooking, electricity and hot water.
4. Assumes $4,000 in annual operating expenses plus property taxes estimated at 1.25% of market rate unit value.

TABLE 4
COMPARISON OF NON RESIDENTIAL HOUSING FEE PROGRAMS
CITY OF CUPERTINO, CA

Jurisdiction	Yr. Adopted /Updated	Current Fee Levels per SF	Thresholds & Exemptions	Build Option/ Other	Market Strength	Comments
City of Cupertino	1993; update in process.	• Office/Industrial/Hotel/Retail/ R&D: $6.00 • Planned Industrial Park Zones: $3.00	No minimum threshold.	N/A	Very Substantial	Fee is adjusted annually based on CPI.
City of Palo Alto	1984 Updated in March 2002 Update in process.	• Nonresidential Development $19.31	Churches; colleges and universities; commercial recreation; hospitals, convalescent facilities; private clubs, lodges, fraternal organizations, private educational facilities, day care and nursery school, public facilities are exempt	Yes	Very Substantial	Fee is adjusted annually based on CPI.
City of Menlo Park	1998 Update in process.	• Office & R&D $14.92 • All other commercial and industrial $8.10.	10,000 gross SF threshold Churches, private clubs, lodges, fraternal orgs, public facilities and projects with few or no employees are exempt.	Yes, preferred. May provide housing on- or off-site.	Very Substantial	Fee is adjusted annually based on CPI.
City of Sunnyvale	1984 Updated in 2003. Late 2014 Update.	• Industrial & Office $9.74 • On December 9, Council directed staff to draft ordinance w/ $15.00 psf for office/ind and $7.50 retail/hotel. No further action as of 2/28/15.	Applies only to the portion of the project that is in excess of allowable FAR (typically 0.35:1).	N/A	Very Substantial	Fee is adjusted annually based on CPI.
City of Mountain View	2002; Late 2014 Update.	• Office/High Tech/Industrial $25.00 • Hotel/Retail/Entertainment $2.60	Fee is 50% on building area under thresholds: Office <10,000 SF Hotel <25,000 SF Retail <25,000 SF	Yes	Very Substantial	Fee is adjusted annually based on CPI.
City of Fremont	None	None	None	None	NA	None
City of San Jose	None	None	None	None	NA	None

Note: This chart has been assembled to present an overview, and as a result, terms are simplified. For use other than general comparison, please consult the code and staff of the jurisdiction.

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