



CITY COUNCIL STAFF REPORT

MEETING DATE: October 17, 2018

PREPARED BY: John Lang, Economic Development Manager
APPROVED BY: City Manager

APPROVE AN IMPACT FEE FREEZE AGREEMENT WITH BRIDGE GROUP INVESTMENTS FOR INDUSTRIAL DEVELOPMENT ON 7.9 ACRES LOCATED ON JARVIS DRIVE IDENTIFIED BY ASSESSOR PARCEL NUMBER 726-30-013.

RECOMMENDATION(S)

1. Approve an Impact Fee Freeze Agreement with Bridge Group Investments, LLC. for the development of a 503,000 square foot corporate office/warehouse facility located on Jarvis Drive; and
2. Authorize the City Manager to execute the Impact Fee Freeze Agreement.

COUNCIL PRIORITIES, GOALS & STRATEGIES

Ongoing Priorities

Maintaining Infrastructure

2020-2021 Strategic Priorities

Economic Development

Financial Sustainability

GUIDING DOCUMENTS

Economic Blueprint

REPORT NARRATIVE:

When the Economic Blueprint was adopted in May 2017, it identified four key industry segments of focus including Innovation and Advanced Manufacturing, Retail, Tourism and Healthcare. The Economic Development team continues to receive a great deal of interest from businesses exploring relocation and expansion in Morgan Hill. With limited vacancies in the City's industrial areas, there is renewed interest in new construction in Morgan Hill. Frequently impact fees associated with new development is a key part of a decision to build in Morgan Hill. A key Morgan Hill fiscal strategy includes collecting impact fees to finance critical community infrastructure to accommodate new development as the City grows. While the need to collect Development Impact fees is necessary, it can also be a deterrent to those businesses which the City has targeted.

A City commissioned study prepared by Strategic Economics compared development impact fees between the cities of San Jose, Morgan Hill and Gilroy using three sample prototype projects. The study analyzed a prototype for a hotel development, new automobile dealership and manufacturing/R&D development project. While impact fees are not comparable from city to city because each municipality is solving for different infrastructure needs, the results of the study found that the City of Morgan Hill's development impact fees were higher for both the advanced manufacturing/R&D

development prototype and the automobile dealership project, making the City of Morgan Hill less competitive in two out of the three prototype areas. However, the City of Morgan Hill's Auto Dealer Strategy, which provides a mechanism to offset impact fees through a sales tax rebate, makes Morgan Hill more competitive than Gilroy and San Jose for automobile dealers.

To create consistency in the cost of development, the Economic Blueprint recommends policy and programmatic changes the City should employ to encourage investment in Morgan Hill. The first public policy recommendation formalized from the Economic Blueprint recommendations was approved on June 21, 2017, when the City Council adopted the Development Impact Fee Freeze Program that locks in Fiscal Year (FY) 2016-17 Development Impact Fees for a period of three years for new commercial/industrial development projects that enter into a Development Agreement approved by City Council. On February 21, 2018, City Council amended the Development Impact Fee Freeze Program to require an Impact Fee Freeze Agreement instead of a Development Agreement, to lock impact fees.

Bridge Group Investments, LLC., also known as Shoe Palace Corporation, is a family owned business specializing in footwear and athletic apparel that has strong roots in Santa Clara County. The business started in 1993 with a single retail store in West San Jose and has grown to 100 retail stores throughout the United States. Shoe Palace purchased 38 acres of land and relocated their corporate headquarters and distribution warehouse to Morgan Hill in 2013. They occupied the former 258,000 square foot Abbot Laboratory building at 755 Jarvis Drive. Shoe Palace owns 7.9 acres of vacant land adjacent to their current facility on which they are proposing to develop a 503,000 square foot warehouse/office facility (SR 2018-013). They anticipate submitting building plans once their site review has been approved.

The existing Shoe Palace operation currently has approximately 200 personnel on site Monday through Friday generally between 6 AM to 11 PM. The new facility will result in an additional 100 personnel bringing the total projected personnel to 300.

To create certainty for Bridge Group Investments LLC, staff is recommending the City Council approve an Impact Fee Freeze Agreement for the construction of the new warehouse/office building for Shoe Palace Corporation. The Impact Fee Freeze Agreement will utilize the FY 2016-17 development impact fee schedule through June 30, 2020. The developer will have until June 30, 2020 to apply for, and receive building permits, to benefit from the impact fee freeze. The estimated development impact fees using the Fee Schedule for FY 2016-17 are \$2.17 million.

Once operational, it is estimated the new warehouse/office will generate \$52,000 in direct on-going property tax (\$43,000) and sales tax (\$9,000) revenue to the City's General Fund. Additionally, staff estimates the City will receive one-time construction benefit in the form of sales tax of about \$103,000. If the Developer applies for building permits before July 2019, the benefit received to the developer from the impact freeze is \$89,000. If the developer applies for building permits after July 2019, but before July

2020, the benefit of the impact freeze is estimated at \$181,000. While the developer receives cost savings for each year the project is deferred, it is very likely that the cost of construction will continue to escalate in the coming years and therefore continued delays on building permit submittal will likely cost the developer more than the savings received from an impact fee freeze.

Impact Fee Benefit to Developer

Year		2018	2019*
Impact Fee Schedule	2016/2017	2018/2019	2019/2020*
Impact Fee Estimate	\$2,169,000	\$2,258,000	\$2,350,000
Potential Savings to Development		(\$89,000)	(\$181,000)

*Estimated with an escalation of 4.1% per year

COMMUNITY ENGAGEMENT: Inform

Approving a Fee Freeze Agreement with Bridge Group Investments, LLC is consistent with the Impact Fee Freeze Program and aligns with the Economic Blueprint Strategy #3 “Attract New Development,” Action #5, “Explore Incentive Programs to Attract Industry Specific Development.”

ALTERNATIVE ACTIONS:

The City of Morgan Hill could choose to not enter into a Fee Freeze Agreement with Shoe Palace Corporation to freeze impact fees. This option saves the City \$89,000 in forgone impact fee revenue.

PRIOR CITY COUNCIL AND COMMISSION ACTIONS:

On June 7, 2017, a Development Agreement with an impact fee freeze was approved for DivcoWest to stimulate new commercial/industrial development for that specific property.

On June 21, 2017 City Council approved the Citywide Impact Fee Freeze Program establishing FY 2016-17 Development Impact Fees as the basis for the three-year term for any new commercial/industrial development project that enters into a Development Agreement for an Impact Fee Freeze approved by City Council.

On February 21, 2018 City Council made a minor adjustment to the Impact Fee Freeze program by changing the agreement structure to an Impact Fee Freeze Agreement from a Development Agreement.

FISCAL AND RESOURCE IMPACT:

The potential loss of impact fee revenue to the City from entering into this Impact Fee Freeze Agreement is expected to range between \$89,000 and \$181,000. On the opposite, the City expects to receive one-time construction benefit, in the form of sales tax, of about \$103,000. Once operational, the City will receive an ongoing benefit of approximately \$52,000 in direct property and sales tax revenue to the City’s General Fund.

CEQA (California Environmental Quality Act):

An Environmental Impact Report (EIR) for the Morgan Hill 2035 Project, which included the General Plan Update, was prepared in accordance with the California Environmental Quality Act (CEQA) and certified by the Morgan Hill City Council on July 27, 2016. Commercial and industrial development as discussed above is consistent with the general plan policies for which the EIR was certified. There is no substantial evidence that freezing impact fees will have a significant effect on the environment beyond that already analyzed in the certified EIR; therefore, no further environmental analysis is required.

Any project specific development that occurs in the future will undergo an independent analysis pursuant to the requirements of CEQA.

LINKS/ATTACHMENTS:

1. Impact Fee Freeze Agreement- Bridge Group Investments
2. Exhibit B: FY 16-17 Fee Schedule