SENATE COMMITTEE ON HOUSING
Senator Nancy Skinner, Chair
2023 - 2024 Regular

Bill No: AB 2488 **Hearing Date:** 7/2/2024
Author: Ting
Version: 4/18/2024
Urgency: No **Fiscal:** No
Consultant: Hank Brady

SUBJECT: Downtown revitalization and economic recovery financing districts: City and County of San Francisco.

DIGEST: This bill allows the City and County of San Francisco (SF) to create a Downtown Revitalization and Economic Recovery Financing District (district) to finance office-to-residential conversion projects using incremental property tax revenues.

ANALYSIS:

Existing law:

1) Authorizes local governments to create enhanced infrastructure financing districts (EIFDs) and to use tax increment financing to finance public capital facilities or other specified projects, as specified.

2) Authorizes local governments to establish community revitalization infrastructure authorities (CRIAs) to use property tax increment revenues to finance a community revitalization plan within a community revitalization area, as specified.

3) Authorizes local governments to create Affordable Housing Authorities (AHAs) to provide low- and moderate-income housing and affordable housing, defined as housing affordable to households with incomes at or below 120% of area median income (AMI).

This bill:

1) Allows SF to create a district to finance office-to-residential conversion projects with incremental tax revenues (also referred to as tax increment financing or TIF) generated by office-to-residential conversion projects and outlines the

districts: formation process, governance structure, powers, financing plan, payment mechanics, affordability requirements, labor standards, and accountability measures.

Formation process

2) Allows the SF Board of Supervisors to form a district by adopting a resolution that:

   a) States the intent to form a district.
   b) Describe the district's boundaries, which must be contiguous with the boundaries of SF.
   c) States the need for, and the goals of, the district.
   d) States the district will use incremental property tax revenue to finance these activities.
   e) Fixes a time and place for a public hearing on the proposal.

Governance structure

3) Requires that when the Board of Supervisors establishes the district, it must also form a district board at the same time with three members of the Board of Supervisors and two members of the public chosen by the Board of Supervisors. Additionally, the Board of Supervisors may appoint one supervisor to serve as an alternate who can vote in place of another member who is absent or disqualifies themselves from participating in the meeting. Members cannot receive compensation, but they can be reimbursed for actual and necessary expenses.

District powers

4) Allows the district to use incremental property tax revenues generated by office-to-residential conversion projects that opt into the district.

5) Allows the district to only finance office-to-residential conversion projects the district determines are of communitywide significance and provide significant benefits to the district or SF.

Financing plan

6) Requires the district to create a financing plan it must approve at a public hearing. The plan must comply with specified conditions and outline certain

actions the district will take. The conditions and actions outlined in the bill include obligations that the financing plan:

a) Include a map and legal description of the proposed district.
b) Describe the potential office-to-residential conversion projects in the district, including those the private sector provides, governmental entities provide without funding from the district, public improvements that would receive financing from the district, and those provided jointly. Eligible projects can be mixed-use, but must dedicate at least two-thirds of the square footage for residential use.
c) Require each project that includes nonresidential development to develop residential and nonresidential portions of the development concurrently, as specified.
d) Identify each existing commercial office building within the district that is eligible for conversion to residential use and that may opt in to receive incremental tax revenue.
e) Require the incremental tax revenues generated by each individual office-to-residential conversion project be allocated back to that project to finance the debt service of the project.
f) Require that any incremental tax revenues remaining after allocating funds to the project must go to support downtown revitalization. After allocations have ceased, the tax increment returns to SF.
g) Specify the maximum portion of the incremental tax revenue proposed for the district for each year.
h) Include a date when the district ceases to exist no more than 45 years from the date the district allocates funding to the first project. If the district is divided into project areas, each project area can have its own time limit, which cannot exceed 45 years from when the district receives $100,000 in increment from that area.
i) Analyze the cost to SF to provide facilities and services to the area of the district before and after its development, which must include analysis of the tax, fee, charge, and other revenues SF expects to receive in the area of the district.
j) Analyze the projected fiscal impact of the district on SF.
k) Require, if a project proposes to remove or demolish any residential units, a plan to protect or replace those units, and relocate residents consistent with existing law.
l) Include the goals the district proposes to achieve for each project.
m) Prohibit the district from receiving property tax increment that would go to other taxing entities.

Payment mechanics

7) Provides that projects cannot opt in after December 31, 2032. After a project opts in, the district must establish the base assessed value for the property using the last assessment roll equalized prior to the issuance of the first building permit for the project. The district must pay SF for the costs of calculating property tax revenue amounts.

8) Provides direction on how to calculate the portion of property tax revenue that goes to the district, requires the district to place revenue in a special fund, and prohibits it from receiving revenue from other taxing entities.

Affordability Requirements

9) Provides that no affordability requirements apply to the first three million square feet of opted-in office to residential conversion projects.

10) After the first three million square feet are developed projects must comply with one of the following affordability requirements:

   a) At least 5% of total units for rent are affordable to very low-income households or the local inclusionary requirement, whichever is higher.
   b) At least 10% of total units for rent are affordable to lower- income households or the local inclusionary requirement whichever is higher.
   c) At least 10% of total units for sale are affordable to moderate-income households, or the local inclusionary requirement, whichever is higher.

Labor Standards

11) Expresses intent for the bill to be amended to specify minimum labor standards

Accountability measures

12) Requires the district to submit an annual report to the relevant committees of the Legislature on the projects the district finances if the Board of Supervisors creates a district.

COMMENTS:

1) *Author's statement*. "In the aftermath of the COVID-19 pandemic, many cities are struggling to adjust to decreased foot traffic in their once-thriving downtowns. Fewer people in city centers results in struggling small businesses, declines in transit ridership, and record-breaking rates of empty office buildings. San Francisco has an estimated 32-34% office vacancy rate and tens of millions of square feet of vacant office space. AB 2488 gives the city a new tool to adapt to the post-pandemic normal by allowing them to create a district to help finance the conversion of empty office buildings into new homes. This will solve two problems for San Francisco; it will provide the food traffic and transit ridership needed to spur economic recovery downtown while also reducing the impacts of the housing crisis. AB 2488 will empower San Francisco to turn empty office buildings and a struggling downtown into vibrant, walkable, mixed-use community with exciting new cultural, social, and economic opportunities."

2) *SF Downtown.* Before the pandemic, SF estimated 470,000 people commuted to SF for work from other places. This not only filled now-vacant office space, but also spurred the creation of other businesses and generated considerable economic development. However, the shift of people working from home during and after the COVID-19 pandemic has decreased the need for office space. According to the City and County of SF"Office vacancy reached historically low levels in 2019. Then, the pandemic created a significant increase in office vacancy rates. From March 2020 to June 2021, office vacancy rates increased from 5% to 20% as offices adopted hybrid and fully remote reporting schedules. This suggests that with fewer employees physically reporting to work, many offices reduced the size of their office or let go of their office space entirely. By late 2022, the rate remained higher than it had been in decades, but the rate of increase had slowed."[1]

   According to data it updated on April 15, 2024, 32% of SF's office space is vacant. Other large cities have lower vacancy rates: New York 18%, Los Angeles 27%, Austin 23%, and Seattle 22%.

3) *Adaptive reuse.* Adaptive reuse is the process of converting an existing non-residential building to housing. The ability to adaptively reuse a building is highly dependent on the initially designed use. For example, uses such as warehouses and big box retail are not generally suitable to adaptive reuse,

[1] https://www.sf.gov/data/san-francisco-office-space-vacancy

because their tall ceilings, single stories, and rudimentary plumbing would need to be completely redone to be appropriate for human habitation. Office buildings maintain some potential for conversion, because their multi-floor layout is conducive to housing; however, the large configuration of most office buildings makes it difficult to provide the necessary light and air that is required for residential units. For these conversions to occur, they would also need to be financially beneficial to the property owner. Other commercial properties, like hotels and motels, are more conducive to adaptive reuse, since they already have separate residential units often with bathrooms.

4) *Tax increment financing (TIF).* According to Governor's Office of Planning and Research (OPR), TIF is a mechanism used to fund and finance public facilities and other improvements, often in infill locations where up-front investments are needed to enable real estate development.[2] TIF captures incremental growth in tax revenues (usually property tax, although other types of revenue can also be collected) above and beyond what taxing entities receive within a designated area. TIF revenues are typically used to pay back upfront costs or debt service for bonds issued to fund improvements such as infrastructure and other public facilities that are needed to facilitate private investment. Historically, TIF was a financing tool used by local redevelopment agencies (RDAs). While they were active, RDAs enjoyed broad powers and often played a role in encouraging infill and TOD. RDAs were also an important local source of funding for affordable housing, because state law required RDAs to set aside 20% of revenues for that purpose. RDAs were dissolved by the state in 2012, partly due to concerns about how TIF revenues were being used (*i.e.* not meeting their obligations to fund affordable housing).

5) *Alphabet soup: IFDs, EIFDs, IRFDs, CRIAs, AHAs, NIFTIs, and NIFTI-2s.* Since the dissolution of RDAs, the Legislature has created numerous new TIF tools to authorize local governments to raise revenues to finance local infrastructure. Below is a chart summarizing the various available TIF tools already available to local governments:

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[2] Office of Planning and Research. *Housing Financing Tools and Equitable, Location-Efficient Development in California: Report on the Use of Tax Increment Financing.* (December 29, 2020) https://www.opr.ca.gov/docs/20210203-TIF_Tools_Final_Report.pdf

TIFs + Enabling Legislation	Location Reqs	Rev Sources	Affordable Housing Reqs	Expenditures	Number Created
Infrastructure Financing Districts (IFD), SB 208 (Seymour, Chapter 1575, 1990)	None	Property tax increment	None	Capital improvements only, such as highways, transit, water systems, sewer projects, flood control, childcare facilities, libraries, parks, and solid waste	2
Enhanced Infrastructure Financing Districts (EIFD), SB 628 (Beall, Chapter 785, 2014)	None	Property tax increment, increment from property tax in-lieu of vehicle license fees	None	Purchase, construction, or improvement of real property; can be used for maintenance of public faclities, as specified	5
Infrastructure and Revitalization Financing District (IRFD), AB 229 (Perez, Chapter 775, 2014)	None	Property tax increment	None	Same as IFDs plus watershed lands, flood management, brownfield restoration and other environmental mitigation, purchase of real property, housing acquisition or construction, commercial acquisition or construction, and repayment transfer funds nto a military base reuse authority	0
Community Revitalization and Infrastructure Authority (CRIA), AB 2 (Alejo, Chapter 319, 2015)	Disadvantaged communities, as specified, or an area within a former military base, as specified.	Property tax increment, increment from property tax in-lieu of vehicle license fees	25% for affordable housing	Wide range of capital improvements within its boundaries	0
Affordable Housing Authorities, AB 1598 (Mullin, Chpater 764, 2017)	None	Property tax increment, increment from property tax in-lieu of vehicle license fees, sales and use tax increment	95% for increasing and preserving affordable housing, as specified.	Financing low- and moderate-income housing, including supportive and transitional housing.	0
Neighborhood Infill Finance and Transit Districts (NIFTI), AB 1568 (Bloom, Chapter 562, 2017)	Qualified infill site	Property tax increment, increment from property tax in-lieu of vehicle license fees, sales and use tax increment	20% of revenues for acquisition, rehabilitation or construction of affordable housing; 20% for all housing to be affordable	Wide range of capital improvements and affordable housing	0

Second Neighborhood Infill Finance and Transit Districts (NIFTI-2), SB 961 (Allen, Chapter 559, 2018)	Qualified infill site and within 1/2 mile of a major transit stop	Property tax increment, increment from property tax in-lieu of vehicle license fees, sales and use tax increment	40% of revenues must be spent on affordable housing; 50% of affordable housing funds for households below 60% AMI and 50% for households below 30% AMI		0

6) *OPR reports.* SB 961 (Allen, Chapter 559, Statutes of 2018) required OPR to, on or before January 1, 2021, complete a study and make recommendations on (1) the effectiveness of TIFs, (2) the relative advantages and disadvantages of different types of TIF tools, and (3) the impacts of extending NIFTI-2s to areas around bus stops, including segregated bus lanes. The first report identified several key limitations current TIF districts share:

   a) They have limited revenue potential to make district formation worthwhile.
   b) Unlike redevelopment where taxing entity participation was mandatory, current TIF districts rely on volunteer participation.
   c) They have limited powers compared to RDAs.
   d) Some technical challenges interfere with their development.

   The reports found that despite the multitude of TIF tools available for local agencies to choose from, only five EIFDs had been created by the end of 2020: Otay Mesa (San Diego County), Placentia (Orange County), La Verne (Los Angeles County), West Sacramento (Yolo County), and Sacramento (Sacramento County).[3] Of these five, only the Placentia and La Verne EIFDs will include County participation.

7) *It will work this time!* According to the sponsors, SF's record breaking commercial vacancy rate requires creative ways to save downtown from a 'doom loop' of economic decline. Supporters of the measure argue that owners of office space do not have sufficient capital to secure a loan to convert the office space into housing. They contend that making public funds available to these property owners (via TIF) will make office to residential conversions economically feasible. They argue that this bill will help replace lost foot traffic in the city center and will lessen the housing supply shortage in SF.

[3] The report points out that two IFDs were created, but these were created under unique circumstances prior to the end of redevelopment

As noted above, SF and other local governments already enjoy authority to fund housing developments through creation of various districts that can dedicate TIF to these projects (see Comment 5). While other TIF districts can finance housing projects, these measures typically prohibit using property tax increment on market rate units. In this bill, however, the developer keeps all of the property tax increment the project generates to build any type of housing or mixed-use project in return for converting empty office space into needed housing units. However for the first handful of conversions the district is authorized to finance there is no affordability requirement for these projects. After that point, projects must include affordable units. **Given that this bill deviates from existing precedent the author has agreed to add intent language clarifying that this allowance is a response to the uniquely acute commercial vacancy rates in Downtown SF**.

8) *Labor standards?* This bill was amended on March 18, 2024 to express the author's intent to require some form of labor standards to apply to projects funded by the bill. This bill has progressed through the three committees and was approved on the Assembly Floor with this same ambiguous language. On July 2, 2024 this Committee will be the last to review and vote on this bill, yet substantive language is not available for this Committee, or any previous committee to review. At the time this analysis was published, it was not clear when a compromise would be reached.

9) *Amendments.* Due to compressed committee referral deadlines, the author was unable to adopt author's amendments or accept amendments agreed to in Senate Local Government Committee before the bill could be heard in this Committee. Author's amendments, amendments agreed to in Local Government Committee, and amendments requested by this Committee must be adopted as Committee amendments. In summary, **the author has agreed to accept the following amendments:**

   a) **Clarify that SF can approve or deny a project that requests to opt in to the district.**
   b) **Allow SF to approve less than the entire amount of property tax increment.**
   c) **Require annual reports of the district.**
   d) **Strengthen the meeting and notice requirements for SF to create a district.**
   e) **Strengthen actions SF must take to demonstrate compliance with the bill.**

- **f) Clarify that a directly elected mayor can be selected to serve on the district's board**
- **g) Delete the requirement to include a description of potential office-to-residential conversion projects provided by the private sector or other governmental entities.**
- **h) Limit the bill to only allow SF to create a single district in downtown SF and remove reference to project areas.**
- **i) Define what benefits the project must include to be of communitywide significance.**
- **j) Clarify that allocations to a project cannot exceed the incremental revenues generated by the project and only includes the increment generated by residential use in the project.**
- **k) Reduce the threshold for when affordability requirements apply to projects to begin after the first 1.5 Million square feet are developed.**
- **l) Specify that authorizing public financing for market-rate developments under this bill is a temporary remedy necessary to address the acute crisis of commercial vacancy rates in the area of downtown SF identified in the bill.**
- **m) Make other technical and clarifying changes.**

10) *Opposition.* The State Association of County Auditors (SACA) are opposed to the bill and raise several issues. SACA is concerned that it is unclear how these newly created districts would overlap with RDA successor agencies that are still receiving tax increment. They also note concerns about overlap with other tax increment entities such as EIFDs.

11) *Incoming.* This bill was heard in the Local Government Committee where it as approved on June 26, 2024 on a 5-1 vote.

RELATED LEGISLATION:

AB 930 (Friedman, 2023) — allows local agencies to create Reinvestment in Infrastructure for a Sustainable and Equitable California (RISE) districts and provides these new districts various financing powers to finance sustainable infrastructure projects. *The measure is being heard at this same hearing.*

AB 3068 (Haney, 2024) — enacts the Office to Housing Conversion Act, which creates a streamlined, ministerial approval process for adaptive reuse projects and provides certain financial incentives for the adaptive reuse of existing buildings. *The measure is being heard at this same hearing.*

SB 1227 (Wiener) — would have created an alternate welfare exemption from property tax for housing available to those of moderate income in downtown SF, and enacts a CEQA exemption and allows CEQA streamlining for specific projects in the area. *The measure was held on the Senate Appropriations suspense file.*

FISCAL EFFECT: Appropriation: No Fiscal Com.: No Local: No

POSITIONS: (Communicated to the committee before noon on Wednesday, June 26, 2024.)

SUPPORT:

Mayor London Breed, City & County of San Francisco
Advance SF
Bay Area Council
Build Group
California Apartment Association
Emerald Fund
Forell Elsesser Engineers
Grow the Richmond
Housing Action Coalition
Northern Neighbors Sf
Progress Noe Valley
San Francisco Bay Area Planning and Urban Research Association (SPUR)
San Francisco Chamber of Commerce
San Francisco YIMBY
Southside Forward
Streets for People
Sylvan Development Group, LLC
TMG Partners
Urban Environmentalists
YIMBY Action

OPPOSITION:

State Association of County Auditors

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