



LEGISLATIVE ANALYST REPORT

To: Members of the Board of Supervisors
From: Andrew Murray, Office of the Legislative Analyst
Date: September 26, 2005
Re: **Feasibility of Housing Above Retail** (BOS File No. 051203) (OLA No. 050-05)

SUMMARY OF REQUESTED ACTION

The Board passed a motion introduced by Supervisor Dufty requesting that the Office of the Legislative Analyst research, analyze, and gather data on housing above retail. Particularly, how have other municipalities dealt with this issue, have other cities (including Seattle and Portland) offered incentives to encourage housing above retail, and have the incentives been successful?

EXECUTIVE SUMMARY

Given record residential sale prices, in many cases market forces alone are sufficient to promote housing development on virgin or vacant parcels. However, market forces have not alone incentivized the quick transformation in San Francisco of large, low intensity sites to those with housing. For this reason, groups advocating for housing are encouraging legislators to create incentives to encourage this redevelopment, particularly of sites currently occupied by large grocery stores with surface parking.

Portland, Seattle, and Vancouver have witnessed a number of mixed-use projects involving grocery stores and housing, a handful on redeveloped sites formerly occupied by grocery stores. City planners and developers indicated that this redevelopment was usually not due to particular incentives offered by the jurisdictions, but rather the right combination of market forces and development partners. Nonetheless, there are steps that jurisdictions can take to help encourage specific patterns of redevelopment.

BACKGROUND

According to Simon Alejandrino of local real estate and urban development consultancy Bay Area Economics, "Given the current market, developers are actively pursuing high-density residential development throughout the region if they can find a site." This is true in San Francisco, where residential dwellings, including mixed-use structures, are being built in almost every Neighborhood Commercial¹ district throughout the City. However, the absence of undeveloped parcels, along with uncertainty, length of the permit process, and neighborhood opposition², have nonetheless contributed

¹ Neighborhood Commercial districts are commercial centers where everyday goods and services are located within close proximity to residential neighborhoods. They often include uses such as professional and business offices, retail and service shops, child care, community facilities, financial institutions, and residential clusters.

² "Planning for Housing in San Francisco," City and County of San Francisco Planning Department

to a situation in which housing stock growth has not kept pace with population growth. For example, from 1990 to 2000, San Francisco's population increased by approximately 50,000 people, while the housing stock only increased by an amount sufficient to accommodate half that number.³ (For additional information, please refer to the Office of the Legislative Analyst's June 2003 report, "San Francisco Housing Development," www.sfgov.org/site/bdsupvrs_page.asp?id=17966)

In 2002, the San Francisco Planning Department released a Citywide Action Plan (CAP) that provided guidance on how to meet the City's need for jobs and housing. The plan noted that although there are few undeveloped parcels in the City appropriate for housing, there are significant opportunities to redevelop existing low intensity uses, such as grocery stores and strip shopping centers (in many cases containing substantial surface parking), to heighten intensity and incorporate housing. The department found that such low intensity sites occupied nearly 100 acres. Subsequent to these findings, in 2003 the San Francisco Planning and Urban Research Association (SPUR) issued an article noting that many of the buildings on these sites are reaching the end of their useful lives, having been constructed 20 – 40 years ago, and might soon need significant rebuilding.

The housing potential of these sites is considerable. The Planning Department estimates that 4,500 units could be created through the redevelopment of all large, underutilized sites in Neighborhood Commercial districts citywide, or 2,000 – 3,000 on sites currently occupied by grocery stores alone.⁴ Many of the sites are suitable and attractive for significant housing development, as they are located on transit corridors and their current low intensity with surface parking can be disruptive of the urban fabric of neighborhoods.

Despite this opportunity, zoning requirements that encourage housing development⁵, and market pressure for additional housing, few of these low-intensity sites are being redeveloped as mixed use. Some have recently been renovated but remain single use, single story. Also, a number of mixed use projects that include housing and grocery stores have recently been created, but most did not occur on sites formerly occupied by grocery stores or other viable retail uses.

A number of barriers hinder this redevelopment. It might simply not be profitable to redevelop the site if development costs are high and it requires closing a viable retail establishment for a long period during construction. Also, property owners, either as landlords or operators of the business on site, might not want to tackle the complexities of significantly altering the building or developing a mixed-use project. Most mixed-use projects are built on land that developers acquire with construction in mind. It is much less common for retailers that own the site to undertake complex development. Chain retailers, which many grocery stores are, particularly like familiar store prototypes, and are hesitant to experiment with new models.⁶ Also, large grocery stores are much more likely to own the land on which they are situated than are other and smaller retailers.

³ "Our Housing Crisis: The Developer's Perspective", San Francisco Planning and Urban Research Association, 2001

⁴ Joshua Switzky, City and County of San Francisco Planning Department

⁵ The City has multiple zoning districts that require housing to be built if non-residential uses are proposed. These include the Van Ness Special Use District, the Rincon Hill Downtown Residential District, and the Residential/Service Mixed Use District. The first two have a requirement of 6 square feet of housing for every 1 square foot of nonresidential use, and the latter has a requirement of 3:1.

⁶ Simon Alejandrino, Bay Area Economics

An additional barrier to this redevelopment is neighborhood opposition to high-density buildings, which can result in design limitations that make a project infeasible from the developer's perspective. This opposition is in part due to perceptions that high-density housing will create more traffic, less parking, school crowding, blocked views, and less open space.⁷ High-density housing projects are also often associated in the public mind with lower socioeconomic residents, who are suspected of being prone to less desirable activities.⁸ Partially as a result of neighborhood opposition, housing densities fell in San Francisco for homes built between 1995 and 1999 compared to pre-1995 housing stock.⁹ The market has also been a factor in lower densities – larger units are commanding a higher price per square foot than smaller units¹⁰, providing incentive to develop fewer, but larger, units for a given space. This is a recent phenomenon that might not last.

There has also been substantial opposition from neighbors, merchants, and local elected officials to new large retail uses. Chain retailers have been barred from some of the City's districts. Because every neighborhood needs a grocery store, and residents are familiar with and generally receptive to their presence, creating mixed use sites containing grocery stores as the retail component might be more acceptable than projects with other retail, particularly "big box" retail.

The SPUR report stated that "Seattle, Portland, and Vancouver have each seen a wave of new and rehabbed grocery stores developed in more urban mixed-use models. All of these cities have planning code controls that encourage and sometimes require a mixture of housing with commercial development. Fortunately, almost all of the mixed-use grocery store projects to date in Portland and Seattle have materialized due to strong initiative from the development community..."¹¹ Therefore, although these cities have incentives to promote mixed use development and redevelopment, it is not clear to what degree incentives provided to developers have resulted in redevelopment of low-intensity sites opposed to market forces alone.

INCENTIVES

Incentives can generally do two things to encourage development, reduce costs or increase potential revenues. Relaxing existing zoning and planning regulations can have both effects. Such relaxation (referred to as "incentive zoning") can address requirements of the building size, density, and location. By modifying requirements, jurisdictions can make the environment ripe for residential and mixed-use projects. Without relaxing requirements, developers could be incentivized through education, financial incentives, permit streamlining, and other mechanisms. Some are likely more acceptable than others to different stakeholder groups. Notably, municipal actions that signal that high-density mixed-use development is welcome reduce uncertainty, which equates to risk for developers and their financial

⁷ "Building Better Communities With Well-Planned Density: What Works, What Doesn't", National Multi Housing Council, 2002

⁸ "Building Better Communities With Well-Planned Density: What Works, What Doesn't", National Multi Housing Council, 2002

⁹ "Estimating the Housing Infill Capacity of the Bay Area", Working Paper, Juan Sandoval and John Landis, 2000

¹⁰ Kate Funk, Keyser Marston Associates

¹¹ "Large Retail Commercial Sites in San Francisco: Issues and Opportunities," San Francisco Planning and Urban Research Association, July 1, 2003

backers, and provide encouragement. Some incentives that could be used to promote the redevelopment of grocery sites include those described below.

Zoning Changes

- Allowable uses – zoning regulations dictate what uses are allowable in different districts “as-of-right” or with conditional approval (conditional use), which often involves a lengthy public hearing process. In cases where mixed-use development is conditional, changing it to as-of-right would simplify mixed-use project approval. Zoning to require mixed-use development would be a stronger approach, requiring the developer to demonstrate that mixed use is not feasible and obtain a variance for a single-use development. Note that the conditional use approval process is one of many levers in a project that involve public input. Others include design review and approval of CEQA findings. (Although approvals of CEQA findings are not intended to be forums for public input on design, they have served as such in some cases.) Note that in San Francisco there is no formal design review opportunity for public input for projects that do not require conditional use approval. If conditional use restrictions were lessened, an alternative public design review process would likely be desirable.
- Density allowances – relaxing the density restrictions (often expressed as maximum number of dwelling units per acre) of residential units. The State currently requires cities to grant higher densities to projects that contain a certain amount of affordable housing. Cities have also relaxed density restrictions in order to encourage the development of housing over retail.¹²
- Physical exemptions - relaxing building envelope restrictions (e.g., setbacks, height restrictions, lot coverage limits, rear yard requirements, and floor-area-ratio) allows a larger building on a site, which in turn allows more units. Changes to density and envelope restrictions can be addressed through overlay zoning or the creation of a special use district (SUD), which can cover neighborhoods or single, large lots.
- Parking and signage limitations – some cities impose restrictions, which can be relaxed, on the allowable amount of parking and size and design of signage, two issues of particular interest to retailers.
- Specific plans (also referred to as precise plans or area plans) – creating plans for specific subregions of a jurisdiction, the contents of which can be crafted to explicitly encourage certain types of development. The development of specific plans can signal the City’s desire to developers.
- Underlying zoning – an alternative to creating special use districts or floating overlays is changing the underlying zoning of districts.

¹² Paul Zykofsky, Local Government Commission

Other Incentives

- Analysis – requiring that developers analyze the feasibility of incorporating desirable elements, such as mixed use, into projects.
- Design guidelines - design guidelines dictate elements of a building’s design to clarify for developers and plan reviewers desirable characteristics. This helps to reduce the developer’s uncertainty regarding the design review process. Specific plans, discussed above, often include design guidelines. Note that in many cities design guidelines are non-binding and adhering to them does not guarantee design approval.
- Education – outreach to developers about underutilized sites signals a jurisdiction’s ambitions and can reduce uncertainty about project approval. Also, city planners can educate developers of the benefits of mixed use during project planning. Kate Funk of real estate advisory firm Keyser Marston Associates notes that “Many property owners are passive. Tinkering with economic incentives is not the biggest need; it’s education, awareness and changing perceptions about the obstacles, etc.” This presupposes that the community (i.e., elected officials, planning commission, and public) does, in fact, support mixed-use projects.
- Facilitation – cities can actively recruit developers for underutilized sites and otherwise attempt to shepherd projects. Even where mixed use is not required, staff can encourage projects to adopt mixed use.
- Financial incentives – rebating or reducing fees related to development or providing tax credits (such as property tax). Nonprofit developers already enjoy such fee reductions in some jurisdictions, including San Francisco.
- Permit/Process streamlining – relaxing hearing processes or requirements (including eliminating conditional use designations, discussed above). Streamlining can include setting a time limit on permit processing, prioritizing the review of certain types of projects, assigning staff to shepherd projects, and preparing environmental impact reports in advance for specific plans rather than on a per project basis.
- Redevelopment agency involvement - redevelopment agencies can contribute to the redevelopment of sites in numerous ways, from using urban renewal funds to offset project costs and close financing gaps to purchasing sites outright and overseeing redevelopment.

SPUR Proposal

A 2004 SPUR report¹³ proposed incentives that the City could employ to encourage the development of housing as part of the redevelopment of low intensity sites. The incentives included a number of those described above, such as increasing height limits, eliminating density restrictions, allowing greater

¹³ “Housing Above Retail: Creating Incentives For the Replacement of Single-Story Retail Sites with Mixed-Use Projects”, San Francisco Planning and Urban Research Association, 2004

parking, allowing flexibility in signage, removing the conditional use designation for mixed use development, and providing design guidelines. In addition, for redevelopments or renovations of low intensity sites that do not contain housing, applicants requesting a conditional use authorization would be required to indicate that they have studied in good faith a mixed-use development and concluded that such a project is not economically and/or architecturally feasible.

The City Attorney’s office is currently investigating whether mandating such a feasibility study, which might require that a nexus exists regarding housing near retail, is allowable.¹⁴ Even if allowable, there is reason to believe that implementing such a requirement might be challenging, as the City would have to determine what constituted a “good faith effort” and what recourse it would pursue of non-compliant developers. In a similar case, the City of Davis stopped requiring developers to complete a study when nonresidential land was proposed for conversion to residential use. The studies regularly concluded that nonresidential development was infeasible for the site, when in fact it was likely feasible, although not as profitable as residential development.¹⁵ The city had no means of contesting the findings. An alternative to requiring a study such as that SPUR proposes is identifying the general conditions under which the City thinks that mixed-use development makes sense and alerting developers to such.

OTHER JURISDICTIONS

As noted, the SPUR report indicated that Portland, Seattle, and Vancouver have seen a number of new and rehabilitated grocery stores developed as mixed use. In addition, they “have planning code controls that encourage and sometimes require a mixture of housing with commercial development.” As such, it would be informative to look at the experiences of these jurisdictions and determine the success of various incentives they offer. Table 1, below, summarizes these incentives.

Table 1. Incentives for High Density Mixed Use Redevelopment	
Jurisdiction	Incentives
Portland	<ul style="list-style-type: none"> - Substantial mixed use as-of-right - Parking not required for residential in mixed use - Use of urban renewal funds to support mixed-use projects - List of underutilized sites
Seattle	<ul style="list-style-type: none"> - Unlimited residential density for mixed-use buildings in commercial and mixed-use zones - Height bonus for multipurpose retail in mixed-use buildings - Possible relaxation of design requirements during design review - Possible change from a lot coverage basis to a floor-area-ratio (FAR) basis benefiting mixed-use projects
Vancouver	<ul style="list-style-type: none"> - Director of Planning discretion to approve conditional development applications - Occasional increased height and density allowances

Portland

Portland has created a development environment that encourages mixed-use. The city has designated a substantial amount of area for mixed use as-of-right. Parking is not required for residential components of mixed use developments, which reduces the project costs or allows the retail component to have

¹⁴ Ms. Funk believes that such a nexus exists

¹⁵ Katherine Hess, Community Development Administrator, City of Davis, CA

more parking, depending on the developer's preference. In specific instances, the city has used urban renewal funds to help developers close their financing gap for mixed-use site redevelopment. The Portland Development Commission (PDC) (the city's redevelopment agency) has funded or loaned funds for sidewalk enhancements, underground parking facilities, and affordable units on mixed-use redevelopment projects incorporating grocery retail.

According to Steve Dotterer, principal planner for policy of the Portland Bureau of Planning, the city actively encouraged redevelopment of some sites by creating and disseminating a list of lots that it considered underutilized, most of which were abandoned or badly maintained. The list was developed in cooperation with the community such that it was vetted to ensure general support for the redevelopment of the sites, even if it involved the creation of new multi-story buildings. The bad condition of the sites made neighbors more accepting of redevelopment.

As noted in the SPUR report, the city is home to a number of mixed-use developments that incorporate grocery stores and housing. Many are on sites not formerly occupied by a grocery, but some other low intensity use or an abandoned site, such as the well-known Belmont Dairy project created on the site of a defunct dairy. Mr. Dotterer noted that some of the grocery redevelopments planned at the time of the SPUR report have been cancelled or are still in the planning process. Only two were built on or near sites formerly occupied by grocery stores, neither of which appeared on the city's list of underutilized sites. In one case, the new facility was built on the surface parking lot while the old store remained active. In another case involving a Safeway store on a prime downtown lot adjacent to the art museum, the new facility was built on a nearby lot while the old store remained active.¹⁶ No special incentives were offered by the city in the former case. The latter case involved some incentives, described below.

According to Francesca Gambetti of Portland- and Seattle-based urban development firm Shields Oblatz Johnsen, which was instrumental in the redevelopment of the downtown Safeway and the Belmont Dairy, public grants and loans were key (the Safeway project received a 10-year property tax abatement and a \$3 M low-interest loan). However, the grants and loans were offered due to special circumstances of these projects not simply related to their mixed-use redevelopment nature, and would not likely be offered for less ambitious projects. For example, Belmont Dairy required cleaning a brownfield, and the downtown Safeway was part of the redevelopment of a prime three-block area that included substantial affordable housing.

Seattle

Seattle's land use code incentivizes mixed-use buildings by providing unlimited residential density for mixed-use buildings in commercial and mixed-use zones. It also encourages retail uses like grocery stores to be incorporated into such mixed-use developments by allowing buildings containing multipurpose retail uses (such as grocery stores) to have a seven foot height bonus in certain commercial zones (30 and 40 foot zones). However, certain provisions of the code implicitly discourage mixed-use

¹⁶ In this case, a single story Safeway occupied a parcel downtown, directly behind the city's art museum. A new multi-story, mixed-use development was built on a nearby lot occupied by low intensity uses (a single story office and other buildings).

housing development in commercial areas. For example, mixed-use buildings have restricted upper lot coverage (64%), whereas commercial buildings can cover the full lot.

Seattle has both citywide and neighborhood design guidelines. Almost all mixed-use projects are subject to design review relative to these standards. The land use code allows design requirements (except parking and height) to be relaxed during this review and approval process if it will result in a better project.

Seattle's city council is currently considering legislation (the Neighborhood Business District Strategy) crafted by the Department of Planning and Development that will address issues related to mixed-use development. One of the objectives of the strategy is to spur housing growth in neighborhood business districts. This involves a possible change in the regulation of the building envelope from a lot coverage basis to a floor-area-ratio (FAR) basis, under which mixed use projects might be allowed a greater FAR relative to other projects.

According to senior land use planner Kristian Kofoed, the city has experienced the development of a number of mixed-use buildings that incorporate grocery stores and housing. In one case, a non-grocery retail site was redeveloped into a grocery store and housing. Former grocery stores have only been redeveloped to mixed use in a few cases, including one in which a former Safeway store was rebuilt with housing above. Seattle did not offer any particular incentives to spur this project.

Vancouver

Vancouver is somewhat unique in that a Director of Planning has the authority to approve discretionary or conditional development applications (typically only rezoning applications go before City Council). This power and flexibility allows staff to review all aspects of built form including architecture, scale, landscaping, livability, and use. Therefore, opposed to San Francisco where public opposition might threaten high density or tall developments, in Vancouver such projects are more likely to secure approval.¹⁷

Although there has been substantial mixed-use redevelopment in commercial areas¹⁸, Vancouver offers few particular incentives for mixed-use redevelopment. According to Larry Beasley, co-director of planning for Vancouver, “the amount of money made on the redevelopment is so dramatic that we don’t

¹⁷ Opponents have recourse to the decisions of the Director of Planning, as all can be appealed to the Board of Variance, which hears and decides upon appeals regarding zoning, development permit, signage, parking, and other matters. The Board is independent of local elected officials and consists of five members, two appointed by the City, two by the Province, and a Chair, appointed by the other members. No appointed or elected city official may sit as a member. Official city committees or Council may provide information to the Board on particular appeals, but they cannot direct the Board on jurisdiction or whether an appeal should be granted or denied. Applications for permits for major projects are considered by the Development Permit Board, which is composed of the Director of Development Services, the Deputy City Manager, the General Manager of Engineering Services, and a Co-Director of Planning. The Board makes all final decisions but is advised in all deliberations by an Advisory Panel consisting of eight members appointed by Council. Two members represent the development industry, two are from the design profession and four are from the general public.

¹⁸ "Insights into Population and Housing", City of Vancouver Planning Department, 2002

need any public incentives to speak of.”¹⁹ The city does however promote high intensity mixed use where appropriate through increased density and occasional height increases.

Vancouver has a large percentage of low-density "single family" zoning (approximately 60%- 70%) which surrounds one of the densest core neighborhoods in North America. Density has been created either in areas specifically targeted for higher residential densities or areas along major streets where there has historically been a mix of apartments or offices above ground floor commercial uses (old "village" centers or commercial strips). Residents' familiarity with the historical high density of these neighborhoods likely results in lower levels of opposition to new high-density developments. "Over time, there really hasn't been a problem getting people to build density in Vancouver", according to city planner James Boldt. Also, Vancouver has only had a zoning bylaw since 1956, before which many mixed-use districts had already been established, and these uses were accommodated in the zoning code.

CONCLUSION

The findings of the Office of the Legislative Analyst confirm those of SPUR, that Portland, Seattle, and Vancouver have all seen a number of mixed-use projects incorporating grocery stores and housing, although few involved the redevelopment of existing grocery stores. As reported by SPUR, "almost all of the mixed-use grocery store projects to date in Portland and Seattle have materialized due to strong initiative from the development community."²⁰ As these cities do not offer incentives targeted specifically to this redevelopment opportunity, it is difficult to ascertain from their experience what impact incentives might have. If the redevelopment of grocery stores to mixed use is a priority in San Francisco, the City should investigate the affect of incentives, including those described above, and consider their implementation.

¹⁹ "City planners look north for mixed-use model," The Examiner, 7/5/2005, page 8

²⁰ "Large Retail Commercial Sites in San Francisco: Issues and Opportunities," San Francisco Planning and Urban Research Association, July 1, 2003