



# Memorandum

**TO:** HONORABLE MAYOR  
AND CITY COUNCIL

**FROM:** Kim Walesh

**SUBJECT:** SEE BELOW

**DATE:** December 11, 2017

Approved

*D. D. Syl*

Date

12/11/17

## INFORMATION

**SUBJECT: GROUND LEASE AGREEMENT WITH SILICON VALLEY CREATES FOR THE CREATIVE CENTER FOR THE ARTS ON THE FORMER CORPORATION YARD SITE IN JAPANTOWN**

Please see the attached draft City Council memorandum for a proposed Ground Lease Agreement with Silicon Valley Creates for the Creative Center for the Arts on the former corporation yard site in Japantown, pursuant to San Jose City Council adopted Resolution 77135. Resolution 77135 requires that a public hearing be conducted for any public subsidy over \$1,000,000 and that notice of such public hearing be posted on the City's web site 28 calendar days in advance of the City Council meeting at which a public subsidy is to be considered. This public subsidy will be considered at the January 9, 2018 City Council meeting.

/s/

KIM WALESH  
Deputy City Manager  
Director of Economic Development

For questions, please contact Nanci Klein, Assistant Director of Economic Development, at (408) 535-8184.



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**COUNCIL DISTRICT: #3**

**SUBJECT: GROUND LEASE AGREEMENT WITH SILICON VALLEY CREATES FOR THE CREATIVE CENTER FOR THE ARTS ON THE FORMER CORPORATION YARD SITE IN JAPANTOWN**

## RECOMMENDATION

1. Conduct a Public Hearing regarding an economic development subsidy in connection with a below-market Ground Lease Agreement for a privately-funded cultural and arts facility at the former Japantown Corporation Yard in the amount of \$5,769,920 over the 55-year term; and
2. Adopt a resolution approving a Ground Lease Agreement with Silicon Valley Creates, a non-profit organization, for a 0.75-acre, City-owned parcel (APN: 249-39-044) at the former Japantown Corporation Yard site (between Jackson Street and Taylor Street at N. 7th St.) for the construction and operation of the Creative Center for the Arts, for a term of 55 years and for an amount of \$1 per year.

## OUTCOME

City Council approval of this Ground Lease Agreement will allow Silicon Valley Creates (“SVCreates”) to develop, construct, and operate an approximately 55,000 square foot facility called the Creative Center for the Arts to support the local and regional arts community on the City’s 0.75-acre parcel at the former Japantown Corporation Yard. During the term, the City will continue to own title to the land, and SVCreates will own title to the improvements. At the end of the term, title to the improvements will be transferred to the City.

Aside from the public subsidy through use of the land, no financial assistance will be provided by the City to support the development, construction, or operation of the facility.

To provide context, similar facilities, such as the Mexican Heritage Plaza, were constructed with former Redevelopment Agency funds and receive ongoing financial support from the City's General Fund. The Mexican Heritage Plaza currently receives \$450,000 per year from the City for operations and maintenance.

## **BACKGROUND**

The Creative Center for the Arts ("CCA") has been an integral component of the longstanding Japantown Corporation Yard redevelopment vision, and the land in the proposed Ground Lease Agreement was negotiated specifically for this use.

On December 16, 2014, City Council approved a Purchase and Sale Agreement and Development Agreement with Jackson Taylor Partners LLC/Related Companies ("Related") for the sale of the former Corporation Yard in Japantown. A key element of the transaction included transferring *back* to the City (at no cost) a 0.75-acre parcel to be the home of the CCA. In April of 2017, Related completed the purchase of the property for \$18.5 million dollars, and re-conveyed the 0.75-acre parcel to the City.

The CCA is under development with the strong leadership of SVCcreates and three partner organizations that have committed to participate in the CCA as equity partners and anchor tenants: San Jose Taiko, the New Ballet School and CreaTV San Jose. Initial additional anchor tenants who have signed lease term sheets include: SJ Jazz, Los Lupenos, Empire 7 Gallery, Vivace Youth Chorus, Teatro Vision, Abhinaya Dance Co., Silicon Valley Shakespeare, and Red Ladder Theater Company.

Staff from SVCcreates and the City have worked collaboratively to complete a ground lease for the 0.75 acres, on which the approximately 55,000 square foot CCA will be constructed. The CCA will be home to the three listed anchor tenants and provide space for a wide range of nonprofit arts groups and creative professionals.

## **ANALYSIS**

### ***The Creative Center for the Arts***

The CCA is a new model for supporting the arts in the 21st century. The CCA will create a nexus of flexible services and spaces with both physical and virtual infrastructures. The CCA will be a sustainable hub of resources for the non-profit creative sector in San Jose and part of the growing national network of shared facilities.

The Silicon Valley region presents a unique set of challenges and opportunities for creatives and arts organizations that the CCA is designed to address. The Silicon Valley environment promotes innovation, collaboration, and diverse thinking. At the same time, the prosperity of the region

makes available facility space for creative pursuits and arts groups rare and costly. To survive arts groups must be innovative and lean with financial models and business management.

The CCA will become a focal point for arts services and creative practice by offering dynamic and innovative opportunities for resources and space for resident organizations, independent creatives and small cultural groups needing back office, studio, and rehearsal space. It will provide unifying and cost-saving solutions for participants by offering affordable operations such as finance, human resources, legal, marketing, procurement, and IT solutions. By representing a larger group of creative enterprises, CCA will improve buying power, reduce the overall burden of administration, and enhance the level of benefits and services for all.

The CCA will be owned by a member-governed LLC and managed by SVCCreates (as the managing member). It will provide below-market rental of rehearsal, studio, meeting room and office space to nonprofit arts organizations, independent artists, and for-profit creative and community groups throughout Santa Clara County. The initial anchor tenants include SVCCreates, San Jose Taiko, the New Ballet School and CreaTV. These core anchor tenants have each made a capital investment in the project and will have dedicated, custom-designed space in the building. Service to the wider arts and creative community will be provided through various types of leases, a membership model for flexible access to office space, meeting rooms, event space and shared services, and hourly/daily rentals for rehearsal space, event space and visual artist studios.

The goal of the CCA capital project is to provide a self-sustaining, mortgage free facility to serve the local cultural ecosystem. SVCCreates and the anchor tenants are engaged in a campaign to secure investment and grant funding to cover the costs of project planning and construction. In total SVCCreates seeks to raise approximately \$30 million through local and national grants, major gifts and through the use of programs such as the New Market Tax Credit Program.

To date, grant and equity funding includes the following:

- \$1 million from the Packard Foundation
- \$250,000 from the Hewlett Foundation
- \$360,000 from ArtPlace America
- \$1 million from SVCCreates
- \$1 million from CreaTV
- \$1 million from SJ Taiko
- Additional grants pending approval of the Ground Lease Agreement

### ***Ground Lease Agreement Terms***

City staff have negotiated a proposed 55-year Ground Lease Agreement, with terms further described below, that is intended to facilitate an iconic and innovative CCA to serve as a major hub of arts activity throughout Silicon Valley.

Aside from the public subsidy provided use of the land at below market rent, no financial assistance will be provided by the City to support the development, construction, or operation of the facility.

Outlined below are major terms and conditions of the proposed Ground Lease Agreement by and between the City of San Jose and SVCCreates for the Creative Center for the Arts. The Draft lease is attached to this memorandum for the Council's and the Public's review.

#### Net Lease/Utility Service

Typical in commercial real estate, a "net lease" requires the tenant to pay a portion or all of the taxes, fees and maintenance costs for the property in addition to rent. All costs incurred in the operation and maintenance of the Property, including utilities, shall be paid by the Lessee.

#### Term

Fifty-five years commencing on the Commencement Date and terminating on the 55th anniversary of the Commencement Date. The Commencement Date shall occur when the Lessee has satisfied certain conditions, which include a notice of completion of construction being filed with the County, and the first sub-lessee moving into the building. If the Commencement Date has not occurred within six years after the Effective Date, either party may terminate the Lease.

If either Party elects to terminate per lease specifications, the Lessee shall return the land to the City and convey any improvements on the land to the City.

Lessee agrees to make reasonable efforts to cause the construction of the Center to be commenced by June 1, 2019, but no later than four years after the Effective Date, and completed six years from the Effective Date.

Lessee may renew the lease for a period exceeding 55 years, but not exceeding 99 years total, upon satisfactory performance review by the City.

#### Below-Market Rent/Public Subsidy

Lessee shall pay \$1.00 per year for rental, use and occupancy of the property. Additional information pertaining to the public subsidy is provided in the section below entitled "Addendum #1."

#### Community Use

Lessee shall establish a rental structure that encourages activation while still covering the cost of event operation, and provide below-market rental space. Lessee shall provide space in the Center for up to two meetings or events per month to City, at no cost, upon reasonable notice and mutually agreeable dates.

### Condition of Property

Lessee agrees that the land is leased for use in its existing condition, as-is, with all faults, without warranty and without obligation on the part of the City to perform work to prepare the land for occupancy. Lessee shall bear the cost of remediating the hazardous material requirements as may be required.

### Maintenance of Property Lessee Obligations

Lessee shall keep the property in a neat and clean condition without cost to the City.

If the Lessee fails to maintain the Property or make repairs or replacements and if Lessee fails to cure same after ten days City may, but shall not be required to, enter the Property, and perform the maintenance or make the repairs.

### Indemnification and City Liability

Lessee, for and on behalf of its directors, officers, employees, and agents, covenants and hereby agrees to indemnify, defend, protect and hold harmless City, its officers, employees, contractors and agents, from and against any and all claims, demands, damages, obligations, liabilities, losses, costs, expenses, penalties, suits or judgments, at any time received, incurred or accrued by City parties or members of the public using the center or any other part of the Property arising out of or resulting in whole or in part from any act (or failure to act) of Lessee, its directors, officers, employees, contractors, subcontractors, agents, permittees or invitees, or which results from their noncompliance with any laws respecting the condition, use, occupation or safety of the property, or any part thereof, or which arises from the authorized activities hereunder or which arises from Lessee's failure to do anything required under the Ground Lease Agreement, except as may arise from the sole active negligence or the willful misconduct of City parties. City's right to full indemnity hereunder shall arise notwithstanding that principles of joint, several or concurrent liability or comparative negligence, might otherwise impose liability on City or City parties pursuant to statutes, ordinances, regulations or other laws. All of Lessee's obligations under Section 16.1 are intended to apply to the fullest extent permitted by law and shall survive the expiration or sooner termination of the Ground Lease Agreement. In an action or claim against City in which Lessee is defending City, City shall have the right to approve legal counsel providing City's defense.

### Insurance

At least ten business days prior to the commencement of construction of the Center or any Alterations and Improvements having a value in excess of \$25,000, Lessee or its contractor shall provide City with certificates of insurance acceptable to City, showing City as an additional insured party as to all insurance coverage provided by Lessee's contractor concerning work performed by Lessee's contractor on the Property. Insurance Coverage requirements include:

Commercial General Liability - \$1,000,000; Automobile Liability - \$1,000,000; Workers' Compensation and Employers' Liability - \$1,000,000; Professional Liability Errors & Omissions - \$1,000,000; Contractor's Pollution Liability Insurance - \$1,000,000.

#### City Obligations

City shall have no obligation to maintain the land or improvements.

#### No Right to Demolish

Lessee shall have no right to demolish the Center or any improvement once built unless Lessee shall have received the prior written consent of the City.

#### Utility Services

Lessee shall secure and directly pay for any electrical, gas, water, sewer, and telephone services to the Property.

#### Signs/Advertising

Lessee shall not install any sign or advertising or media on the Property without the prior written consent of the City. Any advertising or media shall be removed by Lessee at Lessee's sole cost and expense upon termination or expiration of the Agreement.

#### No Transfer without City Consent

Lessee shall not assign, sublease, convey or encumber or otherwise transfer this Agreement without the prior written consent of City, which may be withheld at City's sole and absolute discretion.

Upon City's reasonable approval of certain items detailed in the Lease, City shall consent to Lessee's assignment of the Agreement to an LLC titled, "Creative Center at Japantown Square, LLC," in which Lessee is the managing member with CreaTV San Jose and San Jose Taiko Group, and has and maintains a 51% or more interest in the LLC.

#### Termination of Agreement

An Event of Default shall occur in one of several possible ways:

Lessee shall have failed to pay rent, fees, charges, or obligation of Lessee requiring the payment of money under the terms of this Agreement within ten (10) days of the date same become due; Lessee shall have failed to commence construction of the Center within four (4) years of the Effective Date of the Agreement. Lessee shall have failed to maintain any insurance required

### **CITY AND STATE PUBLIC SUBSIDY DISCLOSURE REQUIREMENTS**

The proposed Ground Lease Agreement includes a public subsidy greater than \$1,000,000 over the term of the agreement. Please see the section below entitled "Addendum #1" with information addressing the requirements set forth in the City of San Jose's Resolution No. 77135 for publication of information related to an economic development subsidy of more than \$1,000,000. The second table in this section addresses the requirements set forth in the State of California AB 562 (Government Code 53083) for publication of information related to an economic development subsidy and a public hearing.

### **EVALUATION AND FOLLOW-UP**

City staff will continue to be involved with and oversee development, construction, and operations of the CCA. No further action is needed by City Council.

### **POLICY ALTERNATIVES**

#### ***Alternative #1: Do not enter into a Ground Lease Agreement with Silicon Valley Creates***

**Pros:** The owner/developer of the adjacent parcels at the former Japantown Corporation Yard has an option to purchase the City's 0.75-acre parcel for \$2,659,338 if the parcel is not developed within the 6-year option period. The proceeds of the sale would be deposited into the City's General Fund.

**Cons:** If purchased by the developer, the site would most likely be used for commercial activities that would not support or promote cultural and arts activities that *would* be supported by the proposed Lessee.

**Reason for not recommending:** The proposed Lessee will leverage private funding to construct and operate a facility that will support important arts-related activities and groups, and enhance the local and regional community, which otherwise may not be possible without significant public funding.

### **PUBLIC OUTREACH**

The redevelopment of the Japantown Corporation Yard has been contemplated since 2003. The community has been an active and engaged partner throughout the process. Approximately 109 community meetings have been held on the project over the years.

This memorandum will be posted on the City's website for the December 19, 2017, City Council agenda.



**COORDINATION**

This memorandum was coordinated with the City Attorney’s Office and City Manager’s Budget Office.

**COMMISSION RECOMMENDATION/INPUT**

No commission recommendation or input is associated with this action.

**FISCAL/POLICY ALIGNMENT**

This project aligns with the City’s Economic Strategy #12, “Develop a Distinctive Set of Sports, Arts, and Entertainment Offerings Aligned With San Jose’s Diverse, Growing Population.”

Benefits:

- Estimated one-time revenue to the City: \$1,576,896
  - Development/Permit Fees: \$76,821
  - Construction Taxes: \$1,500,075
- Free City use of the facility for two meetings or events each month for the term of the Agreement, valued at \$10,000 per year, or \$550,000 over the 55-year term
- At the end of the term of the Agreement, title to the 55,000 square foot building will be transferred to the City.
  - In today’s dollars, a 55-year-old building of a similar size (minus land value) in San Jose is valued at \$100-\$150 per square foot.
  - The value of the building to be transferred back to the City at the end of the term is estimated between \$5,500,000 and \$8,250,000

The table below addresses the requirements set forth in the City of San Jose’s Resolution No. 77135 for publication of information related to an economic development subsidy of more than \$1,000,000.

**ADDENDUM #1**

<b>i. Accountability</b>	If SVCcreates is unable to fund the construction of the CCA, is unable to meet the construction timeframes, or otherwise causes an event of default and fails to cure, the City may terminate the Agreement and regain control of the land, thereby ending the economic development subsidy.
<b>ii. Net Fiscal Impact</b>	The one-time revenue to the City generated by development and permit fees, and construction taxes, of the CCA is \$1,576,896. There are no tax revenues lost as a direct impact of the project.

<p><b>iii. Net Job Impact</b></p>	<p>The CCA project expects to create or retain the following jobs through its construction and operations. Note that jobs retained as a result of the CCA’s unique model supporting arts organizations through below-market rents, could otherwise be lost as a result of rising rents throughout the region.</p> <ul style="list-style-type: none"> <li>• Create 100 temporary FTE construction jobs with annual salaries greater than \$80,000</li> <li>• Create 10 new permanent FTE jobs among the major tenants with annual salaries of at least \$40,000 to \$60,000</li> <li>• Retain 62 permanent jobs among tenants through the provision of the below-market rents for office/rehearsal space in the CCA; Of the 62, 47 are full-time, and the remaining 15 are part-time</li> <li>• Retain 92 seasonal jobs among tenants for teaching artists and performers, which will be documented living wage jobs</li> <li>• San Jose’s Living Wage hourly rate is currently \$20.57 for jobs with health benefits, and \$21.82 without health benefits. These wages equate to \$42,785.60 and \$45,385.60 per year for full-time work.</li> <li>• For a 1-bedroom housing unit with 2-person occupancy, the Extremely Low Income threshold is \$28,650. For a 2-bedroom unit with 3-person occupancy, the Extremely Low income threshold is \$32,250.</li> <li>• Therefore, the Living Wage jobs created and retained by the project are not expected to increase demand for Extremely Low Income housing units.</li> </ul> <p>Finally, SVCCreates and its partners and tenants will make strong and documented efforts to fill all vacant positions locally, with first consideration of San Jose’s Japantown community (zip code 95112).</p>
<p><b>iv. Housing Impact</b></p>	<p>No housing units will be demolished as part of the project. This project is related to the adjacent mixed-use development “Japantown Square” that is expected to provide up to 600 new apartment units. No new demand for Extremely Low Income Housing units is expected to be generated by employees of this project.</p>
<p><b>v. Source of Funds</b></p>	<p>This project does not provide funds directly to the project, but does provide a below-market lease rate with an estimated value of \$5,769,920.</p>
<p><b>vi. Neighborhood Impacts</b></p>	<p>Environmental impacts of the project were identified and mitigated through the Addendum to the Japantown Corporation Yard Redevelopment Project Final Environmental Impact Report, Resolution No. 74384.</p>

The table below addresses the requirements set forth in the State of California AB 562 (Government Code 53083) for publication of information related to an economic development subsidy and a public hearing.

<p><b>i. Name/Address of Benefitting Business Entity</b></p>	<p>Silicon Valley Creates, a California nonprofit public benefit corporation doing business as SVCcreates          38 W. Santa Clara St.          San Jose, CA 95113</p>
<p><b>ii. Start and End Dates for the Subsidy</b></p>	<p><u>Start Date:</u> Upon City's execution of the Ground Lease Agreement  <u>End Date:</u> 55 years from Commencement Date, with an option to extend up to a total of 99 years after the Commencement Date</p>
<p><b>iii. Description of the Subsidy, Estimated Total Amount of Expenditure of Public Funds or Revenue Lost</b></p>	<p>This project does not provide funds directly to the project, but does provide a below-market lease rate with an estimated value of \$5,769,920.</p>
<p><b>iv. Statement of Public Purpose</b></p>	<p>The CCA is a new model for supporting the arts in the 21st century. The CCA will create a nexus of flexible services and spaces with both physical and virtual infrastructures. The CCA will be a sustainable hub of resources for the non-profit creative sector in San Jose and part of the growing national network of shared facilities.</p> <p>The Silicon Valley region presents a unique set of challenges and opportunities for creatives and arts organizations that the CCA is designed to address. The Silicon Valley environment promotes innovation, collaboration, and diverse thinking. At the same time, the prosperity of the region makes available facility space for creative pursuits and arts groups rare and costly. To survive arts groups must be innovative and lean with financial models and business management.</p> <p>The CCA will become a focal point for arts services and creative practice by offering dynamic and innovative opportunities for resources and space for resident organizations, independent creatives and small cultural groups needing back office, studio, and rehearsal space. It will provide unifying and cost-saving</p>

	<p>solutions for participants by offering affordable operations such as finance, human resources, legal, marketing, procurement, and IT solutions. By representing a larger group of creative enterprises, CCA will improve buying power, reduce the overall burden of administration, and enhance the level of benefits and services for all.</p>
<p><b>v. Projected Tax Revenue</b></p>	<p>This project will result in construction tax revenue of \$1,500,075. Because the Lessee is a non-profit organization, it is exempt from many taxes.</p>
<p><b>vi. Estimated Number of Jobs Created, Broken Down by Full-Time, Part-Time, and Temporary Positions</b></p>	<p>The CCA project expects to create or retain the following jobs through its construction and operations. Note that jobs retained as a result of the CCA’s unique model supporting arts organizations through below-market rents, could otherwise be lost as a result of rising rents throughout the region.</p> <ul style="list-style-type: none"> <li>• Create 100 temporary FTE construction jobs with annual salaries greater than \$80,000</li> <li>• Create 10 new permanent FTE jobs among the major tenants with annual salaries of at least \$40,000 to \$60,000</li> <li>• Retain 62 permanent jobs among tenants through the provision of the below-market rents for office/rehearsal space in the CCA; Of the 62, 47 are full-time, and the remaining 15 are part-time</li> <li>• Retain 92 seasonal jobs among tenants for teaching artists and performers, which will be documented living wage jobs</li> <li>• San Jose’s Living Wage hourly rate is currently \$20.57 for jobs with health benefits, and \$21.82 without health benefits. These wages equate to \$42,785.60 and \$45,385.60 per year for full-time work.</li> <li>• For a 1-bedroom housing unit with 2-person occupancy, the Extremely Low Income threshold is \$28,650. For a 2-bedroom unit with 3-person occupancy, the Extremely Low income threshold is \$32,250.</li> <li>• Therefore, the Living Wage jobs created and retained by the project are not expected to increase demand for Extremely Low Income housing units.</li> </ul> <p>Finally, SVCcreates and its partners and tenants will make strong and documented efforts to fill all vacant positions locally, with first consideration of San Jose’s Japantown community (zip code 95112).</p>

**COST SUMMARY/IMPLICATIONS**

Revenue generated from rental, use, and occupancy of this property will go to the General Fund.

**CEQA**

An Addendum to the Japantown Corporation Yard Redevelopment Project Final Environmental Impact Report, Resolution No. 74384.

/s/  
KIM WALES  
Deputy City Manager  
Director of Economic Development

For questions please contact Nanci Klein, Assistant Director of Economic Development at 408-535-8184.



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