



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Jacky Morales-Ferrand
Jim Shannon

SUBJECT: SEE BELOW

DATE: March 11, 2021

Approved

Date

03/12/21

COUNCIL DISTRICT: 3

SUBJECT: APPROVAL OF A LOAN COMMITMENT OF UP \$250,000 TO HABITAT FOR HUMANITY EAST BAY/SILICON VALLEY FOR CONSTRUCTION AND REHABILITATION COST OF FOUR AFFORDABLE UNITS FOR SALE AT THE PROPERTY LOCATED AT EAST REED STREET AND SOUTH FOURTH STREET

RECOMMENDATION

(a) Adopt a resolution:

- (1) Approving a total commitment of up to \$250,000 in Affordable Housing Impact Fee Funds (“Loan”) to Habitat for Humanity East Bay/Silicon Valley, Inc., a California nonprofit public benefit corporation, for the construction and rehabilitation costs of four owner-occupied For Sale affordable units at 80% AMI, at the property located at the corner of East Reed Street and South 4th Street (“4th and Reed Development”) and;
- (2) Authorizing the Director of Housing to negotiate and execute loan documents, and any amendments thereto, and all other documents related to the Loan and the 4th and Reed Development.

(b) Adopt the following Appropriation Ordinance Amendments in the Multi-Source Housing Fund:

- (1) Increase the Housing Loans and Grants appropriation to the Housing Department by \$250,000; and
- (2) Decrease the Unrestricted Ending Fund Balance appropriation by \$250,000.

OUTCOME

Approval of the proposed loan will enable Habitat for Humanity East Bay/Silicon Valley (“Developer”) to assemble construction financing to rehabilitate four affordable for-sale homes at the property located at 4th and Reed Development site in San José (*See Attachment A-Site Map*). The building will be relocated to this site from South First and East Reed Streets, where

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the historic building needs to be moved to make way for development of new housing on the site. The 4th and Reed Development will provide four homes affordable to families with incomes less than 80% of the area median income (“AMI”). This funding commitment supports the Mayor and City Council’s 10,000-unit goal.

BACKGROUND

This proposed development is an example of creative problem solving where the City and community have come together to find a solution meeting multiple priorities. A historic building (*photo included as Attachment B*) was facing an uncertain future due to a proposed housing development, an underutilized city-owned site was identified, and the need for homeownership opportunities for low-income households all converged into this proposed solution. Working together, the community and the City will be investing resources to preserve the historic building and open the doors to home ownership to four low-income households.

Preservation of Historic Building

KT Urban is developing a new mixed-use tower project at the corner of South 1st Street & East Reed Street in downtown San José. The historic Pallesenour Apartment building, consisting of residential units, is located on the South 1st Street and East Reed Street site and was scheduled for demolition in March 2021 because the developer could not relocate it. The Pallesen Apartment building is on San José’s historic inventory list. It is not on the national registry (renovation work on the building is not dictated by the U.S. National Park Service), and therefore it is not protected from demolition.

Locating A Suitable Site

Habitat has been working diligently with the Preservation Action Council of San José (“PAC*SJ”) and the City of San José to find a suitable relocation site for the building to save the historic building from the impending demolition. Habitat for Humanity, along with the Office of Economic Development, Real Estate Services, identified an approximately 10,454 sq. ft. City-owned property less than three blocks away at South 4th Street & East Reed Street (APN 472-27-106). On February 4, 2020, this property was declared surplus to the needs of the City by the City Council in Resolution No. 79396. The City agreed to sell a portion of the lot, approximately 5,100 sq. ft., as a potential relocation site to Habitat for Humanity for \$1, subject to various affordability restrictions with the intent to have Habitat relocate the historic building and rehabilitate the units for affordable for-sale housing.

Habitat for Humanity

Habitat for Humanity East Bay/Silicon Valley has historically been involved in small rehabilitation or single-family construction projects. This project involves the rehabilitation of a two-story building, consisting of four one-bedroom, one-bath units (two on the ground floor and two upstairs) which is aligned with Habitat’s affordable housing model. Habitat for Humanity’s affordable housing model requires eligible households to participate in the construction/rehabilitation to accrue sweat-equity in their future home and community. Homeowners are also

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required to participate in a series of trainings on topics like financial management, leadership development, conflict resolution, and communication. This prepares homeowners for managing a Homeowners Association and collectively maintaining their communities. Habitat for Humanity employs construction staff and contracts with building professionals like any other typical housing developer. They also rely on dedicated volunteers and donations to offset the costs of construction and to keep costs affordable. With deed restrictions on every home, Habitat for Humanity also ensures that when the homes are resold, they are resold at an affordable price to another lower-income household. This allows the owner to receive limited equity while preserving the affordability for future low-income family.

ANALYSIS

The recommended action for the City Council's consideration is the final piece to this transaction, authorizing the Housing Department to invest \$250,000 in Affordable Housing Impact Fee funds to finance the rehabilitation of the historic building once it is relocated to the vacant site. The analysis describes the terms and conditions of this loan to Habitat for Humanity to complete the construction.

Project Costs

The cost of relocating the apartment building from its current location on South 1st and East Reed, to the South 4th & East Reed site is estimated to be approximately \$250,000. The building relocation will need to occur before mid-March, as the tower project at South 1st & East Reed is scheduled to start construction. PAC*SJ and Habitat have coordinated a fundraising campaign to raise the funds for the move and the City of San José Housing Department has agreed to loan Habitat \$250,000 in Affordable Housing Impact Fee funds to assist with the completion of the overall project.

Scope of Work

The four units are each approximately 1,100 sq. ft. and three of them have had some level of renovation in the past 15 years. The current plan will be to bring the electrical, plumbing and mechanical up to code, add new cabinets, countertops, windows, doors, drywall patch, appliances, bathroom fixtures, and paint, as updates to the units. The larger floorplans may provide opportunities to change the layout to one or more of these units, such as adding an additional bedroom, thereby increasing the family sizes for these units. Habitat will need to obtain foundation, site development and off-site permits for placing the building permanently on the site and providing utilities to the structure. Habitat will also develop and process a condo map for the structure so that the units can be sold as individual units.

Affordability

Habitat anticipates selling all of the homes to Low Income households at less than 80% AMI, as required by the Housing Department for its funding contribution. Current values for a one bedroom/one bathroom range from \$510,000 to \$620,000. Habitat's renovated homes would be priced at 37%-45% of current market rates, estimated at \$232,800.

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Habitat EBSV would maintain the right of first refusal to buy back the homes, with an 80% AMI 45-year deed restriction protecting the affordability of the homes for almost half of a century. The City of San José Housing Department will also record two affordability restrictions against the property as required by the funding source.

Financing

Prior to the close of the loan the Developer shall submit to the Housing Department for approval a final proforma budget reflecting the Developer’s estimated income and operating expense, and the projected cash flow from the sales of the units, for the Development.

Habitat EBSV will apply for additional financing through a construction loan, and other assistance programs to make the Project as viable as possible. Habitat EBSV also plans to contribute private capital and donor funding, with other cash sources including but not limited to the AHP/WISH Funding. The City’s loan will be applied to each unit as a silent second loan. If the unit is sold to another income qualified household, the funds will remain invested, and will be repaid at the end of the affordability period when sold at market rate.

Table 1: Construction Cash Sources

			% of
Construction Cash Sources	TOTAL	PER UNIT	TOTAL COST
Construction Loan	\$ 931,200	\$ 232,800	60.25%
HFHEBSV – Internal Capital	\$ 84,254	\$ 21,063	5.45%
HFHEBSV – Private Donor Funding (w/PAC*SJ)	\$ 220,000	\$ 55,000	14.24%
Governmental Assistance -AHP/WISH	\$ 60,000	\$ 15,000	24.27%
Governmental Assistance – City of San Jose	\$ 250,000	\$ 62,500	113.64%
Total Construction Sources	\$ 1,545,454	\$ 386,363	220.85%

Next Steps

The Housing Department will work with Developer to negotiate and execute loan documents and any other documents related to City financing for the project to be located at 4th and Reed Streets in the City of San José.

CONCLUSION

Staff recommends the 4th and Reed Development for approval of a funding commitment of \$250,000 from Affordable Housing Impact Fee Fund to create four new affordable homes in San José.

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EVALUATION AND FOLLOW-UP

The Housing Department produces quarterly Information Memoranda regarding the use of the Director of Housing's Delegation of Authority under the Municipal Code; therefore, final loan business terms would be summarized in those memoranda. In addition, the Housing Department posts periodic reports on the status of its affordable properties undergoing rehabilitation or construction to its website, www.sihousing.org. If the recommended actions are approved and Developer successfully closes construction financing, it would be included in these Production Reports.

CLIMATE SMART SAN JOSE

The recommendation in this memo aligns with one or more of Climate Smart San José energy, water, or mobility goals.

POLICY ALTERNATIVES

The Housing Department considered the following alternative before making these recommendations for this affordable housing development.

Alternative #: *The City Council could deny the requested funding commitment.*

Pros: The requested funds could be used for other affordable housing developments.

Cons: The City is facing a tremendous need for affordable housing, particularly the for Low- and Moderate-Income individuals that comprise what is known as the "Missing Middle".

Reason for not recommending: The 4th and Reed Development provides a unique opportunity to provide homeownership opportunities to low income households.

PUBLIC OUTREACH

There has been no formal public outreach meetings held for the relocation and rehabilitation of the Pallesen property. However, the Office of Economic Development went to City Council on February 4th, 2020 to authorize the City Manager to execute an option agreement to sell the surplus land to Habitat For Humanity EBSV. City Council approved this action, and the sale is pending.

City Council Member Raul Peralez has also worked with Preservation Action Council of San José, and the members of the District 3 local community, to raise awareness about the relocation and rehabilitation of the Historic Building, as noted in the attached letter dated December 16, 2020. (*Attachment C*).

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COORDINATION

Preparation of this report was coordinated with the City Attorney's Office, and the Office of Economic Development Real Estate Division.

COMMISSION RECOMMENDATION/INPUT

This item was not heard by the Housing and Community Development Commission, as approvals of affordable development financing do not fall under the functions, powers, and duties of the Commission delineated in Section 2.08.2840 of the San José Municipal Code.

FISCAL/POLICY ALIGNMENT

This action is consistent with the City's *Consolidated Plan 2015-2020*, adopted by City Council on May 5, 2015, to provide homes for very low- and extremely low-income households; and with Goal H-2 of the City's *Housing Element 2014-2023*, adopted by City Council on January 27, 2015, to "increase, preserve, and improve San José's affordable housing stock."

COST SUMMARY/IMPLICATIONS

1. AMOUNT OF RECOMMENDATION/COST OF PROJECT: \$250,000

SOURCE OF FUNDING: Multi-Source Housing Fund
(Affordable Housing Impact Fee Fund)

2. FISCAL IMPACT: Funding in the amount of \$250,000 has been reserved in the Affordable Housing Impact Fee Fund, which is contained within the Multi-Source Housing Fund, is recommended for allocation to the Housing Loans and Grants appropriation to encumber and draw upon when construction is initiated. There is no ongoing fiscal impact as a result of this action.

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BUDGET REFERENCE

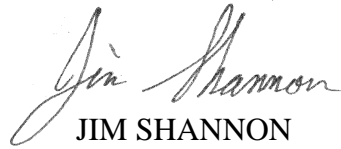
The table below identifies the fund and appropriations to fund the actions recommended as part of this memo.

Fund #	Appn #	Appn. Name	Total Appn	Rec. Budget	2020-2021 Adopted Operating Budget Page	Last Budget Action (Date, Ord. No.)
448	0070	Housing Loans and Grants	\$4,400,000	\$250,000	X-76	9/15/2020, Ord. No. 30477
448	8999	Unrestricted Ending Fund Balance	\$18,231,005	(\$250,000)	X-77	2/9/2021, Ord. No. 30531

CEQA

Garden Gate Tower Final Supplemental Environmental Impact Report, File No. SP18-001 and T18-001.

/s/
JACKY MORALES-FERRAND
Director, Housing Department


JIM SHANNON
Budget Director

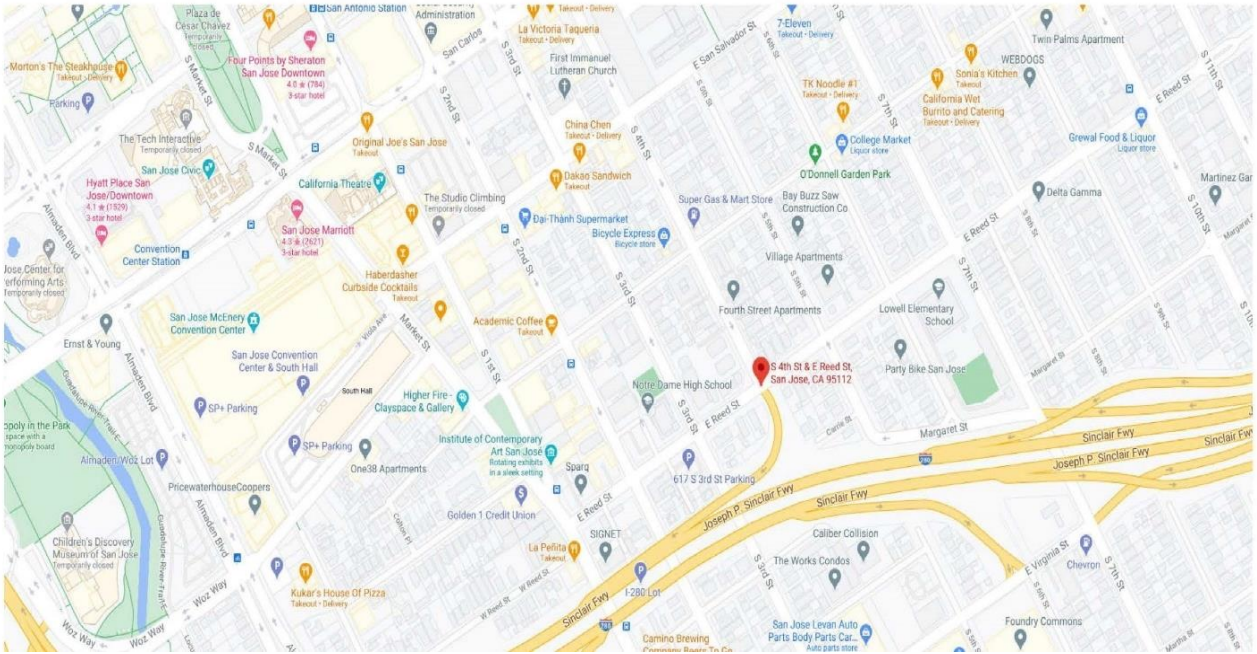
For questions, please contact Rachel VanderVeen, Deputy Director, Housing Department, at (408) 535-8231.

Attachments:

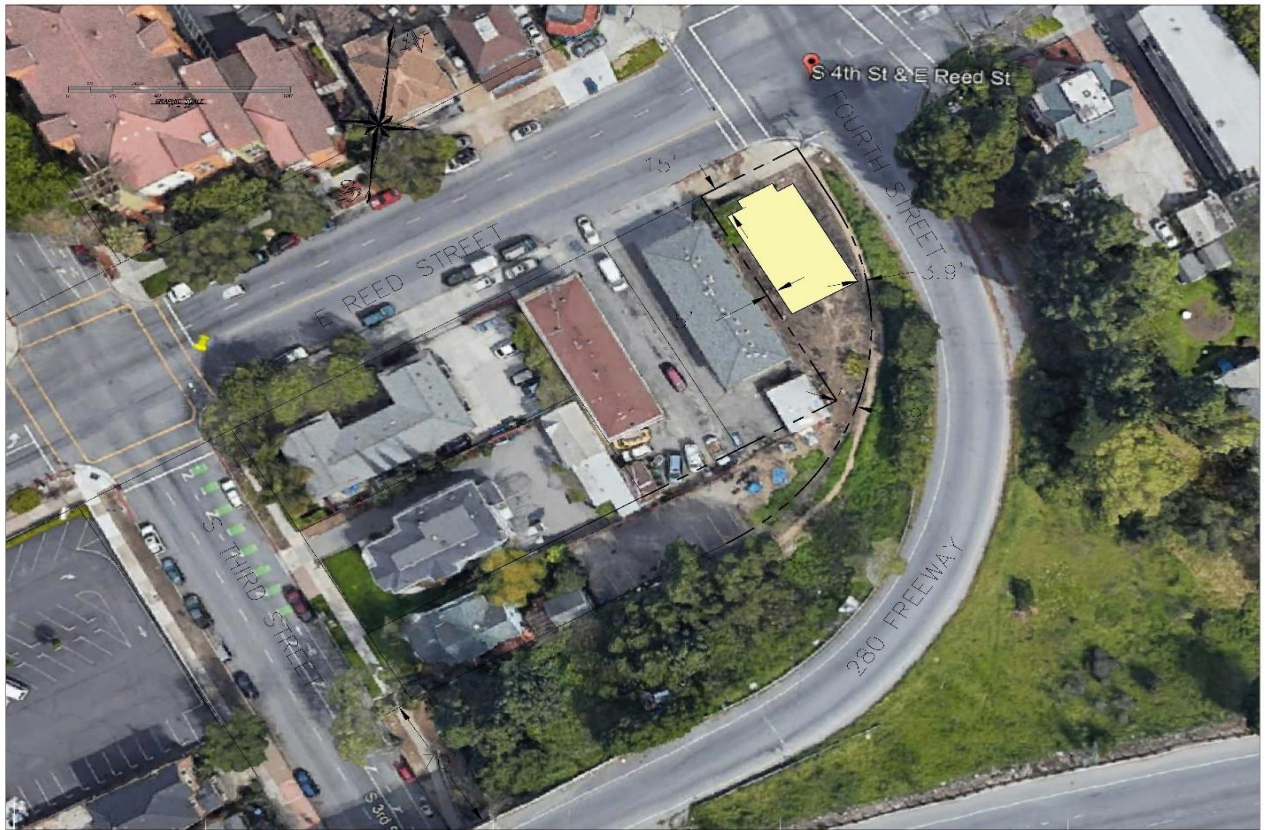
- Attachment A - Site Map
- Attachment B – Photo of Historic Building
- Attachment C – Letter Dated December 16, 2020

Attachment A: Site Maps

Site Map: 4th and Reed



Site Map: Ariel View



Attachment B: Historic Building Photos

Pallesen Apartment Building Picture



December 16, 2020

SUBJECT: Pallesen Apartment Building

To Whom It May Concern,

Thank you for your interest in the Pallesen Apartment Building (“the Pallesen”) located at South First Street and East Reed Street. The purpose of this email is to outline the events relating to the Pallesen and what the future holds for this historic building. As the Councilmember for this area, I have sought to balance historic preservation with growth in our Downtown area. This is why I helped initiate the Historic Inventory Update that is currently underway.¹ I’ll state it simply that it was my desire to work to exhaust all options in preserving and saving the Pallesen.

The following is in detail the events that occurred, and the efforts put forward in attempting to preserve the Pallesen.

THE FACTS

- The Pallesen is a four-unit residential structure constructed in 1910, listed on the City’s historic resources inventory.
- The Pallesen currently sits near the corner of 1st Street and Reed Street which is the site of the Garden Gate Tower Project, a mixed-use project site led by developer KT Urban (“KT Urban”).²
- The City of San José (“City”) owns a portion of the parcel located at the corner of 4th Street and E Reed Street with frontage along E Reed Street (APN 472-27-106), constrained by I-280 on-ramp, and is approximately 10,454 square feet (“Property”).
 - The City is required to comply with the Surplus Land Act to transfer ownership of the property. However, Surplus Land Act provides certain exemptions for the transfer of City-owned property to non-profit housing developers to acquire it for affordable housing before going out to the open market. The City is open to using one of these exemptions to transfer the property and any interested non-profit housing developer will need to likewise comply with the requirements of the relevant exemption.

TIMELINE

1. **October 10, 2019:** KT Urban and Habitat for Humanity begin discussing the project to move the Pallesen to the Property, in particular, to cover the following project costs:

¹ http://sanjose.granicus.com/MetaViewer.php?view_id=&event_id=2689&meta_id=640688

² Special Use Permit #SP18-001. Issued: November 19, 2019. <https://www.sjpermits.org/permits/general/generalfolder.asp?id=4>

- \$79,000 appraised sale price for the City's 4th and Reed Property
- The cost to move the Pallesen building to the Property
- The cost to install a foundation on the Property
- Any entitlement fees

2. **October 23, 2019:** The Planning Commission held a Public Hearing on the Garden Gate Tower Project. At this hearing KT Urban said the project team would welcome the opportunity to move the building if a site is readily available, and noted the opportunity to relocate the Pallesen to the Property.
3. **November 19, 2019:** San José City Council approved the KT Urban Garden Gate Tower Project including my memo stating the following condition³

“Allow demolition of the Pallesen Apartment Building after a 90-day period following the issuance of the planning permit. During that period, the applicant should in good faith make all attempts to relocate the historic building in collaboration with the historic preservation community, Office of Economic Development, Housing Department and Planning Department including the Historic Preservation Officer.”

In the Council session, KT Urban verbally agreed to move the structure once a suitable site was located. I had also asked City Staff whether 90 days was sufficient to complete this Task and they had stated that it was. (Nov 19 + 90 days excl. weekends & holidays = April 3, 2020).

Active negotiations for the sale of the Property and payment for other project costs begin including the City, Habitat for Humanity, and KT Urban.

4. **December 2019:** KT Urban declines to pay the \$79,000 acquisition cost of the Property. The City decides to forego receiving payment for the land to facilitate the deal.
5. **January 30 – March 30, 2020:** As part of the conditions of approval, the developer was required to *“advertise the availability of the structure for relocation for a period of no less than 60 days. The advertisements must include notification in a newspaper of general circulation, on a website, and notice placed on the placed site. The project applicant shall provide evidence (i.e., receipts, date and time stamped photographs, etc.) to the City's Historic Preservation Officer that this condition has been met prior to the issuance of demolition permits”*. The newspaper ad ran for 60 days from January 30, 2020 through March 30, 2020. The sign was installed onsite on February 26, 2020. KT Urban provided the information to the then-City's Historic Preservation Officer (“HPO”) on April 27, 2020 to confirm the condition had been met. The then-HPO confirmed on May 22, 2020 that the condition had been met.

³ <https://sanjose.legistar.com/View.ashx?M=F&ID=7903723&GUID=20289A37-6B61-41EA-B1D9-AD3736A6CF05>

6. **February 4, 2020:** The City Council authorized a Purchase Option with Habitat to sell the Property to Habitat for \$1 to reduce project costs and facilitate moving the Pallesen to the Property.
7. **March 6, 2020:** It was announced that KT Urban had sold the Garden Gate project to a UK-based developer called Scape.⁴
8. **March 17, 2020:** The Santa Clara County COVID-19 Shelter in Place health order went into effect.
9. **April 2020:** The City and Habitat agreed to a proforma where the City contributes the Property for \$1, in addition to support from the Housing Department, to ensure the project was financially feasible with an assumed additional \$150,000 for the foundation paid by KT Urban. Parties meet with KT Urban to finalize the deal, and KT Urban clarifies that they never intended to cover the cost of the foundation.
10. **April - July 2020:** City and Habitat confer to update project proforma to cover the cost of the foundation. Habitat adjusts the affordability limits of the project upward to realize increased revenue and the City Housing Department agrees to adjust Area Median Income (AMI) requirements to ensure financial feasibility. With this arrangement agreed to between the City and Habitat, the parties seek a meeting with KT Urban.

In response to Habitat's request to schedule a meeting, KT Urban notifies Habitat that a different receiver site has been located at S. 30th Street and Shortridge ("Alternate Site") through another interested party, and KT Urban will no longer seek to move the Pallesen to the Property.

11. **July 17, 2020:** The Alternate Site received no support from the current HPO due to concerns regarding its incompatibility with the surrounding neighborhood. Without following up with City Officials, KT Urban subsequently elects to demolish the Pallesen because 90 days have passed from the issuance of the planning permit.
12. **September 2020:** My office ("District 3") became increasingly involved after hearing from the Preservation Action Council of San José ("PACSJ") that the plan to move the Pallesen to the Property failed. District 3 took the following actions:
 - Connected with City Staff to conduct due diligence on what had occurred;
 - Reached out to KT Urban to facilitate a meeting in hopes to appeal for reconsideration;
 - Initiated contact with KT Urban's interested buyer of the Pallesen ("Alternate Buyer"). The Alternate Buyer is currently the owner of the alternate site and claims he has experience in rehabilitating old historic buildings;

⁴ <https://www.bizjournals.com/sanjose/news/2020/03/06/garden-gate-development-downtown-san-jose.html>

- Scheduled an all hands meeting to explore the feasibility of relocating the Pallesen to the Alternate Site.

13. **October 8, 2020:** I convened the first emergency all-hands meeting with the following parties:

- | | |
|-------------------------------------|-------------------------------------|
| a. Alternate Buyer | g. Ryan Do, <i>CSJ-DPW</i> |
| b. Mark Tersini, <i>KT Urban</i> | h. Lily Lim-Tsao, <i>CSJ- DOT</i> |
| c. Jennifer Jodoin, <i>KT Urban</i> | i. Nanci Klein, <i>CSJ-OED</i> |
| d. Rosalynn Hughey, <i>CSJ-PBCE</i> | j. Ben Leech, <i>PAC SJ</i> |
| e. Robert Manford, <i>CSJ-PBCE</i> | k. David Tran, <i>District 3</i> |
| f. Dana Peak, <i>CSJ-PBCE</i> | l. Patricia Ceja, <i>District 3</i> |

The following was the outcome of the meeting:

- Planning stated that while there were initial concerns of the site, after further internal discussion, the site was ultimately deemed appropriate for the Pallesen to facilitate its preservation and would support the move. Staff also committed to researching if there were any historic preservation grants available.
- Determination for the cost from both City Staff and Alternate Site owner was priority to determine feasibility, including moving route.
- KT Urban, representing Scape, indicated there was intent to demolish the building in mid December, though I appealed for additional time in which they agreed to explore further.
- The 4th and Reed site remained a potential option and the Alternate Buyer expressed interest in purchasing the site and the relocation if the Alternate Site was deemed financially infeasible. There were concerns raised by OED though regarding legal limitations due to the Surplus Land Act and its impact on the timeline.

14. **October 14, 2020:** District 3 reconvened the second emergency all hands meeting with the same attendees from meeting sans OED. The following was the outcome of the meeting:

- a. The Alternate Buyer shared the map of his mover's proposed route which was Reed → 3rd → Santa Clara → 28th → Shortridge. Staff responded by providing a sample, the municipal cost for the San José State University move of the Associate Students house from San Fernando Street / 4th to 10th which was as follows:
 - i. Traffic Signals: \$340,000
 - ii. SJPD: \$26,000
 - iii. Tree trimming: \$88,000

Note that this does not include the cost of the move itself. Regardless, City Staff committed to reviewing the proposed route from the Alternate Buyer to provide a more accurate quote.

- b. KT Urban shared that the mid-December date remains a soft date and that the best they can offer is they will inform the “group” when time gets closer to actual demolition.
 - c. Planning shared they were not able to find any available historic preservation grants.
 - d. As OED was absent from the meeting, District 3 offered to facilitate another meeting with Alternate Buyer and OED to explore whether there may be a legal mechanism that allows him to move the building to the original property at 4th and Reed.
15. **November 6, 2020:** District 3 meets with OED and the Alternate Buyer in an attempt to find a legal solution to allow the Alternate Buyer to acquire and move the Pallesen to the 4th & Reed Property.
 - a. Unfortunately, per the City Attorney’s Office, the City can only directly sell surplus city-owned land to a non-profit housing developer without going out to an open market bid.
 - b. The only other option is to go to an open market bid which may take several months and will most likely exceed the demolition deadline.
16. **November 10, 2020:** The City Department of Transportation notified the Alternate Buyer that the municipal cost of the moving the Pallesen to the alternate site would be *“\$750,000 and 2-3 days of work before and possibly after; add \$5k for tow away permit and fees.”*
17. **November 18, 2020:** Alternate Buyer notifies District 3 and City Staff that after internal discussions, the cost altogether to relocate the building would be within the \$1.5 million range. Therefore, per the Alternate Buyer: “the option of moving the Pallesen building to 30th St. regrettably is financially unfeasible at this time.” District 3 at this point in time determined that they have exhausted their options and notified PACSJ of the outcome of this effort.

SO WHAT IS NEXT?

- The property at 4th and Reed remains available, and the City Council had authorized for City Staff to execute a Purchase & Sale Agreement / Option Agreement with Habitat. The City’s Housing Department was ready to support the project costs in addition to donating the Property. PACSJ also originally donated \$10,000 to the overall cost as well.

Therefore, the Pallesen could technically still be delivered to the 4th and Reed site at any time and left suspended on jacks while Habitat completes work on a new foundation and infrastructure. Nevertheless, the cost and the question of who is covering the cost of the move before the developer proceeds with demolition in the next few months would be the outstanding issue.

- Unfortunately, despite the best efforts from the District 3 office in early autumn, a relocation solution could not be reached, and the developer is legally within their rights to demolish the Pallesen, if they so choose.
- KT Urban and Scape are working with the Department of Public Works to set up a site utilization plan for construction as well as refine the schedule, including demolition. We hope they will notify us in a timely manner.
- The Garden Gate project is currently going through a Special Permit Amendment (SPA18-001-01) to request for extended construction hours, a community meeting is scheduled on January 11, 2021.

CONCLUSION

There were indeed many lessons learned throughout this experience and I intend to work with City Staff to evaluate our processes and bandwidth to ensure this does not occur again in the future.

In closing, I first would like to share my gratitude with the Alternate Buyer for his time and efforts in attempting to find a solution. I would also like to thank PACSJ for their advocacy and while we were unsuccessful in this instance, this has highlighted the importance of having a collaborative spirit between the City and the Historic Preservation Community.

Sincerely,



Raul Peralez
Councilmember, District 3
City of San José