



Good Neighbors

San Diego
Housing Commission

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REPORT

DATE ISSUED: January 7, 2005

ITEM 103

REPORT NO.: HCR05-04
For the Agenda of January 14, 2005

SUBJECT: Supplemental Multifamily Housing Revenue Bonds to Complete Construction of Rancho del Norte Apartments (Council District 1)

SUMMARY

Issue # 1: Should the Housing Authority take the initial steps to issue supplemental multifamily housing revenue bonds to complete the construction of Rancho del Norte Apartments, located at the Northwest corner of Camino del Norte and Rancho Bernardo Road in the Black Mountain Ranch Planning subarea of the North City Future Urbanizing Area (NCFUA)?

Recommendation #1: That the Housing Commission recommend that the:

- A. Housing Authority approve a bond inducement resolution in an amount up to \$400,000 to complete construction of the 119-unit Rancho del Norte Apartments. This action will increase the total issuance amount from \$9.825 million to \$10.225 million. All other aspects of the project will remain as originally approved.
- B. Housing Authority approve an application (and subsequent applications if necessary) to the California Debt Limit Allocation Committee for an allocation of authority to issue tax-exempt "private activity bonds" for the Rancho del Norte Apartments; and,
- C. City Council hold a public hearing (*known as a TEFRA hearing - Tax Equity and Fiscal Responsibility Act*) and adopt a resolution approving the issuance of tax-exempt bonds in an amount up to \$400,000 by the Housing Authority.

Issue #2: Should the Housing Commission approve a financing team to work on preparing the proposed bond issuance?

Recommendation #2: That the Housing Commission approve Joe C. Litten of Public Financial Management as financial advisor and Orrick, Herrington & Sutcliffe LLP as bond



A state agency authorized by the City of San Diego

counsel to begin work on the project. Staff recommends selecting these two firms because they worked on the initial bond issuance.

Fiscal Impact: The issuance of the bonds will not financially obligate the City, the Housing Commission, or the Housing Authority because security for the repayment of the bonds will be limited to specific private revenue sources. All costs of the financing, including compensation for staff efforts in preparing the bonds, will be borne by the developer. The Housing Commission has no subordinate financing on the project that will be affected by a larger loan.

Housing Affordability Impact: The project will restrict 8% of the apartments for occupancy by families earning no greater than 20% of the State Median Income (SMI) (\$13,700 for a family of four); 23% of the apartments for families earning no greater than 30% SMI (\$20,550 for a family of four); and 69% of the apartments for families earning no greater than 60% of the area median income (\$41,100 for a family of four). One unit will be reserved for a resident manager.

Previous Related Action: Beginning in December 2002, the Housing Commission and Housing Authority considered and approved several items to permit the issuance of bonds for this project. Please see Attachment 1 (HCR03-101) for a summary of prior actions.

Future Related Action(s): Specific authorization to issue supplemental bonds for Rancho del Norte Apartments will be sought from the Housing Authority at a future date (Refer to Attachment 2, Section 4 "Final Bond Approval"). All other financial participants have already approved the increase in the bond amount.

DISCUSSION

The 119-unit Rancho del Norte Apartments are currently under construction with first moves currently scheduled for late January. The project was originally estimated to cost \$21,922,000.

On December 5, 2003, the Housing Authority issued two series of bonds totaling \$9.825 million for the project. The \$6.2 million senior series will provide permanent financing for the project, while the \$3.625 million subordinate series will only be outstanding during construction. In addition to bond proceeds, the project was funded from tax credit equity investments (\$6,987,000) a low-interest loan from the State of California's Multifamily Housing Program (\$5,928,222), a deferred developer fee (\$287,994), and a contribution from the master developer (\$2,520,000).

In the past eighteen months, the costs of residential building materials have increased significantly. In particular, the cost of steel has increased by approximately 80% and the cost of lumber has increased by approximately 40%. To pay for these increased costs, the

developer, Chelsea Investment Corporation, is now requesting that the Housing Authority issue an additional \$400,000 in housing revenue bonds.

The project was initially underwritten using restricted rents for calendar year 2003. Due to increases in the 2004 restricted rents, the mortgage lender has indicated that the project can now afford to borrow the additional \$400,000 in bond funds. The \$400,000 in supplemental bonds will increase the total issuance amount to \$10.225 million. The bonds will be secured by a construction letter of credit issued by Bank of America and Fannie Mae will continue to provide the credit enhancement.

The issuance of an additional \$400,000 in bonds will not have any negative impacts on the financial feasibility of the project. The Housing Commission does not have any subordinate financing on the project that would be affected by a larger loan and the tax credit investor has consented to the increase. Neither the faith and credit nor the taxing power of the City or the Authority would be pledged to the payment of the bonds.

Approval of the bond inducement and TEFRA resolutions will not commit the Housing Authority to issue bonds. Specific authorization to issue the supplemental bonds will be sought from the Housing Authority at a future date.

Besides the proposed increase in the bond amount, all other characteristics of the project will remain the same. An updated disclosure statement and audited financials are included as Attachment 3.

ALTERNATIVE

Do not recommend approval of the bond inducement and TEFRA resolutions. If the recommended actions are not taken, the financing shortfall will need to be filled with either higher interest rate debt if available or an increased deferred developer fee.

Respectfully submitted,

Cissy Fisher
Director of Housing Finance & Development

**Signature on File
With Original Document**

Approved by,

Elizabeth C. Morris
President & Chief Executive Officer

- ATTACHMENTS:**
1. HCR03-101
 2. Description of Multifamily Bond Program
 3. Developer Disclosure and Financial Statements*

*Distribution of this attachment is limited. A copy is available for review at the Housing Commission's 1625 Newton Avenue office and the office of the City Clerk, 2nd floor, 202 "C" St.



REPORT

DATE ISSUED: November 7, 2003

ITEM 102

REPORT NO.: HCR03-101

For the Agenda of November 14, 2002

SUBJECT: Final Authorization to Issue Multifamily Housing Revenue Bonds for Rancho del Norte Apartments (Council District 1)

SUMMARY

Issue: Should the Housing Authority take the final step to issue tax-exempt multifamily housing revenue bonds to finance the acquisition and construction by Chelsea Investment Corporation of Rancho del Norte Apartments, to be located at the Northwest intersection of Camino del Norte and Rancho Bernardo Road in the Black Mountain Ranch Planning subarea of the North City Future Urbanizing Area (NCFUA) of Council District 1?

Recommendation: That the Housing Authority authorize the issuance of tax-exempt multifamily housing revenue bonds in an amount not to exceed \$9,825,000 for the acquisition and construction of the 119-unit Rancho del Norte Apartments complex.

Fiscal Impact: The issuance and sale of the bonds will not financially obligate the City, the Housing Authority or the Housing Commission because security for the repayment of the bonds will be limited to specific private revenue sources. All costs of the financing, including compensation for staff efforts in preparing the bonds, will be borne by the developer. The Housing Commission's origination fee as well as the annual administrative fee under the financing will be up to \$22,598 (0.23 percent of the bond amount).

Housing Affordability Impact: Because the development will utilize bonds, tax credits, and State Multifamily Housing Program funds, very deep affordability can be achieved. The project will restrict 8% of the apartments for occupancy by families earning no greater than 20% of the Area Median Income (AMI) (\$12,762 for a family of four); 23% of the apartments for families earning no greater than 30% of the AMI (\$19,150 for a family of four); and 68% of the apartments for families earning no greater than 60% AMI (\$38,280 for a family of four). One unit, which is reserved for the manager, will be unrestricted. The affordability restrictions will remain in place for 55 years. The restricted rents would also apply if Section 8 tenants occupy the units.



Previous Related Action: On November 15, 2002, HCR02-101, the Housing Commission approved the project's financing team (Bond Counsel and Financial Advisor) and recommended the following actions, which were approved by the Housing Authority and City Council on December 10, 2002:

- ?? Housing Authority Bond inducement resolution number 1177 declaring the Housing Authority's "Official Intent" to issue up to \$9,300,000 in tax-exempt bonds;
- ?? City Council resolution R-297502 approving the Housing Authority's issuance of tax-exempt bonds.

On July 18, 2003, HCR03-048, the Housing Commission recommended the following action, which was approved by the City Council on August 5, 2003:

- ?? City Council resolution R-298314 approving the Housing Authority's issuance of up to \$9,825,000 in tax-exempt bonds (\$525,000 more than previously approved).

BACKGROUND

On June 25, 2003, the Housing Authority, on behalf of the developer, submitted an application to the California Debt Limit Allocation Committee (CDLAC) for a bond allocation in the amount of \$9,825,000 for Rancho del Norte Apartments. On September 24, 2003, CDLAC awarded the requested bond allocation to the project. The project's bond allocation will automatically revert to CDLAC unless the bonds are issued by December 23, 2003.

A general description of the Housing Commission's Multifamily Bond Program and actions that must be taken by the Housing Authority and by the City Council to initiate and finalize the proposed financing are described in Attachment 1.

THE DEVELOPER

The applicant and developer for the proposed project is Chelsea Investment Corporation (Chelsea), which is headquartered in Solana Beach. Mr. James Schmid is President and 100% shareholder of the corporation. Formed in 1986, Chelsea is involved in the acquisition, development, and management of multifamily housing projects in California and Arizona. Chelsea currently manages seven apartment communities, including 689 multifamily units located in San Luis, Arizona and in San Diego, Chula Vista, and Calexico, California. Chelsea and its affiliates own, have developed, or are now developing (not including the proposed project) 21 apartment projects comprising a total of 2,346 units located in Southern California and Arizona. The Developer's Statement for Public Disclosure is included as Attachment 2.

Chelsea, through its 100% owned affiliate, CIC Santaluz, LLC, will act as administrative general partner in Santaluz Family Apartments, L.P., a California limited partnership. Pacific Southwest Community

Development Corporation, an experienced California nonprofit public benefit corporation with which Chelsea has partnered on several projects, will serve as the managing general partner; an organizational profile is included as Attachment 3. Lend Lease Real Estate Investments, Inc. is expected to be the limited partner (99.5% partnership interest).

The San Diego Housing Commission and Housing Authority have worked successfully with Chelsea over the past three years to issue a total of \$19,927,000 in multifamily housing revenue bonds for five developments totaling 326 units:

<u>Project Name</u>	<u>Council District</u>	<u>Year Bonds Issued</u>	<u>Bond Amount</u>	<u># Of Units</u>
Regency Centre Apts.	4	2000	\$4,100,000	100
Torrey Highlands	1	2001	\$4,780,000	76
Villa Andalucia	1	2002	\$2,231,000	32
Villa Glen	1	2002	\$2,048,000	26
Windwood Village Apts.	1	2002	\$6,768,000	92

Chelsea is now requesting that the Housing Authority take the final step to issue a total of up to \$9,825,000 in multifamily housing revenue bonds for Rancho del Norte Apartments. Development of the apartment complex will partially fulfill the affordable housing requirements for market rate developments by the Master Developer, Santaluz LLC, in the Black Mountain Ranch Planning Subarea. To completely satisfy their affordable housing obligations, Santaluz LLC is also developing a 70-unit for-sale affordable housing condominium project, "Sycamore Walk," that will be located on a different site. The two affordable projects were approved under one discretionary permit application, and, as such, will use the average affordability between the two projects (59% AMI at Rancho del Norte and 75% AMI at Sycamore Walk) to satisfy the NCFUA affordability requirement of 65% AMI.

PROJECT NARRATIVE

Rancho del Norte Apartments is a new construction project that will create a total of 119 units. The development will be located in the northern portion of Black Mountain Ranch (Subarea I) at the intersection of Camino del Norte and Rancho Bernardo Road (west of I-15). The location map is included as Attachment 4. The development will include four 3-story residential buildings, a community facility of approximately 1,800 Sq. Ft., two tot lots, and a trellis covered picnic area with barbeques. A walking trail will circle the perimeter of the affordable site and the neighboring single-family neighborhood. Adjacent to the site on the south side is an open space corridor, which will buffer the affordable site from traffic on Camino del Norte.

The four residential buildings will consist of 24 one-bedroom, one-bath apartments; 47 two-bedroom, two-bath apartments; and 48 three-bedroom, two-bath apartments. The units will be air-conditioned

and include refrigerators, dishwashers, gas ranges, built-in computer desk, and balconies or patios. The project will restrict 8% of the apartments for occupancy by families earning no greater than 20% AMI (\$12,762 for a family of four); 23% of the apartments for families earning no greater than 30% of the AMI (\$19,150 for a family of four); and 68% of the apartments for families earning no greater than 60% AMI (\$38,280 for a family of four). The restricted rents for the project (outlined below) will also apply if Section 8 tenants occupy the units.

Rent and Income restrictions for the project are outlined in the chart below:

Type	Square Footage	AMI	Number of Units	Average Current Rents	Restricted Rent (Minus utility Allow)	Market Rate	Savings per unit
1 Bedroom	682	20% AMI	2	N/A	\$214	\$1,215	\$1,001
1 Bedroom	682	30% AMI	7	N/A	\$312	\$1,215	\$903
1 Bedroom	682	60% AMI	15	N/A	\$690	\$1,215	\$525
2 Bedroom	880	20% AMI	4	N/A	\$237	\$1,561	\$1,324
2 Bedroom	880	30% AMI	10	N/A	\$373	\$1,561	\$1,188
2 Bedroom	880	60% AMI	33	N/A	\$827	\$1,561	\$734
3 Bedroom	1,122	20% AMI	4	N/A	\$296	\$2,250	\$1,954
3 Bedroom	1,122	30% AMI	10	N/A	\$427	\$2,250	\$1,823
3 Bedroom	1,122	60% AMI	34*	N/A	\$914	\$2,250	\$1,336
Total:			119				

* Includes one manager's unit

Financing Structure

Two separate issues of bonds are proposed for the project: 2003 C bonds ("Senior Bonds") and Series D bonds ("Subordinate Bonds"). The Senior Bonds, in the amount of \$5,895,000 will be credit enhanced and purchased by Fannie Mae through its Tax-Exempt Direct Bond Purchase Program. This program, which is restricted to bond issuances of up to \$8 million, will provide significant savings to the developer through elimination of an underwriter's fee and their related legal, marketing, and publication expenses. The bonds are expected to receive an "AAA" rating by Standard and Poor's Corporation.

Bank of America will purchase \$3,930,000 in Subordinate Bonds through a private sale. The Subordinate Bonds will be used to finance the construction of the project, and will be redeemed at conversion from permanent financing sources. Upon conversion (anticipated to occur within 24 months), only the Senior Bonds will remain outstanding.

In addition to bond proceeds, the project, which has a total development cost of \$25,752,197 will be funded from tax credit equity investments (\$6,948,000) a low-interest loan from the State of California's Multifamily Housing Program (\$5,928,222), deferred developer fees (\$530,975), and a

contribution from the master developer (\$2,520,000 as well as contribution of the land) as partial fulfillment of its obligations to provide affordable housing in the NCFUA. Sources and uses of the funds are also shown in Exhibit A of Attachment 5.

RISKS AND MITIGATIONS

Staff has been working with Public Financial Management, Inc., the Housing Commission's financial advisor for this project, to perform due diligence under the proposed financing and in formulating the resulting recommendation for the Housing Authority. After evaluating the project's financial circumstances, the terms of the proposed financing and public benefits to be achieved, it is the financial advisor's recommendation that the bond issuance for the project be authorized. The Financial Advisor's analysis and recommendation to proceed is included as Attachment 5.

Under the Senior/Subordinate Bond structure proposed for this project, only the Senior Bonds are credit enhanced and rated. However, other assurances are in place to mitigate the risks associated with the Subordinate Bonds. Pursuant to Housing Commission policy, Bank of America will be required to sign an "Investor Letter" agreeing that, should a mortgage default occur, there would not be a bond default. In case of a default under the mortgage loan, Bank of America would have the ability to accelerate and redeem the bonds in exchange for ownership of the project. Bank of America will retain sole ownership of the Subordinate Bonds until maturity.

Issuance of bonds for the project does not constitute a debt or liability of the Housing Authority or the City of San Diego. Neither the faith and credit nor the taxing power of the City or the Authority would be pledged to the payment of the bonds because the security for the bond repayment is limited to the value of the subject property and its revenue sources. The developer is responsible for the payment of all costs under the financing, including the Housing Commission's annual administrative fees.

If the bond issuance were authorized, the following primary documents would be executed on behalf of the Housing Authority: Indenture of Trust, Financing Agreement, Regulatory Agreement and Bond Purchase Agreement. These documents, in a substantially final form, will be on file in the Housing Commission at the time of docketing for consideration by the Housing Authority.

ALTERNATIVE

Do not authorize the issuance of the bonds at this time. If the bonds are not issued, the bond allocation will automatically revert to the State. Also, if the recommended action is not taken, the project will not be able to benefit from tax-exempt below-market financing, and the applicant would not be able to provide the lower than required level of affordability (60% AMI). Further, if the recommended action is not taken, the master developer's ability to meet its affordable housing obligations could be jeopardized.

Respectfully submitted,

Approved by,

Jack D. Farris
Manager, Housing Finance &
Development

Elizabeth C. Morris
Chief Executive Officer

ATTACHMENTS:

1. Description of Multifamily Bond Program
2. Developer Disclosure and Financial Statements*
3. Profile of Nonprofit Managing General Partner
4. Project Location Map
5. Financial Advisor's Letter

*Distribution of this attachment is limited. A copy is available for review at the Housing Commission's 1625 Newton Avenue office and the office of the City Clerk, 2nd floor, 202 "C" Street.

For the Housing Commission Agenda of November 14, 2003
Issuance of Multifamily Housing Revenue Bonds for Rancho del Norte Apartments
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ATTACHMENT 2

MULTIFAMILY BOND PROGRAM

General Description

The Housing Commission's multifamily bond program provides below market financing (based on tax exemption of bond interest) for developers willing to set aside a portion of the units in their projects as affordable housing. The actual issuer of these bonds is the Housing Authority. At the present time, over \$540 million in outstanding bonds provides permanent financing for more than 9,200 multifamily rental units in the City, of which 4,316 units are restricted at various levels of affordability.

Bonds issued by the Housing Authority require a minimum "A" rating, which is typically achieved through the provision of an outside credit enhancement by participating financial institutions that underwrite the project loans and guarantee the repayment of bonds.

The authority to issue bonds is limited under the US Internal Revenue Code. The California Debt Limit Allocation Committee (CDLAC) accepts applications generally two to three times a year (funding "rounds"), and typically receives more applications than is available under its financing authority. Recent congressional action increased the state's bonding capacity from \$50 to \$62.50 per capita in 2001 and \$75 in 2002.

The following actions must be taken by the Housing Authority and by the City Council to initiate a bond financing:

1. Bond Inducement

The adoption of an "inducement resolution" is an initial step required by the Internal Revenue Service to initiate a possible new-money bond issuance. It does not represent any commitment by the Housing Authority or the applicant to proceed with the financing. Rather, it establishes, through public record, the date from which project costs incurred may be determined to be reimbursable from bond proceeds. Generally, the bond inducement amount is higher than the estimated bond amount to reflect a 10-15 percent contingency. The adoption also authorizes staff to work with the selected financing team to perform a due diligence process to determine the feasibility of the financing, the level of affordability of the set-aside units and structure a resulting proposal for the issuance of bonds.

2. TEFRA Hearing and Approval

In order for interest on the bonds to be tax-exempt and in accordance with the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, Section 147(f) of the Internal Revenue Code of 1986, the issuance of bonds must be approved by representatives of the governmental unit with jurisdiction over the area in which the project is located after a public hearing for which a reasonable public notice was given. Therefore, federal regulations require that the issuance of bonds by the Housing Authority be approved by the City Council, as the elected legislative body of the City. A notice of public hearing to be held by the City Council with respect to the proposed issuance of bonds will be published in the San Diego Daily Transcript at least fourteen days prior to the scheduled meeting. The purpose of

such public hearing is to provide an opportunity for interested persons to provide their views on the proposed bond issuance and on the nature and location of the project.

3. Bond Allocation

The issuance of bonds for projects owned by private developers (i.e., projects owned by private developers or by nonprofit sponsors with for profit investor participation - "private activity bonds") requires an allocation of a bond issuing authority from the State of California. In order to apply for the bond allocation, an application approved by the Housing Authority and supported by an adopted inducement resolution and by proof of credit enhancement (or bond rating) must be filed with the California Debt Limit Allocation Committee (CDLAC). In addition, evidence of a TEFRA hearing and approval must be submitted prior to the CDLAC meeting.

4. Final Bond Approval

The Housing Authority retains absolute discretion over the issuance of bonds through adoption of a final resolution authorizing the issuance. Initially, the information about the proposed tax-exempt financing of the project is preliminary. If the inducement resolutions are approved, a due diligence process conducted by staff and financing team members will generate additional information and analysis. Prior to final consideration of the proposed bond issuance by the Housing Authority, the project will have to comply with all the program's financing and affordability requirements, and undergo all required planning procedures/reviews by local planning groups, etc.