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Good Neighbors

San Diego  
Housing Commission

# REPORT

**DATE ISSUED:** September 9, 2005 **ITEM 103**

**REPORT NO.** HCR 05-87  
For the Agenda of September 16, 2005

**SUBJECT:** Proposed Loan for New Construction of Lillian Place  
(Council District 2)

**SUMMARY:**

**Issue:** Should the Housing Commission recommend that the Housing Authority approve a \$731,000 loan to facilitate completion of an in-progress new construction 74-unit apartment complex for families with children at Lillian Place, on J Street between 14<sup>th</sup> & 15<sup>th</sup> Streets (Lillian Place)?

**Recommendation:** That the San Diego Housing Commission recommend Housing Authority approval of a loan up to \$731,000 to Lillian Place L.P. as described in this report, including:

- a) The Housing Commission's loan would be contingent upon the Redevelopment Agency of the City of San Diego approving an amendment to its existing Agreement to allow a proportional share of the residual receipts to be used for payment of the Housing Commission's loan.
- b) Documentation of the terms and conditions of this loan would be contingent upon satisfaction of the General Counsel. The President and Chief Executive Officer would be authorized to take all actions necessary to effectuate this transaction.

**Fiscal Impact:** Approval of the above recommendation would result in a loan of \$731,000. All costs of the proposed loan including all Housing Commission legal, escrow, and title costs, (estimated at approximately \$5,500) would be borne by the developer.

**Certificate of Funding Availability:**

Certificate No.:	FY 06-040
Amount:	\$731,000
Revenue Source:	Inclusionary Funds
Division:	Housing Finance and Development
Line Item:	Loans and Grants

**Affordable Housing Impact:** This project will create 74 new rental units: 23 one-bedroom, 28 two-bedroom and 23 three-bedroom units. Fifty-nine of these units (80%) will be affordable

units with rents ranging from 30% to 60% of area median income (“AMI”) (a range of \$20,700 to \$41,400 for a family of four). The 59 Housing Commission restricted units will be affordable for 55-years. One unit will be the manager’s unit. The remaining fourteen units will be rented to persons up to 110% AMI (under Redevelopment Agency restrictions). A location map is included as [Attachment 1](#) and Initial Rents are shown on [Attachment 2](#).

**Environmental Review:** On December 9, 2003 by Resolution R-298743 and by Resolution R-03707, the Redevelopment Agency of the City of San Diego (the Redevelopment Agency) certified that the Redevelopment Agency had reviewed and considered:

- a) Information contained in the Master Environmental Impact Report for the Centre City Redevelopment Project (“MEIR”) previously certified by the City of San Diego,
- b) The Subsequent Environmental Impact Report (“SEIR”) to the MEIR and associated MEIR Amendments, and
- c) a Secondary Study for the proposed development of the Lillian Place housing project.

Based on the foregoing, the Redevelopment Agency determined: (i) that the Secondary Study for the proposed Lillian Place housing development was prepared and completed in compliance with the California Environmental Quality Act of 1970 (CEQA); (ii) No substantial changes are proposed due to the involvement of new significant environmental effects or substantial increase in the severity of identified significant effects; (iii) no negative declaration or subsequent environmental impact report or supplement or addendum to the MEIR or the SEIR is necessary or required; and (iv) the development of the Lillian Place housing project will have no significant effect on the environment, except as identified in the MEIR/SEIR. No federal funding is contemplated by this action and NEPA processing is not required.

**Community Planning Group:** Prior to 2004 funding approval by the Redevelopment Agency, and prior to the construction start, the developer presented the project to and obtained comments from a number of community organizations, including: the East Village Association; the East Village Community Action Network; Centre City Advisory Committee; and Barrio Logan Project Area Committee.

**Equal Opportunity:** Wakeland Housing and Development Corporation is not certified as a Disadvantaged, Women or Disabled Veteran Business Enterprise. A Certificate of Compliance, a Workforce Report, and an Affirmative Fair Housing Marketing Plan have been analyzed and show compliance with the San Diego Housing Commission Equal Opportunity Program.

**Previous Related Actions:** The Loan Committee reviewed this action on September 13, 2005. No prior Housing Commission actions.

**Future Related Actions:** Centre City Development Corporation consideration on September 21, 2005. If approved by the Housing Commission, this item and changes to the Redevelopment Agency’s loan would be processed as contingent companion items at a regular meeting of the Housing Authority and a special meeting of the Redevelopment Agency on November 1, 2005.

## **BACKGROUND**

Lillian Place is 74 units of new construction apartments targeting families with children. The project is at J Street, between 14<sup>th</sup> & 15<sup>th</sup> Streets, in the downtown East Village Ballpark area. There will be a mix of bedroom sizes with rents affordable to persons earning from 30% to 110% of “AMI” (low income and moderate income), and one manager’s unit. In 2004, the non-profit developer, Wakeland Housing and Development Corporation (“Wakeland”), was successful in obtaining: a \$7,289,000 loan from the Redevelopment Agency; a 9% tax credits allocation of \$10,348,744 (equity, with Prevailing Wage rates being paid) from the State Tax Credit Allocation Committee (“TCAC”); and a \$12,818,000 construction loan from Wells Fargo Bank.

#### Property Description

This 35,719 square feet property is located on J Street between 14<sup>th</sup> & 15<sup>th</sup> Streets, six blocks east of downtown’s Petco Park, in the East Village area. The developer demolished four single-family houses that were in major disrepair and retained one historic structure for rehabilitation. The site was designated culturally significant by the City’s Historic Resources Board, as related to the settlement of African Americans and other minorities in downtown San Diego.

The area near the site is a mixture of warehouses, miscellaneous commercial and light industrial buildings. The area is undergoing rapid redevelopment due to its proximity to the Petco Ballpark and has a number of new residential projects currently under construction or in planning. In the near term future, the predominate land use in the East Village area may be residential. All necessary community facilities and services are located within a reasonable distance of the proposed development.

#### The Proposed Development

This 74-unit, 3-story and 4-story rental development will include 59 Housing Commission restricted units: 17 one-bedroom units, 22 two-bedroom units, and 20 three-bedroom units. The remaining 14 units will have rents based on 110% AMI (Redevelopment Agency restricted), and one manager’s unit. Seventy-six parking spaces will be located in an underground, secured parking garage.

The proposed project includes: a tot lot, laundry facility, a passive garden space, several linked interior courtyards, elevators, balconies, and large windows. A special project feature will include rehabilitation of a historic structure at 14<sup>th</sup> & J, contiguous to the new construction, as a community center building. The second story of the historic building will house two units and the first story will include a 1,750 square foot community room with a computer center for resident use. The community center will house an interior museum exhibit and an exterior wall design facing J Street, commemorating the history of African-Americans in that area. “Lillian Place” is named after Lillian Grant, a former owner of a portion of the site and a prominent African American entrepreneur of the 1940’s and 1950’s.

The architect is Studio E, which has designed several other recent affordable housing projects and has won architectural design awards. Four units (five percent of the project) are designed as fully handicap accessible units, and an additional two units (two percent) will be for sensory-impaired tenants. The project will utilize materials that increase energy efficiency by at least 15% above State Title 24 energy standards. The contractor is Sun Country Builders.

#### Construction Start

In 2004 Lillian Place received its necessary city approvals/permits. In March 2005 the developer started construction. The project is now over 20% built, with completion of site excavation, shoring and footings for the foundation; completion is estimated for July 2006.

#### Funding Shortfall - Increases in Project's Construction Cost and Scope

The developer identified an initial funding shortfall of approximately \$1.15 million due to a number of factors (as shown on [Attachment 3](#)) including: discovery during construction of 3400 tons of lead-contaminated soil that needed to be removed; addition of a masonry boundary/security fence; increased architectural/engineering/survey costs; a three month delay in the construction start (due to weather and issues with adjacent property owner) which resulted in higher subcontractor bids and higher construction materials costs; large increases in insurance; additional professional consulting costs; certain litigation costs; and historic-related artwork costs on exterior wall panels. Also, additional funds became necessary for construction-site security at night. The developer notes that the project's hard cost contingency balance will be needed for construction change orders and thus the hard cost contingency is not available for these shortfall costs.

In order to reduce the \$1.15 million initial funding shortfall, Wakeland applied for and received a \$235,000 Affordable Housing Program (AHP) 0% loan award from the Federal Home Loan Bank, increased its California Community Reinvestment Corporation (CCRC) permanent first mortgage loan by \$185,794, and obtained \$56,744 in additional tax credits from TCAC. However, even after obtaining these additional funds, the project still has a revised current shortfall of approximately \$731,000. The developer was forced to utilize their line of credit to temporarily deal with the shortfall costs, but the developer cannot permanently meet this shortfall with its own resources.

#### Loan Request

On June 20, 2005, the developer requested that the Redevelopment Agency increase its loan; subsequently Centre City Development Corporation staff asked the Housing Commission staff to consider the developer's request using Inclusionary funds generated from the downtown area. On August 9, 2005, the developer submitted a loan application under the Housing Commission's current NOFA for \$731,000 to complete the in-progress construction ([Attachment 5](#)). Currently there are no Housing Commission funds in this project.

#### The Borrower

The developer/borrower is Lillian Place LP, a tax credit limited partnership composed of: Wakeland Housing and Development Corporation ("Wakeland"), Lillian Interfaith Housing Corporation ("Lillian Interfaith"), and National Equity Fund (Limited Partner/tax credit investor). Lillian Place would be the partnership's sole asset. Wakeland, a California 501(c)(3) corporation established in 1998 with a mission of developing affordable housing, is the managing General Partner in the tax credit limited partnership. Wakeland has developed over 3,500 units of affordable housing. Most of their developments are located in San Diego County, with some in Orange County, Sacramento and Seattle. Their developments vary in size from six units to 504 units and include "for sale," senior apartment living and large family projects. This developer recently received national recognition, for its Via Roble Apartments in Escondido, as a finalist for the August 2005 *Affordable Housing Finance* magazine's Readers' Choice awards.

Wakeland's staff is the project development team for the limited partnership. Wakeland's executive director is Ken Sauder and its project manager for Lillian Place is Barry Getzel.

In San Diego, Wakeland's projects include the following Housing Commission funded projects:

- Coronado Terrace, (new construction - 9% tax credits with a Housing Commission loan currently at \$1,369,085) 312 units, 1183 25<sup>th</sup> St, San Diego, (general partner).
- Vista Terrace, (new construction - 9% tax credits with a Housing Commission loan currently at \$1,165,969) 262 units, 1606 Del Sur Blvd, San Diego, (general partner).
- Beyer Courtyard, (new construction - 9% tax credits with a Housing Commission loan currently at \$4,198,887) 60 units, 920 Beyer Blvd, San Diego, (general partner).

Housing Commission staff notes satisfactory performance on Wakeland's existing loans. The developer's disclosure statement is found in [Attachment 6](#). Wakeland's financial statements have been reviewed by Housing Commission staff and found to be satisfactory (see [Attachment 7](#)). Staff has reviewed Wakeland's credit report; it is satisfactory and on file at the Housing Commission offices.

Lillian Interfaith is the Co-General Partner in the tax credit limited partnership, and it is an affiliate of the nonprofit San Diego Interfaith Housing Foundation ("SDIHF"). SDIHF is a nonprofit housing development and management organization incorporated in 1969 by local church bodies seeking to respond to housing needs in San Diego. SDIHF has built and manages various successful properties consisting of over 900 affordable housing units, including the two Housing Commission financed projects Mission Terrace Apartments (77 units at 10400 San Diego Mission Road) and Palm Terrace Apartments (60 units at 2885 Palm Avenue). SDIHF has formed multiple independent corporations, including one specializing in management of affordable housing properties. Interfaith Housing will be the Lillian Place property manager.

#### Estimated Project Costs and Sources

The estimated total development cost of the project is \$23,458,538 (\$317,007/unit). State Prevailing Wage rates are being paid on the project. Proposed financing sources include: \$10,348,744 equity from the sale of 9% percent tax credits; \$4,454,794 conventional bank permanent loan from CCRC; \$7,289,000 loan from the Redevelopment Agency; \$235,000 loan from AHP; a \$400,000 deferred Developer Fee loan; and a proposed Housing Commission loan up to \$731,000.

## **DISCUSSION**

#### Housing Commission Proposed Loan Financial Structure:

It is proposed that the Housing Commission would fund a \$731,000 construction/permanent residual receipts loan to "Lillian LP" (\$12,390 per restricted unit), at 3% simple interest, due in 55 years.

#### Deferred Housing Commission Loan:

The developer's existing Agreement with the Redevelopment Agency calls for the developer to defer \$400,000 of its \$1,200,000 developer fee and that cash flow would go first toward payment of the deferred developer's fee. It is estimated that all Residual Receipts for approximately the first eight years would be needed to pay for the deferred developer fee (plus interest). Since

there would be no available residual receipts for the first eight years, it is proposed to defer payments on the Housing Commission's loan for the first eight years (3% interest would accrue but payments would not be required until after year eight).

Public Agencies' Proportionate Loan Amounts and Proportionate Residual Receipts:

After payment of the deferred developer's fee, the developer's existing Agreement with the Redevelopment Agency allocates residual receipts for the first 30 years: 50% of the residual receipts to the developer and 50% to the Redevelopment Agency; and for years 31-55: 20% to the developer and 80% to the Redevelopment Agency.

It is proposed that the Redevelopment Agency revise its existing Agreement to allow the Housing Commission to proportionally share in the Redevelopment Agency's existing 50% split of residual receipts, in proportion to the Agencies' loan amounts:

Public Agencies Proportionate Loans and Proportionate Split on 50% of Residual Receipts:

Public Agencies' Proportionate Loans:	Public Agencies' Proportionate Share of 50% of Residual Receipts
Redevelopment Agency Existing Loan = \$7,289,000 (91%)	- Redevelopment Agency's Share of Total Residual Receipts = (91% X 50% = 45.5%) - Housing Commission's Share of Total Residual Receipts = (9% X 50% = 4.5%)
Proposed Housing Commission Loan = + 731,000 (9%)	
Total Public Agency Funds = \$8,020,000	

Summary - Proposed Split of Total Residual Receipts:

	Existing Agreement Distribution of Residual Receipts	Proposed Distribution of Residual Receipts
Developer's Share	50% yr 1-30; 20% yr 31-55	50% yr 1-30; 20% yr 31-55
Redevelopment Agency Share	50% yr 1-30; 80% yr 31-55	45.5% yr 1-30; 73% yr 31-55
Housing Commission's Share	--	4.5% yr 1-30; 7% yr 31-55

In summary, from year one through year eight, payments would be deferred but 3% interest would continue to accrue. Starting in year nine, annual debt service payments will equal 4.5% of total residual receipts which is based on a proportionate (9%) share of the Redevelopment Agency's 50% of residual receipts.

Prior to distribution of Residual Receipts, the developer would receive a General Partner Management Fee starting at \$14,500 in year one and increasing by 3% each year (in addition to the developer fee).

Existing Encumbrances On the Property

The existing first deed of trust is \$12,818,000 for a Wells Fargo Bank construction loan. The existing second deed of trust is \$7,289,000 for a City Redevelopment Agency loan (3% interest due in 55 years). Also, there is a \$235,000 (0% interest for 55 years) loan from the Federal Home Loan Bank's Affordable Housing Program (AHP).

The Proposed Financial Plan:

Total Development Cost (TDC): TDC is \$23,458,538 including: land value; construction; demolition and site preparation;

interest costs; builder overhead and profit; consultants; permits/fees and a developer fee.

- Cost Per Unit: The estimated cost per unit of \$317,007/unit includes significant site work and State Prevailing Wage rates.
- Housing Commission Loan Amount: The proposed Commission loan is up to \$731,000 (\$12,390 per assisted-unit and \$6,041 per assisted bedroom) and would leverage \$22,727,538 from other sources. Commission funds provide 3% of TDC and other sources provide 97%.
- Housing Commission Interest Rate: The proposed loan would be at 3% simple interest (not compounded).
- Housing Commission Loan Term: Due in fifty-five years.  
Refinancing of the permanent financing with no cash out shall not require a payoff of the Housing Commission loan within the term of the Commission loan.
- Housing Commission Loan Annual Debt Service Payments: From year one through year eight, payments would be deferred but 3% interest would continue to accrue. Starting at the beginning of year nine, annual debt service payments will equal 4.5% of total residual receipts which is based on a proportionate (9%) share of the Redevelopment Agency's 50% of residual receipts. No minimum payment is proposed on this loan.
- Equity Investment: Tax credit investment is \$10,348,744 equity from the sale of 9% tax credits
- First Trust Deed: The limited partnership has obtained a \$12,818,000 construction loan from Wells Fargo Bank. A permanent loan is estimated to be \$4,454,794 at 6.88%, from California Community Reinvestment Corporation; due in 30 years.
- Second Trust Deed: There is an existing \$7,289,000 55-year 3% loan from the Redevelopment Agency of the City of San Diego. It is proposed that the Redevelopment Agency's \$7,289,000 loan would remain in second position. The proposed use of Housing Commission funds would require revision of the existing Redevelopment Agency agreement, to

allow a proportional share of the Redevelopment Agency's residual receipts to be used for payment of the Housing Commission's loan.

Third Trust Deed:

The \$731,000 Housing Commission loan is proposed to be in third position. The developer has reported that the existing AHP \$235,000 third position loan would subordinate to the proposed Housing Commission loan.

Fourth Trust Deed:

\$235,000 AHP loan (0%, forgivable after 30 years) award from the Federal Home Loan Bank. This loan is currently in third position.

Deferred Developer's Fee:

\$400,000 deferred Developer Fee.

Security:

- During construction, the Commission's loan will be subordinate to the \$12,818,000 Wells Fargo Bank construction loan.
- Upon permanent financing, the Commission's \$731,000 loan will be secured by a third trust deed against the property.
- After timely completion of project construction, the permanent loan will be non-recourse as provided for in the Housing Commission lending policy for tax credit projects.

Appraised Value:

On July 12, 2004, Pacific Real Estate Appraisal, appraised the project at \$13,525,000, (assuming completion of construction and assuming market rents); see [Attachment 8](#).

Loan to Value:

Loan to value to be determined upon receipt of an as-built appraisal. Using the July 12, 2004 appraisal it is estimated the \$13,525,000 appraised value would support an estimated \$12,709,794 in proposed total loans for 93.97% loan-to-value ratio. ( $\$12,709,794 / \$13,525,000 = 93.97\%$  Loan to Value)

\$ 4,454,794	- CCRC permanent first
\$ 7,289,000	- Redevelopment Agency loan
\$ 731,000	- proposed Housing Commission loan
<u>+ 235,000</u>	- AHP loan
\$12,709,794	- proposed total loans

Debt Service Ratio:	1.21 (Year 1)
Rent Restrictions:	A Declaration of Covenants and Restrictions with a 55-year term will be recorded against the property to restrict rents on 59 units at levels affordable to 30% to 60% of AMI (as shown on <a href="#">Attachment 2</a> ).
Occupancy Restrictions:	Occupancy of 59 assisted units will be restricted to households earning no more than 30% to 60% of AMI. One additional unit will be set-aside as the manager's unit and 14 additional units will not be subject to Housing Commission restrictions.
Management Plan:	A Management Plan has been reviewed and approved by Housing Commission staff.
Operating Expense:	Operating expenses are estimated at \$344 per unit per month (not including general partnership management fee [\$14,500 at year one], and \$22,200/yr replacement reserves).
Pro Forma Assumptions:	Income increases are projected at 2.5% per year. Operating expenses are projected at 3.5% per year and vacancy rate is at 5% per year.
Replacement Reserves:	As required by TCAC, an annual \$22,200 replacement reserve (\$300/unit/yr) is included in the pro forma. Reserve expenditures would be subject to Housing Commission approval.
Deferred Developer Fee:	\$400,000 of the developer's \$1,200,000 fee will be deferred and paid from cash flow, plus interest at the applicable federal rate, prior to residual receipts payments.

#### Funding Source

The Inclusionary Housing Program (San Diego Municipal Code Chapter 9, Article 8, Division 5, Section 98.0505) states that reinvestment of Inclusionary in-lieu fees in the community plan area from which they were collected is a priority. This loan would use Centre City fees in the downtown area, conforming with this priority. Centre City fees of approximately \$500,000 are immediately available with significant fee collection expected in the near future.

#### Risks and Mitigation

1. The Housing Commission's risk is mitigated by the fact that the developer has already obtained the necessary tax credits and other necessary financing for this project, and by this developer's general development experience.

2. Nonrecourse: This project has already received tax credits. After the award of tax credits, loans to tax credit projects become non-recourse upon the timely completion of the construction of the project. This is due to IRS regulations that make the investment undesirable if structured otherwise. The conventional first position loan is also non-recourse for the same reason. This limits the Housing Commission's ability to recover funds to the property itself. This risk is typically taken by the Commission in tax credit financed developments, and is deemed mitigated by conservative underwriting assumptions and the equity contribution provided by the tax credit financing.

CONCLUSION - The project has already started construction and is estimated for completion in July 2006. The new construction of 74 units will add to the affordable rental housing stock for local families. The Housing Commission's \$731,000 loan would restrict 59 units for 55 years at a relatively low cost of \$12,390 per assisted-unit (\$6,041 per assisted bedroom). The Housing Commission funds will enable this project's in-progress construction to be completed. For the reasons stated above, staff recommends project funding upon the terms and conditions outlined in this report.

ALTERNATIVE

Do not recommend funding this project. Instead the shortfall could be funded with the \$800,000 of undeferred developer fee balance. However, this alternative would create a hardship for the developer and is therefore not recommended.

Respectfully submitted,

**Signature on File** Approved by,  
**With Original Document**

Cissy Fisher  
Director of Housing Finance & Development

Elizabeth C. Morris  
President & Chief Executive Officer

- Attachments:
1. Location Map
  2. Initial Rents
  3. Developer's June 20,2005 Letter to CCDC
  4. Development Summary
  5. SDHC Application Form
  6. Disclosure Statement \*
  7. Financial Statement \*
  8. Appraisal Summary \*

\* - Distribution of this attachment is limited. A copy is available for review at the Housing Commission office at 1625 Newton Avenue, San Diego, CA.