



REPORT

DATE ISSUED: August 8, 2003

ITEM 106

REPORT NO.: HCR03-065
For the Agenda of August 15, 2003

SUBJECT: Spending Plan for Mercado Apartments Debt Service Savings
(Council District 8)

SUMMARY

Issue: Should the Housing Commission approve a spending plan for the debt service savings resulting from refinancing the conventional development loan for the 144-unit Mercado Apartments?

Recommendation: Approve a spending plan for the annual debt service savings from refinancing a bank loan to: 1) fortify the project's regular operating and replacement reserves; 2) reimburse the project's owner, Metropolitan Area Advisory Committee (MAAC Project), for loan refinancing costs; 3) increase the partnership management fee; and 4) deposit the remainder of the savings into a reserve against potential financial liabilities when the project's tax credit partnership is dissolved.

Fiscal Impact: The proposed spending plan would have no direct fiscal impact for the Housing Commission.

Affordable Housing Impact: The Mercado Apartments are restricted at 35 to 60 percent of Area Median Income and will remain at those levels for 55 years from project inception, or until 2047.

Environmental Review: This activity is exempt from environmental review under the California Environmental Quality Act (CEQA), pursuant to §15060(c)(2) of the CEQA Guidelines.

Previous Related Actions: In 1992, the Housing Commission entered into a three-way agreement with the Redevelopment Agency and MAAC regarding development of Mercado Apartments.

In 1995, the Redevelopment Agency assigned its deed of trust for the Mercado loan to the Housing Commission.



BACKGROUND

In 1992, the City Council directed Centre City Development Corporation to transfer \$1,425,000 to the Housing Trust Fund. The funds were to be used for a loan to MAAC Project for the development of the 144-unit Mercado Apartments at 2001 Newton Avenue. Under the terms worked out by the Redevelopment Agency, the loan is deferred until 2047.

The project financing also included Low Income Housing Tax Credits (for which the MAAC Project formed a partnership with the California Equity Fund) and a loan from the Bank of America.

DISCUSSION

Late in 2001, MAAC Project negotiated an interest rate reduction with Bank of America, bringing the interest rate down from 10 percent to 8.25 percent per annum. The refinancing freed up approximately \$44,000 in annual debt service savings. Recently MAAC asked the Housing Commission and the Redevelopment Agency to agree to allocate the savings in the following manner:

- Add \$5,000 of the annual debt service savings to the operating reserves, now budgeted at three percent of gross rent (approximately \$32,000 per year);
- Add \$10,000 of the debt service savings to replacement reserves, now at two percent of gross rent (approximately \$21,000 per year);
- Reimburse MAAC Project for its out-of-pocket refinancing fee in two payments: approximately \$85,000 in 2003 and \$15,000 in 2004 (using the accrued debt service savings from 2001 and 2002 plus portions of the 2003 and 2004 savings); and
- Deposit the balance of the debt service savings into the operating reserve account in preparation for any exit tax liability or other expenses for which MAAC Project might be liable in connection with dissolution of the partnership, Mercado Apartments, L.P., in 2008 (15 years after formation).

In addition, MAAC Project has proposed a change to the Partnership Management Fee. Currently the formula is \$10,000 plus a four percent annual increase; however, MAAC received no fee at all prior to the refinancing. Staff recommends that the Partnership Management Fee be set at \$25,000 for the current year and allowed to increase at the same rate as the actual increase in Effective Gross Revenue (EGI). MAAC's original proposal was for a \$25,000 fee in 2003, with a four percent annual increase. (The projected annual increase in EGI is three percent.)

If the partnership exit financial obligations prove to be less than the amount accrued in reserve at that time, any excess would be retained in project reserves.

The refinancing and related savings improve the property's cash flow. Investing these savings in reserve accounts protects the financial health of the project. MAAC Project's request for

compensation is reasonable given that MAAC Project has foregone reimbursement for staff and other costs related to the project in order to preserve the project's operating budget in prior years.

ALTERNATIVES

Approve the spending plan as proposed by MAAC Project.

Do not approve an increase in the Partnership Management Fee, instead assigning all debt service savings to project reserves.

Respectfully submitted,

Approved by,

Signature on File with Original Document

Jack D. Farris
Housing Finance and Development Manager

Elizabeth C. Morris
Chief Executive Officer

Attachment: Location Map

Information: M. MANASTER 578.7589

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ATTACHMENT 1

Location Map