



REPORT

DATE: For the Agenda of March 22, 2002 **ITEM 105**

REPORT NO.: HCR02-018

SUBJECT: Ratification of New Loan Terms for Grant Heights Park and Review of Non-Substantive Changes to Other Recent Multifamily Loans (Districts 4 and 8)

SUMMARY

Issue: Should the Housing Commission approve the creation of a “Special Reserve” fund to help current tenants of Grant Heights Park remain in their homes if Section 8 rental assistance terminates?

Recommendation: It is recommended that the Housing Commission approve this change to the loan terms, which was requested by the primary lender.

Fiscal Impact: The creation of a reserve fund for Grant Heights Park will diminish funds available for residual receipts loan payments.

Previous Related Actions: The Commission approved terms and conditions of funding for: 1) Mandel Apartments on October 20, 2000 (HCR00-099); 2) Mesa Family Villas on January 19, 2001 (HCR01-015); 3) Tesoro Grove Apartments on January 19, 2001 (HCR01-009); 4) Market Square Manor on May 11, 2001 (HCR01-058); and 5) Grant Heights Park on June 1, 2001 (HCR01-062).

Future Related Actions: None.



BACKGROUND

In September of 2001, five local development proposals received tax credit reservations from the California Tax Credit Allocation Committee. To comply with Internal Revenue Code (IRC) requirements and retain the allocated tax credits, escrows for these properties had to close by February 15, 2002.

DISCUSSION

The intent of this Report is to request ratification of an amendment to the loan for Grant Heights Park and report on specific changes that took place in four other tax-credit projects for which escrows recently closed.

During the closing process of any complex escrow, it is not uncommon for differences to arise as the needs of various development partners and ownership entities, construction and permanent lenders, and other funding sources are melded together. Projects that include tax credit financing have deadlines imposed by the Internal Revenue Service; missing one of these deadlines will result in the loss of the tax credit financing. Because this financing typically provides about 50 percent of the development funds, such a loss can be expected to cause the collapse of the affected project's financing.

To meet these critical deadlines and to assure compliance with other requirements, staff is occasionally called upon to consider an arrangement that has not been previously presented to the Housing Commission Board. When this occurs, staff confers with General Counsel to assure that any proposed item would not change the character of the Commission's participation as approved by the Board or add significant risk to the Commission's loan.

Review of Chief Executive Officer's Authority

Housing Commission Policy 600.301 Paragraph 4.3(E) ("Financial Participation – Contract Amendments") states that the CEO may authorize amendments to a loan agreement that exceed the contract amount by no more than the lesser of 5 percent or \$50,000. Such amendments are to be promptly reported to the Board.

The policy does not articulate an approval process for changes that do not result in increased costs. In the absence of explicit instruction, the implication is that such changes can be made by the CEO provided that there is not a material adverse effect on the terms and conditions previously approved by the Housing Commission. As a practice, changes of this nature are reviewed and approved by General Counsel.

In the case of substantive changes (those that could materially increase the risk associated with the Housing Commission loan), the CEO would also confer with the Board Chairman.

Grant Heights Park: Ratification of Rent Reserve

In accordance with Housing Commission policy, staff is presenting a recommendation to make a change in the Grant Heights Park loan and is also disclosing other non-substantive changes to four additional loans.

The National Equity Fund (NEF) purchased the tax credits for Grant Heights Park. To protect current tenants and the cash flow of the project, NEF is requiring that any Section 8 rental income that results from the existing HUD project-based subsidy agreement and is over and above the rents approved for underwriting will be deposited into a special reserve fund. If Section 8 funding ends prior to the expiration of the current HAP contract (May 2004), availability of these funds for operating expenses would allow current tenants to remain in place and continue to pay no more than 30 percent of actual income. This additional subsidy would be available until funds are exhausted or for a maximum of 6 months.

This change will reduce the potential residual receipts for the project during the term of the HAP contract. This change was incorporated into the project loan documents subject to approval by the Housing Commission Board. To avoid loss of the tax credit financing, staff recommends such approval.

Changes to Other Tax-Credit Projects

1. Four Projects: Higher Interest Rate

The Internal Revenue Code states that projects using federal tax credits and HOME funds must be charged at least the Applicable Federal Rate (AFR) for HOME-funded loans if the developers use the higher cost rate allowed in designated "Difficult to Develop Areas." The AFR is posted monthly by the Internal Revenue Service. San Diego is a designated "Difficult to Develop" area. Four of the five projects (Mandel Apartments, Market Square Manor, Mesa Family Villas, and Tesoro Grove) chose the higher cost tier; the interest rate on their Housing Commission loans was changed from 3.0 percent to 5.6 percent. The mostly likely result is that these projects will accrue more deferred debt on Housing Commission loans.

2. Tesoro Grove Apartments: Clarification of Residual Receipts

In a Housing Commission Report of January 19, 2001 (HCR01-009), staff outlined proposed loan terms for the Tesoro Grove Apartments. The Report

states that residual receipts will be shared between the owner and the Housing Commission on a 50/50 basis; a minimum Annual Payment of \$20,830 will be required starting at year three. To clarify that the minimum payment was not intended to subvert the primary lender's underwriting requirements regarding cash flow and debt service, staff agreed that the Housing Commission would waive the right to receive an amount in excess of the available receipts. Instead, in the case of such a shortfall, the Annual Payment amount will be satisfied by the payment of up to 100 percent of the available residual receipts. This formula will affect the owner's cash flow but will not affect the Housing Commission's repayment; this is standard for Commission loans.

3. Mandel Apartments: Budget and Funding Change

After the Housing Commission approved funding for Mandel Apartments (HCR01-092), the Centre City Development Corporation (CCDC) imposed design changes that increased the cost of the development. At the time of closing, CCDC had not yet approved a contribution of the additional funds that will be needed to pay for the new items. To assure that funding will be available to complete the project, St. Vincent de Paul Village, Inc. agreed to provide the gap funding. However, it is anticipated that CCDC will approve funding that will replace St. Vincent's pledge. The Housing Commission's loan remains in first position; loan terms do not change.

Submitted by,

Approved by,

Signature on File with Original Document

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