Good Neighbors
San Diego
Housing Commission

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REPORT

DATE: For the Agenda of November 15, 2002 **Item 102**

REPORT NO: HCR02-101

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

SUMMARY

Issue No. 1: Should the Housing Commission recommend that the Housing Authority and City Council take the initial steps to issue tax-exempt and taxable housing revenue bonds to finance the new construction by Chelsea Investment Corporation of Rancho del Norte Apartments located in Subarea I of Council District 1 in the North City Future Urbanizing Area (NCFUA)?

Recommendation: No. 1: That the Housing Commission recommend that the:

A. Housing Authority approve a bond inducement resolution for new construction of the 119-unit Rancho del Norte Apartments to be located in the northern portion of Black Mountain Ranch (Subarea I) for up to $9.3 million in multifamily housing revenue bonds (Council District 1);

B. Housing Authority approve applications to Round I and, if necessary, subsequent rounds of the State's 2003 allocation rounds for bond issuing authority; 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 bonds by the Housing Authority.

Issue No. 2: Should the Housing Commission approve a financing team from the previously approved list of Financial Advisors and Bond Counsels to work on preparing the proposed bond issuance?

Recommendation No. 2: That the Housing Commission approve Joe C. Litten as financial advisor and Orrick, Herrington & Sutcliffe, LLP as bond counsel to begin work on the project.

Fiscal Impact: Approval of the bond inducement resolution does not commit the Housing Authority to issue bonds. The developer is responsible for the payment of all costs under the financing for the proposed project.

Housing Affordability Impact: The project will restrict 10% (12) of the apartments for occupancy by families earning no greater than 50% Area Median Income (AMI) ($30,050 for a family of four) and 90% (107) of the apartments for families earning no greater than 60% AMI ($36,060 for a family of four). The affordability restrictions will remain in place for 55 years.

Previous Related Action(s): On August 16, 2002, the Housing Commission recommended Housing Authority approval of the first affordable for-sale development in the NCFUA – the 70-unit Santaluz "Sycamore Walk" project (HCR02-067). On October 8, 2002, the Housing Authority convened to approve the Commission's recommendation (Resolution 1172). The average affordability between Sycamore Walk (70% AMI) and the proposed Rancho del Norte Apartments (59% AMI) cannot exceed the NCFUA affordability restriction level (65% AMI).

Future Related Action(s): Specific authorization to issue bonds for Rancho del Norte Apartments will be sought from the Housing Authority at a future date (Refer to Attachment 1, Section 4 "Final Bond Approval").

BACKGROUND

There are two primary ways the Housing Commission provides financial assistance for development of affordable housing: 1) direct lending of Housing Commission HOME and Housing Trust Fund monies; and 2) issuance of tax-exempt multifamily housing revenue bonds through the Housing Commission's multifamily bond program. The Housing Commission utilizes the Housing Authority's tax-exempt borrowing status to pass on lower interest rate financing to developers of affordable housing. Some projects require both forms of assistance. This report pertains specifically to the issuance of tax-exempt multifamily housing revenue bonds, as the project will not require other financing assistance from the Housing Commission.

The Housing Authority's ability to issue bonds is limited under the U.S. Internal Revenue Code. The California Debt Limit Allocation Committee (CDLAC) accepts applications generally two to three times during the year (funding "rounds"), and typically receives more applications for bonding authority than it has available.

Prior to the CDLAC funding rounds, projects are brought to the Housing Commission, Housing Authority and City Council. Bond inducement resolutions must be obtained prior to application submittal and TEFRA resolutions must be secured no later than 30 days after application submittal. The next CDLAC application submittal date is January 15, 2003.

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

PROJECT NARRATIVES

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) 20 apartment projects comprising a total of 2,254 units located in Southern California and Arizona. The Developer's Statement for Public Disclosure is included as Attachment 2.

Chelsea will act as administrative general partner in a partnership that will be created for the project. 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. The tax credit investors will be the limited partners of the partnership.

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:

Project Name	Council District	Year Bonds Issued	Bond Amount	# Of Units
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 also the developer of the following three 9% tax credit financed projects:

- 200-unit senior studio housing, Market Square Manor* (Council District 8). The project benefited from a $2 million Housing Commission loan.
- 90-unit Harvey Mandel Villas* for St. Vincent de Paul (Council District 2). The project benefited from a $1,590,000 Housing Commission loan.
- 38-unit Longacres at Seabreeze Farms (Council District 1).

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* Currently under construction.

Chelsea is now requesting that the Housing Authority and City Council take the initial steps to issue a total of up to $9.3 million 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.

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 3. 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 10% of the units to households earning no greater than 50% of AMI and 90% of the units to households earning no greater than 60% of AMI. The restricted rents for the project (outlined below) will also apply if Section 8 tenants occupy the units. The Regulatory Agreement that determines the level of affordability for the project will be in existence for 55 years.

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	50% AMI	2	N/A	$537	$1,215	$ 678
1 Bedroom	682	60% AMI	22	N/A	$650	$1,215	$ 565
2 Bedroom	880	50% AMI	5	N/A	$644	$1,561	$ 917
2 Bedroom	880	60% AMI	42	N/A	$779	$1,561	$ 782
3 Bedroom	1,122	50% AMI	5	N/A	$710	$2,250	$ 1,540
3 Bedroom	1,122	60% AMI	43*	N/A	$861	$2,250	$ 1,389
Total:			**119**				

*** Includes one manager's unit**

SELECTION OF THE FINANCING TEAM MEMBERS

Staff recommends assigning Joe C. Litten as financial advisor and Orrick, Herrington & Sutcliffe, LLP as bond counsel to work on the project. The proposed financing team members have been selected in accordance with the existing policy for the issuance of bonds. Financial advisors and bond counsels are designated on a rotating basis from the firms selected under the program through a competitive RFP process.

FINANCING STRUCTURE

The allocation that will be sought from CDLAC, $9.3 million, is approximately 10% higher than the amount for which the project is currently being underwritten, $8,463,165. The developer has requested this cushion to account for possible increases in the bond amount resulting from further decreases in the assumed interest rate. It is anticipated that $700,000 of the assumed bond amount of $8.5 million will be paid off at the conversion to permanent financing, resulting in a permanent bond of approximately $7.8 million.

It is anticipated that the bonds will be sold through one of the following two financing structures:

- Public offering: credit enhancement of the bonds through the Federal National Mortgage Association ("Fannie Mae"), which would provide an AAA rating of the bonds; or,

- Direct (Private) purchase: Fannie Mae AAA credit enhanced bonds sold directly to Fannie Mae through its Tax-Exempt Direct Bond Purchase Program. This program, which is restricted to properties with bond amounts of up to $8 million, would provide significant savings to the developer through elimination of an underwriter's fee and their related legal, marketing, and publication expenses.

Pursuant to Housing Authority approval, staff will submit, on behalf of Chelsea, an application for private activity bond allocation to CDLAC. If successful, the bond financing will qualify the project for an allocation of 4% low-income housing tax credits, which will be sold to a tax credit partner. These proceeds will serve as a contribution of project equity. If the application is unsuccessful, at the request of the developer, staff will resubmit the application for a subsequent round.

In the future, should the Housing Authority, under a separate action, authorize the issuance of bonds for the project, the bonds would 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 repayments 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 fee.

RISKS AND MITIGATIONS

Approval of the bond inducement resolution does not commit the Housing Authority to issue bonds. The recommended actions do not represent any commitment by the Housing Authority or the applicant to proceed with the tax-exempt or taxable financing of the project. When eventually issued, the financing risks associated with the project will be minimal since repayment of the bonds will be guaranteed by a third party.

ALTERNATIVE

Do not recommend approval of the bond inducement and TEFRA resolutions. If the recommended actions are not taken, the project will not be able to benefit from tax-exempt below-market financing. Furthermore, the applicant will not be able to provide the proposed low level of affordability (59% AMI) at this project to have it average with the proposed affordability level (75% AMI) at Santaluz LLC's 70-unit for-sale in order to satisfy the NCFUA level of affordability (65% AMI).

Respectfully submitted,

Signature on File with Original Document

Jack D. Farris
Manager, Housing Finance & Development

Approved by,

Signature on File with Original Document

Elizabeth C. Morris
Chief Executive Officer

ATTACHMENTS:

1. Description of Bond Program and Actions to be Taken
2. Developer Disclosure Statement and Financial Statements*
3. Project Location Map

*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.

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ATTACHMENT 1

SAN DIEGO HOUSING COMMISSION
MULTIFAMILY BOND PROGRAM

General Description

The 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 issuer of these bonds is the Housing Authority. At the present time, $515 million in outstanding bonds provides permanent financing for more than 8,900 multifamily rental units in the City, of which 4,200 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.