



Good Neighbors

San Diego  
Housing Commission

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# REPORT

**ITEM 104**

**DATE:** For the Housing Commission Agenda of March 2, 2001

**REPORT NO:** HCR01-032

**SUBJECT:** Issuance of Multifamily Housing Revenue Bonds for New  
Construction of Fox Hollow Apartments (Council District 3)

## SUMMARY

**Issue:** Should the Housing Commission recommend that the City Council take initial steps toward issuance of taxable and tax-exempt revenue bonds for construction of the 96-unit Fox Hollow Apartments located at 4366 Home Avenue, San Diego, CA 92105?

**Recommendation:** That the Housing Commission: 1) recommend the City Council hold a public hearing ("TEFRA" hearing) and adopt a resolution approving the issuance of bonds in the approximate amount of \$7,000,000 for the project; and 2) approve Dain Rauscher Incorporated as financial advisor, Stradling Yocca Carlson & Rauth as bond counsel and Newman & Associates, Inc. as bond underwriter.

**Fiscal Impact** - None. Approval of the resolution does not commit the Housing Authority to issue bonds. The developer is responsible for the payment of all costs under the financing.

**Housing Affordability Impact** – 90% percent of the project (85 units) are to be set aside for occupancy by low-income tenants earning 60 percent or less of the area median income (\$32,220 for a four-person household) for 55 years. The remaining ten percent of the units (10 units) will be set-aside for occupancy by low-income tenants earning 50 percent or less of the area median income (\$26,850 for a four-person household) at rents restricted at the corresponding affordability level for 55 years. The restricted rents would also apply if Section 8 tenants occupy the units.

The rent schedule for the project proposed by the applicant is included as part of the project description.



**Future Related Action(s)** - A specific authorization to issue bonds for the project will be sought from both the Housing Commission and the Housing Authority at future dates. The Housing Commission approved the staff recommendation on the condition that the identities as well as the roles of all partners will be brought back to the Housing Commission for 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 revenue bonds through the Housing Commission's multifamily bond program. The Housing Commission utilizes the Housing Authority tax-exempt borrowing status to pass on lower interest rate financing to developers of affordable housing. This report pertains specifically to the issuance of tax-exempt multifamily revenue bonds.

The authority to issue bonds is limited under the US Internal Revenue Code. The California Debt Limit Allocation Committee (CDLAC) accepts applications generally twice a year (funding "rounds"), and receives more applications than is available under its financing authority. Despite recent congressional action that has increased the state's bonding capacity by 50%, competition is expected to remain keen.

The first CDLAC funding round is May of this year with applications and proof of an inducement resolution due on February 21, 2001 and proof of a TEFRA hearing by the local jurisdiction held prior to March 23, 2001.

In order to meet the CDLAC application deadlines, the owner requested that the California Statewide Communities Development Authority (CSCDA) issue the inducement resolution and will serve as the applicant to CDLAC. CSCDA will subsequently transfer its resolution to the San Diego Housing Commission.

California Statewide Communities Development Authority is a statewide joint powers authority created in 1987 by a number of California cities and counties for the purpose of issuing bonds and other debt instruments on behalf of program participants to promote economic development, including the provision of multifamily housing. Currently, 148 cities (including the City of San Diego), 44 counties and 40 districts or agencies are program participants of CSCDA.

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. In order for the application for bond authority to be considered for the May 2001 CDLAC allocation meeting, proof of the TEFRA hearing must be submitted to CDLAC prior to March 23, 2001.

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 financings are described in Attachment 1.

## **DISCUSSION**

The current owner of the property is San Diego/Fox Hollow L.P. Charles Ashley controls Alpha III, Inc., general partner in the current limited partnership. A new entity will be formed to own the project following issuance of the tax-exempt debt. Alpha III, Inc. will serve as the general partner of the to be formed limited partnership.

The project sponsor and developer is Charles Ashley of Alpha III, Inc. (the co-general partner) and Alpha III Development, Inc. (the development entity). Mr. Ashley has significant experience in development, construction, and operation of multifamily properties throughout the State of California. Since 1980, Mr. Ashley has built approximately 2,500 multifamily units. Since 1996, Ashley has completed and placed in service six "9%" tax credit projects. Mr. Ashley's operation is based in Clovis, California.

The Developer's Statement for Public Disclosure is included as Attachment 2.

### Financing Structure

The project is under construction and is approximately 50% complete. Please refer to Project Narrative below for additional discussion on the project status.

The project requires the current ownership and the current financing to be restructured. The current owner and general partner have applied for and expect to receive in April 2001 an allocation of the tax-exempt debt through CDLAC. Following receipt of the CDLAC allocation, the project will automatically qualify to receive an allocation of four percent low-income housing tax credits. After both allocations have been confirmed, a new limited partnership will be established. Ownership of the property will be transferred to the new limited partnership. The current general partner will serve as the general partner in the new limited partnership. A new limited partner will capitalize the partnership with approximately \$4,192,000 in equity through the purchase of a 99.9% limited partnership interest. The \$7,000,000 in tax-exempt bonds will be issued in favor of the project and the new limited partnership.

The project costs are projected to total \$12,740,000, as outlined below. Approximately \$5,229,000 has been spent to date on development and construction, financed by the current limited partner. The project requires an additional \$5,963,000 to be completed plus the deferral of \$1,548,000 in developer and general contractor fees. The requested bond and tax credit allocation will generate \$11,192,000. These funds will be applied to refinance the current limited partner's investment and to complete construction.

**Uses of Funds**

Land	\$850,000
Construction Costs	\$7,779,000
Other Construction Costs	\$1,824,000
Project Soft Costs	\$731,000
Financing Placement	\$356,000
Developer Fee	<u>\$1,200,000</u>
TOTAL COSTS	\$12,740,000

**Sources of Financing**

Tax Exempt Bonds	\$7,000,000
Tax Credit Equity	\$4,192,000
Deferred Developer Fee	\$800,000
Deferred Contractor Fee	<u>\$748,000</u>
TOTAL SOURCES	\$12,740,000

It is anticipated that the bond-financed loan will be underwritten utilizing a Fannie Mae (FNMA) credit enhancement provided by ARCS Commercial Mortgage resulting in a AAA rating of the bonds. A construction lender will finance the balance of the construction costs, providing its credit enhancement together with ARCS FNMA until the project is completed, leased, and stabilized. Should the Housing Authority authorize the issuance of bonds for the project in the future under a separate action, 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 repayment is limited to the value of the property and the project revenue sources. The developer is responsible for the payment of all costs under the financing, including the Housing Commission's annual fees.

Project Narrative

Fox Hollow Apartments is a 96-unit new construction project, located in San Diego, California at 4366 Home Avenue just east of Interstate 805 and north of Highway 94. The project will be well suited for large families with 50% of the units consisting of three- and four-bedroom units. The project is located in a residential area with convenient access to schools, recreation, transportation and employment centers. The project is also a part of the City of San Diego's City Heights Redevelopment Plan. The location map is included as Attachment 3.

The proposed development will have 15 residential buildings consisting of two, three, and four bedroom units with unit sizes of 820 sf, 1,000 sf, and 1,200 sf respectively.

The buildings will be of wood frame construction with a stucco exterior finish and red concrete tile roofs. Window and sliding glass doors will be duo-glazed, set in aluminum frames. Kitchens will include garbage disposals, energy efficient appliances and frost-free refrigerators. Each unit will include an individual gas-fired water heater. Exterior paint will be earth tones with additional accent features. Each unit will have a covered balcony and separate balcony as well as private entrances.

The proposed development project is located on 14.48 acres, including County tax assessment parcels 541-650-46, 541-650-47, 541-650-48. Two hundred and sixteen parking spaces will be provided on site, including 96 covered and 120 uncovered spaces. All parking will be on an asphalt covered on grade surface.

Property amenities will include a 2,100 sf recreation building, barbecue area, adult swimming pool, tot lot with a children's pool and sunshades surrounding the recreation area as well as general open areas for both adults and children. The recreation area including the children's play areas totals 6,775 sf. Three laundry rooms will be available on site, each with five washers and five dryers and folding tables.

The project is owned by San Diego/Fox Hollow L.P. with Alpha III, Inc as the general partner. Community Housing Assistance Program (CHAPA), a qualified non-profit, is the managing general partner. The project developer is Alpha III Development, Inc, which is controlled by Charles Ashley. The limited partner is Boston Capital.

The project received a "9%" tax credit allocation in 1998. The developer was not, however, able to meet the tax credit deadline that required the issuance of Certificates of Occupancy for all units by December 31, 2000. As a result, the owner turned back the "9%" credits to California Tax Credit Allocation Committee in December 2000 with the project approximately 50% complete.

The owner/developer has determined that in order to complete the project and preserve the affordability, the clearest course is to restructure the project and finance the project with tax-exempt debt and "4%" tax credits. Under this scenario, a new limited partnership would be formed that would include Alpha III, Inc as the general partner and a new limited partner. The combination of the tax-exempt debt and the tax credits would refinance the project's construction costs incurred to date and provide financing to complete construction.

Alternate options would include application for "9%" tax credits in mid-2001 or utilizing 501(c)3 bonds. The "9%" option is less desirable due to the intense level of competition for a scarce resource and, therefore, a lower likelihood of success. The 501(c)3 option

requires the owner to compromise affordability at the 50% and 60% of median income range for much higher rents that support the financing structure.

Based on CDLAC's scoring criteria, the project is well positioned to receive a tax-exempt debt allocation in April 2001. In the unlikely event the project is not successful in receiving a tax-exempt allocation, the owner will pursue additional sources of "soft" equity that could provide additional support to a "9%" application to be submitted in mid-2001. Additionally, the owner will consider applying for tax-exempt debt in following rounds.

### Selection of the Financing Team Members

The financing team members for the proposed financing 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 among the firms previously selected through a competitive RFP process. The recommended firms are: Dain Rauscher Incorporated as financial advisor, Stradling Yocca Carlson & Rauth as bond counsel and Newman & Associates, Inc. as bond underwriter.

### Rents and Affordability Levels

Ninety percent of the project (85 units) is to be set-aside for occupancy by low-income tenants earning 60 percent or less of the area median income (\$32,220 for a four-person household) for 55 years. The remaining ten percent of the units (10 units) will be set-aside for occupancy by low-income tenants earning 50 percent or less of the area median income (\$26,850 for a four-person household) at rents restricted at the corresponding affordability level for 55 years. The restricted rents would also apply if Section 8 tenants occupy the units.

The proposed rent schedule for the project is outlined in the following chart.

### **FOX HOLLOW APARTMENTS**

Type	Sq. Ft.	AMI	Number of Units	Average Current Rents*	Proposed Restricted Rent	Market Rate	Savings
2 Bedroom	820	50% AMI	6	NA	\$604	\$963	\$359
3 Bedroom	1,000	50% AMI	3	NA	\$671	\$1143	\$472
4 Bedroom	1,200	50% AMI	2	NA	\$725	\$1415	\$690
2 Bedroom	800	60% AMI	42	NA	\$645	\$963	\$318
3 Bedroom	1,000	60% AMI	25	NA	\$725	\$1143	\$418
4 Bedroom	1,200	60% AMI	18	NA	\$806	\$1415	\$609
<b>Total</b>			106				

\* New construction; no existing rents available

## RISKS AND MITIGATIONS

Approval of the resolutions does not commit the Housing Authority to issue bonds. The recommended actions do not represent any commitment by the Housing Commission, Housing Authority or the applicant to proceed with the tax-exempt financing of the project. When eventually issued, the financing risks would be minimal since a third party would guarantee repayment of the bonds.

## ALTERNATIVE

Do not recommend approval of the TEFRA resolution. If the recommended actions are not taken, the project will not be able to benefit from the tax-exempt below-market financing and the applicant would have to seek alternative financing sources for the project.

Respectfully submitted,

Pat Duplechan  
Director, Housing Programs

Approved by,

Elizabeth C. Morris  
Chief Executive Officer

**Signature on File  
With Original Document**

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- Attachments: 1. Bond Program Description and Actions to be Taken  
2. Developer's Statement for Public Disclosure  
3. Project Location Map

## ATTACHMENT 1

### HOUSING COMMISSION'S 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, nearly \$400 million in outstanding bonds provides permanent financing for more than 6,900 multifamily rental units in the City, of which 2,373 units are restricted at various levels of affordability.*

The Housing Commission's policy for the issuance of bonds requires 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.

#### **Actions that must be taken by the Housing Authority and by the City Council to initiate 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 Commission, 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. In the case of the Fox Hollow Apartments, the California Statewide Communities Development Authority will issue the inducement resolution and will subsequently transfer its resolution to the San Diego Housing Commission.

##### **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.