



Good Neighbors

San Diego
Housing Commission

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REPORT

DATE: For the Agenda of June 1, 2001 **ITEM 107**

REPORT NO: HCR01- 069

SUBJECT: Issuance of Multifamily Housing Revenue Bonds for Acquisition and Rehabilitation of Harbor View Villas (Council District 4)

SUMMARY

Issue: Should the Housing Commission recommend that the City Council take the initial step towards issuance of taxable and tax-exempt revenue bonds for acquisition and rehabilitation by Avalon Communities of the 60-unit Harbor View Villas located at 404 North 47th Street, San Diego, CA 92102?

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 \$4,500,000 for the project; 2) approve CSG Advisors Incorporated as financial advisor and Quint & Thimmig, LLP as bond counsel; and 3) recommend that the Housing Authority's final approval of the project is subject to the Housing Commission's approval of the roles and responsibilities of the locally based non-profit Managing General Partner, as well as the locally based managing agent.

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 (54 units) are to be set aside for occupancy by low-income tenants earning 60 percent or less of the area median income (\$34,140 for a four-person household) for 55 years. The remaining ten percent of the units (6 units) will be set-aside for occupancy by low-income tenants earning 50 percent or less of the area median income (\$28,450 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.

Community Planning Group Review: The project was presented to the Encanto Neighborhoods Community Planning Group on May 21st. Due to the preliminary nature of the project, the Planning group recommends that the Housing Authority (as part of a future related action – see below) does not authorize the issuance of bonds to the project until such time as Avalon Communities meets again with the group to present a more substantive presentation detailing the rehabilitation and management plans for the project.

Previous Related Action(s): None.

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 when details regarding the project's financing structure and rehabilitation and management plans have been developed further.

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's tax-exempt borrowing status to pass on lower interest rate financing to developers of affordable housing. Some projects require both forms of assistance. The project developer intends to apply for a Housing Commission loan in addition to the bonds. 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 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 this year and \$75 in 2002.

The Housing Authority benefited from this increase, as evidenced by its recent receipt of bond allocation authority from CDLAC for six of seven first round applications submitted on February 21, 2001.

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 on June 1, 2001.

In order to meet the June 1st CDLAC application deadline, the developer requested that the California Statewide Communities Development Authority (CSCDA) issue the inducement resolution and serve as the applicant to CDLAC. CSCDA will subsequently transfer its resolution to the San Diego Housing Authority.

CSCDA 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 September 2001 CDLAC allocation meeting, proof of the TEFRA hearing must be submitted to CDLAC prior to July 1, 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 financing is described in *Attachment 1*.

DISCUSSION

Harbor View Villas is currently owned by Davidson Housing Family Partnership (Benjamin and Kathleen Davidson). The applicant and developer, Avalon Communities, LLC (Avalon) has entered into a purchase and sale agreement with the current owners to purchase the property for \$4,200,000.

Avalon is a development company that seeks to provide affordable housing throughout the Western United States. Leo Puig, a co-founder of the firm, heads Avalon. Since its inception in 1997, Avalon has developed six properties totaling 511 units. The Developer's Statement for Public Disclosure is included as *Attachment 2*.

PROJECT NARRATIVE

Harbor View Villas is a 60-unit apartment complex located at 404 N. 47th Avenue in the southeastern section of the City of San Diego. The immediate neighborhood consists primarily of single and multifamily residences. To the North are multifamily apartments; a trolley stop to the immediate South; mobile homes are located to the East; and to the West is a canyon providing open space. The property is located near schools, shopping, parks, and medical facilities. The location map is included as *Attachment 3*.

The project is situated on 3.1 acres and consists of 10 two-story residential buildings and 1 office/community building. The apartment complex consists of: 24 two-bedroom, one bathroom; 24 three-bedroom, two bathrooms; and 12 three-bedroom, two and one-half bathroom, townhouse units. The buildings were constructed in 1985. Unit amenities include refrigerators, stoves, ovens, garbage disposals, forced air heating, window coverings and patios/balconies. Site amenities include a computer lab, tot lot, security gates and lighting, on-site laundry facilities, and picnic areas.

The rehabilitation of the units is expected to commence shortly after closing on the bonds and will take approximately six to eight months to complete. The rehab will be scheduled as an "in-place" rehab, mitigating the need for tenant relocation. The scope of work will include repair or replacement of all appliances, flooring, cabinets, countertops, fixtures, doors and also painting of the interiors. All major building systems, roofs, building exteriors, and landscaping will be repaired or replaced as needed.

The entire 60 units in the project would be set-aside for occupancy by low-income renters. Ten percent of the units (6 units) would be affordable to households earning 50 percent of MAI; the remaining ninety percent (54 units) would be affordable at 60 percent of MAI. The restricted rents would also apply if Section 8 tenants occupy the units. The Regulatory Agreement that determines the level of affordability for the project would be in existence for 55 years.

The project currently does not have any rent or income restrictions. However, almost half of the current residents receive individual Section 8 vouchers. All of the current tenants will qualify under the propose rent restrictions at the 50% and 60% of MAI levels outlined in the chart below.

HARBOR VIEW VILLAS

Type	MAI	Sq. Ft.	Number of Units	Restricted Rent (net of utility allowance)	Current Project Rents	Market Rate	Savings
Two Bdrm	50% MAI	850	2	\$568	\$700 (Avg.)	\$850	\$282
Two Bdrm	60% MAI	850	21	\$696	\$700 (Avg.)	\$850	\$154
Two Bdrm *	N.A.	850	1	\$0	N.A.	N.A.	N.A.
Three Bdrm	50% MAI	1,100	4	\$652	\$820 (Avg.)	\$950	\$298
Three Bdrm	60% MAI	1,100	32	\$800	\$820 (Avg.)	\$950	\$150
Total Units			60				\$9,790

*Indicates Manager's unit

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: CSG Advisors Incorporated as financial advisor and Quint & Thimmig, LLP as bond counsel.

FINANCING STRUCTURE

The financing structure has not yet been determined. However, it would involve either publicly offered credit enhanced bonds or private sale of the bonds to an institutional investor. Staff and the financing team will work with Avalon to determine the most appropriate financing structure for the transaction.

Should a public offering structure be pursued, the bond-financed loan would be underwritten utilizing Federal National Mortgage Association ("Fannie Mae") or Federal Home Loan Mortgage Corporation ("Freddie Mac") credit enhancement resulting in an AAA rating of the bonds.

Should a private offering structure be pursued, staff and the financing team will ensure that it conforms to the Housing Commission's Bond policy. Under private placement, the minimum rating requirement of "A" or its equivalent by recognized rating agencies would be waived if the entire bond issue is privately placed with an institutional investor who would be required to sign an investor letter ("Investor Letter") certifying the investor's sophistication to understand the risk associated with the

purchase of the debt instrument. While the note for the bonds remains unrated, its transferability would be restricted to an institutional investor who signs the Investor Letter. The holder of the tax-exempt note would agree that, should a mortgage default occur, there would not be a bond default. A default under the mortgage loan (including default due to non-payment) would not result in a bond default. In case of default under the mortgage loan, the bondholder would have the ability to accelerate and "redeem" the bonds in exchange for the ownership of the project.

The bond financing would qualify the projects for allocation of 4% low-income housing tax credits, which would be sold to a tax credit partner. These proceeds would serve as a contribution of project equity. Avalon, and its nonprofit partner (to be determined) will act as co-managing general partners of a yet to be formed tax credit limited partnership. The roles and responsibilities of the locally based nonprofit managing general partner, as well as the locally based managing agent, are subject to the approval of the Housing Commission. A tax credit investor will comprise the limited partner.

The total anticipated development costs for the project is approximately \$6.2 million. The permanent first position funding will be tax-exempt permanent bond financing for the approximate amount of \$3.7 million (\$800,000 lower than amount sought for bond inducement as it is anticipated that this portion of the bonds will be paid down after the rehabilitation is completed from tax credit). The total equity assumed from the sale of 4% tax credit is approximately \$1.8 million. Avalon will defer \$700,000 in fees. The developer has also expressed a desire to seek a loan from the Housing Commission for additional enhancements to the project. In addition to Loan Committee, Housing Commission, and Housing Authority approvals, such loan would be subject to Housing Commission underwriting standards and availability of funds.

RISKS AND MITIGATIONS

If the application for bond allocation is unsuccessful, the TEFRA resolution allows the issuer (CSCDA or the Housing Authority), up to one year from the date of the public hearing, the option of resubmitting, at the request of the developer, another application for bond allocation at the subsequent allocation round. Once the project receives an allocation, CSCDA will transfer its inducement resolution to the San Diego Housing Authority and the project will return to the Housing Commission and Housing Authority for approval to issue the bonds.

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 project revenue sources. The developer is responsible for the payment of all costs under the financing, including the Housing Commission's annual fees.

City Council approval of the TEFRA resolution does not commit the Housing Authority to issue bonds. The recommended action does not represent any commitment by the Housing Commission, Housing Authority, City Council, CSCDA 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, *Signature on File* Approved by,

With Original Document

Pat Duplechan
Director, Housing Programs

Elizabeth C. Morris
Chief Executive Officer

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

* Limited distribution. Copies are available for review at the San Diego Housing Commission office located at 1625 Newton Avenue and at the Office of the City Clerk, 2nd Floor, 202 "C" Street.

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 \$470 million in outstanding bonds provides permanent financing for more than 7,900 multifamily rental units in the City, of which 3,203 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.

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 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.

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

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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.