



Good Neighbors

San Diego
Housing Commission

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REPORT

DATE: For the Housing Commission Agenda of June 22, 2001

REPORT NO.: HCR01-078

Item No. 102

SUBJECT: Loan Subordination for the Sara Frances Hometel
Located at 943 Tenth Avenue (Council District 2)

SUMMARY

Issue: Should the Housing Commission approve the owner's request to subordinate two development loans, totaling \$566,738, to a refinance of the property that will provide cash to the owner of approximately \$522,000?

Recommendation: That the Housing Commission allow the refinance in return for 27 additional restricted units that will be affordable to persons earning 35 percent or less of median area income (MAI).

Fiscal Impact: No additional Housing Commission funds will be needed to complete this transaction.

Affordable Housing Impact: Approval of the recommended action will increase the number of affordable units at the Sara Frances Hometel from 48 to 75 units, restricted to a level that is affordable to persons earning 35 percent or less of MAI.

Previous Related Action(s): On December 12, 1986, the Housing Commission conceptually approved two loans to Seymour and Sara Frances Reichbart for the development of a new single room occupancy hotel. On June 19, 1989, the Housing Commission approved the extension of the due date on the \$250,000 loan to April 1997. On February 24, 1997, the Housing Commission approved the restructuring of the loans to 30-year terms, fully amortized at three percent interest.



BACKGROUND

The Sara Frances Hometel, located at 943 Tenth Avenue, is a four-story building over a partial basement, 158-room single room occupancy (SRO) residential hotel. The rooms range in size from: 20-units at 80 square feet, 76-units are 110 to 135 square feet, 41-units are 140 to 160 square feet and 21-units are 170 to 220 square feet. All but 45 units have private bathrooms. There are common restroom facilities on each floor and central laundry rooms and kitchens on two floors. The project offers security entry, lobby area, open courtyard and a full time room attendant.

In April 1987, the Housing Commission funded two loans totaling \$625,000 for the construction of the SRO to Seymour and Sara Frances Reichbart. One loan in the amount of \$375,000 had a term of 10 years with options to extend in five-year increments for a total of 30 years with a three percent interest rate. The loan required annual interest only payments. The loan was supported by an agreement to set-aside 20 percent of the rooms for persons earning 40 percent or less of MAI.

The second loan, in the amount of \$250,000, had a term of three years with an interest rate of six percent and annual interest only payments. This loan was supported by an agreement to set-aside 10 percent of the rooms for persons earning 40 percent or less of MAI. The original intent was that this loan would be paid in full through the refinancing of the property upon completion of the construction. Subsequent refinancing did not provide sufficient funds to retire the \$250,000 loan, and in June 1989, the Housing Commission agreed to extend the due date to correspond with the original due date on the \$375,000 loan.

In February 1997, the Housing Commission approved the restructuring of the debt that extended the loan terms for 30 years at three percent interest. The loans are fully amortized, requiring monthly payments totaling \$2,653.03. As a compensation for the loan modifications, the rents on the 48 restricted units were reduced from levels affordable to 40 percent to 35 percent of MAI.

The existing encumbrances against the property are:

1st TD - Wells Fargo Bank	\$ 959,420
2nd TD - San Diego Housing Commission	<u>566,738</u>
TOTAL ENCUMBRANCES	\$1,526,158

Based on a narrative appraisal completed in June 2001, the “as-is” market value of the property is \$5,150,000. The appraiser stated the overall quality and condition of the subject property is above average.

DISCUSSION

On May 31, 2001, Housing Commission staff received a letter from Mr. Reichbart requesting the Commission subordinate its loans to the refinancing of the property. The new loan, in the amount of \$2,000,000, will be used to payoff the existing senior lien in order to reduce the interest rate from 9.50 to 7.875 percent. In addition, a loan secured by another property will be paid in full with the proceeds. As shown on the Borrower Estimated Closing Statement (Attachment 1), the owner will derive approximately \$522,000 in cash from this transaction. Mr. Reichbart states he intends to use \$275,000 of the proceeds for improvement to the subject property (Attachment 2 – Capital Improvements and Upgrades).

Pursuant to the Loan Agreement dated April 14, 1987, the Housing Commission agreed to subordinate its liens, two times only, to secure permanent financing once the construction of the Sara Frances Homotel was completed and to execute and acknowledge any and all documents necessary to effectuate the subordination. The terms and conditions of the subordinations were specifically stated in the Agreement including: 1) the total loan-to-value cannot exceed 90 percent of the appraised value or \$2,700,000; and 2) proceeds of the new financing shall be used solely and exclusively for payment in full of the loans being retired, payment of actual cost to obtain the financing and payment of capital improvements previously approved in writing by the Commission. On August 22, 1989, the Housing Commission allowed the recording of two subordination agreements in accordance with the terms and conditions of the Loan Agreement.

It has been the Housing Commission’s practice to subordinate its loans to the refinance of a senior lien in order to reduce the interest rate or if the lien has become all due and payable. In no cases has the Commission allowed a borrower to receive any cash from the transaction or payoff other debt (including revolving or installment loans).

While subordinating to a refinance whereby the borrower obtains additional cash from the transaction has not been a practice of the Housing Commission, staff is requesting Board consideration of Mr. Reichbart’s proposal to refinance his existing first trust deed loan to new financing not to exceed \$2,000,000. If the requested subordination is

granted, the resulting loan-to-value would be 50 percent, leaving the Housing Commission in a secure position. Staff is recommending approval of the subordination contingent upon it furthering a public purpose, that of restricting an additional 27 units resulting in a total of 75 units affordable to persons earning 35 percent of MAI.

ALTERNATIVES

Deny the owner's request to subordinate the development loans to a refinance the property.

Respectfully submitted,

Steven L. Mikelman
Director of Operations

**Signature on File
With Original Document**

Approved by,

Elizabeth C. Morris
Chief Executive Officer

Monce (Reichbart Subordination. HC)

Attachment(s): 1 – Borrower Estimated Closing Statement
2 – Capital Improvements and Upgrades