



Good Neighbors

San Diego
Housing Commission

REPORT

DATE: For the Housing Authority Agenda of February 13, 2001

REPORT NO: HAR01-002

SUBJECT: Issuance of Multifamily Housing Revenue Bonds for Projects with Previous Related Actions (Council Districts 1,4,6)

SUMMARY

Issue: Should the Housing Authority take the *intermediate steps* to issue tax-exempt and taxable housing revenue bonds to finance the acquisition, rehabilitation, and construction of three projects located in Council Districts 1, 4, and 6 for which the Housing Authority has previously approved Housing Authority loans as well as tax exempt bond financing?

Recommendation: The Housing Commission recommends that:

- A. The Housing Authority approve **Applications** to Round 1 and, if necessary, Round 2, of the State's 2001 allocation rounds for bond issuing authority for the following three projects:
1. Conversion of \$3 million in taxable bonds to tax-exempt bonds for the 504-unit **Canyon Rim Apartments** (formerly known as Penasquitos Gardens) located at 10931 Gerana Street (Council District 1),
 2. Conversion of \$805,000 in taxable bonds to tax-exempt bonds for the 312-unit **Stratton Apartments** (formerly known as Mt. Aguilar Apartments) located at 5765 Mount Alifan Drive (Council District 6); and
 3. Permanent financing of approximately \$4.2 million for the 70-unit **Summit Crest Apartments** (formerly known as Mayberry Apartments) located at 4328-4490 Mayberry Street (Council District 4).
- B. The City Council hold a public hearing (known as a TEFRA hearing -Tax Equity and Fiscal Responsibility Act) and adopt resolutions approving the issuance of bonds by the Housing Authority for the abovementioned three Projects.



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Fiscal Impact: Each project developer is responsible for the payment of all costs under the financing for their project.

Housing Affordability Impact: Each of the three projects will restrict, at a minimum, 10% of the apartments for occupancy by families earning no greater than 50% Median Area Income (MAI), which is \$26,850 for a family of four; and at least 30% of the remaining units for families earning no greater than 60% MAI, which is \$32,220 for a family of four. Each project is subject to additional affordability requirements, varying from site, as described below, and illustrated in *Attachment 3*. The affordability restrictions will remain in place for 55 years.

Previous Related Actions: The **Canyon Rim Apartments**, **Stratton Apartments**, and **Summit Crest Apartments** each have Inducement and TEFRA resolutions previously approved by the Housing Authority and the City Council, respectively. However, the length of time from the previous TEFRA approvals to the proposed issuances in early summer of 2001 might exceed the twelve-month “shelf life” of a TEFRA resolution. Therefore, a recommendation to provide for more recent TEFRA resolution approvals is included in Issue No. 1. In addition, the Housing Commission has previously approved financing teams and the Housing Authority has previously authorized Housing Commission loans for each of these three projects. The Housing Authority has issued bonds totaling \$32,440,000, and \$19,825,000 for Canyon Rim and Stratton, respectively. See *Attachment 2* for more detail.

Future Related Action(s): Specific authorization to issue bonds for **Summit Crest Apartments** will be sought from both the Housing Commission and the Housing Authority at future dates (Refer to *Attachment 1*, Section 4 “Final Bond Approval”).

Also, should new TEFRA resolutions be required for any of the three projects, staff would request that the City Council hold the abovementioned public (TEFRA) hearing for the respective project.

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. Some projects require both forms of assistance, as is the case for each of the three

projects described in this report. However, 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.

Prior to the CDLAC funding rounds, projects are grouped and brought to the Housing Commission, Housing Authority, and City Council; all necessary approvals must be obtained prior to Round I application submittal on February 21, 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*.

PROJECT NARRATIVES

Canyon Rim and Stratton Apartments

FF Canyon Rim, LLC., the developer and applicant for Canyon Rim Apartments, and FF Stratton, LLC, the developer and applicant for Stratton Apartments, are requesting that the Housing Authority take the initial steps to issue tax-exempt debt to retire taxable debt issued for these projects last year by the Housing Authority. The partners for each project consist of the same entities – Paramount Financial Group is a tax credit investor serving as the limited partner with a 99% interest; Wakeland Housing and Development Corporation is a 501 (c) (3) nonprofit entity serving as the managing general partner with a 0.1% interest; and FF Canyon Rim, LLC and FF Stratton, LLC are single asset entities 100% owned by Fairfield Residential, LLC, which is serving as the administrative general partner with a 0.9% interest. The Developer’s Statement for Public Disclosure is included as *Attachment 4.1*.

Canyon Rim and Stratton Apartments are in need of an increase of allowable tax-exempt debt of \$3 million and \$805,000, respectively, to replace the loss of tax credit equity resulting from a HUD imposed mixed income requirement on the properties. The issuance of additional tax-exempt debt, if approved, would retire the same amount of taxable debt issued last year.

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Last year, the Housing Authority issued \$29.5 million dollars in tax-exempt and \$3 million in taxable bonds to allow FF Canyon Rim, L.P. to acquire and rehabilitate the 504-unit property located at 10931 Gerana Street in Council District 1 (the location map is included as *Attachment 4*). The Authority also issued \$17.5 million in tax-exempt and \$2.5 million in taxable debt to allow FF Stratton L.P. to acquire and rehabilitate the 312-unit property located at 5765 Mount Alifan Drive in Council District 6 (the location map is included as *Attachment 5*). In addition, junior financing of \$1,565,000 and \$1,565,000, respectively, were made available by the Commission to these developments.

The actions requested in this report were approved previously by the Housing Commission and Housing Authority at its meeting of May 19, 2000 and June 6, 2000, respectively. Staff subsequently submitted an application to the state, on behalf of the developer, for bond allocation. The application for Canyon Rim was unsuccessful while the application for Stratton Apartments was partially successful - the State provided an allocation of \$1,420,810 to Stratton Apartments, \$805,000 less than the amount sought. Accordingly, the developer has requested that the Authority reapply to the state for allocations to both projects.

Existing resolutions and bond documents executed by the Housing Authority for both Canyon Rim and Stratton Apts. authorize the conversion of taxable bonds to tax-exempt bonds without further resolutions by the Authority. Pursuant to these documents, \$1,420,810 in taxable bonds for the Stratton Apts. project will be converted to tax-exempt bonds on February 15, 2001. The state's award letter is included as *Attachment 6* and the Financial Advisor's analysis of the conversion and recommendation to proceed is included as *Attachment 7*.

Seventy percent of the units in the projects (354 units at Canyon Rim Apts. and 220 units at Stratton Apts.) have been set-aside for occupancy by low-income renters. Ten percent of the units (51 units at Canyon Rim Apts. and 32 units at Stratton Apts.) are affordable to households earning 50 percent of MAI (\$26,850 for a family of four) and sixty percent are affordable at 60 percent of MAI (\$32,220 for a family of four). The Regulatory Agreements, determining the level of affordability for each project, will be in existence until the year 2055. The remaining 30% of the units are at market, as required by HUD. These recommended actions do not alter the original affordability requirements.

Summit Crest

The applicant for Summit Crest Apartments (formerly known as Mayberry Apartments) is Southwest Summit Crest, LLC (Southwest). The principals of Southwest are William J. Zures and Michael A. Cassiola, each having a 50% interest in this limited liability company. The Developer's Statement for Public Disclosure is included as *Attachment 8.1*.

Southwest is requesting that the Housing Authority take the initial steps to issue approximately \$4 million in multifamily revenue bonds to replace interim financing for the 70-unit property located at 4328-4490 Mayberry Street in Council District 4. The location map is included as *Attachment 8*.

In March of 1999, the project's developers borrowed \$670,000 from the Housing Commission to cover a portion of the acquisition cost. At that time, it was envisioned that permanent bond financing would be sought.

The property consists of 70 units (35 2-br/1.5ba, 35 3-br/1.5ba) located in 18 two-story buildings and is situated on a 3.02-acre site. All units have been rehabilitated and provide refrigerators, washer & dryer hook-ups and a fenced patio. The property is located close to downtown, major highways, city buses, shopping and hospitals. It also is situated a few blocks away from the Educational Cultural Complex, which provides job training, and also serves as a sports park complex and senior center.

Twenty-eight units in the project are set-aside for occupancy by low-income renters. Of that total, 30 percent, or 21 units, will be reserved for households earning 60 percent or less of the area median income (\$32,220 for a family of four). The remaining ten percent of the units, 7 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 family of four). The affordability restrictions will remain in place for 55 years. The restricted rents would also apply if the units were occupied by Section 8 tenants.

Like Canyon Rim Apts. and Stratton Apts., the actions requested in this report for this project were approved previously by the Housing Commission and Housing Authority at its meeting of January 22, 1999 and February 16, 1999, respectively. Staff subsequently submitted an application to the state, on behalf of the developer, for bond allocation. That application, which contained within it a proposed financing structure that involved credit enhancement in the form of a guaranty by HUD to create an AAA-rated loan, was successful. However, subsequent to receiving the bond allocation, the Authority learned that HUD policy had changed so that local and

regional HUD officials no longer had discretion to grant the Housing Commission the ability to enforce its rights, as a second position lender, under the loan documents with regards to foreclosure. Given those circumstances, the proposed financing was infeasible. The developer requested that the Authority return the allocation to the state with the intention of reapplying this year, now that a feasible financing structure has been identified.

SELECTION OF THE FINANCING TEAM MEMBERS

The financing team members for the proposed financings 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. Notwithstanding this procedure, for projects that were unsuccessful in obtaining or utilizing bond allocations from prior allocation rounds, financing team members typically are reassigned these projects to complete their work. Accordingly, Dain Rauscher Incorporated (financial advisor) and Stradling, Yocca, Carlson & Rauth (bond counsel) will continue the work they began last year on each of these projects.

FINANCING STRUCTURE

Based on information received from the developers of all three projects, staff expects the financing structure will be the same for each project. It is anticipated that the bond-financed loans will be underwritten utilizing Federal National Mortgage Association ("Fannie Mae") or Federal Home Loan Mortgage Corporation ("Freddie Mac") credit enhancement resulting in a AAA rating of the bonds with equity provided by a tax credit partner.

Subsequent to Housing Commission and Housing Authority approval, staff would submit, on behalf of each developer, applications for Round I private activity bond allocation to the California Debt Limit Advisory Committee (CDLAC) on February 21, 2001. If successful, the bond financing will automatically qualify the projects for the 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. If an application were unsuccessful, at the request of the developer, staff would resubmit the application for the Round II allocation on, or about, June 1, 2001.

In the future, should the Housing Authority under a separate action authorize the issuance of bonds for the projects, the bonds would not constitute a debt or liability of the Housing Authority or the City of San Diego. (The recommendation under Issue No. 2 does authorize a \$1,420,810 bond issuance for **Stratton Apts.**) 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. In addition, the owners of the bonds will agree that, should a mortgage default occur, there would not be a bond default. Should a mortgage default occur, the bondholder or institutional investor (i.e., Fannie Mae or Freddie Mac) would have the ability to redeem the bonds in exchange for the ownership of the project. The developers are responsible for the payment of all costs under the financing, including the Housing Commission's annual fees.

RISKS AND MITIGATIONS

The recommended actions for **Summit Crest Apartments** do not represent any commitment by the Housing Commission, Housing Authority or the applicant to proceed with the tax-exempt financing of that project. However, based on prior resolutions and existing bond documents, the recommended actions for **Canyon Rim Apts.** and **Stratton Apts.** would represent a commitment to proceed with the conversions from taxable to tax-exempt financing. When eventually issued/converted, the financing risks associated with each project would be minimal since repayment of the bonds would be guaranteed by a third party. Additionally, with regards to the **Canyon Rim** and **Stratton** conversions, the reduction in interest costs will serve to enhance the financial strength of each project.

ALTERNATIVE

Do not recommend approval of resolutions authorizing applications to the State for bond allocation, or the TEFRA resolutions, for one or more to the proposed projects. If the recommended actions are not taken for any particular project, that project will not be able to benefit from tax-exempt below-market financing and the applicant would have to seek alternative financing sources.

Respectfully submitted,

Approved by,

Pat Duplechan
Director, Housing Programs

Elizabeth C. Morris
Chief Executive Officer

**Signature on File
With Original Document**

ATTACHMENTS:

1. Description Bond Program and Actions to be Taken
2. Previous Related Actions (All three projects)
3. Affordability Restrictions and Rents

Canyon Rim & Stratton Apartments

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4. Project Location Map (Canyon Rim Apts.)
- 4.1. The Developer's Statement for Public Disclosure (Canyon Rim Apts.)*
5. Project Location Map (Stratton Apts.)
- 5.1 The Developer's Statement for Public Disclosure (Stratton Apts.)*
6. Bond Allocation Letter from the State for Stratton Apts.
7. Financial Advisor's Letter for Stratton Apts.

Summit Crest

8. Project Location Map
- 8.1. The Developer's Statement for Public Disclosure*

*Distribution of this attachment is limited. A copy is available for review at the Housing Commission's 1625 Newton Avenue office.

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 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 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.

ATTACHMENT 2

PREVIOUS RELATED ACTIONS

Canyon Rim Apartments and Stratton Apartments - On October 22, 1999, the Housing Commission approved the bond financing team of Litten Financial and Kosmont & Associates, Inc. (MBE-20%) as financial advisor (Mr. Joe Litten, the Principal of Litten Financial has since gained employment with Dain Rauscher, Inc.; Mr. Litten's financial advisory work, initiated prior to January 12, 2000, was transferred to Dain Rauscher, Inc.); Stradling Yocca Carlson & Rauth and Robinson & Pearman (MBE - 20 percent) as bond counsel; and Newman & Associates, Inc. as bond underwriter. A bond inducement resolution, a TEFRA resolution and an application for the allocation of bond issuing authority for the projects was also recommended by the Housing Commission at that time (Report No. HCR 99-113) and approved by the Housing Authority and City Council on November 9, 1999 (Resolution No. R-1028 and Resolution No. R-292437). On May 19, 2000, a new bond inducement resolution, TEFRA resolution and applications for the allocation of bond issuing authority for the projects were recommended by the Housing Commission (Report No. HCR 00-048) and approved by the Housing Authority and City Council on June 6, 2000 (Resolution No. R-1055 and Resolution No. R-293261). Bonds totaling \$32,440,000 and \$19,825,000 have been issued for Canyon Rim and Stratton, respectively.

The Housing Authority, at its February 8, 2000, meeting approved the following two loans to the developer: 1) A three percent loan, amortized over 55 years, in the amount of \$1,565,000 for the acquisition and rehabilitation of Canyon Rim Apts.; and, 2) A three percent loan, amortized over 55 years, in the amount of \$1,565,000 for the acquisition and rehabilitation of the Stratton Apts. (Report No. HCR00-007, Resolution No. R-1039).

Summit Crest - On January 22, 1999, the Housing Commission recommended Housing Authority approval of a \$670,000 loan to finance a portion of the acquisition cost of Summit Crest Apartments and, at that time, also recommended Housing Authority approval of the bond inducement Resolution and the City Council's approval of the TEFRA for the tax-exempt financing of the project (Report No. HCR99-002). The Housing Authority and City Council convened on February 16, 1999 and approved the Housing Commission's recommendations (Housing Authority Resolution Number R-00985 and 00986 and City Council Resolution Number R-291309). The \$670,000 loan was drawn down, and no bond financing has yet been finalized.

ATTACHMENT 3

AFFORDABILITY REQUIREMENTS AND RENT STRUCTURE

Canyon Rim Apartments		HUD Restrictions July 2000 to Nov. 2011	Affordability Restrictions November 2011 to July 2055			
Type	Square Footage	Number of Units	Number of Units	Restricted Rent (net of utility allowance)	Market Rate	Savings
2 Bedroom @ 50% MAI	795	213	44	\$552	\$920	\$368
2 Bedroom @ 60% MAI	795	95	264	\$673	\$920	\$247
2 Bedroom @ market	795	*132	132	N/A	\$920	N/A
3 Bedroom @ 50% MAI	889	31	7	\$604	\$1055	\$451
3 Bedroom @ 60% MAI	889	14	39	\$739	\$1055	\$316
3 Bedroom @ market	889	*19	18	N/A	\$1055	N/A
Total:		504	504			\$96,881

* Units may be rented to households of any income, but the rents must be restricted to be affordable at 85% MAI.

Stratton Apartments		HUD Restrictions July 2000 to Nov. 2011	Affordability Restrictions November 2011 to July 2055			
Type	Square Footage	Number of Units	Number of Units	Restricted Rent (net of utility allowance)	Market Rate	Savings
2 Bedroom @ 50% MAI	691	146	28	\$552	\$900	\$348
2 Bedroom @ 60% MAI	691	47	166	\$673	\$900	\$227
2 Bedroom @ market	691	**83	82	N/A	\$900	N/A
3 Bedroom @ 50% MAI	924	19	4	\$604	\$1050	\$446
3 Bedroom @ 60% MAI	924	6	22	\$739	\$1050	\$311
3 Bedroom @ market	924	**11	10	N/A	\$1050	N/A
Total:		312	312			\$56,052

** Units may be rented to households of any income, but the rents must be restricted to be affordable at 85% MAI.

Summit Crest Apartments

Type	Square Footage	Number of Units	Restricted Rent (net of utility allowance)	Market Rate	Savings
2 Bedroom @ 50% MAI	840	4	\$529	\$750	\$221
2 Bedroom @ 60% MAI	840	3	\$554	\$750	\$196
2 Bedroom @ 60% MAI	840	7	\$615	\$750	\$135
2 Bedroom @ Market	840	21	N/A	\$750	N/A
3 Bedroom @ 50% MAI	1009	3	\$582	\$850	\$268
3 Bedroom @ 60% MAI	1009	4	\$650	\$850	\$200
3 Bedroom @ 60% MAI	1009	8	\$710	\$850	\$140
3 Bedroom @ Market	1009	20	N/A	\$850	N/A
Total:		70			\$5,141