

REPORT

DATE ISSUED: July 2, 2008 REPORT NO: HCR 08-58
ATTENTION: Chair and Members of the Housing Commission
For the Agenda of July 9, 2008
SUBJECT: Amendments to the Multifamily Mortgage Revenue Bond Policy (Citywide)

REQUESTED ACTION:

Recommend approval and forward to the City Council's Budget and Finance Committee the following changes to the Multifamily Mortgage Revenue Bond Policy.

STAFF RECOMMENDATION:

Housing Commission recommend Housing Authority approval of proposed amendments to the Multifamily Mortgage Revenue Bond Policy in the following two areas: 1) amend the requirements for unrated private placements to address current market practices; and 2) delegate authority to the President and Chief Executive Officer of the Housing Commission to streamline the bond initiation process in order to better serve the affordable housing development community. Additional changes have been made to the formatting and organization of the policy. The amended policy is included as Attachment 1.

BACKGROUND:

The Housing Commission's Multifamily Mortgage Revenue Bond Program (Bond Program) has been utilized since 1982 to support the development of affordable housing in the City of San Diego. Since inception, the Bond Program has issued approximately \$1 billion in tax-exempt bonds to provide below-market rate financing for affordable housing projects. Currently more than \$600 million in outstanding bonds provide financing for 45 housing communities with a total of 9,107 units—5,821 of which are restricted at various levels of affordability. The Bond Program policy has been regularly updated to respond to changes in the regulatory environment and to remain a useful incentive to produce affordable housing within the City.

The Bond Program is able to provide below-market rate financing because interest earnings on bonds issued for eligible projects are, in general, exempt from state and federal income taxes. Bonds issued under the Bond Program can also qualify projects for allocations of federal low-income housing tax credits. Equity from the sale of tax credits can provide a significant portion of the financing necessary to develop affordable housing.

Multifamily housing revenue bonds are also known as "private activity bonds" because the projects are owned by private entities with nonprofit or for-profit sponsors. Although the Housing Authority acts as the issuer of the bonds, there is no financial liability to the City, the Housing Authority, or the Housing Commission in connection with the issuance or repayment of bonds. The bonds are special, limited obligations of the Housing Authority payable solely from private revenue sources, such as project cash flows and equity payments. Moreover, the Housing Commission receives fees to pay for the staff time necessary to prepare bond issuances and administer the Bond Program.

Under federal and state law, to be eligible for bond financing, projects must set aside at least 20% of their units for occupancy by, and one-half of these units must have rents affordable to, households earning no more 50% of Area Median Income (AMI) (\$39,500 for a family of four). Alternatively, a minimum of 10% of the units may be restricted at 50% AMI with an additional 30% of the units restricted at 60% AMI (\$42,660 for a family of four). Due to the combined requirements of state, local, and federal funding sources, projects financed under the Bond Program are normally affordable for 55 years and often provide deeper affordability levels than the minimum levels required under the Bond Program.

Private Placement Policy

The Bond Program policy currently permits unrated private placements if the following conditions are met:

1. The entire bond issue is privately placed with an institutional investor who would be required to sign an investor letter certifying that they understand the risks associated with the purchase of the bond issue.
2. The transfer of the bonds by the initial institutional investor or any subsequent bondholder should be restricted to transferees who would take all of the bonds (to maintain ownership by a single bondholder), and who would represent to the Authority and the Commission that they are sophisticated investors, are buying for investment and not for resale and have made due investigation of the information they would deem material in connection with the purchase of the bonds.
3. 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) shall not result in a bond default. In case of default under the mortgage loan, the bondholder shall have the ability to accelerate and “redeem” the bonds in exchange for the ownership of the project.

Recommendation #1

Further specify the types of investors that may purchase unrated bonds. The current policy allows “institutional investors” to purchase bonds. However, the term “institutional investor” is not defined in securities law. As a result, staff recommends permitting unrated private placements to qualified institutional buyers (QIBs), as defined under Rule 144A of the Securities Act of 1933, and accredited investors, as generally defined under Regulation D of the Securities Act of 1933. Please see Attachment 2 for the definition of QIBs and accredited investors from the Securities Act.

Recommendation #2

Permit unrated private placements in minimum denominations of \$100,000 or greater, rather than requiring the entire bond issue to be purchased by a single investor and, unless otherwise approved by the Housing Authority, limit the number of investors to 15. In addition, bonds may be placed in a trust or custodial arrangement with participations sold to investors upon terms acceptable to the Housing Authority.

Under current market conditions, investors are sometimes unwilling or unable to purchase the entire bond amount, especially for larger projects. The recommended change would make more capital available to the Bond Program so that the most competitive interest rates can be offered to affordable housing projects. All investors would have to be qualified institutional buyers or accredited investors, and continue to sign investor letters. The recommended change mirrors policies from other issuers of housing revenue bonds and would be consistent with current City practice for private placements.

Recommendation #3

Remove the third provision of the private placement policy. This provision was included so that bonds issued by the Housing Authority would not go into technical default, avoiding any negative perceptions in the financial markets. Given that housing revenue bonds issued by the Housing Authority are not secured by any City revenues, and market participants are well aware of the financial structure of these transactions, the Housing Commission does not believe that this provision is useful or necessary.

Approval Process Streamlining

The current process for initializing and finalizing bond issuances for affordable housing projects requires multiple actions by the Housing Authority and City Council. Please see Attachment 3 for a summary of the bond approval process.

Bond Inducement Process

Recommendation #4

Delegate approval of the bond inducement resolution to the President and Chief Executive Officer of the Housing Commission (President and CEO). The purpose of the bond inducement resolution is to establish the date from which project costs may be reimbursed from bond proceeds (if bonds are ultimately issued). The bond inducement resolution also permits staff to submit an application to the State of California for an allocation of tax exempt bond issuing authority. Approval of the inducement resolution does not represent any commitment by the Housing Commission to proceed with the financing, nor does it convey approval of the project for the purposes of planning, zoning, or building codes.

This change would align San Diego's practices with those of several large volume housing bond issuers, such as Los Angeles and San Jose. From time to time, developers need quick approval of an inducement resolution in order to preserve an affordable housing opportunity or persuade a seller to agree to work through the processes required for public financing. In addition, securing bond allocations from the State has become increasingly competitive, so submitting funding applications as early as possible is recommended.

The recommended delegation of authority would not lessen the Housing Authority's absolute discretion over the issuance of bonds for projects because the final authorization resolution would continue to be subject to Housing Authority approval. Prior to approval of the final authorization to issue bonds, projects must comply with all applicable financing, affordability, and legal requirements and successfully secure all necessary planning and zoning approvals.

Delegation of authority for approving bond inducement resolutions to President and CEO complies with all relevant sections of the Treasury Regulations and the Internal Revenue Code.

Tax Equity and Fiscal Responsibility Act (TEFRA) Process

To assure that projects making use of tax-exempt financing meet appropriate governmental purposes and provide reasonable public benefits, the Internal Revenue Code requires that a noticed public hearing be held and that the issuance of bonds be approved by representatives of the governmental unit with jurisdiction over the area in which the project is located (i.e. the City Council). Under the current bond approval process, the City Council holds the TEFRA hearing and approves the TEFRA resolution at a single public hearing.

Recommendation #5

Allow staff to conduct the TEFRA hearing separately, and prior to, approval of the TEFRA resolution by the City Council.

Typically, citizen questions or concerns regarding development of a specific project are made known via reports to the community planning group, dialogue with City Council staff, and testimony at Planning Commission or other land use hearings. In addition, the public may express concerns or support at the public hearing (TEFRA hearing) which is required for the issuance of housing bonds.

This amended process would increase access and convenience for public comment. The Housing Commission would hold the TEFRA hearing after publishing a notice in the Daily Transcript (or another newspaper of general circulation within the City) as the City Council does now. The published notice would give interested members of the public a specific meeting date and time, rather than having to attend City Council meetings with multiple agenda items.

All public comments received at the hearing would be presented to the City Council as part of the City Council Report recommending approval of the TEFRA resolution. The presentation of the Report would provide an additional opportunity for public comment and would continue to serve as an opportunity for comment and questions from the members of the City Council.

FISCAL CONSIDERATIONS:

There are no fiscal impacts to the Housing Commission, City, or Housing Authority associated with amending the Bond Program policy. Financing costs for individual projects, including compensation for staff efforts in preparing the bonds, are funded through project development budgets.

PREVIOUS HOUSING AUTHORITY And/Or COMMITTEE ACTIONS:

The Housing Commission's Bond Program policy was originally adopted by the Housing Authority in 1989, and subsequently revised in 1992, 1994, 1996, and 1999.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:

The proposed amendments to the Bond Program policy will be discussed at the next meeting of the San Diego Housing Federation's policy committee.

ENVIRONMENTAL REVIEW:

This activity is not a project within the meaning of the California Environmental Quality Act (CEQA) pursuant to Section 15060(c)(3) of the State CEQA guidelines. This activity is also exempt from review under the National Environmental Policy Act as no federal funding is involved in this action.

KEY STAKEHOLDERS & PROJECTED IMPACTS:

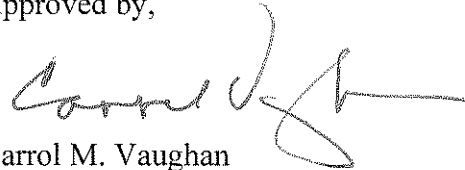
Service to affordable housing developers, prospective low income tenants, and interested members of the public would be improved by implementation of the proposed Bond Program policy amendments.

Respectfully submitted,



Cissy Fisher
Director of Housing Finance & Development

Approved by,



Carrol M. Vaughan
Interim President & Chief Executive Officer

- Attachments:
1. Amended Policy
 2. Definition of QIBs and Accredited Investors
 3. Bond Program Summary

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1. SUMMARY

- 1.1. Federal, state and local legislation authorize issuance of mortgage revenue bonds by local governments to finance the development, acquisition and rehabilitation of multifamily rental projects. The interest on the bonds can be exempt from federal and state taxation. As a result, bonds provide below market financing for qualified rental projects located in the City of San Diego (the "City"). In addition, the bonds issued under the program can qualify projects for allocations of federal low-income housing tax credits, which can provide a significant portion of the funding necessary to develop affordable housing. The program is administered by the San Diego Housing Commission (the "Housing Commission") and uses tax-exempt mortgage revenue bonds issued by the Housing Authority of the City of San Diego (the "Housing Authority").
- 1.2. There is no direct legal liability to the City, the Housing Authority or the Housing Commission in connection with the issuance or repayment of bonds; there is no pledge of the City's or the Housing Authority's faith, credit or taxing power and the bonds do not constitute general obligations of the issuer because the security for repayment of bonds is limited to project revenue and other funding sources specified under each financing. Project loans are, in most cases, secured by a first deed of trust on the bond-financed property. The program is completely self-supporting; developers must secure funding to pay for costs of issuance of the bonds and all other costs under each financing.
- 1.3. Bonds issued under the program may bear interest at a fixed or variable rate as long as they otherwise comply with the requirements of this policy. This flexibility allows affordable housing developers to secure the most cost effective financing available.

Given the financial and legal structure of multifamily mortgage revenue bonds discussed in Section 1.2, the use of variable rate bonds can further leverage the City's resources to develop affordable housing without creating risk for the Housing Authority. Under certain circumstances, variable rate bonds provide cost effective financing for affordable housing projects by reducing borrowing rates, providing flexible debt structuring, minimizing construction interest, and minimizing costs incurred due to different rates on the investment of bond proceeds and interest payable to bondholders (i.e. negative arbitrage). Loans from the Housing Commission and the Redevelopment Agency constitute as much as 25% to 50% of the funding necessary to develop affordable housing, so it is in the City's interest to maximize the use of other funding sources.

- 1.4. Bonds issued under the program should generally be privately placed with a financial institution or rated "AAA", or its equivalent, with a minimum rating being "A", or its equivalent, by the nationally recognized rating agencies listed in Section 4.1. The bonds may be used for both construction or rehabilitation and permanent financing. The effective mortgage rate is the aggregate of the applicable bond rate and the add-on fees charged under the program, such as lender, trustee, issuer's fee, etc. The bond rate, for fixed rate bonds, is determined at the time of a bond sale and the resulting mortgage rate is approximately 1.5% - 2% below conventional mortgage rates. The project loans generally have a 30-year amortization schedule.
- 1.5. The goals of the program include: increase and preserve the supply of affordable rental housing; encourage economic integration within residential communities; maintain a quality living environment for residents of assisted projects and surrounding properties; and, in the event of provision of public funds towards the project, optimize the effectiveness of Housing Commission, Redevelopment Agency, or other public funding by maximizing the leveraging of private sector funds.
- 1.6. There is no limit on the maximum loan amount; however, the minimum loan amount is determined by the overall cost effectiveness of the financing, which includes payment for the costs of issuance,

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services of the financing team members, rating fees, etc. The bond issuance amount for individual projects is based upon project costs, interest rates, and revenues available to pay debt service. The Housing Authority will consider multiple properties as part of a single bond financing on a case by case basis.

- 1.7. Projects must consist of complete rental units, including kitchens and bathrooms. Loan funds may be used for costs of property acquisition (up to 25% of bond proceeds), construction, rehabilitation, improvements, architectural and engineering services, construction interest, loan fees and other capital costs of the project incurred after the bond inducement date specified in Section 7.3. Loan funds cannot be used to acquire property from a party related to the buyer. No more than 2% of any tax-exempt bond loan can be used to finance costs of issuance, such as the services of the financing team members, rating and printing of bonds, bond allocation, etc. Pursuant to federal requirements, if bonds are used for acquisition and rehabilitation, at least 15 percent of the portion of the acquisition cost of the building and related equipment financed with the proceeds of bonds must be used for rehabilitation of the project. The loans are assumable upon transfer of the project with the approval of the credit enhancement provider or bond purchaser, and the President and Chief Executive Officer of the San Diego Housing Commission (the "President and CEO").
- 1.8. The Housing Commission receives compensation for its services in preparing bond issuances by charging an up-front fee payable at the bond closing. In addition, the Housing Commission also receives as compensation for compliance monitoring of regulatory restrictions and the administration of outstanding bonds an annual administrative fee payable in arrears in semiannual or annual installments. The up-front fee and the annual ongoing administrative fee are each equal to 23 basis points (0.23%) of the initial amount of bonds issued. For small projects, a minimum ongoing fee may be charged to recover administrative and monitoring costs.

2. TYPES OF BONDS

- 2.1 The Housing Authority may issue either tax-exempt or taxable bonds. Taxable bonds would generally be issued only in combination with tax-exempt bonds. Taxable bonds do not require an allocation of bond authority from the California Debt Limit Allocation Committee ("CDLAC").

Tax-Exempt Private Activity Bonds (Non-Refunding) require an allocation of bond authority from CDLAC. To obtain the allocation, the Housing Authority must submit an application to CDLAC on behalf of the developer. Submittal of the application is at the discretion of the Housing Authority, not the developer. The developer must pay all required CDLAC fees when due.

The Housing Authority may issue 501(c)(3) bonds on behalf of qualified nonprofit organizations. 501(c)(3) bonds are tax-exempt and do not require an allocation from CDLAC, but cannot be used with the Low Income Housing Tax Credit Program.

The interest on taxable bonds is not exempt from federal taxation. These bonds are not subject to federal volume "cap" limitations and therefore do not require allocation authority from CDLAC. Taxable bonds can be used in combination with low-income housing tax credits awarded by the Tax Credit Allocation Committee. Taxable bond issues must meet all applicable requirements of this Policy (including rating requirements) and any additional regulations that may be promulgated, from time to time, by the Housing Commission.

The Housing Authority will allow refunding of bond issues that meet the following conditions:

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- A. The project sponsor agrees to cover all costs of the issuer.
- B. Projects originally financed by tax-exempt bonds prior to the 1986 Tax Act will have to make a minimum ten percent of the units affordable to persons earning 50 percent of median area income with the rents affordable at the same level.
- C. The affordability restrictions of the existing bond regulatory agreement are subject to extension. The Housing Commission reserves the right to impose additional requirements on a case by case basis. All specifics of refunding proposals must be approved by the Housing Authority.
- D. Default refunding applications require a default refunding analysis (to determine the eligibility for a default refunding). The Housing Commission shall choose the firm to conduct the analysis. The project applicant will deposit the cost for the study with the Housing Commission before the study begins.

3. AFFORDABILITY REQUIREMENTS

- 3.1 Term of Rental and Affordability Restrictions—The project must remain as rental housing and continuously meet the affordability requirements as provided in Sections 3.2, 3.3 and 3.4 for the longer of (a) 15 years from the date of the original issuance or refunding, as applicable, (b) as long as the bonds remain outstanding, (c) such period as may be required in the opinion of Bond Counsel to satisfy applicable federal or State law, or (d) such period as may be required by CDLAC (typically 55 years). The rent of "in-place" tenants at the conclusion of the required affordability period will continue to be governed by the applicable affordability restriction, so long as those tenants continue to live in the development. The Housing Authority reserves the right to impose additional affordability restrictions.

A Regulatory Agreement containing the rental and affordability restrictions will be recorded against the property and must be complied with by subsequent owners. The Regulatory Agreement will be terminated upon expiration of restrictions or in the event of casualty loss or foreclosure, and the subsequent retirement of bonds as a result of foreclosure.

State law requires advance notice and other requirements upon termination of affordability requirements, some of which also place restrictions on the sale of previously affordable housing projects.

- 3.2 Income Restrictions—To be eligible for tax-exempt bond financing, **federal law** requires that the project meet one of the following conditions:

- A. A minimum of 20% of the units in the project must be set aside for occupancy by households whose incomes do not exceed 50% of area median income, as adjusted for family size; or
- B. A minimum of 40% of the units in the project must be set aside for occupancy by households whose incomes do not exceed 60% of area median income, as adjusted by family size.

At the same time, **state law** requires that a minimum of 10% of the units in the project be set aside for occupancy by households whose incomes do not exceed 50% of area median income, as adjusted for family size, at specified rent levels.

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Project owners must certify their tenant's eligibility annually. If a tenant is no longer eligible, the next available unit in the project must be rented to a new eligible tenant and the current tenant's rent can be raised to a market level. A unit occupied only by full time students does not count towards the set-aside requirement.

Affordability definitions are based on the area median income for the County of San Diego as established by the US Department of Housing and Urban Development. The median income is subject to change annually. Household size is determined by adding one person to the bedroom size of the unit.

- 3.3 Rent Restrictions—The maximum rent for one-half of the set-aside units may not exceed 30% of one-twelfth of 50% of area median income, or 30% of one-twelfth of 60% of area median income (as the case may be, depending on the selected set-aside). The maximum rent amounts are further reduced by a utility allowance for tenant-paid utilities in the amounts determined by the President and CEO. In the event tax-exempt bonds are used with Low Income Housing Tax Credits, or any other public funds, the most restrictive rents of the applicable programs shall apply. The affordability of restricted units in relation to the project's market rents will be considered as part of the Housing Commission's approval of the financing. The maximum rent amounts will also apply if the set-aside units are occupied by Section 8 tenants.
- 3.4 Unit Distribution—The set-aside units must proportionately reflect the mix of all units in the project, be distributed throughout the project and have the same floor area, amenities, and access to project facilities as market-rate units. The objective of the program is to provide a set-aside of units with lower rents, not to create special "low-income sections" within larger developments.
- 3.5 Additional Affordability Restrictions under Restructuring of Existing Bond Issues—Additional public benefit in the form of deeper income targeting; additional rent restrictions; extension of the term of restrictions; additional number of restricted units; or any combination thereof, will be negotiated in connection with refundings or debt restructurings of existing bond issues. The level of additional restrictions will be determined in the context of the overall financial feasibility of each financing. The maximum rent amounts will also apply if the set-aside units are occupied by Section 8 tenants. Should the bond restructuring result in an extension of the maturity of the bonds, a minimum of 10% of the units in the project will be set aside for occupancy by households whose incomes do not exceed 50% of area median income, as adjusted for family size, with rents set at the corresponding affordability level, for the term of the restructured bond.

4. CREDIT CONSIDERATIONS

- 4.1 Required Rating on the Bonds—Any bonds issued under the program that are sold to the public should generally be rated "A", or its equivalent, or better from the following nationally recognized rating agencies: Moody's Investors Service, Standard & Poors Corporation, or Fitch Ratings. The same rating requirement applies in the case of a substitution of existing credit facility for bonds which are outstanding.
- 4.2 Credit Enhancement—A preferred way of obtaining the required rating on the bonds in accordance with Section 4.1 is through the provision of additional, outside credit support for the bond issue provided by rated, financially strong private institutions, such as bond insurance companies; domestic and foreign banks and insurance companies; savings and loans and smaller commercial banks willing to pledge ratable collateral to bond trustee; FHA mortgage insurance or co-insurance, etc. The rating on the bonds is determined based on the credit worthiness of the participating credit

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enhancement provider. The applicant is required to identify and obtain credit enhancement for each bond issuance. As the primary source of security for the repayment of bonds, the credit enhancement provider reviews and approves the borrower (credit, financial capability, experience, etc.) and the project and its feasibility, including the size of the loan and the terms of repayment, using their own underwriting criteria.

- 4.3 Rated Bonds Without Credit Enhancement—Fixed rate bonds, or their portion, can be issued without credit enhancement if the proposed financing structure results in the required minimum rating on the bonds by a rating agency as provided in Section 4.1. Bonds issued without credit enhancement will be sold to institutional investors in minimum \$100,000 denominations.
- 4.4 Privately Placed Bonds—The rating requirement specified in Section 4.1 is waived under the following conditions:
- A. The bonds are privately placed with “qualified institutional buyers” as defined under Rule 144A of the Securities Act of 1933, or “accredited investors,” as generally defined under Regulation D of the Securities Act of 1933.
 - B. The bonds must be sold in minimum \$100,000 denominations.
 - C. All initial and subsequent purchasers must be willing to sign a sophisticated investor letter (Investor Letter) in a form approved by the Housing Commission. While the bonds remain unrated, their transferability will be restricted to qualified institutional buyers or accredited investors who sign an Investor Letter.
 - D. Unless otherwise approved by the Housing Authority, the bonds must be sold to 15 or fewer investors.
 - E. Upon terms acceptable to the Housing Authority, bonds may be placed in a trust or custodial arrangement with participations sold to investors.

The purpose of these conditions is to assure that the bonds are placed with investors who are experienced in municipal securities investing and analysis or real estate credit underwriting. Bond funds and affordable lending banks are the types of entities this condition anticipates.

5. OTHER ISSUERS

- 5.1 The Housing Authority, in very limited situations, will allow “other issuers” than the Housing Authority to issue bonds for multifamily housing projects located within the City of San Diego. Any applicant considering the use of any “other issuer” should contact Housing Commission staff prior to proceeding with the project. The required City approvals of bond issuances by “other issuers” will be recommended only if the financing proposal is part of a pooled issuance involving projects located in multiple jurisdictions and the overall cost effectiveness of the financing proposal is increased. All Housing Authority affordability requirements, procedures and requirements will apply to projects using “outside issuers,” including an issuance fee of 0.23 percent of the bond issuance amount to be paid to the Authority upon issuance of the bonds. A TEFRA hearing and approval by the City Council, as described in Section 7.4, on behalf of another issuer will include a provision that the owner, operator or manager of the project considered for financing by tax-exempt debt will not change without the prior approval of the President and CEO.

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6. SELECTION OF THE FINANCING TEAM

- 6.1 Through separate Requests for Qualifications ("RFQ"), a pool of bond counsels, and a pool of financial advisors, will be established to serve as financing team participants on individual bond transactions. The RFQ process is a fair and competitive process which includes advertising, a competitive selection process and interviewing, if necessary. Firms will be selected in accordance with the Housing Commission's applicable equal opportunity policies.
- 6.2 The establishment of each pool will be made by a selection committee with the approval of the Housing Commission Board. The selection committee will consist of Housing Commission staff and representatives from other City departments, such as the City Attorney's Office, City Auditor, and Office of the Chief Financial Officer. Generally, the selection will be made for a two-year period. The term may be extended for two additional one-year periods by the President and CEO.
- 6.3 The bond counsel and financial advisor specifically represent the interests and concerns of the Housing Commission, the Housing Authority and the City of San Diego in ensuring the integrity of the bond transaction. The project sponsor may, at its own expense, add additional members to the finance team to represent its interests.
- 6.4 The Financial Advisor for each transaction will be designated by the President and CEO from the selected pool for approval by the Housing Commission Board on a rotating basis. The Financial Advisor will prepare a feasibility study on whether it is economically advisable to proceed with the financing, including: evaluation of the financial strength of the project; assumptions regarding income and expenses; sources of security for bonds in addition to the project; developer's financial situation and experience in operating and managing rental projects; marketability of the bonds; rights and resources of parties to the transaction in the event of default; and provide financial advice on all relevant issues to best protect the interests of the City and the Housing Authority. The compensation for financial advisory services to determine whether it is advisable to proceed with a financing will not be contingent on the sale of the bonds.
- 6.5 Bond Counsel will be designated for each financing by the President and CEO from the selected pool on a rotating basis subject to approval by the Housing Commission Board. Bond Counsel will prepare the necessary legal documentation, including provisions regarding compliance with any applicable continuing disclosure requirements, provide an opinion regarding the validity of the bonds and their tax exemption, and provide legal advice on all relevant issues to best protect the interests of the City and the Housing Authority.
- 6.6 Bond Underwriter/Remarketing Agent/Private Placement Purchaser—The developer shall select the debt provider and method of selling the bonds for a given transaction subject to the approval of the Housing Commission. The practice of allowing the developer to propose the debt provider and bond structure is intended to create an incentive for qualified financial firms to actively work with developers to structure and present feasible financing proposals that meet program requirements.
- 6.7 In the event the developer has not identified a proposed financing structure for a given transaction, the Housing Commission will select an underwriter or private placement purchaser through a request for proposals process.

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6.8 The Bond Trustee (a bank designated by the Housing Authority as the custodian of funds and official representative of bondholders), if required by the bond structure for the financing, will be approved by the President and CEO based upon a Request for Proposals process.

7. THE FINANCING PROCESS

7.1 Application—A developer interested in new-money financing must submit an application for bond financing or, in the case of an existing financing, a request for bond refunding or restructuring to the Housing Commission. Part of the required information is a disclosure statement on each of the parties involved in the developer/ownership entity. Housing Commission staff will review the application for feasibility.

7.2 Deposit—At the time of the application, the developer must pay an application fee to cover the cost of the feasibility analysis of the proposed bond issuance, reissuance or restructuring. If the financing goes ahead, the fee will be subject to reimbursement as a required cost of issuance at the bond closing. The application fee may be waived by the President and CEO.

7.3 Inducement Resolution—In conjunction with the City Attorney's Office and Bond Counsel, a bond inducement resolution will be drafted and approved by the President and CEO of the Housing Commission. All new-money projects must be induced. An inducement resolution is a conditional expression of the Housing Authority's "official intent" to issue bonds for a given project and is required under Treasury Regulation Section 1.150-2(e) 1.150-2(e). Approval of the inducement resolution establishes, through the public record, the date from which project costs incurred may be determined to be eligible for financing under the program. Therefore, applicants are encouraged to induce their projects as soon as practicable to clearly identify the project, its location, maximum number of units, the maximum amount of financing, and the proposed ownership entity.

A. Application to CDLAC—The inducement resolution also authorizes Housing Commission staff to submit an application to CDLAC, on behalf of the developer/project sponsor, for a private activity bond allocation.

B. No Binding Financial Commitment—Adoption of the inducement resolution does not represent any commitment by the Housing Commission, Housing Authority, or the developer to proceed with the financing. The approval of the inducement resolution, by itself, does not authorize any subordinate financing by the Housing Authority or any other entity of the City. The Housing Authority retains absolute discretion over the issuance of bonds through adoption of a resolution authorizing such issuance.

C. No Land Use or Building Code Approval—Approval of the inducement resolution shall not be construed to signify that the project complies with the planning, zoning, subdivision and building laws and ordinances of the City or suggest that the Housing Authority, the City, or any officer or agent of the Housing Authority or the City will grant any such approval, consent or permit that may be required in connection with the development of a given project

7.4 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

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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. As the legislative body for the City of San Diego, federal regulations require that the issuance of bonds by the Housing Authority be approved by the City Council. The purpose of the 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. The TEFRA hearing will be conducted by Housing Commission staff at the date and time specified in the TEFRA notice. The TEFRA notice shall be published in a newspaper of general circulation within the City. All public comments received by Housing Commission staff at the TEFRA hearing will be presented in writing to the City Council.

- 7.5 Bond Allocation—Prior to the issuance of private activity, tax exempt bonds, the Housing Authority must apply for, and receive an allocation of bond issuing authority from CDLAC. To receive such an allocation, the Housing Authority and the developer must document their readiness to proceed with the bond financing.
- 7.6 Performance Deposit—At the time of the application to CDLAC, the developer must deposit with the Housing Authority one half of one percent of the requested allocation amount as a performance deposit. The deposit will be returned to the developer according to the CDLAC procedures; the deposit is subject to reversion to the CDLAC if the financing does not close according to the CDLAC procedures.
- 7.7 Local Review—All projects must be in compliance with the City's land use requirements and the adopted community plans. Prior to requesting Housing Authority's approval of new-money bond issuance, the project must undergo all planning procedures, discretionary reviews and land use approvals, including review by the local planning group and environmental analysis, as required.
- 7.8 Coordination with City Finance Representatives—Housing Commission staff will work with the City Attorney's Office, the Office of the Chief Financial Officer, and other City departments, as necessary, in preparing bond issuances for affordable housing projects.
 - A. Compliance with City's Disclosure Ordinance—As a related entity of the City, the Housing Commission will adhere to the City disclosure ordinance (O-19320) as it may be amended from time to time. The Housing Commission will present offering statements and disclosure documents for review and approval, as appropriate, by the City's Disclosure Practices Working Group.
- 7.9 Housing Commission/Housing Authority Final Approval—Housing Commission staff's recommendation to proceed with a proposed bond issuance, reissuance, or bond restructuring will be presented for approval by the Housing Commission. If approved, staff will work with the approved financing team to structure the financing and to prepare the necessary bond documents. The resulting bond documents, authorizing resolution, staff report, and other relevant docket materials will be submitted for final approval by the Housing Authority.

[Supersedes PO300.301, effective June 6, 1999]

Authorized:

POLICY

Subject: **MULTIFAMILY MORTGAGE REVENUE BOND PROGRAM**

Number: **PO300.301**

Effective Date: 10/16/89

Page 9 of 9

Carrol M. Vaughan, President and CEO

Cissy Fisher, Director
Housing Finance

Date

Date

History:

Adopted: 10/16/89

Revised: 6/23/92

Revised: 6/28/94

Revised: 5/28/96

Revised: 6/4/99

Revised: 6/25/2008

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Attachment 2
DEFINITIONS

Qualified institutional buyer

Under Rule 144A of the Securities Act of 1933 a qualified institutional buyer shall mean:

- i. Any of the following entities, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least \$100 million in securities of issuers that are not affiliated with the entity:

- A. Any *insurance company* as defined in section 2(a)(13) of the Act;

Note: A purchase by an insurance company for one or more of its separate accounts, as defined by section 2(a)(37) of the Investment Company Act of 1940 (the "Investment Company Act"), which are neither registered under section 8 of the Investment Company Act nor required to be registered, shall be deemed to be a purchase for the account of such insurance company.

- B. Any *investment company* registered under the Investment Company Act or any *business development company* as defined in section 2(a)(48) of that Act;
- C. Any *Small Business Investment Company* licensed by the U.S. Small Business Administration under section 301© or (d) of the Small Business Investment Act of 1958;
- D. Any *plan* established and maintained by a state, its political subdivisions, or any agency or instrumentality of a state or its political subdivisions, for the benefit of its employees;
- E. Any *employee benefit plan* within the meaning of the title I of the Employee Retirement Income Security Act of 1974;
- F. Any trust fund whose trustee is a bank or trust company and whose participants are exclusively plans of the types identified in paragraph (a)(1)(i)(D) or (E) of this section, except trust funds that include as participants individual retirement accounts or H.R. 10 plans.

- G. Any *business development company* as defined in section 202(a)(22) of the Investment Advisers Act of 1940;
 - H. Any organization described in section 501(c) (3) of the Internal Revenue Code, corporation (other than a bank as defined in section 3(a)(2) of the Act or a savings and loan association or other institution referenced in section 3(a)(5)(A) of the Act or a foreign bank or savings and loan association or equivalent institution), partnership, or Massachusetts or similar business trust; and
 - I. Any *investment adviser* registered under the Investment Advisers Act.
- ii. Any *dealer* registered pursuant to section 15 of the Exchange Act, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least \$10 million of securities of issuers that are not affiliated with the dealer, *Provided*, That securities constituting the whole or a part of an unsold allotment to or subscription by a dealer as a participant in a public offering shall not be deemed to be owned by such dealer;
 - iii. Any *dealer* registered pursuant to section 15 of the Exchange Act acting in a riskless principal transaction on behalf of a qualified institutional buyer;

Note: A registered dealer may act as agent, on a non-discretionary basis, in a transaction with a qualified institutional buyer without itself having to be a qualified institutional buyer.

- iv. Any investment company registered under the Investment Company Act, acting for its own account or for the accounts of other qualified institutional buyers, that is part of a family of investment companies which own in the aggregate at least \$100 million in securities of issuers, other than issuers that are affiliated with the investment company or are part of such family investment companies. *Family of investment companies* means any two or more investment companies registered under the Investment Company Act, except for a unit investment trust whose assets consist solely of shares of one or more registered investment companies, that have the same investment adviser (or, in the case of unit investment trusts, the same depositor), *Provided That*, for purposes of this section:

- A. Each series of a series company (as defined in Rule 18f-2 under the Investment Company Act) shall be deemed to be a separate investment company; and
 - B. Investment companies shall be deemed to have same adviser (or depositor) if their advisers (or depositors) are majority-owned subsidiaries of the same parent, or if one investment company's adviser (or depositor) is a majority-owned subsidiary of the other investment company's adviser (or depositor);
- v. Any entity, all of the equity owners of which are qualified institutional buyers, acting for its own account or the accounts of other qualified institutional buyers; and
 - vi. Any *bank* as defined in section 3(a)(2) of the Act, any savings and loan association or other institution as referenced in section 3(a)(5)(A) of the Act, or any foreign bank or savings and loan association or equivalent institution, acting for its own account or the accounts of other qualified institutional buyers, that in the aggregate owns and invests on a discretionary basis at least \$100 million in securities of issuers that are not affiliated with it and that has an audited net worth of at least \$25 million as demonstrated in its latest annual financial statements, as of a date not more than 16 months preceding the date of sale under the Rule in the case of a U.S. bank or savings and loan association, and not more than 18 months preceding such date of sale for a foreign bank or savings and loan association or equivalent institution.

Accredited Investors

The Securities Act of 1933 defines the term accredited investor in Rule 501 of Regulation D as:

1. a bank, insurance company, registered investment company, business development company, or small business investment company;
2. an employee benefit plan, within the meaning of the Employee Retirement Income Security Act, if a bank, insurance company, or registered investment adviser makes the investment decisions, or if the plan has total assets in excess of \$5 million;
3. a charitable organization, corporation, or partnership with assets exceeding \$5 million;

4. a director, executive officer, or general partner of the company selling the securities;
5. a business in which all the equity owners are accredited investors;
6. a natural person who has individual net worth, or joint net worth with the person's spouse, that exceeds \$1 million at the time of the purchase;
7. a natural person with income exceeding \$200,000 in each of the two most recent years or joint income with a spouse exceeding \$300,000 for those years and a reasonable expectation of the same income level in the current year; or a trust with assets in excess of \$5 million, not formed to acquire the securities offered, whose purchases a sophisticated person makes.

Attachment 3
HOUSING COMMISSION MULTIFAMILY
HOUSING REVENUE BOND PROGRAM
Summary

General Description: The multifamily housing bond program provides below-market financing (based on bond interest being exempt from income tax) for developers willing to set aside a percentage of project units as affordable housing. Multifamily housing revenue bonds are also known as “private activity bonds” bonds because the projects are owned by private entities, often including nonprofit sponsors and for-profit investors.

Bond Issuer: Housing Authority of the City of San Diego. There is no direct legal liability to the City, the Housing Authority or the Housing Commission in connection with the issuance or repayment of bonds; there is no pledge of the City’s or the Housing Authority’s faith, credit or taxing power. The bonds do not constitute a general obligation of the issuer because security for repayment of the bonds is limited to specific private revenue sources, such as project revenues. The developer is responsible for the payment of costs of issuance and all other costs under each financing.

Affordability: Minimum requirement is that at least 20% of the units are affordable at 50% of Area Median Income (AMI). Alternatively, a minimum of 10% of the units may be affordable at 50% AMI with an additional 30% of the units affordable at 60% AMI. The Housing Commission requires that the affordability restriction be in place for a minimum of 15 years. In practice, projects financed by multifamily housing bonds are affordable for a minimum of 30 years. Bonds may also be combined with other financing sources to create deeper affordability and longer terms of restriction.

Rating: Generally “AAA” or its equivalent with a minimum rating of “A” or, under conditions that meet IRS and Housing Commission requirements, bonds may be unrated for private placement with institutional investors (typically, large banks). Additional security is normally achieved through the provision of outside credit support (“credit enhancement”) by participating financial institutions that underwrite the project loans and guarantee the repayment of the bonds. The credit rating on the bonds reflects the credit quality of the credit enhancement provider.

Approval Process:

- Inducement Resolution: The bond process is initiated when the issuer (Housing Authority) adopts an “Inducement Resolution” to establish the date from which project costs may be reimbursable from bond proceeds (if bonds are later issued) and to authorize staff to work with financing team to perform a due diligence process. The Inducement Resolution does not represent any commitment by the Housing Commission, Housing Authority, or the developer to proceed with the financing.

- TEFRA Hearing and Resolution (Tax Equity and Fiscal Responsibility Act of 1982): To assure that projects making use of tax-exempt financing meet appropriate governmental purposes and provide reasonable public benefits, IRS Code requires that a public hearing be held and that the issuance of bonds be approved by representatives of the governmental unit with jurisdiction over the area in which the project is located (City Council). This process does not make the City financially or legally liable for the bonds or for the project.

[Note: It is uncommon for the members of the City Council to be asked to take two actions at this stage in the bond process---one in their capacity as the City Council (TEFRA hearing and resolution) and another as the Housing Authority (bond inducement). Were the issuer (Housing Authority) a more remote entity, the TEFRA hearing and resolution would be the only opportunity for local elected officials to weigh in on the project.]

- Application for Bond Allocation: The issuance of these “private activity bonds” (bonds for projects owned by private developers, including projects with nonprofit sponsors and for-profit investors) requires an allocation of bond issuing authority from the State of California. To apply for an 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.
- Final Bond Approval: The Housing Authority retains absolute discretion over the issuance of bonds through adoption of a final resolution authorizing the issuance. Prior to final consideration of the proposed bond issuance, the project must comply with all applicable financing, affordability, and legal requirements and undergo all required planning procedures/reviews by local planning groups, etc.
- Funding and Bond Administration: All monies are held and accounted for by a third party trustee (or bondholder representative for some private placements). The trustee disburses proceeds from bond sales to the developer in order to acquire and/or construct the housing project. Rental income used to make bond payments is collected from the developer by the trustee and disbursed to bond holders. If rents are insufficient to make bond payments, the trustee obtains funds from the credit enhancement provider. No monies are transferred through the Housing Commission or Housing Authority, and the trustee has no standing to ask the issuer for funds.

Bond Disclosure: The offering document (typically a Preliminary Offering Statement or bond placement memorandum) discloses relevant information regarding the project, the developer, and the credit enhancement provider. Since the Housing Authority is not responsible, in any way, for bond repayment, there are no financial statements or summaries about the Housing Authority or the City that are included as part of the

offering document. The offering document includes a paragraph that states that the Housing Authority is a legal entity with the authority to issue multifamily housing bonds and that the Housing Commission acts on the behalf of the Housing Authority to issue the bonds. The offering document also includes a paragraph that details that there is no pending or threatened litigation that would affect the validity of the bonds or curtail the ability of the Housing Authority to issue bonds. This is the extent of the disclosure required of the Housing Authority, Housing Commission, or the City. However, it is the obligation of members of the Housing Authority to disclose any material facts known about the project, not available to the general public, which might have an impact on the viability of the project.