



REPORT

DATE: For the Agenda of June 7, 2002 **ITEM 107**

REPORT NO: HCR02-050

SUBJECT: Final Authorization to Issue Supplemental Multifamily Housing Revenue Bonds to Complete Construction of Hollywood Palms Apartments (Council District 3)

SUMMARY

Issue 1: Should the Housing Commission consider subordinating its \$2,200,000 loan to Hollywood Palms to a larger tax-exempt indebtedness during construction?

Recommendation 1: That the Housing Commission authorize the subordination of its \$2,200,000 loan to Hollywood Palms for additional tax-exempt bonds during construction if the bonds are fully-secured with a bank letter of credit, and meet the Housing Commission's underwriting standards.

Issue 2: Should the Housing Commission recommend that the Housing Authority take the final steps to issue supplemental tax-exempt multifamily housing revenue bonds to complete the construction of the 94-unit Hollywood Palms Apartments located at 4366 Home Avenue, San Diego, CA 92105?

Recommendation 2: That the Housing Commission recommend that the Housing Authority authorize:

- (a) the issuance of up to \$1,500,000 in tax-exempt multifamily housing revenue bonds to San Diego/Fox Hollow, LP, to complete the construction of the 95-unit Hollywood Palms Apartments located at 4366 Home Avenue, San Diego, CA 92105; and
- (b) the Executive Director of the Housing Authority or the Chief Operating Officer of the Housing Commission, or their designee, to execute all documents necessary to facilitate the financing.

Fiscal Impact – No additional Housing Commission funds are required, however the amount of debt in front of the Housing Commission's \$2.2 million loan will increase by an estimated \$1,250,000 (the amount of the bond issuance) during



construction. Debt service coverage is not affected as the bonds are only outstanding during construction. Boston Capital, the equity investor, will make the interest payments on the bonds while they are outstanding. The issuance and sale of the bonds will not financially obligate the City, the Housing Authority or the Housing Commission because security for the repayment of the bonds will be limited to specific private revenue sources. All costs of the financing, including compensation for staff efforts in preparing the bonds, will be borne by the developer. The Housing Commission's origination fee under the financing will be up to \$2,875 (0.23 percent of the bond amount).

Housing Affordability Impact – 90% percent of the project (85 units) will be set aside for occupancy by low-income renters 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 (9 units) will be set-aside for occupancy by very low-income renters 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 rent schedule for the project proposed by the applicant is included as part of the project description.

Traffic Impact – The project is estimated to generate less than 1,000 average daily trips. Although traffic mitigation is not required, due to community concern a number of traffic improvements are being considered: (1) The development will be served by a bus stop on Home Avenue that will be renovated, (2) the addition of a deceleration lane for traffic turning into the development from Home Avenue, (3) a left turn only median brake to facilitate traffic turning into the development.

Previous Related Actions – The Housing Commission and Housing Authority considered issuance of bonds and a Housing Commission loan to this project at numerous public hearings, beginning in March, 2001. On July 17, 2001, the Housing Authority authorized the issuance of bonds in the amount of \$7,000,000, a Housing Commission loan of \$2,200,000, and the execution of project-based Section 8 contracts for 23 units (HA Resolution No. 1111). On January 15, 2002, the Housing Authority approved the initial steps for a supplemental bond issuance not to exceed \$1,500,000 (HA Resolution No. 1146).

Future Related Action(s) – Final approval to issue multifamily housing revenue bonds will be sought at the Housing Authority meeting of June 11, 2002.

BACKGROUND

The previously approved Housing Commission loan and bond financing for this project closed on August 9, 2001. Shortly after the close of escrow, the original construction contractor failed to perform in accordance with the contract terms and the contract was terminated.

The developer, Affirmed Housing Group, was forced to pursue a new construction contractor, and signed a new construction contract with Wermer's Construction. Because construction could not be continued and completed under the original contract, additional expenses were incurred, including but not limited to the payment of outstanding invoices to previous subcontractors, costs associated with delay of the construction, and the added cost of having another contractor come on to the site to correct items, obtain all previous inspection records and continue with the work needed to complete the project.

In December 2001, the developer requested a supplemental issuance of tax-exempt bonds to help cover a portion of the additional costs. Along with the bonds will come additional 4% tax credit equity that will substantially cover the additional permanent funding gap. The limited partner, Boston Capital, has committed to cover the balance of extra costs.

The bonds will be short-term (approximately 9 months), and will be retired by Boston Capital's equity contribution to the project. During the time the bonds are outstanding (during construction), Boston Capital will pay all interest payments. The additional tax credit equity that will be obtained under this scenario is estimated to be approximately \$1,250,000.

The Housing Authority's application to the State on behalf of the developer for a supplemental bond allocation was successful. 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 NARRATIVE

Fox Hollow Apartments is a 94-unit new construction project located at 4366 Home Avenue. The project was approved by the City Council in 1987, and development entitlements were vested with City Council approval of the Final Map in 1992. The project received 9% tax credit financing in 1998. Development permits were obtained and construction began in late summer 2000. Because the project could not be placed in service by the December 31, 2000 deadline established for the tax credit financing, the tax credits were forfeited and financing was withdrawn.

The owner/developer determined that in order to complete the project and preserve the affordability, the clearest course was to restructure the project and finance the project with tax-exempt debt and 4% tax credits. After substantial community testimony, the City Council on April 17, 2001, voted 7 to 1 to support the application for bond financing. Councilmember Atkins committed to be personally involved in the progress of the project to ensure the community concerns were addressed.

As a result of the ongoing discussions between the new development team and community leaders, a number of changes to the project were made and include

enhancements to the project design, site work and landscaping. The project financing was approved on July 17, 2001, and closed on August 9, 2001. Construction of the project is now approximately 80% complete.

Rents and Affordability Levels

Ninety percent of the project (85 units) is to be set-aside for occupancy by low-income residents earning 60 percent or less of the area median income (\$36,060 for a four-person household) for 55 years. The remaining ten percent of the units (9 units) will be set-aside for occupancy by low-income residents earning 50 percent or less of the area median income (\$30,050 for a four-person household) at rents restricted at the corresponding affordability level for 55 years.

HOLLYWOOD PALMS APARTMENTS

Type	Sq. Ft.	AMI	Number of Units	Average Current Rents*	Maximum Rent Paid by Tenant	Market Rate	Savings
2 Bedroom	820	50% AMI	4	NA	\$591	\$943	\$352
3 Bedroom	1,050	50% AMI	10	NA	\$651	\$1138	\$487
4 Bedroom	1,200	50% AMI	7	NA	\$693	\$1415	\$722
2 Bedroom	820	60% AMI	40	NA	\$719	\$943	\$224
3 Bedroom	1,050	60% AMI	18	NA	\$794	\$1138	\$344
4 Bedroom	1,200	60% AMI	15	NA	\$847	\$1415	\$568
Total			94				

* New construction; no existing rents available

FINANCING STRUCTURE

The project is owned under a limited partnership, San Diego/Fox Hollow, LP. Affirmed Housing Group is the General Partner responsible for completion of the development. City Heights Community Development Corporation, the nonprofit partner of Affirmed, is the Managing General Partner. Boston Capital is the investor limited partner.

The project is under construction and is approximately 80% complete. Since the closing of the bonds, permanent project costs have increased approximately \$2.5 million. Of this amount, approximately \$1.7 million are construction costs, with the balance attributable to architectural, engineering and financing costs. Cost increases in the short term will be funded by the issuance of the bonds, tax credits and additional partnership capital contributions. At completion of construction the bonds will be retired with an additional capital contribution from Boston Capital.

The bonds will 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 will be pledged to the payment of the bonds because the security for the bond repayment is limited to the value of the property and the project revenue sources. The developer is responsible for the payment of all costs under the financing, including the Housing Commission's annual fees.

RISKS AND MITIGATIONS

If approved, the Housing Commission's loan will be subordinate to another approximately \$1,250,000 of tax-exempt debt. This increases the project's loan to value during construction from 121% to 138%. The investor-limited partner, Boston Capital, is guaranteeing 100% of the additional debt. Boston Capital is the nation's fourth largest owner/investor in multifamily real estate and a pioneer in affordable housing. The company's holdings consist of over 2,300 properties located in 49 states, including 110,000 apartments units valued at over \$8 billion.

Staff has been working with Joe Litten, the Housing Commission's Financial Advisor on this project, to perform due diligence under the proposed additional financing and in formulating the resulting recommendation for the Housing Authority. After evaluating the project's financial circumstances, the terms of the proposed financings and public benefits to be achieved, it is the Financial Advisor's recommendation that the bond issuance for the project be authorized. The financial Advisor's analysis and recommendation to proceed is included as Attachment 3.

ALTERNATIVE

Do not authorize the issuance of the bonds at this time. The project's bond allocation will automatically revert to the State unless the Bonds are issued by July 1, 2002. If the recommended actions are not taken, the project will not be able to benefit from the additional tax-exempt below-market financing. If the request for additional bond financing is not approved, the investor limited partner, Boston Capital, has committed to invest the additional funds necessary to complete the project.

Respectfully submitted,

Approved by,

Signature on File with Original Document

Jack D. Farris
Manager, Housing Finance &
Development

Elizabeth C. Morris
Chief Executive Officer

For the Housing Commission Agenda of June 7, 2002
Supplemental Bonds for the Construction of Hollywood Palms Apartments
Page 6

- Attachments:
1. Bond Program Description and Actions to be Taken
 2. Project Location Map
 3. Financial Advisor's Analysis
 4. Developer's Disclosure Statement
 5. Development Timeline

ATTACHMENT 1

HOUSING COMMISSION'S MULTIFAMILY BOND PROGRAM

General Description

The Housing Commission's multifamily bond program provides below market financing (based on tax exemption of bond interest) for developers willing to set aside a portion of the units in their projects as affordable housing. The actual issuer of these bonds is the Housing Authority. At the present time, nearly \$400 million in outstanding bonds provides permanent financing for more than 6,900 multifamily rental units in the City, of which 2,373 units are restricted at various levels of affordability.

The Housing Commission's policy for the issuance of bonds requires a minimum "A" rating, which is typically achieved through the provision of an outside credit enhancement by participating financial institutions that underwrite the project loans and guarantee the repayment of bonds.

Actions that must be taken by the Housing Authority and by the City Council to initiate bond financing:

1. Bond Inducement

The adoption of an "inducement resolution" is an initial step required by the Internal Revenue Service to initiate a possible new-money bond issuance. It does not represent any commitment by the Housing Commission, Housing Authority or the applicant to proceed with the financing. Rather, it establishes, through public record, the date from which project costs incurred may be determined to be reimbursable from bond proceeds. Generally, the bond inducement amount is higher than the estimated bond amount to reflect a 10-15 percent contingency. The adoption also authorizes staff to work with the selected financing team to perform a due diligence process to determine the feasibility of the financing, the level of affordability of the set-aside units and structure a resulting proposal for the issuance of bonds. In the case of the Fox Hollow Apartments, the California Statewide Communities Development Authority will issue the inducement resolution and will subsequently transfer its resolution to the San Diego Housing Commission.

2. TEFRA Hearing and Approval

In order for interest on the bonds to be tax-exempt and in accordance with the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, Section 147(f) of the Internal Revenue Code of 1986, the issuance of bonds must be approved by representatives of the governmental unit with jurisdiction over the area in which the project is located after a public hearing for which a reasonable public notice was given. Therefore, federal regulations require that the issuance of bonds by the Housing Authority be approved by the City Council, as the elected legislative body of the City. A notice of public hearing to

be held by the City Council with respect to the proposed issuance of bonds will be published in the San Diego Daily Transcript at least fourteen days prior to the scheduled meeting. The purpose of such public hearing is to provide an opportunity for interested persons to provide their views on the proposed bond issuance and on the nature and location of the project.

3. Bond Allocation

The issuance of bonds for projects owned by private developers (i.e., projects owned by private developers or by nonprofit sponsors with for profit investor participation - "private activity bonds") requires an allocation of a bond issuing authority from the State of California. In order to apply for the bond allocation, an application approved by the Housing Authority and supported by an adopted inducement resolution and by proof of credit enhancement (or bond rating) must be filed with the California Debt Limit Allocation Committee (CDLAC). In addition, evidence of a TEFRA hearing and approval must be submitted prior to the CDLAC meeting.

4. Final Bond Approval

The Housing Authority retains absolute discretion over the issuance of bonds through adoption of a final resolution authorizing the issuance. Initially, the information about the proposed tax-exempt financing of the project is preliminary. If the inducement resolutions are approved, a due diligence process conducted by staff and financing team members will generate additional information and analysis. Prior to final consideration of the proposed bond issuance by the Housing Authority, the project will have to comply with all the program's financing and affordability requirements, and undergo all required planning procedures/reviews by local planning groups, etc.

ATTACHMENT 5

DEVELOPMENT TIMELINE

- Loan Committee June 13, 2001
- Housing Commission June 22, 2001
- Housing Authority July 17, 2001
- Loan & Bond Closing August 9, 2001
- Housing Commission - Supp. Bonds December 14, 2001
- Housing Authority - Supp. Bonds January 15, 2002
- Housing Commission - Bond Approval June 7, 2002
- Housing Authority – Bond Approval June 11, 2002
- Estimated Completion of Construction September, 2002
- Estimated Full Occupancy November, 2002