SACRAMENTO HOUSING AND REDEVELOPMENT AGENCY

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APR 07 1988

April 12, 1988

Budget & Finance Committee of
the City Council
Sacramento, CA

Honorable Members in Session:

SUBJECT: Tax Credit Syndication - Riverview Plaza

SUMMARY

The attached report is submitted to you for review and recommendation prior to consideration by the Housing Authority and Redevelopment Agency of the City of Sacramento.

RECOMMENDATION

The staff recommends approval of the attached resolution authorizing tax credit syndication.

SUBJECT: Retention of Brokerage Services to Assist in the Public Housing Site Selection Process

Respectfully submitted,

William H. Edgar
WILLIAM H. EDGAR
Executive Director

TRANSMITTAL TO COMMITTEE:

Jack R. Crist
JACK R. CRIST
Deputy City Manager

Attachment

SACRAMENTO
HOUSING AND REDEVELOPMENT
AGENCY

April 6, 1988

Housing Authority of the
City of Sacramento
Sacramento, California
and
Redevelopment Agency of the
City of Sacramento
Sacramento, California

Honorable Members in Session:

SUBJECT: Tax Credit Syndication--Riverview Plaza

SUMMARY

Staff requests approval to syndicate Riverview Plaza. Sale of limited partnership shares has the potential for raising $3-$5 million (initial estimate) based on the value of available low income housing tax credits. These proceeds will be used to ensure the fiscal soundness of Riverview Plaza and to the extent proceeds exist, to provide funding for other low income housing projects. The recommendations to this report outline the various approvals required to effectuate the syndication. These include: contracting for a development coordinator/consultant and legal counsel with expertise in tax credits and syndications; creating a limited partnership; designating the Housing Authority as the general partner or using Fund, Inc., or a newly created nonprofit to serve as the general partner; transferring the project to the partnership; applying to the Mortgage Bond and Tax Credit Allocation Committee for a tax credit allocation; and taking those steps necessary to market the limited partnership interests. Through contractural arrangement, the Housing Authority would continue to manage the project. It is intended that some time in the future, project ownership would revert back to the Housing Authority.

BACKGROUND

The 1986 federal Tax Act created a new tax subsidy program using tax credits for low income housing. The program provides tax credits to investors for a ten year period. The credits can range from four percent to nine percent of qualified costs depending on the project. To qualify for the tax credit, the project must retain at a minimum: a) 20 percent of its units affordable to households who earn under 50 percent of median

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income adjusted for family size, at rents not to exceed 30 percent of 50 percent of median, less a utility allowance; or b) 40 percent of the units affordable to households who earn less than 60 percent of median income at rents not to exceed 30 percent of 60 percent of median, less a utility allowance. The project must retain this low-income occupancy and rent structure for 15 years under the Federal Tax Act.

The amount of credit available to a project is based on the number of low income units set aside in a project. The more low income units, the greater the available tax credit on the project.

The following example illustrates how the credit works. We assume a 100 percent low income project, with $1 million in eligible costs against which to apply the credit. (Ineligible costs include land, non-depreciable items, and those financed by federal grants. Eligible costs are most soft and hard development costs.) If we assume the project qualifies for the nine percent credit, the project will be allocated $90,000 in tax credits annually for ten years. Although the pricing of credits is negotiable, in other projects investors have payed between 40% and 50% of the ten year tax credit, or $360,000 - $450,000. The investor may pay a lump sum amount up front, or pay in his share over several years.

The benefit of the federal tax credit was enhanced in 1987 by enactment of a state tax credit. The state tax credit is similar to the federal credit. However, the State credit is valued at 30% of the eligible costs and is only available for four years. Using the above example, the state credit could raise an additional $120,000 - $150,000 to the project. State law requires that the project remain affordable for 30 years.

The state and federal tax credit programs offer the Housing Authority the possibility of raising a considerable amount of money by selling tax credits on Riverview Plaza. Riverview Plaza, the 124 unit elderly housing project owned by the Housing Authority is an ideal candidate for tax credits. The project as currently conceived, offers 30 percent of its units to households that earn under 50 percent of median income and 10% of its units to households that earn under 80% of median income. The fact that the project will be available for occupancy in August, strengthens its marketability to investors.

Staff's initial analysis indicates that between $3 and $5 +/- million of net proceeds could be raised from the sale of tax credits on Riverview Plaza. The actual amount will depend on which project costs and funds are deemed eligible pursuant to the federal law on tax credits, and the percentage of units designated as low income. To maximize the credit value, the unit mix of very low, low and moderate income households may have to be changed from what was originally planned for the project. The Authority could receive all the funds up front or, more typically, over 5-10 years. If the pay in is spread over several years, a larger amount of proceeds can be raised.

Attachment A provides one analysis of the value of the credit, assuming that 100 percent of the project is affordable to low income as defined by federal rules. In this example, 40 percent of the units will be affordable to households who earn under 50 percent of median and, 60 percent of the units will be affordable to households who earn under 60 percent of median. As you may recall Riverview, as originally conceived, contained 40 percent low income units and 60 percent market rate units. By making the project 100 percent low income, the value of the credit is maximized. However, an operating deficit is created by converting the market rate units to units affordable to households who earn under 60% of median income. The rent for these units will decline from $420 to $326 per month.

As shown in Attachment A, the total equity to the project from the sale of the credits could be $4.5 million (based on the pricing formula used by one corporate equity fund), assuming a six year pay in. This generates about $764,000 annually for six years. For the sake of comparison, if we assume that only 40 percent of the units are reserved for low income, the project syndication could generate between $2.0 and $2.3 +/- million.

The operating shortfall noted above, could be handled by establishing a reserve or annuity from some of the syndication proceeds, or by reducing the loan amount from the California Housing Finance Agency. The latter proposal would reduce the project debt service by an amount commensurate with the operating shortfall. Staff contemplates using a portion of the syndication proceeds to ensure the fiscal soundness of Riverview, and to fund services to benefit the tenants. The deal would be structured so that the balance of the proceeds would then flow back to the Housing Authority in the form of various fees and lease payments to be used to fund other affordable housing projects. Because these credits can potentially raise a substantial amount of money, staff strongly recommends pursuing the tax credits.

The long-term affordability and ultimate Housing Authority recontrol of the project could be achieved through the terms of the limited partnership agreement. The Housing Authority could reserve the right to repurchase the property after ten years (when all tax benefits are exhausted) at its appraised value as a low-income project subject to a long-term regulatory agreement. Under these circumstances, investors would not expect any residual receipts.

There are a great number of issues and tasks that need to be addressed and accomplished before proceeds will be raised. To accomplish the syndication, a limited partnership will have to be created. The general partner of the limited partnership will probably be a nonprofit entity established by the Authority. Fund Inc., which is an existing Agency created nonprofit may be used. Another possibility is to create a separate nonprofit controlled by the Authority. It is likely the Housing Authority or Redevelopment Agency will have to capitalize the nonprofit with a demand note, to provide the entity with some net worth. To qualify for federal tax credits, the partnership should be created and improvements and financial commitments transferred to the partnership before the project receives its certificate of occupancy. The certificate of occupancy is expected by August 1st.

Transfer of ownership requires approvals from HUD, because of the HoDAG loan, and the California Housing Finance Agency (CHFA) because of the $7 million mortgage loan. These approvals will be immediately sought after determining the form of the limited partnership.

The maximum amount of credits that can be raised must also be determined. This requires both a legal and financial analysis. Once the maximum feasible amount of credits is determined, staff will submit an application to the Mortgage Bond and Tax Credit Allocation Committee for a reservation of allocation. The State Treasurer's office is responsible for allocating tax credits.

Once a tax credit allocation is received, staff will begin seeking bids from broker/dealers to market the partnership interests and, from corporations who might be interested in purchasing the credits. The new tax law placed restrictions on deduction of losses from passive activities, including limited partnerships, that limit the type and number of private individual investors who can benefit from purchasing the tax credits. Corporate investors, however, are not subject to these same passive activity rules and are the ideal investors for these credits. Unfortunately, the corporate investor market is still unfamiliar with tax credits and, so far, has not been an easy market to reach. There are several private and nonprofit funds created specifically for investors (both individual and corporate) seeking the benefits of the tax credits. As the tax credits become more accepted in the market, and the number of such syndications grows, it will be easier to sell these deals. Staff will tap all possible investor markets to syndicate the credits. One broker/dealer, Affirmative Investments, has already expressed an interest in the project. Although we think it highly likely that investors who are willing to pay a competitive price for the credits will be found, the success of the syndication is not guaranteed.

This financing scheme will be technically and legally complicated. Staff proposes contracting with a development coordinator who has had experience with feasibility analysis, deal structuring and syndication of tax credits. The consultant will assist staff in analyzing ways to obtain the maximum credit amount, preparing a bid package, developing a strategy to successfully syndicate the project, contacting broker dealers or potential private and corporate investors, analyzing bids and assisting in completing the syndication and real estate transactions. In addition, legal counsel with expertise in tax credits, real estate and syndications will be hired. This team, with active Agency staff involvement, will attempt to accomplish the syndication by September 1, 1988, when the CHFA permanent loan is expected to fund. (If necessary, the permanent loan funding can be delayed three months by payment of an extension fee).

Staff proposes selecting the development coordinator from the responses received from the request for qualifications for various consulting services recently approved by the City Council. The deadline for submission of qualifications is April 18th. Staff has already spoken with various firms who have experience with tax credit projects and who plan on responding to the RFQ. Staff proposes sole sourcing the legal work to Goldfarb and Lipman. This firm has a demonstrated track record with tax credit projects, syndications and nonprofits and public agencies. The firm was involved in the development of the State Tax Credit Program. In addition, the firm represents most of the non-profits in Northern California who have syndicated projects, and has represented several local governments who have syndicated publicly owned housing projects. The firm is also very active in Redevelopment related activities. Staff has informally contacted other law firms and believes Goldfarb and Lippman can best meet the Authority's needs.

FINANCIAL DATA

The following major expenses will be required to accomplish the syndication.

- Development coordinator contract not to exceed $25,000.
- Legal services not to exceed $60,000.
- Appraisal $10,000.
- Tax Credit Allocation Committee fee of two percent of the first year's federal credit value. (We estimate this amount to be $7,557). Plus, a performance deposit of four percent of the value of the first 12 months federal tax credit. We estimate this amount to be $15,114. The performance deposit is returned if the project receives its Certificate of Occupancy by December 31, 1988. If the syndication is not successful, the Authority loses its two percent application fee but receives a refund on the performance deposit.

Staff will attempt to negotiate a contract with the development coordinator, so that the fee is contingent on the successful syndication of the project. The legal fees will be contingent upon syndication, assuming the Housing Authority does not change its mind in the middle of the transaction to proceed. If so, staff proposes a $5,000 reserve for non-contingent legal expenses.

Finally, the Authority may have to pledge a demand note to the nonprofit entity to establish a net worth for the entity. The need for and amount of this note will be further investigated.

Funding for the non-contingent costs are projected at approximately $65,000 and will come from that portion of the Downtown tax increment fund balance which must be set aside for housing purposes pursuant to State law. Staff has set aside these reserves for housing purposes, to meet AB265 housing set aside requirements. Staff proposes transferring $65,000 from reserves to B00200 Low Income Housing Set-Aside Cost Center, Fund 100. These funds will then be loaned to Riverview Plaza (A00410 Cost Center, Organization 6300) to be paid back from syndication proceeds. Payment of all other expenses for the syndication will come from syndication proceeds.

ENVIRONMENTAL REVIEW DATA

NEPA: Exempt activity Section 58.34(a)(9)(ii) the services effect only the social or economic environment.

CEQA: Categorical exemption 15321(a)(2) the adoption of an administrative decision to fulfill an objective by a public agency.

This is purely a financial transaction on a previously reviewed project.

POLICY IMPLICATIONS

This report presents a new concept in financing for the City Housing Authority. Other jurisdictions are beginning to use syndication as a form of project finance. Tulare County and the City of Thousand Oaks have created affiliated nonprofit entities to own projects financed through syndication proceeds. Nonprofits have been syndicating projects for several years now. There is no question that syndication affects the Authority's control over the project, and exposes the Authority to some level of risk. However, this risk is probably no greater than the risk created by the California Housing Finance Agency loan (since the loan is secured by the project's performance). The attorneys will structure the partnership and the transaction to minimize the Authority's exposure and to assure ultimate control of the project by the Housing Authority.

To accomplish the syndication, project ownership will be transferred to a limited partnership, with an Authority affiliated nonprofit as the general partner. SHRA already has an affiliated nonprofit: Fund, Inc., which would seem a logical possibility. If it is necessary to create a new nonprofit, staff will ensure that the Agency retains a majority if not full control of the nonprofit. In bringing limited partners to the deal, the Authority will have to negotiate with the syndicator on various aspects of the project and its financing (reserve funds, management controls, resale provisions, etc.).

It is likely that to maximize the tax credits, the project will need to be converted to 100 percent low income. This is a variance from the original project concept, and may affect the marketing strategy and limit the usage of the service package available at the project. However, this change will make the project more affordable to low-income persons, and we believe more in line with the Authority's mission.

Ownership by a nonprofit and syndication of projects as a way to raise equity capital is a model that will likely be replicated in future Agency housing projects. The Housing Finance Task Force will be recommending creation of an Agency affiliated nonprofit development corporation to provide the Agency another means of accomplishing the affordable housing goals of the City. The syndication of Riverview will provide staff with considerable experience to pursue other projects.

VOTE AND RECOMMENDATION OF COMMISSION

At its regular meeting of April 11, 1988, the Sacramento Housing and Redevelopment Commission adopted a motion recommending approval of the attached resolutions. The votes were as follows:

AYES:

NOES:

ABSENT:

RECOMMENDATIONS

Staff recommends that you approve the attached resolutions which:

1. Approve the use of syndication to raise the maximum amount of proceeds through the sale of tax credits to be applied towards Riverview Plaza and to promote other low income and affordable housing projects.

2. Authorize staff to select and enter into a contract with a development coordinator and legal counsel (the firm of Goldfarb and Lipman). This team will analyze the best way to maximize the credit value; develop a bid package for the syndication of Riverview Plaza; establish a limited partnership; take those steps necessary to transfer ownership of Riverview Plaza to the partnership; approach broker/dealers; analyze bids; and consummate the syndication.

3. Authorize the Executive Director to submit an application to the Tax Credit Allocation Committee and pay all necessary fees and deposits.

4. Authorize the Executive Director to sign any and all documents necessary to establish the limited partnership.

5. Authorize the Executive Director to use Fund Inc., or create a new nonprofit to serve as the general partner of the limited partnership.

6. Authorize the Executive Director to sign any and all documents to effectuate the transfer of the property and its loans, grants, and existing funding to the limited partnership.

7. Authorize the Executive Director to modify the existing financing structure within the parameters of now approved funding sources in order to generate the maximum tax credits for the project without jeopardizing the project's security and financial integrity.

8. Authorize the Executive Director to modify the occupancy requirements of the project so that the ultimate mix of very low, low and moderate income households allows the maximum credit value; and, that the project income and rent restrictions comply with State and Federal tax credit requirements.

Respectfully submitted,

TRANSMITTAL TO COUNCIL:

WALTER J. SLIPE
City Manager

WILLIAM H. EDGAR
Executive Director

RESOLUTION NO.

ADOPTED BY THE HOUSING AUTHORITY OF THE CITY OF SACRAMENTO

ON DATE OF

TAX CREDIT SYNDICATION - RIVERVIEW PLAZA

BE IT RESOLVED BY THE HOUSING AUTHORITY OF THE CITY OF SACRAMENTO:

Section 1: The Executive Director is authorized to proceed with those steps necessary to accomplish the syndication of Riverview Plaza as described in the staff report filed with this resolution ("Staff Report").

Section 2: The Executive Director is authorized to select and enter into contracts with a qualified development coordinator and with legal counsel for services as described in the Staff Report.

Section 3: The Executive Director is authorized to submit an application for a tax credit allocation for Riverview Plaza to the Tax Credit Allocation Committee.

Section 4: The Executive Director is authorized to execute all documents and take all actions necessary to hold title to Riverview Plaza.

Section 5: The Executive Director is directed to investigate and determine appropriate form of the entity to serve as the General Partner of said limited partnership and is authorized to take all steps and sign all documents necessary to create the entity to serve as General Partner.

Section 6: The Executive Director is authorized to sign any and all documents to effectuate the transfer of the property to said limited partnership and to assign loans, grants and existing funding as necessary to carry out such transfer.

Section 7: The Executive Director is authorized to modify the existing finance structure for Riverview Plaza within the parameters of funding sources now approved for the purpose of generating the maximum tax credits without jeopardizing the project's security and financial integrity.

Section 8: The Executive Director is authorized to modify the Riverview Plaza occupancy requirements regarding the mix of very low income, low income and moderate income tenants, so as to ensure the maximum benefit of the low income tax credit, and to comply with additional occupancy requirements that may be imposed as a result of the state and federal requirements under the tax credit program.

Section 9: The Executive Director is authorized to take all actions and execute all documents necessary to market and fund said limited partnership.

Section 10: This resolution is effective immediately.

CHAIR

ATTEST:

SECRETARY

1100WPP2(120)

RESOLUTION NO.

ADOPTED BY THE HOUSING AUTHORITY OF THE CITY OF SACRAMENTO

ON DATE OF

TAX CREDIT SYNDICATION - RIVERVIEW PLAZA

BE IT RESOLVED BY THE HOUSING AUTHORITY OF THE CITY OF SACRAMENTO:

Section 1: The sum of $65,000 from downtown tax increment reserves is transferred to Cost Center B00200, fund 100, for payment of costs necessary to effectuate the syndication of Riverview Plaza as described in the staff report filed with this resolution ("Staff Report"). The monies so expended shall be loaned to Riverview Plaza (Cost Center A00910, Organization 6300) to be repaid upon syndication of the project.

Section 2: Said funds shall be allocated in the maximum amounts as follows:

$25,000 for consulting fees; 10,000 for an appraisal update; payment of the Tax Credit Allocation Committee fee totalling six percent of the first year value of the credit; and expenses of Legal Counsel not to exceed $5,000.

Section 3: This resolution is be effective immediately.

CHAIR

ATTEST:

SECRETARY

1100WPP2(120)

ATTACHMENT A

LOW-INCOME HOUSING TAX CREDITS

RIVERVIEW PLAZA
6th and I Streets
Sacramento, Ca. 95814

1. FINANCING

		%
Federal Grant (HODAG)	2,000,000	12.38%
Tax exempt bonds (CHFA)	7,040,000	43.57%
Tax allocation bonds (Downtown TI)	967,680	5.99%
RHCP (HCD)	850,000	
Other	5,301,219	32.81%
	16,158,899	100.00%

2. ELIGIBLE USE -(sq. ft.)

		Total	Residential	Commercial	Residential non-shelter
Basement		23,668	19,162	4,506	
First floor					
Agora		5,642	4,568	1,074	
Commercial		15,447		15,447	
Apt. lobby		1,236	1,236		
Second floor - Commercial		11,074		11,074	
Third floor - residential		9,449	9,449		
Floors 4,6,8,10,12,14 - res.	8,824	52,944	52,944		
Floors 5,7,9,11,13 - res.	9,309	46,545	46,545		
Floor 15 - dining, kitchen		6,651			6,f
Floor 16 - recreation, storage		2,623	2,623		
Total sq. ft.		175,279	136,527	32,101	6,651
Percent sq. ft.			77.89%	18.31%	3.79%

3. COST ESTIMATES

	a. Total	b. Eligible Basis	c. Depreciable Basis
Land	198,000	0	0
Hard Construction	13,040,000	10,157,053	13,040,000
Soft Costs			
Fees/permits	236,972	184,581	236,972
Arch/eng	825,692	643,144	825,692
Organization	92,145	71,773	92,145
Financing costs			
Nonrefundable loan fees	337,802	263,118	337,802
Potentially refundable fees	522,337	0	0
Equipment & furnishings			
Furnishings	183,794	0	0
Tools	29,590	23,048	0
Maint. equipment	12,000	0	0
Tenant improvements			
1st & 2nd floors	300,000	0	300,000
Day care	246,500	0	246,500
Marketing	133,269	103,805	133,269
	16,158,899	11,446,522	15,212,378

4. QUALIFYING INCOME & RENTS

	@ 50% med.		@60% med.	
	Income	Max rent	Income	Max rent
One person	11,850	266	14,220	325
Two persons	13,500	303	16,200	370

5. PROPOSED RENTS/ APPLICABLE PERCENTAGE

	Number units	Rents	Number Applicable @ 60%
	25	106	25
	13	221	13
	12	287	12
	73	326	73
Total	123		123
Applicable percentage			100.00%

6. TAX CREDIT CALCULATIONS

			a. Federal	b. State
	Eligible basis		11,446,522	11,446,522
Less	Federal grant		2,000,000	0
			9,446,522	11,446,522
Times	Applicable Percentage		100.00%	100.00%
Equals	Qualified basis		9,446,522	11,446,522
Times	Tax Credit percentage		4.00%	9.00%
Equals	Annual Tax Credit	1	377,861	1,030,187
		2	377,861	1,030,187
		3	377,861	1,030,187
		4	377,861	343,396
		5	377,861	
		6	377,861	
		7	377,861	
		8	377,861	
		9	377,861	
		10	377,861	
	Total		3,778,609	3,433,957

7. EQUITY POTENTIAL - LISC California Equity Fund (CEF) model

Federal Credits				
Annual credit		377,861		
CEF load	1.22	309,722		
Pay-ins	6			
TOTAL FEDERAL CREDIT EQUITY				1,858,332
State Credits				
Annual Credit		1,030,187		
Effective %	67%	690,225		
CEF load	1.22	565,758		
First 3 pay-ins			1,697,275	
Fourth year credit		343,396		
Effective %	67%	230,075		
CEF load	1.22		280,692	
TOTAL STATE CREDIT EQUITY				1,977,967
Passive Losses				
Basis		15,212,378		
Schedule		40 years		
Annual depreciation		380,309		
Effec. rate	40%	152,124		
CEF load	1.22	124,692		
Pay-ins	6			
TOTAL PASSIVE EQUITY				748,150
TOTAL PROJECTED EQUITY TO PROJECT				4,584,449
ANNUAL PAY - IN				764,075
PERCENT TOTAL DEVELOPMENT COSTS				28.37%
PERCENT RESIDENTIAL DEVELOPMENT COSTS				40.05%