COUNCIL AGENDA: 04-29-08
ITEM: 4.2

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Julia H. Cooper
Leslye Krutko

SUBJECT: SEE BELOW

DATE: April 1, 2008

Approved [signature] Date 4-2-2008

COUNCIL DISTRICT: 7
SNI AREA: N/A

SUBJECT: APPROVAL OF THE ISSUANCE OF BONDS, LOAN OF BOND PROCEEDS AND RELATED DOCUMENTS FOR THE FAIRGROUNDS SENIOR HOUSING APARTMENTS

RECOMMENDATION

Adoption of a resolution of the City Council:

(a) Authorizing the issuance of tax-exempt multifamily housing revenue bonds designated as "City of San José Multifamily Housing Revenue Bonds (Fairgrounds Senior Housing Apartments), Series 2008B" in an aggregate principal amount not to exceed $28,000,000 (the "Bonds");

(b) Approving a loan of Bond proceeds to Fairgrounds Senior Housing, L.P., a California limited partnership, for financing a portion of the costs of constructing the Fairgrounds Senior Housing Apartments located at 520 Tully Road in San José;

(c) Approving in substantially final form the Bonds, Trust Indenture, Loan Agreement, Regulatory Agreement, Declaration of Restrictive Covenants and Assignment of Deed of Trust and Loan Documents and Bond Purchase Agreement; and

(d) Authorizing the City Manager or other authorized officers to execute and, as appropriate, to negotiate, execute and deliver these bond documents and other related bond documents as necessary.

OUTCOME

Approval of the recommended actions will allow for the issuance of multifamily housing revenue bonds for the purpose of financing a portion of the costs of constructing 201 one bedroom/one bathroom senior housing apartment units, 199 of which will be affordable for 55 years, and 2 unrestricted manager units.

EXECUTIVE SUMMARY

ROEM Development Corporation (the "Developer") has requested that the City issue tax-exempt multifamily housing revenue bonds for the purpose of lending the bond proceeds to Fairgrounds Senior Housing, L.P. (the "Borrower") in an amount up to $28,000,000. The proceeds of the loan, together with other funds, will finance a portion of the costs of constructing 201 one bedroom/one bathroom senior housing apartment units to be known as the Fairgrounds Senior Housing Apartments. Additionally, the Housing Department will provide a loan to the Borrower in an expected amount of $12,300,000, subject to a maximum loan amount of $12,900,000, for this Project, as approved by Council on November 20, 2007. The Bonds will be non-rated and not credit-enhanced and will be structured as a private placement with Citicorp Municipal Mortgage Inc., a Delaware statutory trust, or an affiliated entity, as the initial private placement purchaser.

BACKGROUND

ROEM Development Corporation (the "Developer") has requested that the City issue tax-exempt multifamily housing revenue bonds for the purpose of lending the bond proceeds to Fairgrounds Senior Housing, L.P., a California limited partnership (the "Borrower") created by the Developer. The Borrower will consist of: (1) Pinmore HDC, Inc., an affiliate of the Housing Authority of the County of Santa Clara, as the Managing General Partner, (2) ROEM FG Senior, LLC, an affiliate of the Developer, and (3) Alliant Capital, or an affiliated entity.

The proceeds of the bond loan, together with other funds, will be used by the Borrower to finance the new construction of 201 one bedroom/one bathroom senior housing apartment units to be known as the Fairgrounds Senior Housing Apartments (the "Project"). Upon completion of the Project, 34 percent of the affordable units (68 units) in the Project will be initially rented to senior tenants with incomes that do not exceed 30 percent of the area median income ("AMI") and 66 percent of the affordable units (131 units) will be rented to senior tenants with incomes that do not exceed 50 percent of AMI. The units rented at 30 percent of AMI will be subject to a Housing Assistance Payment Contract that will run initially for ten years. Two of the Project's 201 units will be unrestricted manager's units.

The rental restrictions for the Project will remain for a period of 55 years; however, the units initially restricted to senior tenants with incomes that do not exceed 30 percent of AMI may be rented to senior tenants at 50 percent of AMI if the Housing Assistant Payment Contract for the Project is not reauthorized by HUD.

On December 11, 2007, the Director of Finance pursuant to Municipal Code Section 5.06.430 held a TEFRA Hearing to receive public comment on the City's expressed intent to issue an amount not to exceed $28,000,000 in tax-exempt multifamily housing revenue bonds to finance the construction of the Project. On November 24, 2007, the Director of Housing submitted an application to the California Debt Limit Allocation Committee ("CDLAC") for an allocation of up to $28,000,000 in private activity bonds, pursuant to the City Council's delegation of authority. The City received the requested allocation from CDLAC on January 23, 2008.

The bonds (the "Bonds") will be structured as a single series in the amount of $28,000,000. Bond proceeds will fund a portion of the total Project costs, which are estimated at approximately $47,307,412. The estimated sources of funding differ during construction and following completion and lease-up ("permanent"), as shown in the following table:

Source	Construction	Permanent
Bond Proceeds	$28,000,000	$13,900,000
City Loan	12,300,000	12,300,000
County of Santa Clara Loan	1,475,000	1,475,000
Tax Credit Equity	2,291,395	17,293,546
Interest Income	757,484	757,484
Income from Operations	1,127,436	1,581,382
Deferred Developer Fee	1,356,097	0
Total	**$47,307,412**	**$47,307,412**

Tax credit equity funds received pursuant to a limited partnership agreement between the Borrower and Alliant Capital (or an affiliated entity) are scheduled to prepay the Bonds in two installments: (1) by an estimated $2,820,000 during construction and (2) by an estimated $11,280,000 following completion and lease-up (expected to occur no later than November 1, 2010). These prepayments totaling $14,100,000 will leave the permanent Bond in the amount of $13,900,000.

CDLAC requires that the bond closing for the Project occur by May 12, 2008[1]. It is anticipated that the Bonds will close on or about April 28, 2008.

[1] The original CDLAC expiration date was April 22, 2008 (90 days from the original approval date). An extension of the expiration date was required to accommodate the lender's approval process. Staff has obtained a verbal approval from CDLAC's Executive Director to extend the expiration date by 20 days to May 12, 2008. Written approval is expected shortly.

ANALYSIS

This portion of the report is divided into several sections to address the items in staff's recommendation to proceed with the Project financing. These sections include descriptions of the Bond financing structure, Bond financing documents, the City funding, financing team participants and the financing schedule.

Bond Financing Structure

Overview of Multifamily Bond Financing

General As a brief summary, multifamily housing revenue bonds are issued to finance the development by private developers of qualifying rental apartment projects. The City issues the bonds and then loans the proceeds to the developer/borrower. The bonds are typically issued as tax-exempt securities. The advantages of tax-exempt bonds to developers include below-market interest rates, long-term fixed rate financing and low income housing tax credits – features not available in the conventional multifamily housing construction loan mortgage market. The Bonds are limited obligations of the City, payable solely from loan repayments by the Borrower.

Requirements for Tax-Exemption For multifamily housing revenue bonds to qualify for tax-exemption, federal law generally requires that one of two affordability restrictions must apply: either (1) at least 20 percent of the units in the housing development must be reserved for occupancy by individuals and families of very-low income (50% of area median income) or (2) at least 40 percent of the units must be reserved for occupancy by individuals and families of low income (60% of area median income). The restriction in clause (2) is expected to be incorporated into the Regulatory Agreement and Declaration of Restrictive Covenants for the Project.

Structure of the Bonds

Private Placement Structure The Bonds will be non-rated and not credit-enhanced and will be structured as a private placement with Citicorp Municipal Mortgage, Inc., a Delaware statutory trust, or an affiliated entity ("Private Placement Purchaser") as the initial private placement purchaser. Pursuant to the City's policies regarding non-credit enhanced bonds, the Private Placement Purchaser will sign an Investor's Letter acknowledging that it is a "qualified institutional buyer" or an "accredited investor"; a large institutional investor which understands and accepts the risks associated with unrated bonds secured by a first priority lien on the Project. If the Private Placement Purchaser wishes to transfer the Bonds, the new bondholder must sign and deliver a similar Investor Letter to the Bond Trustee. The Bonds will be held by a tender option bond trust formed by the Private Placement Purchaser. Minimum denominations of the Bonds will be at least $100,000.

Principal Amount and Term The Bonds will be issued as tax-exempt bonds in an amount not to exceed $28,000,000. The Bonds are expected to be prepaid in two installments from tax credit equity: (1) in the estimated amount of $2,820,000 during construction and (2) in the estimated amount of $11,280,000 following construction and lease-up (expected no later than November 1, 2010). These prepayments totaling $14,100,000 will leave a "permanent" Bond in the amount of $13,900,000. The Bonds are structured with two maturities: (1) November 1, 2019 in an estimated amount of $2,000,000 (amortized over nine years beginning November 1, 2010) and (2) November 1, 2040 (final maturity) in an estimated amount of $11,900,000 (amortized over 35 years beginning November 1, 2010). The November 1, 2019 maturity corresponds to the initial term of the Housing Assistance Payment Contract from HUD. The Private Placement Purchaser reserves the right to direct a mandatory redemption of the Bonds on or about November 1, 2026, with six months prior written notice. The final dates, amounts and other financial terms are subject to change based on final pricing information.

Interest Rate The Bonds will pay interest during the construction and lease-up phase until May 1, 2010 at a variable rate equal to SIFMA[2] + 1.50%. After May 1, 2010, during the permanent (or "post-conversion) phase, the Bonds will pay a fixed interest rate expected to be approximately 5.50%. The actual rates on the Bonds are subject to final pricing.

Bond Financing Documents

The following is a brief description of each document the City Council is being asked to approve and authorize the execution of. Copies of these documents will be available in the City Clerk's Office on or about April 11, 2008.

Trust Indenture The Bonds will be issued under a Trust Indenture (the "Indenture") between the City and Wells Fargo Bank, National Association, as the trustee (the "Trustee"). The Indenture is executed by the City Manager, or other authorized officers on behalf of the City, and attested by the City Clerk. The Indenture sets forth the terms of the Bonds, including their interest rates, final maturity and redemption provisions. The Indenture establishes various funds and accounts for the deposit of Bond proceeds and repayment sources. Pursuant to the Indenture, the Trustee is given the authority to receive, hold, invest and disburse the Bond proceeds and other funds; to authenticate the Bonds; to apply and disburse payments to the Bondholders; and to pursue remedies on behalf of the Bondholders. The Indenture sets forth the guidelines for the administration, investment and treatment of investment earnings generated by each fund and account, and restrictions relating to any subsequent transfer of the Bonds. The Loan Agreement (described below) obligates the Borrower to compensate the Trustee for services rendered under the Indenture.

Loan Agreement This agreement (the "Loan Agreement") is between the City and the Borrower. The Loan Agreement is executed by the City Manager or other authorized officer on behalf of the City. The Loan Agreement provides for the loan of the Bond proceeds to the

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[2] SIFMA is the national tax-exempt weekly variable rate index.

Borrower for the construction of the Project and for the repayment of such loan by the Borrower. The Loan is evidenced by a promissory note (the "Note"). The City's rights to receive payments under the Note will be assigned to the Trustee, along with certain other rights under the Indenture, the Loan Agreement and the Note; however, certain reserved rights have been retained by the City, such as the City's right to indemnification.

Regulatory Agreement and Declaration of Restrictive Covenants This agreement (the "Regulatory Agreement") is among the City, the Trustee and the Borrower. The Regulatory Agreement is executed by the City Manager, or other authorized officers on behalf of the City. The Regulatory Agreement contains certain covenants and restrictions regarding the Project and its operations intended to assure compliance with Federal tax requirements. The Regulatory Agreement restricts the rental of Project units (except for the two manager's units) to low- or very-low income seniors for a period of 55 years.

Assignment of Deed of Trust and Loan Documents This agreement (the "Assignment") is by the City in favor of the Trustee and assigns to the Trustee the Deed of Trust, the Note and other Loan Documents.

Bond Purchase Agreement. This agreement ("Purchase Agreement") is among the City, the Borrower and Private Placement Purchaser and is executed by the City Manager or other authorized officer on behalf of the City. The Purchase Agreement sets forth the Private Placement Purchaser's agreement to purchase the Bonds, specifies the representations and warranties of the City, the Borrower and the Private Placement Purchaser, the documents to be executed at closing, and the conditions that allow the Private Placement Purchaser under certain circumstances to terminate the Purchase Agreement.

City Subordinate Funding

Per City Council approval obtained on November 20, 2007, Resolution No. 74118, the Housing Department will provide a loan to the Borrower in an aggregate amount not to exceed $12,900,000 to finance a portion of the costs of constructing the Project. Currently, it is expected that the City loan amount will be $12,300,000.

Financing Team Participants

The financing team participants consist of:

• City's Financial Advisor	Ross Financial
• Bond Counsel	Hawkins, Delafield & Wood LLP
• Trustee	Wells Fargo Bank, National Association
• Private Placement Purchaser	Citi Municipal Mortgage Inc.

All costs associated with the financial advisor, bond counsel and trustee are contingent on the sale of the Bonds and will be paid most likely from tax credit equity payments at Closing, or another available funding source at Bond closing.

Financing Schedule

The current proposed schedule is as follows:

- Council Approval of Bond Documents April 22, 2008
- Pre-Close and Close Bonds April 24, 2008 and April 28, 2008
- CDLAC Deadline for Bond Closing May 12, 2008

EVALUATION AND FOLLOW-UP

This memorandum presents the set of recommendations related to the City Council's approval of the issuance of the Bonds for the Fairgrounds Senior Housing Apartments and requires no follow-up to the City Council. Once the Bonds close, anticipated in late April 2008 and the construction of the Project commences, the Housing Department will provide updates in its Quarterly Production Updates to the City Council.

PUBLIC OUTREACH

The method of notifying the community of the City's intent to issue tax-exempt private activity bonds is for the City Council to hold a Tax Equity and Fiscal Responsibility Act (TEFRA) Hearing. The TEFRA Hearing was held on December 11, 2007 by the Director of Finance. The public hearing notice was published in the *San José Mercury News* on November 20, 2007.

☐ **Criterion 1**: Requires Council action on the use of public funds equal to $1 million or greater. **(Required: Website Posting)**

☐ **Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**

☐ **Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

COORDINATION

This report has been prepared by the Finance Department in coordination with the City Attorney's Office.

FISCAL/POLICY ALIGNMENT

This action is consistent with the City's *2007-2012 Five-Year Housing Investment Plan,* adopted by City Council in June 2007 in increasing the supply of affordable housing, and with the City's *Consolidated Plan, 2007-08* in providing households units for very low- and extremely low-income households.

COST IMPLICATIONS

All costs of the Project will be paid from Bond proceeds, City and County loans, tax credit equity, income from operations and deferred developer fee. The Bonds are tax-exempt obligations secured by a first priority lien against the 1.66 acre site located at 520 Tully Road and the improvements thereon. No payment of the Bonds will be paid from or guaranteed through the general taxing power of the City or any other City asset. The City will receive an issuance fee of approximately $95,000. The City will also receive an annual fee for monitoring the Bonds and the Regulatory Agreement. Under current City policy, the annual fee is equal to one-eighth of a point (0.125%) of the original principal amount of the Bonds (approximately $35,000 per year).

No appropriation of funds is required at this time. Compensation for the financing team participants (financial advisor, bond counsel, and trustee), as well as the costs of the financing, are contingent on the sale of the Bonds and will be paid most likely from Bond tax credit equity at Bond closing.

BUDGET REFERENCE

This section is not applicable to the issuance of Bonds requested in this Staff Report.

CEQA

Exempt.

Julia H Cooper
JULIA H. COOPER
Deputy Director of Finance

LESLYE KRUTKO
Director, Housing Department

For questions, please contact Julia Cooper, Deputy Director of Finance at 408-535-7011.