COUNCL AGENDA: 12/12/06
ITEM: 2.25

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Leslye Krutko

SUBJECT: **AMENDMENT OF REGULATORY AGREEMENT AND SALE OF THE KIMBERLY WOODS APARTMENTS**

DATE: December 5, 2006

Approved [signature] Date 12/6/06

COUNCIL DISTRICT: 6
SNI AREA: **Burbank / Del Monte**

REASON FOR ADDENDUM

The project Sponsor has entered into a sales agreement for several multifamily rental properties located in California, including the Kimberly Woods Apartment Project in San Jose, with an expiration date of December 31, 2006. The City's consent for the sale is required prior to the sales agreement expiration date. The City is willing to consent to the sale upon certain modifications to the Amended and Restated Regulatory Agreement.

RECOMMENDATION

It is recommended that the City Council adopt a resolution approving an amendment to the Amended and Restated Regulatory Agreement and Declaration of Restrictive Covenants to modify the affordable rent for the project to allow the sale of the existing Kimberly Woods Apartment, a 208-unit affordable rental housing development located at 935 Willowleaf Drive, to INVESCO Core Real Estate-U.S.A., L.L.C. ("INVESCO").

OUTCOME

The City Council's authorization to amend the Amended and Restated Regulatory Agreement and Declaration of Restrictive Covenants will permit the project sponsor, Kimberly Woods Associates, to complete the sale of the property to INVESCO Core Real Estate. The City Council's authorization will result in a stabilization of the affordable rents and also extend by a minimum of five years, or through December 29, 2024, the minimum period for which set-aside affordable units are made available to lower-income tenants.

BACKGROUND

On November 15, 1984, the City of San Jose issued $16,650,000 of tax-exempt Variable Rate Demand Multifamily Housing Revenue Bonds, Issue 1984 (Kimberly Woods Apartment Project) (the "1984 Bonds") to finance the construction of the Kimberly Woods Apartment project (the "Project") by Kimberly Woods Associates (the "Borrower"). The Borrower is a California general partnership consisting of three limited partnerships, including a limited partnership in which the William Lyon Company is the general partner.

In 1984, under the Regulatory Agreement executed in connection with the City's issuance of the Multifamily Bonds, 20% of the dwelling units in the Project were reserved for occupancy by individuals and families of low- or moderate income ("Lower Income Tenants") at rents not exceeding Section 8 Fair Market Rents for new construction. Pursuant to the applicable Federal tax law at the time the 1984 Bonds were issued, the set-aside restrictions in the Regulatory Agreement were to run for approximately 12 years from the date of the 1984 Bond issuance.

In the Fall of 1999, the Borrower requested that the City consent to a refunding of the outstanding bonds. On November 17, 1999, the City Council authorized the refunding of the tax-exempt multifamily housing revenue bonds ("Refunding Bonds"). Under the terms approved by the City Council for issuance of the Refunding Bonds, the Borrower agreed to restrictions for affordable units that exceeded those contained in the City's refunding bond policy. Specifically, in the Amended and Restated Regulatory Agreement and Declaration of Restrictive Covenants (the "Regulatory Agreement") the Borrower agreed to maintain the affordable units for the longer of 20 years (rather than 15 years) or the term of the Refunding Bonds and to limit new tenants of affordable units to those with total household income not exceeding 65% (rather than 80%) of Area Median Income (AMI). The Regulatory Agreement defined affordable rent and established that, five years following the execution of the Agreement, affordable rents were to be no greater than the U.S. Department of Housing and Urban Development ("HUD") established fair market rents for comparable units in the City.

The Project consists of 60 one-bedroom units, 96 two-bedroom units, and 52 two-bedroom town homes. Construction was completed in 1986.

ANALYSIS

The Borrower has requested that the City consent to sale of the Property to INVESCO and the assumption by INVESCO of the Borrower's obligations, including the requirements for the provision of affordable housing units as set forth in the Regulatory Agreement.

As written in the Regulatory Agreement, no later than five years from the date of execution of the Regulatory Agreement (or December 2004), rents for set-aside affordable units at Kimberly Woods were to be no higher than fair market rents ("FMR") as determined by HUD. However, the Borrower does not believe that the Regulatory Agreement properly reflects the affordable rent for the Project. The Borrower has indicated that, under the terms of the negotiations at the time that the Refunding Bonds were authorized, rent levels were intended to be limited to 30% of 65% of AMI.

To provide for the consent of sale and transfer of Kimberly Woods to INVESCO, City staff have agreed with the Borrower to a compromise definition of affordable rent to allow for the affordable rent to be calculated at 30% of 60% AMI. The compromise will result in a more stable affordable rent for the tenants, which under the HUD FMR could fluctuate below or above 60% of AMI. As additional consideration for the agreement to amend the Regulatory Agreement, the Borrower has agreed to adhere to the revised Regulatory Agreement and extend for a period of five years the limitation on the income eligibility for set-aside affordable units. For the additional five years, tenants who would not have otherwise qualified to rent a unit will be able to rent one of the units. Although the rent to be paid by those tenants will not be restricted under the Regulatory Agreement, the Borrower believes that market forces will require that the rents be voluntarily restricted for that five-year period.

Staff has reviewed the relationship between Fair Market Rents and rents based on AMI and have determined that, while 60% AMI currently exceeds FMR, historically these rents have been very close, with FMRs exceeding the 60% AMI level in several years. Accordingly, it is not expected that the adoption of rent limits of 60% AMI at Kimberly Woods will result in higher rents than would otherwise be the case. Furthermore, the requirement that affordable rents be no greater than 30% of 60% of AMI is the typical requirement for projects for which the City has issued tax-exempt multifamily housing revenue bonds. Because the revised Amended Regulatory Agreement would be more consistent with the other projects in the Housing Department's portfolio, the revision will facilitate the Department's ongoing compliance monitoring and enforcement efforts.

Currently, rent levels for all tenants in set-aside affordable units at the project pay rents that are below the recommended 60% AMI level. The Borrower has agreed to extend for a period of five years, or through 2024, the minimum period through which all set-aside units are to be made available to Low Income Tenants.

POLICY ALTERNATIVES

The Housing Department considered an alternative before recommending a change in the Regulatory Agreement on the Kimberly Woods Apartments:

Alternative #1: The City could decline to amend the Regulatory Agreement and not consent to the sale of the project

Pros: In the short run, tenants may be subject to lower rent increases.

Cons: The current difference in the interpretation of the affordable rent levels involving AMI and FMR would continue, likely leading to litigation. The sale of the project would be obstructed, resulting in potential financial losses to the Borrower.

Reason for not recommending: The borrower has expressed a desire to clarify the Regulatory Agreement and complete the sale of the project. The tenants will benefit through extended occupancy restrictions.

PUBLIC OUTREACH/INTEREST

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

This project does not meet any of the criteria above. This report will be posted to the City's website for the December 12, 2006 Council Agenda.

On December 7, 1999 a public hearing was held, as required by the Tax Equity and Fiscal Responsibility Act of 1982, to solicit public comments on the proposed issuance by the City of tax-exempt multifamily housing revenue refunding bonds for the Kimberly Woods project. The public hearing notice was published in the San Jose Mercury News, announcing the time and the location of the public hearing.

COORDINATION

This recommendation has been coordinated with the City Attorney's Office and the Finance Department.

CEQA

CEQA: Exempt, PP 06-208.

LESLYE KRUTKO
Director of Housing

For questions please contact Mike Meyer at (408) 535-3855.