

MEMORANDUM

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DATE: JULY 7, 2011 WK1990
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TO: CRA/LA BOARD OF COMMISSIONERS
FROM: CHRISTINE ESSEL, CHIEF EXECUTIVE OFFICER
STAFF: LESLIE LAMBERT, REGIONAL ADMINISTRATOR
MICHELLE BANKS-ORDONE, PROJECT MANAGER
JERRY HAMMOND, SENIOR HOUSING FINANCE OFFICER
SUBJECT: The Serrano. Loan Agreement with 979 Serrano Partners, L.P., not to exceed \$4,000,000 for development of The Serrano at 975, 979 and 983 S. Serrano Avenue in the Wilshire Center/Koreatown Recovery Redevelopment Project Area
HOLLYWOOD & CENTRAL REGION (CD 10)

INVESTMENT COMMITTEE: Approved May 25, 2011

RECOMMENDATIONS

That the CRA/LA Board of Commissioners:

1. Request that the City Council acknowledge and approve CRA/LA's implementation of The Serrano affordable housing development (Project) under the Cooperation Agreement for Payment of Costs Associated with certain CRA/LA funded Capital Improvements, Public Improvements and Housing Projects, dated as of March 10, 2011, between the CRA/LA and the City of Los Angeles.

That the CRA/LA Board of Commissioners take the following actions:

1. Adopt a resolution finding that an economically feasible alternative method of financing the Project on substantially comparable terms without subordination of CRA/LA's deed of trust and affordability restrictions on the Project site is not reasonably available, and authorizing subordination of said deed and restrictions to conventional loans during both the construction and permanent phases of the Project;
2. Approve and adopt by resolution the Replacement Housing Plan;
3. Approve and adopt the Relocation Plan for the relocation of six (6) households who currently reside at the Project site;
4. Approve the Design Development Drawings; and

That the CRA/LA Board of Commissioners, subject to City Council review and approval, authorize the Chief Executive Officer or designee to:

5. Amend the Proposed FY12 Budget and Work Program to recognize advance carryover of \$2,000,000 in unanticipated FY11 Wilshire Center/Koreatown Tax Increment Funds; and

6. Execute a Loan Agreement and related documents with 979 Serrano Partners, L.P. (Borrower) no fewer than 30 days after approval of the Replacement Housing Plan and Relocation Plan to provide a loan totaling not more than \$4,000,000 from Wilshire Center/Koreatown FY11 unanticipated Tax Increment Funds, FY12 Low and Moderate Income Housing and/or future Tax Allocation Bonds (Loan) and take such other actions as are necessary to carry out said Loan Agreement.

SUMMARY

Approval of the recommended Loan Agreement would provide \$4 million in loan funds to the Project. The recommended actions are necessary to permit the Borrower to demonstrate a CRA/LA funding commitment needed for the upcoming July 13, 2011 TCAC application deadline. Disbursement of the identified CRA/LA funds will occur at construction closing and are conditioned upon the Borrower evidencing all the necessary financing commitments, including an allocation of Low Income Housing Tax Credits. The total acquisition price for the Site is \$3 million; the estimated Project total development cost including land acquisition is \$17,153,000. The Project is comprised of forty-four (44) affordable family units including one unrestricted one-bedroom manager's unit. The complex will include five residential stories over a ground floor consisting of parking and a lobby, and a single level of subterranean parking. Restrictive income and use covenants will be recorded and in effect for a period of not less than 55 years.

PREVIOUS ACTIONS

Initial Action.

DISCUSSION & BACKGROUND

Project Site

The Site is comprised of 3 contiguous lots, totaling approximately 18,603 sq. ft. (0.43 acre) and is located approximately two blocks east of S. Western Avenue and just north of W. Olympic Boulevard. Both Western Avenue and Olympic Boulevard are major transportation arteries and, as such, the site qualifies as transit-oriented development (see Attachment A, Location Map). The neighborhood is primarily characterized by schools, commercial and retail business establishments, community parks and recreational facilities. To make way for the proposed development the Borrower intends to demolish two older apartment buildings (a duplex and a 4-plex), a single family residence, and associated automobile garages.

Project History and Developer

American Communities, LLC (or assignee) entered into a purchase and sale agreement with Elshinor Property, LLC on August 27, 2010 to acquire the site for \$3 million prior to September 1, 2011. An acquisition appraisal, dated January 3, 2011, concluded the property's value at \$3,020,000. Although the primary developer for The Serrano is American Communities, LLC, it has reported its intention to form a California limited partnership to be the ultimate Borrower for the CRA/LA loan. It has further indicated that the name of the Borrower entity will be 979 Serrano Partners, L.P. The limited partnership will be a single-asset entity whose sole purpose is the development and operation of The Serrano. The general partners of 979 Serrano Partners, L.P. will be Central Valley Coalition for Affordable Housing (CVCAH) as managing general partner, and 979 Serrano Developers, LLC, as the administrative general partner (see Attachment I, Organizational Chart).

Constituent Members of Developer

The managing general partner, CVCAH, is a California nonprofit corporation formed in 1989. CVCAH was originally formed by the Housing Authority of Merced for the purpose of assisting in the production of new affordable housing in Merced County. Since that time, CVCAH has been involved in the development of approximately 189 housing projects throughout the state of California and encompassing some 13,292 units, and has participated with American Communities' affiliates on four CRA/LA funded projects. A review of CVCAH's financial statements revealed that the organization is strongly capitalized, very liquid and well managed. As of December 31, 2010, the organization had excellent liquidity, with just over \$1.3 million in cash, and current assets of nearly \$4.7 million balanced against current liabilities of only \$311,000. Net assets of \$7 million were a healthy 39 percent of the organization's total assets of \$17.8 million. Over the last three years, CVCAH has been consistently profitable.

The administrative general partner, 979 Serrano Developers, LLC, is a California limited liability company whose sole purpose will be to own and operate the Project. Its members will be Frank Fonseca and Mark Walther, who are both principals/members of American Communities, LLC. American Communities was formed in May 2002 as a for-profit company, one of whose purposes is the development of affordable housing. Since that time, the principals of American Communities have been involved in the development of 17 affordable housing developments encompassing 817 units. Five of these projects were CRA/LA funded, including: Normandie Terrace, Carondelet Court, Bonnie Brae, The Hobart, and The Ardmore. A sixth project, The Gordon, is currently working its way through the CRA/LA approval process. American Communities' most recent financial statements show that as of December 31, 2010, it was cash poor, with cash and equivalent totaling only \$16,818. However, it reports that its cash position is merely the result of delaying receipts for the purposes of minimizing income taxes. Total liabilities are minimal at only \$15,340. The company has strong shareholders' equity totaling \$8.1 million, which is primarily composed of short- and long-term fee receivables. The company appears to be consistently profitable, showing net income of more than \$1 million in each of the last three years.

As is common in CRA/LA housing transactions, the members of 979 Serrano Developers, LLC will have no financial liability to the project or the partnership. Similarly, American Communities will not technically be affiliated with the borrowing entity, and will have no financial liability to the project or partnership.

The other members of the development team include PSL Architects, and John Stewart Company (JSCo), property manager. No general contractor has yet been identified for the proposed project, but American Communities, which has its own contracting arm (American Community Home Builders) generally puts its projects out for bid once construction drawings are ready. PSL Architects is an accomplished architectural firm which has worked on numerous affordable housing developments, including 4 CRA/LA funded projects with American Communities. JSCo is a highly respected property management firm with a 32-year operating history. Their management portfolio includes 350 properties in California encompassing more than 20,000 units. JSCo specializes in managing affordable housing with regulatory encumbrances and is widely used throughout the affordable housing community in California. A full-time property manager will live and work at the site.

Developer Selection Process

This Project was Developer-initiated with the support of Council District 10.

Proposed Project

The proposed Project is a 49,457 sq. ft., 6-story development with twenty (20) one-bedroom apartments (654 sq. ft.), nine (9) two-bedroom apartments (903 sq. ft.), and fifteen (15) three bedroom apartments (1,131 sq. ft.), with 45 parking spaces. Based on HCD rents, 11 units will be restricted to Very Low Income households, eight (8) units to Low Income households, and twenty-four (24) units to Moderate Income households. The one-bedroom manager's unit will be unrestricted. Design Development Drawings are attached in Attachment H. Existing under-utilized structures on the Site will be demolished. American Communities has engaged Del Richardson & Associates, Inc. (DRA) to complete a relocation plan (Relocation Plan) (Attachment F), and has budgeted \$250,000 for relocation expenses (slightly more than recommended in the Relocation Plan). The Borrower has agreed to enter into a tri-party agreement with DRA and the CRA/LA to permit direct involvement by the CRA/LA in the relocation process. Relocation activities will not commence until an allocation of Low Income Housing Tax Credits is received. Relocation funds totaling not less than \$250,000 will be withheld from the total \$4 million CRA/LA loan amount and deposited in a separate CRA/LA retention account. Once relocation activities/payments have been made by the Borrower to the satisfaction of CRA/LA Real Estate staff, the withheld funds will be released to the Borrower or its vendors based on invoices. In the event relocation costs exceed the amount withheld, the Borrower will not be compensated by CRA/LA for the overage. Instead, the Borrower will be responsible for absorbing such overage. The Relocation Plan and Replacement Housing Plan (Attachments F and E, respectively) were placed in three public locations, and with weekly notices in the Daily News, La Opinion, and Korea Daily) for review; no comments were received. Minor updates to the Relocation Plan may be made after execution of the tri-party agreement between the CRA/LA, the Borrower and DRA. The Replacement Housing Plan Resolution is attached (Attachment G-2).

Community Benefits

The proposed Project will eliminate existing dilapidated and deteriorated structures and site conditions, as well as provide decent, safe and sound affordable housing for very low, low and moderate income families and large families. Additionally, it will be designed to LEED Silver standards at a minimum, and will include energy and water conservation features, including energy-efficient heating, ventilation, and air conditioning as well as energy-efficient appliances, dual-flush toilets, and drought resistant landscaping. The Site is approximately 2/3 mile from the Wilshire and Western Metro Purple Line station, and within walking distance to heavily used bus lines on Western Avenue and Olympic Boulevard. On-site social services, such as health and wellness classes, job training, computer education and tutoring will be provided to tenants. The Borrower will comply with all applicable CRA/LA Policies, which are listed in the Project Summary Report (Attachment J).

Financial Analysis

The Project's proposed financing structure consists of conventional construction and permanent loans, a loan from the Los Angeles Housing Department (LAHD) Affordable Housing Trust Fund, and equity from the syndication of 9% Low-Income Housing Tax Credits (see Attachment D, Sources and Uses). The permanent loan request from the CRA/LA represents approximately 23% of the Project's total development costs. The Project is slated to commence construction after the Borrower satisfactorily obtains commitments/awards for all funding sources sufficient for development of the Project as proposed. If LAHD and TCAC commitments/awards are obtained in the current and upcoming rounds, respectively, construction is expected to commence by winter 2011. The Borrower applied for funding in LAHD's April 2011 NOFA round, and intends to apply for a TCAC allocation by the July 6, 2011 deadline (assuming approval of the \$4 million loan request). The Borrower will be allowed up to two attempts to obtain LAHD and TCAC commitments/awards. If unsuccessful, CRA/LA will reconsider whether the funds should be reprogrammed for other uses.

Upon approval of the recommendations, CRA/LA will enter into a Loan Agreement with the Borrower, which will provide a total of \$4 million in construction and permanent loan funds. Once the Project is fully ready for construction and all preconditions for closing have been satisfied, the CRA/LA loan would close. The associated second-lien deed of trust would be subordinate to the liens of the construction, and permanent conventional lenders. At construction completion, once the preconditions for conversion have been satisfied, the construction loan will automatically convert into a permanent loan. The permanent loan will have a 55-year term and 3% simple interest accruing from the date of the promissory note, payable based on CRA/LA's prorata share of residual receipts (see Attachment B, Project Term Sheet).

The Project's total development cost is \$17,153,000, or approximately \$398,889 per affordable unit (\$209,179 per affordable bedroom). These amounts are inclusive of 45 parking spaces, 2 community rooms, laundry room, a one-bedroom manager's unit, open space, LEED sustainability features and other project amenities. The 6,891 sq. ft. of open space, including balconies, landscaped areas, and usable common open space (not including set-backs) exceeds City of LA Municipal Code requirements by 28%.

The Borrower has incorporated the following underwriting consultant and Investment Committee recommended changes into the project proforma:

- Capitalized operating reserve increased to a full 3 months' expenses plus debt service;
- Annual replacement reserve deposits funded at no less than \$350 per unit per year;
- Soft cost contingency line item added to the development budget of not less than \$61,000 or at least 2.5% of development soft costs (excluding developer fee); and
- Hard cost contingency increased to 10%.

ECONOMIC IMPACT

The following table* describes the economic impacts estimated to be created by this project.

Estimated Economic Impacts Created by this Project*	
Estimated Construction Jobs Created	91
Estimated Permanent Jobs Created	2

*The figures provided in the table about are for estimation purposes only; actual fiscal impact or job creation may be higher or lower than these estimates. Standardized formulas were used to generate these figures and are based on accepted econometric practices and basic tax calculations taken from research performed by a variety of sources, including the Los Angeles Economic Roundtable, California Redevelopment Association, US Department of Housing and Urban Development, CRA/LA, and the City and County of Los Angeles.

In addition to the creation of these construction and permanent jobs, redevelopment of the site will eliminate the existing deteriorated structures and improve the neighborhood by replacing them with a new, high-quality apartment building that will benefit 43 very low, low and moderate income households.

SOURCE OF FUNDS

Wilshire Center/Koreatown unanticipated FY11 Tax Increment; FY12 Low and Moderate Income Housing Funds and/or future Tax Allocation Bonds Proceeds

PROGRAM AND BUDGET IMPACT

This action will amend the Proposed FY12 Budget by recognizing the use of advance carryover in the amount of \$2,000,000 from FY11 unanticipated Wilshire Center/Koreatown Tax Increment. Staff is

analyzing the feasibility of issuing tax allocation bonds in FY12. In the event this occurs, tax allocation bond proceeds would be used instead of tax increment to fund this project. There is no impact on the City's General Fund.

ENVIRONMENTAL REVIEW

The proposed project is exempt from the California Environmental Quality Act (CEQA) pursuant to Section 15194 (Affordable Housing Exemption) of CRA/LA and State CEQA Guidelines.

FINDINGS

The State Redevelopment Law was amended in 1989 (Section 33334.14) to allow subordination of income and use restrictions. The subordination is permitted when the CRA/LA makes a finding that an economically feasible alternative method of financing or refinancing without subordination is not reasonably available and when the CRA/LA obtains written commitments reasonably designed to protect the CRA/LA's investment in the event of default.

Staff recommends that the CRA/LA Board of Commissioners make a finding that an economically feasible alternative method of financing or refinancing without subordination of CRA/LA's deed of trust and affordable housing covenant is not reasonably available, but only when the CRA/LA obtains written commitments reasonably designed to protect the CRA/LA's investment in the event of default (see Attachment G-1, Subordination Resolution). The Subordination Agreement will contain notice provisions such as one or more of the following rights as set forth in the statute:

- A. A right of the CRA/LA to cure a default on the loan(s).
- B. A right of the CRA/LA to negotiate with the lender after notice of default from the lender.
- C. An agreement that if prior to foreclosure of a loan, the CRA/LA takes title to the property and cures the default on the loan(s), the lender will not exercise any right it may have to accelerate the loan(s) by reason of transfer of title to the CRA/LA.
- D. Right of the CRA/LA to purchase property from the owner at any time after a default on the loan(s).

Currently, CRA/LA staff is not aware of any domestic lending institutions willing to provide conventional financing without subordination of covenants, as well as CRA/LA loans. Such well-margined low-risk loans are still eligible for credit under the Community Reinvestment Act. The conventional construction and permanent lender has indicated that subordination of the CRA/LA's covenants will be required.

As indicated in the Proportionality Analysis section of Attachment C (Affordable Housing Information), with the approval of this proposal, the Wilshire Center/Koreatown Redevelopment Project will be on target to comply with the statutory obligation to spend funds from the Low and Moderate Income Housing Fund in proportion to need.

As indicated in the Age Restricted Housing Expenditures section of Attachment C (Affordable Housing Information), with the approval of this proposal, the Wilshire Center/Koreatown Recovery Redevelopment Project will not have spent funds from the Low and Moderate Income Housing Fund in proportion to need, in that the amount of LMIHF spent to date on Senior Housing will exceed the allowable percentage. However, the proposed Project does improve the number of non-age restricted housing units. CRA/LA staff expects to come into full compliance on or before the December 31, 2014 statutory compliance deadline as a result of funding the development of one or more proposed non-age restricted affordable housing projects currently under consideration.

AUTHORITY GRANTED TO CEO OR DESIGNEE

It is anticipated that the Loan Agreement will authorize the CRA/LA Chief Executive Officer or designee to take such actions as may be necessary to implement it, including, but not limited to, executing related CRA/LA loan documents and taking the following actions: (1) approving revisions to the Project Budget, so long as the changes do not increase the amount of the CRA/LA Loan or otherwise have a material adverse impact on the feasibility of the Project; (2) negotiating and executing subordination agreements meeting the requirements of California Health and Safety Code Section 33334.14, and making reasonable modifications to the CRA/LA loan documents that may be requested by any Senior Lender or Tax Credit Equity Investor, so long as such changes do not adversely affect the receipt of any material benefit by CRA/LA; (3) negotiating and executing Inter-creditor Agreements with and Estoppel Certificates to other lenders, to the extent such Inter-creditor Agreements and Estoppel Certificates are consistent with the terms of the Loan Agreement; and (4) approving certain non-material revisions to the terms of the Loan Agreement reasonably requested by a Permitted Lender or Tax Credit Equity Investor.

PROJECT SUPPORT

Councilmember Herb Wesson and the Wilshire Center/Koreatown Community Advisory Committee support the recommended actions.

Christine Essel
Chief Executive Officer

By:

Dalila Sotelo, Deputy Chief Executive Officer

There is no conflict of interest known to me which exists with regard to any CRA/LA officer or employee concerning this action.

Attachment A: Location Map
Attachment B: Project Term Sheet
Attachment C: Affordable Housing Information
Attachment D: Sources/Uses
Attachment E: Replacement Housing Plan
Attachment F: Relocation Plan
Attachment G1: Subordination Resolution
Attachment G2: Replacement Housing Plan Resolution
Attachment H: Design Development Drawings
Attachment I: Organizational Structure
Attachment J: Project Summary Report